# OneSavings Bank plc

Annual Report and Financial Statements
For the year ended 31 December 2020
Company number: 07312896

# OneSavings Bank plc
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# OneSavings Bank plc
# Company information

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| **DIRECTORS** | Graham Allatt<br>Andrew Golding<br>Elizabeth Noël Harwerth<br>Sarah Hedger<br>Rajan Kapoor<br>Mary McNamara<br>April Talintyre<br>David Weymouth |
| **SECRETARY** | Jason Elphick |
| **REGISTERED OFFICE** | Reliance House<br>Sun Pier<br>Chatham<br>Kent<br>ME4 4ET<br>United Kingdom |
| **REGISTERED NUMBER** | 07312896 (England and Wales) |
| **AUDITOR** | Deloitte LLP<br>Statutory Auditor<br>London<br>United Kingdom |

# OneSavings Bank plc
# Strategic Report
For the Year Ended 31 December 2020

The Directors present their Annual Report, together with the audited Financial Statements and Auditors Report for the year ended 31 December 2020.

**Insertion of a new ultimate holding company**

A new ultimate holding company, OSB GROUP PLC (OSBG), was inserted in November 2020 as part of the Group's integration strategy following the Combination with Charter Court Financial Services Group (CCFS).

OSBG became the new ultimate holding company and listed entity of the OSB Group. The OSB Group comprises OSBG and its subsidiaries, which include One Savings Bank plc (the Company or OSB) and its subsidiaries. OSB is a wholly-owned subsidiary of OSBG. The Onesavings Bank plc Group (the Group) comprises OSB and its subsidiaries.

Upon insertion of OSBG, each OSB share was cancelled and replaced with one OSBG share with no change to voting rights or ranking.

**Our business model**

The Group is a leading specialist mortgage lender, primarily focused on carefully selected sub-segments of the mortgage market. Our specialist lending is supported by our Kent Reliance and Charter Savings Bank retail savings franchises. Our purpose is to help our customers, colleagues and communities prosper.

**Resources and relationships**

Brands and heritage

We have a family of specialist lending brands targeting selected segments of the mortgage market which are underserved by large UK banking institutions. We have well-established savings franchises through Kent Reliance, with its 150-year heritage, and the Charter Savings Bank brand.

Employees

Our team of highly skilled employees possesses expertise and in-depth knowledge of the property, capital and savings markets, risk assessment and customer management.

Infrastructure

We benefit from cost and efficiency advantages provided by our whollyowned subsidiary, OSB India, as well as credit expertise and mortgage administration services provided by CCFS.

Relationships with intermediaries and customers

Our strong and deep relationships with the mortgage intermediaries that distribute our products continue to win us industry recognition.

Capital strength

We have a strong CET1 ratio and the management capability to add capital through significant profitable loan book growth.

**Our business model explained**

Following the Combination, the Group segmented its lending business into two segments: OSB and CCFS.

**OneSavings Bank**

**Buy-to-let/SME sub-segments**

Buy-to-Let

We provide loans to limited companies and individuals, secured on residential property held for investment purposes. We target experienced and professional landlords or high net worth individuals with established and extensive property portfolios.

Commercial mortgages

We provide loans to limited companies and individuals, secured on commercial and semi-commercial properties held for investment purposes or for owner-occupation.

Residential development

We provide development loans to small and medium sized developers of residential property.

Funding lines

We provide funding lines to non-bank lenders who operate in high-yielding, specialist sub-segments such as residential bridge finance.

Asset finance

We provide loans under hire purchase, leasing and refinancing arrangements to UK SMEs and small corporates to finance business-critical assets.

Residential sub-segments

First charge

We provide loans to individuals, secured by a first charge against their residential home. Our target customers include those with a high net worth and complex income streams. We are also experts in shared ownership, lending to first-time buyers and key workers buying a property in conjunction with a housing association.

Funding lines

We provide funding lines to non-bank lenders who operate in high-yielding, specialist sub-segments such as residential bridge finance.

**Charter Court Financial Services**

Specialist lending business

Buy-to-Let

We provide products to professional and non-professional landlords with good quality credit history, through a wide product offering, including personal and limited company ownership.

**Our business model explained** (continued)

Residential

We provide a range of competitive products to prime borrowers, complex prime borrowers (including self-employed, Help to Buy, Right to Buy and new-build) and near-prime borrowers.

Bridging

We offer products with flexible features, focusing on lending to prime borrowers only, for customers who need to fund short-term cash flow needs, for example, to cover light and heavy refurbishments, home improvements, auction purchases and also to 'bridge' delays in obtaining mortgages and 'chain breaks'.

Second charge

We offer loans to prime residential and Buy-to-Let customers, with low loan-to-value ratios, who require additional capital and who wish to secure a loan with a charge against a property which is already charged to another lender.

**Retail savings**

Online

Kent Reliance is our award winning retail savings franchise with over 150 years of heritage, attracting retail savings deposits via the internet. Charter Savings Bank is a multi-award-winning online bank providing a range of competitive savings products.

Direct

The direct channel sources savings products via telephone (Kent Reliance) and post (Kent Reliance and Charter Savings Bank).

Kent Reliance and Charter Savings Bank offer accounts to SMEs and Charter Savings Bank is also present in the pooled deposits market.

High street branches

Our Kent Reliance branded network operates in the South East of England and offers a variety of fixed, notice, easy access and regular savings products, including ISAs.

Our securitisation platforms

CCFS has been a programmatic issuer of high-quality residential mortgage-backed securities through the Precise Mortgage Funding (PMF) and Charter Mortgage Funding (CMF) franchises, completing 14 securitisations worth more than £4.5bn since 2013 to 31 December 2020.

OSB issued two additional securitisations under Canterbury Finance in 2020, the majority of which have been fully retained, completing three transactions in total under this programme worth more than £2.6bn to 31 December 2020.

**Our business model explained** (continued)

**Unique operating model**

Customer service

The Group operates customer service functions in multiple locations across the UK in Wolverhampton, Fareham, London, Fleet and including its head office in Chatham. These, together with our wholly-owned subsidiary OSB India, help us deliver on our aim of putting customers first.

We deliver cost efficiencies through excellent process design and management. We have efficient, scalable and resilient infrastructure supported by strong IT security.

OSB India

OSB India (OSBI) is a wholly-owned subsidiary based in Bangalore, India. OSBI puts customer service at the heart of everything it does, demonstrated by our excellent customer Net Promoter Score. Various functions are also supported by OSBI, including support services, operations, IT, finance and human resources. We have a one team approach between the UK and India. OSBI operates a fully paperless office – all data and processing are in the UK.

**Relationships with our key stakeholders**

Our purpose is to help our customers, colleagues and communities prosper.

Strong relationships, built on regular engagement and open dialogue with all our stakeholders, are fundamental to achieving this purpose. These relationships are central to the Group's strategy and culture; and are embedded in the Board's responsibilities.

We outline below how OSB Group and its Directors engaged with key stakeholders and in doing so, discharged their duties under section 172.

**Customers**

We pride ourselves on building long-term, strong relationships with our customers. In 2020, we demonstrated our dedication to providing excellent service by supporting our borrowers and savers throughout the pandemic. This included responding to customers requesting mortgage payment deferrals, continuing to help those looking to finance their projects and supporting our savers safely in branches or via telephone, post and the internet.

When our savers call or interact with us, we offer them an opportunity to let us know how we did. We listen to them and act upon what they tell us. Throughout the year, we have been collecting customer feedback and despite the difficulties of the pandemic, increased volume of calls and savers' activity, we are incredibly proud of achieving strong satisfaction metrics for both Kent Reliance and Charter Savings Bank. We consistently achieve high satisfaction scores and in 2020 the Kent Reliance customer Net Promoter Score increased to +67 (2019: +66), Charter Savings Bank +72 in 2020 and 2019.

The needs of our customers are at the heart of our business and the Board believes that the long-term success of the Group is dependent on the strength of our relationships with our customers. The Board's engagement with customers is indirect and Directors are kept informed of customer-related matters through regular reports, feedback and research. Satisfaction scores and retention rates, together with the number of complaints and resolution times, form part of the management and Board monthly reporting packs, ensuring the visibility of customer experience to management and the Board. Customer satisfaction scores are also used as part of the executive remuneration assessment and form the basis of new initiatives and actions which continually improve customer experience.

**Relationships with our key stakeholders** (continued)

The following matters, which were identified as affecting our stakeholders, were of particular interest to the Board in 2020:

- the impact of COVID-19 on customers in terms of their savings behaviours, mortgage payment deferral requests and signs of repayment distress;
- industry-related conduct risk issues and the potential impact on customers; and
- management information in relation to customer complaints and complaints data from the Financial Ombudsman Service, engagement scores, satisfaction scores and retention rates.

In addition, management and the Board engaged with customers through the Kent Reliance Provident Society (KRPS) which conducts customer engagement activity studies for OSB. During 2020, KRPS conducted five such studies.

**Intermediaries**

Our lending products, with the exception of funding lines and residential development loans, are distributed via mortgage brokers. Mortgage brokers are vital to our success and we adapted the way in which we assist them to provide even better service in 2020.

We pride ourselves in providing unique and consistent lending propositions across all lending brands which fulfil our goal of making it easier for intermediaries to serve our borrowers. Our efforts extend beyond our proposition, as we continuously enhance the service we provide and regularly engage with the broker community. Our business development managers listen and work with intermediaries, making themselves available to discuss cases and helping to obtain swift and reliable decisions.

The Board and management track broker and borrower satisfaction scores; and the details of complaints in monthly Board reporting packs.

Intermediary events were reduced during 2020, but the Group's sales teams participated in 416 physical and virtual intermediary events, interacting with brokers and keeping abreast of industry developments and intermediary requirements.

The broker Net Promoter Score increased to +49 (2019: +27) for OSB, and to +54 (2019: +18) for Charter Savings Bank.

**Colleagues**

Our nearly 1,800 colleagues are our key asset and our success depends on the talented individuals we employ. We have always favoured two-way communication between management and our employees through regular town hall meetings, informal sessions with management and opportunities to ask questions anonymously. Even though these events were held virtually in 2020, with the majority of employees working from home, they proved popular and contributed to many initiatives that were undertaken by the business.

Engagement also took place via Group-wide surveys and the results were presented to the Board. We are proud that the Group retained its 'Two Star' rating in The Sunday Times 100 Best Companies to Work For and for the fourth consecutive year, OSB India was officially certified as a 'Great Place to Work' in 2020. The Group also participated in the Banking Standards Board Survey in 2020.

The interests of the Group's employees were considered by the Board and its Committees during the year via regular updates provided by senior management, the Group's HR function and the feedback from meetings of working groups. One of the key topics at the forefront of the Board's mind in 2020 was the impact of the pandemic on our employees' lives, both professionally and personally, their well-being and mental health.

**Relationships with our key stakeholders** (continued)

Mary McNamara is the Non-Executive Director appointed by the Board with responsibility for employee engagement and is a permanent member of the Workforce Advisory Forum (known internally as OneVoice). Members of the Board and senior management are also encouraged to attend OneVoice meetings in order to understand and discuss employee-related issues directly from representatives across the entire business. Employee feedback from each meeting is shared and discussed with members of the Board and it forms the basis of new policies, benefits and any other employee-related projects.

Another key area of Director engagement was their oversight of the decision to harmonise grades, benefits and terms and conditions across the Group as part of the integration programme.

Members of the Board also have standing invitations to attend meetings of the newly-formed Diversity and Inclusion Working Group and Health and Safety Working Group, with its members consisting of employee representatives from across the business. Updates from both working groups are submitted to the Board or its Committees on an annual basis. Members of the Board oversee the Group's talent management initiatives and senior executive succession planning.

Finally, the Board has oversight of the Group's whistleblowing activity and reviews and approves the Group's gender pay gap reporting and its commitment to the Women in Finance Charter.

**Shareholders**

In 2020, the Board took the decision to cancel the 2019 final dividend in order to help serve the needs of businesses and households through the extraordinary challenges presented by Coronavirus (COVID-19). More information about this key strategic decision is presented on page 10.

**Suppliers**

Our business is supported by a large number of suppliers, which in turn allows us, as a Group, to provide high standards of service to our customers. The members of the Board do not interact directly with the Group's suppliers; however, they are involved in overseeing the Group's supplier relationships and are regularly kept up to date by senior management on supplier considerations and developments.

In 2020, the Board was also involved with the following aspects of supplier relationships:

- consideration of potential supplier challenges as a result of the integration and the impact of COVID-19;
- consideration of the risks associated with suppliers and the framework for assurance;
- oversight of key supplier relationships including the engagement between the Group Audit Committee and the external auditor; and
- oversight of all levels of insurance in place for the Group.

The Board reviews and approves the Group's Modern Slavery and Human Trafficking Statement on an annual basis, which can be found on our website at www.osb.co.uk.

**Relationships with our key stakeholders** (continued)

**Communities**

Each year, OSB engages with charitable causes in Kent and supports a national charity chosen by employees by taking part in a variety of charitable events and partnerships. CCFS is involved in the West Midlands community and every year supports a chosen local charity. OSB India is also active in the community local to the office in Bangalore, as well as in areas where there are critical needs.

Employees and the business donated c.£516,000 to its charity partners in the year and our employees also dedicated time in a variety of volunteering activities

Engagement with our local communities is actively encouraged by the Board and senior management who believe that the fostering of such relationships is part of contributing to the communities in which we operate to make a positive impact.

In 2020, the Board endorsed the initiative of the Group Executive Committee to forgo their potential 2020 cash bonuses. The Board decided to use some of the savings to help support charities focused on homelessness. In this vein, the Group committed to a minimum of £250,000, with £100,000 donated to Shelter, which offers support and advice to those facing housing issues or homelessness across the UK. The remainder was donated to local charities that serve homeless people and to finance the purchase of dialysis machines for the HBS Dialysis Unit in India, which provides dialysis for underprivileged patients.

**Regulators**

The Board recognises the importance of open and continuous dialogue with all of our regulators, as well as other government bodies and trade associations. The Group maintains proactive dialogue with the Prudential Regulation Authority and Financial Conduct Authority. Engagement typically takes the form of regular and ad hoc meetings attended by both members of the Board and executives, as well as subject matter experts. The number of meetings held with regulators increased in 2020 and included, among other topics, operational resilience, the ability to respond to a financial stress, business continuity review and incident management. There was also significant interaction with our regulators with regard to the insertion and approval of the new holding company and the complexities of maintaining two banking licences within the Group.

Even though the Directors do not participate in all meetings, the senior management including the CFO and Chief Risk Officers provide the Board and its Committees with feedback and regular updates in respect of the broader regulatory developments and compliance considerations.

The Group also regularly interacts and has constructive relationships with the Bank of England and HM Revenue & Customs, among others, which helps to ensure that the Group is aligned with the relevant regulatory frameworks and that the business is engaged with issues impacting the financial services industry.

**Environment**

The Group is committed to operating sustainably and to continually reducing our environmental impact by not only promoting awareness of environmental issues among our employees, but also by adhering to our plan to become a greener organisation.

The Board is responsible for encouraging and overseeing an environmentally-friendly culture and ensuring that the business is ready to respond to the growing impact of climate change on the Group's activities and enhanced regulation.

**Section 172 statement**

The Directors are bound by their duties under section 172(1)(a) to (f) of the Companies Act 2006 and the manner in which these have been discharged; in particular their duty to act in the way they consider, in good faith, promotes the success of the Company for the benefit of its members as a whole.

The stakeholders which the Directors considered in this regard are customers, intermediaries, employees, shareholders, suppliers, regulators and the local communities in which we are located. These stakeholders are considered to be those the most likely to be impacted by decisions taken by the Board. The disclosures on pages 6 to 9 and those that follow, set out how Directors complied with the requirements of section 172 during the year.

**Decision making**

The Board recognises that considering our stakeholders in key business decisions is fundamental to our ability to deliver the Group's strategy in line with our long-term values and operating the business in a sustainable way. Balancing the needs and expectations of our key stakeholders has been at the forefront of the Board's mind and has been more important than ever during 2020, as a result of the global pandemic; whilst acknowledging that some decisions will result in different outcomes for each stakeholder.

**Key strategic decision in the year**

*Cancellation of the 2019 final dividend*

In April 2020, given the unprecedented and rapidly developing situation due to the outbreak of COVID-19 and the associated uncertainties, the Board took the difficult decision to cancel the 2019 final dividend.

The Board spent an extensive amount of time in discussions, not only internally, but also obtained advice from the Group's external advisers and communicated with the regulator. The Board also closely monitored the situation among the Group's peers and the larger systemic banks. The Board discussed the impact that a non-payment of dividend would have on investors who had become accustomed to receiving a regular dividend. The Board also considered other stakeholders and how paying a dividend may negatively impact them. The Board was aware that COVID-19 was unprecedented and that the extent of its impact remained uncertain at the time the decision was made. The Board decided that in order to help to serve the needs of businesses and households through the extraordinary challenges presented by COVID-19, the dividend would be cancelled. The decision-making process of the Board demonstrated that the best outcome for all stakeholders concerned was to preserve the Group's capital, even though the Group's regulator did not specifically disallow the payment of the Group's dividend. The Group's strong capital position also provided certainty for our employees and their jobs; to our suppliers; and demonstrated our prudent management in times of crisis.

**The Group's response to COVID-19**

The COVID-19 pandemic dominated 2020 and had a material impact on society, businesses and the economy. Despite the unprecedented nature of the events in the year and the challenges that arose, the Group proved its ability to successfully manage through its adaptability, operational resilience and prudent management and continued to create value for all stakeholders in the year.

**Resilient business**

The Group's business model, based on a secured balance sheet, prudent and diligent risk management and strong capital and liquidity positions, withstood the test of 2020.

Management and the Board took early decisions about the Group's risk appetite and chose to further protect the business by withdrawing most products in late March 2020. Once the situation improved, the Group returned to the market with a limited set of products with tighter underwriting criteria and higher pricing. The Group also controlled the volume of new business by pausing lending in more cyclical segments of the market, including commercial, development finance and funding lines.

To strengthen its capital position, in April 2020, the Group took the difficult but prudent decision not to pay the 2019 final dividend. Previous crises have shown that maintaining strong levels of liquidity has been critical for banks and the Group increased liquidity at the outbreak of the pandemic in March 2020 by drawing additional, attractively-priced funds, under the Bank of England's Indexed Long-Term Repo scheme, which were later replaced by the Term Funding Scheme with additional incentives for SMEs. Throughout the remainder of the year, the Group managed its capital and liquidity positions conservatively in order to maintain a suitable excess in the face of an uncertain and rapidly changing environment. A major modelling and benchmarking exercise for extreme stresses was also completed by the Group's Risk function to ensure that the Group is well positioned to withstand a severe crisis with appropriate contingency plans in place.

None of this would have been possible without the operational flexibility the Group has demonstrated both in the UK and in India. Mortgage payment deferrals meant redeployment of resources at short notice, our call centres in India had to be rapidly adapted for employees working from home and our UK offices and Kent Reliance branches were made compliant with social distancing requirements to keep our employees and customers safe.

2020 was also a time when we were able to reflect and learn from the pandemic. The Board is taking the opportunity to review some of the existing plans for the business to create an even more operationally resilient organisation, taking into account challenges presented by the crisis, not relying on single suppliers or geographical locations, but rather diversifying to protect the business.

**The Group's response to COVID-19** (continued)

**For our customers**

The Group's priority throughout the year was to offer assistance to our customers who might have been experiencing financial difficulty as a result of the pandemic, both those borrowing with the Group and those saving with Kent Reliance or Charter Savings Bank.

Within days of the mortgage payment deferral scheme being announced by the government, the Group had acted quickly and assertively, redeploying resources to respond to the spike in calls from mortgage customers. By the end of June 2020, the Group had granted payment deferrals to c.26,000 accounts, with a value equivalent to 28% of the Group's mortgage book. Research amongst customers suggested that the significant majority of requests for payment deferrals were to conserve cash and not as a result of customers facing financial difficulty. As at 31 December 2020, active payment deferrals represented only 1.3% of the Group's loan book by value.

The Group continued to process existing mortgage applications on a limited range of products and, at the same time, successfully assisted borrowers requesting mortgage payment deferrals. Due to restrictions placed on physical valuations during the first lockdown, the Group enhanced its risk assessment processes to accept alternative valuation methods for certain products from mid-April 2020, to assist borrowers further.

In October 2020, InterBay Asset Finance launched the Coronavirus Business Interruption Loan Scheme product, enabling us to finance new deals for SME customers affected by COVID-19.

To assist our savers, we kept Kent Reliance branches open throughout the pandemic with appropriate safety protocols in place. Both Kent Reliance and Charter Savings Bank encouraged the use of online access to accounts with an additional channel of contact via secure messaging and maintained postal and telephone channels. Our savings customers also received emails notifying them of alternative ways they could transact and we regularly placed COVID-specific updates as well as information about our service levels on our website.

**For our intermediaries**

As a result of the pandemic, we became not only more proactive in our engagement with brokers, but we also provided additional virtual ways of interaction and allowed more flexible working hours for our sales teams to accommodate brokers' changing hours.

At the outset of the pandemic in March 2020, the Group stopped accepting new applications for a short period of time, however, we continued to process all applications already in place where we had physical valuations.

**The Group's response to COVID-19** (continued)

**For our employees**

It has been of paramount importance for the Group to ensure the physical safety and well-being of its employees throughout the pandemic. From the end of March 2020, the majority of the Group's employees in the UK and India have been working from home. For those whose roles could not be performed adequately from home, the Group offered safe working conditions in our offices. In India, the Group prepared ahead of lockdown, which enabled the majority of employees to work from home with safe and secure technology in place. In addition, we instigated business continuity plans and were granted a number of government licences for critical employees to attend offices in two additional locations as well as in the main Bangalore site. The Group took actions to ensure that flexible working arrangements were available for our employees, across its different locations, as well as additional equipment and reliable technology. Communication between colleagues continued via online forums, team and Executive updates, virtual town halls and informal quizzes. The Group cascaded mindfulness guidance, published mental health support information and held training workshops, amongst other measures, to aid employees to better manage their new working conditions.

The Group did not place any of its employees on the UK Government's furlough scheme and welcomed 222 new colleagues in 2020.

**Rising to the challenge**

The COVID-19 global pandemic presented the Group with the unprecedented challenge of balancing the needs and safety of our customers with the welfare of our colleagues.

The combination of a dramatic increase in volumes for some of our services, such as mortgage payment deferral requests, coupled with the need to transition the majority of our colleagues to homeworking, was undoubtedly challenging. Throughout the year, we continued to meet the demands of both our savings and borrowing customers, not least by ensuring that our branch network remained open for those unable to interact with us through alternative channels.

Whilst the effectiveness of the Group's response is a result of many contributing factors, the roll-out of a Group video communication platform, together with the very high levels of reliability and stability of the Group's IT systems, were crucial factors, as was the flexibility, resilience and professionalism of our colleagues.

During 2020, approximately 80% of the Group's employees in the UK and India were working from home, at times operating outside core business hours in order to protect the bandwidth and capacity of IT systems and to meet business demands. For those that were in the offices or branches, a range of additional safety measures were introduced in order to provide a COVID-secure operating environment.

**Market review**

**The UK housing and mortgage market**

According to the Bank of England, gross mortgage lending reached £243.1bn in 2020, down 9% compared to £267.9bn in 2019[1].

Mortgage transaction volumes in 2020 decreased to the lowest level since 2016[1] due to the impact of the COVID-19 pandemic and the measures introduced by the UK Government in order to limit the spread of the virus. In addition, lingering uncertainty remained for much of the year over the UK's future relationship with the European Union, as negotiations appeared to hit an impasse until a breakthrough was made and a trade deal was agreed in December.

**Market review** (continued)

The first national lockdown, which began in March 2020, introduced a number of significant challenges for the housing and mortgage market:

- social distancing measures required staff across the industry to adapt to working from home, while conducting business remotely
- physical property valuations were suspended by many large surveying firms as house visits were not possible due to social distancing requirements
- furlough of staff across many industries raised concerns about job security and the potential for the unemployment rate to rise
- the government, with support from UK lenders, announced the ability for individuals to take a mortgage payment deferral. This required the prioritisation of mortgage payment deferral requests and meant that mortgage lenders had to scale back new lending activity to ensure that service levels could be maintained.

Lockdown measures remained in place throughout the second quarter of the year and continued to cause delays in property transactions, easing from April onwards. In particular, there was a large reduction in the number of products available at high loan to value (LTV) as lenders sought to limit exposure to the higher-risk segments of the market.

In May 2020, the UK Government published guidance on how to work **safely in other people's homes** during COVID-19. This announcement enabled physical valuations to resume which meant that lenders could begin to reduce the backlog of cases that had built up throughout the lockdown and gradually expand lending criteria.

New lending activity steadily recovered in the second half of the year as pent-up demand was released and the Stamp Duty Land Tax (SDLT) holiday led to a rebound in purchase transactions towards the end of the year. This surge in demand, combined with continued low mortgage interest rates, led to upwards pressure on house prices during the year.

Increasing infection rates throughout October and growing concerns regarding a second wave, led to a second national lockdown during November. The new processes and procedures put in place by mortgage professionals during the first lockdown ensured that the impact of these measures was largely mitigated.

The Bank of England noted in its Monetary Policy Report in February 2021 that markets had reacted positively to the news of successful vaccines and the delivery of the vaccine programme, which should support the removal of restrictions and a bounce back in economic activity.

**The UK savings market**

The UK savings market was also impacted by the COVID-19 pandemic as customers stopped spending and started saving at the highest rate in nearly 30 years. The percentage of disposable income saved rose from 9.6% to 29.1%, which was more than double the previous record of 14.4% set in 1993[2].

While some of the increased savings will have come from prudence in an uncertain world, the majority came as a result of enforced saving as national lockdowns prevented discretionary spending on everything from houses and cars, to holidays and entertainment. Over £150bn was deposited with banks and building societies in 2020 and c. £56bn was deposited in the three months between April and June alone, during the first national lockdown, compared to c. £6bn the month before[3]. The NS&I increased their deposit requirement from £6bn to £35bn[4] and competed strongly to obtain it.

**Market review** (continued)

Savings rates fell to historically low levels following the decision by the Bank of England to cut its base rate by 65 basis points to a record low of 0.1% by mid-March, although there was a delay in banks and other deposit takers passing the base rate cuts on to savers in full, as they prudently managed liquidity at the start of the pandemic. Between the start of March and the start of July, the average rate paid on an easy access savings account more than halved from 0.50% to 0.23%, while the average rate on a one year fixed rate bond dropped from 1.15% to 0.66%[5]. Many providers chose to simply exit the market altogether, with the number of savings accounts on offer reducing from 1,906 in November 2019 to 1,517 in November 2020[5].

Rates were forced down further in the second half of the year as banks and building societies had to control savings inflows to avoid amassing unnecessary liquidity, as lending volumes reduced and NS&I announced significant rate cuts[6].

**The Group's lending segments**

**Buy-to-Let**

In the Buy-to-Let segment of the mortgage market, the March lockdown was the main driver behind the annual decrease in volumes. According to UK Finance, Buy-to-Let gross advances reached 37bn in 2020, a 13% decrease from £42.5bn in 2019.7

Purchase activity was more significantly affected in the early months of the pandemic, with fewer landlords entering the market; however, this was mitigated to a degree by the SDLT holiday which supported a recovery in house purchase activity during the fourth quarter of the year. Buy-to-Let purchases reached £9.8bn during the year, down 8% compared to 2019, while remortgage originations reached £26.3bn, down 13% year-on-year[7]. The professionalisation of the Buy-to-Let market that has been driven by increased tax liability for private landlords and sustained regulatory change over a number of years continued. On 6 April 2020, the final phase of the Buy-to-Let tax relief changes were introduced, meaning that private landlords would no longer be able to deduct any mortgage interest payments from their rental income when calculating their tax liability. Instead, this has been replaced by a tax credit calculated at 20% of the mortgage interest payment. For some landlords, especially those that are higher rate or additional rate taxpayers, this would result in a larger tax bill.

In addition, changes to Capital Gains Tax (CGT) rules that come into force from the 2020-21 tax year, mean that landlords must now declare and pay any CGT liabilities within 30 days of selling an investment property, whereas in the past any CGT liability did not need to be declared until the next annual tax return. This provides a much shorter window for paying the tax bill and in combination with more restrictive rules around Private Residence Relief and Letting Relief could further increase the tax liability for certain landlords.

Research conducted by BVA BDRC in its Landlords Panel survey[8] reported that in the fourth quarter of 2020, 66% of landlords believed that their lettings business will be negatively affected by the coronavirus pandemic; however, this proportion decreased compared to the first half of the year (Q1 2020: 81%) signalling negative, but improving, sentiment among landlords. This is also reflected in the landlords confidence measure, which initially saw a sharp decline as the pandemic started then showed signs of a rebound and a greater sense of optimism towards the end of the year.

The proportion of landlords seeking to reduce the size of their portfolio (20%) remains higher than the proportion intending to buy new properties (16%); however, the gap has closed from this point last year (22% and 14% respectively)[8]. Of those landlords looking to buy new properties, a majority now intend to do so within a limited company structure, with the most desirable attribute for new properties being potential rental yield. The market is becoming increasingly dominated by professional landlords whose primary source of income is from their property portfolio.

**Market review** (continued)

The fundamentals underpinning the private rented sector remain strong, with continued increases in house prices stretching affordability further and the reduced availability of high LTV mortgages generating high demand for rental properties.

**Residential**

The UK residential mortgage market was equally affected by the outbreak of coronavirus and the measures that were introduced subsequently. The national lockdown in March was the primary driver of the reduced lending volumes in 2020 as lenders faced significant service pressures as they adapted to working from home and prioritised processing of mortgage payment deferral requests. Many of them reduced new business activity by tightening criteria and withdrawing products as they focused on low LTV, prime lending.

The purchase market was more impacted than the remortgage market, where it is easier to transact without face-to-face contact, with strong product transfer activity continuing. Purchase activity accelerated in the second half of 2020, stimulated by pent-up demand, the SDLT holiday and upcoming changes to the Help-to-Buy scheme.

House prices continued to rise, potentially increasing affordability challenges, with many buyers seeking to complete their purchases before the government incentives are withdrawn.

**Commercial**

The commercial property market, which was largely shut in the second quarter of 2020, due to the pandemic, experienced contrasting dynamics stemming directly from the social measures introduced to contain the virus and dividing it into sectors that were thriving or struggling.

The hospitality and leisure sectors of the commercial market were severely impacted by coronavirus restrictions, which have also further exacerbated the difficult situation shopping centres and the High Street were already experiencing pre-pandemic. As consumers moved online, traditional retailers struggled to pay rents and therefore shut shops. Many pubs, bars and restaurants also remaining closed, contributing to retail tenant demand and rents on the High Street falling in all but the most prime locations, with CBRE Group reporting an annual decline of 8.3% in rent for 'all retail'[9]. However, convenience retail showed growth in 2020, as shopping for essentials became even more local[10]. In addition, mixed use asset classes such as semi-commercial property, which offers a diverse income stream underpinned by the residential lettings, continued to be attractive to investors.

In contrast, the industrial sector, especially warehouse and distribution, saw greater occupier and investor demand, resulting in an increase in rents and capital values, with CBRE reporting annual rental value and capital value growth of 2.8% and 4.7% respectively for 'all industrial'[9]. Finally, office space was impacted by lower occupancy rates as office workers were working from home for the majority of 2020. This trend has also created some uncertainty around future occupier requirements for office space, as many businesses may not be renewing their leases or may be choosing smaller office spaces and adopting flexible and agile working post pandemic[10].

Overall, in 2020, there was £41.8bn invested into UK commercial property, a fall of 22% from 2019[11].

**Market review** (continued)

**Residential development**

The UK has experienced a long period of house price growth, creating affordability problems, as demand for housing outstripped both supply and real wage growth. Transaction volumes for new build sales were affected by the national lockdown in March, as they were for the second hand market.

However, the furlough scheme, mortgage payment deferrals and, to a lesser extent, the suspension on lenders and landlords taking possessions, as well as other government schemes supporting lending and house purchases, protected both housing markets from the effects of the pandemic and boosted the demand for housing throughout 2020.

The strongest demand experienced by Heritable's customers was for houses that were affordable to local populations in the regions, which the business has concentrated on funding. It was notable that sales rates for the few apartment schemes funded in London were also high, seemingly bucking the trend of that particular market. These have resulted in high levels of repayments for the Heritable business through 2020.

It appears that some regions remain structurally reliant on the government's Help to Buy scheme and therefore these areas tend to be avoided by Heritable. When government intervention into the housing markets, both directly and indirectly, is withdrawn there is a risk that these transaction volumes will fall and the support required by small and medium sized developers, which forms OSB Group's core audience for development finance, will therefore increase.

**Second charge lending**

Second charge lending was severely disrupted by the measures introduced to slow the spread of coronavirus, as lenders scaled back their appetite for new business with lower maximum LTVs and stricter lending criteria. According to the FLA, second charge mortgage lending reached £728m in 2020, down 42% compared to 2019[12].

**Funding lines**

There are a number of successful non-bank or alternative providers of finance to retail and SME customers in the UK. These businesses are funded through a variety of means, including wholesale finance provided by banks, investment funds and securitisation/bond markets, high net worth investors and market-based peer-to-peer platforms.

OSB Group is an active provider of secured funding lines to these specialty finance providers, primarily focusing on short-term real estate finance and development finance. Through these activities, the Group has achieved senior secured exposure at attractive returns to asset classes that it knows well, primarily secured against property-related mortgages. OSB Group sees a regular flow of opportunities; however, given the COVID-19 pandemic and economic uncertainty, in 2020 the Group did not consider any new client facilities, choosing to focus on servicing the existing borrowers and applying amended, restricted lending criteria.

1. UK Finance, New mortgage lending by purpose of loan, UK (BOE), Feb 2021
2. House of Commons Library, Research Briefing, Coronavirus: Impact on Household Saving and Debt, Jan 2021
3. Bank of England Database, LPMVVHS, Dec 2020
4. NS&I press release 16 July 2020
5. Moneyfacts Treasury Reports 2020
6. NS&I press release 21 Sept 2020
7. UK Finance, New and outstanding Buy-to-Let mortgages, Feb 2021.
8. BVA BDRC Landlords Panel, Q4 2020, Jan 2021
9. CBRE UK Monthly Index, Dec 2020
10. Commercial Auction 2020 Annual review, Allsops
11. https://www.savills.co.uk/research_articles/229130/310162-0
12. FLA, Feb 2021

**Key performance indicators**

Throughout the Strategic report the KPIs are presented on a statutory and an underlying basis for 2020, and a statutory and pro forma underlying basis for 2019.

Management believe these provide a more consistent basis for comparing the Group's performance between financial periods. Underlying results for 2020 exclude exceptional items, integration costs and other acquisition-related items.

Pro forma underlying results for 2019 assume that the Combination occurred on 1 January 2019 and include 12 months of results from CCFS. They also exclude exceptional items, integration costs and other acquisition-related items. For a reconciliation of statutory results to underlying and pro forma underlying results, see page 31.

**1. Gross new lending**

Statutory £3.8bn (2019: £4.1bn)
Underlying £3.8bn (2019: pro forma underlying £6.5bn)

Definition - Gross new lending is defined as gross new organic lending before redemptions.

2020 performance
The reduction in gross new lending in the year reflects the impact of the coronavirus pandemic on the Group's lending activities.

**2. Net interest margin (NIM)**

Statutory 216bps (2019: 243bps)
Underlying 247bps (2019: pro forma underlying 266bps)

Definition - NIM is defined as net interest income as a percentage of a 13 point average of interest earning assets (cash, investment securities, loans and advances to customers and credit institutions). It represents the margin earned on loans and advances and liquid assets after swap expense/income and cost of funds.

2020 performance
Both statutory and underlying NIM were lower in 2020 primarily due to a delay in passing on the base rate cuts in full to retail savers. Statutory NIM was also impacted by the dilutive effect of including CCFS' results post Combination.

**3. Cost to income ratio**

Statutory 31% (2019: 32%)
Underlying 27% (2019: pro forma underlying 29%)

Definition - Cost to income ratio is defined as administrative expenses as a percentage of total income. It is a measure of operational efficiency.

2020 performance
Statutory and underlying cost to income ratios improved in 2020 as the Group benefitted from the delivery of synergies and lower discretionary spend during lockdowns. The statutory cost to income ratio was also impacted by a full year of amortisation of the fair value uplift on CCFS' net assets which reduced total income on a statutory basis.

**Key performance indicators** (continued)

**4. Management expense ratio**

Statutory 71bps (2019: 76bps)
Underlying 70bps (2019: pro forma underlying 84bps)

**Definition**
Management expense ratio is defined as administrative expenses as a percentage of a 13 point average of total assets. It is a measure of operational efficiency.

2020 performance
Statutory and underlying management expense ratios improved in 2020 as the Group benefitted from the delivery of synergies and lower discretionary spend during lockdowns.

**5. Loan loss ratio**

Statutory 38bps (2019: 13bps)
Underlying 38bps (2019: pro forma underlying 10bps)

Definition - Loan loss ratio is defined as impairment losses expressed as a percentage of a 13 point average of gross loans and advances. It is a measure of the credit performance of the loan book.

2020 performance
Statutory and underlying loan loss ratios increased, despite the stable credit profile of the Group and positive house price movements in the year, primarily as a result of adopting more adverse forward-looking macroeconomic scenarios due to the pandemic, changes to the Group's staging criteria in line with PRA guidance, COVID-19 related enhancements to the Group's models and recognising an impairment provision in relation to potentially fraudulent activity by a third-party on a secured funding line provided by the Group.

**6. Return on equity**

Statutory 13% (2019: 18%)
Underlying 19% (2019: pro forma underlying 25%)

Definition
Return on equity is defined as profit attributable to ordinary shareholders, which is profit after tax and after deducting coupons on Additional Tier 1 securities (AT1 securities), gross of tax, as a percentage of a 13 point average of shareholders' equity (excluding £60m of AT1 securities).

2020 performance
Statutory and underlying return on equity reduced in 2020 due to higher impairment losses and a strengthened equity position, which benefitted from the cancellation of the 2019 final dividend and strong capital generation from profitability. The statutory return on equity was also adversely impacted by a full year of amortisation of the net fair value uplift to CCFS' net assets on Combination.

**Key performance indicators** (continued)

**7. OSB solo CRD IV fully-loaded Common Equity Tier 1 capital ratio**

The PRA has granted the Company a waiver to comply with the Capital Requirements Regulation (CRR) as an individual consolidation which includes the Company and subsidiaries except for the offshore servicing entity OSB India, Special Purpose Vehicles relating to securisations and the CCFS entities acquired in October 2019.

OSB solo 17.2% (2019: 14.1%)

Definition
This is defined as Common Equity Tier 1 (CET1) capital as a percentage of risk-weighted assets (calculated on a standardised basis) and is a measure of the capital strength of the Company.

2020 performance
The CET1 ratio strengthened in the year supported by the cancellation of the final dividend for 2019, the application of the Capital Requirements Regulation 'Quick Fix' package and strong capital generation from profitability.

**8. Savings customer satisfaction – Net Promoter Score (NPS)**

OSB +67 (2019: +66)
CCFS +72 (2019: +72)

Definition
The NPS measures our customers' satisfaction with our service and products. It is based on customer responses to the question of whether they would recommend us to a friend. The question scale is 0 for absolutely not to 10 for definitely yes. Based on the score, a customer is defined as a detractor between 0 and 6, a passive between 7 and 8 and a promoter between 9 and 10. Subtracting the percentage of detractors from the percentage of promoters gives an NPS of between -100 and +100.

2020 performance
OSB's savings customer NPS improved to +67 and CCFS' remained an outstanding +72.

**Financial review**

**Summary statutory results for 2020 and 2019**

| Summary Profit or Loss | For the year ended 31 December 2020 £m | For the year ended 31 December 2019 £m |
|---|---|---|
| Net interest income | **472.2** | 344.7 |
| Net fair value gain/(loss) on financial instruments | **7.4** | (3.3) |
| Gain/(loss) on sale of financial instruments | **20.0** | (0.1) |
| Other operating income | **9.0** | 2.1 |
| Administrative expenses | **(157.0)** | (108.7) |
| Provisions | **(0.1)** | - |
| Impairment of financial assets | **(71.0)** | (15.6) |
| Impairment of intangible assets | **(7.0)** | - |
| Gain on Combination with CCFS | **-** | 10.8 |
| Integration costs | **(9.8)** | (5.2) |
| Exceptional items | **(3.3)** | (15.6) |
| Profit before taxation | **260.4** | 209.1 |
| Profit after taxation | **196.3** | 158.8 |
| **Key ratios** | | |
| Net interest margin | **216bps** | 243bps |
| Cost to income ratio | **31%** | 32% |
| Management expense ratio | **0.71%** | 0.76% |
| Loan loss ratio | **0.38%** | 0.13% |
| Return on equity | **13%** | 18% |

| Extracts from the Statement of Financial Position | As at 31 December 2020 £m | As at 31 December 2019 £m |
|---|---|---|
| Loans and advances to customers | **19,230.7** | 18,446.8 |
| Retail deposits | **16,603.1** | 16,255.0 |
| Total assets | **22,654.5** | 21,417.1 |

**Financial review** (continued)

**Strong profit growth**

The Group reported 25% growth in statutory profit before taxation to £260.4m (2019: £209.1m) after exceptional items, integration costs and other acquisition-related items of £85.8m[1] (2019: £33.2m[2]) primarily due to the inclusion of a full year of profits from CCFS following the Combination in October 2019, which more than offset the impact of higher impairment charges as the Group adopted more adverse COVID-19 related forward-looking assumptions in its IFRS 9 models and recognised an impairment provision in relation to potentially fraudulent activity by a third-party on a secured funding line provided by the Group.

Statutory profit after taxation in 2020 increased by 24% to £196.3m (2019: £158.8m) including the after tax exceptional items, integration costs and other acquisition-related items of £68.6m[1] (2019: £27.4m[2]), broadly in line with the increase in profit before tax.

The Group's effective tax rate increased to 23.1%[3] in 2020 (2019: 22.8%), primarily due to the impact of the government's cancellation of planned corporation tax rate reductions on 19 March 2020 on the deferred tax liability in relation to the Combination and a larger portion of the profit being subject to the Bank Corporation Tax Surcharge from the inclusion of a full year of profits from CCFS.

Statutory return on equity for 2020 fell to 13% (2019: 18%), primarily due to a full year of amortisation of the net fair value uplift to CCFS' net assets on Combination, higher impairment charges and a strengthened equity position, which benefitted from the cancellation of the 2019 final dividend and strong capital generation from profitability.

**Net interest margin (NIM)**

The Group reported an increase in statutory net interest income of 37% to £472.2m in 2020 (2019: £344.7m), reflecting the inclusion of a full year of net interest income from CCFS, which more than offset the impact of higher amortisation of the net fair value uplift to CCFS' net assets on Combination.

Statutory NIM for 2020 reduced to 216bps (2019: 243bps), primarily due to the dilutive impact of including CCFS' results post Combination as well as the dilutive impact of a delay in passing on the base rate cuts in full to retail savers.

The CCFS business has a lower NIM than the OSB business and statutory NIM in 2020 was also adversely impacted by a full year of amortisation of the fair value uplift on acquisition of CCFS' net assets.

**Net fair value gain/(loss) on financial instruments**

The statutory net fair value gain on financial instruments of £7.4m in 2020 (2019: £3.3m loss) includes a £13.0m gain (2019: £nil) from the amortisation of hedge accounting inception adjustments, a £17.0m gain from the unwind of acquisition-related inception adjustments (2019: £3.3m) and a £2.2m gain (2019: £5.3m loss) from other items including the amortisation of the fair value relating to de-designated hedge relationships due to ineffectiveness, offset by a net loss of £6.8m (2019: £4.8m loss) in respect of the ineffective portion of hedges and an £18.0m net loss on unmatched swaps (2019: £3.5m net gain).

The net loss on unmatched swaps primarily related to fair value movements on mortgage pipeline swaps, prior to them being matched against completed mortgages and was caused by a fall in outlook on the LIBOR and SONIA yield curves. The Group economically hedges its committed pipeline of mortgages and this unrealised loss unwinds over the life of the swaps through hedge accounting inception adjustments.

**Financial review** (continued)

The amortisation of fair value relating to de-designated hedge relationships occurs when hedge relationships are cancelled due to ineffectiveness.

**Gain on sale of financial instruments**

The gain on sale of financial instruments of £20.0m in 2020 on a statutory basis, comprised a gain of £19.9m on disposal of the remaining notes under the Canterbury No.1 and PMF 2020-1B securitisations in January and a gain of £0.1m on the sale of £150.0m of AAA notes from the Canterbury No. 3 securitisation in September.

In 2019 the Group identified that an additional £0.1m of customer receipts was due to the purchaser of the personal loan portfolio, recognising an additional loss on sale of £0.1m.

**Other operating income**

Statutory other operating income of £9.0m (2019: £2.1m) largely related to fees and commissions receivable, and the increase was due to the inclusion of a full year of CCFS fees and commissions and servicing fees, including those relating to securitised loans which have been deconsolidated from the Group's balance sheet.

**Administrative expenses**

Statutory administrative expenses increased 44% to £157.0m in 2020 (2019: £108.7m) primarily due to the inclusion of CCFS' administrative expenses for the full year, which more than offset the impact of the delivery of synergies and lower discretionary spending during lockdowns.

The Group's statutory cost to income ratio of 31% (2019: 32%) improved with the delivery of synergies and the benefit of lower discretionary spending during lockdowns, which more than offset the impact of lower income due to a full year of acquisition-related adjustments (including the amortisation of the fair value uplift on CCFS' net assets), partially offset by gains on structured asset sales in the year.

The statutory management expense ratio improved to 71bps (2019: 76bps) reflecting the delivery of synergies and lower discretionary spend during lockdown.

**Impairment of financial assets**

Statutory impairment losses increased to £71.0m in 2020 (2019: £15.6m) representing 38bps on average gross loans and advances (2019: 13bps).

Impairment losses in 2020 increased primarily due to the impact of adopting more adverse forward looking macroeconomic scenarios as the coronavirus pandemic changed the outlook for the UK economy, changes to the Group's staging criteria in line with PRA guidance, which moved certain higher risk accounts with payment deferrals to stage 2, and COVID-related enhancements to the Group's models. For more detail see the Risk review. The Group also recognised an impairment provision of £20.0m in relation to potential fraudulent activity by a third party on a funding line provided by the Group, secured against lease receivables and the underlying hard assets.

**Financial review** (continued)

**Impairment of intangible assets**

The impairment of intangible assets of £7.0m related to the intangible assets recognised on the acquisition of CCFS and the impact of lower actual and expected lending volumes in CCFS due to COVID-19 on the recoverable amount of the broker relationship intangible.

**Integration**

Progress towards achieving the synergies from the Combination has been strong. By the first anniversary of the Combination, we had delivered run rate savings of over £15m, well ahead of our £6.6m target and representing more than 65% of our end of year three target run rate. This was achieved primarily by streamlining the Board and senior management team earlier than planned and through efficiencies from combining various central and support functions. The synergies realised during 2020 from these efficiencies were equivalent to a c.2% points improvement in the Group's underlying cost to income ratio. We continue to find additional synergies and are ahead of schedule towards realising the planned run rate savings for the end of year two, with a projected end of year three run rate marginally in excess of the £22m target.

The Board is taking the opportunity to review whether some planned consolidation of locations and suppliers should take place, based on a heightened focus on operational resilience. In light of additional opportunities found, any decision is not expected to have a material impact on the overall quantum of run-rate synergies targeted by the end of year three. No material dis-synergies have been identified to date.

In the first year following the Combination, costs to achieve the synergies were £10m against an expectation of £13m. However, some costs were delayed into the second year meaning that we anticipate being closer to plan at the end of year two. Final costs are expected to be marginally below the target of £39m by the end of year three.

**Financial review** (continued)

**Integration costs**

The Group recorded £9.8m (2019: £5.2m) of integration costs largely related to staff costs for key personnel retained to assist in the integration for a fixed period and fees incurred for external advice on the Group's future operating structure.

**Exceptional items**

Statutory exceptional items of £3.3m in 2020 related to the insertion of OSB GROUP PLC as the new holding company and listed entity of the Group.

The exceptional items of £15.6m in 2019 comprised transaction costs incurred by OSB in relation to the Combination with CCFS.

**Balance sheet growth**

Net loans and advances to customers increased by 4% in 2020 to £19,230.7m (31 December 2019: £18,446.8m) on a statutory basis, reflecting subdued originations due to the pandemic as well as structured asset sales in the year. Excluding the impact of structured asset sales, the statutory net loan book increased by 9%.

On a statutory basis, retail deposits increased by 2% to £16,603.1m from £16,255.0m, which the Group supplemented by participating in the Bank of England's funding schemes.

As at 31 December 2020, the Group's drawings under the Term Funding Scheme (TFS) remained at £2.6bn (2019: £2.6bn) with a repayment of £60.0m during the year. In the first half of 2020, the Group was accepted to participate in the Term Funding Scheme for SMEs (TFSME) with drawings of £1.0bn as at the end of 2020, which were used to replace Indexed Long-Term Repo (ILTR) funding and support net loan book growth. All of the Group's borrowings under the ILTR scheme were repaid during the year (2019: £290m).

The TFS drawdowns are offered in the form of collateralised cash loans. The scheme closed to new drawings at the end of February 2018 and the Group has four years from the date of drawing to repay the existing loans. TFSME drawdowns are also offered in the form of collateralised cash loans. The scheme commenced in March 2020 and offers four-year funding of at least 10% of participants' stock of real economy lending at interest rates at, or very close to, Bank Base Rate. Additional funding is available for banks that increase lending, especially to small and medium-sized enterprises. The TFSME is available for new funding until 31 October 2021.

The Group had up to £350m (2019: £600m) of contingent wholesale funding capacity available to it through the CCFS warehouse facilities, none of which was utilised at the year end.

The Group also utilises sophisticated securitisation platforms to complement its retail funding requirements and to optimise its collateral for commercial and central bank funding. For further details of securitisation activity in 2020, see the Wholesale funding overview.

Total assets grew by 6% to £22,654.5m (31 December 2019: £21,417.1m) primarily reflecting the growth in loans and advances and liquid assets.

**Financial review** (continued)

**Liquidity**

Both OSB and CCFS operate under the Prudential Regulation Authority's liquidity regime and are managed separately for liquidity risk. Both Banks hold their own significant liquidity buffer of liquidity coverage ratio (LCR) eligible high-quality liquid assets (HQLA).

As at 31 December 2020, OSB had £1,366.7m (2019: £1,231.8m) and CCFS had £1,069.1m (2019: £1,077.3m) of HQLA LCR eligible assets. Both Banks also held a significant portfolio of unencumbered prepositioned Bank of England level C eligible collateral in the Bank of England Single Collateral Pool.

Both Banks operate within a target liquidity runway in excess of the minimum LCR regulatory requirement, which is based on internal stress testing. Both Banks have a range of contingent liquidity and funding options available for possible stress periods.

As at 31 December 2020, OSB had a liquidity coverage ratio of 254% (2019: 199%) and CCFS 146% (2019: 145%), significantly in excess of the 2020 regulatory minimum of 100%.

The Group maintained prudent levels of liquidity as at 31 December 2020 in light of the continued uncertainty due to COVID-19.

**Capital**

The OSB solo capital position remained strong with a fully-loaded CET1 capital ratio of 17.2% as at 31 December 2020 (31 December 2019: 14.1%).

The OSB solo CET1 capital ratio as at 31 December 2020 benefitted from the cancelled final dividend for 2019, the application of the Capital Requirements Regulation 'Quick Fix' package and strong capital generation from profitability.

**Summary cash flow statement**

| | **For the year ended 31 December 2020** | **For the year ended 31 December 2019** |
|---|---|---|
| **Profit before tax** | **260.4** | 209.1 |
| Net cash generated/(used in): | | |
| Operating activities | **(1,326.3)** | (536.1) |
| Investing activities | **755.8** | 826.6 |
| Financing activities | **838.3** | 488.1 |
| Net increase/(decrease) in cash and cash equivalents | **267.8** | 778.6 |
| **Cash and cash equivalents at the beginning of the period** | **2,102.8** | 1,324.2 |
| **Cash and cash equivalents at the end of the period** | **2,370.6** | 2,102.8 |

**Cash flow statement**

The Group's cash and cash equivalents increased by £267.8m during the year to £2,370.6m as at 31 December 2020.

**Financial review** (continued)

Loans and advances to customers increased by £1,705.0m during the year, partially funded by £348.1m of deposits from retail customers offset by an increase in loans and advances to credit institutions (primarily the Bank of England call account) of £154.0m. Additional funding was provided by cash generated from financing activities of £838.3m and included £935.9m of net drawings under the Bank of England's TFS and TFSME schemes and £381.6m of net proceeds from securitisation of mortgages, partially offset by the repayment of warehouse funding, ILTR and commercial repos during the year. Cash generated from investing activities was £755.8m, mainly from the sale of RMBS securities and derecognition of securitisations.

In 2019, the increase in the Group's loans and advances to customers of £2,230.8m was partially funded by £1,637.8m of deposits from retail customers. Additional funding was provided by cash generated from financing activities of £488.1m and included £170.0m of net drawings under the Indexed Long-Term Repo scheme, £220.4m of proceeds from securitisation of mortgages, warehouse funding of £93.5m and £41.3m from commercial repos offset by a dividend payment of £37.3m. Cash generated from investing activities was £826.6m, largely as a result of £870.4m of cash and cash equivalents acquired on the Combination with CCFS.

1. As shown in the reconciliation of statutory to underlying results in Financial review.
2. In 2019, this comprised £48.9m (£42.9m after tax) of acquisition-related items as shown in the reconciliation of statutory to pro forma underlying results in Financial review, less CCFS' pre-acquisition transaction costs of £15.7m (£15.5m after tax).
3. Effective tax rate excludes a £4.4m charge for the impact of the deferred tax rate change and a benefit of £0.4m in respect of earlier years.

**Financial review** (continued)

**Summary of underlying results for 2020 and results on a pro forma underlying basis for 2019**

| Summary Profit or Loss | For the year ended 31 December 2020 £m | For the year ended 31 December 2019 £m |
|---|---|---|
| Net interest income | **534.0** | 518.4 |
| Net fair value loss on financial instruments | **(5.9)** | (20.3) |
| Gain on sale of financial instruments | **33.1** | 58.6 |
| Other operating income | **9.0** | 5.8 |
| Administrative expenses | **(152.7)** | (165.1) |
| Provisions | **(0.1)** | - |
| Impairment of financial assets | **(71.2)** | (16.3) |
| Profit before taxation | **346.2** | 381.1 |
| Profit after taxation | **264.9** | 294.2 |
| | | |
| **Key ratios** | | |
| Net interest margin | **247bps** | 266bps |
| Cost to income ratio | **27%** | 29% |
| Management expense ratio | **0.70%** | 0.84% |
| Loan loss ratio | **0.38%** | 0.10% |
| Return on equity | **19%** | 25% |

| Extracts from the Statement of Financial Position | As at 31 December 2020 £m | As at 31 December 2019 £m |
|---|---|---|
| Loans and advances | **19,020.8** | 18,151.4 |
| Retail deposits | **16,600.0** | 16,248.6 |
| Total assets | **22,472.2** | 21,166.5 |

**Alternative performance measures**

The Group presents alternative performance measures (APMs) in this Strategic report as Management believe they provide a more consistent basis for comparing the Group's performance between financial periods. Underlying results for 2020 exclude exceptional items, integration costs and other acquisition-related items. Pro forma underlying results for 2019 assume that the Combination occurred on 1 January 2019 and include 12 months of results from CCFS. They also exclude exceptional items, integration costs and other acquisition-related items.

APMs reflect an important aspect of the way in which operating targets are defined and performance is monitored by the Board. However, any APMs in this document are not a substitute for IFRS measures and readers should consider the IFRS measures as well.

**Financial review** (continued)

### Underlying profit before and after tax

Underlying profit before taxation was £346.2m for the year, down 9% from pro forma underlying profit before taxation of £381.1m in 2019, primarily due to higher impairment losses as the Group adopted more adverse COVID-19 related forward-looking assumptions in its IFRS 9 models, and recognised an impairment provision of £20.0m in relation to potential fraudulent activity by a third party on a funding line provided by the Group, secured against lease receivables and the underlying hard assets, which more than offset the benefit from balance sheet growth.

Underlying profit after taxation was £264.9m in 2020, down 10% from pro forma underlying profit after taxation of £294.2m in 2019, in line with the decrease in profit before tax and a higher effective tax rate. On an underlying basis, the Group's effective tax rate was 23.5% in 2020 (2019: 22.8%) as a larger portion of the Group's profit was subject to the Bank Corporation Tax Surcharge.

Underlying return on equity for 2020 remained strong at 19%, although it was lower than 25% in 2019, due primarily to the higher impairment charges and a strengthened equity position, which benefitted from the cancellation of the 2019 final dividend and strong capital generation from profitability.

### Net interest margin

On an underlying basis, net interest income increased 3% in 2020 to £534.0m from £518.4m in 2019 and underlying net interest margin (NIM) was 247bps (2019: 266bps).

The reduction in underlying NIM to 247bps from 266bps in 2019, primarily reflects the dilutive impact of a delay in passing on the base rate cuts in full to retail savers. The full impact of the base rate cuts was passed on to savers by the end of the third quarter of 2020.

### Net fair value loss on financial instruments

The underlying net fair value loss on financial instruments decreased to £5.9m from a pro forma underlying loss of £20.3m in 2019.

The loss for 2020 included a net loss of £6.8m (2019: £5.1m loss) from hedge ineffectiveness, a net loss on unmatched swaps of £18.0m (2019: £13.3m loss) and a £16.7m gain (2019: £1.7m gain) relating to the amortisation of hedging adjustments arising when hedge accounting commences on derivative instruments previously taken out against the mortgage pipeline. Other hedging and fair value movements amounted to a gain of £2.2m (2019: £3.9m loss).

The net loss on unmatched swaps primarily relates to fair value movements on mortgage pipeline swaps, prior to them being matched against completed mortgages and due to a fall in outlook on the LIBOR and SONIA yield curves. The Group economically hedges its committed pipeline of mortgages and this unrealised loss unwinds over the life of the swaps through hedge accounting inception adjustments.

### Gain on sale of financial instruments

The underlying gain on structured asset sales of £33.1m in the year (2019: £58.6m) related to a gain of £33.0m on disposal of the remaining notes under the Canterbury No.1 and PMF 2020-1B securitisations in January 2020. In September, the Group sold £150.0m of notes from the Canterbury No. 3 securitisation generating a gain of £0.1m.

In 2019, the gain on sale of loans consisted of a gain of £58.7m from sales of residual interests in three CCFS securitisations to third party investors prior to the Combination and a £0.1m loss from customer receipts due to the purchaser of the personal loan portfolio.

**Financial review** (continued)

### Other operating income

Other operating income of £9.0m (2019: £5.8m) primarily related to CCFS' fees for servicing third party mortgage portfolios and servicing fees for derecognised securitised mortgages, where the Group continued to service the loans.

### Administrative expenses

Underlying administrative expenses were £152.7m in 2020, a decrease of 8% from £165.1m in 2019, as the synergies from the integration of OSB and CCFS continued to be delivered and the Group benefitted from lower discretionary spend in lockdowns, including those relating to travel, accommodation and marketing, as employees continued to follow COVID-19 restrictions in the UK and India.

The underlying cost to income and underlying management expense ratios improved to 27% and 70bps respectively (2019: 29% and 84bps respectively) reflecting the delivery of synergies and lower discretionary spend during lockdowns.

### Impairment of financial assets

Impairment losses on an underlying basis increased to £71.2m in 2020 (2019: £16.3m) representing 38bps on average gross loans and advances (2019: pro forma underlying 10bps).

Impairment losses in 2020 increased primarily due to the impact of adopting more adverse forward-looking macroeconomic scenarios as the onset of the coronavirus pandemic changed the outlook for the UK economy, changes to the Group's staging criteria in line with PRA guidance, which moved certain higher risk accounts with payment deferrals to stage 2, and COVID-related enhancements to the Group's models. For more detail, see the Risk review. The Group also recognised an impairment provision of £20.0m in relation to potential fraudulent activity by a third party on a funding line provided by the Group, secured against lease receivables and the underlying hard assets.

### Balance sheet

On an underlying basis, the loan book increased 5% to £19,020.8m (2019: £18,151.4m) reflecting reduced originations due to the pandemic as well as structured asset sales at the start of the year. Excluding the impact of the structured asset sales, the underlying net loan book growth would have been 9%.

Underlying retail deposits increased by 2% during 2020 to £16,600.0m (2019: £16,248.6m) as both Banks continued to attract new savers by offering attractively priced savings products and outstanding customer service. The balance of the Group's funding requirement was provided by the Bank of England's funding schemes and RMBS which provided £935.9m and £381.6m of net new funding respectively. For further details of the Group's securitisation activity in 2020, see the Wholesale funding overview.

The Group's total underlying assets increased in the year by 6% to £22,472.2m from £21,166.5m in 2019, primarily reflecting the growth in loans and advances and liquid assets.

## Financial review (continued)

### Reconciliation of statutory to underlying and pro forma underlying results

| | 2020 | | | 2019 | | | |
|---|---|---|---|---|---|---|---|
| | Statutory results £m | Reverse acquisition-related and exceptional items £m | Underlying results £m | Statutory results £m | CCFS pre-acquisition results £m | Reverse acquisition-related items £m | Pro forma underlying results £m |
| **Net interest income** | **472.2** | **61.8[1]** | **534.0** | 344.7 | 152.1 | 21.6 | 518.4 |
| Net fair value gain/(loss) on financial instruments | **7.4** | **(13.3)[2]** | **(5.9)** | (3.3) | (13.7) | (3.3) | (20.3) |
| Gain/(loss) on sale of loans | **20.0** | **13.1[3]** | **33.1** | (0.1) | 58.7 | - | 58.6 |
| Other operating income | **9.0** | - | **9.0** | 2.1 | 3.7 | – | 5.8 |
| **Total income** | **508.6** | **61.6** | **570.2** | 343.4 | 200.8 | 18.3 | 562.5 |
| Administrative expenses | **(157.0)** | **4.3[4]** | **(152.7)** | (108.7) | (57.7) | 1.3 | (165.1) |
| Provisions | **(0.1)** | - | **(0.1)** | - | – | – | - |
| Impairment of financial assets | **(71.0)** | **(0.2)[5]** | **(71.2)** | (15.6) | (4.3) | 3.6 | (16.3) |
| Impairment of intangible assets | **(7.0)** | **7.0[6]** | - | - | - | - | - |
| Gain on Combination with CCFS | - | - | - | 10.8 | - | (10.8) | – |
| Integration costs | **(9.8)** | **9.8[7]** | - | (5.2) | – | 5.2 | – |
| Exceptional costs | **(3.3)** | **3.3[8]** | - | (15.6) | (15.7) | 31.3 | – |
| **Profit before tax** | **260.4** | **85.8** | **346.2** | 209.1 | 123.1 | 48.9 | 381.1 |
| **Profit after tax** | **196.3** | **68.6** | **264.9** | 158.8 | 92.5 | 42.9 | 294.2 |
| | | | | | | | |
| **Summary Balance Sheet** | | | | | | | |
| Loans and advances to customers | **19,230.7** | **(209.9)[9]** | **19,020.8** | 18,446.8 | - | (295.4) | 18,151.4 |
| Other financial assets | **3,341.8** | **36.8[10]** | **3,378.6** | 2,878.2 | - | 63.2 | 2,941.4 |
| Other non-financial assets | **82.0** | **(9.2)[11]** | **72.8** | 92.1 | - | (18.4) | 73.7 |
| **Total assets** | **22,654.5** | **(182.3)** | **22,472.2** | 21,417.1 | - | (250.6) | 21,166.5 |
| Amounts owed to retail depositors | **16,603.1** | **(3.1)[12]** | **16,600.0** | 16,255.0 | - | (6.4) | 16,248.6 |
| Other financial liabilities | **4,296.6** | **4.4[13]** | **4,301.0** | 3,544.0 | - | 10.0 | 3,554.0 |
| Other non-financial liabilities | **77.9** | **(61.4)[14]** | **16.5** | 141.1 | - | (63.1) | 78.0 |
| **Total liabilities** | **20,977.6** | **(60.1)** | **20,917.5** | 19,940.1 | - | (59.5) | 19,880.6 |
| **Net assets** | **1,676.9** | **(122.2)** | **1,554.7** | 1,477.0 | - | (191.1) | 1,285.9 |

1. Amortisation of the net fair value uplift to CCFS' mortgage loans and retail deposits on Combination.
2. Reversal of £17.0m of acquisition-related inception adjustments and recognition of £3.7m of inception adjustments under CCFS' entity level hedge accounting.
3. Recognition of additional gain on sale of securitised loans.
4. Amortisation of intangible assets recognised on Combination.
5. Adjustment to expected credit losses on CCFS loans on Combination.
6. Impairment of intangible asset post Combination.
7. Costs of integration of the two Banks post Combination.
8. Reversal of exceptional costs incurred during the year.
9. Recognition of a fair value uplift to CCFS' loan book less accumulated amortisation of the fair value uplift and a movement on credit provisions.
10. Fair value adjustment to hedged assets.
11. Adjustment to current tax asset and recognition of acquired intangibles on Combination.
12. Fair value adjustment to CCFS' retail deposits less accumulated amortisation.
13. Fair value adjustment to hedged liabilities.
14. Adjustment to deferred tax liability and other acquisition-related adjustments.

## Risk review

### Executive summary

During the year, the Group primarily focused on developing a considered and measured response to the global pandemic based on its strategic objectives, risk appetite and risk management capabilities. In particular, the Board and senior management ensured that the Group continued to operate with sufficient financial buffers and operational capacity to withstand any future extreme but plausible economic shocks.

The Group leveraged the underlying risk management frameworks to assess, monitor and respond to the emerging economic, business and operational challenges arising from the pandemic. The Group's response was subject to extensive planning, coordination and implementation oversight by the Board and senior management through both formal Committee meetings and ad hoc engagement sessions. The Group benefitted greatly from the extensive and diverse risk management experience of the Board and senior management during all phases of the pandemic.

The Group's response to the pandemic has been centrally coordinated whilst being cognisant of the specific business and operational characteristics of the individual banking entities. The Board and senior management responded quickly to assess the potential implications and impacts of the emerging pandemic across all identified principal risks, with a particular focus on credit, capital, liquidity and operational risks.

Well established stress testing and analytical capabilities were leveraged to identify the risks and vulnerabilities to the business, and economic and operational drivers which may be impacted by the pandemic. This analysis highlighted the potential implications of the pandemic on the Group's assets, liabilities, funding and solvency positions, operational capacity and customers. Continued and progressive enhancements were made to the risk assessment approaches to ensure that the Group's response was aligned to the evolving nature of the pandemic.

The Board and senior management maintained an open and active dialogue with primary stakeholders including employees, customers and regulatory authorities throughout 2020.

At the onset of the pandemic, the Group took appropriate actions to ensure full compliance with social distancing and lockdown guidelines, utilising its business continuity and operational resilience frameworks. As the majority of the Group's workforce transitioned to working from home, the Group took appropriate actions to ensure operational risks were subject to active identification, assessment and monitoring.

As payment deferral guidelines were introduced, the Group took timely actions to ensure effective compliance with the emerging regulatory guidelines, swiftly updating its risk modelling and provisioning approaches, whilst modifying its operational procedures to ensure an effective response to customers requesting payment deferrals.

The Group updated its IFRS 9 provisioning approach to reflect the emerging pandemic-based economic scenarios, including the varied permutations of how the UK economy may be impacted. Appropriate adjustments were also applied to the underlying model-based judgements and estimates. The Group continuously monitored and updated its credit provisioning approach. The Group remains mindful of the potential for future risks which may manifest themselves post the removal of the government support schemes, particularly the furlough scheme, and is confident that its provisioning approach is sufficiently agile and responsive to emerging trends and issues.

**Risk review** (continued)

To ensure that the quantum of model-based provisions remained appropriate, a top-down triangulation exercise was commissioned by the Board. The top-down assessment benchmarked IFRS 9 provisions to historical stresses, peer assessment and look through assessments of Buy-to-Let (BLT), residential and commercial portfolios, to underlying borrower and tenant characteristics. The IFRS 9 based provisions were supported by the independent top-down triangulation exercise.

The Group also adjusted its risk appetite, primarily through tightening its lending criteria to effectively manage the risk of lending in a highly disrupted and economically uncertain market. The actions taken were framed to ensure that the Group maintained its asset quality profile whilst sustaining its core lending brands and delivering appropriate levels of balance sheet growth.

Following extensive review, the Board approved actions to strengthen the liquidity positions across both banking entities through drawdowns under the Bank of England Indexed Long-Term Repo facility, which were later replaced with drawings from the new Term Funding Scheme for SMEs (TFSME). Both bank entities continued to retain prudent levels of liquidity, considering the uncertain economic outlook. The Group's capital position strengthened throughout the year, supported by actions taken such as the cancellation of the 2019 final dividend, tightened lending criteria and the impact of regulatory capital preservation rule changes as outlined within the PRA's 'Quick Fix' package, which included revisions to the IFRS 9 transitional arrangements for the capital impact of IFRS 9 expected credit losses and revisions to the small and medium-sized enterprises support factor.

The Risk and Compliance function provided extensive oversight and advisory support to customer-facing functions enabling the Group to respond effectively to customer expectations, regulatory guidelines and the conduct and compliance-based risk appetite. The Group ensured that customers' account performance was reported to credit reference agencies, in accordance with regulatory guidance.

To enable the Board and senior management to remain fully abreast of the evolving impact of the pandemic, the level and frequency of risk-based analysis and management information were increased. Information provided was used to monitor customer behaviours and outcomes, whilst also detailing sensitivity and stress test analysis on capital, IFRS 9 provision levels and funding metrics. Reverse stress test and recovery option analysis was also performed to inform the going concern assessment of the Group and its banking entities. Operational capacity thresholds were actively monitored and reported to ensure timely action was taken to enable continuity of all key services.

Despite the highly disruptive and uncertain business, economic and operating environment, the Group continued to operate within the defined risk appetite levels. Some risk metrics have operated outside acceptable thresholds, such as expected credit losses, however, the underlying performance of the loan portfolios remained broadly stable with respect to borrower credit profiles, arrears and loan to value (LTV) levels, notwithstanding the potential fraud by a third party on a funding line provided by the Group, secured against lease receivables and the underlying hard assets. The number of customers who requested payment deferrals reduced progressively throughout 2020 to only 1.3% of the Group's loan book by value as at year end.

We continued to make good progress towards IRB during the year, albeit some elements of the project were inevitably delayed by the impact of COVID-19, which created the need to deploy significant resources to support additional stress testing and expected credit loss modelling and also restricted the ability of external advisers to access our premises and systems. Nevertheless, we are still aiming to submit our module 1 application by the end of 2021. In the meantime, the Group continues to benefit from the enhanced risk models and assessment in its decision making.

**Risk review** (continued)

The Group maintained prudent levels of contingent financial resources to sustain its business operations and to withstand an extreme but plausible stress. Operational resilience was also demonstrated by the fact that, during lockdowns, a fundamental change to the Group's operating model did not result in a material operational risk incident or an increase in realised operational risk losses.

The Board and senior management remain mindful of the continuously evolving nature of the pandemic and are fully engaged to ensure that appropriate and timely actions continue to be taken, such that the Group continues to operate within its specific risk appetite levels and delivers against its stated strategic objectives.

**Key achievements in 2020**

During the year, the Group sustained momentum on strategically important risk and compliance initiatives. In particular, the Board and senior management were mindful of ensuring that the pandemic did not impact continued progress and investment in the following initiatives:

- Design and implementation of a comprehensive framework to assess and report on pandemic-based risks, leveraging enhanced risk data and analytical capabilities.
- The development and implementation of key Group level frameworks and policies. In particular, a transitional overarching Group Risk Management Framework was developed, including Group risk appetite statements and limits.
- Though the Group continues to maintain two independently regulated banking entities, the Risk and Compliance functions have been transitioned to a shared service operating model, whereby the individual functions and teams are Group based, providing necessary supporting services to the entity specific Boards and wider business functions.
- Completion of Group and banking entity Internal Capital Adequacy Assessment Processes (ICAAPs), including risk and capital-based assessments which were consistent in approach but reflect the individual banking entity risk profiles. Climate change risks, including physical risks and transitional risks, associated with transitioning to a low carbon economy, were also assessed as part of the ICAAP development process.
- Delivery of aligned liquidity and funding risk assessment and monitoring capabilities, which will support the Group and solo banks' Internal Liquidity Adequacy Assessment Processes (ILAAPs).
- Continued progress against the Group IRB programme agenda, including development of next generation models, enhanced model performance monitoring, governance and integration of IRB-based outputs within wider business and decision-making processes.
- Integration risk was also identified as a principal risk and is subject to the necessary disciplines as articulated in the Group Risk Management Framework. Integration risk is identified as a risk to and from the integration programme which is subject to review, monitoring and reporting against an integration risk appetite. Key integration activities are subject to second and third line oversight and assurance activity.
- Operational resilience assessment and management has progressively been aligned across the two banking entities, and was subject to a review against emerging regulatory expectations. The Group's operational resilience capabilities helped to guide the response to the operational disruptions resulting from the pandemic.
- Continued improvement and alignment of vulnerable customer identification and management procedures. During the period, the Group performed a number of internal thematic reviews to ensure that account management procedures resulted in fair customer outcomes and any learning from these reviews were used to further enhance customer management strategies.

**Risk review** (continued)

**Priority areas for 2021**

The ongoing COVID-19 pandemic continues to contribute to significant uncertainty around the macroeconomic outlook and operating environment for 2021. Therefore, continued close monitoring of the Group's risk profile and operating effectiveness remains a key priority.

Further development and embedding of the overarching Group risk management framework also remains a key priority, including:

- Continued integration of the Risk and Compliance functions in accordance with the target end state, reflecting industry best practice and regulatory expectations.
- Development and embedding of Group-level recovery and resolution plans. The Risk function is also committed to ensuring effective and timely compliance with the requirements of the Resolution Assessment Framework over the coming two years, whilst providing oversight and advisory support with respect to the Group's minimum requirement for own funds and eligible liabilities (MREL) strategy and planning.
- Delivering further enhancements to the Group and individual entity ILAAPs and related liquidity risk management arrangements.
- Further embedding of the Group's IRB risk measurement capabilities including the monitoring and management of the credit risk profile utilising enhanced analytics, to ensure improved credit decisioning, pricing and risk management. Continued progression of the Group's IRB programme in accordance with defined timelines also remains a key area of focus.
- Alignment of operational risk management systems and operational risk frameworks across the Group.
- Continued close monitoring, scenario analysis and stress testing of the Group's capital and liquidity projections.
- Delivery of a climate change risk management framework covering both physical and transitional risks.

The Board and senior management are fully committed to achieving the objectives above through continued investment in people, systems, data and processes.

**Risk review** (continued)

**Risk management**

**Approach to risk management**

The Group views its capabilities to effectively identify, assess and manage its risk profile as critical to its growth strategy. The Group has developed a transitional overarching Risk Management Framework (RMF) to drive a consistent approach to risk identification and assessment across both licensed bank entities. This framework will continue to evolve and be updated as integration activity continues prior to the Group reaching its target end state.

The RMF is the overarching framework which enables the Board and senior management to actively manage and optimise the risk profile within the constraints of the risk appetite. The RMF also enables informed risk-based decisions to be taken in a timely manner, ensuring the interests and expectations of key stakeholders can be met.

The RMF also provides a structured mechanism to align critical components of an effective approach to risk management. The RMF links overarching risk principles to day-to-day risk monitoring and management activities.

The modular construct of the RMF provides an agile approach to keeping pace with the evolving nature of the risk profile and underlying drivers. The RMF and its core modular components are subject to periodic review and approval by the Board and its relevant Committees. The key modules of the RMF structure are as follows:

1. Risk principles and culture - the Group has established a set of risk principles which inform and guide all risk management activities and it has a strong, proactive and transparent 'risk culture' where all employees across the Group are aware of their responsibilities in relation to risk management.
2. Risk strategy and appetite – the Group has a clear business purpose, vision and values strategy which is supported by an articulated risk vision and underlying principles. The Group calibrates its risk appetite to reflect the Group's strategic objectives and business operating plans, as well as external economic, business and regulatory constraints.
3. Risk assessment and control – the Group's business model and strategy exposes it to a defined risk profile and the risk governance structure is informed by this risk profile such that the Group can identify and manage its risks in an effective and efficient manner.
4. Risk definitions and categorisation – the Group sets out its principal risks which represent the primary risks to which the Group is exposed.
5. Risk analytics (including stress testing and scenario analysis) – the Group uses quantitative analysis and statistical modelling to help improve its business decisions.
6. Risk data and Information Technology – the maintenance of high quality risk information, along with the Group's data enrichment and aggregation capabilities, are central to the Risk function's objectives being achieved.
7. Risk frameworks, policies and procedures – risk frameworks, policies and supporting documentation outline the process by which risk is effectively managed and governed within the Group.
8. Risk management information (MI) and reporting – the Group has established a comprehensive suite of risk MI and reports covering all principal risk types.

**Risk review** (continued)

9. Risk governance and function organisation – risk governance refers to the processes and structures established by the Board to ensure that risks are assumed and managed within the Board-approved risk appetite, with clear delineation between risk taking, oversight and assurance responsibilities. The Group's risk governance framework is structured to adhere to the 'three lines of defence' model.

**Risk appetite**

The Group aligns its strategic and business objectives with its risk appetite, enabling the Board and senior management to monitor the risk profile relative to its strategic and business performance objectives. Risk appetite is a critical mechanism through which the Board and senior management are able to identify adverse trends and respond to unexpected developments in a timely and considered manner.

The Group risk appetite is articulated by means of a series of statements which outline the level and nature of risks that the Group is able and willing to assume in pursuit of its strategic and business objectives. These statements are further supported by a suite of risk thresholds which ensure that the Group's risk profile is monitored and controlled within defined parameters and that appetite breaches are subject to appropriate management and Board oversight. The Risk Appetite Framework also helps to outline roles and responsibilities relating to all aspects of the risk appetite, based on a defined structure, processes, procedures and governance.

Risk appetite is calibrated to reflect the Group's strategic objectives, business operating plans, as well as external economic, business and regulatory constraints. In particular, risk appetite is calibrated to ensure that the Group continues to deliver against its strategic and business objectives and maintains sufficient financial resource buffers to withstand plausible but extreme stresses. The primary objective of the risk appetite is to ensure that the Group's strategy and business operating model is sufficiently resilient.

The Group's risk appetite is calibrated using statistical analysis and stress testing to inform the process for setting management triggers and limits against key risk indicators. The calibration process is designed to ensure that timely and appropriate actions are taken to maintain the risk profile within approved thresholds. The Board and senior management actively monitor actual performance against approved management triggers and limits. Currently, whilst there are two regulated banking entities within the Group, risk appetite metrics and thresholds are set at both individual entity and Group levels.

The Group's risk appetite is subject to a full refresh annually across all principal risk types and an additional mid-year review where any metrics can be assessed and updated as appropriate. The assessment of the Group's risk profile against its strategy and risk appetite has been enhanced to ensure early detection and response to adverse trends.

**Risk review** (continued)

**Approach to managing climate change risk**

Climate change and society's response to it, may result in a number of financial risks materialising. Supervisory statement 3/19 was published in April 2019 and it sets out the PRA's expectations concerning financial services firms developing their approaches to identifying, monitoring and controlling climate change risk relevant to their specific business.

The PRA published a 'Dear CEO' letter in July 2020 emphasising its expectations for firms to have fully embedded their approaches to managing climate-related financial risk by the end of 2021.

The Group is exposed to physical, transitional and reputational risks relating to climate change:

- Physical risks and the risks associated with a transition to a low carbon economy, arise from a number of factors, and relate to specific weather events (such as heatwaves, floods, wildfires and storms) and longer-term shifts in the climate (such as changes in precipitation, extreme weather variability, rising sea level risk and rising mean temperatures). These risks could include adverse movements in the value of certain properties that are in coastal or low lying areas, or located in areas prone to increased subsidence and heave such as clay soils.
- Transitional risks may arise from the process of adjustment towards a low-carbon economy which may lead to changes in policy, regulation, the emergence of disruptive technology or business models shifting sentiment, and societal preferences, or evolving evidence, frameworks and legal interpretations. These risks include a potential adverse impact in the value of properties that require substantial updating to meet future energy performance requirements.
- Reputational risk arising from a failure to meet changing societal, investor or regulatory demands.

**How the Group identifies and assesses climate change risk**

Within the Group's 2020 ICAAP, a number of financial and transitional climate change risks were identified, and a series of detailed financial risk assessments (IFRS 9 impairment and capital) were conducted over a range of scenarios to quantify the potential impact on the Group, should any of the scenarios materialise. This process was supported by the acquisition of data from an external third party.

The key conclusion from this analysis was that the Group is currently exposed to a low level of climate change risk, when assessing the potential impairment and capital impacts over a range of physical perils such as flooding, subsidence and coastal erosion across the Group's loan book. The Risk function also analysed the energy performance certificate (EPC) profile of the Buy-to-Let loan book and the risks relating to landlords having extensive remediation activity to ensure an appropriate EPC rating is in place. Again, this analysis indicated that the Group's EPC profile is strong and the modelled impact of remediation remains low.

The ongoing provision of this data will allow the Group to monitor how its climate change risk profile evolves over time, and consequently take action if required to ensure that the risk of climate change remains at an acceptable level.

**Processes in place to manage climate change risk**

Climate change risk impacts a number of the Group's other principal risk types, therefore work is ongoing to assess the wider consequences across the Group. This will involve the management of climate change risk being overseen by a number of the Group's Risk Committees.

**Risk review** (continued)

**How the management of climate change risk is integrated within the Group's wider risk management approaches**

The Board has overseen the Group's plans to comply with the PRA's expectations and emerging industry best practice around climate change risk management, with progress made across the following areas during 2020:

- The overarching Risk Management Framework was updated to articulate the Group's approach to climate change risk management.
- A dedicated working group was established to oversee and manage the Group's response to climate change risk.
- A detailed financial risk assessment of the Group's exposure to climate change risk was conducted as part of the 2020 ICAAP.
- The Chief Risk Officers of the two banks have designated senior management function (SMF) responsibility for the management of climate change risk.

During 2021 the Group plans to further enhance and embed its approaches to identifying, monitoring and managing climate change risk, including the development of a dedicated Climate Change Risk Management Framework, coupled with further enhancements to climate change risk profile monitoring, whilst conducting further sensitivity analysis. The development of formal climate change risk appetite statements and limits, together with a full suite of key risk and performance indicators, is also planned. Plans will be developed in the first half of 2021 to ensure that the Group complies with the recommendations set out by the Task Force on Climate-related Financial Disclosures, which have been introduced into UK listing requirements on or after 1 January 2021.

**Principal risks and uncertainties**

The Board carried out an assessment of the principal risks and uncertainties which may threaten the Group's operating model, strategic objectives, financial performance and regulatory compliance commitments. The outcome of that assessment is summarised in each principal risk section below.

<u>Strategic and business risk</u>

Definition
The risk to the Group's earnings and profitability arising from its strategic decisions, change in business conditions, improper implementation of decisions or lack of responsiveness to industry changes.

Risk appetite statement
The Group's strategic and business risk appetite states that the Group does not intend to undertake any medium to long-term strategic actions that would put at risk its vision of being a leading specialist lender, backed by a strong and dependable saving franchise. The Group adopts a long-term sustainable business model which, while focused on niche sub-sectors, is capable of adapting to growth objectives and external developments.

### **Principal risks and uncertainties** (continued)

| Risk | Mitigation | Direction |
|---|---|---|
| **Performance against targets**<br><br>Performance against strategic and business targets does not meet stakeholder expectations. This has the potential to damage the Group's franchise value and reputation. | Regular monitoring by the Board and the Group Executive Committee of business and financial performance against strategic agenda and risk appetite. The financial plan is subject to regular reforecasts. The balanced business scorecard is the primary mechanism to support the Board and assesses management performance against key targets. Use of stress testing to flex core business planning assumptions to assess potential performance under stressed operating conditions. | **Increased**<br><br>The COVID-19 pandemic has adversely impacted the Group in meeting its strategic and business targets.<br><br>Opportunities remain, including the Group realising integration benefits as planned, which will support the Group in any future macroeconomic stress, whilst managing challenges posed by increasing levels of competition in our key market segments. |
| **Economic environment**<br><br>The economic environment in the UK is an important factor impacting the strategic and business risk profile.<br><br>A macroeconomic downturn may impact the credit quality of the Group's existing loan portfolio and may influence future business strategy as the Group's new business proposition becomes less attractive due to lower returns. | The Group continued to utilise and enhance its stress testing capabilities to assess and minimise potential areas of macroeconomic vulnerability. | **Increased**<br><br>Economic risks remain elevated due to the ongoing COVID-19 pandemic and risks surrounding the removal of government support measures.<br><br>The risk relating to a no trade deal Brexit subsided following an agreement being reached, however the full implications of the deal arrangements being operationalised are yet to be observed. |
| **Regulatory requirements**<br><br>The potential for emerging regulatory requirements to increase the demands on the Group's operational capacity and increase the cost of compliance. | The Group continues to invest in its IT and data management capabilities to increase the ability to respond to regulatory change.<br><br>A structured approach to change management and fully leveraging internal and external expertise allows the Group to respond effectively to regulatory change. | **Increased**<br><br>Increased levels of regulatory scrutiny and greater regulatory expectations are driven by the increased size of the Group post Combination. |
| **Competition risk**<br><br>The risk that new bank entrants and existing peer banks shift focus to the Group's market segments, which increases the level of competition. | The Group continues to develop products and services which meet the requirements of the markets in which it operates.<br><br>Post the Combination, the Group has an enlarged suite of products and capabilities to utilise, along with increased scale and financial resources to support a response to changes in competition. | **Unchanged**<br><br>The Group responded well to all competition and market changes throughout 2020 and is well positioned to respond to changes in competition in 2021. |

Reputational risk

Definition

**The potential risk of adverse effects that can arise from the Group's reputation being affected due to** factors such as unethical practices, adverse regulatory actions, customer dissatisfaction and complaints or negative/adverse publicity.

Reputational risk can arise from a variety of sources and is a second order risk – the crystallisation of a credit risk or operational risk can lead to a reputational risk impact.

**Principal risks and uncertainties** (continued)

Risk appetite statement
The Group does not knowingly conduct business or organise its operations to put its reputation and franchise value at risk.

| Risk | Mitigation | Direction |
|---|---|---|
| **Deterioration of reputation**<br><br>Potential loss of trust and confidence that our stakeholders place in us as a responsible and fair provider of financial services. | Culture and commitment to treating customers fairly and being open and transparent in communication with key stakeholders. Established processes to proactively identify and manage potential sources of reputational risk. | **Unchanged**<br><br>Expectations remain high to deliver the integration in a timely and effective manner while achieving strategic objectives. Expectations have been raised across all stakeholders, including employees, customers, regulators and shareholders. |

Credit risk

Definition
Potential for loss due to the failure of a counterparty to meet its contractual obligation to repay a debt in accordance with the agreed terms.

Risk appetite statement
The Group seeks to maintain a high quality lending portfolio that generates adequate returns, under normal and stressed conditions. The portfolio is actively managed to operate within set criteria and limits based on profit volatility, focusing on key sectors, recoverable values, and affordability and exposure levels. The Group aims to continue to generate sufficient income and control credit losses to a level such that it remains profitable even when subjected to a credit portfolio stress of a 1 in 20 intensity stress scenario.

**Principal risks and uncertainties** (continued)

| Risk | Mitigation | Direction |
| --- | --- | --- |
| **Individual borrower defaults**<br><br>Borrowers may encounter idiosyncratic problems in repaying their loans, for example loss of a job or execution problems with a development project.<br><br>While in most cases of default the Group's lending is secured, some borrowers may fail to maintain the value of the security. | Across both OSB and CCFS, a robust underwriting assessment is undertaken to ensure that a customer has the ability and propensity to repay and sufficient security is available to support the new loan requested. At CCFS, an automated scorecard approach is taken, whilst OSB utilises a bespoke manual underwriting approach.<br><br>Should there be problems with a loan, the Collections and Recoveries team works with customers who are unable to meet their loan service obligations to reach a satisfactory conclusion while adhering to the principle of treating customers fairly.<br><br>Our strategic focus on lending to professional landlords means that properties are likely to be well-managed, with income from a diversified portfolio mitigating the impact of rental voids or maintenance costs. Lending to owner-occupiers is subject to a detailed affordability assessment, including the borrower's ability to continue payments if interest rates increase. Lending on commercial property is based more on security, and is scrutinised by the Group's independent Real Estate team as well as by external valuers.<br><br>Development lending is extended only after a deep investigation of the borrower's track record and stress testing the economics of the specific project. | **Increased**<br><br>The impact of COVID-19 on the UK economy is uncertain and could result in a material increase in unemployment levels and decreases in property prices, which could drive higher impairment levels.<br><br>The impact of the government support measures ending remains unknown and the knock-on impact into borrower defaults thereafter. |
| **Macroeconomic downturn**<br><br>A broad deterioration in the UK economy would adversely impact both the ability of borrowers to repay loans and the value of the Group's security. Credit losses would impact the Group's lending portfolios, even if individual impacts were to be small, the aggregate impact on the Group could be significant. | The Group works within portfolio limits on LTV, affordability, name, sector and geographic concentration that are approved by the Group Risk Committee and the Board. These are reviewed on a semi-annual basis. In addition, stress testing is performed to ensure that the Group maintains sufficient capital to absorb losses in an economic downturn and continues to meet its regulatory requirements. | **Increased**<br><br>The economic outlook is uncertain, driven by the potential range of outcomes resulting from COVID-19 and the end of government support measures. |
| **Wholesale credit risk**<br><br>The Group has wholesale exposures both through call accounts used for transactional and liquidity purposes and through derivative exposures used for hedging. | The Group transacts only with high quality wholesale counterparties. Derivative exposures include collateral agreements to mitigate credit exposures. | **Unchanged**<br><br>The Group's wholesale credit risk exposure remains limited to high quality counterparties, overnight exposures to clearing banks and swap counterparties. |

**Principal risks and uncertainties** (continued)

Market risk

Definition
Potential loss due to changes in market prices or values.

Risk appetite statement
The Group actively manages market risk arising from structural interest rate positions. The Group does not seek to take a significant interest rate position or a directional view on interest rates and it limits its mismatched and basis risk exposures.

| Risk | Mitigation | Direction |
|---|---|---|
| **Interest rate risk**<br><br>The risk of loss from adverse movement in the overall level of interest rates. It arises from mismatches in the timing of repricing of assets and liabilities, both on and off balance sheet. It includes the risks arising from imperfect hedging of exposures and the risk of customer behaviour driven by interest rates, e.g. early redemption. | The Group's Treasury function actively hedges to match the timing of cash flows from assets and liabilities. | **Unchanged**<br><br>The Group continues to assess interest rate risk on a regular basis ensuring that risk exposure is limited. |
| **Basis risk**<br><br>The risk of loss from an adverse divergence in interest rates. It arises where assets and liabilities reprice from different variable rate indices. These indices may be market rates (e.g. Bank Base Rate, Sterling Overnight Index Average (SONIA), or the London Interbank Offered Rate (LIBOR)) or administered (e.g. the Bank's Standard Variable Rate (SVR), other discretionary variable rates, or that received on call accounts with other banks). | Due to the Group balance sheet structure, no active management of basis risk was required by the Group during 2020.<br><br>Key mitigants include new swaps being linked to SONIA and existing LIBOR linked swaps being transitioned to SONIA. LIBOR linked mortgages will also be transitioned to referencing either the Bank of England base rate or SONIA. | **Unchanged**<br><br>Product design, balance sheet structure and replacing LIBOR swaps with SONIA swaps enabled the Group to maintain the overall level of basis risk across both Banks throughout the year.<br><br>The basis risk position will reduce over 2021 as CCFS and OSB fully transition from LIBOR. |

Liquidity and funding risk

Definition
The risk that the Group, although solvent, does not have sufficient financial resources to enable it to meet its obligations as they fall due.

Risk appetite statement
The Group will maintain sufficient liquidity to meet its liabilities as they fall due under normal and stressed business conditions; this will be achieved by maintaining a strong retail savings franchise, supported by a high quality liquid asset portfolio comprised of cash and readily-monetisable assets, and through access to pre-arranged secured funding facilities. The Board requirement to maintain balance sheet resources sufficient to survive a range of severe but plausible stress scenarios is interpreted in terms of the liquidity coverage ratio and the ILAAP stress scenarios.

### Principal risks and uncertainties (continued)

| Risk | Mitigation | Direction |
|---|---|---|
| **Retail funding stress**<br><br>As the Group is primarily funded by retail deposits, a retail run could put it in a position where it could not meet its financial obligations.<br><br>Increased competition for retail savings driving up funding costs, adversely impacting retention levels and profitability. | The Group's funding strategy is focused on a highly stable retail deposit franchise. The Group's large number of depositors provides diversification, where a high proportion of balances are covered by the FSCS protection scheme, thus there is no material risk of a retail run.<br><br>In addition, the Group performs in-depth liquidity stress testing and maintains a liquid asset portfolio sufficient to meet obligations under stress. The Group holds prudential liquidity buffers to manage funding requirements under normal and stressed conditions.<br><br>The Group has further diversified its retail channels bycexpanding the range of pooled deposit providers used.<br><br>The Group proactively manages its savings proposition through both the Liquidity Working Group and the Group Assets and Liabilities Committee. Finally, the Group has prepositioned mortgage collateral and securitised notes with the Bank of England which allows it to consider alternative funding sources to ensure it is not solely reliant on retail savings. The Group also has a mature RMBS programme and access to warehouse facilities. | **Unchanged**<br><br>The Group's funding levels and mix remained strong throughout the year.<br><br>During the year, OSB and CCFS were both able to attract significant flows of new deposits and depositors when required. |
| **Wholesale funding stress**<br><br>A market-wide stress could close securitisation markets or make issuance costs unattractive for the Group. | The Group continuously monitors wholesale funding markets and is experienced in taking proactive management actions where required.<br><br>The Group issued a number of securitisations during 2020 where both CCFS and OSB saw strong market demand for secured wholesale issuance. | **Unchanged**<br><br>The Group's range of wholesale funding options available, including repo or sale of retained notes, collateral upgrade trades and warehouse facilities, remains broadly unchanged. |
| **Refinancing of Term Funding Scheme (TFS) and TFSME**<br><br>The Group has drawn a total of £2.6bn funding under the TFS and £1.0bn under the TFSME creating a refinancing concentration around the maturity of the schemes. | The Group has fully factored in repayment of TFS into the funding plans of both Banks, with planned repayment prior to the contractual date to minimise timing and concentration risk. The Group has a wider range of funding options to manage this process.<br><br>The Group has a TFSME allowance significantly above its wholesale funding requirements which allows the TFS scheme to be fully refinanced by TFSME. | **Decreased**<br><br>The TFSME scheme will allow the Group to significantly extend the maturities of its Bank of England based funding. |

**Principal risks and uncertainties** (continued)

Solvency risk

Definition
The potential inability of the Group to ensure that it maintains sufficient capital levels for its business strategy and risk profile under both the base and stress case financial forecasts.

Risk appetite statement
The Group and each regulated bank seeks to ensure that it is able to meet its Board-level capital buffer requirements under a severe but plausible stress scenario. The solvency risk appetite is informed by the Group's and each regulated bank's prudential requirements and strategic and financial objectives. We manage our capital resources in a manner which avoids excessive leverage and allows us flexibility in raising capital.

| Risk | Mitigation | Direction |
|---|---|---|
| **Deterioration of capital ratios**<br><br>Key risks to solvency arise from balance sheet growth and unexpected losses which can result in the Group's capital requirements increasing, or capital resources being depleted, such that it no longer meets the solvency ratios as mandated by the PRA and Board risk appetite.<br><br>The regulatory capital regime is subject to change and could lead to increases in the level and quality of capital that the Group needs to hold to meet regulatory requirements. | Currently the Group operates from a strong capital position and has a consistent record of strong profitability.<br><br>The Group actively monitors its capital requirements and resources against financial forecasts and plans and undertakes stress testing analysis to subject its solvency ratios to extreme but plausible scenarios.<br><br>The Group also holds prudent levels of capital buffers based on CRD IV requirements and expected balance sheet growth.<br><br>The Group engages actively with regulators, industry bodies, and advisers to keep abreast of potential changes and provides feedback through the consultation process. | **Unchanged**<br><br>Proactive management of the Group's balance sheet and support measures provided by the PRA via the CRR 'Quick Fix' package which included a reset of the IFRS 9 capital transitional relief and the extension of the SME support factor, together with ongoing profitability, resulted in the Group's capital ratios strengthening.<br><br>Risks remain around adverse credit profile performance, resulting from the ongoing COVID-19 pandemic and the removal of government support measures. |

Operational risk

Definition
The risk of loss or a negative impact on the Group resulting from inadequate or failed internal processes, people or systems, or from external events.

Risk appetite statement
The Group's operational processes, systems and controls are designed to minimise disruption to customers, damage to the Group's reputation and any detrimental impact on financial performance. The Group actively promotes the continual evolution of its operating environment through the identification, evaluation and mitigation of risks, whilst recognising that the complete elimination of operational risk is not possible.

**Principal risks and uncertainties** (continued)

| Risk | Mitigation | Direction |
|---|---|---|
| **IT security (including cyber risk)**<br><br>The risks resulting from a failure to protect the Group's systems and the data within them. This includes both internal and external threats. | The Group invested significantly in enhancing its protection against IT security threats, deploying a series of tools designed to identify and prevent network/system intrusions. This is further supported by documented and tested procedures intended to ensurethe effective response to a security breach. | **Increased**<br><br>Due to the COVID-19 pandemic and the resulting high number of employees working and accessing systems from home, the risk of a cyber-attack was heightened.<br><br>Whilst IT security risks continue to evolve, the level of maturity of the Group's controls and defences has significantly increased, supported by dedicated IT security experts.<br><br>The Group's ongoing penetration testing continues to drive enhancements by identifying potential areas of risk. |
| **Data quality and completeness**<br><br>The risks resulting from data being either inaccurate or incomplete. | The Group established a dedicated Data Strategy Programme, designed to ensure a consistent approach to the maintenance and use of data. This includes both documented procedures and frameworks and also tools intended to improve the consistency of data use. | **Unchanged**<br><br>Further progress was made during 2020 in embedding Group-wide governance frameworks, standards and controls. Further work is planned in 2021, to move closer to the Group's target end state. |
| **Change management**<br><br>The risks resulting from unsuccessful change management implementations, including the failure to respond effectively to release-related incidents. | The Group recognises that implementing change introduces significant operational risk and has therefore implemented a series of control gateways designed to ensure that each stage of the change management process has the necessary level of oversight. | **Increased**<br><br>The Group continues to adopt an ambitious change agenda, driven by the integration programme. During 2020 this risk was monitored and managed well, however further change is planned in 2021, against the backdrop of the ongoing COVID-19 pandemic and likely periods of employees working from home. |
| **IT failure**<br><br>The risks resulting from a major IT application or infrastructure failure impacting access to the Group's IT systems. | The Group continues to invest in improving the resilience of its core infrastructure. It has identified its prioritised business services and the infrastructure that is required to support them. Tests are performed regularly to validate its ability to recover from an incident. | **Unchanged**<br><br>Whilst progress was made in reducing both the likelihood and impact of an IT failure, the risks remain, in particular due to the new operating environment. Further work is planned during 2021. |
| **Organisational change and integration**<br><br>The risks resulting from the Group's ongoing integration activities, including systems, people and infrastructure. | There is a low risk integration project plan (e.g. no large-scale integration-related IT project change planned). The Group has an experienced and capable project management office, with close oversight and direction provided by the Group Executive and Board Integration Committees. | **Unchanged**<br><br>To date, organisational change resulting from the integration project has been managed well, with no material risks emerging during 2020. Further work is required to reach the target end state and carefully considered plans, strong risk identification and monitoring and management capabilities remain in place. |

**Principal risks and uncertainties** (continued)

Conduct risk

Definition
The risk that the Group's behaviours or actions result in customer detriment or negatively impact the integrity of the markets in which it operates.

Risk appetite statement
The Group aims to operate and conduct its business to the highest standards which ensure integrity and trust with respect to how the Group operates and manages its relationships with key stakeholders. In this regard, the Group has no appetite to knowingly assume risks which may result in an unfair outcome for customers and/or cause disruptions in the market segments in which it operates. However, where the Group identifies potential conduct risks it will proactively intervene by managing, escalating and mitigating them promptly to ensure a fair outcome is achieved.

| Risk | Mitigation | Direction |
|---|---|---|
| **Product suitability**<br><br>Whilst the Group originates relatively simple products, there remains a risk that products (primarily legacy) may be deemed to be unfit for their original purpose in line with current regulatory definitions. | The Group has a strategic commitment to provide simple, customer-focused products. In addition, a Product Governance framework is established to oversee both the origination of new products and to revisit the ongoing suitability of the existing product suite. | **Unchanged**<br><br>Whilst this risk remained low as a result of increased awareness and dedicated oversight, the Group remains aware of the changes to the regulatory environment and their possible impact on product suitability. |
| **Data protection**<br><br>The risk that customer data is accessed inappropriately, either as a consequence of network/ system intrusion or through operational errors in the management of the data. | In addition to a series of network/system controls, the Group performs extensive root cause analysis of any data leaks in order to ensure that the appropriate mitigating actions are taken. | **Unchanged**<br><br>Despite a number of additional controls introduced in 2020, the network/system threats continue to evolve in both volume and sophistication. |
| **Integration risk**<br><br>The risk that the integration programme directly or indirectly causes poor outcomes for customers and the market. | During the integration process, the Group is committed to adopting a low-risk approach with a view to taking reasonable steps to avoid causing poor outcomes for its customers and the market. The Group will conduct detailed analysis of potential customer harm associated with particular integration steps. | **Unchanged**<br><br>No material issues have been identified to date and controls are in place to ensure that the integration programme does not result in poor customer outcomes. |

Compliance / regulatory risk

Definition
The risk that a change in legislation or regulation, or an interpretation that differs from the Group's, will adversely impact the Group.

Risk appetite statement
The Group views ongoing conformity with regulatory rules and standards across all the jurisdictions in which it operates as a critical component of its risk culture. The Group does not knowingly accept compliance risk which could result in regulatory sanctions, financial loss or damage to its reputation. The Group will not tolerate any systemic failure to comply with applicable laws, regulations or codes of conduct relevant given its business operating model.

## Principal risks and uncertainties (continued)

| Risk | Mitigation | Direction |
|---|---|---|
| **Prudential regulatory changes**<br><br>The Group continues to see a high volume of key compliance regulatory changes that impact its business activities. These include: change in Standardised Approach capital rules and implementation of an IRB floor, implementation of the European Standardised Information Sheet, extending the Senior Managers and Certification Regime to all FCA regulated firms and introduction of Strong Customer Authentication requirements.<br><br>The focus on external wall cladding for high-rise buildings was extended to smaller buildings in February 2021, and the value of properties supporting the Group's loan portfolios could be impacted, or customer behaviour could change if significant remediation activity is required to ensure building safety regulations are met. | The Group has an effective horizon scanning process to identify regulatory change.<br><br>All significant regulatory initiatives are managed by structured programmes overseen by the Project Management team and sponsored at Executive level.<br><br>The Group has proactively sought external expert opinions to support interpretation of the requirements and validation of its response, where required.<br><br>The Group has initiated a study into external wall cladding and is reviewing its own property portfolio along with the collateral supporting lending portfolios. The Group also notes the recent support measures announced by the Government to help individuals to ensure compliance with building safety standards, including the removal of defective cladding. | **Unchanged**<br><br>The Group continues to have a high level of interaction with the UK regulators and continues to respond effectively to all regulatory changes. |
| **Conduct regulation**<br><br>Regulatory changes focused on the conductof business could force changes in the way the Group carries out business and impose substantial compliance costs.<br><br>Product design, underwriting, arrears and forbearance policies are misaligned to regulatory expectations which result in customers not being treated fairly, particularly those experiencing financial hardship or vulnerable customers, with the potential for reputational damage, redress and other regulatory actions. | The Group has a programme of regulatory horizon scanning linking into a formal regulatory change management programme. In addition, the focus on simple products and customer oriented culture means that current practice may not have to change significantly to meet new conduct regulations.<br><br>All Group entities utilise underwriting, arrears, repossession, forbearance and vulnerable customer policies which are designed to comply with regulatory rules and expectations. These policies articulate the Group's commitment to ensuring that all customers, including those who are vulnerable or experiencing financial hardship, are treated fairly, consistently and in a way that considers their individual needs and circumstances.<br><br>The Group does not tolerate any systematic failure to deliver fair customer outcomes. On an isolated basis, incidents can result in detriment due to human and/or operational failures. Where such incidents occur, they are thoroughly investigated, and the appropriate remedial actions are taken to address any customer detriment and prevent recurrence. | **Unchanged**<br><br>The level of regulatory change continues to be high, but the Group has sufficient resources and capabilities to respond to any changes in an effective and efficient manner.<br><br>During the year, the Group took part in a numberof FCA thematic reviews, including reviews on long-term forbearance in the second charge market and a Business model drivers and unaffordable lending review. |

**Principal risks and uncertainties** (continued)

Integration risk appetite statement

Definition
The risks resulting from the Group's ongoing integration activities, including business, operational and financial performance, systems, people and infrastructure.

Risk appetite statement
The Combination of OSB and CCFS is intended to enhance scale, bringing together resources and capabilities, and to explore further growth opportunities which deliver attractive long-term returns. The delivery against the integration strategy is framed within the Group's purpose, vision and values and the broader risk appetite. The integration is deemed to be inherently low risk owing to the retention of core operating brands, similarities of business models, no large-scale IT integration or substantial migration of customer accounts. Accordingly, the Board has a low risk appetite for adverse integration activity outcomes, which put the strategic rationale of the merger, the Group's purpose, vision and values or broader risk appetite at risk. In the event that integration workstreams are subject to delay or reprioritisation, the Board expects the rationale to be clearly understood and justified, with defined mitigation actions implemented, overseen by robust levels of governance.

| Risk | Mitigation | Direction |
|---|---|---|
| A reduction in the oversight of business as usual operational performance, increased risk to operational resilience via the change process, unintended staff attrition or infrastructure failure, which in turn adversely impact operating and financial performance. | The Board is maintaining oversight of the integration process through the Board Integration Committee. A dedicated Integration Management Office has been established to drive the integration process forward.<br><br>Independent assessment, monitoring and reporting is being undertaken by the Risk and Internal Audit functions. | **Unchanged**<br><br>To date the integration project has progressed as planned, and the governance, project management and control structures have operated effectively, with no material risks crystallising. |

**Principal risks and uncertainties** (continued)

The Group proactively scans for emerging risks which may have an impact on its ongoing operations and strategy. The Group considers its top emerging risks to be:

| Emerging risk | Description | Mitigating action |
|---|---|---|
| **Political and macroeconomic uncertainty** | The impact of COVID-19 and the removal of government support measures remains uncertain. The Group's lending activity is predominantly focused in the United Kingdom (with a legacy back book of mortgages in the Channel Islands) and, as such, will be impacted by any risks emerging from changes in the macroeconomic environment. Risks also remain around the disruption that the UK's exit from the European Union will have on the economy. | The Group implemented robust monitoring processes and via various stress testing activity (i.e. ad hoc, risk appetite and ICAAP) understands how the Group performs over a variety of macroeconomic stress scenarios and has developed a suite of early warning indicators, which are closely monitored to identify changes in the economic environment. The Board and management review detailed portfolio reports to identify any changes in the Group's risk profile. |
| **Climate change** | As the worldwide focus on climate change intensifies, both the physical risks and the transitional risks associated with climate change continue to grow. Climate change risks include:<br><br>Physical risks can relate to specific weather events, such as storms and flooding, or to longer-term shifts in the climate, such as rising sea levels. These risks could include adverse movements in the value of certain properties that are in coastal and low lying areas, or located in areas prone to increased subsidence and heave.<br><br>Transitional risks may arise from the adjustment towards a low-carbon economy, such as tightening energy efficiency standards for domestic and commercial buildings. These risks could include a potential adverse movement in the value of properties requiring substantial updates to meet future energy performance requirements.<br><br>Reputational risk arising from a failure to meet changing societal, investor or regulatory demands. | The Group developed an approach to assessing and managing the risks relating to climate change within its Risk Management Framework. This includes scenario analysis, development of key risk indicators and inclusion of climate risks within operational resilience activities.<br><br>A cross-functional working group is overseeing the Group's response to climate change, in line with industry best practice and regulatory guidelines.<br><br>As part of the Group's ICAAP a detailed analysis was conducted using third party data to complete an initial assessment of the financial risk that climate change could pose to the Group. This analysis will be developed further during 2021 and will be aligned with activity to develop an integrated ESG plan during the first half of 2021.<br><br>The Group's Chief Risk Officers have designated senior management responsibility for the management of climate change risk; during 2021 a Board member will be specified to ensure that the Group meets regulatory and wider stakeholder expectations. |

## Principal risks and uncertainties (continued)

| Emerging risk | Description | Mitigating action |
|---|---|---|
| **Model risk** | The risk of financial loss, adverse regulatory outcomes, reputational damage or customer detriment resulting from deficiencies in the development, application or ongoing operation of models and ratings systems.<br><br>Post the completion of the Combination with CCFS, the Group notes the increasing usage of models to conduct financial assessments whilst informing business decisions. The Group also notes changes in industry best practice with respect to managing model risk. | During 2020, Board and Executive level model oversight Committees and a suite of Group level policies were introduced.<br><br>Further enhancements are planned during 2021 to ensure that the model governance arrangements meet regulatory expectations and model risk is managed effectively. |
| **LIBOR reform** | The LIBOR benchmark may cease to be set after the end of 2021 due to the low level of supporting unsecured loans in the wholesale interbank loan market. The Group has exposure to the LIBOR benchmark within some of its customer lending products and wholesale derivative hedging transactions. If the benchmark were to cease or become unreliable, these loans and derivatives may reflect rates that do not accurately represent short-term funding costs, therefore having an adverse effect on returns. | The Group ALCO has set up a dedicated working group to focus on this risk and transition away from the LIBOR benchmark. Key mitigating actions include new swaps being linked to SONIA and existing LIBOR linked swaps being transitioned to SONIA. LIBOR linked mortgages will also be transitioned to referencing either the Bank of England base rate or SONIA. |
| **Coronavirus** | The COVID-19 pandemic has had a material impact on individuals and businesses where the Group has operations, including the UK and India. The lockdown measures introduced to stem the spread of the virus have had a profound effect on how businesses operate and individuals work, which may have a materially adverse impact on the Group's profitability, capital and liquidity positions.<br><br>It is unclear how the COVID-19 pandemic will evolve during 2021 and the impact that the roll-out of vaccines will have and whether any new strains emerge. A further risk relates to the impact once government support measures are withdrawn during 2021 and the resulting impact on business failures, unemployment levels and house prices. | The Group has taken a considered approach to minimising and managing the impact of a coronavirus-related global pandemic. The Group approach represents a comprehensive response strategy covering both severity and consequences of a global pandemic. The Group's response strategy covers key aspects of an effective pandemic response approach, including prevention, continuity, impact assessment and stress testing. Supporting the Group's response strategy are established underlying capabilities to facilitate operational and financial resilience testing and planning, active monitoring and reporting procedures, and active communications with all employees (UK and India) and supervisory authorities. |

**Principal risks and uncertainties** (continued)

| Emerging risk | Description | Mitigating action |
|---|---|---|
| **Negative interest rates** | To support economic performance, resulting from the impact of the pandemic, the Bank of England may consider reducing the Bank of England base rate below 0%. The Group would be impacted across its lending portfolios with adverse movements in interest income, offset by reductions in interest payable on savings accounts.<br><br>A further risk relates to increased operational and conduct risks arising from system and process changes required to accommodate negative interest rates.<br><br>Negative interest rates may also impact customer behaviour, with changes in the demand for lending and savings products potentially impacting the Group's loan book growth plans and liquidity coverage levels. | The Group has reviewed readiness for negative interest rates and presented findings to the Board. The review covered the terms and conditions of the Group's financial contracts and any systems limitations. Some key servicing systems have been identified as requiring further development to allow negative rates and in particular negative pay rates. Given a mixture of floors in terms and conditions for certain products and the Group's margins, negative interest rates would be unlikely to cause an issue until the Bank of England base rate reaches a rate of -75bps or below. A working group is currently examining further system development to manage significant negative rates. |

**Risk profile performance overview**

**Credit risk**

The Group's fully secured loan portfolios performed robustly throughout 2020, with the credit profile remaining broadly stable, post careful monitoring and management of both the OSB and CCFS lending portfolios.

The Group's credit risk appetite approach ensured that the loan portfolios were positioned to perform well in both benign and stressed macroeconomic environments. Prudent management actions taken shortly after the onset of the COVID-19 pandemic, such as tightening loan to values (LTVs) and other credit policy criteria across all loan types, ensured that new lending performed well and was positioned to withstand future stress.

Cautious underlying net loan book growth of 5%, or 9% excluding the impact of structured asset sales in the year, was delivered via controlled new lending in the Group's core Buy-to-Let and residential owner-occupier segments, which more than offset reductions in bridging and second charge outstanding balances. The Group also tightened criteria in its more cyclical product lines. Mortgage lending balances against semi-commercial and commercial lending also reduced, as did the Group's development finance and funding lines ub-segments due to tighter lending criteria and strong repayment inflows.

Sensible new lending LTV criteria and favourable property price indexing resulted in the average weighted stock LTV for OSB and CCFS reducing during 2020 to 64% and 67% respectively as at 31 December 2020 (31 December 2019: OSB restated[2] 65% and CCFS 69%), which resulted in a prudent average weighted LTV profile of 65% at the Group level.

A low level of arrears continued to be observed during 2020, with just 0.9% of net loan balances greater than three months in arrears, which was in line with the position as at 31 December 2019. These stable metrics are in part supported by accounts being offered COVID-19 payment deferrals, which will have stopped accounts missing payments during the eligible period.

**Risk profile performance overview** (continued)

Group and solo banks interest coverage ratios for new lending improved during 2020 to 201% for OSB and 193% for CCFS (2019: restated[3] 199% OSB and 187% CCFS).

During 2020, forward looking external credit bureau probability of default and customer indebtedness scores improved across the Group's core lending segments.

To support our customers during the COVID-19 pandemic the Group granted payment deferrals c. 26k accounts representing 28% of the loan book by value during the peak at the end of June 2020. As at 31 December 2020 active payment deferrals represented only 1.3% of the Group's loan book by value. Low levels of arrears have been observed from the payment holiday cohort to date.

1. Average weighted LTV for OSB includes KR and Interbay Buy-to-Let, semi-commercial and commercial, first and second charge residential lending.
2. The Group restated the comparative LTVs due to a change in calculation methodology.
3. Interest coverage ratio for 2019 was restated due to an improvement in calculation methodology.

**Expected Credit Losses (ECL)**

Full year statutory impairment losses totalled £71.0m versus £15.6m for 2019, with the increase being driven by the potential impact of the COVID-19 pandemic on the UK economy and resulting changes in customer behaviour and property valuations. The Group also recorded an impairment provision of £20m in relation to potential fraudulent activity by a third-party on a secured funding line provided by the Group.

Detailed below are a number of the COVID-19 related factors and other material items which drove the elevated impairment charge within the year:

a) Macroeconomic scenarios – during 2020 the Group adopted a suite of more adverse economic scenarios, which reflected the potential impact of the COVID-19 pandemic across the UK economy. Rising unemployment levels may result in increasing levels of customers falling into arrears and defaulting on loan payments, whilst falling house prices may result in lower levels of equity and therefore potential future losses post sale. Downside scenarios also included the impact of economic disruption caused from the United Kingdom's exit from the European Union. Throughout the year, these scenarios were updated as the pandemic progressed and government support measures were introduced. The introduction and consequent updates made to forward-looking macroeconomic scenarios drove £21.2m of the total impairment charge during 2020 or 11bps of the annualised loan loss ratio.

b) Staging criteria – the Group ensured it complied with industry best practice and regulatory guidance with respect to payment deferrals and their treatment in IFRS 9 staging criteria, which included payment deferrals on their own not being treated as a significant increase in credit risk. During 2020 the Group made iterative enhancements to staging criteria, leveraging both internal and external information to identify performing higher risk cohorts across the entire customer base, but also including the payment deferral population, moving eligible exposures into stage 2 where a lifetime loss allowance was held. During 2020 the impact from these staging enhancements was £4.8m of the annual impairment charge or 3bps of the annualised loan loss ratio.

**Risk profile performance overview** (continued)

c) COVID-19 post model adjustments – the Group implemented a number of post model adjustments to ensure that modelled estimates remained appropriate, considering the impact that government support measures such as the repossession moratorium and payment deferrals had on credit bureau files and on loss given default and probability of default estimates. The quantum of these post model adjustments was impacted by the interaction with the severe forward looking macroeconomic scenarios, during the impairment calculation process. The combined impact of these COVID-19 related post model adjustments contributed £10.4m of the total 2020 impairment charge which equated to c. 6bps of the annualised loan loss charge.

d) Model enhancements - post Combination, the Group continued to make enhancements across the full suite of IFRS 9 impairment models, aligning modelling approaches and definitions where appropriate. An example of this was the implementation of an aligned definition of default across the Group. In line with the normal course of business a number of model recalibrations were made during the year, to ensure that modelled estimates continued to align to actually observed performance. The cumulative impact of these modelling enhancements contributed £10.7m of the total loan loss charge during 2020, which contributed 6bps to the loan loss ratio. The interaction of the severe forward looking macroeconomic scenarios within IFRS 9 impairment calculations elevated the impact of these modelling enhancements.

**Macroeconomic scenarios**

The measurement of ECL under the IFRS 9 approach is complex and requires a high level of judgement. The approach includes the estimation of probability of default (PD), loss given default (LGD) and likely exposure at default (EAD). An assessment of the maximum contractual period with which the Group is exposed to the credit risk of the asset is also undertaken.

IFRS 9 requires firms to calculate ECL allowances simulating the effect of a range of possible economic outcomes, calculated on a probability weighted basis. This requires firms to formulate forward-looking macroeconomic forecasts and incorporate them in ECL calculations.

**i. How macroeconomic variables and scenarios are selected**

During the IFRS 9 modelling process, the relationship between macroeconomic drivers and arrears, default rates and collateral values is established. For example, if unemployment levels increase, the Group would observe an increasing number of accounts moving into arrears. If residential or commercial property prices fall, the risk of losses being realised on the sale of a property would increase.

The Group has adopted an approach which utilises four macroeconomic scenarios. These scenarios are provided by an industry leading economics advisory firm, that provide management and the Board with advice on which scenarios to utilise and the probability weightings to attach to each scenario.

A base case forecast is provided, along with a plausible upside scenario. Two downside scenarios are also provided (downside and a severe downside).

**ii. How macroeconomic scenarios are utilised within ECL calculations**

Probability of default estimates are either scaled up or down based on the macroeconomic scenarios utilised.

Loss given default estimates are impacted by property price forecasts which are utilised within loss estimates should an account be possessed and sold.

Exposure at default estimates are not impacted by the macroeconomic scenarios utilised.

**Risk profile performance overview** (continued)

Each of the above components are then directly utilised within the ECL calculation process.

**iii. Macroeconomic scenario governance**

The Group has a robust governance process to oversee macroeconomic scenarios and probability weightings used within ECL calculations. Updated scenarios are provided on a monthly basis where an assessment is carried out by the Group's Risk function to determine whether an update is required.

On a periodic basis, the Group's Risk function and economic adviser provide the Group Risk and Audit Committees with an overview of recent economic performance, along with updated base, upside and two downside scenarios. The Risk function conducts a review of the scenarios comparing them to other economic forecasts, which results in a proposed course of action, which once approved is implemented.

**iv. Changes made during 2020**

a. **Macroeconomic scenario**

Post the onset of the COVID-19 pandemic, the Group implemented a suite of adverse economic scenarios, which incorporated the potential impact of the lockdown periods on economic activity, resulting in rising forecasted unemployment levels and falling property prices. The Group continued to utilise four scenarios including base and upside scenarios and two downside scenarios. The downside scenarios also include potential future economic disruption, resulting from the United Kingdom leaving the European Union.

Throughout 2020, the scenario suite was monitored and updated as government measures were updated and the impact of the pandemic evolved.

**Risk profile performance overview** (continued)

Forecast macroeconomic variables over a five-year period (includes average over five years and the peak to trough projections):

| **31 December 2020** | | **Base case %** | **Upside scenario %** | **Downside scenario %** | **Severe downside scenario %** |
|---|---|---|---|---|---|
| Weighting applied | | 40 | 30 | 23 | 7 |
| **Economic driver** | **Measure** | | | | |
| Gross Domestic Product (GDP) | 5 year average (yearly GDP growth %) | 3.2 | 3.6 | 2.6 | 2.2 |
| | Cumulative growth/(fall) to peak/(trough) (%) | -5.8 | -5.6 | -6.7 | -8.0 |
| House Price Index (HPI) | 5 year average (yearly HPI growth %) | 2.1 | 3.6 | -0.4 | -2.2 |
| | Cumulative growth/(fall) to peak/(trough) (%) | -8.5 | -6.3 | -18.9 | -26.4 |
| Bank Base Rate (BBR) | 5 year average (%) | 0.5 | 0.8 | 0.1 | 0.1 |
| | Cumulative growth/(fall) to peak/(trough) (%) | +1.4 | +1.7 | +0.0 | +0.0 |
| Unemployment Rate (UR) | 5 year average (%) | 6.9 | 6.1 | 8.8 | 9.6 |
| | Cumulative growth/(fall) to peak/(trough) (%) | +3.7 | +3.1 | +5.8 | +6.5 |
| Commercial Real Estate Index (CRE) | 5 year average (yearly HPI growth %) | 2.1 | 3.6 | -0.4 | -5.5 |
| | Cumulative growth/(fall) to peak/(trough) (%) | -8.5 | -6.3 | -18.9 | -40.0 |

**Risk profile performance overview** (continued)

| **31 December 2019** | | **Base case** % | **Upside scenario** % | **Downside scenario** % | **Severe downside scenario** % |
|---|---|---|---|---|---|
| Weighting applied | | 40 | 10 | 35 | 15 |
| **Economic driver** | **Measure** | | | | |
| Gross Domestic Product (GDP) | 5 year average (yearly GDP growth %) | 1.2 | 1.7 | 0.5 | -0.3 |
| | Cumulative growth/(fall) to peak/(trough) (%) | 6.4 | 8.5 | -3.6 | -5.8 |
| House Price Index (HPI) | 5 year average (yearly HPI growth %) | 1.3 | 3.2 | -1.5 | -3.2 |
| | Cumulative growth/(fall) to peak/(trough) (%) | 5.6 | 14.8 | -13.4 | -21.1 |
| Bank Base Rate (BBR) | 5 year average (%) | 1.3 | 1.5 | 0.2 | 0.1 |
| | Cumulative growth/(fall) to peak/(trough) (%) | +1.5 | +1.7 | -0.7 | -0.6 |
| Unemployment Rate (UR) | 5 year average (%) | 4.5 | 3.4 | 6.3 | 7.2 |
| | Cumulative growth/(fall) to peak/(trough) (%) | +0.7 | -1.0 | +2.9 | +4.1 |
| Commercial Real Estate Index (CRE) | 5 year average (yearly HPI growth %) | 1.3 | 3.2 | -1.5 | -5.8 |
| | Cumulative growth/(fall) to peak/(trough) (%) | +5.6 | +14.8 | -13.4 | -40.0 |

**b. Significant increase in credit risk rules**

The Group's Significant Increase in Credit Risk (SICR) rules, prior to the COVID-19 pandemic, considered changes in default risk, internal impairment measures, changes in customer credit bureau files, or whether forbearance measures had been applied.

The Group took steps to adjust the SICR criteria through the pandemic to account for the changes in risk profile and specifically for payment deferrals granted, noting that not all of the instances of a payment deferral would be a significant increase in credit risk. Payment deferrals granted due to COVID-19 alone were not automatically considered as a SICR event in line with issued guidance, and adjustments to the rules were as follows:

- Payment deferrals considered as a SICR event where other significant high risk factors are identified on customer's credit files;
- Payment deferrals considered as a SICR event where an account also had recent arrears; and
- Customers with stress to their income considered as a SICR event.

**Risk profile performance overview** (continued)

**Forbearance**

Where borrowers experience financial difficulty, which impacts their ability to service their financial commitments under the loan agreement, forbearance may be used to achieve an outcome which is mutually beneficial to both the borrower and the Bank.

By identifying borrowers who are experiencing financial difficulties pre-arrears or in arrears, a consultative process is initiated to ascertain the underlying reasons and to establish the best course of action to enable the borrower to develop credible repayment plans and to see them through the period of financial stress.

The specific tools available to assist customers vary by product and the customers' status. The various treatments considered for customers are as follows:

- Temporary switch to interest only: a temporary account change to assist customers through periods of financial difficulty where arrears do not accrue at the original contractual payment. Any arrears existing at the commencement of the arrangement are retained.
- Interest rate reduction: the Group may, in certain circumstances, where the borrower meets the required eligibility criteria, transfer the mortgages to a lower contractual rate. Where this is a formal contractual change the borrower will be requested to obtain independent financial advice as part of the process.
- Loan term extension: a permanent account change for customers in financial distress where the overall term of the mortgage is extended, resulting in a lower contractual monthly payment.
- Payment holiday: a temporary account change to assist customers through periods of financial difficulty where arrears accrue at the original contractual payment. Any arrears existing at the commencement of the arrangement are retained.
- Voluntary-assisted sale: a period of time is given to allow borrowers to sell the property and arrears accrue based on the contractual payment.
- Reduced monthly payments: a temporary arrangement for customers in financial distress. For example, a short-term arrangement to pay less than the contractual payment. Arrears continue to accrue based on the contractual payment.
- Capitalisation of interest: arrears are added to the loan balance and are repaid over the remaining term of the facility or at maturity for interest only products. A new payment is calculated, which will be higher than the previous payment.
- Full or partial debt forgiveness: where considered appropriate, the Group will consider writing off part of the debt. This may occur where the borrower has an agreed sale and there will be a shortfall in the amount required to redeem the Group's charge, in which case repayment of the shortfall may be agreed over a period of time, subject to an affordability assessment or where possession has been taken by the Group; and on the subsequent sale where there has been a shortfall loss.
- Arrangement to pay: where an arrangement is made with the borrower to repay an amount above the contractual monthly instalment, which will repay arrears over a period of time.
- Promise to pay: where an arrangement is made with the borrower to defer payment or pay a lump sum at a later date.
- Bridging loans more than 30 days past due: bridging loans which are more than 30 days past their maturity date. Repayment is rescheduled to receive a balloon or bullet payment at the end of the term extension where the institution can duly demonstrate future cash flow availability.

The Group aims to proactively identify and manage forborne accounts, utilising external credit reference bureau information to analyse probability of default and customer indebtedness trends over time, feeding pre-arrears watch list reports. Watch list cases are in turn carefully monitored and managed as appropriate.

**Risk profile performance overview** (continued)

### Fair value of collateral methodology

The Group ensures that security valuations are reviewed on an ongoing basis for accuracy and appropriateness. Commercial properties are subject to annual indexing, whereas residential properties are indexed against monthly House Price Index data.

### Solvency risk

The Group and each regulated bank maintains an appropriate level and quality of capital to support its prudential requirements with sufficient contingency to withstand a severe but plausible stress scenario. The solvency risk appetite is based on a stacking approach, whereby the various capital requirements (Pillar 1, ICG, CRD IV buffers, Board and management buffers) are incrementally aggregated as a percentage of available capital (CET1 and total capital).

Solvency risk is a function of balance sheet growth, profitability, access to capital markets and regulatory changes. The Group actively monitors all key drivers of solvency risk and takes prompt action to maintain its solvency ratios at acceptable levels. The Board and management also assess solvency when reviewing the Group's business plans and inorganic growth opportunities.

During 2020, the Group proactively managed the balance sheet, whilst the PRA introduced capital support measures detailed within the CRR 'Quick Fix' package which resulted in capital ratios strengthening. The counter-cyclical buffer was also cut from 1% to 0% during the period as a regulatory response to COVID-19.

### Liquidity and funding risk

The Group has a prudent approach to liquidity management through maintaining sufficient liquidity resources to cover cash flow imbalances and fluctuations in funding under both normal and stressed conditions, arising from market-wide and Bank-specific events. OSB's and CCFS' liquidity risk appetites have been calibrated to ensure that both Banks always operate above the minimum prudential requirements with sufficient contingency for unexpected stresses, whilst actively minimising the risk of holding excessive liquidity which would adversely impact the financial efficiency of the business model.

The Group continues to attract new retail savers and has high retention levels with existing customers. In addition, the Combination allowed the Group a wider range of wholesale funding options, including securitisation issuances and use of retained notes from both Banks.

In 2020, both Banks actively managed their respective liquidity and funding profiles within the confines of their risk appetites as set out in each Bank's ILAAP.

Each Bank's risk appetite is based on internal stress tests that cover a range of scenarios and time periods and therefore are a more severe measure of resilience to a liquidity event than the standalone liquidity coverage ratio (LCR). As at 31 December 2020, OSB had a liquidity coverage ratio of 254% (2019: 199%) and CCFS 146% (2019:145%), significantly in excess of the 2020 regulatory requirement of 100%.

**Risk profile performance overview** (continued)

**Market risk**

The Group proactively manages its risk profile in respect of adverse movements in interest rates, foreign exchange rates and counterparty exposures.

The Group accepts interest rate risk and basis risk as a consequence of structural mismatches between fixed rate mortgage lending, sight and fixed term savings and the maintenance of a portfolio of high quality liquid assets. Interest rate exposure is mitigated on a continuous basis through portfolio diversification, reserve allocation and the use of financial derivatives within limits set by the Group ALCO and approved by the Board.

The Group's balance sheet is completely GBP denominated. The Group has some minor foreign exchange risk from funding the OSBI business. This is minimised by pre-funding a number of months in advance and regularly monitoring GBP/INR rates. Wholesale counterparty risk is measured on a daily basis and constrained by counterparty risk limits.

**Transition away from LIBOR**

The PRA and FCA have continued to encourage banks to transition away from using LIBOR as a benchmark in all operations before the end of 2021. Throughout the UK banking sector LIBOR remains a key benchmark and, for each market impacted, solutions to this issue are progressing through various industry bodies.

An internal working group has been established with strong oversight from the Compliance and Risk functions. Risk assessments have been completed to ensure this process is managed in a measured and controlled manner. The Group no longer writes any LIBOR-linked business and is transitioning new and back book swaps from a LIBOR to a SONIA basis.

**Interest rate risk**

The Group does not actively assume interest rate risk, does not execute client or speculative securities transactions for its own account, and does not seek to take a significant directional interest rate position. Limits have been set to allow management to run occasional unhedged positions in response to balance sheet dynamics and capital has been allocated for this. Exposure limits are calibrated in proportion to available CET1 capital and estimated annual net interest income to cover capital and profit and loss risks.

The Group sets limits on the tenor and rate reset mismatches between fixed rate assets and liabilities, including derivatives hedges, with exposure and risk appetite assessed by reference to historical and potential stress scenarios at consistent levels of modelled severity.

Throughout 2020, both Banks managed their interest rate risk exposures within risk appetite limits.

**Basis risk**

Basis risk arises from assets and liabilities repricing with reference to different interest rate indices, including positions which reference variable market and managed rates. As with structural interest rate risk, the Group does not seek to take a significant basis risk position, but maintains defined limits to allow operational flexibility.

For both OSB and CCFS, exposure is assessed and monitored regularly across a range of 'business as usual' and stressed scenarios.

Throughout 2020, both Banks managed their basis risk exposure within their risk appetite limits.

**Risk profile performance overview** (continued)

**Operational risk**

The Group continues to adopt a proactive approach to the management of operational risks. The operational risk management framework has been designed to ensure a robust approach to the identification, measurement and mitigation of operational risks, utilising a combination of both qualitative and quantitative evaluations. The Group's operational processes, systems and controls are designed to minimise disruption to customers, damage to the Group's reputation and any detrimental impact on financial performance. The Group actively promotes the continual evolution of its operating environment.

Where risks continue to exist, there are established processes to provide the appropriate levels of governance and oversight, together with an alignment to the level of risk appetite stated by the Board.

A strong culture of transparency and escalation has been cultivated throughout the organisation, with the Operational Risk function having a Group-wide remit, ensuring a risk management model that is well embedded and consistently applied. In addition, a community of Risk Champions representing each business line and location has been identified. Operational Risk Champions ensure that the operational risk identification and assessment processes are established across the Group in a consistent manner. Risk Champions are provided with appropriate support and training by the Operational Risk function.

Due to the COVID-19 pandemic and the resulting high number of employees working and accessing systems from home, the risk of a cyber attack has heightened. Whilst IT security risks continue to evolve, the level of maturity of the Group's controls and defences has significantly increased, supported by dedicated IT security experts. The Group's ongoing penetration testing continues to drive enhancements by identifying potential areas of risk.

**Regulatory and compliance risk**

The Group is committed to the highest standards of regulatory conduct and aims to minimise breaches, financial costs and reputational damage associated with non-compliance.

The Group has an established Compliance function which actively identifies, assesses and monitors adherence with current regulation and the impact of emerging regulation.

In order to minimise regulatory risk, the Group maintains a proactive relationship with key regulators, engages with industry bodies such as UK Finance, and seeks external expert advice. The Group also assesses the impact of upstream regulation on itself and the wider market in which it operates, and undertakes robust assurance assessments from within the Risk and Compliance functions.

**Conduct risk**

The Group considers its culture and behaviour in ensuring the fair treatment of customers and in maintaining the integrity of the market segments in which it operates to be a fundamental part of its strategy and a key driver to sustainable profitability and growth. The Group does not tolerate any systemic failure to deliver fair customer outcomes.

On an isolated basis, incidents can result in detriment owing to human and/or operational failures. Where such incidents occur they are thoroughly investigated and the appropriate remedial actions are taken to address any customer detriment and to prevent recurrence.

The Group considers effective conduct risk management to be a product of the positive behaviour of all employees, influenced by the culture throughout the organisation and therefore continues to promote a strong sense of awareness and accountability.

**Risk profile performance overview** (continued)

**Strategic and business risk**
The Board has clearly articulated the Group's strategic vision and business objectives supported by performance targets. The Group does not intend to undertake any medium to long-term strategic actions, which would put at risk the Group's strategic or financial objectives.

To deliver against its strategic objectives and business plan, the Group has adopted a sustainable business model based on a focused approach to core niche market segments where its experience and capabilities give it a clear competitive advantage.

The Group remains highly focused on delivering against its core strategic objectives and strengthening its position further through strong and sustainable financial performance.

**Reputational risk**
Reputational risk can arise from a variety of sources and is a second order risk – the crystallisation of a credit risk or operational risk can lead to a reputational risk impact.

The Group monitors reputational risk through tracking media coverage, customer satisfaction scores, and Net Promoter Scores provided by brokers.

**Integration risk**
At the point of the Combination, integration risk was identified as a principal risk for the duration of the integration programme, though the integration of the two entities was deemed inherently low risk owing to the similarity of the two business models, with the programme involving no material system or data migrations. The Group's Board took the view that it has limited appetite for integration related risks and deemed it appropriate to identify, assess and manage integration risks in full compliance with the wider risk management framework and governance disciplines of the Group.

Integration risk relates to any risk which may result in the nondelivery of planned integration objectives with respect to desired strategic outcomes and costs and synergies performance targets. Additionally, integration risk is also assessed with respect to the other principal risks which may be adversely impacted as a consequence of the integration activities.

The Board exercises oversight of the integration programme through the Board Integration Committee based on defined critical success factors and an integration risk appetite. The integration programme is supported by an Integration Management Office, with clearly defined plans, established roles and responsibilities, necessary financial discipline and governance arrangements. The integration programme is subject to second line oversight and third line assurance to enable the Board and senior management to monitor progress against plan and performance against integration risk appetite.

The integration programme and the underlying risk profile continued to perform in line with expectations during 2020, where no material risk incidents or trends where identified during the year. The integration programme did experience some level of disruption owing to the pandemic, but overall the programme has continued to progress as planned.

**Non-Financial Information Statement**
The requirements of sections 414CA and 414CB of the Companies Act 2006 relating to non-financial reporting are addressed in this section. We have a range of policies and guidance that support key outcomes for all our stakeholders. Performance against our strategic non-financial performance measures is one indicator of the effectiveness and outcomes of policies and statements. The Group's policies and statements include, but are not limited to, those summarised in the table below. During the year, the policies of OSB and CCFS were reviewed and combined to apply at a Group level, as appropriate. The table provides cross references to where further information is included within the Annual Report.

**Non-Financial Information Statement** (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Environmental matters** | | |
| Our **Environmental Policy** outlines our commitment to reducing our environmental impact and to continually improving our environmental performance as an integral part of our business strategy. The policy seeks to ensure that we meet or exceed all relevant legal and regulatory environmental obligations. | The Environmental Policy was reviewed by the newly-established Environmental Working Group which focuses on:<br><br>1. assessing the impact of business activities and driving initiatives to minimise the consumption of energy, water, paper, office supplies, transportation, maintenance and cleaning;<br><br>2. aligning the environmental data and actions for all entities within the Group;<br><br>3. developing an environmental culture across the Group; and<br><br>4. Encouraging environmental responsibility with employees and within supply chains. | The focus of actions in 2020 has been on extending our environmental management system and sharing best practice across the Group. Key highlights for the year include:<br><br>1. submitting our Energy Saving Opportunity Scheme (ESOS), which highlighted areas for improvement across our sites which have been taken forward for consideration;<br><br>2. purchasing electric vans for the fleet and electric vehicle charge points have been introduced in Chatham and Wolverhampton;<br><br>3. introducing video conferencing across the Group to reduce travel-related carbon footprint;<br><br>4. introducing automatic LED lighting where possible and as offices are refurbished; and<br><br>5. creating an Environmental Working Group across the Group to raise awareness of the work being undertaken and drive initiatives across all sites to improve employee engagement. |
| Our **Group Flexible Working Policy** sets out a range of flexible working arrangements and the approach that the Group will take in reviewing formal Flexible Working Requests from employees.<br><br>Our **Group Homeworking Policy** is applicable to all UK employees and provides clarity in respect of the Group's approach regarding formal homeworking arrangements (i.e. following a Flexible Working Request being agreed), informal arrangements and enforced arrangements (e.g. COVID-19). | The Group Flexible Working Policy was drafted by HR Management and reviewed by the Group's Legal and Company Secretariat function. The policy was then endorsed by the Governance Forum and approved by the Group Executive Committee.<br><br>A similar process, as outlined above, was followed for the Group Homeworking Policy. In addition, the policy was reviewed by the Health and Safety, Data Protection and Information Security teams and the Governance Forum requested that an external review of content be undertaken given the high percentage of employees working from home as a result of COVID-19. An external review was undertaken prior to the policy being approved. | We seek to accommodate, where possible, all requests for flexible working, with the majority of requests being agreed.<br><br>The Group Homeworking Policy introduced an attestation for those working from home (formally, informally and on an enforced basis).<br><br>The attestation is linked to the Group Homeworking Policy requiring employees who work from home to confirm that they are aware of and can appropriately mitigate risks presented by working from home in respect of data protection, information security and health and safety. |

## Non-Financial Information Statement (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Employee matters** | | |
| Our **Diversity and Inclusion Policy** sets out the Group's commitment to promoting equality of opportunity, providing an inclusive workplace and eliminating any unfair treatment or unlawful discrimination. | In order to ensure appropriate Board oversight of matters relating to diversity and inclusion, updates are regularly provided to the Group Nomination and Governance Committee.<br><br>In addition, the Group General Counsel and Company Secretary, who is the Executive responsible for diversity and inclusion, issues regular updates to all employees in order to drive awareness of ongoing internal initiatives and progress relating to diversity and inclusion.<br><br>An external adviser, Legal and HR were involved in drafting the new policy, which was endorsed by the Governance Forum and approved by the Group Executive Committee. | A Group-wide Diversity and Inclusion Working Group was established during 2020, broadening the scope of the Women's Networking Forum which was previously in place.<br><br>The Group has progressed towards achievement of our published Women in Finance Charter target and in respect of published Gender Pay Gap data, which is related to our diversity and inclusion initiatives.<br><br>In recent years, the Group's diversity and inclusion focus has tended to centre around gender.<br><br>The Group is committed to ensuring a broader focus on diversity matters, with this being robustly demonstrated during National Inclusion Week 2020. |
| Our **Whistleblowing Policy – Raising a Concern** ensures that all employees are encouraged to raise any concerns they may have about the conduct of others in the business or the way in which the business is run, in good faith and without fear of unfair treatment. | A Whistleblowing Report is regularly presented to the Group Audit Committee and an annual report is presented to the Board. The Chair of the Group Audit Committee is the designated Whistleblowers' Champion. | The Group Audit Committee receives a whistleblowing report quarterly and is responsible for overseeing the effective operation of the policy; this aims to mitigate the risk of undetected wrongdoing and unwanted exposure for the Group. |
| Our **Group Health and Safety Policy** outlines our approach and responsibilities under statutory legislation. We recognise our duty and responsibility and the Health and Safety Policy ensures that the Group complies with legislation to protect its employees and customers, and provides a suitable and safe environment for employees, customers and anyone affected by the Group's operations. | An external health and safety risk assessment was undertaken in 2020 at our offices and branches to ensure that we adhered to the UK Government-issued document Working Safely during COVID-19 in offices and contact centres.<br><br>The Health and Safety Working Group meet twice per annum to review the objectives of the Health and Safety Policy. Any relevant matters arising from these meetings are reported to Operational Risk.<br><br>An accountable Executive is responsible for the Health and Safety Policy and a third party adviser reviews it annually prior to it being approved by the Board. | Additional measures were put in place in accordance with COVID-19 guidelines to ensure any employees attending our offices or customers visiting our branches could do so in a safe way.<br><br>Health and safety statistics are provided on a dashboard shared monthly with the Board along with an annual Health and Safety Report.<br><br>Risk assessments are completed across the Group annually and in 2020 included COVID-secure certification.<br><br>Annual health and safety training is completed by all employees.<br><br>Health and Safety awareness in the workplace has increased with updates provided on the Group intranet to reduce the possibility of injury to employees and customers. |

**Non-Financial Information Statement** (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Social matters** | | |
| Our **Modern Slavery Statement** outlines the measures we have taken to combat the risks of modern slavery and human trafficking in our businesses and supply chains.<br><br>As part of our ongoing compliance, a review was undertaken of the policies potentially impacted by modern slavery and human trafficking with appropriate amendments made, where necessary. | The Modern Slavery Working Group annually reviews the Vendor Code of Conduct which is issued to our approved third party service providers at the time of onboarding and as part of the annual assessment. This year, the Vendor Code of Conduct has been updated to align with Home Office Guidance issued in respect of the additional risks of modern slavery posed by COVID-19.<br><br>We perform relevant checks via the Organisation for Economic Co-operation and Development (OECD) Watch at the onboarding stage and, where required, as part of our ongoing due diligence checks. In addition, our standard contract terms include reference to the required modern slavery or relevant contract terms.<br><br>All employees are required to complete mandatory training to raise awareness. | Our Vendor Management team includes specific testing of key controls within the Vendor Management Risk Assessment Matrix. Relationship owners are also tested for their awareness of the process and requirements in respect of modern slavery which forms part of the Group's mandatory training programme and awareness updates, in line with the Vendor Management Framework.<br><br>There are breach reporting procedures in place and there were no reportable incidents in this financial year. |
| Our **Group Vendor Management and Outsourcing Policy** sets out the core requirements which we must meet and provides a structure to efficiently manage potential and contracted third-party relationships ensuring the right level of engagement and due diligence, in compliance with our regulatory obligations. | The required due diligence and risk assessment criteria changes and updates have been included in the policy to align with the European Banking Authority and other applicable guidelines.<br><br>Activities during the year included:<br><br>1. a review of existing third party services to ensure alignment with the new policy and reclassification;<br><br>2. implementation of the new policy which is being managed through business communication, training and awareness sessions scheduled for assigned relationship owners; and<br><br>3. annual assurance update provided to the Board. | We recognise the importance of building strong relationships and governance with our third parties and of the possible reputational risk this can impose. We actively monitor our third parties to ensure they are adhering to our requirements, so that we can in turn meet our obligations to stakeholders. |

**Non-Financial Information Statement** (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Social matters** | | |
| Our **Lending Policy** sets out the parameters within which we are willing to lend money responsibly within our set criteria and credit risk appetite. | All changes to the Lending Policy require approval from the Group Credit Committee, with material changes escalated to the Group Risk Committee.<br><br>As a second line of defence, the Credit Quality Assurance process monitors adherence to the policy through a risk-based sampling approach.<br><br>System parameters and underwriting processes act as an additional control to ensure lending parameters are not breached. | The Group Risk Committee challenges how the Lending Policy is applied to ensure that the right outcomes are achieved.<br><br>The credit risk appetite of the Group monitors the performance and make-up of the portfolio relative to pre-agreed trigger limits and therefore is a measure of the overall performance of the Lending Policy.<br><br>Non-adherence to the credit risk appetite could lead to business being written outside the agreed risk appetite. |
| Our **Group Complaint Handling Policy** outlines, at a high level, our regulatory expectations for complaint handling from a customercentric perspective. | We investigate complaints competently, diligently and impartially, supported by appropriately trained employees. Root cause analysis is used to identify and solve underlying issues rather than apply quick fixes.<br><br>Complaint performance forms part of management information provided to Management Committees and to the Board. Analysis of complaints outcomes and potential business and customer impact is an integral part of the Group's processes. | Complaints remained aligned to the level of business activity.<br><br>Complaints are also a component of Executive bonus scheme metrics affecting remuneration outcomes.<br><br>Complaints may be an early warning of not treating customers fairly, which has regulatory consequences for the Group. |
| Our **Group Customer Vulnerability Policy** sets the standards and approach for the identification and treatment of vulnerable customers and provides guidance to all areas of the Group to ensure vulnerable customers consistently receive fair outcomes. | Regular case study reviews through the Vulnerable Customer Review Committee ensure best practice processes across the different customer journeys are monitored and shared with representatives from differing customer-facing and second line functions.<br><br>The Compliance function conducts second line thematic reviews across both vulnerable customer and other operational processes should the need arise. | An enhanced training programme has been developed to focus on more complex customer scenarios including identifying vulnerable customers and how best to serve them and their changing needs.<br><br>There is a potential impact to our reputation and regulatory risks for not treating customers fairly.<br><br>Customer complaint data shows there were no systemic issues in vulnerability processes and outcomes for the year. |
| Our **Group Data Protection Policy** ensures that there are adequate policies and procedures in place to enable compliance with the General Data Protection Regulation (GDPR) and the Data Protection Act 2018; and confirms the necessary steps that should be taken when processing personal data. | The Group Data Protection Officer reports twice each year, to the Group Executive Committee and the Board, regarding compliance with the Data Protection Policy and reports on any data incidents and data subject access requests. | The privacy and security of personal information is respected and protected. We regard sound privacy practices as a key element of corporate governance and accountability. Non compliance would expose the Group to the potential breach of GDPR provisions. |

## Non-Financial Information Statement (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Social matters** | | |
| Our **Group Arrears Management and Forbearance Policy** ensures that we address the need for internal systems and processes to treat customers in financial difficulties fairly, including being proactive with customers who display characteristics of being on the cusp of financial difficulty. | As the second line of defence, the Compliance function reviewed customer journeys; these reviews are risk-based and look at customer outcomes across the collections and litigation processes to ensure customers are dealt with in an effective and fair manner.<br><br>The Compliance function conducts second line thematic reviews across collection and litigation processes, should the need arise. | Our arrears rates are monitored through the Group Credit Committee on a monthly basis to ensure senior management oversight of arrears trends. There is credit risk associated with credit losses following the ineffective management of customer accounts.<br><br>This has been an area of focus for the Board and Executives and adjustments were made to accommodate payment deferral requests, as a result of COVID-19. |
| Our **Anti-Bribery and Corruption policies** outline our stance to conduct all of our business in a honest and ethical manner. We take a zero- tolerance approach to bribery and corruption and are committed to acting professionally, fairly and with integrity in all of our business dealings and relationships.<br><br>The purpose of the policies are to provide employees and contractors with clear guidelines to ensure that we conduct our activity in an ethical and appropriate manner including complying with the laws and regulations of each jurisdiction in which we operate. | The policies are subject to an annual review process with approval provided by the Group Audit Committee.<br><br>Anti-Bribery and Corruption training forms part of the wider Financial Crime training package that is mandatory for each employee to complete on an annual basis.<br><br>In addition, the requirements set out in the Anti-Bribery and Corruption policies are incorporated into the Group's Vendor Management and Outsourcing Policy.<br><br>Gifts, hospitality and donations are closely monitored through a log maintained by Risk and Compliance in accordance with our associated policies and procedures. | No material issues or breaches have arisen from the Group's adherence to the existing Anti-Bribery and Corruption policies and processes.<br><br>We recognise that there may be instances where an employee may be exposed to the risk of bribery or corruption and as result, provide numerous channels in which an employee can report such an event, including via the whistleblowing process.<br><br>During the tender process for a new supplier, all employees involved in the process must ensure compliance with the Anti-Bribery and Corruption policies and requirements. This approach also applies to the Conflict of Interest Policy. |

**Non-Financial Information Statement** (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Social matters** | | |
| Our **Conflict of Interest Policy** aims to identify, maintain and operate effective organisational and administrative arrangements to identify and take all reasonable steps in order to avoid conflicts where possible. | During the year, a combined Group level policy was adopted to ensure that a consistent approach is taken across the Group in relation to the systems and controls in place to identify, report and manage potential and realised conflicts of interest.<br><br>A detailed roll-out plan has been developed to ensure the policy is implemented effectively which will include employee training, embedding a consistent Conflicts of Interest declaration process, developing Group-wide procedures and ensuring risk-based assurance activity on adherence to the policy is undertaken.<br><br>In addition, Conflicts of Interest requirements are incorporated into the Group's Vendor Management and Outsourcing Policy. | No material issues or breaches have arisen from the Group's adherence to the existing Conflicts of Interest Policy and processes.<br><br>As a financial services provider, we face the risk of actual and potential conflicts of interest periodically. We recognise that there may be instances where conflicts of interest are unavoidable and that a conflict may exist even if no unethical or improper act or outcome results from it. Where it is not possible to avoid a potential conflict of interest, we are committed to ensuring that any conflicts of interest that arise are managed fairly and in the best interests of our customers.<br><br>Group Compliance maintains the conflict register, which is reviewed annually by the Risk Management Committees. In addition, the Group Nomination and Governance Committee reviews Executive and Director conflicts. |
| Our **Fraud Policy** outlines our duty to comply with prevailing legal and regulatory requirements and to have appropriate systems and controls in place to mitigate the risk of fraud. This includes ensuring appropriate monitoring and escalation procedures are in place and are operating effectively.<br><br>Our strategy for managing fraud risk is to adopt a zero-tolerance approach towards any form of fraud; however, we accept that incidents of fraud will occur as a result of doing business.<br><br>The purpose of the policy and supporting procedures is to provide a consistent approach throughout the Group to the prevention, detection and investigation of fraud. The policy forms an integral part of the Group Financial Crime Framework. | The Policy is subject to an annual review with approval provided by the Group Audit Committee.<br><br>Fraud awareness training forms part of the wider Financial Crime training package that is mandatory for each employee to complete on an annual basis.<br><br>External stakeholders, customers, clients and relevant third parties are made aware of our robust stance towards fraud management through literature or similar communication channels.<br><br>The Risk Management Committees and the Group Risk Committee regularly review and monitor fraud reporting. | As a financial services provider, we recognise that we are inherently exposed to the risk of fraud and that incidents will occur as a result of doing business. In order to mitigate these risks we have appropriate systems and controls in place.<br><br>Key risk and performance indicators are agreed by senior management and reviewed on a regular basis. Management information on fraud-related activity is presented on a regular basis to senior management in order to provide visibility of our fraud exposure and any associated loss.<br><br>All potential fraud incidents are investigated by a dedicated Financial Crime team that is specifically trained in identifying and reporting fraudulent behaviour. |

### Non-Financial Information Statement (continued)

| Description of policies/statement | Due diligence undertaken | Outcomes/Impacts/Risks |
|---|---|---|
| **Social matters** | | |
| Our **Anti-Money Laundering and Counter Terrorist Financing Policy** seeks to explain the responsibility of senior managers, the Money Laundering and Reporting Officer (MLRO) and all employees. The policy requires that the highest ethical standards are met and requires all employees to act with integrity at all times. We have no appetite for breaching legislation or regulation regarding anti-money laundering or counter terrorist financing. | All employees are required to complete annual training.<br><br>The policy is subject to an annual review process with approval provided by the Group Audit Committee.<br><br>We have documented processes and procedures in place to identify the Group's customers prior to entering into a relationship. Systems and controls have been adopted to highlight activity deemed to be suspicious.<br><br>All suspicious activity is investigated by a dedicated Financial Crime team who are specifically trained in identifying and reporting suspicious behaviour. | No material issues or breaches have arisen from the Group's adherence to the existing Anti-Money Laundering and Counter Terrorist Financing Policy and processes.<br><br>As a financial services provider, the Group recognises that it is inherently exposed to the risk of financial crime.<br><br>Key risk and performance indicators are agreed by senior management and reviewed on a regular basis. Management information on financial crime related activity is presented to senior management in order to provide visibility of our exposure to financial crime. |
| Our **Group Operational Resilience Policy** documents the approach and expectations of the Group in establishing and maintaining the appropriate levels of operational resilience as well as the level of impact tolerance that the Group is willing to accept in respect of incidents or events that may impact the provision of its services.<br><br>The policy is closely linked with our Business Continuity Plan. | The policy is subject to an annual review process with approval provided by the Risk Management Committees.<br><br>We analyse the probability and consequences of an unplanned event that could affect the Group. We also identify the key risks faced by the Group and put measures and controls in place to protect the Group against these risks.<br><br>In September 2020, a data centre recovery exercise took place which involved a full shutdown of primary servers. As a result, further enhancements will be worked through, during 2021. | In March 2020, the UK Government announced a UK-wide lockdown due to COVID-19.<br><br>Whilst we believe that we have taken appropriate actions and have an operating model that is well positioned to support the Group throughout the crisis, we remain on alert to respond to any further changes in circumstances.<br><br>Failing to be resilient could have a devastating effect on the business to the extent that it becomes difficult or even impossible to carry out business as usual activities. |

### Description of the business model

A description of the business model is set out on page 3.

### Principal risks and uncertainties

A description of the principal risks and uncertainties is set out on pages 39 to 52.

This Strategic report was approved by the Board and signed on its behalf by:

**Jason Elphick**
General Counsel and Company Secretary
27 April 2021

The Directors present their Report, together with the audited Financial Statements and Auditor's Report, for the year ended 31 December 2020.

**Information presented in other sections**

Information relating to future developments, principal risks and uncertainties and engagement with suplliers, customers and others has been included in the Strategic Report.

Information on financial instruments including financial risk management objectives and policies including, the policy for hedging the exposure of the Group to price risk, credit risk, liquidity risk and cash flow risk can be found in the Risk review on pages 32 to 62.

Details on how the Company has complied with section 172 can be found throughout the Strategic and Directors' Reports and on page 10.

**Results**

The results for the year are set out in the Statement of Comprehensive Income on page 94.

**Directors**

The Directors who served during the year and to the date of this report were as follows:

Graham Allatt
Eric Anstee (until 4 February 2020)
Timothy Brooke Thom (until 7 May 2020)
Rodney Duke (until 4 February 2020)
Andrew Golding
Elizabeth Noël Harwerth
Margaret Hassall (until 7 May 2020)
Sarah Hedger
Rajan Kapoor
Mary McNamara
April Talintyre
Ian Ward (until 7 May 2020)
David Weymouth
Sir Malcolm Williamson (until 4 February 2020)

None of the Directors had any interest either during or at the end of the year in any material contract or arrangement with the Company.

**Directors' indemnities**

The Articles provide, subject to the provisions of UK legislation, an indemnity for Directors and Officers of the Company in respect of liabilities they may incur in the discharge of their duties or in the exercise of their powers, including any liabilities relating to the defence of any proceedings brought against them, which relate to anything done or omitted, or alleged to have been done or omitted, by them as Officers or employees of the Company. Directors' and Officers' liability insurance cover is in place in respect of all Directors.

**Equal opportunities**

The Group is committed to applying its Diversity and Inclusion Policy at all stages of recruitment and selection. Short-listing, interviewing and selection will always be carried out without regard to gender, gender reassignment, sexual orientation, marital or civil partnership status, colour, race, nationality, ethnic or national origins, religion or belief, age, pregnancy or maternity leave or trade union membership. Any candidate with a disability will not be excluded unless it is clear that the candidate is unable to perform a duty that is intrinsic to the role, having taken into account reasonable adjustments. Reasonable adjustments to the recruitment process will be made to ensure that no applicant is disadvantaged because of his/her disability. Line Managers conducting recruitment interviews will ensure that the questions they ask job applicants are not in any way discriminatory or unnecessarily intrusive. This commitment also applies to existing employees, with the necessary adjustments made, where there is a change in circumstances.

**Employee engagement**

Employees are kept informed of developments within the business and in respect of their employment through a variety of means, such as employee meetings, briefings and the intranet. Employee involvement is encouraged and views and suggestions are taken into account when planning new products and projects.

The OSBG Sharesave 'save as you earn' Scheme is a Group wide all-employee share option scheme which is open to all UK-based employees. The Sharesave Scheme allows employees to purchase options by saving a fixed amount of between £5 and £500 per month over a period of either three or five years, at the end of which the options, subject to leaver provisions, are usually exercisable. The Sharesave Scheme has been in operation since June 2014 and options are granted annually, with the exercise price set at a 20% discount of the share price on the date of grant.

The Workforce Advisory Forum (known as OneVoice ) was established in 2019 to gather the views of the workforce to enable the Board and Group Executive Committee to consider a broadly representative range of stakeholder perspectives to guide strategic decisions for the future of the Company and its subsidiaries. OneVoice consists of volunteer representatives (of which there are 21 in total) from each of the various business areas and locations, as well as permanent members consisting of a designated NED, Mary McNamara; a member of the Group Executive Committee, Jason Elphick; and a representative from HR Management. Other NEDs and members of the Group Executive Committee are invited to attend meetings on a rotational basis.

Members of the Board are keen to engage with our employees across all locations and find the experience of visiting our branches and offices within the UK and India invaluable; however, due to travel restrictions in place throughout 2020 as a result of COVID-19, these visits have not been physically possible. It is hoped that once restrictions are lifted and, provided it is safe to do so, visits to branches and offices will resume.

During 2020, three OneVoice meetings were held. In advance of each meeting, employee representatives are encouraged to engage with employees within their nominated business areas and across all Group locations and identify topics impacting the workforce, which it is felt should be brought to the attention of the Board and Group Executive Committee. A number of items were considered and discussed by OneVoice including communication, HR harmonisation activities, integration, technology, as well as the impact of COVID-19, particularly, in relation to employee well-being.

The Group is committed to diversity and to making sure everyone in our business feels included, this year we introduced a Diversity and Inclusion Working Group. This working group brings together a broad mix of employees from across the UK business to drive our diversity and inclusion agenda. Jason Elphick, our Diversity Champion delivered a Q&A session for employees to understand more about the Group's diversity and inclusion agenda.

**Political donations**

Neither the Company nor any of its subsidiaries made any political donations this year.

**Going concern statement**

The Board undertakes regular rigorous assessments, in accordance with the 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting', published by the Financial Reporting Council in September 2014, of whether the Group is a going concern in light of current economic conditions and all available information about future risks and uncertainties. In assessing whether the going concern basis is appropriate, projections for the Group have been prepared, covering its future performance, capital and liquidity for a period in excess of 12 months from the date of approval of these Financial Statements. These forecasts have been subject to sensitivity tests, including stress scenarios, which have been compared to the latest Brexit and COVID-19 pandemic economic scenarios provided by the Group's external economic advisors, as well as reverse stress tests. The assessments were significantly influenced by COVID-19 implications, covering the Group's capital, liquidity and operational resilience, including the following:

- The Financial and capital forecasts were prepared under stress scenarios which were assessed against the latest COVID-19 related economic forecasts provided by the Group's external economic advisors. Reverse stress tests were also run, to assess what combinations of House Price Index and unemployment variables would result in the Group utilising its regulatory capital buffers in full and breaching the Group's minimum prudential requirements along with analysis and insight from the Group's ICAAP. The Directors assessed the likelihood of those reverse stress scenarios occurring within the next 12 months and concluded that the likelihood is remote.
- The latest liquidity and contingent liquidity positions and forecasts were assessed against the ILAAP stress scenarios, which were reviewed for suitability in the context of COVID-19 related stresses.
- The Group continues to assess the resilience of its business operating model and supporting infrastructure in the context of the emerging economic, business and regulatory environment. The key areas of focus continue to be on the provision of critical services to customers, employee health and safety and the evolving governmental policies and guidelines. The Group has assessed and enhanced its information technology platforms to support its employees with flexible working and homeworking across all locations, ensuring stable access to core systems, data and communication devices. The response to the pandemic demonstrates the inherent resilience of the Group's critical processes and infrastructure. It also reflects the necessary agility in responding to future operational demands. The operational dependencies on third-party vendors and outsourcing arrangements continues to be an important area of focus.

The Group's financial projections, supported by the COVID-19 assessments, demonstrate that the Group has sufficient capital and liquidity to continue to meet its regulatory capital requirements as set out by the PRA.

The Board has therefore concluded that the Group has sufficient resources to continue in operational existence for a period in excess of 12 months and as a result, it is appropriate to prepare these Financial Statements on a going concern basis.

**The role and structure of the Board**

The Board of Directors (the Board) is responsible for the long-term success of the Company and provides leadership to the Group. The Board focuses on setting strategy and monitoring performance and ensures that the necessary financial and human resources are in place to enable the Company to meet its objectives.

The Board is responsible for setting the tone from the top in relation to conduct, culture and values, for ensuring continuing commitment to treating customers fairly, carrying out business honestly and openly and preventing bribery, corruption, fraud or the facilitation of tax evasion.

The Board operates in accordance with the Company's Articles of Association (the Articles) and its own written terms of reference. The Board has established an Audit and a Risk Committee, which each have their own terms of reference and are reviewed at least annually. Details of each Committee's activities during 2020 are shown below.

The Board retains specific powers in relation to the approval of the Group's strategic aims, policies and other matters, which must be approved by it under legislation or the Articles. These powers are set out in the Board's written terms of reference and Matters Reserved to the Board which are reviewed at least annually.

The Board met 15 times during 2020. All Directors are expected to attend all meetings of the Board, any Committees of which they are members and to devote sufficient time to the Company's affairs to fulfil their duties as Directors. Where Directors are unable to attend a meeting, they are encouraged to submit any comments on the meeting materials in advance to the Chair, to ensure that their views are recorded and taken into account during the meeting. David Weymouth, Graham Allatt and Noël Harwerth provided comments for the meetings they were not able to attend.

**Roles of the Chairman, Chief Executive Officer and Senior Independent Director**

The roles of Chairman and Chief Executive Officer (CEO) are distinct and held by different people. There is a clear division of responsibilities, which has been agreed by the Board and is formalised in a schedule of responsibilities for each.

The Chairman, David Weymouth, is responsible for setting the 'tone at the top' and ensuring that the Board has the right mix of skills, experience and development so that it can focus on the key issues affecting the business and for leading the Board and ensuring it acts effectively. Andy Golding, as CEO, has overall responsibility for managing the Group and implementing the strategies and policies agreed by the Board.

Noël Harwerth is the Senior Independent Director (SID). The SID's role is to act as a sounding board for the Chairman and to support him in the delivery of his objectives. This includes ensuring that the views of all other Directors are communicated to, and given due consideration by, the Chairman.

**Balance and independence**

The effectiveness of the Board and its Committees in discharging their duties is essential for the success of the Company. In order to operate effectively, the Board and its Committees comprise a balance of skills, experience, independence and knowledge to encourage constructive debate and challenge to the decision-making process.

**Audit Committee**

The primary role of the Committee is to assist the Board in overseeing the systems of internal control and external financial reporting. The Committee's specific responsibilities are set out in its terms of reference, which are reviewed at least annually. The Audit Committee is Chaired by Rajan Kapoor, the other members are Graham Allatt, Noël Harwerth and Sarah Hedger. The Committee met eight times during 2020; all members attended these meetings. The Committee considered, on behalf of the Board, whether the 2020 Annual Report and Accounts taken as a whole are fair, balanced and understandable and, whether the disclosures are appropriate. Further details on the activities of the Committee are set out in the Group's annual report and accounts.

### Risk Committee

The primary objective of the Committee is to support the Board in discharging its risk oversight and governance responsibilities. The Committee's specific responsibilities are set out in its terms of reference, which are reviewed at least annually. The Committee is Chaired by Graham Allatt, the other members are Noël Harwerth and Rajan Kapoor. The Committee met 11 times during 2020. All members attended these meetings. Further details on the activities of the Committee are set out in the Group's annual report and accounts.

### Environment

Environmental matters are considered in the Strategic report above.

### Internal Control

The Board retains ultimate responsibility for setting the Company's risk appetite and ensuring that there is an effective Risk Management Framework to maintain levels of risk within the risk appetite. The Board regularly reviews its procedures for identifying, evaluating and managing risk, acknowledging that a sound system of internal control should be designed to manage rather than eliminate the risk of failure to achieve business objectives.

Key information in respect of the Group's SRMF and objectives and processes for mitigating risks, including liquidity risk, are set out in detail on pages 32 to 62.

### Auditor

Deloitte LLP was appointed as auditor for the year and has indicated its willingness to continue in office as auditor. A resolution to re-appoint Deloitte as external auditor will be presented at the Company's Annual General Meeting.

Each of the persons who is a Director at the date of approval of this Annual Report confirms that:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Strategic Report and Directors' Report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.
- so far as the Director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- the Director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

This report was approved by the Board on 27 April 2021 and signed on its behalf by:

**Jason Elphick**
Group General Counsel and Company Secretary
OneSavings Bank plc
Registered number: 07312896

# OneSavings Bank plc
# Directors' responsibilities statement
For the Year Ended 31 December 2020

The Directors are responsible for preparing the Annual Report and the Group and parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent Company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and applicable law and have elected to prepare the parent Company financial statements on the same basis.

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 Group and parent Company and of their profit or loss for that period. In preparing each of the Group and parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the parent Company and the Group enabling them to ensure that the financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error and, have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report, Directors' Report, that complies with that law and those regulations.

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.

Approved by the Board and signed on its behalf by:

**Jason Elphick**
General Counsel and Company Secretary
27 April 2021

# Independent auditor's report to the members of OneSavings Bank plc

For the Year Ended 31 December 2020

## Report on the audit of the Financial Statements

### 1. Opinion

In our opinion:

- the Financial Statements of OneSavings Bank plc (the 'parent company') and its subsidiaries (the 'Group') give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2020 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006; and
- the Financial Statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the Financial Statements which comprise:

- the consolidated statement of comprehensive income;
- the consolidated and parent company statements of financial position;
- the consolidated and parent company statements of changes in equity;
- the consolidated and parent company statements of cash flows; and
- the related notes 1 to 53.

The financial reporting framework that has been applied in their preparation of the Group financial statements is applicable law and international accounting standards in conformity with the requirements of the Companies Act 2006 and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and international accounting standards in conformity with the requirements of the Companies Act 2006.

### 2. 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 Group and the parent company in accordance with the ethical requirements that are relevant to our audit of the Financial Statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the parent company.

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

## 3. Summary of our audit approach

| | |
|---|---|
| **Key audit matters** | The key audit matters that we identified in the current year were:<br>• loan impairment provisions; and<br>• effective interest rate income recognition.<br><br>Within this report, key audit matters are identified as follows:<br><br>Newly identified<br>Increased level of risk<br>Similar level of risk<br>Decreased level of risk |
| **Materiality** | The materiality that we used for the Group financial statements was £14m which was determined by reference to normalised profit before tax and net assets. Normalised profit before tax is explained on page 85. |
| **Scoping** | Our Group audit scope focused primarily on three subsidiaries subject to a full scope audit. The subsidiaries selected for a full scope audit were OneSavings Bank plc, Charter Court Financial Services Limited and Interbay ML, Ltd. These three subsidiaries account for 98% of the Group's total assets, 98% of the Group's total liabilities, 96% of the Group's interest receivable and similar income and 98% of the Group's profit before tax. |
| **Significant changes in our approach** | In the prior year we identified the accounting for the acquisition of the Charter Court Financial Services Group and the classification of exceptional items and integration costs to be key audit matters. In the current year, due to the Group undertaking no new acquisitions and the reduction in exceptional items and integration costs, these areas have not been identified as key audit matters for the year ended 31 December 2020. |

## 4. 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 Group's and parent company's ability to continue to adopt the going concern basis of accounting included:

- We obtained and read management's going concern assessment, which included specific consideration of the impacts of the Covid-19 pandemic and the Group's operational resilience, in order to understand, challenge and evidence the key judgements made by management;

- We obtained an understanding of relevant controls around management's going concern assessment;
- We obtained management's income statement, balance sheet and cash flow forecasts and challenged key assumptions and their projected impact on capital and liquidity ratios, particularly with respect to loan book growth and potential credit losses;
- Supported by our in-house prudential risk specialists, we read the most recent ICAAP and ILAAP submissions, assessed management's capital and liquidity projections, assessed the results of management's capital reverse stress testing, challenged key assumptions and methods used in the capital reverse stress testing models and tested the mechanical accuracy of the capital reverse stress testing models;
- We read correspondence with regulators to understand the capital and liquidity requirements imposed by the Group's regulators, and evidence any changes to those requirements;
- We met with the Group's lead regulators, the Prudential Regulation Authority and the Financial Conduct Authority, and discussed their views on existing and emerging risks to the Group and we considered whether these were reflected appropriately in management's forecasts and stress tests;
- We assessed the historical accuracy of forecasts prepared by management; and
- We assessed the appropriateness of the disclosures made in the Financial Statements in view of the FRC guidance.

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 Group's and parent company's ability to continue as a going concern for a period of at least twelve months from when the Financial Statements are authorised for issue.

Our responsibilities and the responsibilities of the Directors with respect to going concern are described in the relevant sections of this report.

## 5. Key audit matters

Key audit matters are those matters that, in our professional judgement, 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 forming our opinion thereon, and we do not provide a separate opinion on these matters.

In the prior year we identified the accounting for the acquisition of the Charter Court Financial Services Group and the classification of exceptional items and integration costs to be key audit matters. In the current year, due to the Group undertaking no new acquisitions and the reduction in exceptional items and integration costs from £20.8m in 2019 to £13.1m in 2020, these areas have not been identified as key audit matters for the year ended 31 December 2020.

### 5.1 Loan impairment provisions

Refer to the judgements in applying accounting policies and critical accounting estimates on page 115 and Note 22 on page 135.

| | |
|---|---|
| **Key audit matter description** | IFRS 9 requires loan impairment provisions to be recognised on an expected credit loss ("ECL") basis. The estimation of ECL provisions in the Group's loan portfolios is inherently uncertain and requires management to make significant judgements and estimates. ECL provisions as at 31 December 2020 were £111.0m (2019: £42.9m), which represented 0.58% (2019: 0.23%) of loans and advances to customers. ECLs are calculated both for individually significant loans and collectively on a portfolio basis which require the use of statistical models incorporating loss data and assumptions on the recoverability of customers' outstanding balances.<br><br>Covid-19 has increased the complexity in estimating ECLs, particularly with regards to determining appropriate forward looking macroeconomic scenarios and appropriately identifying significant increases in credit risk. The ECL provision requires management to make significant judgements and estimates. We therefore consider there to be a key audit matter due to fraud or error in respect of the Group's ECL provision.<br><br>We identified five specific areas in relation to the ECL that require significant management judgement or relate to assumptions to which the overall ECL provision is particularly sensitive.<br><br>• Significant increase in credit risk (SICR): The assessment of whether there has been a significant increase in credit risk between the date of origination of the exposure and 31 December 2020. There is a risk that management's staging criteria does not capture SICR and/or are applied incorrectly. |

- Macroeconomic scenarios: As set out on page 109, the Group sources economic forecasts from a third party economics expert and considers a minimum of four probability weighted scenarios, including base, upside, downside and severe downside scenarios. Due to the economic uncertainty arising from Covid-19, there have been significant changes to the economic assumptions in each of the scenarios, as well as a change to the weightings applied to each scenario. The key economic variables were determined to be the house price index ("HPI") and unemployment. There is significant judgement in determining the probability weighting of each scenario and the assumptions and characteristics of each scenario applied.

- Probability of Default (PD) for accounts which have taken Covid-19 payment holidays: Management applies significant judgement in determining the PD for borrowers who have taken Covid-19 payment holidays. There are limited observed behavioural data for accounts which took payment holidays in 2020, and these data are likely to have been distorted by current government support measures and therefore may not be an accurate reflection of the underlying credit risk of the Covid-19 payment holiday population as at 31 December 2020.

- Propensity to go into possession following default ("PPD") and forced sale discount ("FSD") assumptions: PPD measures the likelihood that a defaulted loan will progress into repossession. FSD measures the difference in sale proceeds between a sale under normal conditions and sale at auction. The loss given default ("LGD") by loan assumed in the ECL provision calculation is highly sensitive to the PPD and FSD assumptions.

- Commercial and individually assessed collateral valuations: In 2020, management implemented a blended approach to value semi commercial properties held by the Group, using a combination of both residential and commercial index movements. The use of a blended commercial property index involves management judgement in determining the weightings assigned to the residential and commercial components of the blended commercial property index. In addition, management uses an in-house real estate team to estimate the market value of collateral on a case by case basis for individually assessed loans.

**How the scope of our audit responded to the key audit matter**

We obtained an understanding of the relevant financial controls over the ECL provision with particular focus on controls over significant management assumptions and judgements used in the ECL determination.

To challenge the Group's SICR criteria, we:

- Evaluated the Group's SICR policy and assessed whether it complies with IFRS 9
- Assessed the PD thresholds used in the SICR assessment by reference to standard validation metrics including the proportion of transfers to stage two driven solely by being 30 days past due, the volatility of loans in stage two and the proportion of loans that spend little or no time in stage two before moving to stage three;

- Challenged the appropriateness of changes made to management's staging framework in response to Covid-19 during the year against the requirements of IFRS 9 and, supported by our modelling specialists, assessed the appropriateness of the changes made in the staging model;
- Tested whether the PD thresholds set by management had been appropriately applied in practice as at 31 December 2020; and
- Performed an independent assessment for a sample of loan accounts, including a focused sample of Covid-19 payment holiday accounts which exited forbearance, to determine whether they have been appropriately allocated to the correct stage.

To challenge the Group's macro-economic scenarios and the probability weightings applied we:

- Agreed the macroeconomics scenarios used in the ECL model to reports prepared by the third party economics expert;
- Assessed the competence, capability and objectivity of the third party economics expert, which included making specific inquiries to understand their approach and modelling assumptions to derive the scenarios;
- Supported by our economic specialists, assessed and challenged management's assessment of scenarios considered and the probability weightings assigned to them in light of the economic position as at 31 December 2020;
- Involved our economic specialists to challenge the Group's economic outlook by reference to other available economic outlook data;
- Performed a benchmarking exercise to compare the appropriateness of selected macroeconomic variables and weightings to those used by peer lenders. The key economic variables were the house price index ("HPI") and unemployment;
- Supported by our analytics and modelling specialists, assessed and challenged the changes made to the model methodology and computer code in the macroeconomics overlay model which applies the scenarios to the relevant ECL components; and
- For a sample of loans, we independently recalculated the ECL using the macroeconomic variables to check they were being applied appropriately.

To challenge the Group's PDs for accounts which took Covid-19 payment holidays in 2020 we:

- Evaluated the Group's staging framework and assessed whether the treatment of accounts which took Covid-19 payment holidays in 2020 complies with IFRS 9;
- Supported by our analytics and modelling specialists, assessed and challenged the computer code script to determine whether the PD adjustments for accounts which took Covid-19 payment holidays in 2020 had been implemented within the model correctly;

| | |
|---|---|
| | • Performed an independent assessment for a sample of loan accounts which took Covid-19 payment holidays in 2020 and those which had not taken such holidays to challenge the completeness and accuracy of the recording of payment holiday forbearance in the lending systems;<br>• Assessed the recent performance of borrowers who were granted payment holidays in order to challenge the PDs applied;<br>• Performed a peer benchmarking exercise to industry peers to compare the Group's ECL coverage ratio on the Covid-19 payment holiday population.<br><br>To challenge the Group's PPD and FSD assumptions we:<br>• Supported by our analytics and modelling specialists, challenged the changes made to computer code in the LGD models;<br>• Recalculated the PPD rates observed on defaulted cases and compared them with the rates used by the Group in the ECL models;<br>• Recalculated the FSD observed on recent property sales on the defaulted accounts and compared them with the rates used by the Group in the ECL models;<br>• Assessed the appropriateness of PPD and FSD assumptions adopted by management through benchmarking to industry peers; and<br>• Assessed the impact of findings raised in management's independent model validation conducted in 2020.<br><br>We performed the following procedures to challenge the Group's blended commercial property index used for commercial property valuations and the case by case estimate of the market value of collateral for individually assessed loans:<br>• Supported by our property valuation specialists, examined management's valuation policies, challenged the use of a blended commercial property index approach and tested a sample of collateral valuations for commercial properties and individually assessed loans by reference to available market data; and<br>• Tested the mechanical accuracy of management's blended commercial property index calculation and that the indexed valuation was appropriately applied in the ECL determination. |
| **Key observations** | We determined that the methodology used and the SICR criteria, PDs applied to accounts which took Covid-19 payment holidays in 2020, and PPD and FSD assumptions management have made in determining the ECL provision as at 31 December 2020 were reasonable. We determined management's collateral valuations to be reasonable and the blended commercial property index to be appropriately determined and applied.<br><br>Notwithstanding that estimating the probability and impact of future economic outcomes is inherently judgemental and that there is heightened economic uncertainty due to Covid-19, on balance, we consider that the macroeconomic scenarios selected by the Directors and the probability weightings applied generate an appropriate portfolio loss distribution. We therefore determined that loan impairment provisions are appropriately stated. |

### 5.2 Effective interest rate income recognition

**Refer to the judgements in applying accounting policies and critical accounting estimates on page 115, the accounting policy on page 102 and Notes 3 and 4 on pages 118 and 119.**

| | |
|---|---|
| **Key audit matter description** | In accordance with the requirements of IFRS 9, management is required to spread directly attributable fees, discounts, incentives and commissions on a constant yield basis ("effective interest rate, EIR") over the shorter of the expected and contractual life of the loan assets. EIR is complex and the Group's approach to determining the EIR involves the use of models and significant estimation in determining the behavioural life of loan assets. Given the complexity and judgement involved in accounting for EIR, there is an opportunity and incentive for management to manipulate the amount of interest income reported in the Financial Statements and revenue recognition is an area susceptible to fraud.<br><br>The Group's net interest income for the year ended 31 December 2020 was £472.2m (2019: £344.7m).<br><br>EIR adjustments arise from revisions to estimated cash receipts or payments for loan assets that occur for reasons other than a movement in market interest rates or credit losses. They result in an adjustment to the carrying amount of the loan asset, with the adjustment recognised in the income statement in interest income and similar income. As the EIR adjustments reflect changes to the timing and volume of forecast customer redemptions, they are inherently judgemental. The level of judgement exercised by management is increased given the limited availability of historical repayment information. For two of the loan portfolios, KRBS and Precise, the EIR adjustments are sensitive to changes in the behavioural life "curves". Covid-19 introduces additional uncertainty with regards to forecasting expected behavioural lives and prepayment rates due to its significant impact on the UK economy and housing market, as well as the measures taken by the UK government to stimulate the economy in response to Covid-19, such as the furlough scheme, payment holidays and the stamp duty holiday. We therefore identified the estimation of the behavioural life for these portfolios as a focus area of our audit.<br><br>We also identified a key audit matter in relation to EIR adjustments on the Group's legacy acquired portfolios. EIR on acquired loan portfolios is inherently more judgemental than originated loan portfolios as it involves modelling the expected cash flows on acquisition and comparing to actual and forecast cash flows at each balance sheet date. These loan portfolios are also underwritten outside of the Group's standard processes and therefore may have different profiles than self-originated loans. |

| | |
|---|---|
| **How the scope of our audit responded to the key audit matter** | We obtained an understanding of the relevant controls over EIR, focusing on the calculation and review of EIR adjustments and the determination of prepayment curves.<br><br>For the two portfolios where the EIR adjustments were most significant and sensitive to changes in behavioural life, we involved our in-house analytics and modelling specialists to run the Group's loan data for all products through our own independent EIR model, using the behavioural life curves derived by the Group. We compared our calculation of the EIR adjustment required to the amount recorded by management.<br><br>For the same portfolios, we involved our in-house modelling specialists to independently derive a behavioural life curve using the Group's loan data over recent years. We used these curves in our own independent EIR model to derive an independent output showing the EIR adjustments that should have been recorded in 2020. We compared this output to the amounts recorded by management.<br><br>We also tested the completeness and accuracy of a sample of inputs into the EIR model for originated loans.<br><br>For the legacy acquired portfolios, supported by our analytics and modelling specialists, we challenged the assumptions and modelling approach taken to determine the EIR adjustments, tested the completeness and accuracy of a sample of inputs to the modelling, re-performed the discounted cash flow calculations and challenged whether forecasts were consistent with historical performance and our understanding of the nature of the cash flows.<br><br>In challenging the Group's assumptions over the estimated life of loan accounts, we also independently considered whether behavioural data since the start of the first national lockdown in March 2020 were indicative of future behaviour. We considered factors such as the significant impact that Covid-19 has had on the UK economy and housing market, and the measures taken by the UK government to stimulate the economy, such as the furlough scheme, payment holidays and the stamp duty holiday. |
| **Key observations** | Notwithstanding that estimating the future behaviour of loan assets is inherently judgemental and that there is heightened economic uncertainty due to Covid-19, we determined that the EIR models and assumptions used were appropriate and that net interest income for the period is appropriately stated. |

## 6. Our application of materiality

### 6.1 Materiality

We define materiality as the magnitude of misstatement in the Financial Statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the Financial Statements as a whole as follows:

| | Group financial statements | Parent company financial statements |
|---|---|---|
| **Materiality** | £14.0m (2019: £14.0m) | £11.1m (2019: £10.2m) |
| **Basis for determining materiality** | We determined materiality for the Group by reference to 5% of normalised profit before tax of £271.1m (£13.6m), and 1% of net assets of £1,676.9m (£16.8m), capped at prior year materiality of £14.0m.<br><br>Normalised profit before tax is statutory profit before tax of £260.4m as at 31 December 2020 (2019: £209.1m) excluding integration costs of £9.8m (2019: £5.2m) and exceptional items of £3.3m (2019: £15.6m). In prior year the normalised profit before tax also excluded the negative goodwill credit of £10.8m. | We determined materiality for the parent company based on 5% of normalised profit before tax. We excluded integration costs and exceptional transaction costs from statutory profit before tax, consistent with our approach to Group materiality. |
| **Rationale for the benchmark applied** | We considered both a profit based measure and net assets as benchmarks for determining materiality. This is consistent with the prior year approach.<br><br>The emergence of Covid-19 has caused significant economic uncertainty and we therefore capped the materiality at the prior year level of £14.0m.<br><br>In the prior year we determined materiality for the Group by reference to a range of £11.0m to £15.0m based on 5% of normalised profit before tax of £219.1m and 1% of net assets of £1,477.0m as at 31 December 2019. | We consider a profit based measure to be the most relevant benchmark for users of the accounts. |

### 6.2 Performance materiality

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the Financial Statements as a whole.

| | Group financial statements | Parent company financial statements |
|---|---|---|
| **Performance materiality** | 60% of Group materiality (2019: 70%) | 60% of parent company materiality (2019: 70%) |
| **Basis and rationale for determining performance materiality** | Group performance materiality was set at 60% of Group materiality (2019: 70%). In determining performance materiality, we considered a number of factors, including: our understanding of the control environment; our understanding of the business; and the low number of uncorrected misstatements identified in the prior year. We reduced performance materiality from the prior year in response to the potentially pervasive impact of Covid-19 on the control environment and financial reporting. | |

### 6.3 Error reporting threshold

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £700k (2019: £700k), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the Financial Statements.

## 7. An overview of scope of our audit

### 7.1 Identification and scoping of components

Our Group audit was scoped by obtaining an understanding of the Group and its environment, including Group-wide controls and assessing the risks of material misstatement at the Group level.

Our Group audit scope focused primarily on OneSavings Bank plc and the two main subsidiary entities, being the banking entity Charter Court Financial Services Limited, as well as Interbay ML, Ltd, another significant lending subsidiary. The Company and two subsidiaries were significant components and subject to a full scope audit (2019: the Company and two subsidiaries subject to a full scope audit). They represent 96% (2019: 96%) of the Group's interest receivable and similar income, 98% (2019: 97%) of profit before tax, 98% (2019: 98%) of total assets and 98% (2019: 98%) of total liabilities. The subsidiaries were selected to provide an appropriate basis of undertaking audit work to address the risks of material misstatement including those identified as key audit matters above. Our audits of each of the subsidiaries were performed using lower levels of materiality based on their size relative to the Group. The materiality for each subsidiary audit ranged from £5.3m to £11.1m (2019: £5.4m to £10.2m).





We tested the Group's consolidation process and carried out analytical procedures to confirm that there were no significant risks of material misstatement in the aggregated financial information of the remaining subsidiaries not subject to a full scope audit or specified audit procedures.

### 7.2 Our consideration of the control environment

We identified the key IT systems relevant to the audit to be those used in the financial reporting, lending and savings businesses. For these controls we involved our IT specialists to perform testing over the general IT controls, including testing of user access and change management systems.

In the current year we relied on controls for some of the lending business and related interest income. For the areas where we relied on controls, we performed walkthroughs with management to understand the process and controls, identified and tested relevant controls that address risks of material misstatement in financial reporting.

### 7.3 Oversight of the audit teams

All audit work for the purposes of the Group audit was performed by Deloitte LLP in the UK. The audit team for the Group and the parent company were based in London. There was a component audit team for the component audit of Charter Court Financial Services Limited which is based in Wolverhampton. The Senior Statutory Auditor has responsibility for directing and supervising all aspects of the audit work of the component auditor. In discharging this responsibility, the Group audit team held regular meetings with local management and had regular virtual meetings with the component audit team to oversee the component audit. The Group audit team maintained dialogue with the component auditor throughout all phases of the audit and performed a remote file review of the component audit team's work.

## 8. 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 our 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 this other information, we are required to report that fact.

We have nothing to report in this regard.

## 9. Responsibilities of directors

As explained more fully in the Directors' responsibilities statement, 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 Group's and the parent 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 Group or the parent company or to cease operations, or have no realistic alternative but to do so.

## 10. 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.

A further description of our responsibilities for the audit of the Financial Statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

## 11. Extent to which 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 material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

**11.1 Identifying and assessing potential risks related to irregularities**

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we considered the following:

- the nature of the industry and sector, control environment and business performance including the design of the Group's remuneration policies, key drivers for directors' remuneration, bonus levels and performance targets;
- the Group's own assessment of the risks that irregularities may occur either as a result of fraud or error that was approved by the Board;
- results of our enquiries of management, internal audit and the Audit Committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the Group's documentation of their policies and procedures relating to:
    - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
    - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud. As set out on page 206, the Directors recorded an impairment provision of £20.0m in relation to potential fraudulent activity by a third party on a secured funding line provided by the Group;
    - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations;

- the matters discussed among the audit engagement team including the component audit team and involving relevant internal specialists, including tax, valuations, real estate, IT and analytics and modelling specialists regarding how and where fraud might occur in the Financial Statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in the following areas: loan impairment provisions, effective interest rate income recognition and the classification of exceptional items and integration costs. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory frameworks that the Group operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the Financial Statements. The key laws and regulations we considered in this context included the relevant provisions of the UK Companies Act 2006, Listing Rules and tax legislation.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the Financial Statements but compliance with which may be fundamental to the Group's ability to operate or to avoid a material penalty. These included the Group's prudential regulatory requirements and capital, liquidity and conduct requirements.

**11.2 Audit response to risks identified**

As a result of performing the above, we identified loan impairment provisions and effective interest rate income recognition using the effective interest rate as key audit matters related to the potential risk of fraud. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters.

In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the Financial Statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the Financial Statements;
- enquiring of management, the Audit Committee and in-house and external legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with the Prudential Regulation Authority, the Financial Conduct Authority and HMRC;
- in addressing the risk of fraud in the classification of exceptional items and integration costs, testing the appropriateness of the classification for a sample of these items;

- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws, regulations and potential fraud risks to all engagement team members including internal specialists and the component audit team and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

## Report on other legal and regulatory requirements

### 12. 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 the Directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the Group and the parent company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the Directors' report.

### 13. Opinions on other matters prescribed by the Capital Requirements (Country-by-Country Reporting) Regulation 2013

In our opinion the information given in note 48 to the Financial Statements for the financial year ended 31 December 2020 has been properly prepared, in all material respects, in accordance with the Capital Requirements (Country-by Country Reporting) Regulations 2013.

## 14. Matters on which we are required to report by exception

### 14.1 Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

### 14.2 Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been.

We have nothing to report in respect of these matters.

## 15. Other matters which we are required to address

### 15.1 Auditor tenure

Following the recommendation of the Audit Committee, we were appointed by the shareholders of the Group on 9 May 2019 to audit the Group financial statements for the year ended 31 December 2019 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is two years, covering the years ended 31 December 2019 to 31 December 2020.

### 15.2 Consistency of the audit report with the additional report to the Audit Committee

Our audit opinion is consistent with the additional report to the Audit Committee we are required to provide in accordance with ISAs (UK).

## 16. 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.

Giles Lang

**Giles Lang, FCA (Senior statutory auditor)**
For and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom
27 April 2021

# OneSavings Bank plc
# Statement of Comprehensive Income
For the year ended 31 December 2020

| | Note | **Group 2020 £m** | Group 2019 £m |
|---|---|---|---|
| Interest receivable and similar income | 3 | **711.9** | 539.9 |
| Interest payable and similar charges | 4 | **(239.7)** | (195.2) |
| **Net interest income** | | **472.2** | 344.7 |
| Fair value gains/(losses) on financial instruments | 5 | **7.4** | (3.3) |
| Gain/(loss) on sale of financial instruments | 6 | **20.0** | (0.1) |
| Other operating income | 7 | **9.0** | 2.1 |
| **Total income** | | **508.6** | 343.4 |
| Administrative expenses | 8 | **(157.1)** | (108.7) |
| Provisions | 38 | **(0.1)** | - |
| Impairment of financial assets | 23 | **(71.0)** | (15.6) |
| Impairment of intangible assets | 9 | **(7.0)** | - |
| Gain on Combination with CCFS | | **-** | 10.8 |
| Integration costs | 12 | **(9.8)** | (5.2) |
| Exceptional items | 13 | **(3.3)** | (15.6) |
| **Profit before taxation** | | **260.3** | 209.1 |
| Taxation | 14 | **(64.1)** | (50.3) |
| **Profit for the year** | | **196.2** | 158.8 |
| **Other comprehensive income** | | | |
| **Items which may be reclassified to profit or loss:** | | | |
| Fair value changes on financial instruments measured as Fair Value through Other Comprehensive Income: | | | |
| Arising in the year | | **1.0** | 0.8 |
| Revaluation of foreign operations | | **-** | (0.6) |
| Tax on items in other comprehensive income | | **(0.5)** | (0.2) |
| **Other comprehensive income** | | **0.5** | - |
| **Total comprehensive income for the year** | | **196.7** | 158.8 |

The above results are derived wholly from continuing operations.

The notes on pages 99 to 209 form part of these accounts.

The Financial Statements on pages 94 to 209 were approved by the Board of Directors on 27 April 2021.

# OneSavings Bank plc
## Statement of Financial Position
As at 31 December 2020

| | Note | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash in hand | | **0.5** | 0.4 | **0.5** | 0.4 |
| Loans and advances to credit institutions | 17 | **2,676.2** | 2,204.6 | **1,518.1** | 1,196.0 |
| Investment securities | 18 | **471.2** | 635.3 | **15.0** | 149.8 |
| Loans and advances to customers | 19 | **19,230.7** | 18,446.8 | **8,531.7** | 8,394.2 |
| Fair value adjustments on hedged assets | 25 | **181.6** | 16.8 | **127.4** | 52.8 |
| Derivative assets | 24 | **12.3** | 21.1 | **4.7** | 8.7 |
| Other assets | 26 | **9.1** | 14.3 | **5.7** | 7.5 |
| Current taxation asset | | **8.4** | - | **3.8** | - |
| Deferred taxation asset | 27 | **4.7** | 4.8 | **3.1** | 2.2 |
| Property, plant and equipment | 29 | **39.2** | 41.6 | **20.5** | 21.2 |
| Intangible assets | 30 | **20.6** | 31.4 | **7.0** | 7.7 |
| Investments in subsidiaries and intercompany loans | 31 | **-** | - | **3,137.3** | 3,629.4 |
| **Total assets** | | **22,654.5** | 21,417.1 | **13,374.8** | 13,469.9 |
| **Liabilities** | | | | | |
| Amounts owed to credit institutions | 32 | **3,570.2** | 3,068.8 | **1,900.5** | 1,671.1 |
| Amounts owed to retail depositors | 33 | **16,603.1** | 16,255.0 | **9,705.3** | 9,435.7 |
| Fair value adjustments on hedged liabilities | 25 | **8.2** | (5.1) | **3.1** | (0.1) |
| Amounts owed to other customers | 34 | **72.9** | 29.7 | **5.8** | 8.9 |
| Debt securities in issue | 35 | **421.9** | 296.3 | **-** | - |
| Derivative liabilities | 24 | **163.6** | 92.8 | **93.8** | 54.3 |
| Lease liabilities | 36 | **11.7** | 13.3 | **3.9** | 4.3 |
| Other liabilities | 37 | **27.8** | 34.9 | **13.8** | 17.1 |
| Provisions | 38 | **1.8** | 1.6 | **1.6** | 1.6 |
| Current taxation liability | | **-** | 41.5 | **-** | 16.4 |
| Deferred taxation liability | 28 | **48.3** | 63.1 | **-** | - |
| Deemed loan liabilities | 20 | **-** | - | **66.2** | 240.2 |
| Intercompany loans | 31 | **-** | - | **37.9** | 643.9 |
| Subordinated liabilities | 39 | **10.5** | 10.6 | **10.5** | 10.6 |
| Perpetual subordinated bonds | 40 | **37.6** | 37.6 | **37.6** | 37.6 |
| | | **20,977.6** | 19,940.1 | **11,880.0** | 12,141.6 |
| **Equity** | | | | | |
| Share capital | 42 | **4.5** | 4.5 | **4.5** | 4.5 |
| Share premium | 42 | **-** | 864.2 | **-** | 864.2 |
| Retained earnings | | **1,604.6** | 553.2 | **1,423.7** | 407.0 |
| Other reserves | 43 | **67.8** | 55.1 | **66.6** | 52.6 |
| | | **1,676.9** | 1,477.0 | **1,494.8** | 1,328.3 |
| **Total equity and liabilities** | | **22,654.5** | 21,417.1 | **13,374.8** | 13,469.9 |

The profit after tax for the year ended 31 December 2020 of OneSavings Bank plc as a Company was £164.5m (2019: £155.2m). As permitted by section 408 of the Companies Act 2006, no separate Statement of Comprehensive Income is presented in respect of the Company.

The notes on pages 99 to 209 form part of these accounts. The financial statements on pages 94 to 209 were approved by the Board of Directors on 27 April 2021 and signed on its behalf by:

A.C. Talintyre

**Andy Golding**
Chief Executive Officer
Company number: 07312896

**April Talintyre**
Chief Financial Officer

# OneSavings Bank plc
## Statement of Changes in Equity
For the year ended 31 December 2020

| Group | Share capital £m | Share premium £m | Capital contribution £m | Transfer reserve £m | Own shares[1] £m | Foreign exchange reserve £m | FVOCI reserve £m | Share-based payment reserve £m | Retained earnings £m | Additional Tier 1 securities £m | Total £m |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **At 31 December 2018** | 2.4 | 158.8 | 6.5 | (12.8) | - | (0.4) | (0.1) | 4.7 | 439.3 | 60.0 | 658.4 |
| Profit for the year | - | - | - | - | - | - | - | - | 158.8 | - | 158.8 |
| Shares issued as consideration for CCFS Combination | 2.0 | 705.1 | - | - | - | - | - | - | (6.4) | - | 700.7 |
| Own shares | - | - | - | - | (3.7) | - | - | - | - | - | (3.7) |
| Coupon paid on Additional Tier 1 securities | - | - | - | - | - | - | - | - | (5.5) | - | (5.5) |
| Dividends paid | - | - | - | - | - | - | - | - | (37.3) | - | (37.3) |
| Other comprehensive income | - | - | - | - | - | (0.6) | 0.8 | - | - | - | 0.2 |
| Share-based payments | 0.1 | 0.3 | - | - | - | - | - | (0.2) | 4.3 | - | 4.5 |
| Tax recognised in equity | - | - | - | - | - | - | (0.2) | 1.1 | - | - | 0.9 |
| **At 31 December 2019** | 4.5 | 864.2 | 6.5 | (12.8) | (3.7) | (1.0) | 0.5 | 5.6 | 553.2 | 60.0 | 1,477.0 |
| Profit for the year | - | - | - | - | - | - | - | - | **196.2** | - | **196.2** |
| Own shares[1] | - | - | - | - | **3.7** | - | - | - | **(3.5)** | - | **0.2** |
| Coupon paid on Additional Tier 1 securities | - | - | - | - | - | - | - | - | **(5.5)** | - | **(5.5)** |
| Dividends paid | - | - | - | - | - | - | - | - | - | - | - |
| Other comprehensive income | - | - | - | - | - | - | **1.0** | - | - | - | **1.0** |
| Share-based payments | - | **2.6** | - | - | - | - | - | **2.4** | **3.2** | - | **8.2** |
| Tax recognised in equity | - | - | - | - | - | - | **(0.5)** | **(0.2)** | **0.5** | - | **(0.2)** |
| Transfer between reserves | - | - | **(6.5)** | **12.8** | - | - | - | - | **(6.3)** | - | - |
| Cancellation of OneSavings Bank plc share capital and share premium | **(4.5)** | **(866.8)** | - | - | - | - | - | - | **871.3** | - | - |
| Issuance of OneSavings Bank plc share capital to OSBG | **4.5** | - | - | - | - | - | - | - | **(4.5)** | - | - |
| **At 31 December 2020** | **4.5** | - | **0.0** | - | - | **(1.0)** | **1.0** | **7.8** | **1,604.6** | **60.0** | **1,676.9** |

[1] The Group ceased look-through accounting for the Employee Benefit Trusts following the insertion of OSB GROUP PLC as the listed and ultimate holding company of the Group on 27 November 2020.

# OneSavings Bank plc

## Statement of Changes in Equity (continued)

For the year ended 31 December 2020

| Company | Share capital £m | Share premium £m | Capital contribution £m | Transfer reserve £m | Own shares[1] £m | FVOCI reserve £m | Share-based payment reserve £m | Retained earnings £m | Additional Tier 1 securities £m | Total £m |
|---|---|---|---|---|---|---|---|---|---|---|
| **At 31 December 2018** | 2.4 | 158.8 | 6.2 | (15.2) | - | (0.1) | 4.7 | 296.7 | 60.0 | 513.5 |
| Profit for the year | - | - | - | - | - | - | - | 155.2 | - | 155.2 |
| Shares issued as consideration for CCFS Combination | 2.0 | 705.1 | - | - | - | - | - | (6.4) | - | 700.7 |
| Own shares | - | - | - | - | (3.7) | - | - | - | - | (3.7) |
| Coupon paid on Additional Tier 1 securities | - | - | - | - | - | - | - | (5.5) | - | (5.5) |
| Dividends paid | - | - | - | - | - | - | - | (37.3) | - | (37.3) |
| Other comprehensive income | - | - | - | - | - | 0.1 | - | - | - | 0.1 |
| Share-based payments | 0.1 | 0.3 | - | - | - | - | (0.2) | 4.3 | - | 4.5 |
| Tax recognised in equity | - | - | - | - | - | - | 0.8 | - | - | 0.8 |
| **At 31 December 2019** | 4.5 | 864.2 | 6.2 | (15.2) | (3.7) | - | 5.3 | 407.0 | 60.0 | 1,328.3 |
| Profit for the year | - | - | - | - | - | - | - | 164.5 | - | 164.5 |
| Own shares[1] | - | - | - | - | 3.7 | - | - | (3.9) | - | (0.2) |
| Coupon paid on Additional Tier 1 securities | - | - | - | - | - | - | - | (5.5) | - | (5.5) |
| Dividends paid | - | - | - | - | - | - | - | - | - | - |
| Other comprehensive income | - | - | - | - | - | (0.1) | - | - | - | (0.1) |
| Share-based payments | - | 2.6 | - | - | - | - | 1.6 | 3.8 | - | 8.0 |
| Tax recognised in equity | - | - | - | - | - | - | (0.2) | - | - | (0.2) |
| Transfer between reserves | - | - | (6.2) | 15.2 | - | - | - | (9.0) | | - |
| Cancellation of OneSavings Bank plc share capital and share premium | (4.5) | (866.8) | - | - | - | - | - | 871.3 | - | - |
| Issuance of OneSavings Bank plc share capital to OSBG | 4.5 | - | - | - | - | - | - | (4.5) | | - |
| **At 31 December 2020** | 4.5 | - | - | - | - | (0.1) | 6.7 | 1,423.7 | 60.0 | 1,494.8 |

[1] The Company ceased look-through accounting for the Employee Benefit Trusts following the insertion of OSB GROUP PLC as the listed and ultimate holding company of the Group on 27 November 2020.

The reserves are further disclosed in note 43

# OneSavings Bank plc
# Statement of Cash Flows
For the year ended 31 December 2020

| | Note | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|---|
| **Cash flows from operating activities** | | | | | |
| Profit before taxation | | **260.3** | 209.1 | **197.3** | 189.4 |
| Expenses recognised in equity | | **-** | (6.4) | **-** | (6.4) |
| Adjustments for non-cash items | 50 | **76.7** | 26.2 | **39.2** | 33.2 |
| Changes in operating assets and liabilities | 50 | **(1,537.0)** | (711.8) | **(573.7)** | (577.4) |
| **Cash used in operating activities** | | **(1,200.0)** | (482.9) | **(337.2)** | (361.2) |
| Provisions refunded/(paid) | | **0.1** | (0.2) | **-** | (0.2) |
| Net tax paid | | **(128.8)** | (53.0) | **(53.6)** | (32.4) |
| **Net cash used in operating activities** | | **(1,328.7)** | (536.1) | **(390.8)** | (393.8) |
| **Cash flows from investing activities** | | | | | |
| Unencumbered cash acquired on CCFS Combination | | **-** | 870.4 | **-** | - |
| Maturity and sales of investment securities | 18 | **407.3** | 357.7 | **291.1** | 349.0 |
| Purchases of investment securities | 18 | **(190.9)** | (389.9) | **(205.9)** | (389.9) |
| Interest received on investment securities | | **7.0** | - | **0.4** | 0.0 |
| Sales of financial instruments | 6 | **539.9** | - | **248.9** | - |
| Purchases of equipment and intangible assets | 30,29 | **(7.5)** | (11.6) | **(4.3)** | (6.7) |
| **Cash generated from investing activities** | | **755.8** | 826.6 | **330.2** | (47.6) |
| **Cash flows from financing activities** | | | | | |
| Financing received | 41 | **1,991.2** | 872.7 | **1,059.6** | 601.8 |
| Financing repaid | 41 | **(1,103.6)** | (338.5) | **(764.7)** | (275.0) |
| Cash held in deconsolidated special purpose vehicles | | **(23.0)** | - | **-** | - |
| Interest paid on financing | | **(18.9)** | (2.6) | **(9.8)** | (2.5) |
| Coupon paid on Additional Tier 1 securities | | **(5.5)** | (5.5) | **(5.5)** | (5.5) |
| Dividends paid | 15 | **-** | (37.3) | **-** | (37.3) |
| Proceeds from issuance of shares under employee SAYE schemes | 42 | **2.5** | 0.4 | **2.6** | 0.4 |
| Cash payments on lease liabilities | 36 | **(2.0)** | (1.1) | **(0.6)** | (0.8) |
| **Cash generated from financing activities** | | **840.7** | 488.1 | **281.6** | 281.1 |
| **Net increase/(decrease) in cash and cash equivalents** | | **267.8** | 778.6 | **221.0** | (160.3) |
| **Cash and cash equivalents at the beginning of the year** | 16 | **2,102.8** | 1,324.2 | **1,156.6** | 1,316.9 |
| **Cash and cash equivalents at the end of the year** | 16 | **2,370.6** | 2,102.8 | **1,377.6** | 1,156.6 |
| **Movement in cash and cash equivalents** | | **267.8** | 778.6 | **221.0** | (160.3) |

## 1. Accounting policies

The principal accounting policies applied in the preparation of the financial statements for the Group and the Company are set out below.

### a) Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC).

The financial statements have been prepared on a historical cost basis, as modified by the revaluation of investment securities held at fair value through other comprehensive income (FVOCI) and derivative contracts and other financial assets held at fair value through profit or loss (FVTPL) (see note p(vi)).

As permitted by section 408 of the Companies Act 2006, no Statement of Comprehensive Income is presented for the Company.

### b) Going concern

The Board undertakes regular rigorous assessments of whether the Group is a going concern in the light of current economic conditions and all available information about future risks and uncertainties.

In assessing whether the going concern basis is appropriate, projections for the Group have been prepared, covering its future performance, capital and liquidity for a period in excess of 12 months from the date of approval of these Financial Statements. These forecasts have been subject to sensitivity tests, including stress scenarios, which have been compared to the latest Brexit and COVID-19 pandemic economic scenarios provided by the Group's external economic advisors, as well as reverse stress tests.

The assessments were significantly influenced by COVID-19 implications, covering the Group's capital, liquidity and operational resilience, including the following:

- Financial and capital forecasts were prepared under stress scenarios which were assessed against the latest COVID-19 related economic forecasts provided by the Group's external economic advisors. Reverse stress tests were also run, to assess what combinations of House Price Index and unemployment variables would result in the Group utilising its regulatory capital buffers in full and breaching the Group's minimum prudential requirements along with analysis and insight from the Group's Internal Capital Adequacy Assessment Process (ICAAP). The Directors assessed the likelihood of those reverse stress scenarios occurring within the next 12 months and concluded that the likelihood is remote.

- The latest liquidity and contingent liquidity positions and forecasts were assessed against the ILAAP stress scenarios, which were reviewed for suitability in the context of COVID-19 related stresses.

- The Group continues to assess the resilience of its business operating model and supporting infrastructure in the context of the emerging economic, business and regulatory environment. The key areas of focus continue to be on the provision of critical services to customers, employee health and safety and the evolving governmental policies and guidelines. The Group has assessed and enhanced its information technology platforms to support its employees with flexible working and homeworking across all locations, ensuring stable access to core systems, data and communication devices. The response to the pandemic demonstrates the inherent resilience of the Group's critical processes and infrastructure. It also reflects the necessary agility in responding to future operational demands. The operational dependencies on third-party vendors and outsourcing arrangements continue to be an important area of focus.

**1. Accounting policies** (continued)

The Group's financial projections, supported by the COVID-19 assessments, demonstrate that the Group has sufficient capital and liquidity to continue to meet its regulatory capital requirements as set out by the PRA.

The Board has therefore concluded that the Group has sufficient resources to continue in operational existence for a period in excess of 12 months and as a result, it is appropriate to prepare these Financial Statements on a going concern basis.

**c) Basis of consolidation**

The Group accounts include the results of the Company and its subsidiary undertakings. Subsidiaries are fully consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that control ceases. Upon consolidation, intercompany transactions, balances and unrealised gains on transactions are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency, so far as is possible, with the policies adopted by the Group.

Subsidiaries are those entities, including structured entities, over which the Group has control. The Group controls an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the investee. The Group has power over an entity when it has existing rights that give it the current ability to direct the activities that most significantly affect the entity's returns. Power may be determined on the basis of voting rights or, in the case of structured entities, other contractual arrangements.

Where the Group does not retain a direct ownership interest in a securitisation entity, but the Directors have determined that the Group controls those entities, they are treated as subsidiaries and are consolidated. Control is determined to exist if the Group has the power to direct the activities of each entity (for example, managing the performance of the underlying mortgage assets and raising debt on those mortgage assets which is used to fund the Group) and, in addition to this, control is exposed to a variable return (for example, retaining the residual risk on the mortgage assets). Securitisation structures that do not meet these criteria are not treated as subsidiaries and are excluded from the consolidated accounts. The Company applies the net approach in accounting for securitisation structures where it retains an interest in the securitisation, netting the loan notes held against the deemed loan balance.

The Group's Employee Benefit Trust (EBT) was controlled and recognised by the Company using the look-through approach until 27 November 2020, when OSB GROUP PLC was inserted as the listed holding company of the Group.

The Group is not deemed to control an entity when it exercises power over an entity in an agency capacity. In determining whether the Group is acting as an agent, the Directors consider the overall relationship between the Group, the investee and other parties to the arrangement with respect to the following factors: (i) the scope of the Group's decision-making power; (ii) the rights held by other parties; (iii) the remuneration to which the Group is entitled; and (iv) the Group's exposure to variability of returns. The determination of control is based on the current facts and circumstances and is continuously assessed. In some circumstances, different factors and conditions may indicate that different parties control an entity depending on whether those factors and conditions are assessed in isolation or in totality. Judgement is applied in assessing the relevant factors and conditions in totality when determining whether the Group controls an entity. Specifically, judgement is applied in assessing whether the Group has substantive decision-making rights over the relevant activities and whether it is exercising power as a principal or an agent.

## 1. Accounting policies (continued)

### d) Business combinations

The Group uses the acquisition method to account for business combinations. The Group recognises the identifiable assets acquired and liabilities assumed at their acquisition date fair values. The Group recognises deferred tax on the difference between fair value and the acquisition date carrying value in accordance with International Accounting Standard (IAS) 12. The consideration transferred for each business combination is measured at fair value and, comprises the sum of equity interest issued by the Group. Acquisition-related costs are recognised as exceptional items within profit or loss.

The Group recognises goodwill on business combinations when the fair value of consideration transferred exceeds the fair value of identifiable assets acquired less the fair value of liabilities assumed. The Group recognises a gain within profit or loss when the fair value of consideration transferred is less than the fair value of identifiable assets acquired less the fair value of liabilities assumed.

The Group reports provisional amounts for business combinations when the accounting is incomplete at the reporting date following the combination. During the measurement period, the Group adjusts provisional amounts recognised at the acquisition date to reflect new information obtained that existed as of the acquisition date and would have affected the measurement of the amounts recognised as at that date. The Group also recognises additional assets or liabilities during the reporting period if new information is obtained that existed as of the acquisition date and would have resulted in the recognition of those assets or liabilities as at that date. The Group adjusts the gain taken to profit or loss where there is negative goodwill, or adjusts goodwill recognised on the balance sheet, when provisional amounts are finalised or additional assets and liabilities are recognised during the measurement period. The measurement period shall not exceed one year from the acquisition date.

The Group finalised the acquisition date fair values of assets acquired and liabilities assumed in the Combination with CCFS prior to 3 October 2020. There were no changes to the provisional fair values recognised on the assets or liabilities.

### e) Foreign currency translation

The consolidated financial statements are presented in Pounds Sterling which is the presentation currency of the Group. The financial statements of each of the Company's subsidiaries are measured using the currency of the primary economic environment in which the subsidiary operates (the functional currency). Foreign currency transactions are translated into the functional currencies using the exchange rates prevailing at the date of the transactions. Monetary items denominated in foreign currencies are retranslated at the rate prevailing at the period end.

Foreign exchange (FX) gains and losses resulting from the retranslation and settlement of these items are recognised in profit or loss. Non-monetary items measured at cost in the foreign currency are translated using the spot FX rate at the date of the transaction.

The assets and liabilities of foreign operations with functional currencies other than Pounds Sterling are translated into the presentation currency at the exchange rate on the reporting date. The income and expenses of foreign operations are translated at the rates on the dates of transactions. Exchange differences on foreign operations are recognised in other comprehensive income and accumulated in the foreign exchange reserve within equity.

**1. Accounting policies** (continued)

**f) Segmental reporting**

IFRS 8 requires operating segments to be identified on the basis of internal reports and components of the Group which are regularly reviewed by the chief operating decision maker to allocate resources to segments and to assess their performance. For this purpose, the chief operating decision maker of the Group is the Board of Directors.

The Group provides loans and asset finance within the UK and the Channel Islands only.

The Group segments its lending business and operates under two segments:

- OneSavings Bank (OSB)
- Charter Court Financial Services (CCFS)

The Group has disclosed the risk management tables in note 45 at a sub-segment level to provide detailed analysis of the Group's core lending business.

**g) Interest income and expense**

Interest income and interest expense for all interest-bearing financial instruments measured at amortised cost are recognised in profit or loss using the effective interest rate (EIR) method. The EIR is the rate which discounts the expected future cash flows, over the expected life of the financial instrument, to the net carrying value of the financial asset or liability.

When calculating the EIR, the Group estimates cash flows considering all contractual terms of the instrument and behavioural aspects (for example, prepayment options) but not considering future credit losses. The calculation of the EIR includes transaction costs and fees paid or received that are an integral part of the interest rate, together with the discounts or premiums arising on the acquisition of loan portfolios. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial instrument.

The Group monitors the actual cash flows for each acquired book and where they diverge significantly from expectation, the future cash flows are reset. In assessing whether to adjust future cash flows on an acquired portfolio, the Group considers the cash variance on an absolute and percentage basis. The Group also considers the total variance across all acquired portfolios. Where cash flows for an acquired portfolio are reset, they are discounted at the EIR to derive a new carrying value, with changes taken to profit or loss as interest income.

The EIR is adjusted where there is a change to the reference interest rate (LIBOR or base rate) affecting portfolios with a variable interest rate which will impact future cash flows. The revised EIR is the rate which exactly discounts the revised cash flows to the net carrying value of the loan portfolio.

Interest income on investment securities is included in interest receivable and similar income. Interest on derivatives is included in interest receivable and similar income or interest expense and similar charges following the underlying instrument it is hedging.

Coupons paid on Additional Tier 1 securities (AT1 securities) are recognised directly in equity in the period in which they are paid.

**1. Accounting policies** (continued)

### h) Fees and commissions

Fees and commissions which are an integral part of the EIR of a financial instrument are recognised as an adjustment to the EIR and recorded in interest income. The Group includes early redemption charges within the EIR.

Fees received on mortgage administration services and mortgage origination activities, which are not an integral part of the EIR, are accounted for in accordance with IFRS 15 Revenue from Contracts with Customers, with income recognised when the services are delivered and the benefits are transferred to clients and customers.

Other fees and commissions are recognised on the accruals basis as services are provided or on the performance of a significant act, net of VAT and similar taxes.

### i) Integration costs and exceptional items

Integration costs and exceptional items are those items of income or expenses that do not relate to the Group's core operating activities, are not expected to recur and are material in the context of the Group's performance. These items are disclosed separately within the Statement of Comprehensive Income and the Notes to the Financial Statements.

### j) Taxation

Income tax comprises current and deferred tax. It is recognised in profit or loss, other comprehensive income or directly in equity, consistent with the recognition of items it relates to. The Group recognises tax on the AT1 securities directly in profit or loss.

Current tax is the expected tax charge on the taxable income for the year and any adjustments in respect of previous years.

Deferred tax is the tax expected to be payable or recoverable in respect of temporary differences between the carrying amounts of assets or liabilities for accounting purposes and carrying amounts for tax purposes.

Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available to utilise the asset. The recognition of deferred tax is mainly dependent on the projections of future taxable profits and future reversals of temporary differences. The current projections of future taxable income indicate that the Group will be able to utilise its deferred tax asset within the foreseeable future.

The Company and the subsidiaries are in a group payment arrangement for corporation tax and show a net corporation tax liability and deferred tax asset accordingly. In 2019, the Group's CCFS subsidiaries were not part of the group payment arrangement and the corporation tax liability and deferred tax asset were not netted.

### k) Dividends

Dividends are recognised in equity in the period in which they are paid or, if earlier, approved by shareholders.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

**1. Accounting policies** (continued)

**l) Cash and cash equivalents**

For the purposes of the Consolidated Statement of Cash Flows, cash and cash equivalents comprise cash, non-restricted balances with central banks and highly liquid financial assets with original maturities of less than three months subject to an insignificant risk of changes in their fair value.

**m) Intangible assets**

Purchased software and costs directly associated with the development of computer software are capitalised as intangible assets where the software is a unique and identifiable asset controlled by the Group and will generate future economic benefits. Costs to establish technological feasibility or to maintain existing levels of performance are recognised as an expense. The Group only recognises internally-generated intangible assets if all of the following conditions are met:

- an asset is being created that can be identified after establishing the technical and commercial feasibility of the resulting product;
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Subsequent expenditure on an internally generated intangible asset, after its purchase or completion, is recognised as an expense in the period in which it is incurred. Where no internally generated intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred.

Intangible assets are reviewed for impairment annually, and if they are considered to be impaired, are written down immediately to their recoverable amounts.

Intangible assets are amortised in profit or loss over their estimated useful lives as follows:

| | |
|---|---|
| Software and internally generated assets | 5 year straight line |
| Development costs, brand and technology | 4 year straight line |
| Broker relationships | 5 year profile |
| Bank licence | 3 year straight line |

The Group reviews the amortisation period on an annual basis. If the expected useful life of assets is different from previous assessments, the amortisation period is changed accordingly.

**n) Property, plant and equipment**

Property, plant and equipment comprise freehold land and buildings, major alterations to office premises, computer equipment and fixtures measured at cost less accumulated depreciation. These assets are reviewed for impairment annually, and if they are considered to be impaired, are written down immediately to their recoverable amounts.

Items of property, plant and equipment are depreciated on a straight-line basis over their estimated useful economic lives as follows:

| | |
|---|---|
| Buildings | 50 years |
| Leasehold improvements | 10 years |
| Equipment and fixtures | 5 years |

Land, deemed to be 25% of purchase price of buildings, is not depreciated.

**1. Accounting policies** (continued)

The cost of repairs and renewals is charged to profit or loss in the period in which the expenditure is incurred.

**o) Investment in subsidiaries**

In the Company's financial statements, investments in subsidiary undertakings are stated at cost less provision for any impairment. A full list of the Company's subsidiaries which are included in the Group's consolidated financial statements can be found in note 31.

The Company performs an annual impairment assessment of its investment in subsidiary undertakings, assessing the carrying value of the investment in each subsidiary against the subsidiaries' net asset values at the reporting date for indication of impairment. Where there is indication of impairment, the Company estimates the subsidiaries value in use by estimating future profitability and the impact on the net assets of the subsidiary. The Company recognises an impairment directly in profit or loss when the recoverable amount, which is the greater of the value in use or the fair value less costs to sell, is less than the carrying value of the investment. Impairments are subsequently reversed if the recoverable amount exceeds the carrying value.

**p) Financial instruments**

**i. Classification**

The Group classifies financial instruments based on the business model and the contractual cash flow characteristics of the financial instruments. Under IFRS 9, the Group classifies financial assets into one of three measurement categories:

- **Amortised cost** – assets in a business model to hold financial assets in order to collect contractual cash flows, where the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.
- **Fair value through other comprehensive income (FVOCI)** – assets held in a business model which collects contractual cash flows and sells financial assets where the contractual terms of the financial assets give rise on specified dates to cash flows that are SPPI on the principal amount outstanding.
- **Fair value through profit or loss (FVTPL)** – assets not measured at amortised cost or FVOCI. The Group measures derivatives and an acquired mortgage portfolio under this category.

The Group classifies non-derivative financial liabilities as measured at amortised cost.

The Group has no financial assets and liabilities classified as held for trading.

The Group reassesses its business models each reporting period.

The Group classifies certain financial instruments as equity where they meet the following conditions:

- the financial instrument includes no contractual obligation to deliver cash or another financial asset on potentially unfavourable conditions;
- the financial instrument is a non-derivative that includes no contractual obligation for the issuer to deliver a variable number of its own equity instruments; or
- the financial instrument is a derivative that will be settled only by the issuer exchanging a fixed amount of cash or another financial asset for a fixed number of its own equity instruments.

Equity financial instruments comprise own shares and AT1 securities. Accordingly, the coupon paid on the AT1 securities is recognised directly in retained earnings when paid.

1. **Accounting policies** (continued)

### ii. Recognition

The Group initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated or acquired. All other financial instruments are accounted for on the trade date which is when the Group becomes a party to the contractual provisions of the instrument.

For financial instruments classified as amortised cost, the Group initially recognises financial assets and financial liabilities at fair value plus transaction income or costs that are directly attributable to its origination, acquisition or issue. These financial instruments are subsequently measured at amortised cost using the effective interest rate.

Transaction costs relating to the acquisition or issue of a financial instrument at FVOCI and FVTPL are recognised in the profit or loss as incurred.

### iii. Derecognition

The Group derecognises financial assets when the contractual rights to the cash flows expire or the Group transfers substantially all risks and rewards of ownership of the financial asset. In assessing the Group's retention programmes the principles of IFRS 9 and relevant guidance in IAS 8 in respect of debt issuance, results in the original mortgage asset being derecognised with a new financial asset recognised.

The forbearance measures offered by the Group are considered a modification event as the contractual cash flows are renegotiated or otherwise modified. The Group considers the renegotiated or modified cash flows are not wholly different from the contractual cash flows and does not consider that forbearance measures give rise to a derecognition event.

Financial liabilities are derecognised only when the obligation is discharged, cancelled or has expired.

### iv. Offsetting

Financial assets and financial liabilities are offset and the net amount presented in the Consolidated Statement of Financial Position when, and only when, the Group currently has a legally enforceable right to offset the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

The Group's derivatives are covered by industry standard master netting agreements. Master netting agreements create a right of set-off that becomes enforceable only following a specified event of default or in other circumstances not expected to arise in the normal course of business. These arrangements do not qualify for offsetting and as such the Group reports derivatives on a gross basis.

Collateral in respect of derivatives is subject to the standard industry terms of International Swaps and Derivatives Association (ISDA) Credit Support Annex. This means that the cash received or given as collateral can be pledged or used during the term of the transaction but must be returned on maturity of the transaction. The terms also give each counterparty the right to terminate the related transactions upon the counterparty's failure to post collateral. Collateral paid or received does not qualify for offsetting and is recognised in loans and advances to credit institutions and amounts owed to credit institutions respectively.

1. **Accounting policies** (continued)

### v. Amortised cost measurement

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, plus or minus the cumulative amortisation using the EIR method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

### vi. Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Group has access at that date.

When available, the Group 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 for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. The Group measures the fair value of its investment securities and Perpetual Subordinated Bonds (PSBs) using quoted market prices.

If there is no quoted price in an active market, then the Group uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs.

The Group uses a combination of LIBOR and SONIA curves to value its derivatives however, using overnight index swap (OIS) curves would not materially change their value. The fair value of the Group's derivative financial instruments incorporates credit valuation adjustments (CVA) and debit valuation adjustments (DVA). The DVA and CVA take into account the respective credit ratings of the Bank and counterparty and whether the derivative is collateralised or not. Derivatives are valued using discounted cash flow models and observable market data and will be sensitive to benchmark interest and basis rate curves.

### vii. Identification and measurement of impairment of financial assets

The Group assesses all financial assets for impairment.

**Loans and advances to customers**

The Group uses the IFRS 9 three-stage expected credit loss (ECL) approach for measuring impairment. The three impairment stages are as follows:

- **Stage 1** – a 12-month ECL allowance is recognised where there is no significant increase in credit risk (SICR) since initial recognition.
- **Stage 2** – a lifetime loss allowance is held for assets where a SICR is identified since initial recognition. The assessment of whether credit risk has increased significantly since initial recognition is performed for each reporting period for the life of the loan.
- **Stage 3** – requires objective evidence that an asset is credit impaired, at which point a lifetime ECL allowance is recognised.

The Group measures impairment through the use of individual and modelled assessments.

**1. Accounting policies** (continued)

**Individual assessment**

The Group's provisioning process requires individual assessment for high exposure or higher risk loans, where Law of Property Act (LPA) receivers have been appointed, the property is taken into possession or there are other events that suggest a high probability of credit loss. Loans are considered at a connection level, i.e. including all loans connected to the customer.

The Group estimates cash flows from these loans, including expected interest and principal payments, rental or sale proceeds, selling and other costs. The Group obtains up-to-date independent valuations for properties put up for sale.

If the present value of estimated future cash flows discounted at the original EIR is less than the carrying value of the loan, a provision is recognised for the difference. Such loans are classified as impaired. If the present value of the estimated future cash flows exceeds the carrying value, no provision is recognised.

The Group applies a modelled assessment to all loans with no individually-assessed provision.

**IFRS 9 modelled impairment**

**Measurement of ECL**

The assessment of credit risk and the estimation of ECL are unbiased and probability weighted. ECL is measured on either a 12 month (stage 1) or lifetime basis depending on whether a SICR has occurred since initial recognition (stage 2) or where an account meets the Group's definition of default (stage 3).

The ECL calculation is a product of an individual loan's probability of default (PD), exposure at default (EAD) and loss given default (LGD) discounted at the EIR. The ECL drivers of PD, EAD and LGD are modelled at an account level. The assessment of whether a significant increase in credit risk has occurred is based on quantitative relative PD thresholds and a suite of qualitative triggers.

In accordance with PRA COVID-19 guidance, the Group does not automatically consider the take up of customer payment deferrals during the pandemic to be an indication of a SICR and, in the absence of other indicators such as previous arrears, low credit score or high other indebtedness, the staging of these loans remains unchanged in its ECL calculations.

**Significant increase in credit risk (movement to stage 2)**

The Group's transfer criteria determine what constitutes a SICR, which results in an exposure being moved from stage 1 to stage 2.

At the point of initial recognition, a loan is assigned a PD estimate. For each monthly reporting date thereafter, an updated PD estimate is computed. The Group's transfer criteria analyses relative changes in PD versus the PD assigned at the point of origination, together with qualitative triggers using both internal indicators and external credit bureau information to assess for SICR. In the event that given early warning triggers have not already identified SICR, an account more than 30 days past due has experienced a SICR.

A borrower will move back into stage 1 only if the SICR definition is no longer triggered.

**1. Accounting policies** (continued)

**Definition of default (movement to stage 3)**

The Group uses a number of quantitative and qualitative criteria to determine whether an account meets the definition of default and therefore moves to stage 3. The criteria currently include:

- If an account is more than 90 days past due.
- Accounts that have moved into an unlikely to pay position, which includes forbearance, bankruptcy, repossession and interest-only term expiry.

A borrower will move out of stage 3 when its credit risk improves such that it no longer meets the 90 days past due and unlikeliness to pay criteria and following this has completed an internally-approved probation period. The borrower will move to stage 1 or stage 2 dependent on whether the SICR applies.

**Forward-looking macroeconomic scenarios**

The risk of default and expected credit loss assessments take into consideration expectations of economic changes that are deemed to be reasonably possible.

The Group conducts analysis to determine the most significant factors which may influence the likelihood of an exposure defaulting in the future. The macroeconomic factors relate to the House Price Index (HPI), unemployment rate (UR), Gross domestic product (GDP), Commercial Real Estate Index (CRE) and the BoE Base Rate (BBR).

The Group has derived an approach for factoring probability-weighted macroeconomic forecasts into ECL calculations, adjusting PD and LGD estimates. The macroeconomic scenarios feed directly into the ECL calculation, as the adjusted PD, lifetime PD and LGD estimates are used within the individual account ECL allowance calculations.

The Group currently does not have an in-house economics function and therefore sources economic forecasts from an appropriately qualified third party. The Group considers four probability-weighted scenarios, base, upside, downside and severe downside scenarios.

The base case is also utilised within the Group's impairment forecasting process which in turn feeds the wider business planning processes. The ECL models are also used to set the Group's credit risk appetite thresholds and limits.

**Period over which ECL is measured**

Expected credit loss is measured from the initial recognition of the asset which is the date at which the loan is originated or the date a loan is purchased and at each balance sheet date thereafter. The maximum period considered when measuring ECL (either 12 months or lifetime ECL) is the maximum contractual period over which the Group is exposed to the credit risk of the asset. For modelling purposes, the Group considers the contractual maturity of the loan product and then considers the behavioural trends of the asset.

**Purchased or originated credit impaired (POCI)**

Acquired loans that meet the Group's definition of default (90 days past due or an unlikeliness to pay position) at acquisition are treated as a POCI asset. These assets attract a lifetime ECL allowance over the full term of the loan, even when the loan no longer meets the definition of default post acquisition. The Group does not originate credit-impaired loans.

**1. Accounting policies** (continued)

**Intercompany loans**

Intercompany receivables in the Company financial statements are assessed for ECL based on an assessment of the PD and LGD, discounted to a net present value.

**Other financial assets**

Other financial assets comprise cash balances with the BoE and other credit institutions and high grade investment securities. The Group deems the likelihood of default across these counterparties as low and, hence does not recognise a provision against the carrying balances.

**q) Loans and receivables**

Loans and receivables are predominantly mortgage loans and advances to customers with fixed or determinable payments that are not quoted in an active market and that the Group does not intend to sell in the near term. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the EIR method, less impairment losses. Where exposures are hedged by derivatives, designated and qualifying as fair value hedges, the fair value adjustment for the hedged risk to the carrying value of the hedged loans and advances is reported in fair value adjustments for hedged assets.

Loans and the related provision are written off when the underlying security is sold. Subsequent recoveries of amounts previously written off are taken through profit or loss.

Loans and advances over which the Group transfers its rights to the collateral thereon to the BoE under the TFS, TFSME and Indexed Long-Term Repo (ILTR) schemes are not derecognised from the Statement of Financial Position, as the Group retains substantially all the risks and rewards of ownership, including all cash flows arising from the loans and advances and exposure to credit risk. The Group classifies TFS, TFSME and ILTR as amortised cost under IFRS 9 Financial Instruments.

Loans and advances include a small acquired mortgage portfolio where the contractual cash flows include payments that are not solely payments of principal and interest and as such are measured at fair value through profit or loss. The Group initially recognises these loans at fair value, with direct and incremental costs of acquisition recognised directly in profit or loss and, subsequently measures them at fair value.

Loans and receivables contain the Group's asset finance lease lending. Finance leases are initially measured at an amount equal to the net investment in the lease, using the interest rate implicit in the finance lease. Direct costs are included in the initial measurement of the net investment in the lease and reduce the amount of income recognised over the lease term. Finance income is recognised over the lease term, based on a pattern reflecting a constant periodic rate of return on the net investment in the lease.

**r) Investment securities**

Investment securities comprise securities held for liquidity purposes (UK treasury bills and Residential Mortgage-Backed Securities (RMBS)). These assets are non-derivatives that are designated as FVOCI or classified as amortised cost.

Assets classified as amortised cost are originally recognised at fair value and subsequently measured at amortised cost using the EIR method, less impairment losses.

**1. Accounting policies** (continued)

Assets held at FVOCI are measured at fair value with movements taken to other comprehensive income and accumulated in the FVOCI reserve within equity, except for impairment losses which are taken to profit or loss. When the instrument is sold, the gain or loss accumulated in equity is reclassified to profit or loss.

**s) Deposits, debt securities in issue and subordinated liabilities**

Deposits, debt securities in issue and subordinated liabilities are the Group's sources of debt funding. They comprise deposits from retail customers and credit institutions, including collateralised loan advances from the BoE under the TFS, TFSME and ILTR, asset-backed loan notes issued through the Group's securitisation programmes and subordinated liabilities. Subordinated liabilities include the Sterling PSBs where the terms allow no absolute discretion over the payment of interest. These financial liabilities are initially measured at fair value less direct transaction costs, and subsequently held at amortised cost using the EIR method.

Cash received under the TFS, TFSME and ILTR is recorded in amounts owed to credit institutions. Interest is accrued over the life of the agreements on an EIR basis.

**t) Sale and repurchase agreements**

Financial assets sold subject to repurchase agreements (repo) are retained in the financial statements if they fail derecognition criteria of IFRS 9 described in paragraph p(iii) above. The financial assets that are retained in the financial statements are reflected as loans and advances to customers or investment securities and the counterparty liability is included in amounts owed to credit institutions or other customers. Financial assets purchased under agreements to resell at a predetermined price where the transaction is financing in nature (reverse repo) are accounted for as loans and advances to credit institutions. The difference between the sale and repurchase price is treated as interest and accrued over the life of the agreement using the EIR method.

**u) Derivative financial instruments**

The Group uses derivative financial instruments (interest rate swaps and basis swaps) to manage its exposure to interest rate risk. In accordance with its Treasury Policy, the Group does not hold or issue derivative financial instruments for proprietary trading.

Derivative financial instruments are recognised at their fair value with changes in their fair value taken to profit or loss. Fair values are calculated by discounting cash flows at the prevailing interest rates. All derivatives are classified as assets when their fair value is positive and as liabilities when their fair value is negative. If a derivative is cancelled, it is derecognised from the Statement of Financial Position.

The Group also uses derivatives to hedge the interest rate risk inherent in irrevocable offers to lend. This exposes the Group to movements in the fair value of derivatives until the loan is drawn. The changes to fair value are recognised in profit or loss in the period.

The Group is party to a limited number of options and warrants. These are recognised as a derivative financial instruments as applicable where a trigger event takes place and the fair value of the option or warrant can be reliably measured.

**v) Hedge accounting**

The Group has chosen to continue to apply the hedge accounting requirements of IAS 39 instead of the requirements in Chapter 6 of IFRS 9. The Group uses fair value hedge accounting for a portfolio hedge of interest rate risk.

**1. Accounting policies** (continued)

Portfolio hedge accounting allows for hedge effectiveness testing and accounting over an entire portfolio of financial assets or liabilities. To qualify for hedge accounting at inception, the hedge relationship is clearly documented and the derivative must be expected to be highly effective in offsetting the hedged risk. In addition, effectiveness must be tested throughout the life of the hedge relationship.

The Group applies fair value portfolio hedge accounting to its fixed rate portfolio of mortgages and saving accounts. The hedged portfolio is analysed into repricing time periods based on expected repricing dates, utilising the Group Assets and Liabilities Committee (ALCO) approved prepayment curve. Interest rate swaps are designated against the repricing time periods to establish the hedge relationship. Hedge effectiveness is calculated as a percentage of the fair value movement of the interest rate swap against the fair value movement of the hedged item over the period tested.

The Group considers the following as key sources of hedge ineffectiveness:

- the mismatch in maturity date of the swap and hedged item, as swaps with a given maturity date cover a portfolio of hedged items which may mature throughout the month;
- the actual behaviour of the hedged item differing from expectations, such as early repayments or withdrawals and arrears;
- minimal movements in the yield curve leading to ineffectiveness where hedge relationships are sensitive to small value changes; and
- the transition relating to LIBOR reforms whereby some hedged instruments and hedged items are based on different benchmark rates.

Where there is an effective hedge relationship for fair value hedges, the Group recognises the change in fair value of each hedged item in profit or loss with the cumulative movement in their value being shown separately in the Statement of Financial Position as fair value adjustments on hedged assets and liabilities. The fair value changes of both the derivative and the hedge substantially offset each other to reduce profit volatility.

The Group discontinues hedge accounting when the derivative ceases through expiry, when the derivative is cancelled or the underlying hedged item matures, is sold or is repaid.

If a derivative no longer meets the criteria for hedge accounting or is cancelled whilst still effective, the fair value adjustment relating to the hedged assets or liabilities within the hedge relationship prior to the derivative becoming ineffective or being cancelled remains on the Statement of Financial Position and is amortised over the remaining life of the hedged assets or liabilities. The rate of amortisation over the remaining life is in line with expected income or cost generated from the hedged assets or liabilities. Each reporting period, the expectation is compared to actual with an accelerated run-off applied where the two diverge by more than set parameters.

**w) Debit and credit valuation adjustments**

The DVA and CVA are included in the fair value of derivative financial instruments. The DVA is based on the expected loss a counterparty faces due to the risk of the Group's default. The CVA reflects the Group's risk of the counterparty's default.

The methodology is based on a standard calculation, taking into account:

- the one-year PD, updated on a regular basis;
- the expected exposure at default;
- the expected LGD; and
- the average maturity of the swaps.

**1. Accounting policies** (continued)

**x) Provisions and contingent liabilities**

A provision is recognised when there is a present obligation as a result of a past event, it is probable that the obligation will be settled and the amount can be estimated reliably.

Provisions include ECLs on the Group's undrawn loan commitments.

Contingent liabilities are possible obligations arising from past events, whose existence will be confirmed only by uncertain future events, or present obligations arising from past events which are either not probable or the amount of the obligation cannot be reliably measured. Contingent liabilities are not recognised but disclosed unless they are not material or their probability is remote.

**y) Employee benefits – defined contribution scheme**

The Group contributes to defined contribution personal pension plans or defined contribution retirement benefit schemes for all qualifying employees who subscribe to the terms and conditions of the schemes' policies.

Obligations for contributions to defined contribution pension arrangements are recognised as an expense in profit or loss as incurred.

**z) Share-based payments**

Equity-settled share-based payments to employees providing services are measured at the fair value of the equity instruments at the grant date in accordance with IFRS 2. The fair value excludes the effect of non-market-based vesting conditions.

The cost of the awards are charged on a straight-line basis to profit or loss (with a corresponding increase in the share-based payment reserve within equity) over the vesting period in which the employees become unconditionally entitled to the awards. The cumulative expense within the share-based payment reserve is reclassified to retained earnings upon exercise.

The amount recognised as an expense for non-market conditions and related service conditions is adjusted each reporting period to reflect the actual number of awards expected to be met. The amount recognised as an expense for awards subject to market conditions is based on the proportion that is expected to meet the condition as assessed at the grant date. No adjustment is made to the fair value of each award calculated at grant date.

Share-based payments that are not subject to further vesting conditions (i.e. the Deferred Share Bonus Plan (DSBP) for senior managers) are expensed in the year services are received with a corresponding increase in equity. Awards granted to Executive Directors in March 2020 are subject to service conditions through to vesting and are expensed over the vesting period. Awards granted to Executive Directors in April 2021 are not subject to future service conditions and are expensed in 2020 where the service is deemed to have been provided.

Where the allowable cost of share-based options or awards for tax purposes is greater than the cost determined in accordance with IFRS 2, the tax effect of the excess is taken to the share-based payment reserve within equity. The tax effect is reclassified to retained earnings upon vesting.

Employer's national insurance is charged to profit or loss at the share price at the reporting date on the same service or vesting schedules as the underlying options and awards.

1. **Accounting policies** (continued)

Following the insertion of OSBG, the Group ceased consolidating the EBT and no longer recognises own shares. In 2019, own shares were recorded at cost and deducted from equity and represented shares of OSB that were held by the Employee Benefit Trust.

**aa) Leases**

The Group recognises right-of-use assets and lease liabilities for leases over 12 months long. Right-of-use assets and lease liabilities are initially recognised at the net present value of future lease payments, discounted at the rate implicit in the lease or, where not available, the Group's incremental borrowing cost. Subsequent to initial recognition, the right-of-use asset is depreciated on a straight-line basis over the term of the lease. Future rental payments are deducted from the lease liability, with interest charged on the lease liability using the incremental borrowing cost at the time of initial recognition. The Group recognises lease liability payments within financing activities in the Consolidated Statement of Cash Flows.

The Group assesses the likely impact of early terminations in recognising the right-of-use asset and lease liability where an option to terminate early exists.

Leases with low future payments or terms less than 12 months are recognised on an accruals basis directly in profit or loss.

**bb) Adoption of new standards**

**International financial reporting standards issued and adopted for the first time in the year ended 31 December 2020**

The following financial reporting standard amendments and interpretations were in issue and have been applied in the financial statements from 1 January 2020.

- Amendments to the Conceptual Framework for Financial reporting, including amendments to references to the Conceptual Framework in IFRS Standards.
- Amendments to IFRS 3 – Definition of a business.
- Amendments to IAS 1 and IAS 8 – Definition of material.

There has been no material impact on the financial statements of the Group from the adoption of these financial reporting standard amendments and interpretations.

**International financial reporting standards issued but not yet adopted which are applicable to the Group**

The following financial reporting standards were in issue but have not been applied in the financial statements, as they were yet effective on 31 December 2020.

Effective for accounting periods beginning on or after 1 June 2020:

- Amendments to IFRS 16 – COVID-19 related rent concessions

Effective for accounting periods beginning on or after 1 January 2021:

- Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 Interest Rate Benchmark Reform – Phase 2
- Amendments to IAS 1 – Classification of liabilities as current or non-current.

1. **Accounting policies** (continued)

- Annual improvements to IFRS Standards 2018-2020 – Minor amendments to IFRS 1, IFRS 9 and IFRS 16.

The Group does not expect that the adoption of the financial reporting standards listed above will have a material impact on the financial statements of the Group in future periods.

## 2. Judgements in applying accounting policies and critical accounting estimates

In preparing these financial statements, the Group has made judgements, estimates and assumptions which affect the reported amounts within the current and next financial year. Actual results may differ from these estimates.

Estimates and judgements are regularly reviewed based on past experience, expectations of future events and other factors.

**Judgements**
The Group has made the following key judgements in applying the accounting policies:

**(i) Loan book impairments**

**Significant increase in credit risk for classification in stage 2**
The Group's Significant Increase in Credit Risk (SICR) rules, prior to the COVID-19 pandemic, considered changes in default risk, internal impairment measures, changes in customer credit bureau files, or whether forbearance measures had been applied. The Group took steps to adjust the SICR criteria through the pandemic to account for the changes in risk profile and specifically for payment deferrals granted, noting that not all of the instances of a payment deferral would be a significant increase in credit risk. Payment deferrals granted due to COVID-19 alone were not automatically considered as a SICR event in line with issued guidance, and adjustments to the rules were as follows:

- Payment deferrals considered as a SICR event where other significant high risk factors are identified on customer's credit files;
- Payment deferrals considered as a SICR event where an account also had recent arrears; and
- Customers with stress to their income considered as a SICR event.

**(ii) IFRS 9 classification**
The Group has applied judgement in determining whether the contractual terms of a financial asset give rise on specified dates to cash flows that are solely payments of principal or interest (SPPI) on the principal amount outstanding when applying the classification criteria of IFRS 9. The main area of judgement is over the Group's loans and advances to customers which have been accounted for under amortised cost with the exception of one acquired mortgage book of £19.1m (2019: £22.1m) that is recognised at FVTPL.

**Estimates**
The Group has made the following estimates in the application of the accounting policies that have a significant risk of material adjustment to the carrying amount of assets and liabilities within the next financial year:

**(i) Loan book impairments**
Set out below are details of the critical accounting estimates which underpin loan impairment calculations. Less significant estimates are not discussed as they do not have a material effect. The Group has recognised total impairments of £111.0m (2019: £42.9m) at the reporting date as disclosed in note 22.

## 2. Judgements in applying accounting policies and critical accounting estimates (continued)

**Modelled impairment**
Modelled provision assessments are also subject to estimation uncertainty, underpinned by a number of estimates being made by management which are utilised within impairment calculations. Key areas of estimation within modelled provisioning calculations include those regarding the PD, the LGD and forward-looking macroeconomic scenarios.

**Loss given default model**
The Group has a number of LGD models, which include a number of estimated inputs including propensity to go to possession given default (PPD), forced sale discount (FSD), time to sale (TTS) and sale cost estimates. The LGD is sensitive to the application of the HPI. For the OSB segment at 31 December 2020 a 10% fall in house prices would result in an incremental £25.6m (2019: £13.6m) of provision being required. For the CCFS segment at 31 December 2020 a 10% fall in house prices would result in an incremental £13.9m (2019: £3.8m) of provision being required. The combined impact across both OSB and CCFS businesses of a 10% fall in house prices would result in an increase in total provisions of £39.5m (2019: £17.4m) as at 31 December 2020.

**Forward-looking macroeconomic scenarios**
The forward-looking macroeconomic scenarios affect both the PD and LGD estimates. Therefore the expected credit losses calculations are sensitive to both the scenarios utilised and their associated probability weightings.

The Group sources economic forecasts from an appropriately qualified, independent third party. The Group considers four probability-weighted scenarios: base, upside, downside and severe downside scenarios. Due to the current uncertainty in relation to the ongoing COVID-19 global pandemic and the recently agreed Brexit trade agreement the choice of scenarios and weightings are subject to a significant degree of estimation. The Group's macroeconomic scenarios can be found in the Strategic Report on page 3.

The following tables detail the ECL scenario sensitivity analysis with each scenario weighted at 100% probability. The purpose of using multiple economic scenarios is to model the non-linear impact of assumptions surrounding macroeconomic factors and ECL calculated:

| **As at 31-Dec-20** | **Weighted** | **100% Base case scenario** | **100% Upside scenario** | **100% Downside scenario** | **100% Severe downside scenario** |
|---|---|---|---|---|---|
| Total loans before provisions, £m | **19,322.6** | **19,322.6** | **19,322.6** | **19,322.6** | **19,322.6** |
| Modelled ECL, £m | **71.6** | **54.6** | **40.1** | **113.5** | **166.7** |
| Non-modelled ECL, £m | **39.4** | **39.4** | **39.4** | **39.4** | **39.4** |
| Total ECL, £m | **111.0** | **94.0** | **79.5** | **152.9** | **206.1** |
| ECL Coverage, % | **0.57** | **0.49** | **0.41** | **0.79** | **1.07** |

| As at 31-Dec-19 | | | | | |
|---|---|---|---|---|---|
| Total loans before provisions, £m | 18,467.6 | 18,467.6 | 18,467.6 | 18,467.6 | 18,467.6 |
| Modelled ECL, £m | 37.4 | 24.4 | 14.6 | 48.1 | 62.5 |
| Non-modelled ECL, £m | 5.5 | 5.5 | 5.5 | 5.5 | 5.5 |
| Total ECL, £m | 42.9 | 29.9 | 20.1 | 53.6 | 68.0 |
| ECL Coverage, % | 0.23 | 0.16 | 0.11 | 0.29 | 0.37 |

**2. Judgements in applying accounting policies and critical accounting estimates** (continued)

**(ii) Loan book acquisition accounting and income recognition**
Acquired loan books are initially recognised at fair value. Significant estimation is required in calculating their EIR using cash flow models which include assumptions on the likely macroeconomic environment, including HPI, unemployment levels and interest rates, as well as loan level and portfolio attributes and history used to derive prepayment rates and the amount of incurred losses.

Through the Combination in 2019, the Precise Mortgages book is treated as an acquired book with a fair value uplift to book value, at the point of initial recognition, of £301.0m, reflecting a premium applied to the book. Fair value sensitivities have been completed on the Precise Mortgages book, including the market rate applied to the discounted cash flows, being one month LIBOR plus a margin (margin blended average used 2.91%). Where the margin applied is increased/decreased by 25bps the initial premium recognised on the book increases/decreases by £66.0m/£67.0m.

The EIR on loan books purchased at significant discounts or premiums is particularly sensitive to the weighted average life of the loan book through the constant prepayment rate (CPR) and the constant default rate (CDR) estimates assumed, as the purchase discount or premium is recognised over the expected life of the loan book through the EIR. New defaults are modelled at zero loss (as losses will be recognised in profit or loss as impairment losses) and therefore have the same impact on the EIR as prepayments.

Incurred losses at acquisition are calculated using the Group's modelled provision assessment (see (i) Loan book impairments above for further details).

The EIR calculated at acquisition is not changed for subsequent variances in actual to expected cash flows, unless the variance is due to changes in expectations of market rates of interest. The Group monitors the actual cash flows for each acquired book, and where they diverge significantly from expectation, the revised future cash flows are discounted at the original EIR, with any resulting change in carry value creating a corresponding gain or loss in the Statement of Comprehensive Income as Interest Income. In assessing whether to adjust future cash flows on an acquired portfolio, the Group considers the cash variance on an absolute and percentage basis. The Group also considers the total variance across all acquired portfolios and the economic outlook. The Group recognised a £3.5m loss in 2020 as a result of resetting cash flows on acquired books (2019: gain of £0.5m). The largest acquired book is Precise with sensitivities completed on increasing/reducing the life of the book by six months which results in a reset gain/loss of c. £33m/£37m (2019: c.£48m/£50m).

**(iii) Effective interest rate on organic lending**
Estimates are made when calculating the EIR for newly-originated loan assets. These include the likely customer redemption profiles.

Mortgage products offered by the Group include directly attributable net fee income and a period on reversion rates after the fixed/discount period. Products revert to the standard variable rate (SVR) or Base plus a margin for the Kent Reliance brand or a LIBOR/Base plus a margin for the Precise brand. The Group uses historical customer behaviours, expected take-up rate of retention products and macroeconomic forecasts in its assessment of prepayment rates. Customer prepayments in a fixed rate or incentive period can give rise to Early Repayment Charge (ERC) income.

Estimation is used in assessing whether and for how long mortgages that reach the end of the initial product term stay on reversion rates, and to the quantum and timing of prepayments that incur ERCs. The estimate of customer weighted average life will determine the period over which net fee income and expected reversionary income is recognised.

### 2. Judgements in applying accounting policies and critical accounting estimates (continued)

Sensitivities have been applied to the Precise and Kent Reliance loan books, to illustrate the impact on interest income of a change in the expected weighted average lives of the loan books. An extension of the expected life will typically result in increased expectations of post reversionary income, less ERCs and a recognition of net fee income over a longer period. A shortening of the expected life will lead to reduced post reversionary income, more ERCs and a recognition of net fees over a shorter period.

The potential duration of a change in customer behaviour as a result of COVID-19 remains uncertain. However, a period of six months' variance in the weighted average lives of the loan books was selected for this sensitivity, given the initial quick recovery in the property and mortgage markets post national lockdown experienced in 2020. This recovery was due, in part, to government stimulus in the form of a temporary reduction in stamp duty and the provision of cheaper funding to banks, in the form of the Bank of England's Term Funding Scheme for SMEs.

Applying a six month extension in the expected weighted average life of the organic loan books, would result in a gain of c. £22.6m (2019: £23.6m) recognised in Net Interest Income. It includes a c. £13.8m (2019: £19.5m) gain in relation to the Kent Reliance loan book, where the impact of the proactive Choices programme, which offers borrowers a new product as an alternative to paying the Bank's higher Standard Variable Rate (SVR), may significantly reduce the likelihood of borrowers extending the period of time paying SVR and reduce the amount of the potential reset gain.

Applying a six month reduction in the expected weighted average life of the loan books, would result in a reset loss of c. £6.9m (2019: £4.6m) recognised in Net Interest Income. This includes c. £2.0m (2019: £0.4m) gain in relation to the Kent Reliance loan book.

### 3. Interest receivable and similar income

| | **Group 2020 £m** | Group 2019 £m |
|---|---|---|
| **At amortised cost:** | | |
| On OSB mortgages | **500.6** | 480.5 |
| On CCFS mortgages | **331.9** | 80.2 |
| On investment securities | **2.5** | 0.6 |
| On other liquid assets | **5.3** | 12.2 |
| Amortisation of fair value adjustments on CCFS Combination[1] | **(67.8)** | (22.6) |
| Amortisation of fair value adjustments on hedged assets[2] | **(17.9)** | - |
| **At fair value through profit or loss:** | | |
| Net expense on derivative financial instruments - lending activities | **(47.7)** | (14.0) |
| On CCFS mortgages | **-** | 0.3 |
| **At FVOCI:** | | |
| On investment securities | **5.0** | 2.7 |
| | **711.9** | 539.9 |

[1] Amortisation of fair value adjustments on CCFS loan book at Combination.
[2] The amortisation relates to hedged assets where the hedges were terminated before maturity and were effective at the point of termination.

### 4. Interest payable and similar charges

| | **Group 2020 £m** | Group 2019 £m |
|---|---|---|
| On retail deposits | **245.5** | 177.3 |
| On BoE borrowings | **8.4** | 13.3 |
| On perpetual subordinated bonds | **1.7** | 1.8 |
| On subordinated liabilities | **0.8** | 0.7 |
| On wholesale borrowings | **1.3** | 1.9 |
| On debt securities in issue | **3.4** | 3.7 |
| On lease liabilities | **0.3** | 0.1 |
| Amortisation of fair value adjustments on CCFS Combination[1] | **(3.3)** | (1.0) |
| Net income on derivative financial instruments - savings activities | **(18.4)** | (2.6) |
| | **239.7** | 195.2 |

[1] Amortisation of fair value adjustments on CCFS customer deposits at Combination.

### 5. Fair value gains/(losses) on financial instruments

| | **Group 2020 £m** | Group 2019 £m |
|---|---|---|
| Fair value changes in hedged assets | **107.3** | 70.1 |
| Hedging of assets | **(116.8)** | (75.1) |
| Fair value changes in hedged liabilities | **(4.1)** | (4.6) |
| Hedging of liabilities | **6.8** | 4.8 |
| Ineffective portion of hedges | **(6.8)** | (4.8) |
| Net (losses)/gains on unmatched swaps | **(18.0)** | 3.5 |
| Amortisation of inception adjustments | **13.0** | - |
| Amortisation of acquisition related inception adjustments | **17.0** | 3.3 |
| Amortisation of de-designated hedge relationships | **2.4** | - |
| Fair value movements on mortgages at FVTPL | **(0.2)** | - |
| Amortisation of fair value adjustments on hedged assets | **-** | (5.5) |
| Debit and credit valuation adjustment | **-** | 0.2 |
| | **7.4** | (3.3) |

Amortisation of inception adjustments relates in part to hedged assets and liabilities recognised on the Combination where pre-existing hedge relationships ceased on the date of Combination. The inception adjustment is being amortised over the life of the derivative instruments acquired on Combination and recognises an offsetting asset or liability to the fair value of the derivative instruments on the date of Combination. The remainder of the amortisation of inception adjustment relates to the amortisation of the hedging adjustments arising when hedge accounting commences, primarily on derivative instruments previously taken out against the mortgage pipeline and also on derivative instruments previously taken out against new retail deposits.

### 6. Gain/(loss) on sales of financial instruments

On 17 January 2020, the Group sold the Canterbury A2 note for proceeds of £225.4m. After incurring costs of £0.2m, a gain on sale of £1.9m was recognised.

On 23 January 2020, the Group sold the F note and residual certificates of the Canterbury securitisation for proceeds of £23.6m. Following the sale the Group had no remaining interest in the Canterbury securitisation. As a result, consolidation of Canterbury into the Group ceased on disposal. The Group recognised a gain on sale of £16.0m upon deconsolidation.

On 23 January 2020, the Group securitised £375.5m of mortgage loans through Precise Mortgage Funding 2020-1B plc (PMF 2020-1B), issuing £388.9m of Sterling floating rate notes. The Group retained the class A2 notes, with all other note classes and the residual certificates being sold to the external market. As such, the Group has not consolidated PMF 2020-1B as substantially all of the risks and rewards have been transferred. The Group recognised a gain on sale of £2.0m on disposal. Excluding the impact of the fair value adjustment on the mortgages on Combination with OSB of £13.1m, the underlying gain on sale was £15.1m.

On 14 September 2020, the Group sold £150.0m of Canterbury 3 A2 notes for £150.1m, resulting in a gain on sale of £0.1m.

In 2019, the Group identified an additional £0.1m of customer receipts due to the purchaser of the personal loan portfolio in the prior year, recognising an additional loss on sale of £0.1m.

### 7. Other operating income

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| Interest received on mortgages held at FVTPL[1] | 0.6 | - |
| Fees and commissions receivable | 8.4 | 3.4 |
| Other operating costs[2] | - | (1.3) |
| | 9.0 | 2.1 |

[1] In 2019, £0.3m interest received on mortgages held at FVTPL was included in interest receivable and similar income (see note 3).
[2] Other operating costs includes commission expense incurred on retail savings generated from the branch network which is included in administration expenses from 2020.

## 8. Administrative expenses

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| Staff costs | **86.0** | 60.5 |
| Facilities costs | **5.7** | 3.6 |
| Marketing costs | **5.1** | 4.0 |
| Support costs | **18.6** | 12.7 |
| Professional fees | **22.3** | 10.4 |
| Other costs[1] | **5.6** | 9.3 |
| Depreciation (see note 29) | **5.6** | 3.9 |
| Amortisation (see note 30) | **8.2** | 4.3 |
| | **157.1** | 108.7 |

[1] In 2019, other costs mainly comprised irrecoverable VAT. In 2020, the Group included irrecoverable VAT within the underlying expense.

Included in professional fees are amounts paid to the Company's auditor as follows:

| | Group 2020 £'000 | Group 2019 £'000 |
|---|---|---|
| Fees payable to the Company's auditor for the audit of the Company's annual accounts | **899** | 1,269 |
| Fees payable to the Company's auditor for the audit of the accounts of subsidiaries | **1,299** | 846 |
| Total audit fees | **2,198** | 2,115 |
| Audit-related assurance services[1] | **217** | 187 |
| Other assurance services[2] | **45** | 142 |
| Other non-audit services[3] | **101** | - |
| Total non-audit fees | **363** | 329 |
| **Total fees payable to the Group's Auditor** | **2,561** | 2,444 |

[1] Includes review of interim financial information and profit verifications
[2] 2020 costs comprise an assurance review of APMs, 2019 costs related to the Combination and agreed upon procedures in respect of securitisations
[3] Primarily comprises work related to the insertion of a new holding company.

Staff costs comprise the following:

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| Salaries, incentive pay and other benefits | **68.5** | 49.1 | **30.7** | 31.4 |
| Share-based payments | **5.1** | 4.0 | **4.9** | 4.0 |
| Social security costs | **8.1** | 4.4 | **4.5** | 3.4 |
| Other pension costs | **4.3** | 3.0 | **2.6** | 2.3 |
| | **86.0** | 60.5 | **42.7** | 41.1 |

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

### 8. Administrative expenses (continued)

The average number of people employed by the Group (including Executive Directors) during the year is analysed below. For 2019, the average for CCFS is based on the post Combination period.

| | Group 2020 | Group 2019 | Company 2020 | Company 2019 |
|---|---|---|---|---|
| **OSB** | | | | |
| Operations | **835** | 812 | **356** | 325 |
| Support functions | **297** | 286 | **180** | 204 |
| **CCFS** | | | | |
| Operations | **579** | 530 | **-** | - |
| Support functions | **105** | 161 | **-** | - |
| | **1,816** | 1,789 | **536** | 529 |

### 9. Impairment of intangible assets

Assets arising on the Combination with CCFS in 2019 included a broker relationships intangible asset with a fair value of £17.1m on Combination. A key input to the calculation of the fair value was CCFS anticipated lending volumes over three years post combination which have been revised due to COVID-19 impacts, with an impairment of £7.0m recognised. The remaining carrying value of the broker relationships intangible asset at 31 December 2020 is £5.7m (2019: £16.1m).

### 10. Directors' emoluments and transactions

| | Company 2020 £'000 | Company 2019 £'000 |
|---|---|---|
| Short-term employee benefits[1] | **2,675** | 2,334 |
| Post-employment benefits | **99** | 112 |
| Share-based payments[2] | **425** | 632 |
| | **3,199** | 3,078 |

[1] Short-term employee benefits comprise Directors' salary costs, Non-Executive Directors' fees and other short-term incentive benefits, which are disclosed in the OSB GROUP PLC Annual Report on Remuneration.
[2] Share-based payments represent the amounts received by Directors for schemes that vested during the year. Following the insertion of OSB GROUP PLC as the holding company on 27 November 2020, the share awards and options over OneSavings Bank plc shares were automatically transferred to OSB GROUP PLC shares.

In addition to the total Directors' emoluments above, the Executive Directors were granted deferred bonuses of £495k (2019: £511k) in the form of shares. The DSBP awards that will be granted in April 2021 will have a holding period of three years with no further conditions attached other than standard clawback situations. In March 2020 and prior, the DSBP awards were subject to either a three or five year vesting period with conditions attached, notably if the Director leaves prior to vesting, the award is forfeited unless a good leaver reason applies such as redundancy, retirement or ill health.

The Executive Directors received a further share award under the PSP with a grant date fair value of £1,359k (2019: £1,305k) using a share price of £2.58 (2019: £3.90) (the average mid-market quotation for the preceding five days before grant). These shares vest annually from year three in tranches of 20 per cent, subject to performance conditions discussed in note 11 and the OSB GROUP PLC Annual Report on Remuneration.

**10. Directors' emoluments and transactions** (continued)

Some Non-Executive Directors who left office during the year, received a payment equal to three months' fee in lieu of the unexpired period of notice, totalling £59k. There was no compensation for loss of office during 2019.

There were no outstanding loans granted in the ordinary course of business to Directors and their connected persons as at 31 December 2020 and 2019.

The highest paid Director employed by the Company received emoluments of £1,329k (2019: £1,315k) and payments in respect of personal pension plans of £59k (2019: £67k) in the year. This includes an estimated amount of £406k relating to PSP awards which are due to vest in May 2021.

The OSB GROUP PLC Annual Report on Remuneration and note 11 Share-based payments provide further details on Directors' emoluments.

**11. Share-based payments**

Following the insertion of OSB GROUP PLC as the holding company on 27 November 2020, the share awards and options over OneSavings Bank plc shares were automatically transferred to OSB GROUP PLC shares.

The Group operates the following share-based schemes:

**Sharesave Scheme**
The Save As You Earn (SAYE) or Sharesave Scheme is a share option scheme which is available to all UK-based employees. The Sharesave Scheme allows employees to purchase options by saving a fixed amount of between £5 and £500 per month over a period of either three or five years at the end of which the options, subject to leaver provisions, are usually exercisable. If not exercised, the amount saved is returned to the employee. The Sharesave Scheme has been in operation since 2014 and an invitation to join the scheme is usually extended annually, with the option price calculated using the mid-market price of an OSB GROUP PLC ordinary share over the three dealing days prior to the Invitation Date and applying a discount of 20%.

**Deferred Share Bonus Plan (DSBP)**
The DSBP applies to Executive Directors and certain senior managers with 50% of their performance bonuses to be deferred in shares for three years for Executive Directors and one or five years for senior managers. There are no further performance or vesting conditions attached to deferred awards for senior managers, which also applies to Executive Directors for awards granted from April 2021; the share awards are subject to clawback provisions. The DSBP awards are expensed in the year services are received with a corresponding increase in equity. Awards granted to Executive Directors in March 2020 and prior, are subject to vesting conditions and are expensed over the vesting period.

DSBP awards for senior managers carry entitlements to dividend equivalents, which are paid when the awards vest. DSBP awards granted from April 2021 to Executive Directors are entitled to dividend equivalents; awards granted in prior years were not entitled to dividend equivalents.

**Performance Share Plan (PSP)**
Executive Directors and certain senior managers are also eligible for a PSP award based on performance conditions and vest in tranches over three to seven years.

### 11. Share-based payments (continued)

The performance conditions that apply to PSP awards from 2020 are based on a combination of earnings per share (EPS) weighting of 35%, total shareholder return (TSR) 35%, risk-based 15% and return on equity (ROE) 15%. Prior to 2020, PSP awards were based on a combination of EPS weighting of 40%, TSR 40% and ROE 20%. The PSP conditions are assessed independently. For the EPS element, growth targets are linked to the Group's three-year growth plan, measuring growth from the base figure for the prior year. For the TSR element, the Group's ordinary shares relative performance is measured against the FTSE 250 (excluding investment trusts). The risk-based measure is assessed against the risk management performance with regard to all relevant risks including, but not limited to, an assessment of regulatory risk, operational risk, conduct risk, liquidity risk, funding risk, marketing risk and credit risk. For the ROE element, growth rates are assessed against OSB GROUP PLC's underlying profit after taxation as a percentage of average shareholders' equity.

As part of the Combination, the Group granted mirror PSP awards for the 2018 and 2019 CCFS schemes that terminated upon the Combination. The mirror PSP schemes follow the same performance conditions as the Group's 2018 and 2019 PSP awards.

The share-based expense for the year includes a charge in respect of the Sharesave Scheme, DSBP and PSP. All charges are included in employee expenses within note 8 Administrative expenses.

The share-based payment expense during the year comprised the following:

| | **Group 2020 £m** | Group 2019 £m |
|---|---|---|
| Sharesave Scheme | **0.5** | 0.2 |
| Deferred Share Bonus Plan | **3.9** | 1.3 |
| Performance Share Plan | **0.7** | 2.5 |
| | **5.1** | 4.0 |

Movements in the number of share awards and their weighted average exercise prices are presented below:

| | **Sharesave Scheme** | | **Deferred Share Bonus Plan** | **Performance Share Plan** |
|---|---|---|---|---|
| | **Number** | **Weighted average exercise price, £** | **Number** | **Number** |
| At 1 January 2020 | **2,869,146** | **2.63** | **738,473** | **3,096,371** |
| Granted | **1,483,202** | **2.29** | **839,735** | **2,756,176** |
| Exercised/Vested | **(1,080,430)** | **2.32** | **(449,608)** | **(383,205)** |
| Forfeited | **(526,586)** | **2.79** | **(8,843)** | **(482,815)** |
| **At 31 December 2020** | **2,745,332** | **2.53** | **1,119,757** | **4,986,527** |
| Exercisable: | | | | |
| **At 31 December 2020** | **118,402** | **2.89** | **-** | **-** |

### 11. Share-based payments (continued)

| | Sharesave Scheme | | Deferred Share Bonus Plan | Performance Share Plan |
|---|---|---|---|---|
| | Number | Weighted average exercise price, £ | Number | Number |
| At 1 January 2019 | 841,629 | 2.93 | 1,258,712 | 1,737,997 |
| Granted | 1,261,307 | 2.65 | 476,933 | 1,079,392 |
| CCFS mirror/roll over schemes | 1,183,475 | 2.42 | - | 931,853 |
| Exercised/Vested | (154,963) | 1.96 | (920,891) | (235,241) |
| Forfeited | (262,302) | 3.23 | (76,281) | (417,630) |
| **At 31 December 2019** | 2,869,146 | 2.63 | 738,473 | 3,096,371 |
| Exercisable: | | | | |
| **At 31 December 2019** | - | - | - | - |

For the share-based awards granted during the year, the weighted average grant date fair value was 188 pence (2019: 208 pence).

The range of exercise prices and weighted average remaining contractual life of outstanding awards are as follows:

| | 2020 | | 2019 | |
|---|---|---|---|---|
| **Exercise price** | Number | Weighted average remaining contractual life (years) | Number | Weighted average remaining contractual life (years) |
| **Sharesave Scheme** | | | | |
| 227-335 pence (2019: 134 - 335 pence) | 2,745,332 | 2.5 | 2,869,146 | 2.0 |
| **Deferred Share Bonus Plan** | | | | |
| Nil | 1,119,757 | 0.7 | 738,473 | 0.6 |
| **Performance Share Plan** | | | | |
| Nil | 4,986,527 | 2.5 | 3,096,371 | 1.7 |
| | 8,851,616 | 2.3 | 6,703,990 | 1.7 |

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

**11. Share-based payments** (continued)

**Sharesave Scheme**

| | **2020** | | 2019 | | 2018 | | 2017 | | 2016 | |
|---|---|---|---|---|---|---|---|---|---|---|
| Contractual life, years | **3** | **5** | 3 | 5 | 3 | 5 | 3 | 5 | 3 | 5 |
| Share price at issue, £ | **2.86** | **2.86** | 3.32 | 3.32 | 4.19 | 4.19 | 3.93 | 3.93 | 3.00 | 3.00 |
| Exercise price, £ | **2.29** | **2.29** | 2.65 | 2.65 | 3.35 | 3.35 | 3.15 | 3.15 | 2.40 | 2.40 |
| Expected volatility, % | **57.6** | **57.6** | 31.9 | 31.9 | 16.1 | 16.5 | 18.0 | 17.3 | 18.4 | 20.1 |
| Dividend yield, % | **3.3** | **3.3** | 4.8 | 4.8 | 4.4 | 4.4 | 4.1 | 4.1 | 4.6 | 4.6 |
| Grant date fair value, £ | **1.22** | **1.34** | 0.90 | 0.91 | 0.40 | 0.43 | 0.75 | 0.70 | 0.10 | 0.15 |

The share save schemes are not entitled to dividends between the option and exercise date. A Black Scholes model is used to determine the grant date fair value with two inputs:

- Expected volatility - from 2019, the expected volatility is based on OSBG's share price post insertion, and the OSB share price prior to insertion. Prior to this the Group used the FTSE 350 diversified financials volatility as insufficient history was available for the Company's share price.
- Dividend – based on the average dividend yield across external analyst reports for the quarter prior to scheme grant date.

**Deferred Share Bonus Plan**

| | **2020** | 2019 | 2018 | 2017 | |
|---|---|---|---|---|---|
| Contractual life, years | **3** | 3 | 3 | 3 | 5 |
| Mid-market share price, £ | **2.58** | 3.96 | 3.80 | 4.04 | 4.04 |
| Attrition rate, % | **-** | 8.4 | 9.7 | 11.8 | 11.8 |
| Dividend yield, % | **5.6** | 4.7 | 4.6 | 4.0 | 4.0 |
| Grant date fair value, £ | **2.21** | 3.47 | 3.34 | 3.61 | 3.37 |

For DSBP awards where conditions exists an attrition rate is applied as an estimate of the actual number of awards that will meet the related conditions at the vesting date. These schemes carry no rights to dividend equivalents and a Black Scholes model is used to determine the grant date fair value with a dividend yield input applied – based on the average dividend yield across external analyst reports for the quarter prior to scheme grant date.

**Performance Share Plan**

Performance awards are typically made annually at the discretion of the Group Remuneration Committee. Awards are based on a mixture of internal financial performance targets, risk-based measures and relative TSR.

Performance conditions exist for the scheme notably that you are employed by the Company at the vesting date, with good leaver exceptions, and an attrition rate is applied as an estimate of the actual number of awards that will meet the related conditions at the vesting date. The awards are not entitled to a dividend equivalent between grant date and vesting and a Black Scholes model is used to determine the grant date fair value with a dividend yield input applied – based on the average dividend yield across external analyst reports for the quarter prior to scheme grant date.

### 11. Share-based payments (continued)

The fair value of an option that is subject to market conditions (the relative share price element of the Performance Share Plan) is determined at grant date using a Monte Carlo model at the time of grant.

The inputs into the models are as follows:

| | **2020** | 2019 | 2018 | 2017 |
|---|---|---|---|---|
| Contractual life, years | **3-7** | 3 | 3 | 3 |
| Mid-market share price, £ | **2.58** | 3.96 | 4.11 | 4.04 |
| Attrition rate, % | **7.3** | 8.4 | 9.7 | 11.8 |
| Expected volatility, % | **43.9** | 26.8 | 29.1 | 63.7 |
| Dividend yield, % | **5.6** | 4.7 | 4.6 | 4.0 |
| Vesting rate - TSR % | **27.8** | 44.9 | 54.0 | 60.0 |
| Grant date fair value, £ | **2.06** | 3.47 | 3.61 | 3.61 |

CCFS PSP Mirror Schemes

| | 2019 | 2018 |
|---|---|---|
| Contractual life, years | 3 | 2 |
| Mid-market share price, £ | 3.54 | 3.54 |
| Expected volatility, % | 28.6 | 28.6 |
| Attrition rate, % | - | - |
| Dividend yield, % | 4.8 | 4.8 |
| Vesting rate - TSR, % | 37.4 | 37.4 |
| Grant date fair value, £ | 3.29 | 3.17 |

### 12. Integration costs

| | **Group 2020 £m** | Group 2019 £m |
|---|---|---|
| Consultant fees | **1.7** | 3.0 |
| Staff costs | **8.1** | 2.2 |
| | **9.8** | 5.2 |

Consultant fees relate to advice on the Group's future operating structure. Staff costs relate to key personnel who will leave the Group under the new operating model, but have been retained to assist in the integration for a fixed period.

### 13. Exceptional items

| | **Group 2020 £m** | Group 2019 £m |
|---|---|---|
| Consultant fees | **2.0** | 4.0 |
| Legal and professional fees | **1.3** | 4.6 |
| Success fees | **-** | 7.0 |
| | **3.3** | 15.6 |

Exceptional items for 2020 relate to the insertion of OSB GROUP PLC as the new holding company and listed entity of the OSB Group. 2019 expenses relate to the all-share Combination with CCFS.

### 14. Taxation

The Group publishes its tax strategy on its corporate website. The table below shows the components of the Group's tax charge for the year:

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| Corporation taxation | **(79.7)** | (57.1) |
| Deferred taxation | **0.8** | (0.2) |
| Release of deferred taxation on CCFS Combination[1] | **14.8** | 7.0 |
| **Total taxation** | **(64.1)** | (50.3) |

[1] Release of deferred taxation on CCFS Combination relates to the fair value unwind of the CCFS assets and liabilities at the acquisition date.

The charge for taxation on the Group's profit before taxation differs from the charge based on the standard rate of UK Corporation Tax of 19% (2019: 19%) as follows:

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| Profit before taxation | **260.3** | 209.1 |
| Profit multiplied by the standard rate of UK Corporation Tax (19%) | **(49.5)** | (39.7) |
| Bank surcharge[1] | **(11.0)** | (8.5) |
| **Taxation effects of:** | | |
| Expenses not deductible for taxation purposes | **(1.6)** | (3.0) |
| Impact of deferred tax rate change | **(4.4)** | - |
| Negative goodwill on acquisition not taxable | **-** | 2.0 |
| Adjustments in respect of earlier years | **0.4** | (2.7) |
| Tax adjustments in respect of share-based payments | **(0.8)** | (0.7) |
| Impact of tax losses carried forward | **-** | 0.5 |
| Tax on AT1 securities | **1.5** | 1.0 |
| Timing differences on capital items | **1.3** | 0.2 |
| Other | **-** | 0.6 |
| Total taxation charge | **(64.1)** | (50.3) |

[1] Tax charge for the two banking entities of £18.4m offset by the tax impact of unwinding CCFS Combination items of £5.8m (2019: Tax charge for the two banking entities of £10.4m offset by the tax impact of unwinding CCFS Combination items of £1.9m).

**Factors affecting tax charge for the year**

The effective tax rate for the year ended 31 December 2020, excluding the impact of the deferred tax rate change and adjustments in respect of earlier years, was 23.1% (2019: 22.8%).

The (£4.4m) impact of the deferred tax rate change relates predominantly to the deferred tax liability from the CCFS combination (see note 28).

During the year a tax charge of £0.3m (2019: tax charge of £1.1m) of tax has been recognised directly within equity relating to the Group's share-based payment schemes.

**14. Taxation** (continued)

During the year a tax credit of £0.5m (2019: tax credit of £0.2m) has been recognised within other comprehensive income relating to investment securities classified as FVOCI.

**Factors that may affect future tax charges**

In the March 2020 Budget, it was announced that the cuts in corporation tax rate to 18% and then to 17% previously enacted would not occur with the corporation tax rate held at 19%. As a result, closing deferred tax balances are calculated at 19% with the impact of the increase from 17%/18% to 19% reflected in the period.

On 3 March 2021, the government announced that the corporation tax rate will increase from 19% to 25% from 1 April 2023. This rate change was not substantively enacted at the balance sheet date and so has not been reflected in these financial statements. The government has also acknowledged that this increase in the main rate will result in an uncompetitive position for UK banks which also currently pay the 8% Bank Surcharge, and so has also announced a review of the Bank Surcharge will take place in Autumn 2021. Given that the majority of the Group's deferred tax is recognised at the combined corporation tax and Bank Surcharge rate, we are not yet able to estimate the impact of the combined rate changes on our deferred tax balances. We have assessed the impact of the increase of the corporation tax rate in isolation and concluded that it will not have a material impact on the Group's deferred tax balances.

**15. Dividends**

During the year, the Company paid the following dividends:

| | **Company 2020** | | Company 2019 | |
|---|---|---|---|---|
| | **£m** | **Pence per share** | £m | Pence per share |
| Final dividend for the prior year | - | - | 25.3 | 10.3 |
| Interim dividend for the current year | - | - | 12.0 | 4.9 |
| | - | | 37.3 | |

The Directors do not a propose a final dividend (2019: nil).

**16. Cash and cash equivalents**

The following table analyses the cash and cash equivalents disclosed in the Consolidated Statement of Cash Flows:

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| Cash in hand | **0.5** | 0.4 | **0.5** | 0.4 |
| Unencumbered loans and advances to credit institutions | **2,370.1** | 2,052.5 | **1,377.1** | 1,106.3 |
| Investment securities with original maturity less than 3 months | **-** | 49.9 | **-** | 49.9 |
| | **2,370.6** | 2,102.8 | **1,377.6** | 1,156.6 |

### 17. Loans and advances to credit institutions

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| **Unencumbered:** | | | | |
| BoE call account | **2,256.5** | 1,916.2 | **1,356.4** | 1,081.8 |
| Call accounts | **55.6** | 81.7 | **20.6** | 24.0 |
| Cash held in special purpose vehicles[1] | **51.0** | 44.0 | **0.1** | 0.5 |
| Term deposits | **7.0** | 10.6 | **-** | - |
| **Encumbered:** | | | | |
| BoE cash ratio deposit | **52.3** | 41.7 | **34.0** | 27.5 |
| Cash held in special purpose vehicles[1] | **42.7** | - | **-** | - |
| Cash margin given | **211.1** | 110.4 | **107.0** | 62.2 |
| | **2,676.2** | 2,204.6 | **1,518.1** | 1,196.0 |

[1] Cash held in special purpose vehicles is ring-fenced for the use in managing the Group's securitised debt facilities under the terms of securitisation agreements.

### 18. Investment securities

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| **Held at FVOCI:** | | | | |
| UK and EU Sovereign debt | **-** | 149.8 | **-** | 149.8 |
| RMBS loan notes | **285.0** | 358.9 | **15.0** | - |
| | **285.0** | 508.7 | **15.0** | 149.8 |
| **Held at amortised cost:** | | | | |
| RMBS loan notes | **186.2** | 126.6 | **-** | - |
| | **186.2** | 126.6 | **-** | - |
| Less: Expected credit losses | **-** | - | **-** | - |
| | **186.2** | 126.6 | **-** | - |
| | **471.2** | 635.3 | **15.0** | 149.8 |

At 31 December 2020 the Group had £147.1m (2019: £173.0m) of FVOCI RMBS and £13.7m (2019: nil) of amortised cost RMBS loan notes sold under repos or pledged as collateral. The Company had no investment securities sold under repos or pledged as collateral as at the 2020 and 2019 reporting dates.

The Directors consider that the primary purpose of holding investment securities is prudential. These securities are held as liquid assets with the intention of use on a continuing basis in the Group's activities and are classified as FVOCI and amortised cost in accordance with the Group's business model for each security.

### 18. Investment securities (continued)

Movements during the year of investment securities held by the Group and Company are analysed as follows:

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| At 1 January | **635.3** | 58.9 | **149.8** | 58.9 |
| Additions[1] | **291.6** | 439.8 | **205.9** | 439.8 |
| CCFS Combination | **-** | 493.5 | **-** | - |
| Disposals and maturities[2] | **(457.2)** | (357.7) | **(341.0)** | (349.0) |
| Movement in accrued interest | **0.5** | - | **0.4** | - |
| Changes in fair value | **1.0** | 0.8 | **(0.1)** | 0.1 |
| **At 31 December** | **471.2** | 635.3 | **15.0** | 149.8 |

[1] The Group's additions include £100.7m of retained RMBS loan notes following the deconsolidation of PMF 2020-1B.
[2] Disposals and maturities include £49.9m of UK Sovereign debt which had an original maturity of less than three months.

At 31 December 2020, the Group's investment securities included investments in unconsolidated structured entities (see note 45) of £100.7m (2019: nil) notes in PMF 2020-1B and £285.0m (2019: £358.9m) notes in PMF 2019-1B. The Company's investment securities included investments in unconsolidated structured entities of £15.0m (2019: nil) notes in PMF 2019-1B. The investments represent the maximum exposure to loss from unconsolidated structured entities.

### 19. Loans and advances to customers

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| **Held at amortised cost:** | | | | |
| Loans and advances (see note 20) | **19,257.1** | 18,419.9 | **8,596.2** | 8,420.8 |
| Finance leases (see note 21) | **65.5** | 47.7 | **-** | - |
| | **19,322.6** | 18,467.6 | **8,596.2** | 8,420.8 |
| Less: Expected credit losses (see note 22) | **(111.0)** | (42.9) | **(64.5)** | (26.6) |
| | **19,211.6** | 18,424.7 | **8,531.7** | 8,394.2 |
| Residential mortgages held at fair value | **19.1** | 22.1 | **-** | - |
| | **19,230.7** | 18,446.8 | **8,531.7** | 8,394.2 |

### 20. Loans and advances

| Group | 2020 OSB £m | 2020 CCFS £m | 2020 Total £m | 2019 OSB £m | 2019 CCFS £m | 2019 Total £m |
|---|---|---|---|---|---|---|
| **Gross carrying amount** | | | | | | |
| Stage 1 | **9,310.8** | **6,749.5** | **16,060.3** | 9,999.2 | 7,240.0 | 17,239.2 |
| Stage 2 | **1,362.0** | **1,327.6** | **2,689.6** | 442.4 | 307.1 | 749.5 |
| Stage 3 | **344.5** | **48.1** | **392.6** | 277.7 | 16.7 | 294.4 |
| Stage 3 (POCI) | **48.6** | **66.0** | **114.6** | 53.6 | 83.2 | 136.8 |
| | **11,065.9** | **8,191.2** | **19,257.1** | 10,772.9 | 7,647.0 | 18,419.9 |

| Company | 2020 £m | 2019 £m |
|---|---|---|
| **Gross carrying amount** | | |
| Stage 1 | **7,080.4** | 7,785.0 |
| Stage 2 | **1,215.2** | 371.3 |
| Stage 3 | **255.2** | 211.1 |
| Stage 3 (POCI) | **45.4** | 53.4 |
| | **8,596.2** | 8,420.8 |

The mortgage loan balances pledged as collateral for liabilities are:

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| BoE under TFS, TFSME and ILTR | **5,203.2** | 4,458.3 | **2,917.8** | 2,775.7 |
| Securitisation | **435.4** | 366.7 | **146.2** | 234.3 |
| Warehouse funding | **-** | 97.4 | **-** | - |
| Master servicer for securitisation vehicle | **-** | 40.4 | **-** | 40.4 |
| | **5,638.6** | 4,962.8 | **3,064.0** | 3,050.4 |

The Group's securitisation programmes, use of TFS, TFSME and ILTR and Warehouse funding arrangements result in certain assets being encumbered as collateral against such funding. As at 31 December 2020, the percentage of the Group's gross customer loans and receivables that are encumbered was 29% (2019: 27%).

At 31 December 2019, £40.4m of retention loans (i.e. loans in securitisation portfolios that are retained by the originator) were treated as encumbered. For 2020, the Group has treated these as unencumbered as they are available to use to raise collateral as long as the risk and rewards of the loans remain with the Group.

**20. Loans and advances** (continued)

The Company adopts a net accounting approach for retained interests in securitisation transactions that are consolidated into the Group, disclosing the net amount as a deemed loan liability. The table below shows the Company's securitised mortgages and retained loan notes:

| | Company 2020 £m | Company 2019 £m |
|---|---|---|
| Loans and advances to customers | 1,920.0 | 464.3 |
| Deemed loan premium | 14.7 | 6.5 |
| Retained loan notes | (1,868.5) | (230.6) |
| | 66.2 | 240.2 |

As at 31 December 2020, the Company had £686.9m (2019: nil) of the retained loan notes sold under repos or pledged as collateral.

The tables below show the movement in loans and advances to customers by IFRS 9 stage during the year, based on the following assumptions:

| Group | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **At 31 December 2018** | 8,279.6 | 436.8 | 225.4 | 56.2 | 8,998.0 |
| Originations[1] | 4,098.6 | - | - | - | 4,098.6 |
| CCFS Combination[3] | 7,091.1 | 43.5 | - | 94.4 | 7,229.0 |
| Repayments and write-offs[2] | (1,825.2) | (21.6) | (47.5) | (17.3) | (1,911.6) |
| Transfers: | | | | | |
| - To Stage 1 | 176.9 | (162.7) | (14.2) | - | - |
| - To Stage 2 | (495.9) | 517.7 | (21.8) | - | - |
| - To Stage 3 | (86.1) | (64.5) | 150.6 | - | - |
| Incurred loss protection | 0.2 | 0.3 | 1.9 | 3.5 | 5.9 |
| **At 31 December 2019** | 17,239.2 | 749.5 | 294.4 | 136.8 | 18,419.9 |
| Originations[1] | **3,767.0** | **-** | **-** | **-** | **3,767.0** |
| Acquisitions | **60.8** | **-** | **-** | **1.5** | **62.3** |
| Disposals | **(787.3)** | **(16.1)** | **(1.0)** | **-** | **(804.4)** |
| Repayments and write-offs[2] | **(2,119.1)** | **(3.9)** | **(41.0)** | **(23.7)** | **(2,187.7)** |
| Transfers: | | | | | |
| - To Stage 1 | **324.8** | **(293.5)** | **(31.3)** | **-** | **-** |
| - To Stage 2[4] | **(2,300.3)** | **2,344.5** | **(44.2)** | **-** | **-** |
| - To Stage 3 | **(124.8)** | **(90.9)** | **215.7** | **-** | **-** |
| **At 31 December 2020** | **16,060.3** | **2,689.6** | **392.6** | **114.6** | **19,257.1** |

[1] Originations include further advances and drawdowns on existing commitments.
[2] Repayments and write-offs include customer redemptions.
[3] The mortgages acquired in the all-share Combination with CCFS are shown at the acquisition date fair value.
[4] Increase from previous year due to the additional qualitative and quantitative tests applied in 2020 for loans with payment deferrals. Payment deferrals increased in 2020 notably through COVID-19 initiatives and impacts.

**20. Loans and advances** (continued)

During the year the Group purchased one external mortgage book at par. The Group did not purchase any external mortgage books during 2019 other than those acquired in the Combination.

| Company | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **At 31 December 2018** | 6,657.0 | 346.6 | 164.8 | 55.9 | 7,224.3 |
| Originations[1] | 2,395.3 | - | - | - | 2,395.3 |
| Repayments and write-offs[2] | (1,153.2) | (19.1) | (26.4) | (6.0) | (1,204.7) |
| Transfers: | | | | | |
| - To Stage 1 | 117.8 | (106.8) | (11.0) | - | - |
| - To Stage 2 | (178.7) | 196.4 | (17.7) | - | - |
| - To Stage 3 | (53.4) | (46.1) | 99.5 | - | - |
| Incurred loss protection | 0.2 | 0.3 | 1.9 | 3.5 | 5.9 |
| **At 31 December 2019** | 7,785.0 | 371.3 | 211.1 | 53.4 | 8,420.8 |
| Originations[1] | **1,523.1** | **-** | **-** | **-** | **1,523.1** |
| Disposals | **(401.3)** | **(8.3)** | **(1.0)** | **-** | **(410.6)** |
| Repayments and write-offs[2] | **(955.0)** | **54.4** | **(28.5)** | **(8.0)** | **(937.1)** |
| Transfers: | | | | | |
| - To Stage 1 | **126.0** | **(107.0)** | **(19.0)** | **-** | **-** |
| - To Stage 2[3] | **(920.5)** | **956.8** | **(36.3)** | **-** | **-** |
| - To Stage 3 | **(76.9)** | **(52.0)** | **128.9** | **-** | **-** |
| **At 31 December 2020** | **7,080.4** | **1,215.2** | **255.2** | **45.4** | **8,596.2** |

[1] Originations include further advances and drawdowns on existing commitments.
[2] Repayments and write-offs include customer redemptions.
[3] Increase from previous year due to the additional qualitative and quantitative tests applied in 2020 for loans with payment holidays. Payment holidays increased in 2020 notably through COVID-19 initiatives and impacts.

The Company did not purchase any external mortgage books during 2020 and 2019 other than those acquired in the Combination.

### 21. Finance leases

The Group provides asset finance lending through InterBay Asset Finance Limited.

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| **Gross investment in finance leases, receivable** | | |
| Less than one year | 21.9 | 14.1 |
| Between one and five years | 50.4 | 38.5 |
| More than 5 years | 1.3 | 1.2 |
| | 73.6 | 53.8 |
| Unearned finance income | (8.1) | (6.1) |
| Net investment in finance leases | 65.5 | 47.7 |
| | | |
| **Net investment in finance leases, receivable** | | |
| Less than one year | 18.6 | 11.5 |
| Between one and five years | 45.7 | 35.0 |
| More than five years | 1.2 | 1.2 |
| | 65.5 | 47.7 |

The Group has recognised £2.6m of ECLs on finance leases as at 31 December 2020 (2019: £0.3m).

### 22. Expected credit loss

The ECL has been calculated based on various scenarios as set out below:

| Group At 31 December 2020 | ECL provision 2020 £m | Weighting 2020 % | Weighted ECL provision 2020 £m | ECL provision 2019 £m | Weighting 2019 % | Weighted ECL provision 2019 £m |
|---|---|---|---|---|---|---|
| **Scenarios** | | | | | | |
| Upside | 40.1 | 30 | 12.0 | 14.6 | 10 | 1.5 |
| Base case | 54.6 | 40 | 21.8 | 24.4 | 40 | 9.7 |
| Downside scenario | 113.5 | 23 | 26.1 | 48.1 | 35 | 16.8 |
| Severe downside scenario | 166.7 | 7 | 11.7 | 62.5 | 15 | 9.4 |
| Total weighted provisions | | | 71.6 | | | 37.4 |
| **Non-modelled Provisions:** | | | | | | |
| Individually-assessed provisions | - | - | 29.0 | - | - | 4.2 |
| Post model adjustments[1] | - | - | 10.4 | - | - | 1.3 |
| **Total provision** | | | 111.0 | | | 42.9 |

[1]COVID-19 post model adjustments – the Group implemented a number of post model adjustments to ensure that modelled estimates remained appropriate, in light of the impact that COVID-19 support measures, such as the repossession moratorium and the impact of payment deferrals on the credit bureau files, had on probability of default and loss given default estimates. In addition updated model estimates were also aligned to recently observed actual performance. Additional information can be found in the Strategic Report on pages 3 to 69.

## OneSavings Bank plc
## Notes to the Financial Statements (continued)
For the year ended 31 December 2020

### 22. Expected credit loss (continued)

| Company<br>At 31 December 2020 | ECL provision 2020 £m | Weighting 2020 % | Weighted ECL provision 2020 £m | ECL provision 2019 £m | Weighting 2019 % | Weighted ECL provision 2019 £m |
|---|---|---|---|---|---|---|
| **Scenarios** | | | | | | |
| Upside | **22.5** | **30** | **6.8** | 9.9 | 10 | 1.0 |
| Base case | **30.1** | **40** | **12.0** | 17.2 | 40 | 6.9 |
| Downside scenario | **65.2** | **23** | **15.0** | 31.1 | 35 | 10.9 |
| Severe downside scenario | **96.9** | **7** | **6.8** | 39.1 | 15 | 5.9 |
| Total weighted provisions | | | **40.6** | | | 24.7 |
| **Non-modelled Provisions:** | | | | | | |
| Individually-assessed provisions | - | - | **22.0** | - | - | 0.8 |
| Post model adjustments[1] | - | - | **1.9** | - | - | 1.1 |
| **Total provision** | | | **64.5** | | | 26.6 |

[1]COVID-19 post model adjustments – the Group implemented a number of post model adjustments to ensure that modelled estimates remained appropriate, in light of the impact that COVID-19 support measures, such as the repossession moratorium and the impact of payment deferrals on the credit bureau files, had on probability of default and loss given default estimates. In addition updated model estimates were also aligned to recently observed actual performance. Additional information can be found in the Strategic Report overview on pages 3 to 69.

The Group and Company ECL by segment and IFRS 9 stage are shown below:

| | 2020 | | | 2019 | | |
|---|---|---|---|---|---|---|
| | **OSB** | **CCFS** | **Total** | OSB | CCFS | Total |
| **Group** | **£m** | **£m** | **£m** | £m | £m | £m |
| Stage 1 | **12.3** | **8.9** | **21.2** | 3.5 | 2.1 | 5.6 |
| Stage 2 | **17.9** | **13.1** | **31.0** | 3.6 | 2.0 | 5.6 |
| Stage 3 | **49.4** | **2.3** | **51.7** | 23.4 | 0.4 | 23.8 |
| Stage 3 (POCI) | **4.0** | **3.1** | **7.1** | 5.1 | 2.8 | 7.9 |
| | **83.6** | **27.4** | **111.0** | 35.6 | 7.3 | 42.9 |

| Company | 2020 £m | 2019 £m |
|---|---|---|
| Stage 1 | **8.4** | 2.8 |
| Stage 2 | **16.3** | 3.3 |
| Stage 3 | **35.9** | 15.4 |
| Stage 3 (POCI) | **3.9** | 5.1 |
| | **64.5** | 26.6 |

### 22. Expected credit loss (continued)

The tables below show the movement in the ECL by IFRS 9 stage during the year. ECLs on originations reflect the IFRS 9 stage of loans originated during the year as at 31 December and not the date of origination. Remeasurement of loss allowance relates to existing loans which did not redeem during the year and includes the impact of loans moving between IFRS 9 stages.

| Group | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **At 31 December 2018** | 4.5 | 5.6 | 10.2 | 1.6 | 21.9 |
| Originations | 1.9 | - | - | - | 1.9 |
| CCFS Combination | - | - | - | 3.6 | 3.6 |
| Repayments and write-offs | (0.6) | (0.4) | (4.3) | (0.2) | (5.5) |
| Remeasurement of loss allowance | (3.4) | (0.5) | 18.8 | (0.6) | 14.3 |
| Transfers: | | | | | |
| - To Stage 1 | 1.9 | (1.6) | (0.3) | - | - |
| - To Stage 2 | (0.2) | 0.6 | (0.4) | - | - |
| - To Stage 3 | (0.1) | (1.0) | 1.1 | - | - |
| Changes in assumptions and model parameters | 1.4 | 2.6 | (3.2) | - | 0.8 |
| Incurred loss protection | 0.2 | 0.3 | 1.9 | 3.5 | 5.9 |
| **At 31 December 2019** | 5.6 | 5.6 | 23.8 | 7.9 | 42.9 |
| Originations | 6.3 | - | - | - | 6.3 |
| Acquisitions | - | - | 0.1 | - | 0.1 |
| Disposals | (0.1) | (0.2) | (0.1) | - | (0.4) |
| Repayments and write-offs | (0.7) | (0.3) | (4.1) | (1.1) | (6.2) |
| Remeasurement of loss allowance | 6.3 | 7.7 | 29.0 | (0.2) | 42.8 |
| Transfers: | | | | | |
| - To Stage 1 | 2.0 | (1.4) | (0.6) | - | - |
| - To Stage 2 | (1.0) | 2.8 | (1.8) | - | - |
| - To Stage 3 | (0.1) | (1.2) | 1.3 | - | - |
| Changes in assumptions and model parameters | 2.9 | 18.0 | 4.1 | 0.5 | 25.5 |
| **At 31 December 2020** | 21.2 | 31.0 | 51.7 | 7.1 | 111.0 |

**22. Expected credit loss** (continued)

| Company | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **At 31 December 2018** | 3.6 | 4.7 | 6.2 | 1.6 | 16.1 |
| Originations | 1.3 | - | - | - | 1.3 |
| Repayments and write-offs | (0.3) | (0.4) | (2.8) | (0.1) | (3.6) |
| Remeasurement of loss allowance | (4.5) | (2.3) | 12.8 | 0.1 | 6.1 |
| Transfers: | | | | | |
| - To Stage 1 | 1.4 | (1.2) | (0.2) | - | - |
| - To Stage 2 | (0.2) | 0.5 | (0.3) | - | - |
| - To Stage 3 | (0.1) | (0.9) | 1.0 | - | - |
| Changes in assumptions and model parameters | 1.4 | 2.6 | (3.2) | - | 0.8 |
| Incurred loss protection | 0.2 | 0.3 | 1.9 | 3.5 | 5.9 |
| **At 31 December 2019** | 2.8 | 3.3 | 15.4 | 5.1 | 26.6 |
| Originations | **2.4** | **-** | **-** | **-** | **2.4** |
| Disposals | **(0.1)** | **(0.1)** | **(0.1)** | **-** | **(0.3)** |
| Repayments and write-offs | **(0.2)** | **(0.2)** | **(2.9)** | **(0.1)** | **(3.4)** |
| Remeasurement of loss allowance | **2.1** | **3.1** | **22.3** | **(1.4)** | **26.1** |
| Transfers: | | | | | |
| - To Stage 1 | **0.8** | **(0.5)** | **(0.3)** | **-** | **-** |
| - To Stage 2 | **(0.4)** | **2.1** | **(1.7)** | **-** | **-** |
| - To Stage 3 | **-** | **(0.8)** | **0.8** | **-** | **-** |
| Changes in assumptions and model parameters | **1.0** | **9.4** | **2.4** | **0.3** | **13.1** |
| **At 31 December 2020** | **8.4** | **16.3** | **35.9** | **3.9** | **64.5** |

The tables below show the stage 2 ECL balances by transfer criteria:

| Group | Carrying value 2020 £m | ECL 2020 £m | Coverage 2020 % | Carrying value 2019 £m | ECL 2019 £m | Coverage 2019 % |
|---|---|---|---|---|---|---|
| **Criteria:** | | | | | | |
| Relative PD movement | **946.9** | **17.0** | **1.80** | 588.2 | 4.8 | 0.82 |
| Qualitative measures | **1,680.7** | **12.7** | **0.76** | 79.8 | 0.4 | 0.44 |
| 30 days past due backstop | **63.4** | **1.3** | **2.05** | 81.5 | 0.4 | 0.54 |
| **Total** | **2,691.0** | **31.0** | **1.15** | 749.5 | 5.6 | 0.75 |

### 22. Expected credit loss (continued)

| Company | Carrying value 2020 £m | ECL 2020 £m | Coverage 2020 % | Carrying value 2019 £m | ECL 2019 £m | Coverage 2019 % |
|---|---|---|---|---|---|---|
| **Criteria:** | | | | | | |
| Relative PD movement | 354.5 | 8.6 | 2.43 | 306.8 | 3.0 | 0.98 |
| Qualitative measures | 835.4 | 6.9 | 0.83 | 35.2 | 0.1 | 0.32 |
| 30 days past due backstop | 25.3 | 0.8 | 3.16 | 29.3 | 0.2 | 0.80 |
| **Total** | 1,215.2 | 16.3 | 1.34 | 371.3 | 3.3 | 0.90 |

The Group has a number of qualitative measures to determine whether a SICR has taken place. These triggers utilise both internal performance information, to analyse whether an account is in distress but not yet in arrears, and external credit bureau information, to determine whether the customer is experiencing financial difficulty with an external credit obligation.

### 23. Impairment of financial assets

The charge for impairment of financial assets in the Consolidated Statement of Comprehensive Income comprises:

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| Write-offs in year | 1.9 | 4.1 |
| Disposals | 0.4 | - |
| CCFS Combination | - | 3.6 |
| Increase in ECL provision | 68.7 | 7.9 |
| | 71.0 | 15.6 |

The CCFS Combination losses relate to the initial ECL recognised on the CCFS loan book following the Combination in October 2019.

### 24. Derivatives

The table below reconciles the gross amount of derivative contracts to the carrying balance shown in the Consolidated Statement of Financial Position:

| Group | Gross amount of recognised financial assets / (liabilities) £m | Net amount of financial assets / (liabilities) presented in the Consolidated Statement of Financial Position £m | Contracts subject to master netting agreements not offset in the Consolidated Statement of Financial Position £m | Cash collateral paid / (received) not offset in the Consolidated Statement of Financial Position £m | Net amount £m |
|---|---|---|---|---|---|
| **At 31 December 2020** | | | | | |
| Derivative assets: | | | | | |
| Interest rate risk hedging | **12.3** | **12.3** | **(11.8)** | **-** | **0.5** |
| | **12.3** | **12.3** | **(11.8)** | **-** | **0.5** |
| Derivative liabilities: | | | | | |
| Interest rate risk hedging | **(163.6)** | **(163.6)** | **11.8** | **210.5** | **58.7** |
| | **(163.6)** | **(163.6)** | **11.8** | **210.5** | **58.7** |
| **At 31 December 2019** | | | | | |
| Derivative assets: | | | | | |
| Interest rate risk hedging | 21.1 | 21.1 | (9.8) | (8.0) | 3.3 |
| | 21.1 | 21.1 | (9.8) | (8.0) | 3.3 |
| Derivative liabilities: | | | | | |
| Interest rate risk hedging | (92.8) | (92.8) | 9.8 | 110.4 | 27.4 |
| | (92.8) | (92.8) | 9.8 | 110.4 | 27.4 |

Included within the Group's derivative liabilities is £0.1m (2019: £3.4m) of derivative contracts not covered by master netting agreements and therefore no cash collateral has been paid.

| Company | Gross amount of recognised financial assets / (liabilities) £m | Net amount of financial assets / (liabilities) presented in the Statement of Financial Position £m | Contracts subject to master netting agreements not offset in the Statement of Financial Position £m | Cash collateral paid / (received) not offset in the Statement of Financial Position £m | Net amount £m |
|---|---|---|---|---|---|
| **At 31 December 2020** | | | | | |
| Derivative assets: | | | | | |
| Interest rate risk hedging | **4.7** | **4.7** | **(4.2)** | **-** | **0.5** |
| | **4.7** | **4.7** | **(4.2)** | **-** | **0.5** |
| Derivative liabilities: | | | | | |
| Interest rate risk hedging | **(93.8)** | **(93.8)** | **4.2** | **106.4** | **16.8** |
| | **(93.8)** | **(93.8)** | **4.2** | **106.4** | **16.8** |
| **At 31 December 2019** | | | | | |
| Derivative assets: | | | | | |
| Interest rate risk hedging | 8.7 | 8.7 | (2.5) | (7.8) | (1.6) |
| | 8.7 | 8.7 | (2.5) | (7.8) | (1.6) |
| Derivative liabilities: | | | | | |
| Interest rate risk hedging | (54.3) | (54.3) | 2.5 | 62.2 | 10.4 |
| | (54.3) | (54.3) | 2.5 | 62.2 | 10.4 |

**24. Derivatives** (continued)

Included within the Company's derivative liabilities is nil (2019: £3.4m) of derivative contracts not covered by master netting agreements and therefore no cash collateral has been paid.

The tables below profile the timing of nominal amounts for interest rate risk hedging derivatives based on contractual maturity:

| Group | Total nominal £m | Less than 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|
| **At 31 December 2020** | | | | | |
| Derivative assets | **8,687.8** | **1,450.7** | **3,407.8** | **3,808.3** | **21.0** |
| Derivative liabilities | **10,392.4** | **148.0** | **1,868.0** | **8,065.9** | **310.5** |
| | **19,080.2** | **1,598.7** | **5,275.8** | **11,874.2** | **331.5** |
| **At 31 December 2019** | | | | | |
| Derivative assets | 7,795.4 | 1,110.8 | 2,608.2 | 3,760.9 | 315.5 |
| Derivative liabilities | 9,982.4 | 144.3 | 2,528.6 | 7,155.5 | 154.0 |
| | 17,777.8 | 1,255.1 | 5,136.8 | 10,916.4 | 469.5 |

The Group has 925 (2019: 1,175) derivative contracts with an average fixed rate of 0.47% (2019: 0.91%).

| Company | Total nominal £m | Less than 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|
| **At 31 December 2020** | | | | | |
| Derivative assets | **3,585.0** | **630.0** | **2,040.0** | **915.0** | **-** |
| Derivative liabilities | **3,729.0** | **-** | **134.0** | **3,422.0** | **173.0** |
| | **7,314.0** | **630.0** | **2,174.0** | **4,337.0** | **173.0** |
| **At 31 December 2019** | | | | | |
| Derivative assets | 3,080.0 | 475.0 | 1,395.0 | 1,110.0 | 100.0 |
| Derivative liabilities | 4,462.9 | 8.3 | 789.6 | 3,549.0 | 116.0 |
| | 7,542.9 | 483.3 | 2,184.6 | 4,659.0 | 216.0 |

The Company has 154 (2019: 205) derivative contracts with an average fixed rate of 0.18% (2019: 1.17%).

## 25. Hedge accounting

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| **Hedged assets** | | | | |
| Current hedge relationships | **197.5** | 64.2 | **134.8** | 36.1 |
| Swap inception adjustment | **(100.5)** | (67.8) | **(50.1)** | - |
| Cancelled hedge relationships | **84.6** | 20.4 | **42.7** | 16.7 |
| **Fair value adjustments on hedged assets** | **181.6** | 16.8 | **127.4** | 52.8 |
| **Hedged liabilities** | | | | |
| Current hedge relationships | **(11.8)** | (2.9) | **(3.3)** | 0.1 |
| Swap inception adjustment | **6.2** | 8.0 | **2.8** | - |
| De-designated hedge relationships | **(2.6)** | - | **(2.6)** | - |
| **Fair value adjustments on hedged liabilities** | **(8.2)** | 5.1 | **(3.1)** | 0.1 |

The swap inception adjustment relates in part to hedged assets and liabilities recognised on the Combination where pre-existing hedge relationships ceased on the date of Combination. The swap inception adjustment is being amortised over the life of the derivative instruments acquired on Combination and recognises an offsetting asset or liability to the fair value of the derivative instruments on the date of Combination. The remainder of the swap inception adjustment relates to the hedging adjustments arising when hedge accounting commences, primarily on derivative instruments previously taken out against the mortgage pipeline and also on derivative instruments previously taken out against new retail deposits.

Cancelled hedge relationships predominantly represent the unamortised fair value adjustment for interest rate risk hedges that have been cancelled and replaced due to IBOR transition ,securitisation activities and legacy long-term fixed rate mortgages (c. 25 years at origination).

The tables below analyse the Group's and Company's portfolio hedge accounting for fixed rate loans and advances to customers:

| | Group 2020 | | Group 2019 | |
|---|---|---|---|---|
| **Loans and advances to customers** | **Hedged item £m** | **Hedging instrument £m** | Hedged item £m | Hedging instrument £m |
| Carrying amount of hedged item/nominal value of hedging instrument | **11,282.4** | **11,159.7** | 10,312.5 | 10,248.3 |
| Cumulative fair value adjustments | **197.5** | **(156.9)** | 64.2 | (75.6) |
| Fair value adjustments for the period | **107.3** | **(116.8)** | 70.1 | (75.1) |
| Cumulative fair value on cancelled hedge relationships | **84.6** | **-** | 20.4 | - |

The cumulative fair value adjustments of the hedging instrument comprise £0.7m (2019: £13.2m) recognised within derivative assets and £157.6m (2019: £88.8m) recognised within derivative liabilities.

**25. Hedge accounting** (continued)

| Loans and advances to customers | **Company 2020** | | Company 2019 | |
|---|---|---|---|---|
| | **Hedged item £m** | **Hedging instrument £m** | Hedged item £m | Hedging instrument £m |
| Carrying amount of hedged item/nominal value of hedging instrument | **3,772.2** | **3,699.0** | 4,574.0 | 4,537.9 |
| Cumulative fair value adjustments | **134.7** | **(89.9)** | 36.1 | (45.5) |
| Fair value adjustments for the period | **72.2** | **(80.6)** | 39.8 | (43.7) |
| Cumulative fair value on cancelled hedge relationships | **42.7** | **-** | 16.7 | - |

The cumulative fair value adjustments of the hedging instrument comprise £0.2m (2019: £6.8m) recognised within derivative assets and £90.1m (2019: £52.3m) recognised within derivative liabilities.

The movement in cancelled hedge relationships is as follows:

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| At 1 January | **20.4** | 17.3 | **16.7** | 17.3 |
| New cancellations[1] | **86.1** | 8.6 | **38.2** | 4.9 |
| Amortisation | **(17.9)** | (5.5) | **(8.2)** | (5.5) |
| Derecognition of hedged item | **(4.0)** | - | **(4.0)** | - |
| **At 31 December** | **84.6** | 20.4 | **42.7** | 16.7 |

[1] Following the securitisation of mortgages during the year and LIBOR swaps transferred to SONIA swaps through the IBOR transition, the Group cancelled swaps which were effective prior to the event, with the designated hedge moved to cancelled hedge relationships to be amortised over the original life of the swap.

The tables below analyse the Group's and Company's portfolio hedge accounting for fixed rate amounts owed to retail depositors:

| Customer deposits | **Group 2020** | | Group 2019 | |
|---|---|---|---|---|
| | **Hedged item £m** | **Hedging instrument £m** | Hedged item £m | Hedging instrument £m |
| Carrying amount of hedged item/nominal value of hedging instrument | **6,849.9** | **6,858.0** | 6,684.6 | 6,687.5 |
| Cumulative fair value adjustments | **(11.8)** | **9.2** | (2.9) | 3.5 |
| Fair value adjustments for the period | **(4.1)** | **6.8** | (4.6) | 4.8 |

The cumulative fair value adjustments of the hedging instrument comprise £9.4m (2019: £5.9m) recognised within derivative assets and £0.2m (2019: £2.4m) recognised within derivative liabilities.

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## Notes to the Financial Statements (continued)

For the year ended 31 December 2020

### 25. Hedge accounting (continued)

| Customer deposits | Company 2020 Hedged item £m | Company 2020 Hedging instrument £m | Company 2019 Hedged item £m | Company 2019 Hedging instrument £m |
|---|---|---|---|---|
| Carrying amount of hedged item/nominal value of hedging instrument | **3,050.4** | **3,050.0** | 2,804.9 | 2,805.0 |
| Cumulative fair value adjustments | **(3.3)** | **3.3** | (0.1) | 0.5 |
| Fair value adjustments for the period | **(1.0)** | **3.8** | (1.8) | 2.2 |

The cumulative fair value adjustments of the hedging instrument comprise £3.3m (2019: £1.0m) recognised within derivative assets and nil (2019: £0.5m) recognised within derivative liabilities.

### 26. Other assets

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| Prepayments | **7.3** | 9.3 | **4.2** | 3.2 |
| Other assets | **1.8** | 5.0 | **1.5** | 4.3 |
| | **9.1** | 14.3 | **5.7** | 7.5 |

### 27. Deferred taxation asset

| Group | Losses carried forward £m | Accelerated depreciation £m | Share-based payments £m | IFRS 9 transitional adjustments £m | Others[1] £m | Total £m |
|---|---|---|---|---|---|---|
| **At 31 December 2018** | 1.4 | (0.1) | 1.5 | 0.7 | - | 3.5 |
| Profit or loss (charge)/credit | (0.5) | 0.3 | 0.8 | (0.1) | (0.7) | (0.2) |
| CCFS Combination | - | (0.1) | 0.5 | 0.1 | 1.4 | 1.9 |
| Transferred to corporation tax liability | - | - | (1.3) | - | - | (1.3) |
| Tax taken directly to OCI | - | - | - | - | (0.2) | (0.2) |
| Tax taken directly to equity | - | - | 1.1 | - | - | 1.1 |
| **At 31 December 2019** | 0.9 | 0.1 | 2.6 | 0.7 | 0.5 | 4.8 |
| Profit or loss credit/(charge) | **-** | **0.3** | **0.9** | **-** | **(0.4)** | **0.8** |
| Transferred to corporation tax liability | **-** | **-** | **(0.6)** | **-** | **-** | **(0.6)** |
| Tax taken directly to OCI | **-** | **-** | **-** | **-** | **(0.5)** | **(0.5)** |
| Tax taken directly to equity | **-** | **-** | **0.2** | **-** | **-** | **0.2** |
| **At 31 December 2020** | **0.9** | **0.4** | **3.1** | **0.7** | **(0.4)** | **4.7** |

[1] Others include deferred taxation assets recognised on financial assets classified as FVOCI, derivatives and short-term timing differences.

**27. Deferred taxation asset** (continued)

In 2020, the profit or loss credit/(charge) includes £(0.3m) impact of the deferred tax rate change (2019: nil).

As at 31 December 2020, the Group had £3.5m (2019: £3.5m) of losses for which a deferred tax asset has not been recognised as the Group does not expect sufficient future profits to be available to utilise the losses.

| Company | Accelerated depreciation £m | Share-based payments £m | IFRS 9 transitional adjustments £m | Total £m |
|---|---|---|---|---|
| **At 31 December 2018** | (0.2) | 1.5 | 0.3 | 1.6 |
| Profit or loss credit | 0.3 | 0.8 | - | 1.1 |
| Transferred to corporation tax liability | - | (1.3) | - | (1.3) |
| Tax taken directly to equity | - | 0.8 | - | 0.8 |
| **At 31 December 2019** | 0.1 | 1.8 | 0.3 | 2.2 |
| Profit or loss credit | **0.3** | **1.2** | **-** | **1.5** |
| Transferred to corporation tax liability | **-** | **(0.8)** | **-** | **(0.8)** |
| Tax taken directly to equity | **-** | **0.2** | **-** | **0.2** |
| **At 31 December 2020** | **0.4** | **2.4** | **0.3** | **3.1** |

**28. Deferred taxation liability:**

The deferred tax liability recognised on the Combination relates to the timing differences of the recognition of assets and liabilities at fair value, where the fair values will unwind in future periods in line with the underlying asset or liability. The deferred tax liability has been measured using the relevant rates for the expected periods of utilisation.

| Group | CCFS Combination £m |
|---|---|
| **At 31 December 2018** | - |
| CCFS Combination | 70.1 |
| Profit or loss credit | (7.0) |
| **At 31 December 2019** | 63.1 |
| Profit or loss credit | **(14.8)** |
| **At 31 December 2020** | **48.3** |

In 2020, the profit or loss credit includes £4.7m impact of the deferred tax rate change (2019: nil).

## OneSavings Bank plc
## Notes to the Financial Statements (continued)
For the year ended 31 December 2020

### 29. Property, plant and equipment

| Group | Freehold land and buildings £m | Leasehold improvements £m | Equipment and fixtures £m | Right of use assets: Property leases £m | Right of use assets: Other leases £m | Total £m |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| At 1 January 2019 | 16.0 | 0.9 | 11.0 | 3.8 | - | 31.7 |
| Additions | 3.1 | 1.5 | 2.4 | 2.5 | 0.1 | 9.6 |
| CCFS Combination | - | 0.3 | 2.1 | 6.4 | 1.2 | 10.0 |
| Disposals and write-offs[1] | - | - | (1.2) | - | - | (1.2) |
| Foreign exchange difference | 0.2 | - | 0.1 | - | - | 0.3 |
| At 31 December 2019 | 19.3 | 2.7 | 14.4 | 12.7 | 1.3 | 50.4 |
| **Additions** | **-** | **0.3** | **2.5** | **0.6** | **-** | **3.4** |
| **Disposals and write-offs[1]** | **-** | **-** | **(3.0)** | **(0.2)** | **-** | **(3.2)** |
| **Foreign exchange difference** | **(0.1)** | **-** | **(0.1)** | **-** | **-** | **(0.2)** |
| **At 31 December 2020** | **19.2** | **3.0** | **13.8** | **13.1** | **1.3** | **50.4** |
| | | | | | | |
| **Depreciation** | | | | | | |
| At 1 January 2019 | 0.8 | 0.3 | 5.0 | - | - | 6.1 |
| Charged in year | 0.3 | 0.2 | 2.3 | 1.0 | 0.1 | 3.9 |
| Disposals and write-offs[1] | - | - | (1.2) | - | - | (1.2) |
| At 31 December 2019 | 1.1 | 0.5 | 6.1 | 1.0 | 0.1 | 8.8 |
| **Charged in year** | **0.3** | **0.4** | **2.9** | **1.8** | **0.2** | **5.6** |
| **Disposals and write-offs[1]** | **-** | **-** | **(3.0)** | **(0.2)** | **-** | **(3.2)** |
| **At 31 December 2020** | **1.4** | **0.9** | **6.0** | **2.6** | **0.3** | **11.2** |
| | | | | | | |
| **Net book value** | | | | | | |
| **At 31 December 2020** | **17.8** | **2.1** | **7.8** | **10.5** | **1.0** | **39.2** |
| At 31 December 2019 | 18.2 | 2.2 | 8.3 | 11.7 | 1.2 | 41.6 |

[1]During the year the Group wrote off fully depreciated assets.

# OneSavings Bank plc

## Notes to the Financial Statements (continued)

For the year ended 31 December 2020

### 29. Property, plant and equipment (continued)

| Company | Freehold land and buildings £m | Leasehold improvements £m | Equipment and fixtures £m | Right of use assets: Property leases £m | Right of use assets: Other leases £m | Total £m |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| At 1 January 2019 | 11.5 | 0.7 | 8.2 | 2.3 | - | 22.7 |
| Additions | - | 1.5 | 1.9 | 2.6 | 0.1 | 6.1 |
| Disposals and write-offs[1] | - | - | (0.9) | - | - | (0.9) |
| At 31 December 2019 | 11.5 | 2.2 | 9.2 | 4.9 | 0.1 | 27.9 |
| **Additions** | **-** | **0.3** | **1.3** | **0.6** | **-** | **2.2** |
| **Disposals and write-offs[1]** | **-** | **-** | **(2.7)** | **-** | **-** | **(2.7)** |
| **At 31 December 2020** | **11.5** | **2.5** | **7.8** | **5.5** | **0.1** | **27.4** |
| **Depreciation** | | | | | | |
| At 1 January 2019 | 0.7 | 0.3 | 3.8 | - | - | 4.8 |
| Charged in year | 0.2 | 0.1 | 1.8 | 0.7 | - | 2.8 |
| Disposals and write-offs[1] | - | - | (0.9) | - | - | (0.9) |
| At 31 December 2019 | 0.9 | 0.4 | 4.7 | 0.7 | - | 6.7 |
| **Charged in year** | **0.2** | **0.2** | **1.7** | **0.8** | **-** | **2.9** |
| **Disposals and write-offs[1]** | **-** | **-** | **(2.7)** | **-** | **-** | **(2.7)** |
| **At 31 December 2020** | **1.1** | **0.6** | **3.7** | **1.5** | **-** | **6.9** |
| **Net book value** | | | | | | |
| **At 31 December 2020** | **10.4** | **1.9** | **4.1** | **4.0** | **0.1** | **20.5** |
| At 31 December 2019 | 10.6 | 1.8 | 4.5 | 4.2 | 0.1 | 21.2 |

[1] During the year the Company wrote off fully depreciated assets.

# OneSavings Bank plc
## Notes to the Financial Statements (continued)
For the year ended 31 December 2020

### 30. Intangible assets

| Group | Development costs £m | Computer software and licences £m | Assets arising on consolidation[2] £m | Total £m |
|---|---|---|---|---|
| **Cost** | | | | |
| At 1 January 2019 | - | 13.6 | - | 13.6 |
| Additions | 0.5 | 3.8 | - | 4.3 |
| CCFS Combination | - | - | 23.6 | 23.6 |
| Disposals and write-offs[1] | - | (2.0) | - | (2.0) |
| At 31 December 2019 | 0.5 | 15.4 | 23.6 | 39.5 |
| **Additions** | **1.8** | **2.6** | **-** | **4.4** |
| **Disposals and write-offs[1]** | **-** | **(1.3)** | **-** | **(1.3)** |
| **At 31 December 2020** | **2.3** | **16.7** | **23.6** | **42.6** |
| | | | | |
| **Amortisation** | | | | |
| At 1 January 2019 | - | 5.8 | - | 5.8 |
| Charged in year | - | 3.0 | 1.3 | 4.3 |
| Disposals and write-offs[1] | - | (2.0) | - | (2.0) |
| At 31 December 2019 | - | 6.8 | 1.3 | 8.1 |
| **Charged in year** | **0.1** | **3.6** | **4.5** | **8.2** |
| **Impairment in the year** | **-** | **-** | **7.0** | **7.0** |
| **Disposals and write-offs[1]** | **-** | **(1.3)** | **-** | **(1.3)** |
| **At 31 December 2020** | **0.1** | **9.1** | **12.8** | **22.0** |
| | | | | |
| **Net book value** | | | | |
| **At 31 December 2020** | **2.2** | **7.6** | **10.8** | **20.6** |
| At 31 December 2019 | 0.5 | 8.6 | 22.3 | 31.4 |

[1] During the year the Group wrote off fully amortised assets.
[2] Assets arising on consolidation comprise broker relationships of £5.8m (2019: £16.1m), technology of £2.9m (2019: £3.2m), brand name of £1.2m (2019: £1.6m) and banking licence of £0.9m (2019: £1.4m). The carrying value of the intangible assets are reviewed each reporting period with a £7.0m impairment recognised in relation to broker relationships due to impacts of the COVID-19 pandemic.

**30. Intangible assets** (continued)

| Company | Computer software and licences £m |
|---|---|
| **Cost** | |
| At 1 January 2019 | 12.1 |
| Additions | 3.3 |
| Disposals and write-offs[1] | (1.9) |
| At 31 December 2019 | 13.5 |
| **Additions** | **2.2** |
| **Disposals and write-offs[1]** | **(1.0)** |
| **At 31 December 2020** | **14.7** |
| | |
| **Amortisation** | |
| At 1 January 2019 | 5.0 |
| Charged in year | 2.7 |
| Disposals and write-offs[1] | (1.9) |
| At 31 December 2019 | 5.8 |
| **Charged in year** | **2.9** |
| **Disposals and write-offs[1]** | **(1.0)** |
| **At 31 December 2020** | **7.7** |
| | |
| **Net book value** | |
| **At 31 December 2020** | **7.0** |
| At 31 December 2019 | 7.7 |

[1] During the year the Company wrote off fully amortised assets.

### 31. Investments in subsidiaries, intercompany loans and transactions with related parties

The balances between the Company and its subsidiaries at the reporting date are summarised in the table below:

| | Shares in subsidiary undertakings £m | Intercompany loans receivable £m | Intercompany loans payable £m |
|---|---|---|---|
| At 1 January 2019 | 1.8 | 1,898.9 | (262.4) |
| Additions | - | 1,062.2 | (378.9) |
| CCFS Combination | 707.1 | - | (3.6) |
| Repayments | - | (40.6) | 1.0 |
| At 31 December 2019 | 708.9 | 2,920.5 | (643.9) |
| Additions | **-** | **53.4** | **(6.2)** |
| Repayments | **-** | **(545.5)** | **612.2** |
| **At 31 December 2020** | **708.9** | **2,428.4** | **(37.9)** |

The Company assesses intercompany loans receivable for impairment.

A list of the Company's direct subsidiaries for 2020 is shown below:

| **At 31 December 2020**<br>**Direct investments** | Activity | Registered office | Ownership |
|---|---|---|---|
| Charter Court Financial Services Group Plc | Holding company | Charter Court | 100% |
| Easioption Limited | Holding company | Reliance House | 100% |
| Guernsey Home Loans Limited | Mortgage provider | Reliance House | 100% |
| Guernsey Home Loans Limited (Guernsey) | Mortgage provider | Guernsey | 100% |
| Heritable Development Finance Limited | Mortgage originator and servicer | Reliance House | 100% |
| Interbay Group Holdings Limited | Holding company | Reliance House | 100% |
| Jersey Home Loans Limited | Mortgage provider | Reliance House | 100% |
| Jersey Home Loans Limited (Jersey) | Mortgage provider | Jersey | 100% |
| OSB India Private Limited | Back office processing | India | 100% |
| Prestige Finance Limited | Mortgage originator and servicer | Reliance House | 100% |
| Reliance Property Loans Limited | Mortgage provider | Reliance House | 100% |
| Rochester Mortgages Limited | Mortgage provider | Reliance House | 100% |

The Company holds ordinary shares in all its direct subsidiaries.

OSB India Private Limited is owned 70.28% by the Company, 29.72% by Easioption Limited and 0.001% by Reliance Property Loans Limited.

**31. Investments in subsidiaries, intercompany loans and transactions with related parties** (continued)

A list of the Company's indirect subsidiaries for 2020 is shown below:

| At 31 December 2020 Indirect investments | Activity | Registered office | Ownership |
|---|---|---|---|
| 5D Finance Limited | Mortgage servicer | Reliance House | 100% |
| Broadlands Finance Limited | Mortgage administration services | Charter Court | 100% |
| Canterbury Finance No.2 plc | Special purpose vehicle | Churchill Place | - |
| Canterbury Finance No.3 plc | Special purpose vehicle | Churchill Place | - |
| Charter Court Financial Services Limited | Mortgage lending and deposit taking | Charter Court | 100% |
| Charter Mortgages Limited | Mortgage administration and analytical services | Charter Court | 100% |
| CMF 2020-1 plc | Special purpose vehicle | Churchill Place | - |
| CML Warehouse Number 1 Limited | Special purpose vehicle | Bartholomew | - |
| CML Warehouse Number 2 Limited | Special purpose vehicle | Churchill Place | - |
| Exact Mortgage Experts Limited | Group service company | Charter Court | 100% |
| Inter Bay Financial I Limited | Holding company | Reliance House | 100% |
| Inter Bay Financial II Limited | Holding company | Reliance House | 100% |
| InterBay Asset Finance Limited | Asset finance and mortgage provider | Reliance House | 100% |
| Interbay Funding, Ltd | Mortgage servicer | Reliance House | 100% |
| Interbay Holdings Ltd | Holding company | Reliance House | 100% |
| Interbay ML, Ltd | Mortgage provider | Reliance House | 100% |
| Precise Mortgage Funding 2014-1 plc | Special purpose vehicle | Great St. Helen's | - |
| Precise Mortgage Funding 2014-2 plc | Special purpose vehicle | Great St. Helen's | - |
| Precise Mortgage Funding 2015-1 plc | Special purpose vehicle | Great St. Helen's | - |
| Precise Mortgage Funding 2015-3R plc | Special purpose vehicle | Great St. Helen's | - |

All investments in subsidiaries are of ordinary shares.

Special purpose vehicles which the Group controls are treated as subsidiaries for accounting purposes.

All of the entities listed above have been consolidated into the Group's consolidated financial statements.

All of the above investments are reviewed annually for impairment. Based on assessment of the future cash flows of each entity no impairment has been recognised.

## 31. Investments in subsidiaries, intercompany loans and transactions with related parties (continued)

A list of the Company's direct subsidiaries for 2019 is shown below:

| At 31 December 2019<br>Direct investments | Activity | Registered Office | Ownership |
|---|---|---|---|
| Charter Court Financial Services Group plc | Holding company | Charter Court | 100% |
| Easioption Limited | Holding company | Reliance House | 100% |
| Guernsey Home Loans Limited | Mortgage provider | Reliance House | 100% |
| Guernsey Home Loans Limited (Guernsey) | Mortgage provider | Guernsey | 100% |
| Heritable Development Finance Limited | Mortgage originator and servicer | Reliance House | 100% |
| Interbay Group Holdings Limited | Holding company | Reliance House | 100% |
| Jersey Home Loans Limited | Mortgage provider | Reliance House | 100% |
| Jersey Home Loans Limited (Jersey) | Mortgage provider | Jersey | 100% |
| OSB India Private Limited | Back office processing | India | 100% |
| Prestige Finance Limited | Mortgage originator and servicer | Reliance House | 100% |
| Reliance Property Loans Limited | Mortgage provider | Reliance House | 100% |
| Rochester Mortgages Limited | Mortgage provider | Reliance House | 100% |

### 31. Investments in subsidiaries, intercompany loans and transactions with related parties (continued)

A list of the Company's indirect subsidiaries for 2019 is shown below:

At 31 December 2019

| Indirect investments | Activity | Registered office | Ownership |
|---|---|---|---|
| 5D Finance Limited | Mortgage servicer | Reliance House | 100% |
| Broadlands Finance Limited | Mortgage administration services | Charter Court | 100% |
| Canterbury Finance No.1 plc | Special purpose vehicle | Reliance House | - |
| Charter Court Financial Services Limited | Mortgage lending and deposit taking | Charter Court | 100% |
| Charter Mortgages Limited | Mortgage administration and analytical services | Charter Court | 100% |
| CMF 2020-1 plc1 | Special purpose vehicle | Canada Square, London | - |
| CML Warehouse Number 1 Limited | Special purpose vehicle | Great St. Helen's,London | - |
| CML Warehouse Number 2 Limited | Special purpose vehicle | Great St. Helen's,London | - |
| Exact Mortgage Experts Limited | Group service company | Charter Court | 100% |
| Inter Bay Financial I Limited | Holding company | Reliance House | 100% |
| Inter Bay Financial II Limited | Holding company | Reliance House | 100% |
| InterBay Asset Finance Limited | Asset finance and mortgage provider | Reliance House | 100% |
| Interbay Funding, Ltd | Mortgage servicer | Reliance House | 100% |
| InterBay Holdings Ltd | Holding company | Reliance House | 100% |
| Interbay ML, Ltd | Mortgage provider | Reliance House | 100% |
| Precise Mortgage Funding 2014-1 plc | Special purpose vehicle | Great St. Helen's,London | - |
| Precise Mortgage Funding 2014-2 plc | Special purpose vehicle | Great St. Helen's,London | - |
| Precise Mortgage Funding 2015-1 plc | Special purpose vehicle | Great St. Helen's,London | - |
| Precise Mortgage Funding 2015-3R plc | Special purpose vehicle | Great St. Helen's,London | - |
| Precise Mortgage Funding 2018-1B plc | Special purpose vehicle | Great St. Helen's,London | - |
| Precise Mortgage Funding 2018-2B plc | Special purpose vehicle | Great St. Helen's,London | - |
| Precise Mortgage Funding 2020-1B plc2 | Special purpose vehicle | Canada Square, London | - |

The following are the registered offices of the subsidiaries:

Bartholomew - 1 Bartholomew Lane, London, England, EC2N 2AX
Charter Court - 2 Charter Court, Broadlands, Wolverhampton, WV10 6TD
Churchill Place – 5 Churchill Place, 10th Floor, London, E14 5HU
Guernsey – 1st Floor, Tudor House, Le Bordage, St Peter Port, Guernsey, GY1 1DB
Great St. Helen's,London - 35 Great St. Helen's, London, EC3A 6AP
India - Salarpuria Magnificia No. 78, 9th & 10th floor, Old Madras Road, Bangalore, India, 560016.
Jersey - 26 New Street, St Helier, Jersey, JE2 3RA
Reliance House – Reliance House, Sun Pier, Chatham, Kent, ME4 4ET

**31. Investments in subsidiaries, intercompany loans and transactions with related parties (continued)**

The transactions between the Company and its subsidiaries are disclosed below:

| | 2020 | | 2019 | |
|---|---|---|---|---|
| | Charged by/(to) the Company during the year | Balance due to/(by) the Company | Charged by/(to) the Company during the year | Balance due to/(by) the Company |
| **Direct investments** | £m | £m | £m | £m |
| Charter Court Financial Services Group plc | - | - | - | (3.6) |
| Easioption Limited | - | 0.5 | - | 0.5 |
| Guernsey Home Loans Limited | 0.2 | 8.8 | 0.2 | 9.6 |
| Guernsey Home Loans Limited (Guernsey) | 0.5 | 23.9 | 0.7 | 29.9 |
| Heritable Development Finance Limited | (1.3) | (0.6) | (1.8) | (0.9) |
| Jersey Home Loans Limited | - | 2.5 | - | 2.5 |
| Jersey Home Loans Limited (Jersey) | 2.1 | 111.6 | 2.9 | 123.2 |
| OSB India Private Limited | (9.3) | 8.0 | (8.9) | 9.0 |
| Prestige Finance Limited | (3.7) | (0.8) | (2.8) | (0.2) |
| Reliance Property Loans Limited | 0.1 | 3.3 | 0.1 | 3.4 |
| **Indirect investments** | | | | |
| Charter Court Financial Services Limited | 4.3 | 4.1 | - | - |
| 5D Finance Limited | - | 0.6 | - | 0.5 |
| Canterbury Finance No.1 plc | - | - | - | 3.7 |
| Inter Bay Financial I Limited | 0.3 | 19.6 | 0.4 | 19.3 |
| Inter Bay Financial II Limited | 0.6 | (5.6) | 0.4 | 125.7 |
| InterBay Asset Finance Limited | 1.1 | 94.9 | 0.5 | 46.0 |
| Interbay Funding, Ltd | (12.0) | (30.9) | (7.6) | (639.2) |
| Interbay ML, Ltd | 47.1 | 2,150.6 | 37.5 | 2,547.2 |
| | **30.0** | **2,390.5** | 21.6 | 2,276.6 |

In addition to the above subsidiaries, the Company has transactions with Kent Reliance Provident Society (KRPS), one of its founding shareholders. KRPS runs member engagement forums for the Company. In exchange, the Company provides KRPS with various services including IT, finance and other support functions. During the year the Company was charged for services provided by KRPS amounting to £0.2m (2019: £0.2m). As at 31 December 2020, KRPS had £0.3m (2019: £0.3m) deposited with the Company.

All related party transactions were made on terms equivalent to those that prevail in arm's length transactions. During the year there were no related party transactions between the key management personnel and the Company other than as described below.

### 31. Investments in subsidiaries, intercompany loans and transactions with related parties (continued)

**Transactions with key management personnel**

During the year the Board extended the definition of key management personnel to comprise the Directors and Executive team, previously Directors only. Directors' remuneration is disclosed in note 10 and in the OSB GROUP PLC Annual Report on Remuneration. The table below shows the Executive team's aggregate remuneration:

| | **Group 2020 £'000** | Group 2019 £'000 |
|---|---|---|
| Short-term employee benefits | **3,743** | 4,282 |
| Post-employment benefits | **49** | 45 |
| Share-based payments | **501** | 1,888 |
| | **4,293** | 6,215 |

No loans were issued to related parties during 2020 (2019: nil).

Key management personnel and connected persons held deposits with the Group of £1.4m (2019: £1.8m).

### 32. Amounts owed to credit institutions

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| BoE TFS | **2,568.6** | 2,632.8 | **1,500.4** | 1,502.8 |
| BoE TFSME | **1,000.1** | - | **400.1** | - |
| BoE ILTR | **-** | 290.6 | **-** | 160.5 |
| Warehouse funding | **-** | 93.6 | **-** | - |
| Commercial repo | **0.1** | 41.4 | **-** | - |
| Cash margin received | **-** | 8.0 | **-** | 7.8 |
| Loans from credit institutions | **1.4** | 2.4 | **-** | - |
| | **3,570.2** | 3,068.8 | **1,900.5** | 1,671.1 |

### 33. Amounts owed to retail depositors

The table below shows the Group's retail depositors by operating segment, where the OSB segment also represents the Company's retail depositors:

| | **OSB 2020 £m** | **CCFS 2020 £m** | **Total 2020 £m** | OSB 2019 £m | CCFS 2019 £m | Total 2019 £m |
|---|---|---|---|---|---|---|
| Fixed rate deposits | **6,275.6** | **4,781.4** | **11,057.0** | 5,617.9 | 4,907.6 | 10,525.5 |
| Variable rate deposits | **3,429.7** | **2,116.4** | **5,546.1** | 3,817.9 | 1,911.6 | 5,729.5 |
| | **9,705.3** | **6,897.8** | **16,603.1** | 9,435.8 | 6,819.2 | 16,255.0 |

### 34. Amounts owed to other customers

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| Fixed rate deposits | **46.0** | 26.0 | **5.8** | 8.9 |
| Variable rate deposits | **26.9** | 3.7 | **-** | - |
| | **72.9** | 29.7 | **5.8** | 8.9 |

### 35. Debt securities in issue

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| Asset backed loan notes at amortised cost | **421.9** | 296.3 |
| | | |
| Amount due for settlement within 12 months | **-** | 40.1 |
| Amount due for settlement after 12 months | **421.9** | 256.2 |
| | **421.9** | 296.3 |

The asset-backed loan notes are secured on fixed and variable rate mortgages and are redeemable in part from time to time, but such redemptions are limited to the net principal received from borrowers in respect of underlying mortgage assets. The maturity date of the funds matches the contractual maturity date of the underlying mortgage assets. It is likely that a large proportion of the underlying mortgage assets and, therefore these notes, will be repaid within five years.

Asset-backed loan notes may all be repurchased by the Group at any interest payment date on or after the call dates, or at any interest payment date when the current balance of the mortgages outstanding is less than or equal to 10% of the principal amount outstanding on the loan notes on the date they were issued.

Interest is payable at fixed margins above LIBOR or SONIA.

As at 31 December 2020, notes were issued through the following funding vehicles:

| | Group 2020 £m | Group 2019 £m |
|---|---|---|
| CMF 2020-1 plc | **288.6** | - |
| Canterbury Finance No.3 plc | **133.3** | - |
| Canterbury Finance No.1 plc | **-** | 256.2 |
| Precise Mortgage Funding 2015-1 plc | **-** | 40.1 |
| | **421.9** | 296.3 |

### 36. Lease liabilities

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| At 1 January | **13.3** | 3.8 | **4.3** | 2.3 |
| CCFS Combination | **-** | 7.7 | **-** | - |
| New leases | **0.1** | 3.6 | **0.1** | 3.5 |
| Lease terminated | **-** | (0.8) | **-** | (0.8) |
| Lease repayments | **(2.0)** | (1.1) | **(0.6)** | (0.8) |
| Interest accruals | **0.3** | 0.1 | **0.1** | 0.1 |
| **At 31 December** | **11.7** | 13.3 | **3.9** | 4.3 |

During the year, the Group incurred expenses of £0.7m (2019: £0.7m) in relation to short-term leases and nil (2019: £0.1m) in relation to low-value assets.

### 37. Other liabilities

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| Falling due within one year: | | | | |
| Accruals | **19.7** | 23.1 | **9.9** | 11.7 |
| Deferred income | **0.6** | 1.1 | **0.6** | 1.0 |
| Other creditors | **7.5** | 10.7 | **3.3** | 4.4 |
| | **27.8** | 34.9 | **13.8** | 17.1 |

### 38. Provisions and contingent liabilities

The Financial Services Compensation Scheme (FSCS) provides protection of deposits for the customers of authorised financial services firms, should a firm collapse. FSCS protects retail deposits of up to £85k for single account holders and £170k for joint holders. As OSB and CCFS both hold banking licences, the full FSCS protection is available to customers of each bank.

The compensation paid out to consumers is initially funded through loans from the BoE and HM Treasury. In order to repay the loans and cover its costs, the FSCS charges levies on firms regulated by the PRA and the FCA. The Group is among those firms and pays the FSCS a levy based on its share of total UK deposits.

The Group has reviewed its current exposure to Payment Protection Insurance (PPI) claims, following the FCA deadline for PPI claims on 29 August 2019 and has recognised a provision of £0.3m as at 31 December 2020 (2019: £0.3m). The Group has maintained its provision for FCA conduct rules exposures of £1.2m (2019: £1.3m) to cover potential future claims.

**38. Provisions and contingent liabilities** (continued)

An analysis of the Group's and Company's FSCS and other provisions is presented below:

| Group | 2020 FSCS £m | 2020 Other regulatory provisions £m | 2020 ECL on undrawn loan facilities £m | 2020 Total £m | 2019 FSCS £m | 2019 Other regulatory provisions £m | 2019 ECL on undrawn loan facilities £m | 2019 Total £m |
|---|---|---|---|---|---|---|---|---|
| At 1 January | **(0.2)** | **1.6** | **0.2** | **1.6** | 0.1 | 1.7 | - | 1.8 |
| Refund/(paid) during the year | **0.3** | **(0.2)** | **-** | **0.1** | (0.1) | (0.1) | - | (0.2) |
| Charge/(credit) | **-** | **0.1** | **-** | **0.1** | (0.2) | - | 0.2 | - |
| At 31 December | **0.1** | **1.5** | **0.2** | **1.8** | (0.2) | 1.6 | 0.2 | 1.6 |

| Company | 2020 FSCS £m | 2020 Other regulatory provisions £m | 2020 ECL on undrawn loan facilities £m | 2020 Total £m | 2019 FSCS £m | 2019 Other regulatory provisions £m | 2019 ECL on undrawn loan facilities £m | 2019 Total £m |
|---|---|---|---|---|---|---|---|---|
| At 1 January | **(0.1)** | **1.6** | **0.1** | **1.6** | 0.1 | 1.7 | - | 1.8 |
| Refund/(paid) during the year | **0.2** | **(0.2)** | **-** | **-** | (0.1) | (0.1) | - | (0.2) |
| Charge/(credit) | **-** | **-** | **-** | **-** | (0.1) | - | 0.1 | - |
| At 31 December | **0.1** | **1.4** | **0.1** | **1.6** | (0.1) | 1.6 | 0.1 | 1.6 |

In January 2020, the Group was contacted by the FCA in connection with a multi-firm thematic review into forbearance measures adopted by lenders in respect of a portion of the mortgage market. The Group is responding to information requests from the FCA. It is not possible to reliably predict or estimate the outcome of the review, if any, on the Group and is a contingent liability.

**39. Subordinated liabilities**

| | **Group and Company 2020 £m** | Group and Company 2019 £m |
|---|---|---|
| At 1 January | **10.6** | 10.8 |
| Repayment of debt at maturity | **(0.1)** | (0.2) |
| At 31 December | **10.5** | 10.6 |

**39. Subordinated liabilities** (continued)

The Group's and Company's outstanding subordinated liabilities are summarised below:

| | Group and Company 2020 £m | Group and Company 2019 £m |
|---|---|---|
| Linked to LIBOR: | | |
| Floating rate subordinated loans 2022 (LIBOR +5%) | **0.1** | 0.2 |
| Floating rate subordinated loans 2022 (LIBOR +2%) | **0.2** | 0.2 |
| Fixed rate: | | |
| Subordinated liabilities 2024 (7.45%) | **10.2** | 10.2 |
| | **10.5** | 10.6 |

The fixed rate subordinated liabilities are repayable at the dates stated or earlier, in full, at the option of the Group with the prior consent of the PRA. All subordinated liabilities are denominated in Pounds Sterling and are unlisted.

The rights of repayment of the holders of these subordinated liabilities are subordinated to the claims of all depositors and all other creditors.

**40. Perpetual subordinated bonds**

| | Group and Company 2020 £m | Group and Company 2019 £m |
|---|---|---|
| Sterling Perpetual Subordinated Bonds (4.5991%) | **22.3** | 22.3 |
| Sterling Perpetual Subordinated Bonds (4.6007%) | **15.3** | 15.3 |
| | **37.6** | 37.6 |

The bonds are listed on the London Stock Exchange.

The 4.5991% bonds were issued with a clause in the terms relating to the Board's discretion over the payment of coupons being conditional and are therefore classified as financial liabilities. The coupon rate is 4.5991% until the next reset date on 7 March 2021.

The 4.6007% bonds were issued with no discretion over the payment of interest and may not be settled in the Group's own equity. They are therefore classified as financial liabilities. The coupon rate is 4.6007% until the next reset date on 27 August 2024.

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

### 41. Reconciliation of cash flows for financing activities

The tables below show a reconciliation of the Group's and Company's liabilities classified as financing activities within the Statement of Cash Flows:

| Group | Amounts owed to credit institutions (see note 32) £m | Debt securities in issue (see note 35) £m | Subordinated liabilities (see note 39) £m | PSBs (see note 40) £m | Total £m |
|---|---|---|---|---|---|
| **At 31 December 2018** | 1,584.0 | - | 10.8 | 37.6 | 1,632.4 |
| **Cash movements:** | | | | | |
| Principal drawdowns | 587.7 | 285.0 | - | - | 872.7 |
| Principal repayments | (273.7) | (64.6) | (0.2) | - | (338.5) |
| **Non-cash movement:** | | | | | |
| CCFS Combination | 1,168.4 | 75.1 | - | - | 1,243.5 |
| Accrued interest movement | 2.4 | 0.8 | - | - | 3.2 |
| **At 31 December 2019** | 3,068.8 | 296.3 | 10.6 | 37.6 | 3,413.3 |
| **Cash movements:** | | | | | |
| Principal drawdowns | **1,505.0** | **486.2** | **-** | **-** | **1,991.2** |
| Principal repayments | **(998.9)** | **(104.6)** | **(0.1)** | **-** | **(1,103.6)** |
| Deconsolidation of special purpose vehicles | **-** | **(256.2)** | **-** | **-** | **(256.2)** |
| **Non-cash movements:** | | | | | |
| Accrued interest movement | **(4.7)** | **0.2** | **-** | **-** | **(4.5)** |
| **At 31 December 2020** | **3,570.2** | **421.9** | **10.5** | **37.6** | **4,040.2** |

| Company | Amounts owed to credit institutions (see note 32) £m | Deemed Loans (see note 20) £m | Subordinated liabilities (see note 39) £m | PSBs (see note 40) £m | Total £m |
|---|---|---|---|---|---|
| **At 31 December 2018** | 1,584.0 | - | 10.8 | 37.6 | 1,632.4 |
| **Cash movements:** | | | | | |
| Principal drawdowns | 316.8 | 285.0 | - | - | 601.8 |
| Principal repayments | (230.0) | (44.8) | (0.2) | - | (275.0) |
| **Non-cash movement:** | | | | | |
| Accrued interest movement | 0.3 | - | - | - | 0.3 |
| **At 31 December 2019** | 1,671.1 | 240.2 | 10.6 | 37.6 | 1,959.5 |
| **Cash movements:** | | | | | |
| Principal drawdowns | **905.0** | **154.6** | **-** | **-** | **1,059.6** |
| Principal repayments | **(672.8)** | **(91.8)** | **(0.1)** | **-** | **(764.7)** |
| **Non-cash movements:** | | | | | |
| Deconsolidation of special purpose vehicles | **-** | **(236.8)** | **-** | | **(236.8)** |
| Accrued interest movement | **(2.8)** | **-** | **-** | **-** | **(2.8)** |
| **At 31 December 2020** | **1,900.5** | **66.2** | **10.5** | **37.6** | **2,014.8** |

### 42. Share capital

| Ordinary shares | Number of shares authorised and fully paid | Nominal value £m | Premium £m |
|---|---|---|---|
| At 1 January 2019 | 244,487,537 | 2.4 | 158.8 |
| CCFS Combination | 199,643,055 | 2.0 | 705.1 |
| Shares issued under OSB employee share plans | 1,312,862 | 0.1 | 0.3 |
| At 31 December 2019 | 445,443,454 | 4.5 | 864.2 |
| Shares issued under OSB employee share plans | **1,860,744** | **-** | **2.6** |
| Cancellation of OneSavings Bank plc £0.01 share capital and share premium | **(447,304,198)** | **(4.5)** | **(866.8)** |
| Issuance of OneSavings Bank plc £0.01 share capital | **447,304,198** | **4.5** | **-** |
| **At 31 December 2020** | **447,304,198** | **4.5** | **-** |

As part of the insertion of OSBG, the existing listed share capital and share premium of the Company was cancelled on 27 November 2020 and the share capital and share premium amounts of the Company transferred to retained earnings. The Company subsequently issued the same number of new unlisted £0.01 ordinary shares from retained earnings to OSBG.

The holders of ordinary shares are entitled to receive dividends as declared from time to time, and are entitled to one vote per share at meetings of the Company. All ordinary shares rank equally with regard to the Company's residual assets.

All ordinary shares issued in the current and prior year were fully paid.

### 43. Other reserves

The Group's and Company's other reserves are as follows:

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| Share-based payment | **7.8** | 5.6 | **6.7** | 5.3 |
| Capital contribution | **-** | 6.5 | **-** | 6.2 |
| Transfer | **-** | (12.8) | **-** | (15.2) |
| Own shares | **-** | (3.7) | **-** | (3.7) |
| FVOCI | **1.0** | 0.5 | **(0.1)** | - |
| Foreign exchange | **(1.0)** | (1.0) | **-** | - |
| Equity bonds | **60.0** | 60.0 | **60.0** | 60.0 |
| | **67.8** | 55.1 | **66.6** | 52.6 |

**Capital contribution**
The capital contribution reserve relates to one-off nil price share awards of shares in OSB granted to certain senior managers on OSB's admission to the London Stock Exchange in June 2014. The awards were granted by OSB's major shareholder at the time of the IPO. The reserve was transferred to retained earnings during the year following distribution of all the awards.

**43. Other reserves** (continued)

**Transfer reserve**
The transfer reserve in 2019 represented the difference between the value of net assets transferred to the Group from Kent Reliance Building Society in 2011 and the value of shares issued to the A ordinary shareholders. The net assets transferred were predominantly savings and mortgages that have now either been replaced by new products, which is a derecognition event of the initial net asset, or are no longer with the Group. The balance was therefore transferred to retained earnings in 2020.

**Own shares**
Following the insertion of OSB GROUP plc as the listed entity of the Group, whose shares will settle obligations under share-based payment awards, the Company ceased adopting the look-through approach for the EBT from 27 November 2020.

**FVOCI reserve**
The FVOCI reserve represents the cumulative net change in the fair value of investment securities measured at FVOCI.

**Foreign exchange**
The foreign exchange reserve relates to the revaluation of the Group's Indian subsidiary, OSB India Private Limited.

**Additional Tier 1 securities**
Additional Tier 1 securities comprise £60.0m of Fixed Rate Resetting Perpetual Subordinated Contingent Convertible Securities that qualify as Additional Tier 1 capital under the Capital Requirements Directive and Regulation (CRD IV). The securities will be subject to full conversion into ordinary shares of OSB in the event that its CET1 capital ratio falls below 7%. The AT1 securities will pay interest at a rate of 9.125% per annum until the first reset date of 25 May 2022, with the reset interest rate equal to 835.9 basis points over the five-year semi-annual mid-swap rate for such a period. Interest is paid semi-annually on 25 May and 25 November. OSB may, at any time, cancel any interest payment at its full discretion and must cancel interest payments in certain circumstances specified in the terms and conditions of the AT1 securities. The AT1 securities are perpetual with no fixed redemption date. OSB may, in its discretion and subject to satisfying certain conditions, redeem all (but not some) of the AT1 securities at the principal amount outstanding plus any accrued but unpaid interest from the first reset date and on any interest payment date thereafter.

**44. Financial commitments and guarantees**

a) The Group did not have any contracted or anticipated capital expenditure commitments not provided for as at 31 December 2020 (2019: nil).

b) The Group's minimum lease commitments under operating leases not subject to IFRS 16 are summarised in the table below:

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| Land and buildings: due within: | | | | |
| One year | **0.1** | 0.6 | **0.1** | 0.1 |
| | **0.1** | 0.6 | **0.1** | 0.1 |

**44. Financial commitments and guarantees** (continued)

c) Undrawn loan facilities:

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| OSB mortgages | **547.2** | 639.2 | **522.0** | 459.7 |
| CCFS mortgages | **420.8** | 568.1 | **-** | - |
| Asset Finance | **11.5** | 3.6 | **-** | - |
| | **979.5** | 1,210.9 | **522.0** | 459.7 |

Undrawn loan facilities are approved loan applications which have not yet been exercised. They are payable on demand and are usually drawn down or expire within three months.

d) The Group did not have any issued financial guarantees as at 31 December 2020 (2019: nil).

**45. Risk management**

**Overview**

Financial instruments form the vast majority of the Group's and Company's assets and liabilities. The Group manages risk on a consolidated basis and risk disclosures that follow are provided on this basis.

**Types of financial instrument**

Financial instruments are a broad definition which includes financial assets, financial liabilities and equity instruments. The main financial assets of the Group are loans to customers and liquid assets, which in turn consist of cash in the BoE call accounts, call accounts with other credit institutions and UK and EU sovereign debt. These are funded by a combination of financial liabilities and equity instruments. Financial liability funding comes predominantly from retail deposits and drawdowns under the BoE TFS, TFSME and ILTR, supported by debt securities, subordinated debt, wholesale and other funding. Equity instruments include own shares and AT1 securities meeting the equity classification criteria. The Group's main activity is mortgage lending; it raises funds or invests in particular types of financial assets to meet customer demand and manage the risks arising from its operations. The Group does not trade in financial instruments for speculative purposes.

The Group uses derivative instruments to manage its financial risks. Derivative financial instruments (derivatives) are financial instruments whose value changes in response to changes in underlying variables such as interest rates. The most common derivatives are futures, forwards and swaps. Of these, the Group only uses swaps.

Derivatives are used by the Group solely to reduce (hedge) the risk of loss arising from changes in market rates. Derivatives are not used for speculative purposes.

**Types of derivatives and uses**

The derivative instruments used by the Group in managing its risk exposures are interest rate swaps. Interest rate swaps convert fixed interest rates to floating or vice versa. As with other derivatives, the underlying product is not sold and payments are based on notional principal amounts.

**45. Risk management** (continued)

Unhedged fixed rate liabilities create the risk of paying above-the-market rate if interest rates subsequently decrease. Unhedged fixed rate mortgages and liquid assets bear the opposite risk of income below-the-market rate when rates go up. While fixed rate assets and liabilities naturally hedge each other to a certain extent, this hedge is usually never perfect because of maturity mismatches and principal amounts.

The Group uses swaps to convert its instruments, such as mortgages, deposits and liquid assets, from fixed or base rate-linked rates to reference linked variable rates. This ensures a guaranteed margin between the interest income and interest expense, regardless of changes in the market rates.

**Transition away from LIBOR**

The PRA and FCA have continued to encourage banks to transition away from using LIBOR as a benchmark in all operations before the end of 2021. Throughout the UK banking sector, LIBOR remains a key benchmark and, for each market impacted, solutions to this issue are progressing through various industry bodies. The Group has closely monitored the market and the output from the various industry working groups managing the transition to new benchmark interest rates. This includes announcements made by LIBOR regulators (including the FCA) regarding the transition from GBP LIBOR to SONIA. The FCA has made clear that, at the end of 2021, it will no longer seek to persuade, or compel, banks to submit to LIBOR.

In 2018, the Group set up an internal working group, comprising all of the key business lines that are involved with this change, including work streams covering risk management, contracts, systems and conduct risk considerations, with strong oversight from the Compliance and Risk functions. The programme is overseen by the LIBOR Transition Working Group which reports into ALCO. Risk assessments have been completed to ensure this process is managed in a measured and controlled manner.

The Group no longer offers any LIBOR-linked loans and is transitioning new and back book swaps from a GBP LIBOR to a SONIA basis. The Group has no exposure to existing IBORs, other than to GBP LIBOR.

The Group adopted the Phase 1 amendments 'Interest Rate Benchmark reform: Amendments to IFRS 9/IAS 39 and IFRS 7'. These amendments modified specific hedge accounting requirements to allow hedge accounting to continue for affected hedges during the period of uncertainty before the hedged items or hedging instruments are amended as a result of the interest rate benchmark reform. The Group has not early adopted 'Interest Rate Benchmark Reform – Phase 2: Amendments to IFRS 9 Financial Instruments, IAS 39 Financial Instruments: Recognition and Measurement, IFRS 7 Financial Instruments: Disclosures, IFRS 4 Insurance Contracts and IFRS 16 Leases' which was issued in August 2020. These amendments will become mandatory for annual reporting periods beginning on or after 1 January 2021. Adopting these amendments will enable the Group to reflect the effects of transitioning from IBOR to alternative benchmark interest rates (also referred to as 'risk free rates' or RFRs) without giving rise to accounting impacts that would not provide useful information to users of financial statements.

The application of the Phase 1 amendments impacts the Group's accounting in the following ways. Hedge accounting relationships will continue even when, for IBOR fair value hedges, the benchmark interest rate component may not be separately identifiable.

The Group will not discontinue portfolio hedge accounting should the retrospective assessment of hedge effectiveness for a hedging relationship, that is subject to the interest rate benchmark reform, fall outside the 80-125 per cent range. For portfolio hedging relationships that are not subject to the interest rate benchmark reform the entity continues to cease hedge accounting if retrospective effectiveness is outside the 80-125 per cent range.

**45. Risk management** (continued)

The Group will continue to apply the Phase 1 amendments to IFRS 9/IAS 39 until the uncertainty arising from the interest rate benchmark reform, with respect to the timing and the amount of the underlying cash flows to which the Group is exposed, ends. The Group expects this uncertainty will continue until the Group's contracts that reference IBORs are amended to specify the date on which the interest rate benchmark will be replaced and the basis for the cash flows of the alternative benchmark rate are determined, including any fixed spread.

The phase 1 relief does not extend to the requirement that the designated interest rate risk component continues to be reliably measurable and if the risk component is no longer reliably measurable, the hedging relationship is discontinued. The Group has determined that GBP LIBOR interest rate risk components continue to be reliably measurable.

*Mortgages*
New loan product transition was completed for CCFS in 2019 and OSB launched new BBR-linked products during 2020 to replace loans with a LIBOR component.

At 31 December 2020, the Group had £8,001.7m of GBP LIBOR-linked lending, including funding lines and mortgages that will revert to LIBOR in the future, out of a total mortgage balance of £19,257.1m. The Group continues to work through the back book transition for existing loans which is planned to be completed before the end of 2021.

*Investment securities*
At 31 December 2020, the Group had £118.7m of GBP LIBOR-linked investment securities, comprising RMBS loan notes and the Group is monitoring the issuers' intentions in respect of IBOR transition with £40.0m transferred to SONIA coupons after the year end.

*Retail savings*
None of the OSB or CCFS current or back book retail savings products have a GBP LIBOR component within the product.

Additional Tier 1 securities
The £60.0m Additional Tier 1 securities pay interest at a rate of 9.125% per annum until the first reset date on 25 May 2022. In advance of the reset date, the Group will agree the benchmark rate to be adopted.

*Derivatives*
As at 31 December 2020, the derivatives in the CCFS segment have all transitioned across to a SONIA basis with the OSB segment yet to complete. The total nominal amount of the Group's derivatives was £19,080.2m, of which the Group had GBP LIBOR-linked swaps with a nominal value of £8,020.0m and a fair value liability of £89.1m hedging assets and liabilities. It is planned that existing derivatives will be actively transitioned onto alternative benchmarks before the end of 2021.

**Types of risk**

The principal financial risks to which the Group is exposed are credit, liquidity and market risks, the latter comprising interest and exchange rate risk. In addition to financial risks, the Group is exposed to various other risks, most notably operational, conduct and regulatory, which are covered in the Risk review on pages 32 to 62.

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

**45. Risk management** (continued)

**Credit risk**

Credit risk is the risk that losses may arise as a result of the Group's borrowers or market counterparties failing to meet their obligations to repay.

The Group has adopted the Standardised Approach for assessment of credit risk regulatory capital requirements. This approach considers risk weightings as defined under Basel II and Basel III principles.

The classes of financial instruments to which the Group is most exposed are loans and advances to customers, loans and advances to credit institutions, cash in the BoE call account, call and current accounts with other credit institutions and investment securities. The maximum credit risk exposure equals the total carrying amount of the above categories plus off-balance sheet undrawn committed mortgage facilities.

**Credit risk - loans and advances to customers**

Credit risk associated with mortgage lending is largely driven by the housing market and level of unemployment. A recession and/or high interest rates could cause pressure within the market, resulting in rising levels of arrears and repossessions.

All loan applications are assessed with reference to the Group's Lending Policy. Changes to the policy are approved by the Group Risk Committee, with mandates set for the approval of loan applications.

The Group Credit Committee and the ALCO regularly monitor lending activity, taking appropriate actions to reprice products and adjust lending criteria in order to control risk and manage exposure. Where necessary and appropriate, changes to the Lending Policy are recommended to the Group Risk Committee.

The following tables show the Group's and Company's maximum exposure to credit risk and the impact of collateral held as security, capped at the gross exposure amount, by impairment stage. Capped collateral excludes the impact of forced sale discounts and costs to sell.

| | 2020 | | | | | |
|---|---|---|---|---|---|---|
| | OSB | | CCFS | | Total | |
| | Gross carrying amount | Capped collateral held | Gross carrying amount | Capped collateral held | Gross carrying amount | Capped collateral held |
| Group | £m | £m | £m | £m | £m | £m |
| Stage 1 | 9,366.8 | 9,303.4 | 6,749.5 | 6,747.9 | 16,116.3 | 16,051.3 |
| Stage 2 | 1,363.4 | 1,359.8 | 1,327.6 | 1,327.6 | 2,691.0 | 2,687.4 |
| Stage 3 | 352.6 | 323.3 | 48.1 | 48.1 | 400.7 | 371.4 |
| Stage 3 (POCI) | 48.6 | 48.4 | 66.0 | 66.0 | 114.6 | 114.4 |
| | 11,131.4 | 11,034.9 | 8,191.2 | 8,189.6 | 19,322.6 | 19,224.5 |

**45. Risk management** (continued)

| | 2019 | | | | | |
|---|---|---|---|---|---|---|
| | OSB | | CCFS | | Total | |
| **Group** | Gross carrying amount £m | Capped collateral held £m | Gross carrying amount £m | Capped collateral held £m | Gross carrying amount £m | Capped collateral held £m |
| Stage 1 | 10,046.9 | 9,987.1 | 7,240.0 | 7,239.5 | 17,286.9 | 17,226.6 |
| Stage 2 | 442.4 | 441.8 | 307.1 | 307.0 | 749.5 | 748.8 |
| Stage 3 | 277.7 | 275.2 | 16.7 | 16.7 | 294.4 | 291.9 |
| Stage 3 (POCI) | 53.6 | 50.1 | 83.2 | 83.1 | 136.8 | 133.2 |
| | 10,820.6 | 10,754.2 | 7,647.0 | 7,646.3 | 18,467.6 | 18,400.5 |

The Group's main form of collateral held is property, based in the UK and the Channel Islands.

The Group uses indexed loan to value (LTV) ratios to assess the quality of the uncapped collateral held. Property values are updated to reflect changes in the HPI. A breakdown of loans and advances to customers by indexed LTV is as follows:

| | **2020** | | | | 2019 | | | |
|---|---|---|---|---|---|---|---|---|
| **Group** | **OSB £m** | **CCFS £m** | **Total £m** | **%** | OSB £m | CCFS £m | Total £m | % |
| **Band** | | | | | | | | |
| 0% - 50% | **1,740.3** | **419.3** | **2,159.6** | **11** | 1,732.6 | 567.8 | 2,300.4 | 12 |
| 50% - 60% | **1,462.0** | **483.3** | **1,945.3** | **10** | 1,301.8 | 612.3 | 1,914.1 | 10 |
| 60% - 70% | **2,813.4** | **1,109.3** | **3,922.7** | **20** | 2,435.7 | 1,588.5 | 4,024.2 | 22 |
| 70% - 80% | **3,942.9** | **5,144.3** | **9,087.2** | **47** | 4,182.1 | 4,236.3 | 8,418.4 | 46 |
| 80% - 90% | **879.1** | **1,033.7** | **1,912.8** | **10** | 946.0 | 641.5 | 1,587.5 | 9 |
| 90% - 100% | **105.8** | **1.3** | **107.1** | **1** | 91.1 | 0.6 | 91.7 | - |
| >100% | **187.9** | **-** | **187.9** | **1** | 131.3 | - | 131.3 | 1 |
| **Total loans before provisions** | **11,131.4** | **8,191.2** | **19,322.6** | **100** | 10,820.6 | 7,647.0 | 18,467.6 | 100 |

The table below shows the LTV banding for the OSB segments' two major lending streams:

| | **2020** | | | | 2019 | | | |
|---|---|---|---|---|---|---|---|---|
| **OSB** | **BTL/SME £m** | **Residential £m** | **Total £m** | **%** | BTL/SME £m | Residential £m | Total £m | % |
| **Band** | | | | | | | | |
| 0% - 50% | **795.7** | **944.6** | **1,740.3** | **16** | 905.9 | 826.7 | 1,732.6 | 16 |
| 50% - 60% | **1,228.1** | **233.9** | **1,462.0** | **13** | 1,062.8 | 239.0 | 1,301.8 | 12 |
| 60% - 70% | **2,602.1** | **211.3** | **2,813.4** | **25** | 2,240.2 | 195.5 | 2,435.7 | 23 |
| 70% - 80% | **3,693.4** | **249.5** | **3,942.9** | **35** | 3,993.5 | 188.6 | 4,182.1 | 38 |
| 80% - 90% | **584.5** | **294.6** | **879.1** | **8** | 621.4 | 324.6 | 946.0 | 9 |
| 90% - 100% | **89.4** | **16.4** | **105.8** | **1** | 45.1 | 46.0 | 91.1 | 1 |
| >100% | **171.4** | **16.5** | **187.9** | **2** | 114.3 | 17.0 | 131.3 | 1 |
| **Total loans before provisions** | **9,164.6** | **1,966.8** | **11,131.4** | **100** | 8,983.2 | 1,837.4 | 10,820.6 | 100 |

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# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

**45. Risk management** (continued)

The tables below show the sub-segment LTV analysis of the OSB BTL/SME lending stream:

| | 2020 | | | | |
|---|---|---|---|---|---|
| **OSB** | **Buy-to-Let £m** | **Commercial £m** | **Residential development £m** | **Funding lines £m** | **Total £m** |
| **Band** | | | | | |
| 0% - 50% | **643.3** | **80.6** | **12.5** | **59.3** | **795.7** |
| 50% - 60% | **1,040.1** | **84.3** | **64.2** | **39.5** | **1,228.1** |
| 60% - 70% | **2,407.4** | **132.0** | **56.4** | **6.3** | **2,602.1** |
| 70% - 80% | **3,411.7** | **251.3** | **-** | **30.4** | **3,693.4** |
| 80% - 90% | **370.1** | **214.4** | **-** | **-** | **584.5** |
| 90% - 100% | **54.1** | **35.3** | **-** | **-** | **89.4** |
| >100% | **117.9** | **24.0** | **-** | **29.5** | **171.4** |
| **Total loans before provisions** | **8,044.6** | **821.9** | **133.1** | **165.0** | **9,164.6** |

| | 2019 | | | | |
|---|---|---|---|---|---|
| **OSB** | Buy-to-Let £m | Commercial £m | Residential development £m | Funding lines £m | Total £m |
| **Band** | | | | | |
| 0% - 50% | 579.9 | 96.5 | 125.7 | 103.8 | 905.9 |
| 50% - 60% | 894.3 | 119.8 | 5.0 | 43.7 | 1,062.8 |
| 60% - 70% | 1,994.1 | 210.2 | 5.0 | 30.9 | 2,240.2 |
| 70% - 80% | 3,514.5 | 445.7 | - | 33.3 | 3,993.5 |
| 80% - 90% | 603.3 | 7.7 | 10.4 | - | 621.4 |
| 90% - 100% | 38.9 | 1.4 | - | 4.8 | 45.1 |
| >100% | 102.0 | 6.7 | - | 5.6 | 114.3 |
| **Total loans before provisions** | 7,727.0 | 888.0 | 146.1 | 222.1 | 8,983.2 |

### 45. Risk management (continued)

The tables below show the sub-segment LTV analysis of the OSB Residential lending stream:

| | 2020 | | | |
|---|---|---|---|---|
| OSB | First charge £m | Second charge £m | Funding lines £m | Total £m |
| **Band** | | | | |
| 0% - 50% | **835.8** | **105.1** | **3.7** | **944.6** |
| 50% - 60% | **167.2** | **64.5** | **2.2** | **233.9** |
| 60% - 70% | **151.7** | **58.1** | **1.5** | **211.3** |
| 70% - 80% | **208.1** | **39.9** | **1.5** | **249.5** |
| 80% - 90% | **274.8** | **19.3** | **0.5** | **294.6** |
| 90% - 100% | **12.4** | **3.6** | **0.4** | **16.4** |
| >100% | **10.7** | **4.9** | **0.9** | **16.5** |
| **Total loans before provisions** | **1,660.7** | **295.4** | **10.7** | **1,966.8** |

| | 2019 | | | |
|---|---|---|---|---|
| OSB | First charge £m | Second charge £m | Funding lines £m | Total £m |
| **Band** | | | | |
| 0% - 50% | 708.0 | 115.4 | 3.3 | 826.7 |
| 50% - 60% | 158.1 | 77.5 | 3.4 | 239.0 |
| 60% - 70% | 122.3 | 70.9 | 2.3 | 195.5 |
| 70% - 80% | 137.0 | 49.5 | 2.1 | 188.6 |
| 80% - 90% | 291.7 | 32.3 | 0.6 | 324.6 |
| 90% - 100% | 40.0 | 5.7 | 0.3 | 46.0 |
| >100% | 9.5 | 7.3 | 0.2 | 17.0 |
| **Total loans before provisions** | 1,466.6 | 358.6 | 12.2 | 1,837.4 |

The table below shows the LTV banding for the CCFS segments' four major lending streams:

| | 2020 | | | | | |
|---|---|---|---|---|---|---|
| CCFS | Buy-to-Let £m | Residential £m | Bridging £m | Second charge lending £m | Total £m | % |
| **Band** | | | | | | |
| 0% - 50% | **92.7** | **242.1** | **50.4** | **34.1** | **419.3** | **5** |
| 50% - 60% | **196.0** | **233.9** | **17.9** | **35.5** | **483.3** | **6** |
| 60% - 70% | **632.9** | **400.2** | **16.8** | **59.4** | **1,109.3** | **14** |
| 70% - 80% | **3,916.2** | **1,155.7** | **21.1** | **51.3** | **5,144.3** | **62** |
| 80% - 90% | **600.7** | **410.8** | **-** | **22.2** | **1,033.7** | **13** |
| 90% - 100% | **0.5** | **0.8** | **-** | **-** | **1.3** | **-** |
| **Total loans before provisions** | **5,439.0** | **2,443.5** | **106.2** | **202.5** | **8,191.2** | **100** |

**45. Risk management** (continued)

| CCFS | 2019 Buy-to-Let £m | Residential £m | Bridging £m | Second charge lending £m | Total £m | % |
|---|---|---|---|---|---|---|
| **Band** | | | | | | |
| 0% - 50% | 144.7 | 261.8 | 121.1 | 40.2 | 567.8 | 7 |
| 50% - 60% | 283.9 | 253.1 | 29.4 | 45.9 | 612.3 | 8 |
| 60% - 70% | 957.0 | 538.6 | 26.6 | 66.3 | 1,588.5 | 21 |
| 70% - 80% | 3,246.6 | 897.7 | 37.5 | 54.5 | 4,236.3 | 56 |
| 80% - 90% | 321.5 | 301.4 | 1.2 | 17.4 | 641.5 | 8 |
| 90% - 100% | 0.2 | 0.4 | - | - | 0.6 | - |
| **Total loans before provisions** | 4,953.9 | 2,253.0 | 215.8 | 224.3 | 7,647.0 | 100 |

The table below shows the LTV banding for the Company's segments' two major lending streams:

| Company | **2020** BTL/SME £m | Residential £m | Total £m | % | 2019 BTL/SME £m | Residential £m | Total £m | % |
|---|---|---|---|---|---|---|---|---|
| **Band** | | | | | | | | |
| 0% - 50% | **560.9** | **880.7** | **1,441.6** | **17** | 670.7 | 763.6 | 1,434.3 | 17 |
| 50% - 60% | **912.8** | **204.6** | **1,117.4** | **13** | 816.4 | 215.0 | 1,031.4 | 12 |
| 60% - 70% | **1,978.7** | **183.1** | **2,161.8** | **25** | 1,639.5 | 175.9 | 1,815.4 | 22 |
| 70% - 80% | **2,855.8** | **243.0** | **3,098.8** | **36** | 2,925.4 | 179.1 | 3,104.5 | 37 |
| 80% - 90% | **322.7** | **292.4** | **615.1** | **7** | 560.7 | 321.0 | 881.7 | 10 |
| 90% - 100% | **49.9** | **16.2** | **66.1** | **1** | 40.0 | 45.1 | 85.1 | 1 |
| >100% | **83.7** | **11.7** | **95.4** | **1** | 54.9 | 13.5 | 68.4 | 1 |
| **Total loans before provisions** | **6,764.5** | **1,831.7** | **8,596.2** | **100** | 6,707.6 | 1,713.2 | 8,420.8 | 100 |

The tables below show the sub-segment LTV analysis of the Company's BTL/SME lending stream:

| Company | **2020** Buy-to-Let £m | Commercial £m | Residential development £m | Funding lines £m | Total £m |
|---|---|---|---|---|---|
| **Band** | | | | | |
| 0% - 50% | **487.2** | **1.9** | **12.5** | **59.3** | **560.9** |
| 50% - 60% | **806.5** | **2.6** | **64.2** | **39.5** | **912.8** |
| 60% - 70% | **1,913.7** | **2.3** | **56.4** | **6.3** | **1,978.7** |
| 70% - 80% | **2,820.5** | **4.9** | **-** | **30.4** | **2,855.8** |
| 80% - 90% | **322.2** | **0.5** | **-** | **-** | **322.7** |
| 90% - 100% | **49.9** | **-** | **-** | **-** | **49.9** |
| >100% | **50.7** | **3.5** | **-** | **29.5** | **83.7** |
| **Total loans before provisions** | **6,450.7** | **15.7** | **133.1** | **165.0** | **6,764.5** |

**45. Risk management** (continued)

| Company | 2019 Buy-to-Let £m | Commercial £m | Residential development £m | Funding lines £m | Total £m |
|---|---|---|---|---|---|
| **Band** | | | | | |
| 0% - 50% | 438.9 | 2.3 | 125.7 | 103.8 | 670.7 |
| 50% - 60% | 765.2 | 2.5 | 5.0 | 43.7 | 816.4 |
| 60% - 70% | 1,601.1 | 2.5 | 5.0 | 30.9 | 1,639.5 |
| 70% - 80% | 2,886.3 | 5.8 | - | 33.3 | 2,925.4 |
| 80% - 90% | 549.8 | 0.5 | 10.4 | - | 560.7 |
| 90% - 100% | 35.2 | - | - | 4.8 | 40.0 |
| >100% | 45.8 | 3.5 | - | 5.6 | 54.9 |
| **Total loans before provisions** | 6,322.3 | 17.1 | 146.1 | 222.1 | 6,707.6 |

The tables below show the sub-segment LTV analysis of the Company's Residential lending stream:

| Company | 2020 First charge £m | Second charge £m | Funding lines £m | Total £m |
|---|---|---|---|---|
| **Band** | | | | |
| 0% - 50% | 771.9 | 105.1 | 3.7 | 880.7 |
| 50% - 60% | 137.9 | 64.5 | 2.2 | 204.6 |
| 60% - 70% | 123.5 | 58.1 | 1.5 | 183.1 |
| 70% - 80% | 201.6 | 39.9 | 1.5 | 243.0 |
| 80% - 90% | 272.6 | 19.3 | 0.5 | 292.4 |
| 90% - 100% | 12.2 | 3.6 | 0.4 | 16.2 |
| >100% | 5.9 | 4.9 | 0.9 | 11.7 |
| **Total loans before provisions** | 1,525.6 | 295.4 | 10.7 | 1,831.7 |

| Company | 2019 First charge £m | Second charge £m | Funding lines £m | Total £m |
|---|---|---|---|---|
| **Band** | | | | |
| 0% - 50% | 644.9 | 115.4 | 3.3 | 763.6 |
| 50% - 60% | 134.1 | 77.5 | 3.4 | 215.0 |
| 60% - 70% | 102.7 | 70.9 | 2.3 | 175.9 |
| 70% - 80% | 127.5 | 49.5 | 2.1 | 179.1 |
| 80% - 90% | 288.1 | 32.3 | 0.6 | 321.0 |
| 90% - 100% | 39.1 | 5.7 | 0.3 | 45.1 |
| >100% | 6.0 | 7.3 | 0.2 | 13.5 |
| **Total loans before provisions** | 1,342.4 | 358.6 | 12.2 | 1,713.2 |

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## Notes to the Financial Statements (continued)

For the year ended 31 December 2020

### 45. Risk management (continued)

**Forbearance measures undertaken**

The Group has a range of options available where borrowers experience financial difficulties which impact their ability to service their financial commitments under the loan agreement. These are explained in the Principal risks and uncertainties on pages 32 to 62.

A summary of the forbearance measures undertaken (excluding COVID-19 related payment deferrals) during the year is shown below. The balances disclosed reflect the year end balance of the accounts where a forbearance measure was undertaken during the year.

| Group<br>Forbearance type | Number of accounts 2020 | At 31 December 2020 £m | Number of accounts[1] 2019 | At 31 December 2019[1] £m |
|---|---|---|---|---|
| Interest-only switch | 108 | 14.1 | 59 | 8.4 |
| Interest rate reduction | 22 | 2.2 | 35 | 1.6 |
| Term extension | 430 | 27.0 | 30 | 6.6 |
| Payment deferral | 447 | 38.7 | 87 | 4.1 |
| Voluntary-assisted sale | 2 | 0.1 | 26 | 1.0 |
| Payment concession (reduced monthly payments) | 34 | 1.7 | 73 | 3.6 |
| Capitalisation of interest | 2 | 0.1 | - | - |
| Full or partial debt forgiveness | 11 | 0.2 | 6 | - |
| **Total** | **1,056** | **84.1** | 316 | 25.3 |
| | | | | |
| **Loan type** | | | | |
| First charge owner-occupier | 570 | 54.0 | 85 | 10.5 |
| Second charge owner-occupier | 372 | 15.0 | 198 | 7.4 |
| Buy-to-Let | 113 | 14.9 | 32 | 7.4 |
| Commercial | 1 | 0.2 | 1 | - |
| **Total** | **1,056** | **84.1** | 316 | 25.3 |

[1] CCFS forbearance is included post Combination.

As at 31 December 2020, active COVID-19 payment deferrals represented only 1.3% of the Group's loan book by value.

### 45. Risk management (continued)

| Company<br>Forbearance type | Number of accounts 2020 | At 31 December 2020 £m | Number of accounts 2019 | At 31 December 2019 £m |
|---|---|---|---|---|
| Interest-only switch | 78 | 9.2 | 48 | 7.2 |
| Interest rate reduction | 19 | 2.1 | 34 | 1.3 |
| Term extension | 19 | 1.6 | 19 | 6.1 |
| Payment deferral | 339 | 20.6 | 72 | 1.7 |
| Voluntary-assisted sale | 2 | 0.1 | 24 | 0.5 |
| Payment concession (reduced monthly payments) | 31 | 1.3 | 69 | 2.5 |
| Capitalisation | 2 | - | - | - |
| Full or partial debt forgiveness | 11 | 0.2 | 6 | - |
| **Total** | 501 | 35.1 | 272 | 19.3 |
| | | | | |
| **Loan type** | | | | |
| First charge owner-occupier | 104 | 16.1 | 59 | 7.0 |
| Second charge owner-occupier | 364 | 14.1 | 185 | 5.8 |
| Buy-to-Let | 33 | 4.9 | 28 | 6.5 |
| **Total** | 501 | 35.1 | 272 | 19.3 |

As at 31 December 2020, active COVID-19 payment deferrals represented only 1.8% of the Company's loan book by value.

**Geographical analysis by region**

An analysis of loans by region is provided below:

| | Group 2020 | | | | Group 2019 | | | |
|---|---|---|---|---|---|---|---|---|
| Region | OSB £m | CCFS £m | Total £m | % | OSB £m | CCFS £m | Total £m | % |
| East Anglia | 407.6 | 866.2 | 1,273.8 | 7 | 391.9 | 810.9 | 1,202.8 | 7 |
| East Midlands | 455.5 | 463.4 | 918.9 | 5 | 415.2 | 410.3 | 825.5 | 4 |
| Greater London | 4,851.9 | 2,837.4 | 7,689.3 | 40 | 4,738.7 | 2,713.7 | 7,452.4 | 41 |
| Guernsey | 35.8 | - | 35.8 | - | 45.3 | - | 45.3 | - |
| Jersey | 122.9 | - | 122.9 | 1 | 141.4 | - | 141.4 | 1 |
| North East | 140.1 | 208.4 | 348.5 | 2 | 136.7 | 179.5 | 316.2 | 2 |
| North West | 635.4 | 674.8 | 1,310.2 | 7 | 587.3 | 605.4 | 1,192.7 | 6 |
| Northern Ireland | 12.9 | - | 12.9 | - | 14.2 | - | 14.2 | - |
| Scotland | 47.0 | 214.2 | 261.2 | 1 | 48.5 | 190.9 | 239.4 | 1 |
| South East | 2,419.8 | 1,316.7 | 3,736.5 | 19 | 2,375.2 | 1,209.6 | 3,584.8 | 20 |
| South West | 757.0 | 478.5 | 1,235.5 | 6 | 747.5 | 466.0 | 1,213.5 | 7 |
| Wales | 249.2 | 209.9 | 459.1 | 2 | 239.3 | 202.6 | 441.9 | 2 |
| West Midlands | 744.5 | 529.2 | 1,273.7 | 7 | 702.2 | 496.0 | 1,198.2 | 6 |
| Yorks and Humberside | 251.8 | 392.5 | 644.3 | 3 | 237.2 | 362.1 | 599.3 | 3 |
| **Total loans before provisions** | 11,131.4 | 8,191.2 | 19,322.6 | 100 | 10,820.6 | 7,647.0 | 18,467.6 | 100 |

**45. Risk management** (continued)

| | **Company 2020** | | Company 2019 | |
|---|---|---|---|---|
| **Region** | **£m** | **%** | £m | % |
| East Anglia | **337.6** | **4** | 319.3 | 4 |
| East Midlands | **321.1** | **4** | 297.1 | 4 |
| Greater London | **3,779.9** | **44** | 3,737.7 | 44 |
| North East | **110.8** | **1** | 109.3 | 1 |
| North West | **478.3** | **6** | 448.1 | 5 |
| Northern Ireland | **12.8** | **-** | 14.1 | - |
| Scotland | **39.2** | **-** | 44.0 | 1 |
| South East | **1,936.8** | **23** | 1,921.3 | 23 |
| South West | **608.5** | **7** | 601.4 | 7 |
| Wales | **194.3** | **2** | 191.1 | 2 |
| West Midlands | **583.5** | **7** | 556.8 | 7 |
| Yorks and Humberside | **193.4** | **2** | 180.6 | 2 |
| **Total loans before provisions** | **8,596.2** | **100** | 8,420.8 | 100 |

**Approach to measurement of credit quality**

The Group categorises the credit quality of loans and advances to customers into internal risk grades based on the 12 month PD calculated at the reporting date. The PDs include a combination of internal behavioural and credit bureau characteristics. The risk grades are further grouped into the following credit quality segments:

- Excellent quality - where there is a very high likelihood the asset will be recovered in full with a negligible or very low risk of default.
- Good quality - where there is a high likelihood the asset will be recovered in full with a low risk of default.
- Satisfactory quality – where the assets demonstrate a moderate default risk.
- Lower quality - where the assets require closer monitoring and the risk of default is of greater concern.

The credit grade for the Group's investment securities and loans and advances to credit institutions is based on the external credit rating of the counterparty.

**45. Risk management** (continued)

The following tables disclose the credit risk quality ratings of loans and advances to customers by IFRS 9 stage:

| Group 2020 | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **OSB** | | | | | |
| Excellent | 4,689.6 | 295.4 | - | - | 4,985.0 |
| Good | 4,564.9 | 756.4 | - | - | 5,321.3 |
| Satisfactory | 106.7 | 242.8 | - | - | 349.5 |
| Lower | 5.6 | 68.8 | - | - | 74.4 |
| Impaired | - | - | 352.6 | - | 352.6 |
| POCI | - | - | - | 48.6 | 48.6 |
| **CCFS** | | | | | |
| Excellent | 4,352.8 | 398.8 | - | - | 4,751.6 |
| Good | 2,338.8 | 667.2 | - | - | 3,006.0 |
| Satisfactory | 55.3 | 140.2 | - | - | 195.5 |
| Lower | 2.6 | 121.4 | - | - | 124.0 |
| Impaired | - | - | 48.1 | - | 48.1 |
| POCI | - | - | - | 66.0 | 66.0 |
| | 16,116.3 | 2,691.0 | 400.7 | 114.6 | 19,322.6 |

| Group 2019 | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **OSB**[1] | | | | | |
| Excellent | 5,033.6 | 11.0 | - | - | 5,044.6 |
| Good | 4,859.3 | 200.5 | - | - | 5,059.8 |
| Satisfactory | 147.3 | 154.8 | - | - | 302.1 |
| Lower | 6.7 | 76.1 | - | - | 82.8 |
| Impaired | - | - | 277.7 | - | 277.7 |
| POCI | - | - | - | 53.6 | 53.6 |
| **CCFS** | | | | | |
| Excellent | 3,632.7 | 20.5 | - | - | 3,653.2 |
| Good | 3,359.7 | 93.7 | - | - | 3,453.4 |
| Satisfactory | 222.8 | 39.1 | - | - | 261.9 |
| Lower | 24.8 | 153.8 | - | - | 178.6 |
| Impaired | - | - | 16.7 | - | 16.7 |
| POCI | - | - | - | 83.2 | 83.2 |
| | 17,286.9 | 749.5 | 294.4 | 136.8 | 18,467.6 |

[1] The Group has restated the prior year comparatives for OSB to include finance lease assets.

**45. Risk management** (continued)

| Company 2020 | Stage 1 £m | Stage 2 £m | Stage 3 £m | Stage 3 (POCI) £m | Total £m |
|---|---|---|---|---|---|
| **Loans and advances to customers** | | | | | |
| Excellent | **3,092.9** | **256.0** | **-** | **-** | **3,348.9** |
| Good | **3,888.9** | **674.1** | **-** | **-** | **4,563.0** |
| Satisfactory | **95.6** | **228.7** | **-** | **-** | **324.3** |
| Lower | **3.0** | **56.4** | **-** | **-** | **59.4** |
| Impaired | **-** | **-** | **255.2** | **-** | **255.2** |
| POCI | **-** | **-** | **-** | **45.4** | **45.4** |
| | **7,080.4** | **1,215.2** | **255.2** | **45.4** | **8,596.2** |

| Company 2019 | | | | | |
|---|---|---|---|---|---|
| **Loans and advances to customers** | | | | | |
| Excellent | 3,565.3 | 10.3 | - | - | 3,575.6 |
| Good | 4,086.1 | 148.0 | - | - | 4,234.1 |
| Satisfactory | 127.3 | 147.0 | - | - | 274.3 |
| Lower | 6.3 | 66.0 | - | - | 72.3 |
| Impaired | - | - | 211.1 | - | 211.1 |
| POCI | - | - | - | 53.4 | 53.4 |
| | 7,785.0 | 371.3 | 211.1 | 53.4 | 8,420.8 |

The tables below show the Group's and Company's other financial assets by credit risk rating grade:

| Group 2020 | Excellent £m | Good £m | Satisfactory £m | Total £m |
|---|---|---|---|---|
| Investment securities | **471.2** | **-** | **-** | **471.2** |
| Loans and advances to credit institutions | **2,432.9** | **233.4** | **9.9** | **2,676.2** |
| Derivative assets | **6.5** | **5.8** | **-** | **12.3** |
| | **2,910.6** | **239.2** | **9.9** | **3,159.7** |

| Group 2019 | Excellent £m | Good £m | Satisfactory £m | Total £m |
|---|---|---|---|---|
| Investment securities | 635.3 | - | - | 635.3 |
| Loans and advances to credit institutions | 2,047.8 | 146.1 | 10.7 | 2,204.6 |
| Derivative assets | 11.6 | 9.5 | - | 21.1 |
| | 2,694.7 | 155.6 | 10.7 | 2,861.0 |

**45. Risk management** (continued)

| Company 2020 | Excellent £m | Good £m | Satisfactory £m | Total £m |
|---|---|---|---|---|
| Investment securities | 15.0 | - | - | 15.0 |
| Loans and advances to credit institutions | 1,442.2 | 75.9 | - | 1,518.1 |
| Derivative assets | 4.7 | - | - | 4.7 |
| | 1,461.9 | 75.9 | - | 1,537.8 |

| Company 2019 | Excellent £m | Good £m | Satisfactory £m | Total £m |
|---|---|---|---|---|
| Investment securities | 149.8 | - | - | 149.8 |
| Loans and advances to credit institutions | 1,140.7 | 55.3 | - | 1,196.0 |
| Derivative assets | 7.2 | 1.5 | - | 8.7 |
| | 1,297.7 | 56.8 | - | 1,354.5 |

**Credit risk - loans and advances to credit institutions and investment securities**

The Group holds treasury instruments in order to meet liquidity requirements and for general business purposes. The credit risk arising from these investments is closely monitored and managed by the Group's Treasury function. In managing these assets, Group Treasury operates within guidelines laid down in the Treasury Policy approved by ALCO and performance is monitored and reported to ALCO monthly, including through the use of an internally developed rating model based on counterparty credit default swap spreads.

The Group has limited exposure to emerging markets (Indian operations) and non-investment grade debt. ALCO is responsible for approving treasury counterparties.

During the year, the average balance of cash in hand, loans and advances to credit institutions and investment securities on a monthly basis was £3,196.0m (2019: £2,016.2m).

The tables below show the industry sector of the Group's loans and advances to credit institutions and investment securities:

| | Group 2020 | | Group 2019 | |
|---|---|---|---|---|
| | £m | % | £m | % |
| BoE[1] | 2,308.8 | 73 | 1,957.9 | 69 |
| Other banks | 367.4 | 12 | 246.7 | 9 |
| Central government | - | - | 149.8 | 5 |
| Securitisation | 471.2 | 15 | - | - |
| Supranationals | - | - | 485.5 | 17 |
| **Total** | 3,147.4 | 100 | 2,839.9 | 100 |

[1]Balances with the BoE include £52.3m (2019: £41.7m) held in the cash ratio deposit.

### 45. **Risk management** (continued)

| | Company 2020 | | Company 2019 | |
|---|---|---|---|---|
| | £m | % | £m | % |
| BoE1 | **1,390.4** | **91** | 1,109.3 | 83 |
| Other banks | **127.7** | **8** | 86.7 | 6 |
| Central government | **-** | **-** | 149.8 | 11 |
| Securitisation | **15.0** | **1** | - | - |
| **Total** | **1,533.1** | **100** | 1,345.8 | 100 |

[1] Balances with the BoE include £34.0m (2019: £27.5m) held in the cash ratio deposit.

The tables below show the geographical exposure of the Group's loans and advances to credit institutions and investment securities:

| | Group 2020 | | Group 2019 | |
|---|---|---|---|---|
| | £m | % | £m | % |
| United Kingdom | **3,137.5** | **100** | 2,829.2 | 100 |
| India | **9.9** | **-** | 10.7 | - |
| **Total** | **3,147.4** | **100** | 2,839.9 | 100 |

| | Company 2020 | | Company 2019 | |
|---|---|---|---|---|
| | £m | % | £m | % |
| United Kingdom | **1,533.1** | **100** | 1,345.8 | 100 |
| **Total** | **1,533.1** | **100** | 1,345.8 | 100 |

The Group monitors exposure concentrations against a variety of criteria, including asset class, sector and geography. To avoid refinancing risks associated with any one counterparty, sector or geographical region, the Board has set appropriate limits.

**Liquidity risk**

Liquidity risk is the risk of having insufficient liquid assets to fulfil obligations as they become due or the cost of raising liquid funds becoming too expensive.

The Group's approach to managing liquidity risk is to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding in order to retain full public confidence in the solvency of the Group and to enable the Group to meet its financial obligations as they fall due. This is achieved through maintaining a prudent level of liquid assets and control of the growth of the business. The Group has established a call account with the BoE and has access to its contingent liquidity facilities.

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# Notes to the Financial Statements (continued)

For the year ended 31 December 2020

### 45. Risk management (continued)

Liquidity management is the responsibility of ALCO, with day-to-day management delegated to Treasury as detailed in the Treasury Policy. ALCO is responsible for setting limits over the level and maturity profile of wholesale funding and for monitoring the composition of the Group financial position. For each material class of financial liability a contractual maturity analysis is provided below.

The Group also monitors a range of triggers, defined in the contingency funding plan and recovery and resolution plan, which are designed to capture liquidity stresses in advance in order to allow sufficient time for management action to take effect. These are monitored daily by the Risk team, with breaches immediately reported to the CRO, CEO, CFO and the Group Treasurer.

The tables below provide a contractual maturity analysis of the Group's financial assets and liabilities:

| Group<br>2020 | Carrying amount<br>£m | On demand<br>£m | Less than 3 months<br>£m | 3 - 12 months<br>£m | 1 - 5 years<br>£m | More than 5 years<br>£m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 16,603.1 | 3,810.7 | 2,733.5 | 6,517.5 | 3,541.4 | - |
| Amounts owed to credit institutions | 3,570.2 | 0.4 | 85.0 | 1,035.3 | 2,449.5 | - |
| Amounts owed to other customers | 72.9 | 26.9 | 7.5 | 38.5 | - | - |
| Derivative liabilities | 163.6 | - | 0.2 | 4.5 | 153.9 | 5.0 |
| Debt securities in issue | 421.9 | - | - | - | 421.9 | - |
| Lease liabilities | 11.7 | - | 0.2 | 0.7 | 3.6 | 7.2 |
| Subordinated liabilities | 10.5 | - | 0.2 | 0.1 | 10.2 | - |
| Perpetual Subordinated Bonds | 37.6 | - | 0.6 | - | - | 37.0 |
| **Total liabilities** | 20,891.5 | 3,838.0 | 2,827.2 | 7,596.6 | 6,580.5 | 49.2 |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.5 | 0.5 | - | - | - | - |
| Loans and advances to credit institutions | 2,676.2 | 2,512.8 | 111.1 | 18.3 | - | 34.0 |
| Investment securities | 471.2 | - | 0.3 | - | 470.9 | - |
| Loans and advances to customers | 19,230.7 | 4.1 | 316.7 | 266.4 | 1,239.7 | 17,403.8 |
| Derivative assets | 12.3 | - | 1.3 | 3.7 | 7.1 | 0.2 |
| **Total assets** | 22,390.9 | 2,517.4 | 429.4 | 288.4 | 1,717.7 | 17,438.0 |
| **Cumulative liquidity gap** | | (1,320.6) | (3,718.4) | (11,026.6) | (15,889.4) | 1,499.4 |

### 45. Risk management (continued)

| Group<br>2019 | Carrying amount<br>£m | On demand<br>£m | Less than 3 months<br>£m | 3 - 12 months<br>£m | 1 - 5 years<br>£m | More than 5 years<br>£m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 16,255.0 | 4,050.7 | 2,411.9 | 6,579.3 | 3,213.1 | - |
| Amounts owed to credit institutions | 3,068.8 | 10.2 | 232.0 | 193.5 | 2,633.1 | - |
| Amounts owed to other customers | 29.7 | 3.7 | 2.8 | 23.1 | 0.1 | - |
| Derivative liabilities | 92.8 | - | - | 2.3 | 83.4 | 7.1 |
| Debt securities in issue | 296.3 | - | - | 40.1 | 256.2 | - |
| Lease liabilities | 13.3 | - | 0.3 | 1.0 | 3.8 | 8.2 |
| Subordinated liabilities | 10.6 | - | 0.2 | 0.1 | 10.3 | - |
| Perpetual Subordinated Bonds | 37.6 | - | 0.6 | - | - | 37.0 |
| **Total liabilities** | 19,804.1 | 4,064.6 | 2,647.8 | 6,839.4 | 6,200.0 | 52.3 |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.4 | 0.4 | - | - | - | - |
| Loans and advances to credit institutions | 2,204.6 | 2,077.1 | 85.8 | - | - | 41.7 |
| Investment securities | 635.3 | - | 49.9 | 116.4 | 469.0 | - |
| Loans and advances to customers | 18,446.8 | 4.5 | 290.7 | 524.1 | 1,174.8 | 16,452.7 |
| Derivative assets | 21.1 | - | 0.3 | 3.0 | 16.0 | 1.8 |
| **Total assets** | 21,308.2 | 2,082.0 | 426.7 | 643.5 | 1,659.8 | 16,496.2 |
| **Cumulative liquidity gap** | | (1,982.6) | (4,203.7) | (10,399.6) | (14,939.8) | 1,504.1 |

**45. Risk management** (continued)

| Company 2020 | Carrying amount £m | On demand £m | Less than 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 9,705.3 | 2,998.8 | 1,325.1 | 3,420.7 | 1,960.7 | - |
| Amounts owed to credit institutions | 1,900.5 | - | 85.0 | 1,035.3 | 780.2 | - |
| Amounts owed to other customers | 5.8 | - | 0.5 | 5.3 | - | - |
| Derivative liabilities | 93.8 | - | - | 1.1 | 88.8 | 3.9 |
| Lease liabilities | 3.9 | - | - | 0.1 | 0.2 | 3.6 |
| Subordinated liabilities | 10.5 | - | 0.2 | 0.1 | 10.2 | - |
| Perpetual Subordinated Bonds | 37.6 | - | 0.6 | - | - | 37.0 |
| **Total liabilities** | 11,757.4 | 2,998.8 | 1,411.4 | 4,462.6 | 2,840.1 | 44.5 |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.5 | 0.5 | - | - | - | - |
| Loans and advances to credit institutions | 1,518.1 | 1,484.1 | - | - | - | 34.0 |
| Investment securities | 15.0 | - | - | - | 15.0 | - |
| Loans and advances to customers | 8,531.7 | - | 151.9 | 82.6 | 269.0 | 8,028.2 |
| Derivative assets | 4.7 | - | 0.6 | 1.8 | 2.1 | 0.2 |
| **Total assets** | 10,070.0 | 1,484.6 | 152.5 | 84.4 | 286.1 | 8,062.4 |
| **Cumulative liquidity gap** | | (1,514.2) | (2,773.1) | (7,151.3) | (9,705.3) | (1,687.4) |

**45. Risk management** (continued)

| Company 2019 | Carrying amount £m | On demand £m | Less than 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 9,435.7 | 3,254.6 | 1,338.4 | 3,229.0 | 1,613.7 | - |
| Amounts owed to credit institutions | 1,671.1 | 7.8 | 160.5 | - | 1,502.8 | - |
| Amounts owed to other customers | 8.9 | - | 0.5 | 8.4 | - | - |
| Derivative liabilities | 54.3 | - | - | 0.6 | 46.8 | 6.9 |
| Lease liabilities | 4.3 | - | - | 0.2 | 0.4 | 3.7 |
| Subordinated liabilities | 10.6 | - | 0.2 | 0.1 | 10.3 | - |
| Perpetual Subordinated Bonds | 37.6 | - | 0.6 | - | - | 37.0 |
| **Total liabilities** | 11,222.5 | 3,262.4 | 1,500.2 | 3,238.3 | 3,174.0 | 47.6 |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.4 | 0.4 | - | - | - | - |
| Loans and advances to credit institutions | 1,196.0 | 1,168.5 | - | - | - | 27.5 |
| Investment securities | 149.8 | - | 49.9 | 99.9 | - | - |
| Loans and advances to customers | 8,394.2 | - | 136.7 | 168.4 | 273.3 | 7,815.8 |
| Derivative assets | 8.7 | - | 0.1 | 1.0 | 7.1 | 0.5 |
| **Total assets** | 9,749.1 | 1,168.9 | 186.7 | 269.3 | 280.4 | 7,843.8 |
| **Cumulative liquidity gap** | | (2,093.5) | (3,407.0) | (6,376.0) | (9,269.6) | (1,473.4) |

**45. Risk management** (continued)

**Liquidity risk – contractual cash flows**

The following tables provide an analysis of the Group's gross contractual cash flows, derived using interest rates and contractual maturities at the reporting date and excluding impacts of early payments or non-payments:

| Group 2020 | Carrying amount £m | Gross inflow/ outflow £m | Up to 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 16,603.1 | 16,644.9 | 7,302.6 | 3,610.5 | 4,121.0 | 1,610.8 |
| Amounts owed to credit institutions and other customers | 3,643.1 | 3,658.8 | 113.4 | 1,048.9 | 826.6 | 1,669.9 |
| Derivative liabilities | 163.6 | 157.7 | 11.0 | 41.4 | 103.8 | 1.5 |
| Debt securities in issue | 421.9 | 426.4 | 17.3 | 52.0 | 67.3 | 289.8 |
| Lease liabilities | 11.7 | 13.2 | 0.5 | 1.2 | 6.4 | 5.1 |
| Subordinated liabilities | 10.5 | 13.1 | 0.4 | 0.5 | 12.2 | - |
| Perpetual Subordinated Bonds | 37.6 | 39.8 | 0.7 | 0.3 | 1.8 | 37.0 |
| **Total liabilities** | 20,891.5 | 20,953.9 | 7,445.9 | 4,754.8 | 5,139.1 | 3,614.1 |
| Off-balance sheet loan commitments | 979.5 | 979.5 | 979.5 | - | - | - |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.5 | 0.5 | 0.5 | - | - | - |
| Loans and advances to credit institutions | 2,676.2 | 2,676.2 | 2,623.9 | 18.3 | - | 34.0 |
| Investment securities | 471.2 | 494.9 | 1.2 | 4.0 | 483.8 | 5.9 |
| Loans and advances to customers | 19,230.7 | 36,156.7 | 373.4 | 1,132.4 | 4,960.5 | 29,690.4 |
| Derivative assets | 12.3 | 12.1 | 3.2 | 4.6 | 4.3 | - |
| **Total assets** | 22,390.9 | 39,340.4 | 3,002.2 | 1,159.3 | 5,448.6 | 29,730.3 |

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# Notes to the Financial Statements (continued)
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### 45. Risk management (continued)

| Group 2019 | Carrying amount £m | Gross inflow/ outflow £m | Up to 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 16,255.0 | 16,407.3 | 5,532.0 | 4,309.7 | 4,911.8 | 1,653.8 |
| Amounts owed to credit institutions and other customers | 3,098.5 | 3,133.3 | 255.1 | 229.5 | 2,648.7 | - |
| Derivative liabilities | 92.8 | 91.4 | 5.6 | 20.7 | 61.4 | 3.7 |
| Debt securities in issue | 296.3 | 315.3 | 14.4 | 82.9 | 218.0 | - |
| Lease liabilities | 13.3 | 22.4 | 0.7 | 1.4 | 17.1 | 3.2 |
| Subordinated liabilities | 10.6 | 14.2 | 0.4 | 0.5 | 13.3 | - |
| Perpetual Subordinated Bonds | 37.6 | 45.5 | 0.4 | 1.3 | 6.8 | 37.0 |
| **Total liabilities** | 19,804.1 | 20,029.4 | 5,808.6 | 4,646.0 | 7,877.1 | 1,697.7 |
| Off-balance sheet loan commitments | 1,210.9 | 1,210.9 | 1,210.9 | - | - | - |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.4 | 0.4 | 0.4 | - | - | - |
| Loans and advances to credit institutions | 2,204.6 | 2,204.6 | 2,162.9 | - | - | 41.7 |
| Investment securities | 635.3 | 672.4 | 52.1 | 123.2 | 497.1 | - |
| Loans and advances to customers | 18,446.8 | 37,024.4 | 371.6 | 1,423.6 | 5,032.4 | 30,196.8 |
| Derivative assets | 21.1 | 23.4 | 2.4 | 5.7 | 15.1 | 0.2 |
| **Total assets** | 21,308.2 | 39,925.2 | 2,589.4 | 1,552.5 | 5,544.6 | 30,238.7 |

**45. Risk management** (continued)

| Company 2020 | Carrying amount £m | Gross inflow/ outflow £m | Up to 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 9,705.3 | 9,686.7 | 6,490.7 | 2,200.4 | 995.6 | - |
| Amounts owed to credit institutions and other customers | 1,906.3 | 1,883.5 | 61.0 | 1,041.4 | 781.1 | - |
| Derivative liabilities | 93.8 | 93.3 | 5.0 | 25.3 | 61.6 | 1.4 |
| Lease liabilities | 3.9 | 4.9 | 0.2 | 0.3 | 2.0 | 2.4 |
| Subordinated liabilities | 10.5 | 13.1 | 0.4 | 0.5 | 12.2 | - |
| Perpetual Subordinated Bonds | 37.6 | 39.8 | 0.7 | 0.3 | 1.8 | 37.0 |
| **Total liabilities** | 11,757.4 | 11,721.3 | 6,558.0 | 3,268.2 | 1,854.3 | 40.8 |
| Off-balance sheet loan commitments | 522.0 | 522.0 | 522.0 | - | - | - |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.5 | 0.5 | 0.5 | - | - | - |
| Loans and advances to credit institutions | 1,518.1 | 1,518.1 | 1,484.1 | - | - | 34.0 |
| Investment securities | 15.0 | 15.0 | - | - | 15.0 | - |
| Loans and advances to customers | 8,531.7 | 17,211.8 | 108.4 | 603.8 | 2,141.1 | 14,358.5 |
| Derivative assets | 4.7 | 4.3 | 1.3 | 2.1 | 0.9 | - |
| **Total assets** | 10,070.0 | 18,749.7 | 1,594.3 | 605.9 | 2,157.0 | 14,392.5 |

**45. Risk management** (continued)

| Company 2019 | Carrying amount £m | Gross inflow/ outflow £m | Up to 3 months £m | 3 - 12 months £m | 1 - 5 years £m | More than 5 years £m |
|---|---|---|---|---|---|---|
| **Financial liability by type** | | | | | | |
| Amounts owed to retail depositors | 9,435.7 | 9,495.9 | 3,657.4 | 917.0 | 3,267.7 | 1,653.8 |
| Amounts owed to credit institutions and other customers | 1,680.0 | 1,697.6 | 174.6 | 13.8 | 1,509.2 | - |
| Derivative liabilities | 54.3 | 55.0 | 2.3 | 11.8 | 37.3 | 3.6 |
| Lease liabilities | 4.3 | 4.8 | 0.2 | 0.4 | 1.9 | 2.3 |
| Subordinated liabilities | 10.6 | 14.2 | 0.4 | 0.5 | 13.3 | - |
| Perpetual Subordinated Bonds | 37.6 | 45.5 | 0.4 | 1.3 | 6.8 | 37.0 |
| **Total liabilities** | 11,222.5 | 11,313.0 | 3,835.3 | 944.8 | 4,836.2 | 1,696.7 |
| Off-balance sheet loan commitments | 459.7 | 459.7 | 459.7 | - | - | - |
| **Financial asset by type** | | | | | | |
| Cash in hand | 0.4 | 0.4 | 0.4 | - | - | - |
| Loans and advances to credit institutions | 1,196.0 | 1,196.0 | 1,168.5 | - | - | 27.5 |
| Investment securities | 149.8 | 150.0 | 50.0 | 100.0 | - | - |
| Loans and advances to customers | 8,394.2 | 18,218.7 | 114.8 | 717.7 | 2,256.2 | 15,130.0 |
| Derivative assets | 8.7 | 8.7 | 0.7 | 1.7 | 6.2 | 0.1 |
| **Total assets** | 9,749.1 | 19,573.8 | 1,334.4 | 819.4 | 2,262.4 | 15,157.6 |

The actual repayment profile of retail deposits may differ from the analysis above due to the option of early withdrawal with a penalty.

Perpetual Subordinated Bonds have been shown to the next interest rate reset date.

The actual repayment profile of loans and advances to customers may differ from the analysis above since many mortgage loans are repaid prior to the contractual end date.

**45. Risk management** (continued)

**Liquidity risk – asset encumbrance**

Asset encumbrance levels are monitored by ALCO. The following tables provide an analysis of the Group's encumbered and unencumbered assets:

| | Group 2020 | | | | |
|---|---|---|---|---|---|
| | Encumbered | | Unencumbered | | |
| | Pledged as collateral £m | Other[1] £m | Available as collateral £m | Other[2] £m | Total £m |
| Cash in hand | - | - | 0.5 | - | 0.5 |
| Loans and advances to credit institutions | 211.1 | 95.0 | 2,256.5 | 113.6 | 2,676.2 |
| Investment securities | 161.0 | - | 310.2 | - | 471.2 |
| Loans and advances to customers | 5,638.6 | - | 2,752.0 | 10,840.1 | 19,230.7 |
| Derivative assets | - | - | - | 12.3 | 12.3 |
| Non-financial assets | - | - | - | 263.6 | 263.6 |
| | 6,010.7 | 95.0 | 5,319.2 | 11,229.6 | 22,654.5 |

| | Group 2019 | | | | |
|---|---|---|---|---|---|
| | Encumbered | | Unencumbered | | |
| | Pledged as collateral £m | Other[1] £m | Available as collateral £m | Other[2] £m | Total £m |
| Cash in hand | - | - | 0.4 | - | 0.4 |
| Loans and advances to credit institutions | 110.4 | 41.7 | 1,916.2 | 136.3 | 2,204.6 |
| Investment securities | 173.0 | - | 462.3 | - | 635.3 |
| Loans and advances to customers | 4,922.4 | 40.4 | 1,939.6 | 11,544.4 | 18,446.8 |
| Derivative assets | - | - | - | 21.1 | 21.1 |
| Non-financial assets | - | - | - | 108.9 | 108.9 |
| | 5,205.8 | 82.1 | 4,318.5 | 11,810.7 | 21,417.1 |

[1] Represents assets that are not pledged but that the Group believes it is restricted from using to secure funding for legal or other reasons.
[2] Represents assets that are not restricted for use as collateral, but the Group treats as available as collateral once they are readily available to secure funding in the normal course of business.

### 45. Risk management (continued)

| | Company 2020 | | | | |
|---|---|---|---|---|---|
| | Encumbered | | Unencumbered | | |
| | Pledged as collateral £m | Other[1] £m | Available as collateral £m | Other[2] £m | Total £m |
| Cash in hand | - | - | 0.5 | | 0.5 |
| Loans and advances to credit institutions | 107.0 | 34.0 | 1,356.4 | 20.7 | 1,518.1 |
| Investment securities | - | - | 15.0 | - | 15.0 |
| Loans and advances to customers | 3,064.0 | - | - | 5,467.7 | 8,531.7 |
| Derivative assets | - | - | - | 4.7 | 4.7 |
| Non-financial assets | - | - | - | 3,304.8 | 3,304.8 |
| | 3,171.0 | 34.0 | 1,371.9 | 8,797.9 | 13,374.8 |

| | Company 2019 | | | | |
|---|---|---|---|---|---|
| | Encumbered | | Unencumbered | | |
| | Pledged as collateral £m | Other[1] £m | Available as collateral £m | Other[2] £m | Total £m |
| Cash in hand | - | - | 0.4 | - | 0.4 |
| Loans and advances to credit institutions | 62.2 | 27.5 | 1,081.8 | 24.5 | 1,196.0 |
| Investment securities | - | - | 149.8 | - | 149.8 |
| Loans and advances to customers | 3,010.0 | 40.4 | 910.1 | 4,433.7 | 8,394.2 |
| Derivative assets | - | - | - | 8.7 | 8.7 |
| Non-financial assets | - | - | - | 3,720.8 | 3,720.8 |
| | 3,072.2 | 67.9 | 2,142.1 | 8,187.7 | 13,469.9 |

[1] Represents assets that are not pledged but that the Group believes it is restricted from using to secure funding for legal or other reasons.
[2] Represents assets that are not restricted for use as collateral, but the Group treats as available as collateral once they are readily available to secure funding in the normal course of business.

**45. Risk management** (continued)

**Liquidity risk – liquidity reserves**

The tables below analyse the Group's liquidity reserves, where carrying value is considered to be equal to fair value:

| | **Group 2020 £m** | Group 2019 £m | **Company 2020 £m** | Company 2019 £m |
|---|---|---|---|---|
| Unencumbered balances with central banks | **2,256.5** | 1,916.2 | **1,356.4** | 1,081.8 |
| Unencumbered cash and balances with other banks | **113.6** | 136.3 | **20.7** | 24.5 |
| Other cash and cash equivalents | **0.5** | 0.4 | **0.5** | 0.4 |
| Unencumbered investment securities | **310.2** | 462.3 | **15.0** | 149.8 |
| | **2,680.8** | 2,515.2 | **1,392.6** | 1,256.5 |

**Market risk**

Market risk is the risk of an adverse change in the Group's income or the Group's net worth arising from movement in interest rates, exchange rates or other market prices. Market risk exists, to some extent, in all the Group's businesses. The Group recognises that the effective management of market risk is essential to the maintenance of stable earnings and preservation of shareholder value.

**Interest rate risk**

The primary market risk faced by the Group is interest rate risk. Interest rate risk is the risk of loss from adverse movement in the overall level of interest rates. It arises from mismatches in the timing of repricing of assets and liabilities, both on and off-balance sheet. The Group does not run a trading book or take speculative interest rate positions and therefore all interest rate risk resides in the banking book (interest rate risk in the banking book (IRRBB)). IRRBB is most prevalent in mortgage lending where fixed rate mortgages are not funded by fixed rate deposits of the same duration, or where the fixed rate risk is not hedged by a fully matching interest rate derivative. Exposure is mitigated on a continuous basis through the use of derivatives and reserve allocations.

Currently interest rate risk is managed separately for OSB and CCFS due to the use of different treasury management and asset and liability management (ALM) systems. However, the methodology applied to the setting of risk appetites was aligned across the Group in 2020. Both Banks apply an economic value at risk approach as well as an earnings at risk approach for interest rate risk and basis risk. The interest rate sensitivity is impacted by behavioural assumptions used by the Group; the most significant of which are prepayments and reserve allocations. Expected prepayments are modelled based on historical analysis and current market rates. The reserve allocation strategy is approved by ALCO and set to reflect the current balance sheet and future plans.

Economic value at risk is measured using the impact of six different internally derived interest rate scenarios. The internal scenarios are defined by ALCO and are based on three 'shapes' of curve movement (shift, twist and flex). Historical data is used to calibrate the severity of the scenarios to the Group's risk appetite. The Board has set limits on interest rate risk exposure of 2.25% and 1% of CET1 for OSB and CCFS, respectively.

**45. Risk management** (continued)

The table below shows the maximum decreases to net interest income under these scenarios after taking into account the derivatives:

| Group | 2020 £m | 2019 £m |
|---|---|---|
| OSB | **5.6** | 4.3 |
| CCFS | **0.7** | 3.7 |
| Group | **6.3** | 8.0 |

Exposure for earnings at risk is measured by the impact of a +/-50bps parallel shift in interest rates on the expected profitability of the Group in the next 12 months. The risk appetite limit is 2% of full year net interest income (NII). The table below shows the maximum decreases after taking into account the derivatives:

| Group | 2020 £m | 2019 £m |
|---|---|---|
| OSB[1] | **(0.1)** | 2.5 |
| CCFS | **2.2** | 0.6 |
| Group | **2.1** | 3.1 |

[1] Due to product floors earnings increases in both the +50bps and -50bps scenarios.

The Group is also exposed to basis risk. Basis risk is the risk of loss from an adverse divergence in interest rates. It arises where assets and liabilities reprice from different variable rate indices. These indices may be market rates (e.g. bank base rate, LIBOR or SONIA) or administered (e.g. the Group's SVR, other discretionary variable rates, or that received on call accounts with other banks).

The Group measures basis risk using the impact of five scenarios on net interest income over a one-year period including movements such as diverging base, LIBOR and SONIA rates. Historical data is used to calibrate the severity of the scenarios to the Group's risk appetite. The Board has set a limit on basis risk exposure of 4% of full year net interest income. The table below shows the maximum decreases to net interest income at 31 December 2020 and 2019:

| Group | 2020 £m | 2019 £m |
|---|---|---|
| OSB | **5.4** | 9.3 |
| CCFS | **8.0** | 9.7 |
| Group | **13.4** | 19.0 |

**Foreign exchange rate risk**

The Group has limited exposure to foreign exchange risk in respect of its Indian operations. A 5% increase in exchange rates would result in a £0.4m (2019: £0.4m) effect in profit or loss and £0.5m (2019: £0.4m) in equity.

The Company is not exposed to foreign exchange risk since all its assets and liabilities are denominated in Pounds Sterling.

**45. Risk management** (continued)

**Structured entities**

The structured entities consolidated within the Group at 31 December 2020 were Canterbury Finance No.2 plc, Canterbury Finance No.3 plc and CMF 2020-1 plc. These entities hold legal title to a pool of mortgages which are used as a security for issued debt. The transfer of mortgages fails derecognition criteria because the Group retained the subordinated notes and residual certificates issued and as such did not transfer substantially the risks and rewards of ownership of the securitised mortgages. Therefore, the Group is exposed to credit, interest rate and other risks on the securitised mortgages.

Cash flows generated from the structured entities are ring-fenced and are used to pay interest and principal of the issued debt securities in a waterfall order according to the seniority of the bonds. The structured entities are self-funded and the Group is not contractually or constructively obliged to provide further liquidity or financial support.

The structured entities consolidated within the Group at 31 December 2019 were Canterbury Finance No.1 plc and Precise Mortgage Funding 2015-1 plc.

**Unconsolidated structured entities**

Structured entities, which were sponsored by the Group include Precise Mortgage Funding 2015-2B plc, Precise Mortgage Funding 2017-1B plc, Charter Mortgage Funding 2017-1 plc, Precise Mortgage Funding 2018-1B plc, Charter Mortgage Funding 2018-1 plc, Precise Mortgage Funding 2019-1B plc, Canterbury Finance No.1 plc and Precise Mortgage Funding 2020-1B plc.

These structured entities are not consolidated by the Group, as the Group does not control the entities and is not exposed to the risks and rewards of ownership from the securitised mortgages. The Group has no contractual arrangements with the unconsolidated structured entities other than the investments disclosed in note 18 and servicing the structured entities' mortgage portfolios.

The Group has not provided any support to the unconsolidated structured entities listed and has no obligation or intention to do so.

During 2020 the Group received £5.0m interest income (2019: £2.7m) and £4.6m servicing income (2019: £1.1m) from unconsolidated structured entities.

## 46. Financial instruments and fair values

### i. Financial assets and financial liabilities

The following tables summarise the classification and carrying value of the Group's financial assets and financial liabilities:

| | | 2020 | | | |
|---|---|---|---|---|---|
| Group | Note | Fair value through profit or loss £m | FVOCI £m | Amortised cost £m | Total carrying amount £m |
| **Assets** | | | | | |
| Cash in hand | | - | - | 0.5 | 0.5 |
| Loans and advances to credit institutions | 17 | - | - | 2,676.2 | 2,676.2 |
| Investment securities | 18 | - | 285.0 | 186.2 | 471.2 |
| Loans and advances to customers | 19 | 19.1 | - | 19,211.6 | 19,230.7 |
| Derivative assets | 24 | 12.3 | - | - | 12.3 |
| | | 31.4 | 285.0 | 22,074.5 | 22,390.9 |
| **Liabilities** | | | | | |
| Amounts owed to retail depositors | 33 | - | - | 16,603.1 | 16,603.1 |
| Amounts owed to credit institutions | 32 | - | - | 3,570.2 | 3,570.2 |
| Amounts owed to other customers | 34 | - | - | 72.9 | 72.9 |
| Debt securities in issue | 35 | - | - | 421.9 | 421.9 |
| Derivative liabilities | 24 | 163.6 | - | - | 163.6 |
| Subordinated liabilities | 39 | - | - | 10.5 | 10.5 |
| Perpetual Subordinated Bonds | 40 | - | - | 37.6 | 37.6 |
| | | 163.6 | - | 20,716.2 | 20,879.8 |

# OneSavings Bank plc

# Notes to the Financial Statements (continued)

For the year ended 31 December 2020

**46. Financial instruments and fair values** (continued)

| | | 2019 | | | |
|---|---|---|---|---|---|
| Group | Note | Fair value through profit or loss £m | FVOCI £m | Amortised cost £m | Total carrying amount £m |
| **Assets** | | | | | |
| Cash in hand | | - | - | 0.4 | 0.4 |
| Loans and advances to credit institutions | 17 | - | - | 2,204.6 | 2,204.6 |
| Investment securities | 18 | - | 508.7 | 126.6 | 635.3 |
| Loans and advances to customers | 19 | 22.1 | - | 18,424.7 | 18,446.8 |
| Derivative assets | 24 | 21.1 | - | - | 21.1 |
| | | 43.2 | 508.7 | 20,756.3 | 21,308.2 |
| **Liabilities** | | | | | |
| Amounts owed to retail depositors | 33 | - | - | 16,255.0 | 16,255.0 |
| Amounts owed to credit institutions | 32 | - | - | 3,068.8 | 3,068.8 |
| Amounts owed to other customers | 34 | - | - | 29.7 | 29.7 |
| Debt securities in issue | 35 | - | - | 296.3 | 296.3 |
| Derivative liabilities | 24 | 92.8 | - | - | 92.8 |
| Subordinated liabilities | 39 | - | - | 10.6 | 10.6 |
| Perpetual Subordinated Bonds | 40 | - | - | 37.6 | 37.6 |
| | | 92.8 | - | 19,698.0 | 19,790.8 |

**46. Financial instruments and fair values** (continued)

| Company | Note | 2020 Fair value through profit or loss £m | FVOCI £m | Amortised cost £m | Total carrying amount £m |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash in hand | | - | - | 0.5 | 0.5 |
| Loans and advances to credit institutions | 17 | - | - | 1,518.1 | 1,518.1 |
| Investment securities | 18 | - | 15.0 | - | 15.0 |
| Loans and advances to customers | 19 | - | - | 8,531.7 | 8,531.7 |
| Derivative assets | 24 | 4.7 | - | - | 4.7 |
| | | 4.7 | 15.0 | 10,050.3 | 10,070.0 |
| **Liabilities** | | | | | |
| Amounts owed to retail depositors | 33 | - | - | 9,705.3 | 9,705.3 |
| Amounts owed to credit institutions | 32 | - | - | 1,900.5 | 1,900.5 |
| Amounts owed to other customers | 34 | - | - | 5.8 | 5.8 |
| Derivative liabilities | 24 | 93.8 | - | - | 93.8 |
| Subordinated liabilities | 39 | - | - | 10.5 | 10.5 |
| Perpetual Subordinated Bonds | 40 | - | - | 37.6 | 37.6 |
| | | 93.8 | - | 11,659.7 | 11,753.5 |

| Company | Note | 2019 Fair value through profit or loss £m | FVOCI £m | Amortised cost £m | Total carrying amount £m |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash in hand | | - | - | 0.4 | 0.4 |
| Loans and advances to credit institutions | 17 | - | - | 1,196.0 | 1,196.0 |
| Investment securities | 18 | - | 149.8 | - | 149.8 |
| Loans and advances to customers | 19 | - | - | 8,394.2 | 8,394.2 |
| Derivative assets | 24 | 8.7 | - | - | 8.7 |
| | | 8.7 | 149.8 | 9,590.6 | 9,749.1 |
| **Liabilities** | | | | | |
| Amounts owed to retail depositors | 33 | - | - | 9,435.7 | 9,435.7 |
| Amounts owed to credit institutions | 32 | - | - | 1,671.1 | 1,671.1 |
| Amounts owed to other customers | 34 | - | - | 8.9 | 8.9 |
| Derivative liabilities | 24 | 54.3 | - | - | 54.3 |
| Subordinated liabilities | 39 | - | - | 10.6 | 10.6 |
| Perpetual Subordinated Bonds | 40 | - | - | 37.6 | 37.6 |
| | | 54.3 | - | 11,163.9 | 11,218.2 |

### 46. Financial instruments and fair values (continued)

The Group has no financial assets nor financial liabilities classified as held for trading.

### ii. Fair values

The following tables summarise the carrying value and estimated fair value of financial instruments not measured at fair value in the Statement of Financial Position:

| | 2020 | | 2019 | |
|---|---|---|---|---|
| Group | Carrying value £m | Estimated fair value £m | Carrying value £m | Estimated fair value £m |
| **Assets** | | | | |
| Cash in hand | 0.5 | 0.5 | 0.4 | 0.4 |
| Loans and advances to credit institutions | 2,676.2 | 2,676.2 | 2,204.6 | 2,204.6 |
| Investment securities | 186.2 | 186.6 | 126.6 | 126.6 |
| Loans and advances to customers | 19,211.6 | 19,352.0 | 18,424.7 | 18,654.2 |
| | 22,074.5 | 22,215.3 | 20,756.3 | 20,985.8 |
| **Liabilities** | | | | |
| Amounts owed to retail depositors | 16,603.1 | 16,666.1 | 16,255.0 | 16,259.7 |
| Amounts owed to credit institutions | 3,570.2 | 3,570.2 | 3,068.8 | 3,068.8 |
| Amounts owed to other customers | 72.9 | 72.9 | 29.7 | 29.7 |
| Debt securities in issue | 421.9 | 421.9 | 296.3 | 296.3 |
| Subordinated liabilities | 10.5 | 10.7 | 10.6 | 10.7 |
| Perpetual Subordinated Bonds | 37.6 | 32.3 | 37.6 | 33.2 |
| | 20,716.2 | 20,774.1 | 19,698.0 | 19,698.4 |

| | 2020 | | 2019 | |
|---|---|---|---|---|
| Company | Carrying value £m | Estimated fair value £m | Carrying value £m | Estimated fair value £m |
| **Assets** | | | | |
| Cash in hand | 0.5 | 0.5 | 0.4 | 0.4 |
| Loans and advances to credit institutions | 1,518.1 | 1,518.1 | 1,196.0 | 1,196.0 |
| Loans and advances to customers | 8,531.7 | 8,670.1 | 8,394.2 | 8,566.3 |
| | 10,050.3 | 10,188.7 | 9,590.6 | 9,762.7 |
| **Liabilities** | | | | |
| Amounts owed to retail depositors | 9,705.3 | 9,736.4 | 9,435.7 | 9,435.8 |
| Amounts owed to credit institutions | 1,900.5 | 1,900.5 | 1,671.1 | 1,671.1 |
| Amounts owed to other customers | 5.8 | 5.8 | 8.9 | 8.9 |
| Subordinated liabilities | 10.5 | 10.7 | 10.6 | 10.7 |
| Perpetual Subordinated Bonds | 37.6 | 32.3 | 37.6 | 33.2 |
| | 11,659.7 | 11,685.7 | 11,163.9 | 11,159.7 |

**46. Financial instruments and fair values** (continued)

The fair values in these tables are estimated using the valuation techniques below. The estimated fair value is stated as at 31 December and may be significantly different from the amounts which will actually be paid on the maturity or settlement dates of each financial instrument.

**Cash in hand**
This represents physical cash across the Group's branch network where fair value is considered to be equal to carrying value.

**Loans and advances to credit institutions**
This mainly represents the Group's working capital current accounts and call accounts with central governments and other banks with an original maturity of less than three months. Fair value is not considered to be materially different to carrying value.

**Investment Securities**
Investment securities' fair values are provided by a third party and are based on the market values of similar financial instruments.

**Loans and advances to customers**
This mainly represents secured mortgage lending to customers. The fair value of fixed rate mortgages has been estimated by discounting future cash flows at current market rates of interest. Future cash flows include the impact of expected credit losses. The interest rate on variable rate mortgages is considered to be equal to current market product rates and as such fair value is estimated to be equal to carrying value.

**Amounts owed to retail depositors**
The fair value of fixed rate retail deposits has been estimated by discounting future cash flows at current market rates of interest. Retail deposits at variable rates and deposits payable on demand are considered to be at current market rates and as such fair value is estimated to be equal to carrying value.

**Amounts owed to credit institutions**
This mainly represents amounts drawn down under the BoE TFS, TFSME and ILTR, warehouse funding and commercial repos. Fair value is considered to be equal to carrying value.

**Amounts owed to other customers**
This represents fixed rate saving products to corporations and local authorities with original maturities greater than three months. The fair value is estimated by discounting future cash flows at current market rates of interest.

**Debt securities in issue**
While the Group's debt securities in issue are listed, the quoted prices for an individual note may not be indicative of the fair value of the issue as a whole, due to the specialised nature of the market in such instruments and the limited number of investors participating in it. Fair value is not considered to be materially different to carrying value.

**Subordinated liabilities and Perpetual Subordinated Bonds**
The fair value of subordinated liabilities is estimated by using quoted market prices of similar instruments at the reporting date. The PSBs are listed on the London Stock Exchange with fair value being the quoted market price at the reporting date.

### 46. Financial instruments and fair values (continued)

#### iii. Fair value classification

The following tables provide an analysis of financial assets and financial liabilities measured at fair value in the Statement of Financial Position grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

| **Group 2020** | **Carrying amount £m** | **Principal amount £m** | **Level 1 £m** | **Level 2 £m** | **Level 3 £m** | **Total £m** |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Investment securities | **285.0** | **284.7** | **-** | **285.0** | **-** | **285.0** |
| Loans and advances to customers | **19.1** | **21.8** | **-** | **-** | **19.1** | **19.1** |
| Derivative assets | **12.3** | **8,687.8** | **-** | **12.3** | **-** | **12.3** |
| | **316.4** | **8,994.3** | **-** | **297.3** | **19.1** | **316.4** |
| **Financial liabilities** | | | | | | |
| Derivative liabilities | **163.6** | **10,392.4** | **-** | **163.6** | **-** | **163.6** |

| Group 2019 | Carrying amount £m | Principal amount £m | Level 1 £m | Level 2 £m | Level 3 £m | Total £m |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Investment securities | 508.7 | 509.5 | 149.8 | 358.9 | - | 508.7 |
| Loans and advances to customers | 22.1 | 24.8 | - | - | 22.1 | 22.1 |
| Derivative assets | 21.1 | 7,795.4 | - | 21.0 | 0.1 | 21.1 |
| | 551.9 | 8,329.7 | 149.8 | 379.9 | 22.2 | 551.9 |
| **Financial liabilities** | | | | | | |
| Derivative liabilities | 92.8 | 9,982.4 | - | 92.8 | - | 92.8 |

| **Company 2020** | **Carrying amount £m** | **Principal amount £m** | **Level 1 £m** | **Level 2 £m** | **Level 3 £m** | **Total £m** |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Investment securities | **15.0** | **15.0** | **-** | **15.0** | **-** | **15.0** |
| Derivative assets | **4.7** | **3,585.0** | **-** | **4.7** | **-** | **4.7** |
| | **19.7** | **3,600.0** | **-** | **19.7** | **-** | **19.7** |
| **Financial liabilities** | | | | | | |
| Derivative liabilities | **93.8** | **3,729.0** | **-** | **93.8** | **-** | **93.8** |

**46. Financial instruments and fair values** (continued)

| Company 2019 | Carrying amount £m | Principal amount £m | Level 1 £m | Level 2 £m | Level 3 £m | Total £m |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Investment securities | 149.8 | 150.0 | 149.8 | - | - | 149.8 |
| Derivative assets | 8.7 | 3,080.0 | - | 8.7 | - | 8.7 |
| | 158.5 | 3,230.0 | 149.8 | 8.7 | - | 158.5 |
| **Financial liabilities** | | | | | | |
| Derivative liabilities | 54.3 | 4,462.9 | - | 54.3 | - | 54.3 |

**Level 1:** Fair values that are based entirely on quoted market prices (unadjusted) in an actively traded market for identical assets and liabilities that the Group has the ability to access. Valuation adjustments and block discounts are not applied to Level 1 instruments. Since valuations are based on readily available observable market prices, this makes them most reliable, reduces the need for management judgement and estimation and also reduces the uncertainty associated with determining fair values.

**Level 2:** Fair values that are based on one or more quoted prices in markets that are not active or for which all significant inputs are taken from directly or indirectly observable market data. These include valuation models used to calculate the present value of expected future cash flows and may be employed either when no active market exists or when there are no quoted prices available for similar instruments in active markets.

**Level 3:** Fair values for which any one or more significant input is not based on observable market data and the unobservable inputs have a significant effect on the instrument's fair value. Valuation models that employ significant unobservable inputs require a higher degree of management judgement and estimation in determining the fair value. Management judgement and estimation are usually required for the selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instruments being valued, determination of the probability of counterparty default and prepayments, determination of expected volatilities and correlations and the selection of appropriate discount rates.

## 46. Financial instruments and fair values (continued)

The following table provides an analysis of financial assets and financial liabilities not measured at fair value in the Statement of Financial Position grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

| | | | Estimated fair value | | | |
|---|---|---|---|---|---|---|
| **Group 2020** | **Carrying amount £m** | **Principal amount £m** | **Level 1 £m** | **Level 2 £m** | **Level 3 £m** | **Total £m** |
| **Financial assets** | | | | | | |
| Cash in hand | **0.5** | **0.5** | **-** | **0.5** | **-** | **0.5** |
| Loans and advances to credit institutions | **2,676.2** | **2,676.1** | **-** | **2,676.2** | **-** | **2,676.2** |
| Investment securities | **186.2** | **186.2** | **-** | **186.6** | **-** | **186.6** |
| Loans and advances to customers | **19,211.6** | **19,200.1** | **-** | **3,314.5** | **16,037.5** | **19,352.0** |
| | **22,074.5** | **22,062.9** | **-** | **6,177.8** | **16,037.5** | **22,215.3** |
| **Financial liabilities** | | | | | | |
| Amounts owed to retail depositors | **16,603.1** | **16,507.3** | **-** | **5,546.1** | **11,120.0** | **16,666.1** |
| Amounts owed to credit institutions | **3,570.2** | **3,569.3** | **-** | **3,570.2** | **-** | **3,570.2** |
| Amounts owed to other customers | **72.9** | **72.7** | **-** | **-** | **72.9** | **72.9** |
| Debt securities in issue | **421.9** | **421.8** | **-** | **421.9** | **-** | **421.9** |
| Subordinated liabilities | **10.5** | **10.3** | **-** | **-** | **10.7** | **10.7** |
| Perpetual Subordinated Bonds | **37.6** | **37.0** | **32.3** | **-** | **-** | **32.3** |
| | **20,716.2** | **20,618.4** | **32.3** | **9,538.2** | **11,203.6** | **20,774.1** |

| Group 2019 | Carrying amount £m | Principal amount £m | Level 1 £m | Level 2 £m | Level 3 £m | Total £m |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Cash in hand | 0.4 | 0.4 | - | 0.4 | - | 0.4 |
| Loans and advances to credit institutions | 2,204.6 | 2,204.3 | - | 2,204.6 | - | 2,204.6 |
| Investment securities | 126.6 | 126.4 | 126.6 | - | - | 126.6 |
| Loans and advances to customers | 18,424.7 | 18,281.3 | - | 3,409.1 | 15,245.1 | 18,654.2 |
| | 20,756.3 | 20,612.4 | 126.6 | 5,614.1 | 15,245.1 | 20,985.8 |
| **Financial liabilities** | | | | | | |
| Amounts owed to retail depositors | 16,255.0 | 16,133.5 | - | 3,817.8 | 12,441.9 | 16,259.7 |
| Amounts owed to credit institutions | 3,068.8 | 3,063.3 | - | 3,068.8 | - | 3,068.8 |
| Amounts owed to other customers | 29.7 | 29.5 | - | - | 29.7 | 29.7 |
| Debt securities in issue | 296.3 | 295.5 | - | 296.3 | - | 296.3 |
| Subordinated liabilities | 10.6 | 10.4 | - | - | 10.7 | 10.7 |
| Perpetual Subordinated Bonds | 37.6 | 37.0 | 33.2 | - | - | 33.2 |
| | 19,698.0 | 19,569.2 | 33.2 | 7,182.9 | 12,482.3 | 19,698.4 |

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

**46. Financial instruments and fair values** (continued)

| | | | Estimated fair value | | | |
|---|---|---|---|---|---|---|
| **Company** | **Carrying amount** | **Principal amount** | **Level 1** | **Level 2** | **Level 3** | **Total** |
| **2020** | **£m** | **£m** | **£m** | **£m** | **£m** | **£m** |
| **Financial assets** | | | | | | |
| Cash in hand | **0.5** | **0.5** | **-** | **0.5** | **-** | **0.5** |
| Loans and advances to credit institutions | **1,518.1** | **1,518.1** | **-** | **1,518.1** | **-** | **1,518.1** |
| Loans and advances to customers | **8,531.7** | **8,702.5** | **-** | **2,382.8** | **6,287.3** | **8,670.1** |
| | **10,050.3** | **10,221.1** | **-** | **3,901.4** | **6,287.3** | **10,188.7** |
| **Financial liabilities** | | | | | | |
| Amounts owed to retail depositors | **9,705.3** | **9,645.8** | **-** | **3,429.7** | **6,306.7** | **9,736.4** |
| Amounts owed to credit institutions | **1,900.5** | **1,900.0** | **-** | **1,900.5** | **-** | **1,900.5** |
| Amounts owed to other customers | **5.8** | **5.8** | **-** | **-** | **5.8** | **5.8** |
| Subordinated liabilities | **10.5** | **10.3** | **-** | **-** | **10.7** | **10.7** |
| Perpetual Subordinated Bonds | **37.6** | **37.0** | **32.3** | **-** | **-** | **32.3** |
| | **11,659.7** | **11,598.9** | **32.3** | **5,330.2** | **6,323.2** | **11,685.7** |

| | | | Estimated fair value | | | |
|---|---|---|---|---|---|---|
| Company | Carrying amount | Principal amount | Level 1 | Level 2 | Level 3 | Total |
| 2019 | £m | £m | £m | £m | £m | £m |
| **Financial assets** | | | | | | |
| Cash in hand | 0.4 | 0.4 | - | 0.4 | - | 0.4 |
| Loans and advances to credit institutions | 1,196.0 | 1,195.7 | - | 1,196.0 | - | 1,196.0 |
| Loans and advances to customers | 8,394.2 | 8,533.2 | - | 2,431.5 | 6,134.8 | 8,566.3 |
| | 9,590.6 | 9,729.3 | - | 3,627.9 | 6,134.8 | 9,762.7 |
| **Financial liabilities** | | | | | | |
| Amounts owed to retail depositors | 9,435.7 | 9,364.5 | - | 3,817.8 | 5,618.0 | 9,435.8 |
| Amounts owed to credit institutions | 1,671.1 | 1,667.8 | - | 1,671.1 | - | 1,671.1 |
| Amounts owed to other customers | 8.9 | 8.8 | - | - | 8.9 | 8.9 |
| Subordinated liabilities | 10.6 | 10.4 | - | - | 10.7 | 10.7 |
| Perpetual Subordinated Bonds | 37.6 | 37.0 | 33.2 | - | - | 33.2 |
| | 11,163.9 | 11,088.5 | 33.2 | 5,488.9 | 5,637.6 | 11,159.7 |

**47. Pension scheme**

**Defined contribution scheme**

The amount charged to profit or loss in respect of contributions to the Group's defined contribution and stakeholder pension arrangements is the contribution payable in the period. The total pension cost in the year amounted to £4.3m (2019: £3.0m).

### 48. Country by country reporting

Country by Country Reporting (CBCR) was introduced through Article 89 of CRD IV, aimed at the banking and capital markets industry.

The name, nature of activities and geographic location of the Group's companies are presented below:

| Jurisdiction | Country | Name | Activities |
|---|---|---|---|
| UK[1] | England | OneSavings Bank plc | Commercial banking |
| | | 5D Finance Limited | |
| | | Broadlands Finance Limited | |
| | | Charter Court Financial Services Group Plc | |
| | | Charter Court Financial Services Limited | |
| | | Charter Mortgages Limited | |
| | | Easioption Limited | |
| | | Exact Mortgage Experts Limited | |
| | | Guernsey Home Loans Limited | |
| | | Heritable Development Finance Limited | |
| | | Inter Bay Financial I Limited | |
| | | Inter Bay Financial II Limited | |
| | | InterBay Asset Finance Limited | |
| | | Interbay Funding, Ltd | |
| | | Interbay Group Holdings Limited | |
| | | InterBay Holdings Ltd | |
| | | Interbay ML, Ltd | |
| | | Jersey Home Loans Limited | |
| | | Prestige Finance Limited | |
| | | Reliance Property Loans Limited | |
| | | Rochester Mortgages Limited | |
| | Guernsey | Guernsey Home Loans Limited | |
| | Jersey | Jersey Home Loans Limited | |
| UK | England | Canterbury Finance No. 2 plc | Special purpose vehicle |
| | | Canterbury Finance No. 3 plc | |
| | | CMF 2020-1 plc | |
| | | CML Warehouse Number 1 Limited | |
| | | CML Warehouse Number 2 Limited | |
| | | Precise Mortgage Funding 2014-1 plc | |
| | | Precise Mortgage Funding 2014-2 plc | |
| | | Precise Mortgage Funding 2015-1 plc | |
| | | Precise Mortgage Funding 2015-3R plc | |
| India | India | OSB India Private Limited | Back office processing |

[1] Guernsey Home Loans Limited (Guernsey) and Jersey Home Loans Limited (Jersey) are incorporated in Guernsey and Jersey respectively but are considered to be located in the UK as they are managed and controlled in the UK with no permanent establishments in Guernsey or Jersey.

### 48. Country by country reporting (continued)

Other disclosures required by the CBCR directive are provided below:

| **2020** | **UK** | **India** | **Consolidation[2]** | **Total** |
|---|---|---|---|---|
| Average number of employees | **1,330** | **486** | **-** | **1,816** |
| Turnover[1], £m | **508.3** | **9.4** | **(9.1)** | **508.6** |
| Profit/(loss) before tax, £m | **260.0** | **1.3** | **(1.0)** | **260.3** |
| Corporation tax paid, £m | **128.6** | **0.2** | **-** | **128.8** |

| 2019 | UK | India | Consolidation[2] | Total |
|---|---|---|---|---|
| Average number of employees | 1,335 | 454 | - | 1,789 |
| Turnover[1], £m | 343.1 | 8.9 | (8.6) | 343.4 |
| Profit/(loss) before tax, £m | 208.8 | 1.6 | (1.3) | 209.1 |
| Corporation tax paid, £m | 52.6 | 0.4 | - | 53.0 |

[1] Turnover represents total income before impairment losses, regulatory provisions and operating costs, but after net interest, net commissions and fees, gains and losses on financial instruments and external servicing fees.
[2] Relates to a management fee from Indian subsidiaries to OneSavings Bank plc for providing back office processing.

The tables below reconcile tax charged and tax paid during the year:

| **2020** | **UK £m** | **India £m** | **Total £m** |
|---|---|---|---|
| **Tax charge** | **63.8** | **0.3** | **64.1** |
| **Effects of:** | | | |
| Other timing differences | **15.7** | **(0.1)** | **15.6** |
| Tax outside of profit or loss | **0.2** | **-** | **0.2** |
| Prior year tax paid during the year | **41.8** | **-** | **41.8** |
| Tax in relation to future periods prepaid | **7.1** | **-** | **7.1** |
| **Tax paid** | **128.6** | **0.2** | **128.8** |

| 2019 | UK £m | India £m | Total £m |
|---|---|---|---|
| **Tax charge** | 49.8 | 0.5 | 50.3 |
| **Effects of:** | | | |
| Other timing differences | 4.3 | (0.1) | 4.2 |
| Tax outside of profit or loss | (0.9) | - | (0.9) |
| Prior year tax paid during the year | 22.1 | - | 22.1 |
| Current year tax to be paid after the reporting date | (22.7) | - | (22.7) |
| **Tax paid** | 52.6 | 0.4 | 53.0 |

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

**49. Operating segments**

The Group segments its lending business and operates under two segments in line with internal reporting to the Board:

- OSB
- CCFS

The Group separately discloses the impact of Combination accounting but does not consider this a business segment.

The financial position and results of operations of the above segments are summarised below:

| 2020 | OSB £m | CCFS £m | Combination £m | Total £m |
|---|---|---|---|---|
| **Balances at the reporting date** | | | | |
| Gross loans and advances to customers | 11,131.4 | 8,001.2 | 209.1 | 19,341.7 |
| Expected credit losses | (83.6) | (28.2) | 0.8 | (111.0) |
| Loans and advances to customers | 11,047.8 | 7,973.0 | 209.9 | 19,230.7 |
| Capital expenditure | 5.3 | 2.4 | - | 7.7 |
| Depreciation and amortisation | 7.1 | 2.4 | 4.3 | 13.8 |
| **Profit or loss for the year** | | | | |
| **Net interest income/(expense)** | 332.8 | 201.2 | (61.8) | 472.2 |
| **Other income** | 18.8 | 17.4 | 0.2 | 36.4 |
| **Total income/(expense)** | 351.6 | 218.6 | (61.6) | 508.6 |
| Administrative expenses | (95.3) | (57.5) | (4.3) | (157.1) |
| Provisions | - | (0.1) | - | (0.1) |
| Impairment of financial assets | (50.7) | (20.5) | 0.2 | (71.0) |
| Impairment of intangible assets | - | - | (7.0) | (7.0) |
| Integration costs | (7.5) | (2.3) | - | (9.8) |
| Exceptional items | (3.3) | - | - | (3.3) |
| **Profit/(loss) before taxation** | 194.8 | 138.2 | (72.7) | 260.3 |
| Taxation | (46.9) | (32.0) | 14.8 | (64.1) |
| **Profit/(loss) for the year** | 147.9 | 106.2 | (57.9) | 196.2 |

## OneSavings Bank plc
## Notes to the Financial Statements (continued)
For the year ended 31 December 2020

**49. Operating segments** (continued)

| 2019 | OSB £m | CCFS £m | Combination £m | Total £m |
|---|---|---|---|---|
| **Balances at the reporting date** | | | | |
| Gross loans and advances to customers | 10,820.6 | 7,374.4 | 294.7 | 18,489.7 |
| Expected credit losses | (35.6) | (8.0) | 0.7 | (42.9) |
| Loans and advances to customers | 10,785.0 | 7,366.4 | 295.4 | 18,446.8 |
| Capital expenditure | 10.2 | 1.1 | - | 11.3 |
| Depreciation and amortisation | 6.3 | 1.3 | 0.6 | 8.2 |
| **Profit or loss for the year** | | | | |
| **Net interest income/(expense)** | 316.2 | 50.1 | (21.6) | 344.7 |
| **Other (expense)/income** | (12.9) | 8.3 | 3.3 | (1.3) |
| **Total income/(expense)** | 303.3 | 58.4 | (18.3) | 343.4 |
| Administrative expenses | (92.3) | (15.1) | (1.3) | (108.7) |
| Provisions | 0.1 | (0.1) | - | - |
| Impairment of financial assets | (11.9) | (0.1) | (3.6) | (15.6) |
| Gain on Combination with CCFS | - | - | 10.8 | 10.8 |
| Integration costs | (2.5) | (2.7) | - | (5.2) |
| Exceptional items | (15.6) | - | - | (15.6) |
| **Profit/(loss) before taxation** | 181.1 | 40.4 | (12.4) | 209.1 |
| Taxation | (47.1) | (10.2) | 7.0 | (50.3) |
| **Profit/(loss) for the year** | 134.0 | 30.2 | (5.4) | 158.8 |

### 50. Adjustments for non-cash items and changes in operating assets and liabilities

| | Group 2020 £m | Group 2019 £m | Company 2020 £m | Company 2019 £m |
|---|---|---|---|---|
| **Adjustments for non-cash items:** | | | | |
| Depreciation and amortisation | **13.8** | 8.2 | **5.7** | 5.4 |
| Interest on investment securities | **(7.5)** | - | **(0.8)** | - |
| Interest on subordinated liabilities | **0.8** | 0.7 | **0.8** | 0.7 |
| Interest on Perpetual Subordinated Bonds | **1.7** | 1.8 | **1.7** | 1.8 |
| Interest on securitised debt | **3.4** | 0.8 | **-** | - |
| Interest on financing debt | **8.4** | 2.4 | **4.4** | 0.3 |
| Impairment charge on loans | **71.0** | 15.6 | **40.4** | 7.5 |
| Impairment on intangible assets acquired on Combination | **7.0** | - | **-** | - |
| (Gains)/losses on sale of financial instruments | **(20.0)** | 0.1 | **(17.8)** | 0.1 |
| Provisions | **0.1** | - | **-** | - |
| Interest on lease liabilities | **0.3** | 0.1 | **0.1** | 0.1 |
| Fair value (gains)/losses on financial instruments | **(7.4)** | 3.3 | **(0.2)** | 13.3 |
| Share-based payments | **5.1** | 4.0 | **4.9** | 4.0 |
| Gain on Combination with CCFS | **-** | (10.8) | **-** | - |
| **Total adjustments for non-cash items** | **76.7** | 26.2 | **39.2** | 33.2 |
| | | | | |
| **Changes in operating assets and liabilities:** | | | | |
| Increase in loans and advances to credit institutions | **(154.0)** | (36.8) | **(51.3)** | (66.2) |
| Increase in loans to customers | **(1,705.0)** | (2,230.8) | **(639.2)** | (1,193.5) |
| Increase in intercompany balances | **-** | - | **(113.9)** | (644.0) |
| Increase in retail deposits | **348.1** | 1,637.8 | **269.6** | 1,363.8 |
| Net decrease/(increase) in other assets | **1.3** | (4.8) | **(0.6)** | (1.9) |
| Net decrease in derivatives and hedged items | **(64.3)** | (20.1) | **(31.7)** | (14.0) |
| Net increase/(decrease) in other customers deposits | **43.2** | (19.2) | **(3.1)** | (24.0) |
| Net decrease in other liabilities | **(6.3)** | (37.3) | **(3.5)** | 2.4 |
| Exchange differences on working capital | **-** | (0.6) | **-** | - |
| **Total changes in operating assets and liabilities** | **(1,537.0)** | (711.8) | **(573.7)** | (577.4) |

### 51. Events after the reporting date

On 26 February 2021, the Group completed the purchase of a c.£55m portfolio of UK residential mortgages, which were serviced by the Group, from a third party. The portfolio was acquired at a discount to current balances.

On 17 March 2021, OSB GROUP PLC issued a trading update stating that it had become aware of potential fraudulent activity by a third party in relation to one of the funding lines provided by the Group, secured against lease receivables and the underlying hard assets. The Group had an outstanding receivable against this funding line of £28.6m as at 31 December 2020. Following an initial report from the Administrator to the third-party company, appointed by the Group the Group concluded that conditions existed as at the end of the reporting period which make this an adjusting post balance sheet event, with an impairment of £20.0m recognised in 2020.

On 22 April 2021, Canterbury Finance No.1 plc (Canterbury 1) sent out a notice from the Company to the Canterbury 1 note holders and the certificate holders informing them of an operational oversight at the Company whereby a proportion of the Canterbury 1 Retention Portfolio, being 107 loans valued at £23.7m that the Company undertook to retain as part of the Canterbury 1 securitisation, was inadvertently included in the portfolio of mortgages acquired by Canterbury Finance No.3 plc (Canterbury 3) for inclusion in a securitisation issued on 4 September 2020 (the Canterbury 3 Securitisation). The Company judges the likelihood of any losses that the Company would have suffered on the Retention Portfolio being mitigated by the transfer of the Canterbury 1 Retention Portfolio to Canterbury 3 to be remote. Nonetheless, to rectify the operational oversight, the Company put in place a guarantee for the benefit of the Canterbury 3 Securitisation which covers losses on the proportion of the Canterbury 1 Retention Portfolio sold to Canterbury 3 in the remote event that such losses were to result in losses on the notes in the Canterbury 3 Securitisation held by third-party investors.

On 27 April 2021, the board approved an interim dividend from the Company to its parent, OSB GROUP PLC (OSBG), for £64.9m payable on the 27 May 2021 subject to the shareholders of OSBG approving the OSBG recommended dividend at the Annual General Meeting on the 27 May 2021.

### 52. Controlling party

As at 31 December 2020 OSB was a wholly owned subsidiary of OSB GROUP PLC (OSBG). OSBG is the largest group preparing consolidated financial statements of which the Company is a member. Copies of OSBG's financial statements may be obtained from the Company Secretary at the registered office: OSB House, Quayside, Chatham Maritime, Chatham, Kent, ME4 4QZ.

### 53. Capital management

The Company's capital management approach is to provide a sufficient capital base to cover business risks and support future business development. The Company remained, throughout the year, compliant with its capital requirements as set out by the PRA, the Group's primary prudential supervisor.

The Company reports on an individual consolidation basis (OSB solo) which includes the Company and subsidiaries except for the offshore servicing entity OSB India, Special Purpose Vehicles relating to securisations and the CCFS entities acquired in October 2019.

The capital management position is based on the three 'pillars' of Basel II.

Under Pillar 1, the minimum capital requirements are based on 8% of risk-weighted assets.

Under Pillar 2, the regulated entities complete an annual self-assessment of risks known as the Internal Capital Adequacy Assessment Process (ICAAP). The PRA applies additional requirements to this assessment amount to cover risks under Pillar 2 to generate a Total Capital Requirement. Further, the PRA sets capital buffers and the regulated entities apply for imposition of the requirements and modification of rules incorporating the capital buffers and Pillar 2 pursuant to the Financial Services and Markets Act 2000.

Basel III came into force through CRD IV. Basel III complements and enhances Basel I and II with additional safety measures. Basel III changed definitions of regulatory capital, introduced new capital buffers, a non-risk adjusted leverage ratio, liquidity ratios and modified the way regulatory capital is calculated.

The ultimate responsibility for capital adequacy rests with the Board of Directors. The Group's ALCO is responsible for the management of the capital process within the risk appetite defined by the Board, including approving policy, overseeing internal controls and setting internal limits over capital ratios.

The regulated entities actively manage their capital position and report this on a regular basis to the Board and senior management via the ALCO and other governance committees. Capital requirements are included within budgets, forecasts and strategic plans with initiatives being executed against this plan.

# OneSavings Bank plc
# Notes to the Financial Statements (continued)
For the year ended 31 December 2020

### 53. Capital management (continued)

The OSB solo Pillar 1 capital information is presented below:

| | **(Unaudited) 2020 £m** | (Unaudited) 2019 £m |
|---|---|---|
| **Common Equity Tier 1 capital** | | |
| Called up share capital | **4.5** | 4.5 |
| Share premium, capital contribution and share-based payment reserve | **8.0** | 875.9 |
| Retained earnings | **1,568.0** | 528.8 |
| Transfer reserve | **-** | (12.8) |
| Other reserves | **(1.1)** | (1.0) |
| Total equity attributable to ordinary shareholders | **1,579.4** | 1,395.4 |
| Foreseeable dividends | **(39.0)** | (25.1) |
| IFRS 9 transitional adjustment[1] | **2.0** | 2.4 |
| COVID-19 ECL transitional adjustment[2] | **20.7** | - |
| Solo consolidation adjustments | **(7.8)** | (6.9) |
| **Deductions from Common Equity Tier 1 capital** | | |
| Investment in subsidiary | **(580.1)** | (603.6) |
| Prudent valuation adjustment[3] | **(0.1)** | (0.2) |
| Intangible assets[4] | **(7.3)** | (8.3) |
| Deferred tax asset | **(0.9)** | (0.9) |
| **Common Equity Tier 1 capital** | **966.9** | 752.8 |
| **Additional Tier 1 capital** | | |
| AT1 securities | **60.0** | 60.0 |
| **Total Tier 1 capital** | **1,026.9** | 812.8 |
| **Tier 2 capital** | | |
| Subordinated debt and PSBs | **47.3** | 47.4 |
| Deductions from Tier 2 capital | **(2.7)** | (0.7) |
| **Total Tier 2 capital** | **44.6** | 46.7 |
| **Total regulatory capital** | **1,071.5** | 859.5 |
| **Risk-weighted assets (unaudited)** | **5,626.3** | 5,351.4 |

[1] The regulatory capital includes a £4.9m add-back under IFRS 9 transitional arrangements. This represents 75% of the IFRS 9 transitional adjustment booked directly to retained earnings of £6.5m. The full impact of IFRS 9, if applied, would reduce total regulatory capital to £1,561.1m.
[2] The COVID-19 ECL transitional adjustment relates to the increase in Stage 1 and Stage 2 ECL following the impacts of COVID-19 and for which transitional rules are being adopted for regulatory capital purposes.
[3] OSB solo has adopted the simplified approach under the Prudent Valuation rules, recognising a deduction equal to 0.1% of fair value assets and liabilities after adjusting for hedge accounting.
[4] All software assets continue to be fully deducted from capital in light of the pending intention of the PRA to consult on the CRR 'Quick Fix' package in this area.

**53. Capital management** (continued)

The movement in CET1 during the year was as follows:

| | (Unaudited) 2020 £m | (Unaudited) 2019 £m |
|---|---|---|
| At 1 January | 752.8 | 561.6 |
| Movement in retained earnings | 1,039.2 | 89.2 |
| Shares issued from Sharesave Scheme vesting | 2.6 | 0.4 |
| Shares issued on Combination with CCFS | - | 707.1 |
| Movement in other reserves | (857.8) | - |
| Movement in investment in subsidiary | 23.5 | (603.6) |
| Movement in foreseeable dividends | (13.9) | 0.1 |
| Movement in solo consolidation adjustment | (0.9) | (1.5) |
| IFRS 9 transitional adjustment | (0.4) | (0.3) |
| COVID-19 ECL transitional adjustment | 20.7 | - |
| Movement in prudent valuation adjustment | 0.1 | (0.1) |
| Net decrease/(increase) in intangible assets | 1.0 | (0.6) |
| Movement in deferred tax asset for carried forward losses | - | 0.5 |
| **At 31 December** | 966.9 | 752.8 |

# OneSavings Bank plc
# Appendices
# Glossary

| | |
|---|---|
| ALCO | Group Assets and Liabilities Committee |
| BoE | Bank of England |
| CCFS | Charter Court Financial Services Group plc |
| CEO | Chief Executive Officer |
| CFO | Chief Financial Officer |
| CRD IV | Capital Requirement Directive and Regulation |
| CRO | Chief Risk Officer |
| DSBP | Deferred Share Bonus Plan |
| EAD | Exposure at Default |
| ECL | Expected Credit Loss |
| EIR | Effective Interest Rate |
| EPS | Earnings Per Share |
| EU | European Union |
| FCA | Financial Conduct Authority |
| FRC | Financial Reporting Council |
| FSCS | Financial Services Compensation Scheme |
| FSD | Forced Sale Discount |
| FTSE | Financial Times Stock Exchange |
| HPI | House Price Inflation |
| IAS | International Accounting Standard |
| ICAAP | Internal Capital Adequacy Assessment Process |
| IFRS | International Financial Reporting Standards |
| ILAAP | Internal Liquidity Adequacy Assessment Process |
| ILTR | Indexed Long-Term Repo |
| IPO | Initial Public Offering |
| IRB | Internal Ratings-Based approach to credit risk |
| LCR | Loss Given Default |
| LIBOR | London Interbank Offered Rate |
| LTV | Loan to value |
| NIM | Net Interest Margin |
| NPS | Net Promoter Score |
| OSB | OneSavings Bank plc |
| OSBG | OSB GROUP PLC |
| PD | Probability of Default |
| PPD | Propensity to go to Possession Given Default |
| PRA | Prudential Regulation Authority |
| PSBs | Perpetual Subordinated Bonds |
| PSP | Performance Share Plan |
| RMBS | Residential Mortgage-Backed Securities |
| RoE | Return on equity |
| RWA | Risk weighted assets |
| SAYE | Save As You Earn or Sharesave |
| SDLT | Stamp Duty Land Tax |
| SICR | Significant Increase in Credit Risk |
| SID | Senior Independent Director |
| SME | Small Medium Enterprise |
| SONIA | Sterling Overnight Index Average |
| SRMF | Strategic Risk Management Framework |
| TFS | Term Funding Scheme |