Secure Trust Bank PLC

Annual Report and Accounts 2018

Straightforward transparent banking

Registered Number 00541132

Contents

Introduction

Secure Trust Bank PLC (‘the Bank’) is an established, well-funded and capitalised UK retail bank. The Bank was founded in 1952, was admitted to AIM in November 2011 and, in October 2016, successfully moved to the Main Market of the London Stock Exchange. The Bank and its subsidiaries are referred to as ‘the Group’.

Our history

2019	New London premises are established at 67 Lombard St, in the heart of the British banking sector
2018	Secure Trust Bank Group customer numbers exceed 1 million and total lending balances exceed £2 billion for the first time
2017	Secure Trust Bank launches into the Consumer Mortgages market in March
2016	Secure Trust Bank Group is awarded Investors In People Gold in December
	Secure Trust Bank Group steps up into the Main Market of the London Stock Exchange in October
	Arbuthnot Banking Group reduces its shareholding in Secure Trust Bank Group to 18% in June
	The Everyday Loans Group is sold in April
2014	Secure Trust Bank’s business finance offer is developed with Commercial Finance and Asset Finance being formed as divisions within the Group
2013	The Real Estate Finance division is formed to support SMEs in providing finance principally for residential development and investment
	The V12 Finance Group is acquired and subsequently the Group’s existing retail finance business is merged with the V12 business
	The Debt Manager Services business is acquired
2012	The Everyday Loans Group is acquired
2011	Secure Trust Bank lists on the Alternative Investment Market in November
2008	Secure Trust Bank’s Motor Finance business begins lending under the Moneyway brand providing hire purchase lending products to a wide range of customers
1985	Secure Trust Bank becomes part of the Arbuthnot Banking Group
1952	Secure Trust Bank is founded

Profit before tax from continuing operations	£34.7 million (2017: £25.0 million)
Total assets	£2.4 billion (2017: £1.9 billion)

31 December 2018 results are stated on an IFRS 9 basis. 31 December 2017 results are stated on an IAS 39 basis.

New business volumes	£million
Business Finance	
Real Estate Finance	303.3
Asset Finance	5.7
Commercial Finance	85.5
Consumer Finance	
Retail Finance	651.5
Motor Finance	141.3
Consumer Mortgages	69.9
Other	4.7
	1,261.9

“Simple and straightforward process. I would recommend to others.”

Strategic report

Group strategy and business model

This section of the Annual Report and Accounts contains the Strategic Report required by the Companies Act 2006 to be prepared by the directors of the Group. It describes the component parts of the Group's business; the principal risks and uncertainties; the development and performance of the business during the financial year; and the position of the business at the end of the year.

Group strategy

The Group's strategy is to build on its current position as an established UK retail bank through a focus on carefully selected and attractively priced segments of the consumer and business markets, prudent underwriting and a prudent approach to capital and liquidity. The Group intends to continue growing its business through responsible lending across its lending divisions, funded by customer deposits and backed by the Group's healthy capital base. It continually monitors and manages its portfolio of assets in line with its risk appetite.

Continued growth and diversification of the balance sheet will be delivered through a combination of organic growth and suitable M&A activity. To achieve this, the Group focuses on:

- Organic growth in responsible lending across a diverse portfolio of attractive segments
- Continued investment in broadening our product offerings to customers
- Pursuing M&A activity on an opportunistic basis
- Optimising our capital and liquidity strategies
- Continuing to target delivery of profit growth in the medium term to create shareholder value.

The Group is well positioned across a range of attractive lending classes and is well placed to meet demand, particularly from businesses needing working capital and from house builders. New consumer products are also being developed in Retail Finance and through the development of the Motor Finance business. As a result, the Group is well placed to continue to deliver balance sheet and earnings growth, particularly if the UK economy improves due to an orderly exit from the EU.

Business model

The Group lends to business and personal customers, funded primarily by customer deposits. It creates value by:

- Delivering high levels of customer satisfaction
- Earning interest, fee and commission income from its lending businesses
- Maintaining efficient funding and operational cost levels
- Controlling loan impairment levels through prudent credit risk management.

Risk management is key to the Group's success. As well as strong credit risk management, the Group manages:

- Its capital and liquidity resources in a prudent manner, and within regulatory limits
- Market risk, particularly the impact of interest rate movements on revenue or asset values
- Operational risk, using a Group-wide framework covering processes, personnel, technology, infrastructure and external factors
- Conduct and regulatory risk, to ensure the Group remains compliant and minimises the risk of customer detriment.

Lending business is sourced primarily through carefully selected business partners and through online channels. The Group intends to grow its lending portfolio across a diverse range of sectors:

Strategic report

Group strategy and business model

Our Divisions

Business Finance	Consumer Finance	Consumer Mortgages	Savings
Secured lending, relatively lower yield and lower risk	Secured and unsecured lending, relatively higher yield and higher risk	Secured lending, relatively lower yield and lower risk	Customer deposits, augmented by modest levels of Bank of England scheme funding
Real Estate Finance Commercial Finance Asset Finance	Retail Finance Motor Finance Debt Managers (Services) Ltd		
Lending decisions are made on an individual transaction basis, using expert judgement and assessment against criteria set out in lending policies	Underwriting technology used to make lending decisions quickly, resulting in high customer satisfaction scores while using strong risk management to minimise bad debt losses	The Consumer Mortgage team is staffed by experienced mortgage and banking individuals with proven property lending expertise and underwriting skills. The team provides full support to customers and introducers over the life of the products	Deposit accounts are promoted to meet funding needs and to broadly match the maturity profiles of loans and deposits. Deposits range from instant access to seven year bonds
Operates primarily from London, Bourne End and Manchester, with offices in Birmingham, Leeds and London	Operates from Solihull, Cardiff and Rotherham	Operates from Bourne End	Operates from Solihull. Deposits are advertised on best buy tables and applied for and serviced online with telephone support
Total Lending at 31 December 2018: £1,027.3 million	Total Lending at 31 December 2018: £905.7 million	Total Lending at 31 December 2018: £84.7 million	Total customer deposits at 31 December 2018: £1,847.7 million
24.7% year on year increase	22.0% year on year increase	413.3% year on year increase	24.6% year on year increase

Asset Finance and Consumer Mortgages are currently closed to new business

Through carefully targeted lending products, the absence of large fixed overheads in the form of a branch network and a policy of not cross-subsidising loss making products with profitable ones, the Group is able to offer competitive deposit interest rates and has been successful in attracting deposits from a wide range of customers.

The Group operates principally from its head office in Solihull, West Midlands, and had 886 employees (full-time equivalent) as at 31 December 2018.

Strategic report

Group strategy and business model

Strategic themes

The Group's strategy is based around three strategic themes. Over 2018, the strategy has developed as follows:

Strategic themes		Developments in 2018
Grow	To maximise shareholder value through strong lending growth by delivering great customer outcomes in both our existing and new markets.	Growth has been maintained across all three lending divisions, driven particularly by Real Estate Finance, Commercial Finance and Retail Finance. Initiatives are underway to develop new Motor Finance products on a new lending platform. Internet banking facilities have been launched to widen the reach and improve accessibility of the Group's savings products.
Sustain	To protect the reputation, integrity and sustainability of the Bank for all of our customers and stakeholders via prudent balance sheet management, investment for growth and robust risk and operational control. Controlled growth is one of the top strategic priorities for the Bank.	The Group has completed the repositioning of its balance sheet, reflecting reduced risk appetite in the face of uncertain market conditions. The residual personal lending book was sold at the end of 2017 and the majority of legacy higher risk loans have run off. The Group withdrew from new Consumer Mortgage lending in early 2019. The Group has added to its capital base and widened its range of available capital sources, having raised £50 million of Tier 2 capital in the year, at an annual coupon of 6.75%.
Love	To ensure that the fair treatment of customers is central to corporate culture and that the Bank is a highly rewarding environment for all staff and one where they can enjoy progressive careers.	The Group has continued to develop its employee and customer propositions. This has resulted in multiple FEEFO Trusted Service awards and recognition at the forthcoming Best Workplace awards. Employee engagement has also been enhanced by the establishment of a Group-wide Employee Council, which includes both the Chief Executive Officer and the Senior Independent Director.

Performance measures

Grow

Key Performance Indicators
- Loans and advances to customers
- Margin ratios:
  - Net interest margin
  - Net revenue margin
  - Gross revenue margin

Sustain

Key Performance Indicators
- Cost ratios:
  - Cost of risk
  - Cost of funds
  - Cost to income ratio
- Funding ratios:
  - Loan to deposit ratio
  - Total funding ratio

Regulatory metrics
- CET 1 ratio
- Total capital ratio
- Leverage ratio

Love

Key Performance Indicators
- Customer FEEFO ratings
- Employee survey trust index score
- Environmental intensity indicator

Key Performance Indicators
- Adjusted profit before tax
- Adjusted profit after tax
- Basic earnings per share
- Adjusted basic earnings per share
- Return ratios:
  - Adjusted return on average assets
  - Adjusted return on average equity
  - Adjusted return on required equity

Strategic report

Group strategy and business model

The Group uses financial and other key performance indicators ('KPIs') to assess its performance against strategic objectives. A summary of the KPIs is set out on page 18 of the Financial Review. Definitions of the KPIs, their calculation and the reasons for their use can be found in the Appendix to the Annual Report on page 218. The regulatory metrics are described on page 24.

Our values

The Group's strategy is underpinned by six values, which are embedded within the Group's culture and are used to evaluate each employee's personal performance:

Our values	
Risk aware	Understanding of risk keeps our customers and us safe and secure.
Change orientated	Embracing change and implementing good ideas gives us a competitive advantage.
Customer focused	Good customer outcomes are at the heart of everything we do.
Performance driven	Secure Trust Bank will only become one of the best banks in Britain by each employee taking personal accountability for their performance.
Teamwork	Companies achieve more when staff work well together.
Ownership	Personal responsibility and taking tasks through to completion benefits the individual as well as customers.

Strategic Report

The following sections of the Strategic Report provide further detail on the Group's strategy, risks and performance:

Chairman's and Chief Executive's statements	Further detail on the Group's performance and key activities in the year, strategic developments, the current business and economic environment, and outlook for the future.
Financial Review	Summary of the Group's financial performance and position, including key performance indicators.
Capital, leverage and liquidity	Description of the Group's capital and liquidity positions, and changes during the year, including regulatory metrics.
Business Review	Further description of the Group's key lending businesses and savings operation, including 2018 performance and future outlook.
Principal risks and uncertainties	Description of the key risks facing the Group, how they are mitigated, and key changes during the year. This includes review of strategic and emerging risks and statements in respect of going concern and viability.
Corporate responsibility	Details of how the Group operates as a responsible business, seeks to exceed customer expectations and builds a culture around its core values.

The Strategic Report is followed by the Corporate Governance Report, which explains the Group's governance arrangements and includes details of the Board of Directors, the Group's corporate governance statement, reports from each of the Board Committees, the Directors' Remuneration Report and summary remuneration policy. The Group's financial statements are then presented from page 134.

Strategic report

Chairman’s statement

2018 has been a successful year for the Group in unsettling economic circumstances. Reducing our exposure to higher risk, higher margin consumer lending activities whilst focusing on lower risk lending has delivered a good set of financial results.

Notable highlights include exceeding more than one million customers; lending balances over £2 billion; growth in statutory profit of 38.8%; growth in basic earnings per share of 42.2%; and the strengthening of our capital base. Our Real Estate Finance, Commercial Finance and Retail Finance businesses have shown strong growth. The Group is now benefiting from the digital savings platform launched in 2017 and won a number of awards including Best Savings Provider, Best Fixed Rate Bond and Best Notice Account Provider from Savings Champion.

An uncertain economic environment creates risks that require careful navigation and this has influenced our risk appetite throughout 2018 and into 2019. We continue to monitor economic indicators and assess the potential impact on our business.

During the year there were a number of changes to the Board. In August Sir Henry Angest and Andrew Salmon stepped down as directors, having contributed significantly to the business over many years including steering the business from wholly owned subsidiary to the Main Market of the London Stock Exchange. On behalf of all my colleagues I would like to record our appreciation and thanks to them. In November I was delighted to welcome Lucy Neville-Rolfe and Paul Myers to the Board following a rigorous search in which the Board was assisted by headhunters Korn Ferry. They bring significant relevant experience to our Board. The introduction of the latest version of the Corporate Governance Code with effect from 1 January 2019 also caused us to review the composition of our Board and Committees and in January I stepped down as a member of the Audit Committee and Paul Lynam stepped down from the Risk Committee. We are now fully compliant with the requirements of the new Corporate Governance Code and intend to continue to be so. The Board comprises two Executive Directors, five independent Non-Executive Directors and myself as Chairman. I am immensely grateful to Ann Berresford, Paul Marrow and Victoria Stewart for the work they have done during the year in chairing the Audit, Risk and Remuneration Committees in what has been a very busy year.

We fully recognise the importance of engaging with all our stakeholders. A new Group-wide Employee Council was established during 2018. We have established direct lines of communication from the Employee Council to the Executive Committee (via the Chief Executive Officer) and to the Board (via the Senior Independent Director and the Chief Executive Officer) both of whom sit on the Employee Council. The results of our employee survey conducted in 2018 were encouraging.

Once again I want to highlight and commend the fantastic charitable and community work being carried out by our employees. I had the opportunity during the year to visit the Birmingham St Mary’s Hospice and see first-hand the impact of what our team can do. This year we were able to enhance our matched giving scheme to support our employees’ fundraising activities. This forms part of our commitment to be a responsible business and make a positive contribution to the community in which we operate.

Strategic report
Chairman's statement

The Board is proposing a final dividend for 2018 of 64 pence per share. This, when added to the interim dividend for 2018 of 19 pence, would mean a full year dividend for 2018 of 83 pence per share. The full year dividend paid in 2017 was 79 pence per share, being made up of an interim dividend of 18 pence plus a final dividend of 61 pence. If approved at the AGM, the 2018 final dividend will be paid on 24 May 2019 to shareholders on the register as at 26 April 2019.

Finally, on behalf of the Board I would like to express my thanks to our CEO, Paul Lynam, and all of our colleagues across the Group for another year of progress and for their continued dedication and commitment. Given the resources at our disposal, the talents of our people, the flexibility of our business model and our clear strategy we can face the future, however uncertain, with optimism and confidence.

Lord Forsyth
Chairman

27 March 2019

Strategic report
Chief Executive's statement

I am delighted to report a strong year's performance for 2018 when viewed across a broad range of customer, staff and financial metrics. I would like to thank the entire STB team for their commitment and professionalism last year and for the way they have continued delivering good outcomes for our all-important customers. As expected, the repositioning of the business model towards lower risk lending, and continued growth in both Business Finance and Consumer Finance, has seen income grow and impairment losses reduce. These factors have driven the strong growth in reported and adjusted earnings.

The financial results for 2018 show the Group statutory profit before tax increasing by 38.8% to £34.7 million compared to the £25.0 million of profit before tax generated from continuing operations during 2017. Adjusted profit before tax on the same basis has increased by 35.9% to £36.7 million. Adjusted earnings per share increased by 39.0% over the same period with basic earnings per share increasing by 42.2%. As shown on page 21, the Group's adjusted return metrics have also improved.

With the benefits of the repositioning of the business model now apparent, the Group entered 2019 with healthy capital and liquidity positions. We have positioned the balance sheet to enable us to navigate the heightened levels of political and economic uncertainty arising from Brexit. The fundamentals of the UK economy are sound and we have seen no discernible change in the behaviour of our consumer customers. The financial sector is resilient. Corporate balance sheets are strong, and the labour market is tight as evidenced by record levels of employment.

Assuming an orderly exit from the EU we expect the UK economic outlook to improve which the Group will seek to leverage as it continues to execute its clearly defined growth strategy. We are well placed to support an increase in demand for working capital funding from businesses and residential development finance from house builders. The latter is aided by a regulatory capital efficient Enable Guarantee we have agreed with the British Business Bank. We are developing new products in our Retail Finance business and are progressing significant investment in our Motor Finance business which will see this portfolio grow considerably over the next 5 years via the provision of dealer stocking finance and a prime motor proposition for consumers. In overall terms we are well positioned in a number of attractive lending classes and have started 2019 strongly. We therefore expect good progress to be made in meeting our goals over the coming period.

Further growth in customer base and satisfaction levels remain very positive

Across our consumer and SME business products we are serving well over 1 million customers. This is a key milestone achievement in 2018. Total customer numbers are a record 1,279,783 customers which is an increase of 29.3% on the total customer base of 989,528 as at 31 December 2017.

We continue to focus on consistently delivering good outcomes for customers and ensuring that the design of our products is appropriate for their needs. From a conduct and behaviour perspective we do not cross subsidise losses or low profits on some products with super profits on others. Nor do we discriminate between customers by, for example, paying very low deposit interest rates to existing loyal customers whilst offering much higher rates to new ones. We believe that our approach is the appropriate way to interact with our customers for the long term benefit of all parties.

Customer satisfaction is measured in a number of ways. It is reassuring that 2018 has once again seen us consistently achieve customer satisfaction ratings in excess of 90% across all of our products as measured by FEEFO. We also use Net Promoter Scores to assess our customer service and these scores exhibit similar positive trends to those derived from FEEFO.

Strategic report
Chief Executive's statement

I am delighted to confirm that for the sixth year running we have retained the Customer Service Excellence standard. This standard was introduced by the Cabinet Office in 2010 to replace the Kite Mark. This indicates our customer service has been judged to meet Government standards of excellence which are benchmarked against high-performing organisations.

Whilst being pleased with external accolades and ongoing high customer satisfaction scores we are in no way complacent. We are focused on improving our existing service and products and diversifying our customer proposition via targeted investment in people, systems, processes and products.

Healthy Capital position

Our ongoing priority is to safeguard the reputation and sustainability of the Group through prudent balance sheet management, investment for long-term sustainable growth and robust risk and operational controls.

Our year end CET1 capital levels are healthy with a CET1 ratio of 13.8% compared to the 2017 year end position of 16.5%. The Total Capital Ratio was 16.3% (2017: 16.8%) and STB's leverage ratio was 10.0% (2017: 12.3%) as at 31 December 2018. The year on year movement in CET1 is a function of the investment of capital to support the strong growth in the loan portfolios. The Total Capital Requirement ratio includes the impact of the issuance of Tier 2 capital, discussed below. The ratios are comfortably ahead of minimum requirements and demonstrate capacity to continue growing customer lending balances in 2019.

As previously disclosed, the Board reviewed the Group's capital structure during the first half of 2018 and determined that an issuance of Tier 2 capital, at the rates available at the time, was advantageous. As a result an issuance of £25 million was made in July and a further issuance of £25 million in October. The annual coupon is 6.75% per annum. This is an annual post-tax cost of 5.4% and represents attractively priced funding which helps the group to reduce its overall weighted average cost of capital.

We will continue to seek to optimise the composition and cost of the Group's capital base particularly given our ongoing growth and ambition albeit barring major developments there are no plans to issue further capital in the forthcoming period.

Prudent liquidity management

Our year end loan to deposit ratio was 109.8% (2017: 107.8%). Customer demand for our deposit products remains very strong, and I am pleased to continue to note that the majority of customers with maturing medium term savings bonds chose to reinvest their funds into deposit products with us. The retention rate reached a new high of 80% for the December 2018 maturities.

The Bank has continued broadly to match-fund its customer lending with customer deposits. This strategy seeks to mitigate maturity transformation and interest basis risks. As the balance sheet grows we have continued to invest in our Treasury function which includes developing the capabilities to utilise hedging instruments should we determine that would be advantageous.

The new deposit platform which went live in the final quarter of 2017 performed well during its first full year of operation in 2018. This is now beginning to deliver benefits for the Group, enhancing the offering, providing internet banking, and improving efficiency and risk controls while providing flexibility to introduce new products. The new technology is also enhancing our customer service proposition whilst providing much greater scalability than the previous platform. This will allow us to fund our very short term lending activities, such as Invoice Finance and some

Retail Finance, with lower cost shorter duration deposit products. This year we also plan to launch cash ISA products which typically offer lower rates than non ISA savings. The planned product diversification will enhance our competitive positioning and continue to support our approach of broadly matching assets and liabilities.

Usage of the Term Funding Scheme (‘TFS’) was increased prior to the closure of the scheme in February 2018 in order to lock in some of the unutilised capacity. This remains a modest part of the Bank’s funding. I flagged in my equivalent statement last year that I expected the closure of the schemes to alter competitive dynamics in the deposit market and this has been the case. Deposit costs have risen modestly and this has been a factor in the compression of Net Interest Margins particularly in the mortgage market. STB’s matched funding strategy and short duration loan book has allowed us to protect NIMs by passing through increases in our funding costs to new borrowers and those whose loans are priced on a variable basis. This key area will require ongoing proactive management whilst TFS continues to unwind.

Income grew and cost of risk reduced

The Group’s operating income grew by 17.1% to a record level of £151.6 million compared to the £129.5 million from continuing operations during 2017. Operating costs rose 18.5% to £84.5 million from £71.3 million in 2017, reflecting continued investment in the business. The cost to income ratio has remained stable at 55.7% (2017: 55.1%).

During 2017 the Group reduced its risk appetite and evolved the business model away from higher risk unsecured consumer credit and towards lower risk secured lending across a focused group of attractive asset classes. This repositioning has driven the expected substantial reduction in cost of risk.

On 1 January 2018, IFRS 9 became effective. IFRS 9 is a more volatile methodology compared to the previous IAS 39. Changes in the performance of underlying loan balances are more immediately reflected in the required IFRS 9 impairment charge as this operates on a forward looking basis whereas under IAS 39 provisions are raised as losses are incurred. The impairment requirement differential is most pronounced in rapidly growing or shrinking and rapidly improving or deteriorating portfolios. The improvement in the quality of the Motor Finance book over 2018, as described in more detail below, has consequently led to a much improved impairment charge for the year using IFRS 9 when compared to the previous year’s result using IAS 39. A future deterioration in performance or economic factors could lead to the reverse impact. Ultimately the profit arising from a particular loan and the associated cash flows are unchanged.

The introduction of IFRS 9 serves to complicate prior year comparisons. On a continuing basis the IAS 39 impairments for 2017 were £33.5 million representing a cost of risk of 2.4% based on average customer lending balances. On a reported basis the IFRS 9 impairment charge for 2018 is £32.4 million representing a cost of risk of 1.8% based on average customer lending balances.

We have carefully monitored lending markets throughout 2018 and note that lenders operating in the sub prime market reported a trend of increasing impairments. These trends would appear to vindicate our decisions to exit sub prime motor finance and near prime medium term personal loans after we identified warning signs in this part of the market in late 2016.

Customer lending activities

Once again strong double digit percentage growth was achieved across the Group's loan portfolio in 2018 notwithstanding the run off of the legacy subprime motor portfolio. Total annual new business lending volumes grew 17.2% to £1,261.9 million (2017: £1,077.1 million) which translated to an increase of 26.9% in overall balance sheet customer lending assets to £2,028.9 million (2017: £1,598.3 million for continuing operations).

Consumer Finance

In 2018 total consumer lending, excluding mortgages, increased 22.0% to £905.7 million (2017: £742.5 million). Our Consumer Finance lending strategy during 2018 centred on running off the sub prime motor portfolio and allocating capital to support the continued growth in Retail Finance, which is shorter term in duration and prime in nature, and higher quality new business in Motor Finance.

The Retail Finance point of sale business, net of provisions, grew strongly as intended, with customer lending balances at 31 December 2018 increasing 32.1% to £597.0 million (2017: £452.3 million). Our Retail Finance business has continued to evolve as we have grown into one of the largest participants in this market. We are writing a broader spectrum of business including increased levels of interest bearing lending. This lending has higher levels of impairments compared to interest free finance and this is factored into our pricing to ensure we achieve our targeted risk adjusted return. The impairments and risk adjusted returns in 2018 have been in line with our expectations. However, the volatility of the IFRS 9 methodology compared to IAS 39, coupled with the rapid balance sheet growth has an impact on the V12 reported results.

During the year we made significant progress in repositioning the motor book. The legacy sub prime loans have been run down to an immaterial level and we have successfully replaced these assets with new originations of a much higher quality. As a result customer lending balances, net of provisions, have been held flat year on year with £276.4 million at 31 December 2018 compared to £274.6 million in the prior year. As expected the repositioning has driven lower like-for-like impairments in the motor portfolio and profitability margins improved as the drag effect of the run off of the sub prime part of the book abated.

The markets for those debt collection agencies fully authorised by the Financial Conduct Authority improved as more operators exited the market or were consolidated within larger entities. These attributes translated into more opportunities for Debt Managers (Services) Limited ('DMS') in the third party debt collection and portfolio acquisition spaces during 2018. The Group has taken advantage of these opportunities, with DMS generating an excellent financial result. Overall, the profit before tax of £1.6 million in 2018 for this business was well above the £0.6 million recorded for the prior year.

Consumer Mortgage lending balances have increased from £16.5 million as at 31 December 2017 to £84.7 million as at 31 December 2018 being growth of 413%. During 2018 the residential mortgage market showed increasingly aggressive competitive pressures, with lenders increasingly competing on price and risk appetite to drive new business volumes. It is no surprise that in the early part of 2019 lenders including Metro Bank, Santander UK and Nationwide Building Society have all reported Net Interest Margin contraction. My expectation is that the trend of increasing loan-to-value metrics and lower new net lending margin is likely to be sustained throughout 2019 before subsequently being tempered or reversed by factors detailed below under the 'evolving regulatory and competitive environment' heading. Given we have the options to profitably deploy capital elsewhere that would otherwise be used to support residential mortgage lending, as previously disclosed we have decided to cease origination of new residential mortgage business until conditions become more favourable. This change is not expected to have a material impact on 2019 earnings.

Strategic report

Chief Executive's statement

Business Finance

The Group's SME lending operations have grown strongly, as targeted, and I expect further positive progress in 2019 given we started the year with a strong new business pipeline. Total business customer lending balances in 2018 increased 24.7% to £1,027.3 million (2017: £824.0 million). Real Estate Finance lending balances increased by 32.5% to £769.8 million as at 31 December 2018 (2017: £580.8 million).The loan book is performing well and remains biased in favour of modestly leveraged residential investment lending. This is reflected in the portfolio composition, which in round terms is split 70% / 30% in favour of investment lending versus development lending. We have continued to adopt a cautious stance towards Central London house building finance. Outside of Central London demand for property development finance has remained robust and the units we have financed have continued to sell well, in a number of cases faster and for higher values than originally expected. The average LTV across the whole Real Estate Finance portfolio remains less than 60%.

In previous statements I noted that some lenders were offering loans up to or exceeding 100% of open market value on asset finance at extremely low margins, by historical standards. 2018 saw a 10% increase in company insolvencies in England and Wales to the highest level since 2014. As such it is not surprising to note that the Asset Finance market has seen an increase in customer defaults and in impairments during the year. We are not prepared to compromise on risk or price simply to achieve short term net balance sheet growth, and as matters stand expect this part of the lending portfolio to continue to contract as we are not writing new business. Asset Finance lending balances contracted to £62.8 million as at 31 December 2018 compared to £116.7 million a year ago. We will revisit our appetite for recommencing new lending in light of market developments in this scale part of the UK SME lending market.

Secure Trust Bank Commercial Finance, the invoice finance division of the Bank, had another excellent year and has now funded over £2.5 billion of customers' invoices since launch. Excluding the systemic banks, based on customer lending balances we are now the 5th largest operator in the invoice finance market but given the fragmented nature of the market we have substantial opportunities to continue to grow very strongly in this sector. This is evidenced by customer lending balances, which net of provisions grew 53.9% to £194.7 million at 31 December 2018 (2017: £126.5 million). I continue to believe we have one of the most capable teams of invoice financiers in the UK, supported by a scalable modern IT platform. This, coupled with Group management's experience in SME and corporate lending, gives STB a distinct advantage when it comes to structuring transactions and responding rapidly to opportunities. Impairments levels here have been immaterial reflecting very robust credit management disciplines.

Fee based accounts

As expected, the legacy OneBill product, which closed for new business in 2009, continues to see customer numbers decline over time. Customer numbers fell to 18,032 by 31 December 2018 compared to 18,963 a year earlier.

Evolving regulatory and competitive environment

From a Prudential Regulation perspective it is apparent that the regulatory direction of travel with the introduction of the MREL regime and the reforms to the Basel Capital requirements is to reduce the capital differentials between the systemic and non-systemic firms which should ultimately bode well for smaller banks.

Strategic report
Chief Executive’s statement

I have noticed a change in regulatory tone particularly by the Financial Conduct Authority (‘FCA’) during 2018. In my opinion the FCA increasingly acknowledges that when it comes to many financial products, not just in banking, loyalty does not pay, it costs. On average, long term savers are paid considerably lower interest rates than newer customers and mortgage borrowers moving from initial fixed rates to standard variable rates (‘SVR’) typically pay the highest interest rates. This is the thrust of the Super Complaint lodged by the Citizens Advice Bureau in 2018 which I believe is intended to tap into the changing public and political mood, especially with the ongoing drive by regulators and politicians to be seen to protect what they describe as vulnerable customers. In late December 2018 the FCA provided the following update: 'The treatment of long-standing customers remains a priority for the FCA. We have worked closely with the CMA since they received the super-complaint. We will continue to do this. It is important that this issue is tackled and harmful practices are stopped. We expect firms to look after the interests of all customers and treat them fairly, whether they are new or longstanding. Where we have concerns about conduct by firms, we will explore all options to address this using the full range of our powers’.

In banking, millions of inert savers are paid extremely low interest rates with this extremely cheap funding helping those banks concerned to use price to dominate large parts of the lending market. This is especially so in mortgages where the additional profit subsidisation effects of high SVRs on back books allows the biggest banks and building societies to charge extremely low margins on front books. These dynamics and the current capital differentials (the latter being addressed over time by the incoming Basel capital floors) are key reasons why the 10 biggest firms control 90% of that market.

The FCA has thus far followed a ‘sunlight’ strategy in the hope that by raising consumer awareness of the costs of inertia they would drive changes in behaviours which would give better outcomes for consumers. This has not been as successful as desired which I believe is a key reason why the FCA is now seriously considering more direct intervention. One manifestation of this is their proposed Basic Variable Minimum Savings Rate which would greatly benefit inert long term savers. This will impact the cost of the deposit back book for the larger banks and some building societies and means they would need to accept lower profits or more likely seek to maintain NIM by increasing lending margins and / or pay less for front book deposits. By definition the challenger banks do not attract inert savings customers. So if the dominant banks need to increase lending margins it should logically increase the proportion of the market that can be economically served by the smaller challengers and specialist banks.

It is worth noting that the last Competition and Markets Authority banking market investigation highlighted that residential mortgage lending was by far the most profitable thing banks do and that the systemic firms were more profitable than the smaller ones. It is entirely possible that the FCA will consider intervention in the SVR market (the huge differences between new lending margins and SVR cannot be objectively justified in my view). This has a range of ramifications not least of which is the impact on Effective Interest Rate (‘EIR’) accounting. EIR allows lenders to recognise mortgage profits now based on assumed customer behaviours in the future. If SVR intervention arises then there will likely be EIR and profit ramifications. Should such a situation come to pass then the likely winners will be those who do not rely on inert savers and those who do not rely on high cost SVR customers providing super profit margins on the mortgage side.

Strategic report
Chief Executive's statement

During 2018 a number of stakeholders have recognised that post Brexit HM Government could choose to adopt a much more proportionate approach to the regulation of smaller non-internationally active banks than is possible today. Certainly one of the implications of the UK's exit from the European Union is that it can address the shortcomings of the 'one size fits all' Capital Requirements Regulation implementing the Capital Requirements Directive IV, if the appetite exists.

In summary whilst the situations above remain somewhat fluid, I am increasingly optimistic that cumulative actual and potential action by regulators could help to materially improve the competitive positioning of smaller banks in the UK.

Strategic priorities

The Group's three strategic priorities of: (i) organic growth, (ii) diversification and (iii) M&A activity are unchanged.

The benefits of a diversified business model have been evident during 2018 when we have been able to reallocate capital from higher risk higher margin to lower risk lower margin lending activities whilst continuing to scale the Group's balance sheet and grow our profitability.

The focus for 2019 is on:

- (i) Organic growth in responsible lending across a diverse portfolio of attractive segments.
- (ii) Continued investment in broadening our product offerings to customers.
- (iii) Pursuing M&A activity on an opportunistic basis.
- (iv) Optimising our capital and liquidity strategies.
- (v) Continuing to target delivering profit growth in the medium term to create shareholder value.

Our long-term ambition remains to grow a broad based portfolio, balanced across consumer finance, SME finance and residential mortgage lending.

We will continue to grow our Retail Point of Sale (V12) and Motor propositions in the Consumer Finance sector. V12 has delivered six years of balance sheet and profit growth since being acquired in January 2013. Whilst now a top five player it has a modest market share and considerable potential to continue growing our lending balances which are relatively short term in duration and prime in nature.

The market for Motor Finance in the UK is nearly £60 billion. This is a highly fragmented and competitive space where we have a £0.25 billion share predominantly in non-prime lending. This is an important and profitable line of business for us. We see opportunities to continue to grow our near-prime lending and have now initiated a transformation programme which will see us offering a whole of market solution to dealers and brokers. This will include dealer stocking and prime / near-prime consumer lending products. The existing lenders in this space enjoy attractive returns on equity and we believe that the combination of the competitive funding costs provided via our banking licence and brand new technology will allow us to gain market share and grow a sizable business in this space over the next 3-5 years.

Economic and political related uncertainties have influenced UK residential house prices during 2018 with these having barely appreciated in value over the period. This has informed our risk appetite for new lending to house builders in the year with our Loan to Gross Development Value limits remaining modest to ensure that the borrower has hard equity in any deal and to provide a buffer lest market values fall. Strategically we remain committed to supporting the Government policy of building more new homes and believe an orderly exit from the EU will be positive for the UK housing market. With this in mind the Group has entered into, but not yet triggered, an ENABLE Guarantee with the British Business Bank. This is designed to enable banks to increase their lending to SMEs by reducing the amount of capital required to be held against such lending. Under an ENABLE Guarantee, the UK Government takes on a portion of the counterparty's risk on a portfolio of loans to smaller businesses in return for a fee. Assuming an orderly Brexit and positive reaction in the UK housing market the Group will allocate this additional capital to increase its funding to new build and redevelopment projects undertaken by SME housebuilders and developers.

The UK Invoice Finance and Asset Finance markets are large, fragmented and growing markets of around £20 billion each. We are very pleased with the progress made by STB Commercial Finance. We see significant future growth potential and would be interested in acquiring businesses in these spaces if the risk profile and economics of any transaction are attractive.

Residential mortgage lending is the biggest single part of the UK lending market. As previously disclosed the Group has ceased originating new residential mortgage loans due to concerns about current market practices in respect of risk and price. The capital that would otherwise have been used to support mortgages lending growth is being deployed for more optimal short-term returns. We remain interested in inorganic opportunities that would get us to the critical mass necessary to be profitable, if the economics of such a transaction were compelling. I believe the factors that will serve to make market conditions more attractive over time will be the introduction of the MREL regime, the significant Basel capital reforms, the unwinding of the Term Funding Scheme, a tightening in the securitisation market which is already impacting some non-bank lenders and the potential for FCA price intervention in the inert savings market. We will closely monitor these evolving situations which will inform our strategic thinking.

In support of our strategy, we have engaged in a number of discussions relating to inorganic business opportunities during 2018 but none progressed to a conclusion that was acceptable to us. Our previous M&A activities have generated considerable shareholder value due in part to the discipline that we apply. We will continue to be disciplined in our approach to opportunities, prioritising the creation of sustainable, long-term shareholder value. We are continuing to work on a diverse pipeline of external business opportunities.

Current trading and outlook

Notwithstanding the slowing in UK economic activity in the latter part of 2018 and into the New Year we are pleased with our performance in the early part of 2019 which is in line with management expectations.

Management and the Board are very carefully monitoring the highly fluid political situation. We have a range of early warning indicators and contingency plans in place in the event a no deal Brexit leads to an economic downturn. We have seen no discernible change in our consumer businesses. We have deliberately repositioned the Group's balance sheet away from higher risk consumer lending to mitigate the potential of a disorderly Brexit and ensured the overall loan book is of a short duration. To provide some context the Group's Retail Finance lending balances now exceed £600 million. On average we are lending over £50 million per month in this area. It follows that in a stressed economy we could reduce these credit exposures in a rapid and orderly fashion. This sort of option does not exist in the medium term unsecured personal loan or credit card market. This was a factor in us exiting the former in December 2017.

Economic and political related uncertainties are weighing on the UK economy albeit this has impacted businesses much more than consumers. Concerns about the potential for a no deal exit from the EU to cause a change in consumer behaviour and an increase in loan impairments due to a squeeze on the cost of living caused by a weaker pound have negatively impacted the values of UK financial assets and bank share prices. Our SME businesses have performed well and have substantial new business pipelines, some of which is due to planned transactions being delayed whilst business owners wait to see on what basis and over what timescale the UK exits the EU. Given this, the fact that current UK economic fundamentals are solid with record employment levels, the lowest unemployment since 1975 and real take home pay rising provides grounds for optimism. My belief is that an orderly Brexit will trigger an increase in business investment which will be good for employment and pay. An abating of political and economic uncertainty should be positive for the value of financial assets and business and consumer confidence generally.

In summary, the Group's lending portfolio is appropriately positioned for the current conditions and the short duration nature of the asset portfolio means the Group can react quickly to both opportunities and threats.

The Group entered 2019 with positive business momentum, healthy capital positions and very strong liquidity and remains well placed to pursue its strategic priorities.

Paul Lynam
Chief Executive Officer

27 March 2019

Strategic report

Financial review

Adjusted profit reconciliation	2018 Total £million	2017 Continuing operations £million	2017 Discontinued operations £million	2017 Total £million
Interest, fee and commission income	188.6	157.3	8.0	165.3
Interest, fee and commission expense	(37.0)	(27.8)	-	(27.8)
Operating income	151.6	129.5	8.0	137.5
Impairment losses	(32.4)	(33.5)	(3.4)	(36.9)
Operating expenses	(84.5)	(71.3)	(0.3)	(71.6)
Profit on sale of Non-Standard Finance plc shares	-	0.3	-	0.3
Profit before tax	**34.7**	**25.0**	**4.3**	**29.3**
Adjustments to profit before tax (see below)	2.0	2.0	(4.3)	(2.3)
Adjusted profit before tax	**36.7**	**27.0**	-	**27.0**
Adjusted tax	(6.8)	(5.5)	-	(5.5)
Adjusted profit after tax	**29.9**	**21.5**	-	**21.5**
Adjusted basic earnings per share (pence)	**161.8**	**116.4**	-	**116.4**
Statutory results				
Profit before tax	34.7	25.0	4.3	29.3
Tax	(6.4)	(5.1)	(0.8)	(5.9)
Profit after tax	**28.3**	**19.9**	**3.5**	**23.4**
Gain recognised on disposal after tax	-	-	0.4	0.4
Profit for the year	**28.3**	**19.9**	**3.9**	**23.8**
Basic earnings per share (pence)	**153.2**	**107.7**	**21.1**	**128.8**
Adjustments to profit before tax				
Fair value amortisation	0.3	0.9	-	0.9
Transformation costs	0.4	0.8	-	0.8
Bonus payments	1.3	0.6	-	0.6
Profit on sale of Non-Standard Finance plc shares	-	(0.3)	-	(0.3)
Discontinued operations	-	-	(4.3)	(4.3)
Adjustments to profit before tax	**2.0**	**2.0**	**(4.3)**	**(2.3)**

Strategic report

Financial review

Key performance indicators

The following key performance indicators, stated for continuing operations, are the primary measures used by management to assess the performance of the Group:

Financial KPIs

Adjusted profit	Earnings per share	Return ratios
Adjusted profit before tax **£36.7 million** 2017: £27.0 million	**Basic earnings per share** **153.2 pence** 2017: 107.7 pence	**Adjusted return on average assets** **1.4%** 2017: 1.3%
Adjusted profit after tax **£29.9 million** 2017: £21.5 million	**Adjusted basic earnings per share** **161.8 pence** 2017: 116.4 pence	**Adjusted return on average equity** **13.1%** 2017: 8.9%
		Adjusted return on required equity **14.8%** 2017: 13.5%

Growth	Margin ratios	Cost ratios	Funding ratios
Loans and advances to customers **£2,028.9 million** 2017: £1,598.3 million	**Net interest margin** **7.4%** 2017: 8.1%	**Cost of risk** **1.8% on an IFRS 9 basis** 2017: 2.4% (on an IAS 39 basis)	**Loan to deposit ratio** **109.8%** 2017: 107.8%
	Net revenue margin **8.3%** 2017: 9.1%	**Cost of funds** **2.0%** 2017: 1.9%	**Total funding ratio** **118.2%** 2017: 115.5%
	Gross revenue margin **10.4%** 2017: 11.1%	**Cost to income ratio** **55.7%** 2017: 55.1%	

Non - financial KPIs

Customer FEEFO ratings **4.7 stars** 2017: 4.7 stars (mark out of 5 based on star rating from 1,175 reviews (2017: 608 reviews))	**Employee survey trust index score** **77%** (new measure, based on 2018 all staff survey 2018 engagement score 76% 2017: 78%)	**Environmental intensity indicator** **3.5** 2017: 4.2 (tonnes carbon dioxide per £1 million Group income)

The Remuneration Report, starting on page 97, sets out how executive pay is linked to the assessment of key financial and non-financial performance metrics.

These KPIs represent alternative performance measures that are not defined or specified under IFRS. Definitions of the financial KPIs, their calculation and an explanation of the reasons for their use can be found in the Appendix to the Annual Report on page 218. In the narrative of this financial review, KPIs are identified by being in bold font. Further explanation of the non-financial KPIs is provided in the corporate responsibility section on page 54.

Strategic report

Financial review

Unless otherwise stated, the analyses within the Strategic Report relate to continuing operations, which represents all of the Group's divisions, excluding PLD.

Interest, fee and commission income

Interest, fee and commission income is made up of interest income, which is predominantly earned on loans and advances to customers, and fee and commission income, which consists principally of fees from the OneBill, Commercial Finance, Retail Finance and Motor Finance products and commissions earned on debt collection activities in DMS.

Interest income was £169.2 million for 2018, increasing by £27.9 million (19.7%) on 2017, which was driven by the growth of the Group's loan books over the year. **Loans and advances to customers** increased from £1,598.3 million to £2,028.9 million over the year.

Fee and commission income was £19.4 million for 2018, increasing by £3.4 million (21.3%) on 2017. The growth relates to increasing levels of fees earned on Commercial Finance and Retail Finance lending, with fee income relating to OneBill continuing to decrease year on year, as this product is closed to new business.

The **gross revenue margin** reduced from 11.1% to 10.4%. This reflects the continued repositioning of the balance sheet to lower risk lower return lending. In particular, growth in Motor Finance lending which yields relatively high margins was modest in 2018, compared with more significant growth in Retail Finance and the low risk Business Finance portfolios.

Interest, fee and commission expense

Interest, fee and commission expenses is made up of interest expense, which is incurred in respect of deposits from customers, subordinated liabilities and TFS borrowings, and fee and commission expense, comprising mainly fees and commissions on the Motor product, and commissions paid on debt collection activities in DMS.

Interest expense was £35.5 million for 2018, increasing by £8.8 million (33.0%) on 2017. The **cost of funds** increased from 1.9% for 2017 to 2.0% for 2018. The impact on the Group of the rise in the Bank of England base rate during the year was limited in 2018, given the predominantly fixed rate deposit funding. The interest expense for 2018 includes the cost of subordinated debt raised during the year, as explained further in Note 24.

The Group's **net interest margin** reduced from 8.1% in 2017 to 7.4% in 2018, primarily due to the mix of business referred to above.

Fee and commission expense has increased by £0.4 million (36.4%), mainly arising from the increase in activity in DMS, as set out in the business review on page 36.

Operating income

Operating income increased by 17.1% to £151.6 million (2017: £129.5 million).

The **net revenue margin** for 2018 was 8.3% compared with 9.1% for 2017. The reduction in this margin is due to the factors referred to above.

Strategic report

Financial review

Impairment losses

Impairment losses during the year were £32.4 million (2017: £33.5 million). The impairment losses for 2018 are calculated using the expected credit loss methodology required by IFRS 9, whereas the comparative impairment losses for 2017 were calculated using the incurred loss methodology set out in IAS 39. The expected increase in charge brought about by the change in methodology to IFRS 9, which accelerates the recognition of losses particularly for growing books, has been offset by improvement in performance, particularly in respect of Motor Finance lending.

The provision charge includes the impact of applying expert credit judgement, resulting in overlays being added to provision levels estimated using the Group's models. A breakdown of the charge by product is shown in Note 3.

The **cost of risk** for 2018 on an IFRS 9 basis was 1.8%. The cost of risk on an IAS 39 basis was 2.4% for 2017. Further analysis of the Group's loan book and its credit risk exposures is provided in Notes 11, 12, 13 and 30.

Operating expenses

Operating expenses have increased, reflecting the investments made in the infrastructure and staff resources of the Group to achieve growth targets, from £71.3 million in 2017 to £84.5 million in 2018. The Group's **cost to income ratio** increased to 55.7% from 55.1% for 2017. The infrastructure growth has been focused on motor transformation, Treasury and risk management enhancements.

Taxation

The effective adjusted tax rate has fallen to 18.5%:

	2018 Effective adjusted tax rate	2018 Effective statutory tax rate	2017 Effective adjusted tax rate	2017 Effective statutory tax rate
	£million	£million	£million	£million
Tax	6.8	6.4	5.5	5.1
Profit before tax	36.7	34.7	27.0	25.0
Effective rate (%)	**18.5%**	**18.4%**	**20.4%**	**20.4%**

The effective rate in the year was reduced by a deferred tax credit of £0.5 million arising from a reassessment of the rates that the deferred tax asset on the IFRS 9 transition adjustment will reverse out at over the next nine years. The tax charge reflects Bank Corporation Tax Surcharge of 8% on taxable profits of Secure Trust Bank PLC in excess of £25.0 million. Future effective tax rates for the Group will be sensitive to the quantum of projected profits in the Bank and other Group companies as well as the level of corporation tax which is due to reduce to 17% with effect from 1 April 2020. Current forecasts show that the effective tax rate is expected to increase by up to 4% over the forecast period, as the effect of the banking surcharge becomes more significant.

Distributions to shareholders

The directors recommend the payment of a final dividend of 64 pence per share which, together with the interim dividend of 19 pence per share paid on 28 September 2018, represents a total dividend for the year of 83 pence per share (2017: 79 pence per share).

Earnings per share
Detailed disclosures of earnings per ordinary share are shown in Note 8 to the Annual Report. Basic earnings per share increased by 42.2% to 153.2 pence per share (2017: 107.7 pence), as a result of the increase in profit after tax. The **adjusted basic earnings per share** increased by 39.0% to 161.8 pence per share (2017: 116.4 pence per share).

Adjusted returns
The Group measures **adjusted returns on average assets, average equity and required equity** as set out in the KPIs table on page 18. Return on average assets demonstrates how profitable the Group's assets are in generating revenue. Return on average equity is a measure of the Group's ability to generate profit from the equity available to it. Return on required equity relates profitability to the capital that the Group is required to hold.

These ratios have all improved in comparison to 2017, driven by a combination of the improving profitability and the impact of the IFRS 9 transition adjustment reducing assets and equity at 1 January 2018.

Summarised balance sheet

	2018 £million	2017 £million
Assets		
Cash and balances at central banks	169.7	226.1
Debt securities	149.7	5.0
Loans and advances to banks	44.8	34.3
Loans and advances to customers	2,028.9	1,598.3
Other assets	51.2	27.9
	2,444.3	**1,891.6**
Liabilities		
Due to banks	263.5	113.0
Deposits from customers	1,847.7	1,483.2
Tier 2 subordinated liabilities	50.4	-
Other liabilities	45.6	46.3
	2,207.2	**1,642.5**

The assets of the Group increased by 29.2% to £2,444.3 million, primarily driven by the growth in the Group's loan portfolios.

The liabilities of the Group increased by 34.4% to £2,207.2 million, primarily driven by the increase in deposits from customers, providing funding for the Group's lending activities, the use of the Term Funding Scheme as shown in amounts due to banks, and the issue of £50 million of Tier 2 regulatory capital.

Loans and advances to customers
Loans and advances to customers include secured and unsecured loans and finance lease receivables. The composition of the loan book remains broadly consistent with 2017, with the Consumer Finance book being approximately 45% of total lending, and the Business Finance book being approximately 51%. The Consumer Mortgage business currently accounts for 4% of total lending.

Financial review

Loan originations in the year, being the total of new loans and advances to customers entered into during the year, increased by 17.2% to £1,261.9 million (2017: £1,077.1 million). Over half of the new business volume (£651.5 million) was generated by the Retail Finance business.

Further analysis of loans and advances to customers, including a breakdown of the arrears profile of the Group's loan books, is provided in Notes 11, 13 and 30.

Debt Securities

Debt Securities consist solely of sterling UK Government treasury bills. The increase in the year to £149.7 million from £5 million in 2017 was for the purpose of providing collateral against Term Funding Scheme drawings with the Bank of England.

Due to Banks

The amount due to banks consists solely of drawings from the Bank of England Term Funding Scheme. The Group has drawn modest levels of this low cost source of funding to supplement customer deposit funding.

Deposits from customers

Customer deposits include term, notice and sight deposits, as well as the Group's current account and OneBill products. Customer deposits grew by 24.6% during the year to close at £1,847.7 million, to fund the increased lending balances.

Tier 2 subordinated liabilities

Tier 2 subordinated liabilities represent two £25 million tranches of 6.75% Fixed Rate Callable Subordinated Notes, including interest accrued. Further details of the note issuances are provided in Note 24. The notes qualify as Tier 2 capital. In the previous year, the Group's Tier 2 capital consisted solely of the collective impairment allowance.

New accounting standards

IFRS 9 'Financial Instruments', effective for the period beginning on 1 January 2018, has replaced IAS 39 'Financial Instruments: Recognition and Measurement'. Adoption of the standard has resulted in new accounting policies for interest income and expense, the classification and measurement of financial instruments and the impairment of financial assets and loan commitments which are set out in Note 1. Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except that comparatives for the year ended 31 December 2017 are stated on an IAS 39 basis, and therefore have not been restated.

IFRS 15 'Revenue from contracts with customers', which is also effective for the period beginning on 1 January 2018, replaces a number of existing standards and interpretations. Following consideration of the Group's operating model, it has been concluded that this standard does not have a material impact on the Group.

Discontinued operations

On 21 December 2017 the Group sold a portfolio of legacy unsecured personal loans ('PLD') to Alpha Credit Solutions 8 S.à.r.l., a company owned by AnaCap Credit Opportunities III LP. Results relating to the portfolio of unsecured personal loans have therefore been classified as discontinued operations for the year ended 31 December 2017 throughout this Annual Report. The profit before tax relating to the unsecured personal loan portfolio announced shortly after its sale for the year ended 31 December 2017 has been adjusted for statutory purposes as follows:

	Profit before tax as announced £million	Internal cost of funds added back £million	Internal attributable costs added back £million	Statutory profit before tax £million	Tax £million	Statutory profit after tax £million
Year ended 31 December 2017	2.4	1.5	0.4	4.3	(0.8)	3.5

Strategic Report

Capital, leverage and liquidity

Capital

The Group's capital management policy is focused on optimising shareholder value over the long-term. Capital is allocated to achieve targeted risk adjusted returns whilst ensuring appropriate surpluses are held above the minimum regulatory requirements. The Board reviews the capital position at every Board meeting.

The Group's regulatory capital is divided into:

- CET1 which comprises shareholders' funds, after adding back the IFRS 9 transition adjustment and deducting intangible assets, both of which are net of attributable deferred tax
- Tier 2 capital, which is solely subordinated debt issued during the year net of unamortised issue costs, capped at 25% of the capital requirement. At 31 December 2017, Tier 2 capital represented the collective allowance for impairment. Under IFRS 9, there is no longer a collective allowance.

In July 2018 the Group issued £25.0 million of Tier 2 capital and a further £25.0 million was issued in October 2018. Further information on these issuances is contained in Note 24.

The Group has elected to adopt the IFRS 9 transitional rules. For 2018 this allowed 95% of the initial IFRS 9 transition adjustment, net of attributable deferred tax, to be added back to eligible capital. Further information is provided in the Group's Pillar 3 report available at www.securetrustbank.com/investor-information.

Strategic and capital allocation decisions are therefore made with reference to estimated credit losses calculated using IFRS 9 methodology.

The Group's Individual Capital Adequacy Assessment Process ('ICAAP') includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. All regulated entities within the Group have complied during the year with all of the externally imposed capital requirements to which they are subject.

The Group operates the standardised approach to credit risk, whereby risk weightings are applied to the Group's on and off balance sheet exposures. The weightings applied are those stipulated in the Capital Requirements Regulation.

Capital, leverage and liquidity

	2018 (IFRS 9 transitional rules basis) £million	2017 £million
Capital		
CET1 capital	251.8	238.9
Total Tier 2 capital	45.7	4.4
Total capital	**297.5**	**243.3**
Total Risk Exposure	**1,824.6**	**1,446.1**

	2018 (IFRS 9 transitional rules basis %	2017 %
CRD IV ratios		
CET1 capital ratio	13.8	16.5
Total capital ratio	16.3	16.8
Leverage ratio	10.0	12.3

The CET1 capital ratio is the ratio of CET1 capital divided by the Total Risk Exposure. The total capital ratio is total capital divided by Total Risk Exposure. The Group has maintained a healthy CET1 capital ratio and total capital ratio and these provide a capital buffer for continued growth.

Leverage

The Basel III framework introduced a relatively simple, transparent, non-risk based leverage ratio to act as a supplementary measure to the risk-based capital requirements. The leverage ratio is intended to restrict the build-up of leverage in the banking sector to avoid destabilising deleveraging processes that can damage the broader financial system and the economy, whilst reinforcing the risk-based requirements with a complementary simple, non-risk based ‘backstop’ measure.

The Basel III leverage ratio is defined by the Capital Requirements Regulation as Tier 1 capital divided by on and off balance sheet asset exposure values, expressed as a percentage. The UK leverage ratio framework sets a minimum ratio of 3.0%, which increased to 3.25% on 1 January 2018. As shown in the table above, the Group’s leverage ratio remains comfortably ahead of the minimum requirement.

Liquidity

The Group continues to manage its liquidity on a conservative basis by holding High Quality Liquid Assets and utilising predominantly retail funding from customer deposits. Secure Trust Bank is a participant in the Bank of England’s Sterling Money Market Operations under the Sterling Monetary Framework. As such, from July 2013, the Group was permitted to draw down facilities under the Funding for Lending Scheme and subsequently its replacement, the Term Funding Scheme.

Strategic Report

Capital, leverage and liquidity

At the year end and throughout the year, the Group had significant surplus liquidity over the minimum requirements due to its stock of High Quality Liquid Assets ('HQLA'), in the form of the Bank of England Reserve Account and UK Treasury Bills. As shown in the table below, total liquid assets increased by 37.2% from £265.4 million to £364.2 million, with the High Quality Liquid Assets balance being £319.4 million.

	2018 £million	2017 £million
Liquid assets		
Aaa – Aa3	319.4	231.1
A1 – A3	39.7	29.3
Unrated	5.1	5.0
Liquidity exposures	**364.2**	**265.4**

For Liquidity Coverage Ratio ('LCR') purposes the HQLA excludes UK Treasury Bills which are encumbered to provide collateral as part of the Group's Term Funding Scheme with the Bank of England. The total of unencumbered HQLA for LCR purposes is £240.8 million (2017: £231.1 million).

The Group has no liquid asset exposures outside of the United Kingdom and no amounts that are either past due or impaired.

The Group's LCR, and other measures used by management to manage liquidity risk, are described in the Principal Risks and Uncertainties section of the Strategic Report.

Strategic report

Business review – Business Finance

Real Estate Finance

Real Estate Finance was formed as a division within the Group in 2013. The division supports SMEs in providing finance principally for residential development and residential investment.

What we do

Residential Development

The Group lends to enable the development of new build property, commercial to residential conversions (including those with permitted development rights) and refurbishment projects.

Residential Investment

The Group lends on portfolios of residential property where the rental income will repay the underlying borrowing over a fixed term period. This excludes the regulated buy-to-let mortgage sector.

Other lending

The Group has limited appetite for other commercial lending (either development or investment) and has limited exposure to mixed development schemes.

How we do it

Financing is typically provided over a term of up to five years with prudent loan-to-value criteria, with a 60% Loan to Gross Development Value to residential house builders. More restrictive policies are implemented from time to time as required: for instance the Group reduced its financing of residential developments in Central London in 2015. The Group's Loan to Gross Development Value / loan-to-value ratios continue to average below 60% across all lending areas. The Group has no significant exposure to any one property scheme or developer.

The Real Estate Finance team is staffed by experienced bankers with proven property lending expertise. The team provides full support to customers and introducers over the life of the products.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	41.2	32.3	28.4
Lending balance	769.8	580.8 (£581.0 million on an IFRS 9 basis*)	451.0
Impairment charge/(credit)	0.5	(0.2)	0.1

*See Appendix for reconciliation

2018 performance

The business has continued to grow its Real Estate Finance business, with balances up 33% in 2018, which generated a 28% increase in revenue. The rate of growth in the first half of 2018 slowed due to an increase in repayments. The mix of the book between development and investment has remained stable, with development lending representing 30% of the book at end of 2018.

The credit quality of the book has remained strong, with no crystallised impairments and a low level of watch list cases. The impairment charge reflects an increase to loss given default due to the estimated impact of a change in the level of property sales in the event of repossession.

Business review – Business Finance

Looking forward

The business further added to its origination team in 2018 and expects to continue to grow balances, with an intent to focus on diversifying the mix of business, both in terms of introduction source and geographic location. The business does however continue to remain cautious around credit policy in the light of more uncertain market conditions, and can react quickly to any threats which may emerge. Growth will be managed carefully to ensure that returns are maximised whilst maintaining credit quality.

“We wanted to express our appreciation of the way Secure Trust Bank have assisted us and joined us in progressing this complicated and exciting project. From the outset the bank has shown real enthusiasm and have committed a lot of time to absorb and assist with the best way forward. You have readjusted the facility to ensure that our progress is both enjoyable and comfortable. We are impressed by the way you are very approachable which has ensured that any complications that have arisen have been resolved without holding up progress.

We are very pleased that we made the decision to go with Secure Trust Bank on this venture and a big thank you from our team to the bank.”
Neobrand No. 2 Limited

Strategic report

Business review – Business Finance

Asset Finance

Asset Finance was formed as a division within the Group in December 2014.

What we do

The Asset Finance business provides funding to support SME businesses in acquiring commercial assets, such as building equipment, commercial vehicles and manufacturing equipment.

How we do it

The Asset Finance business is operated via a joint venture with Haydock, a well-established asset finance company operating across the UK. Following the change in ownership of Haydock in January 2018, the Group has ceased writing new business through the joint venture, although Haydock continues to provide a full business process outsourcing service to the Group in relation to the portfolio funded by the Group.

The current portfolio reflects hire purchase and finance lease arrangements with terms of up to five years.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	6.6	8.5	7.8
Lending balance	62.8	116.7 (£116.5 million on an IFRS 9 basis*)	117.2
Impairment charge	2.2	1.0	0.6

*See Appendix for reconciliation

2018 performance

Following the decision to cease writing new business in February 2018, the portfolio is in run-off. The lending balances and income have reduced during 2018, with balances reducing by £54 million (46%) in 2018. As a consequence of this run-off, lending revenue has also reduced in 2018.

Impairment losses have increased in 2018 by £1.2 million compared to 2017, reflecting an increase in the value of cases taken into collections.

Looking forward

The Asset Finance division has operated through a joint venture with Haydock Finance to date. With the change in ownership of Haydock in January 2018, the business has ceased originating new business, and continues to assess options within the Asset Finance market. The portfolio is expected to reduce in line with contractual repayments from customers.

Strategic report

Business review – Business Finance

Commercial Finance

Commercial Finance was formed as a division within the Group in 2014.

What we do

The division specialises in providing a full range of invoice financing solutions to UK businesses including invoice discounting and factoring.

Invoice discounting services provide access to funding and release typically up to 90% of the value of qualifying invoices, in confidence and allowing clients to stay in control of sales ledger management.

Factoring services, where the sales ledger management is passed on to the Group, may also provide access to funding of typically up to 90% of the value of qualifying invoices and often results in the Group managing credit control, cash allocation, statement and reminder letter distribution.

Other assets can also be funded either long or short term and for a range of loan-to-value ratios alongside these facilities.

How we do it

Commercial Finance complements the broader SME lending proposition which has been developed by the Group. The business also provides SME commercial owner occupiers with finance to buy the property they trade from in conjunction with other financing facilities.

The division has built a strong team of proven business development, credit and operational professionals who have delivered a robust and compliant operational model.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	13.4	7.2	4.6
Lending balance	194.7	126.5 (£126.3 million on an IFRS 9 basis*)	62.8
Impairment charge	-	0.1	0.2

*See Appendix for reconciliation

2018 performance

The Commercial Finance business saw further strong growth in 2018, with lending balances increasing by more than 50%. Income consequently saw strong growth while the cost base increase was marginal. Impairment losses continue to be minimal. In the year Commercial Finance opened offices in Birmingham, Leeds and London and recruited high calibre people from the industry, building on its focus on growth from a strong platform.

Looking forward

The team has built a reputation for high quality service, particularly within its chosen markets, and as a result the prospects for future growth are encouraging. Further national expansion through development of its regional footprint will provide the Group with a more scalable business model on which to achieve this growth.

Strategic report

Business review – Business Finance

Secure Trust Bank Commercial Finance provided a £15 million asset based lending facility to Carpet & Flooring (Trading) Limited, one of the UK's leading distributors of floor covering products. The company supplies to a wide range of sectors, including healthcare, leisure and education. With turnover of £100 million, Carpet & Flooring employs more than 380 people across the country.

"We are delighted to have secured this additional funding from Secure Trust Bank which will support us as we deliver organic growth and pursue targeted acquisitions. The business is now in an excellent position and we're pleased to be working with Secure Trust Bank on the next phase of our plan."
Lisa Tomlin, Chief Executive Officer at Carpet & Flooring

Secure Trust Bank Commercial Finance provided a £2.3 million finance facility to Twisted Automotive to support its purchase of 240 vehicles from the iconic Land Rover Defender's last ever production run.

"With time running out on production, in 2015 we spotted a unique opportunity to increase our inventory and introduce pre-built versions of our vehicles, which helped us tackle the long waiting list and boost our revenues. With this new financial strength, we can look at expanding overseas and ready ourselves for a potential launch of a new Defender model in 2020."
Charles Fawcett, Founder of Twisted Automotive

Strategic report

Business review – Consumer Finance

Retail Finance

Retail Finance includes lending products for in-store and online retailers to enable consumer purchases.

What we do

The Retail Finance business, branded as “V12”, provides unsecured, prime lending products to the UK customers of its retail partners to facilitate the purchase of a wide range of consumer products across in-store, mail order and online channels. This business is driven by V12 Retail Finance, which was acquired in 2013 and has provided finance in cooperation with its retail partners for more than 20 years. The V12 point of sale system is used by the Group’s retail partners and Retail Finance is administered from the V12 offices in Cardiff.

Retail Finance products are unsecured, fixed rate and fixed term loans of up to 84 months in duration with a standard maximum loan size of £25,000. The average new loan is for £1,000 over a 24 month term. Lending is restricted to UK residents who have a good credit history and can demonstrate that they can afford to repay the loan.

The finance products are either interest bearing or have promotional credit subsidised by retailers, allowing customers to spread the cost of purchases into more affordable monthly payments.

How we do it

The Group operates an online e-commerce service to retailers, providing finance to customers of those retailers. The online processing system allows customers to digitally sign their credit agreements, thereby speeding up the pay-out process, and removing the need to handle and copy sensitive personal documents through electronic identity verification.

The Group serves retailers across a broad range of retail sectors including cycle, music, furniture, outdoor/leisure, electronics, dental, jewellery, home improvements and football season tickets.

The Group provides finance to customers of a large number of retailers including household names such as Jessops, Halfords, DFS, Sofology and Watchfinder.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	62.8	50.7	36.7
Lending balance	597.0	452.3 (£442.1 million on an IFRS 9 basis*)	325.9
Impairment charge	19.3	13.8	9.5

*See Appendix for reconciliation

Strategic report

Business review – Consumer Finance

2018 performance

The Retail Finance business has continued to grow strongly, with new gross lending volumes increasing to £651.5 million (an increase of 25% on the previous year). This has driven a further significant increase in lending assets, which during the year rose to £597.0 million (December 2017: £452.3 million). Market share increased from 5.6% in 2017 to 6.8% in 2018 (based on Finance & Leasing Association new business values within retail store and online credit).

Each of the three largest sub-markets for the business (sports and leisure, furniture and jewellery) have contributed to this growth, which as in previous years has been achieved through a combination of gaining increased market share and sector growth.

Revenue increased by 24% to £62.8 million (2017: £50.7 million). Impairment losses were well controlled at £19.3 million (2017: £13.8 million) and reflect accelerated provisioning under IRFS 9 aligned to a growing book.

Customer feedback, measured by FEEFO, provided the business with a score of 4.8 out of 5 for the year based on 400 reviews.

Looking forward

The Group plans further growth in Retail Finance during 2019 with the focus on acquiring increased market share across its target markets.

To underpin the continued growth, the Group continues to invest in initiatives to further enhance its systems capabilities, to ensure that quality of service to both retailers and customers is maintained or improved. This includes the online account management service, which allows customers to view their statement online and make routine self-serve changes to their account such as change of payment date and settlement.

"Great service, reasonable interest rates and fast service, thanks."
"The service we received was brilliant, was really quick to do everything on my phone with no complicated steps. I would absolutely recommend."
"Very good service with quick application and reliable credit check. Have used V12 three times and it's always been quick and easy process."
"Service was efficient and quick. Would highly recommend and currently have other accounts in place - therefore I would use the service again."
"Easy to apply all information required supplied quickly and easily. Would recommend as a hassle free route to fund your purchase at a great rate."

Strategic report

Business review – Consumer Finance

Motor Finance

Finance is arranged through motor dealerships, brokers and internet introducers and involves fixed rate, fixed term hire purchase arrangements, predominantly on used cars.

What we do

The Group's Motor Finance business began lending in 2008 under the Moneyway brand and provides hire purchase lending products to a wide range of customers including those who might otherwise be declined by other finance companies. This helps the Group's customers to gain the freedom and flexibility that motoring gives to their lives as well as helping introducers to sell more cars.

Motor Finance agreements are secured against the vehicle being financed.

The Group has ceased writing new business in the sub prime market and is predominantly lending to finance the purchase of volume franchise used cars in the near-prime market.

How we do it

The Bank distributes its Motor Finance products via UK motor dealers, brokers and internet introducers. New dealer relationships are established and managed by the Group's UK-wide Motor Finance sales team with all introducers subject to a strict vetting policy, which is reviewed on a regular basis.

The technology platform used allows Moneyway to: receive applications online from its introducers; provide an automated decision; facilitate document production through to pay-out to dealer; and manage in-life loan accounts.

Motor lending is administered in Solihull; however the UK motor dealers and brokers are UK-wide.

Lending performance v prior years

	2018 £million	2017 £million	2016 £million
Revenue	48.5	47.1	40.5
Lending balance	276.4	274.6 (£253.0 million on an IFRS 9 basis*)	236.2
Impairment charge	11.3	20.8	14.6

*See Appendix for reconciliation

2018 performance

The Motor Finance business narrowed its credit parameters during 2017 in order to reduce potential future impairment losses. New business volumes in 2018 reflect a higher credit quality. There was a consequent decrease in new business volumes from £142.8 million in 2017 to £141.3 million for 2018.

Impairment losses for the period have improved from £20.8 million to £11.3 million. The improvement in the quality of the book, reflecting both the shift away from sub prime motor lending discontinued during 2017, and improved collections performance have driven the reduction in losses. These improvements are amplified by the change to IFRS 9, because the expected credit loss approach required by that standard accelerates the recognition of improved performance. The improvement has been supported by the Motor Finance leadership increasing levels of resource and delivering process improvement within the Collections and Recoveries teams.

Strategic report

Business review – Consumer Finance

Revenue improved modestly, by 3.0%, reflecting the reduction in margin for higher credit quality business. This shift in business alongside improved collections performance has driven the improvement in impairments.

Looking Forward

The Motor Finance business plans to expand operations into the prime credit market, to drive long-term receivables growth and sustainable return outcomes. A clear opportunity exists to deliver prime and near-prime products and services in the Motor lending market for an innovative and technology led funding provider.

A programme of work is underway to deliver a new platform and business transformation through 2019/2020 with £1.4 million already invested in 2018. As part of this programme the Motor Finance business is aiming to enhance system capabilities and to deliver a broader range of products.

This is expected to improve the credit quality of the portfolio, drive business growth and deliver stable earnings. Alongside these initiatives, the business will continue to focus on the near-prime market sector through its existing introducer channel.

Over the year the business has made some key appointments to support the transformation of the business and drive growth in the prime and near-prime motor business with the new Motor leadership team all now on board.

“Moneyway have been great to deal with in 2018. The Regional support team have been very helpful and we get lots of good feedback from the sites. The improvements made in pay-out times and ease of use have certainly helped lift their reputation."
Evans Halshaw

“Since UK Car Finance began its working relationship with Moneyway, we have seen many changes, innovations and improvements. The entire culture of the business seems geared up to making everything easy, straightforward and above all else, sensible. From the systems, account management team to their processes, Moneyway are without doubt a business we enjoy working with and look forward to working in partnership with them for many years to come.”
UK Car Finance Limited

Business review – Consumer Finance

Debt Managers (Services) Limited

Debt Managers (Services) Limited ('DMS') was purchased by the Group in January 2013.

What we do

DMS is the Group's debt collection business. DMS collects debt on behalf of a range of clients as well as for Group companies. It also selectively invests in purchased debt portfolios from fellow subsidiary undertakings and external third parties.

How we do it

Debt Managers (Services) offers three services across credit management and in order to meet the needs of its clients:

- Business process outsourcing allows DMS to assist in the performance of early arrears accounts on behalf of clients
- Contingent collection allows a client to place accounts with Debt Managers (Services) for DMS to manage those accounts in its own name
- Debt purchase allows DMS to acquire accounts and choose how to liquidate those accounts over a period of 10 years.

DMS aims to provide all customers with the best possible customer service by recognising every customer is different. All customer facing staff receive training on how to effectively use models such as TEXAS and IDEA to help identify signs of vulnerability and on how to use tailored signposting relevant to customers' circumstances. Customers that need additional support are managed by a specialist Customer Care Team. DMS works closely with debt charities such as StepChange, Payplan and Christians Against Poverty and a range of other third parties including the Samaritans, MIND and Marie Curie to ensure that customers receive an appropriate service.

Lending performance v prior years

	2018 £million	2017 £million	2016 £million
Revenue	7.0	4.9	3.7
Lending balance	32.3	15.6 (£15.6 million on an IFRS 9 basis*)	13.5
Impairment charge	N/A	N/A	N/A

*See Appendix for reconciliation

As DMS purchases assets which are credit impaired, impairment charges are unlikely to materialise.

2018 performance

In 2018 DMS performed well with revenue increasing by 43% from £4.9 million to £7.0 million and profit before tax increasing significantly from £0.6 million to £1.6 million. This was achieved through the development of relationships with new and existing clients and a broadening of service offerings.

Looking forward

The positive momentum in the year is expected to continue into 2019 having established strong relationships and forward flow contracts with existing clients. This is expected to result in continued growth of both revenue and profit. Leveraging new technologies will enhance customer engagement and will facilitate penetration of new sectors. The ownership of DMS by the Bank means it is well placed to identify and take advantage of growth opportunities in the coming year.

Strategic report

Business review – Consumer Mortgages

Consumer Mortgages was launched on 20 March 2017. The division supports residential customers who are underserved by the traditional high street lenders.

What we do

The division lends to individuals who wish to purchase a property or remortgage their current property.

How we do it

Consumer Mortgages provides, through intermediaries, competitive fixed rate mortgage products to people whose personal circumstances do not fit the norm but are still credit worthy individuals with good affordability.

Financing is typically provided over a term of up to 35 years with fixed interest rate periods of 2, 3 and 5 years. The Group's purchase and remortgage products have a maximum loan to value of 90% and a maximum loan size of £2 million.

The Consumer Mortgage team is staffed by experienced mortgage and banking individuals with proven property lending expertise and underwriting skills. The team provides full support to customers and introducers over the life of the products.

Revenue and lending performance vs prior years

	2018 £million	2017 £million	2016 £million
Revenue	1.5	0.1	-
Lending balance	84.7	16.5 (£16.5 on an IFRS 9 basis*)	-
Impairment charge	0.2	-	-

*See Appendix for reconciliation

2018 performance

The Mortgage business has steadily grown since its launch. In 2018 Mortgages originated £70 million of lending and finished the year with a book of £84.7 million. As a result of market conditions, with lenders competing aggressively on price and loan-to-value metrics across the sector increasing alongside falling margins, the Group tempered its mortgage lending.

Looking forward

In the first quarter of 2019 due to the difficult economic climate, increased competition and the continued uncertain outlook, the Group announced the decision to cease new mortgage originations until market conditions improve.

Strategic report

Business review – Savings

The Group attracts funding primarily via retail savings, offering individuals competitive, simple products, applied for online and serviced through a highly commended online proposition, backed by UK based customer service.

What we do

The Group offers simple, straightforward notice and fixed term accounts, promoted via best buy tables and with the endorsement of national press and market commentators, available to UK based individuals saving from £1,000. Historically, the Bank has also offered business accounts priced to reflect the different associated costs and risks.

Covered by the UK Financial Services Compensation Scheme up to the specified limits, the Group offers accounts in line with its ongoing funding needs, including 14 to 180 day notice and 1 to 7 year fixed terms with a maximum balance of £1 million for sole account holders and £2 million for business and joint accounts.

Customers can choose to capitalise or pay away their interest, with annual interest on bonds and quarterly on notice accounts. The Group this year also introduced the option on limited bond products to receive a monthly income.

Alongside Savings, the Group continues to service OneBill, in operation for many years and closed in 2009 to new customers, designed to aid with household budgeting. Customers provide details of their annual bills which are aggregated and calculated into a fixed weekly or monthly schedule so customers can spread the cost of their bills through the year, receiving direct debit discounts and support liaising with providers. A monthly fee is charged.

How we do it

By virtue of the absence of a branch network, a policy of not cross-subsidising loss making products with profitable ones, a stable funding base and an operational model based on digital self-service, the Group is able to offer competitive rates and has been successful in attracting high volumes of deposits in short timescales from a wide range of customers. This provides a funding profile which gives additional financial security to the business.

The Group enters the market for deposits as and when it is necessary and maintains a funding strategy of broadly matching the term and tenor of its customer savings to the desired maturity profiles of the Group which are primarily determined by the interest rates and terms offered on loans and advances to customers. This strategy seeks to help mitigate maturity transformation and interest basis risks.

The Group is able to adjust the mix of interest rate offered and term or notice period in a manner that allows it to raise funding quickly. As part of this funding strategy, the Group may only offer savings accounts for limited periods of time and, from time to time, may not offer new products to customers at all. The Group will cease offering products when the need for funding at that time has been satisfied.

The marketing methods employed include providing information about the savings accounts offered on price comparison websites, newspaper best buy tables and articles and via online endorsement (for example Money Saving Expert). In addition to attraction based on interest rate, customers choose Secure Trust Bank based on its financial standing, UK based operation and high standards of cyber and operational security.

Savings balances vs prior years

	2018 £million	2017 £million	2016 £million
Notice deposits	516.4	455.3	373.8
Fixed Term Savings	1,316.8	1,013.4	762.8
Sight/Instant Access	14.5	14.5	15.2
Total Balances	**1,847.7**	**1,483.2**	**1,151.8**

Strategic report

Business review – Savings

2018 performance

2018 represented the first year the Group operated on a new digital platform following on from a successful migration in late 2017. In the year, the Bank grew its retail savings by £364.5 million, an increase of 24.6% - equivalent to almost £12 every second. This represents nearly 26,000 new accounts and 17,000 new savings customers joining the Group this year.

In the year the Bank won a number of awards, including Best Savings Provider from Savings Champion, as well as Best Fixed Rate Bond and Best Notice Account Provider. The Group was also highly commended by The Money Pages as Best Online Savings Provider, with all of these awards independently judged and customer focused.

Throughout the year the Group has offered competitive savings products featuring in a best buy table every week. At the last point of reporting in October 2018, the Group achieved 7.5% of fixed rate bond sales online according to eBenchmarkers – a considerable achievement of many times its natural market share of non-ISA savings balances.

The introduction and adoption of online servicing has been a focus in 2018. At the start of the year, the Group had a handful of trial customers registered. At the end of December, over 30,000 customers are now registered, 70% of the overall deposit customer base, with 58% having signed in at least once. For new customers, 99.9% register and over 74% sign in at least once.

It is worth noting that 2018 marks a number of considerable milestones for the Group's savings business over the past five years, having grown balances by 323% or £1.4 billion from the start of 2014, increased the number of accounts by 115% or 26,000 and opened almost 70,000 new accounts and attracting over 37,000 customers. The Group now has customers across the majority of counties in England, Wales and Scotland, and from Shetland to Cornwall and from Norfolk to Belfast.

Looking forward

The Group plans continued savings growth through 2019 and to underpin this is investing in product diversification to attract a broader pool of customers. Development is underway to launch a Fixed Rate Cash ISA as well as shorter-dated notice and instant access products, the latter being the largest savings market in the UK by value. These new markets represent a clear opportunity to bring material benefit to the Group in its cost of retail funds.

Furthermore, the Group intends to start to invest in significant enhancements to its digital proposition and take advantage of the opportunities arising from a growing customer base. It will also consider the potential to offer savings accounts to businesses in the UK.

Strategic report

Principal risks and uncertainties

Risk overview

On an ongoing basis, the Directors carry out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. The following are considered to be the principal risks facing the Group:

Risk	Description
Credit Risk	The risk that a counterparty will be unable to pay amounts in full when due.
Liquidity Risk	The risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.
Operational Risk	The risk of direct or indirect loss arising from a wide variety of causes associated with the Group's processes, personnel, technology and infrastructure, and from external factors other than the risks identified above.
Capital Risk	The risk that the Group will have insufficient capital resources to support the business.
Market Risk	The risk that the value of, or revenue generated from, the Group's assets and liabilities is impacted as a result of market movements, predominantly interest rates.
Conduct Risk	The potential for customers (and the business) to suffer financial loss or other detriment through the actions and decisions made by the business and its staff.
Regulatory Risk	The risk that the Group fails to be compliant with all relevant regulatory requirements.

Notes 30 to 33 to the financial statements provide further analysis of certain financial risks.

Further details of the principal risks, the changes in risk profile during the 2018 financial year and the Group's risk management framework are set out in the following section. There is also analysis of the key strategic and emerging risks which impact the Group. These include the UK's withdrawal from the European Union, the direct impacts of which are considered to be limited given the Group's UK operation and focus. The main indirect impact of the withdrawal on the Group, if disorderly, is most likely to be to credit risk and on demand for the Group's products.

Principal risks and uncertainties

Credit risk

Description

Credit risk is the risk that a counterparty will be unable to satisfy their debt servicing commitments when due. Counterparties include the consumers to whom the Group lends on a secured and unsecured basis and the small and medium size enterprises ('SME') to whom the Group lends on a secured basis as well as the market counterparties with whom the Group deals.

Mitigation

The Group manages credit risk through internal controls and through a three lines of defence model. The first line is the business operation team with the credit risk team being second line and internal audit being the third line. The Consumer Credit Risk Committee and SME Credit Committees, which are the monitoring committees for credit risk, report to the Board Risk Committee. The Board Risk Committee also approves lending authorities in respect of SME lending. Each consumer lending product has a credit risk committee which reviews business performance from new application metrics through to loss performance by business type and introducer. Policy and scorecard changes are approved at this committee.

For Real Estate Finance and Commercial Finance, lending decisions are made on an individual transaction basis, using expert judgement and assessment against criteria set out in the lending policies. Asset Finance lending is managed via a joint venture with Haydock, who operate in line with the Group's credit policies and risk appetite. Since the change in ownership of Haydock in January 2018, the Group has allowed the Asset Finance portfolio to reduce in line with contractual repayments from customers.

Exposure to credit risk is also managed in part by obtaining security. Motor Finance loans are secured against motor vehicles. Mortgages are secured against land/property and Real Estate Finance and Asset Finance loans are secured against property and tangible assets respectively. Commercial Finance advances are secured against a debtor book, inventory or property if a commercial mortgage is provided.

Management monitors the ratings of the counterparties in relation to the Group's loans and advances to banks. There is no direct exposure to the Eurozone and peripheral Eurozone countries.

Implementation of IFRS 9 on 1 January 2018 has resulted in changes to the timing of reporting credit losses. These changes have been built into Group forecasts and are considered in setting the Group's appetite for volume by sector.

Forbearance

The Group does not routinely reschedule contractual arrangements where customers default on their repayments. It may offer the customer the option to reduce or defer payments for a short period, in which cases the loan will retain the normal contractual payment due dates and will be treated the same as any other defaulting cases for impairment purposes. Forbearance arrangements in respect of Consumer Mortgages customers are described in Note 30.2.

Credit risk (continued)

Change – IMPROVED

Consumer Finance credit risk

Application trends, arrears and loss trends for the Retail Finance Portfolio are monitored monthly by the Credit Risk Team. Losses remain within risk appetite.

The Group's Motor Finance business has continued to grow despite a very competitive landscape. The Group has repositioned the motor finance business away from those customers that are most susceptible to an economic downturn. During the course of 2018 the "rate for risk" proposition was extended. The Group has embarked on a motor transformation plan which will see the implementation of a new application and servicing system. Linked to this, it is looking to expand the product range to include a unit stocking product, to provide short term finance to motor dealers so that they can buy stock together with a prime Hire Purchase ('HP') and Personal Contract Purchase ('PCP') product offering. The PCP offering will introduce a new risk for the Group, with potential for losses should the residual value of the vehicles at the end of the agreement be less than expected at inception of the contract.

Secure Trust Bank entered the Consumer Mortgage market in 2017, offering basic fixed term mortgage and re-mortgage products for those good quality customers with non-straightforward circumstances that struggle to meet the requirements of high street lenders. All loans are secured on the applicant's property. The Bank extended the range of products in 2018 to include interest only and part and part mortgages. In the first quarter of 2019 due to the difficult economic climate, increased competition and continued uncertainties the Group announced the decision to cease new mortgage originations until market conditions improve.

The move to IFRS 9 has enabled the core components of the Expected Credit Loss ('ECL') to be regularly reviewed and used to allow deeper analysis of credit loss drivers. ECL is a function of the Probability of Default ('PD') x Exposure at Default x Loss Given Default and has enabled the Bank to understand more granularly the elements that contribute to ECL. The Group monitors the average PD by product each month both looking at the back book and new business, as well as analysing any reasons for increases and decreases in PD (such as significant increase in credit risk). The recovery rates from debt sales and repossessions are also validated on a regular basis and presented to the Assumptions Committee. Furthermore, the ECL has been used for the stress testing that was used in the ICAAP in 2018.

Business Finance credit risk

Lending balances within the Real Estate Finance and Commercial Finance portfolios have continued to grow, with both portfolios remaining well within all risk appetite parameters. The continued focus on high quality, secured lending with strong counterparties has served the Group well to date. This has been particularly evident in the high value central London residential real estate market, where risk appetite remains substantially reduced and lending has been pared back.

Following the change in ownership of Haydock, in January 2018, the Asset Finance portfolio has continued to run-off over the course of the year. The Group continues to assess its options with regards to future opportunities within the Asset Finance market.

Thanks to the Group's continued adherence to its robust lending policies and credit appetite, alongside the significant experience within the lending teams, impairments and arrears within the Business Finance portfolios have remained minimal to date. Management continues to closely monitor the portfolios and the external events and environment that could impact on each of them.

Concentration risk

Management assesses the potential concentration risk from geographic, product and individual loan concentration. Due to the well diversified nature of its lending operations, the Group does not consider there to be a material exposure arising from concentration risk.

Strategic report

Principal risks and uncertainties

Liquidity risk

Description

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group manages its liquidity in line with internal and regulatory requirements, and at least annually assesses the robustness of the liquidity requirements as part of the Group's Internal Liquidity Adequacy Assessment Process ('ILAAP').

The Group is required to meet daily cash flow requirements arising from maturing deposits and loan draw-downs, and maintains significant cash resources to meet all of these needs as they fall due. The liquidity requirements of the Group are mainly met by maintaining funds in liquid assets including the Bank of England reserve account to cover any short-term net outflow requirements. Longer term funding is also in place for structural liquidity and funding requirements.

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, and can fund its assets at reasonable cost and without incurring unacceptable losses or risking damage to the Group's reputation through a failure to meet its obligations.

Mitigation

Risk tolerance

The Group maintains at all times liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. The Group maintains a buffer of unencumbered High Quality Liquid Assets ('HQLA') that is available to meet its liquidity requirements.

The Group's Board has agreed a liquidity risk appetite to ensure that adequate liquidity resources are held to meet its Overall Liquidity Adequacy Rule ('OLAR') and the minimum Liquidity Coverage Ratio ('LCR'). This appetite ensures that adequate liquidity resources are held to withstand all known reasonable combinations of idiosyncratic and market risks for up to 90 days.

The Group assesses and formally demonstrates the adequacy of its liquidity through the ILAAP. As part of the ILAAP, the Group conducts regular and comprehensive liquidity stress testing to ensure compliance with its internal and regulatory requirements.

Structure and responsibilities for liquidity risk management

The Group has a formal governance structure in place to manage and mitigate liquidity risk on a day to day basis. The Board sets and approves the Group's liquidity risk management strategy. The Assets and Liabilities Committee ('ALCO'), comprising senior management and executives of the Group, meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and ILAAP metrics. These metrics are managed on a day-to-day basis by the Group's Treasury function. The Risk Function is responsible for ensuring that appropriate risk management processes and controls are in place, and that they are sufficiently robust, so as to ensure that key risks are identified, assessed, monitored and mitigated.

Internal liquidity reporting

Liquidity metrics are monitored daily through daily liquidity reporting and on an ongoing basis through monthly ALCO meetings. Metrics are also included in the Monthly Information pack tabled at the Group's Executive Committee ('Exco'), Board Risk Committee and the Board. The aim is not to measure liquidity with a single metric but rather a range of principles and metrics which, when taken together, helps ensure that the Group's liquidity risk is maintained at an acceptable level.

The primary measure used by management to assess the adequacy of liquidity is the OLAR, which is the Board's own view of the Group's liquidity needs as set out in the Board approved ILAAP.

Communication of liquidity risk strategy, policies and practices across business lines and with the Board

The Group's ALCO is responsible for implementing and controlling the liquidity risk appetite established by the Board. ALCO monitors compliance with the Group's policies and oversees the overall strategy, guidelines and limits so that the Group's future plans and strategy can be achieved within risk appetite.

Liquidity risk (continued)

Mitigation (continued)

Funding strategy

The Group's funding risk appetite is to ensure that the Group has access to stable funding markets and is not reliant on any single source of funding. The Group is mainly funded by stable customer deposits and capital (including Tier 2 capital issued in 2018 that is non-callable for five years). The Group also has limited borrowings under Bank of England funding schemes but does not have other direct exposures to wholesale markets. Funding strategy is managed centrally.

Liquidity risk mitigation techniques

The Group seeks to mitigate liquidity risk through a number of strategies and processes:

- The diversification of its deposit and loan products
- Offering depositors competitive interest rates
- A stable funding profile
- Acquiring funding primarily through depositors subject to Financial Services Compensation Scheme protection
- Regular forecasting of liquidity and funding metrics
- Regular ALCO meetings reviewing risk metrics and upcoming risks
- Access to Bank of England liquidity schemes
- Holding adequate levels of High Quality Liquid Assets with a high proportion of cash in the Group's Bank of England Reserve Account.

Stress testing

An integral component of the approach to liquidity risk management is stress testing, some of which is prescriptive using detailed rules and guidance issued within prudential regulations and reported within regulatory returns. In addition to the regulatory prescribed stress testing, the Group undertakes its own stress tests. The Group uses various short and medium term forecasts to monitor future liquidity requirements and these include stress testing assumptions to identify the required levels of liquidity. Stress testing is typically performed on a daily basis and levels of liquidity under stress are forecast regularly and monitored by ALCO and management. The Board approves limits against both regulatory and internal stress testing requirements.

Contingency funding plans

If for reasons which may be beyond the business' control, the Group was to encounter a significant and sustained outflow of deposits or other stress on liquidity resource, the Recovery Plan incorporates the Group's plans to ensure that it remains sufficiently liquid to remain a viable independent financial institution during a severe liquidity stress event. Recovery Plan Early Warning Indicators and Invocation Trigger Points ('ITP') are regularly monitored and reported against.

The Recovery Plan is applied consistently with the Group's ILAAP as part of the overall liquidity risk management framework dealing with contingent funding requirements as they arise. The Group also retains access to the Bank of England liquidity insurance schemes, including the Discount Window Facility.

Change – IMPROVED

The Group has maintained its liquidity ratios in excess of regulatory requirements throughout the year and continues to hold significant levels of high quality liquid assets.

A number of enhancements were made to the liquidity management framework in 2018. These include approval of a revised standards and policy framework by ALCO, additional analysis of liquidity requirements and increased MI reporting frequencies, and the locking-in of an appropriate level of Term Funding Scheme funding. An experienced Liquidity Manager joined the Treasury team in July 2018 and towards the end of 2018, Risk appointed a Senior Manager, Prudential Risk. This role will provide additional scrutiny and oversight in respect of prudential matters including liquidity.

The stress tests performed as part of the ILAAP confirmed that the Group has sufficient funds to satisfy the OLAR requirement and there is no significant risk that liabilities cannot be met as they fall due. The Group's LCR at 31 December 2018 was significantly higher than the regulatory requirement.

Operational risk

Description

Operational Risk is the risk that the Group may be exposed to direct or indirect loss arising from inadequate or failed internal processes, personnel and succession, technology/ infrastructure, or from external factors.

The scope of Operational Risk is broad and includes Business Process, Business Continuity, Third Party, Financial Crime, Change, Human Resources, Information Security and IT Risk, including Cyber Risk.

Mitigation

The Group has adopted an Operational Risk Policy and Framework designed in accordance with the 'Principles for the Sound Management of Operational Risk' issued by the Basel Committee on Banking Supervision.

The approach ensures appropriate governance is in place to provide adequate and effective oversight of the Group's operational risk. The governance framework includes the Board Risk Committee and Group Operational Risk Committee.

The Group has a defined set of qualitative and quantitative operational risk appetite measures. Quantitative measures cover operational losses, complaints, key operational risks, systems availability and information security. The appetite measures are reported and monitored on a monthly basis.

Change – IMPROVED

The improvement of the status of this risk is driven by the Group's continued investment in resource, expertise and systems to support the Operational Risk Framework and Policy. This Framework defines and facilitates the following activities:

- A biannual Risk and Control Self Assessment process to identify, assess and mitigate risks across all business units through improvements to the control environment
- The Governance arrangements for managing and reporting these risks
- All risk appetite measures and associated thresholds and metrics
- An incident management process that defines how incidents should be managed and associated remediation, reporting and root-cause analysis.

In 2018 the Group successfully transitioned to 'The Standardised Approach' for assessing its Operational Risk capital, in recognition of the enhancements made to its framework and embedding this across the Group.

Key Risk themes of Operational Risk focus in 2018 include:

- **Supplier management** – The Group uses a number of third parties to support its IT and operational processes. The Group recognises that it is important to effectively manage these suppliers and has throughout 2018 embedded a suite of standard controls for all its material suppliers to reduce the risk of operational impacts on these critical services. This will continue to be an area of focus for 2019, particularly in relation to the Operational Resilience of the service provided by the most critical suppliers.
- **Operational and IT resilience** – Many elements of the operational risk framework support the ongoing resilience of the Group's operational and IT services, including Business Continuity Management, Disaster Recovery, Incident Management, Process Management and the Cyber strategy. However this will continue to be a key area of focus for 2019 as the Group continues to enhance its defences to any disruption to its most critical services.
- **Information security and cyber risk** – The Group has paid considerable attention to ensuring the effective management of risks arising from a failure or breach of its information technology systems that could result in customer exposure, business disruption, financial losses, or reputational damage.
- **Change Management** – The effective delivery of Change Management programmes plays an important role in meeting the Group's regulatory requirements, improving services and implementing strategic decisions. Ineffective change management processes could lead to poor customer outcomes, business disruption, financial loss and regulatory breaches. Change Management processes and governance are defined and embedded within the Group. Significant changes are planned in 2019, particularly in respect of the Motor Finance transformation, and these will be a key area of focus to ensure the Group maintains its customer and operational service standards and delivers its strategic objectives.

Strategic report

Principal risks and uncertainties

Capital risk

Description

Capital risk is the risk that the Group will have insufficient capital resources to meet minimum regulatory requirements and to support the business. The Group adopts a conservative approach to managing its capital and at least annually assesses the robustness of the capital requirements as part of the Group's Internal Capital Adequacy Assessment Process '(ICAAP').

Mitigation

The Group's capital management policy is focused on delivering shareholder value, in a safe and sustainable manner. The Board regularly reviews the current and forecast capital position to ensure capital resources are sufficient to support planned levels of growth.

In accordance with the EU's Capital Requirements Directive IV ('CRD IV') and the required parameters set out in the EU's Capital Requirement Regulation, the Group maintains an ICAAP which is updated at least annually. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted an approach to determine the level of capital the Group needs to hold. This method takes the Pillar 1 capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequate to cover management's assessment of anticipated risks. Where it is considered that the Pillar 1 calculations do not reflect the risk, an additional capital add-on in Pillar 2 is applied, as per the Total Capital Requirement issued by the PRA.

A complete assessment of the Group's capital requirement is contained in its Pillar 3 disclosures. Pillar 3 disclosures for the Group for the year ended 31 December 2018 are published as a separate document on the Group's website.

Change – STABLE

The Group maintained its capital ratios in excess of regulatory requirements throughout the year. At 31 December 2018, the CET1 ratio was 13.8% (2017: 16.5%), the total capital ratio was 16.3% (2017: 16.8%) and the leverage ratio was 10.0% (2017: 12.3%) on a Group consolidated basis. The CET 1 ratio has decreased due to the investment of capital to support strong lending growth.

The 2018 ICAAP incorporated IFRS 9 provisioning methodology, which accelerates the impact of losses in adverse economic conditions. The ICAAP demonstrated the Group's continued ability to meet its minimum capital requirements, even in severe stress scenarios. The Group's forecasting capability has been enhanced to cover a five year time horizon, with modelling of capital resources and requirements provided over that period, and future ICAAPs will also cover a five year period. Additional early warning indicators have been developed as part of the Recovery Plan process.

In July 2018 the Group raised its first Tier 2 capital: £25 million at 6.75%. A further £25 million was raised in October 2018 at the same price and the mechanisms have been developed to allow raising of Alternative Tier 1 capital, should such be needed. This provides the Group with additional flexibility in terms of capital options, and demonstrates the Group's ability to raise capital to fund planned growth. Capital resources increased during the year to £297.5 million as at 31 December 2018 (31 December 2017: £243.3 million) on a Group consolidated basis.

The improvements in the Group's range and size of capital resources, and to its capital management processes, leave it well positioned to continue to fund balance sheet growth while meeting increasing levels of regulatory capital buffers.

The Group has elected to adopt transitional provisions in respect of the implementation of IFRS 9, as set out by the European Banking Authority. These provisions allow the capital impact of the standard to be phased in over a five year period. Further details are provided in Note 33.

Strategic report

Principal risks and uncertainties

Market risk

Description

For the Group, market risk is primarily limited to interest rate risk, being the potential adverse impact on the Group's future cash flows from changes in interest rates arising from the differing interest rate risk characteristics of the Group's assets and liabilities. When interest rates change, the present value and timing of future cash flows change. This in turn changes the underlying value of the Group's assets, liabilities and off-balance sheet instruments and hence its economic value. Changes in interest rates also affect the Group's earnings by altering interest-sensitive income and expenses, affecting its net interest income.

The principal currency in which the Group operates is Sterling, although a small number of transactions are completed in US dollars, Euros and other currencies in the Commercial Finance business. The Group has no significant exposures to foreign currencies and hedges any significant currency risks to Sterling.

Mitigation

Market risk is managed by the Company's Treasury function and is overseen by the ALCO. The Group does not take significant unmatched positions and does not operate a trading book.

The Group's risk management framework, policies and procedures are regularly reviewed and updated to ensure that they accurately identify the risks that the Group faces in its business activities and are appropriate for the nature, scale and complexity of the Group's business.

The key measure the Group uses to monitor the risk is an Interest Rate Sensitivity Gap analysis which informs the Group of mismatched interest rate risk positions. The Group reports the interest rate mismatch on a monthly basis to ALCO, considering market value sensitivity as a proportion of the overall capital position of the Group, and earnings at risk as a proportion of forecast net interest income. These are assessed against 200bps and 100bps parallel shifts in rates respectively. The Group also measures exposure to basis risk and the economic value of equity. All such exposures are maintained within the risk appetite set by the Board and are monitored by ALCO.

Change – STABLE

The Group's exposure to market risk continues to be limited primarily to interest rate risk, with only modest exposures to foreign exchange risk. The Group remained within risk appetite in respect of interest rate risk throughout the year.

The increasing size of the Group's balance sheet increases the inherent level of interest rate risk, and the Group has responded by enhancing its Treasury capabilities and risk framework, with a wider range of risk measures developed and monitored by ALCO. The Group has developed its capability to use interest rate swaps to further mitigate this risk, if required, in 2019.

Conduct risk

Description

The Group defines conduct risk as the risk that the Group's products and services, and the way they are delivered, result in poor outcomes for customers, or harm to the Group. This could be as a direct result of poor or inappropriate execution of the Group's business activities or staff behaviour.

Mitigation

The Group takes a principles based approach and includes retail and commercial customers in its definition of 'customer', which covers all business units and both regulated and unregulated activities.

Across the Group, conduct risk exposure is managed via monthly review and challenge of key risk indicators ('KRIs') at the Customer Focus Committee, which oversees complaints, FEEFO and Customer Service Excellence as well as conduct risk. Conduct risk management information is also reviewed at product level executive committee meetings.

The Key Risk Indicators vary across the business units to reflect the relevant conduct risks; the business units' key risk indicators are aggregated for measurement against the Group's risk appetite, which is reported to the Group Executive Committee, Risk Committee and the Board.

Change – STABLE

Review of conduct risk and controls within the business units is managed through the regular cycle of risk and control self-assessments, in line with other operational risk categories.

Members of the Customer Focus Committee review monthly key risk indicators across all business units, and meet on a quarterly basis for oversight and challenge of the first line activities to assure senior management that the first line is identifying conduct risks when they arise and taking appropriate actions to mitigate them.

Training on conduct risk continues to be delivered to new starters, with an eLearning module completed by all staff during the year.

Regulatory risk

Description

Regulatory risk is the risk that the Group fails to be compliant with all relevant regulatory requirements. This could occur if the Group failed to interpret, implement and embed processes and systems to address regulatory requirements, emerging risks, key focus areas and initiatives or deal properly with new laws and regulations.

Mitigation

The Group seeks to manage regulatory risks through the Group-wide risk management framework. The Group Compliance and Regulatory Risk Committee is responsible for reviewing and monitoring regulatory changes, and ensuring that appropriate actions are taken, and also reviewing and approving the compliance risk management framework. Further details can be found on the Group's website: www.securetrustbank.com/our-corporate-information/risk-management

Change – STABLE

In the year ended 31 December 2018, the Group has delivered changes to address new and revised regulations and legislation that have come into force, including: Payment Services Directive 2 ('PSD2'), which impacts the Deposits business and came into force on 13 January 2018; changes to the Senior Managers and Certification Regime framework; the General Data Protection Regulation; rules on staff incentives, remuneration and performance management in consumer credit; rules relating to the assessment of creditworthiness and affordability in consumer credit; and the enhanced product disclosures required in the Insurance Distribution Directive.

A number of formal projects and initiatives are in place to address forthcoming regulatory changes in 2019 including extending the Senior Managers and Certification Regime to the Group's regulated subsidiaries; European Banking Authority guidelines on security measures for operational and security risks and fraud reporting under PSD2; and improvements to operational resilience.

Strategic report

Principal risks and uncertainties

Strategic and emerging risks

In addition to the principal risks disclosed above, the Board considers strategic and emerging risks, including key factors, trends and uncertainties which can influence the results of the Group. These risks include the following:

Macroeconomic environment and market conditions

The Group operates exclusively within the UK and its performance is influenced by the macroeconomic environment in the UK. The economy affects demand for the Group's products, margins that can be earned on lending assets and the levels of loan impairment.

Although political and economic uncertainty has been prevalent throughout the year, the fundamental elements of the UK economy remain strong. Employment rates are at a record high and real take home pay is rising. Once current levels of uncertainty have abated, the Group expects levels of business investment, which have been held back, to increase and provide a boost to the economy.

UK withdrawal from European Union

The UK economy continued to grow in 2018. However, this growth was tempered by the uncertainty regarding the nature of the UK's exit from the European Union. Political developments led to a position where, at the end of 2018, it was unclear whether the UK would be leaving the EU with a deal in place regarding the terms of its withdrawal, leaving with no deal in place, leaving at a later date or potentially, if a second referendum were called, not leaving in March 2019 or at all. The decision to extend the deadline and the scheduled indicative votes in the House of Commons on the preferred outcome leaves all of these options open.

The direct impact to the Group of the UK leaving the EU is limited, even in a no deal scenario. The "Partnership Pack" published by the government in December 2018 provides information in respect of cross border processes and procedures, including customs, excise and taxation arrangements, in the event of no deal. This document, and further publications issued in 2019, have not highlighted any additional direct risks to the Group. All continuing trade is within the UK, and the lending sectors that the Group operates in are not significantly reliant on cross border arrangements.

However, the indirect consequences of a no deal scenario could be more significant. If a customs border were established between the UK and the EU, then this could present a significant cost for many UK businesses. A knock on impact to consumer confidence and economic growth could dampen demand for the Group's products, and/or result in deteriorating bad debt performance and hence higher impairment charges.

In particular, for the Group's most significant business units:

Business Unit	Potential indirect impact of no deal exit
Real Estate Finance	Direct consequences on the procedures for the transfer, renting and mortgaging of property are considered unlikely. If there is a reduction in UK Finance providers, then contraction of supply could affect the choice and terms of funding available for investment or development projects. The timing or cost of development projects could be affected by price increases and/or shipping delays. Developers on some, particularly larger projects, may be more cautious about committing to dates and costs without scope for adjustment for the effect of a no deal withdrawal. These factors could reduce demand for the Group's products.

Strategic and emerging risks (continued)

Business Unit	Potential indirect impact of no deal exit
Commercial Finance	No direct consequence is expected due to this division's UK customer base. Invoice financing has some countercyclical characteristics, though its medium term performance is directly linked to macroeconomic conditions, given lending balances are secured against the customer's sales ledger.
Retail Finance	The key market sectors funded by Retail Finance could be impacted by rising raw material or finished goods input prices. Retailers would need to decide whether to pass on costs or absorb them into margins. Rising consumer prices would likely lead to reduced consumer confidence and demand and reduced retailer margins would likely lead to retailers halting or slowing UK expansion. These factors could reduce demand for the Group's products. Consumer affordability issues could also impact on the Group's profitability through increased impairment provisions.
Motor Finance	This division serves the UK used car market, which unlike the supply of new vehicles (often originating from other EU markets and attracting increased tariffs), is largely self-contained. However, subdued economic conditions and lower consumer confidence or spending power may have a potential adverse impact on used car demand, and associated demand for the Group's financing. Affordability issues may also adversely impact the Group's profitability through increased bad debts.

The Group considers the most significant potential impact of a no deal exit to be that on credit risk. In response to the uncertainty regarding the exit from the EU, the Group worked with external consultants to assess the likely impact of a no deal scenario on its Consumer Finance portfolios.

This assessment included stress test modelling of a no deal departure, using the Group's ICAAP models. Assumptions used in the models were based on seven published economic models, developed by: Organisation for Economic Co-operation and Development ('OECD'), London School of Economics ('LSE'), Economists for Brexit ('EfB'), HM Treasury ('HMT'), National Institute for Economic and Social Research ('NIESR'), Oxford Economics ('OE') and PwC. Review of these assumptions led to four summary scenarios: long, sharp recession; long, shallow recession; short, shallow recession; no recession. Each of these four scenarios was modelled to identify the expected impact on impairment provisions in respect of the Group's consumer lending portfolios.

A range of outcomes was provided and reviewed by management. While the outcomes derived from the recession scenarios resulted in higher impairment provisions than those set out in the Group's central plan, these were not at a level that were considered to compromise the Group's viability. It was concluded that the Group did not need to change strategy in the anticipation of a potential no deal exit from the EU.

Following this work, the Group has developed additional early warning indicators that could indicate the need to change strategy, and the activities required in this eventuality to bring impairment losses back to base level. As well as existing measures relating to loan book performance, economic variables were selected which would act as lead indicators of potential issues. These include the Sterling to Euro exchange rate, movements in the FTSE 250 and government bond yields.

Strategic report

Principal risks and uncertainties

Strategic and emerging risks (continued)

Model Risk and the impact of IFRS 9

As reported last year, the Group's modelling capability was significantly enhanced with the introduction of IFRS 9. The suite of models used to derive the probability of default ('PD'), loss given default ('LGD') and exposure at default ('EAD') of the Group's lending portfolios, and therefore impairment provisions, has been monitored throughout the year and found to be working effectively. Modest enhancements have been made which have reduced the need for expert credit judgement overlays to be used in addition to model output.

The Model Governance Committee was established in 2018 and now reports to Risk Committee. In addition to the IFRS 9 models, this committee has also reviewed and approved the models used to derive the effective interest rate and drive income release in respect of the Group's consumer lending portfolios, the IFRS 9 forecasting model and the models used in the Group's ICAAP.

The use of expected loss models for IFRS 9 accelerates impairment provisions and also accelerates the impact of changes, arising from loan performance or macroeconomic factors. This can introduce more volatility into reported earnings, albeit over time the underlying profit on a loan is unchanged. The improvement in the quality of the Group's Motor Finance lending and collections performance delivered a reduction in impairment losses for this portfolio in this accounting period, greater than would have been reported under the previous IAS 39 standard. A future deterioration in performance or in the UK economy more generally could have the opposite effect.

Risk management

Details of the Group's risk management framework, including risk appetite, governance arrangements and key committees, can be found on the Group's website:
www.securetrustbank.com/our-corporate-information/risk-management

Strategic report

Going concern and viability

Going concern

In assessing the Group as a going concern, the directors have given consideration to the factors likely to affect its future performance and development, the Group's financial position and the principal risks and uncertainties facing the Group, as set out in the Strategic Report. The Group uses various short and medium term forecasts to monitor future capital and liquidity requirements and these include stress testing assumptions to identify the headroom on regulatory compliance measures.

The directors are satisfied that the Company and the Group have adequate resources to continue to operate for the foreseeable future as going concerns. For this reason they continue to adopt the going concern basis in preparing these financial statements.

Business viability

In accordance with provision C2.2 of the UK Corporate Governance Code, the directors confirm that there is a reasonable expectation that the Company and the Group will be able to continue in operation and meet their liabilities as they fall due, for the period up to 31 December 2021. The assessment of ongoing viability covers this period as it falls within the Group's five year planning horizon and is the period covered by the Group's stress testing.

Given the Group's healthy capital and liquidity position, reduction in exposure to higher risk lending, continuing growth in profit and positive trading outlook, the directors are confident of the Group's viability over the longer term. However, the inherent uncertainties regarding the economic, regulatory and market environment that the Group operates in may compromise the reliability of longer range forecasts. Given current economic uncertainties, and this being the first year in which the Group has extended its planning horizon to five years, the Board has decided to continue to use a three year period for its assessment of viability rather than extending this over the full planning horizon.

The directors have based the assessment on:

- The latest annual budget, which contains information on the expected financial position and performance for the period to 31 December 2023 and by considering the potential impact of the principal risks facing the Group, as set out on pages 40 to 51.
- The analysis of key sensitivities, undertaken as part of the budget process, which could impact on profitability over the period covered by the budget. Assumptions made to calculate risk weighted assets and capital requirements are clearly stated and additional scenarios are modelled to demonstrate the potential impact of risks and uncertainties on capital.
- The Group's ILAAP, which uses stress scenarios to assess the adequacy of liquidity resources. The results of this scenario analysis are used to set the Group's OLAR and are also the basis of the liquidity requirements set by the PRA. The Group has maintained liquidity levels in excess of regulatory requirements throughout the year and is forecast to continue to do so.
- The Group's ICAAP, which considers a macroeconomic stress and a severe shock scenario in order to assess the adequacy of capital resources. The results of the scenario analysis are used to set the Group's internal and regulatory capital requirements. The Group has maintained capital levels in excess of regulatory requirements throughout the year and is forecast to continue to do so.
- Consideration of the other principal risks as set out on pages 40 to 51, to identify any other severe but plausible scenarios that could threaten the Group's business model, future performance, solvency or liquidity.

- Analysis of further scenarios related to the UK's withdrawal from the European Union. Further details of this analysis are provided on page 49.

In making this statement, the Board has sought input from the Audit Committee and the Risk Committee.

Strategic report

Corporate responsibility

The Group has a clearly defined commitment within the corporate strategy 'To make this a great bank for customers and colleagues'.

The Group strategy is underpinned by six core values that reflect the behaviours required to deliver the Group's promise to deliver straightforward and transparent banking. Exceeding customer expectations and living the Group's values are at the heart of the Group culture and as such it rewards innovative and inspiring behaviours and sets clear expectations around staff being trustworthy, compliant and safe. The Group also always seeks to act as a responsible business. Further details on how the Group meets its commitments are set out below.

Responsible business

The Group takes its commitment to operate as a responsible business very seriously and recognises that this goes beyond the adherence to legal requirements and best practice. Measures are in place to assess the impact of the Group's business model and the delivery of its services on its customers, and the organisation strives to make a positive contribution to the wider community in which it operates. The Board considers that its governance arrangements, including the Group's risk management framework, ensure that environmental and social matters are appropriately dealt with.

The Group considers its ability to have a positive effect on social and community issues to be an extension of its customer centric culture. Employees are encouraged to make a positive contribution through a number of community focused schemes, and the Group's Charity Committees empower colleagues from different business areas to drive forward a wide range of successful charitable activities, backed by a pound-for-pound matching scheme. Last year the Group supported 25 charities through activities run by its Charity Committees, with the enthusiasm of colleagues to help good causes once again generating over £50,000 for charities in 2018.

In addition, many employees participated in the Group's volunteering scheme that enables them to take one day paid leave to make a difference to charities or community groups in their area. Nearly a thousand hours were donated in this way during 2018. Employees have taken part in a wide range of activities and made a positive contribution to many charities and community projects.

Greenhouse Gas emissions from our operations

As a financial services provider, the Group's operations do not have a significant impact on the environment. The Group reports on its greenhouse gas emissions and, to ensure its environmental impact remains low, has included it as a key performance indicator. The key performance indicators are shown on page 18.

The Group's report on all of the emission sources required under the Companies Act 2006 (Strategic Report and Directors' Report) Regulation 2013 is set out below. This is the second Greenhouse Gas report that the Group has issued under the above Regulation and only emission sources where accurate and consistent data is available for the complete reporting period have been included.

Scope 1 emissions resulting from the combustion of natural gas for heating buildings and fuel for business mileage, and Scope 2 and 3 emissions associated with the consumption of purchased electricity are included within the GHG report. Scope 1 emissions resulting from the private use of company owned/leased vehicles have been excluded. All Scope 3 sources, except for purchased electricity transmission, distribution emissions and grey fleet have also been excluded from this report. The Group has set 2017 as the GHG baseline year and reports from 2018 will show emissions for the current year and for each subsequent year following the baseline year.

In compiling this GHG report, the GHG Protocol Corporate Accounting and Reporting Standard (revised edition) and energy supplier invoice data have been used. Greenhouse gas emissions are reported as a single total, by converting them to the equivalent amount of CO_2 using emission factors from the UK Government's GHG Conversion Factors for Company Reporting 2017.

The Group's Greenhouse Gas emissions are shown below.

	2018 Carbon dioxide (tonnes)	2017 Carbon dioxide (tonnes)
Scope 1 – direct emissions from combustion of fuel	25.9	26.7
Scope 2 – indirect emissions from electricity purchased	403.9	501.7
Scope 3 – other indirect emissions from purchased electricity transmission and distribution	135.2	152.7
Total scope 1 to 3 emissions	565.0	681.1
Environmental intensity indicator (tonnes carbon dioxide per £1 million Group income)	3.5	4.2

Employees

Employee Voice

The Group firmly believes that engaging and listening to the views of its employees is crucial in making Secure Trust Bank a great place to work.

The Group currently holds the highly coveted Investors in People Gold Accreditation. This internationally recognised accreditation is held by over 10,000 organisations worldwide and defines what it takes to lead, support and manage people well for sustainable results. The Investors in People Standard is underpinned by a rigorous assessment methodology and a framework which reflects the very latest workplace trends, essential skills and effective structures required to outperform in any industry.

In addition to the actions taken both at a Group and departmental level on its previous 'Your Voice' employee opinion survey, in 2018 the Group implemented a new engagement survey methodology.

Strategic report

Corporate responsibility

The assessment conducted by the Great Place to Work® ('GPTW®') Institute explored the levels of trust and employee engagement across the Group. As a consultancy specialising in workplace culture and partnering with over 10,000 organisations annually, GPTW® has been able to benchmark Secure Trust Bank's employee experience against some of the most progressive workplaces in the UK. The Group changed provider to GPTW® given the links to its strategy to make this a great bank for customers and colleagues.

An excellent response rate of 85% was achieved providing a good mandate for action. There were some very positive highlights from the survey, with 77% of respondents stating that 'Secure Trust Bank is a Great Place to Work'. A number of areas, such as Diversity and Line Management, were identified as being above the 'Best in Class' organisations recognised by GPTW®. As a consequence of the excellent engagement levels, Secure Trust Bank will be recognised at the Best Workplace awards in May 2019, with a subsequent national media campaign publicising this success in The Guardian and The Sunday Telegraph newspapers. There can be little doubt that this will have strong resonance with both existing and potential employees.

The **Trust Index** score resulting from the survey was 77%. The Trust Index is the average of the core survey statements asked in the survey and will now be used as the Group's key performance indicator in respect of employee satisfaction. The **Engagement** score, which is a key outcome measure including questions on positive outcomes for the organisation and its employees, was previously used as the key performance indicator. The **Engagement** score was 76% in 2018 and 78% in 2017, the prior year measure based on the previous survey methodology and provider.

Crucially, to support the Group's desire for continuous improvement, the Leadership Team has reflected upon the results and committed to focusing on the specific areas of opportunity over the coming months to further enhance the employees' workplace experience at Secure Trust Bank. Most notably the Group has joined Business in the Community ('BiTC'), the Prince's Responsible Business Network. BiTC exists to create healthy communities with responsible businesses at their heart. The first phase of the relationship will see the Group working with BiTC to develop a Responsible Business Strategy aligned to the BiTC Responsible Business Framework to further build on the foundations laid in recent years.

As part of this partnership the Group will:
- Consolidate current Responsible Business activity and have it all in one place
- Benchmark future activity and identify Responsible Business gaps
- Access education resources to deliver in schools for positive impact in our local communities
- Provide opportunities for staff at all levels to engage with networking, development and workshop opportunities.

The Group also operates Employee Councils in each of its businesses, consisting of department representatives elected by their colleagues. The Councils meet on a regular basis and encourage a two way process of communication between employees and senior managers. In 2018 the Group introduced a Group Employee Council that meets with the Chief Executive Officer, HR Director and Senior Independent Non-Executive Director.

The aim of the Employee Councils is to further promote employee engagement and provide a structured forum for teams to share their views, enabling colleagues to provide insight, feedback and suggestions to make Secure Trust Bank Group a great place to work.

Various initiatives have been implemented following feedback from this group. Furthermore, key business information is shared with the Councils to enable representatives to support their colleagues and act as advocates for key initiatives such as the Group's recognition schemes and 'Boost', the Group's Employee Benefit and discount platform.

Employee Development

The Group was extremely proud that in 2018 it achieved accreditation from the National Skills Academy for Financial Services for its learning and development provision. Employee Development remains a priority and the Group has a comprehensive induction programme for new employees that achieves consistently high satisfaction scores from attendees.

In addition the Group continues to fund a wide range of specialist professional qualifications and had yet another record number of employees sign up to study towards an external Banking Qualification as part of their career development. The Banking Qualifications are delivered by the London Institute of Banking & Finance (previously the IFS) and are available to all employees.

To give colleagues greater insight into how to progress their careers, last year saw the introduction of a transparent pay and grading structure which is underpinned by a values-based behavioural framework. To further support this, the Group has introduced a Confident Leader Academy for Aspiring to Strategic leaders to provide a clear development path for those who wish to progress in a leadership role.

The Group continues to take steps to address the wider needs and concerns of its staff. A number of people managers attended training in partnership with Mind and Samaritans and, as part of the Group's wellbeing focus on mental health during the year, all staff were given the opportunity to attend mental wellbeing awareness sessions run by Mind. Mental Health Awareness training now forms an integral part of the core development programme for all people leaders.

Employee engagement and recognition

Research has consistently shown a clear link between enhanced levels of performance and teams that are fully engaged and share the values of the organisation that they work for. The positive performance of Secure Trust Bank Group is a result of the efforts of employees and to ensure that colleagues are recognised for this contribution there are a number of schemes in place to celebrate exceptional performance and behaviours.

These schemes together with the Group's annual incentive programme continue to help embed excellence within the culture.

These schemes include:
e thank you cards and Be valued awards: Being thanked is something that everyone appreciates and it makes individuals feel valued and helps create job satisfaction. For those occasions when colleagues deserve a thank you and behaviours are observed that truly reflected one of the Company values, colleagues can recognise each other by sending an e card thank you card. Where behaviour has been exceptional, line managers have the opportunity to reward team members with a Be Valued award which includes a gift and certificate. Colleagues can nominate their peers whenever and as often as they like and in 2018 over 2,500 e cards were sent. This was double the amount sent in the previous year.

Strategic report

Corporate responsibility

Customer Service Excellence Awards: colleagues who go the extra mile when it comes to exceptional internal and external customer service are recognised at monthly Customer Service Excellence Awards.

Outstanding achievers: these are given to colleagues who stand out for their fantastic contribution to the business. Winners are nominated by their peers and then selected by a panel of judges. In 2018 the number of places available was increased by 50% and the format updated following feedback from the Employee Council.

Incentive programme: the Group's incentive scheme links tangible performance targets, which are based on the Group's strategy and values, to the outcomes of the scheme.

Long Service awards: to recognise loyalty and commitment to the Group, long service is awarded at key milestones from five years of service. Colleagues are rewarded with a cash payment, engraved pen, bottle of champagne, certificate and are also invited to lunch with the head of their business area. In 2018 over 400 years of long service were recognised.

Gender diversity

At the year end, the split by gender of the Group's employees was as follows:

	Male	Female
Directors	63%	37%
Senior managers	84%	16%
Other employees	44%	56%
Total	**47%**	**53%**

In 2018 the Group published its first Gender Pay Report and supporting commentary. The Group is committed to diversity in the workplace at all levels and the actions outlined in our report.

To support this a number of initiatives have been introduced including an exciting partnership with everywoman which gives all colleagues, regardless of gender, access to the everywomanNetwork, a highly acclaimed, online development tool, with a particular focus on empowering women to take control of their career development.

Paul Lynam, CEO, was appointed as an Everywoman Advocate and the Group's HR Director and Commercial Director V12 were also appointed as Everywoman Ambassadors. The support from the partnership with Everywoman has been pivotal in shaping our plans over the last year.

In 2018 the Executive Committee has completed comprehensive Inclusive Leadership training through the Employer Network for Equality and Inclusion. The Group continues to ensure that its recruiting managers are trained to ensure that all hiring adheres to equality and inclusion principles and that all talented individuals have the chance to progress in the organisation. Given the diverse nature of the Group, which includes a high number of unique roles with specialist skills, the Board was delighted that in 2018 internal applicants filled almost 40% of roles that had been identified as development opportunities. Of these, 61% were filled by female employees.

To further support its teams the Group has also introduced an enhanced Family Friendly policy which goes significantly beyond statutory obligations and which many of employees have already benefited from.

Strategic report

Corporate responsibility

Social Responsibility

Compliance with regulatory requirements is essential not only from the relevant regulator's perspective but also to maintain the trust of the Group's customers. The Group has a wide range of policies in place across all divisions to ensure that staff and management comply with all regulatory requirements and adhere to the highest professional and ethical standards in dealing with customers, suppliers and each other. All staff are required to complete the relevant regulatory training on an annual basis with further training offered when required, and the Group achieved 100% completion of mandatory training for eligible employees in the year. Some of the Group-wide policies and regulations include:

Anti-bribery and corruption policy

The Group operates a zero tolerance approach to bribery and corruption, ensuring compliance with all applicable anti-bribery and corruption laws and regulations, including the UK Bribery Act 2010.

Anti-money laundering regulations

The Group has implemented policies and procedures in accordance with anti-money laundering regulations and have dedicated money laundering reporting officers where required.

Employment Health and Safety

The Group's health and safety policy ensures the provision of a safe and healthy working environment for employees and visitors in accordance with The Management of Health and Safety at Work Regulations 1999.

Health and Safety is administered by the Group Operational Risk Committee which meets quarterly. The Group is proud of the continued progress in successfully raising the profile of health and safety across the business. This year nine incidents were recorded across all of sites, of which the majority were related to medical conditions, with only three reportable incidents in the year.

The Group engages relevant experts where appropriate to work with staff to assist with managing site-specific risks.

Whistleblowing policy

Employees are encouraged to report any activity that may constitute a violation of laws, regulations or internal policy and reporting channels are provided to staff for this purpose within the framework of a whistleblowing policy.

The Group's comprehensive whistleblowing procedures comply with the rules that came into effect in September 2016. The Group has enhanced the existing policies by the appointment of a whistleblowers' champion and a confidential telephone whistleblowing service, operated by a third party provider. Further information can be found in the Corporate Governance report for the Audit Committee.

Human rights and tackling modern slavery

The Group is subject to the European Convention on Human Rights and the UK Human Rights Act 1998. The fair treatment of customers is central to the Group's strategy and values, and the Group opposes all forms of discrimination.

Strategic report

Corporate responsibility

The Group is committed to tackling modern slavery and human trafficking and has taken steps to ensure it is considered and addressed in its business and throughout its supply chain, consistent with its obligations under the Modern Slavery Act 2015. All suppliers are asked to confirm their approach to modern slavery on an annual basis with the responses reviewed by Compliance. The full Board statement on Slavery and Human Trafficking can be found on the Group's website:
www.securetrustbank.com

Customers first

In the current internet age, getting customer service right has never been more important which is why it is central to the Group's mission to provide straightforward and transparent banking. The Group is focused on maintaining and promoting a culture which has colleague and customer centric attitudes at its heart and this is driven through specific initiatives and lived through day-to-day processes and interactions. This culture is reinforced through recognition and reward structures and a series of independent monitoring tools which facilitate a continuous process of customer service review and improvement.

The Group continues to use FEEFO, an independent global ratings and reviews provider used by the world's most trusted brands, to collect customer feedback. Customer comments and ratings are published in real time on the Group's website and used to monitor and maintain service levels. The Group's average FEEFO rating for the year based on nearly 1,200 reviews stood at 4.7 out of 5 at the end of December 2018 and all poor ratings are followed up by attempting to resolve the issue with the customer.

This year the Group also picked up FEEFO Trusted Service awards across all brands that FEEFO feedback is collected on for the third year running since the awards were launched. The awards are an independent seal of excellence that recognise businesses for delivering exceptional experiences, as rated by real customers. Secure Trust Bank Group's Moneyway and V12 brands were both awarded the coveted FEEFO Gold Trusted Award, whilst the Secure Trust Bank brand received a FEEFO Trusted Award.

The Trusted Service awards, created by FEEFO, are given to businesses using FEEFO to collect genuine ratings and reviews who also meet the criteria of excellence needed to achieve a Trusted Service Award. Only the businesses providing the best experience for their customers, as rated by them, receive an award.

FEEFO ratings and comments are available on the Group's websites:
www.securetrustbank.com
www.moneyway.co.uk

Strategic report

Corporate responsibility

Having been the first bank to be awarded the Customer Service Excellence Award, this year the Group was pleased to announce that it had retained the standard for the sixth year running. This Government backed accolade is awarded following a rigorous annual assessment which looks at processes, documents, reports and research to determine if the Group meets Government standards of excellence. The Customer Service Excellence standard tests areas that are most important to customers, such as delivery, timeliness, information, professionalism and staff attitudes. The assessment report was extremely complimentary noting that "Senior managers demonstrate a very strong commitment to their staff, and it is clear that the work that they do is valued at the highest level. It was evident when speaking to front line staff that they are highly motivated to achieve the best possible service for their customers and are given the opportunity to contribute to making improvements to the service. Staff receive rewards and recognition for their efforts at all levels. The organisation is committed to making improvements to its customers' experience year on year and continues to make significant progress against the CSE standard. The achievement of this accreditation is well deserved."

In addition to independent assessments of customer service levels, the Group's numerous internal recognition schemes are linked closely to its promise to deliver straightforward and transparent banking and its core values. This has been central to building great customer service, high staff engagement and colleagues who understand the vision and buy into the Group's culture.

Non-financial information statement

The Group aims to comply with the new non-financial information reporting requirements contained in sections 414CA and 414CB of the Companies Act 2006. This is intended to help stakeholders understand the Group's position on key non-financial information.

Information regarding environmental matters, employees, social matters, respect for human rights and anti-corruption and anti-bribery matters are included in this corporate responsibility section.

The location of the other information required is set out in the table below:

Reporting requirement	Section	Page
Policy embedding, due diligence and outcomes	Principal risks and uncertainties	40
Description of principal risks and impact of business activity	Principal risks and uncertainties	40
Description of the business model	Group strategy and business model	2
Non-financial key performance indicators	Financial review	18

Approved by the Board and signed on its behalf

Neeraj Kapur
Chief Financial Officer

27 March 2019

Corporate governance report

Chairman's introduction

On behalf of the Board I am pleased to introduce our report on Corporate Governance. This explains the Group's governance arrangements and how the Group has applied the principles of the 2016 UK Corporate Governance Code (the 'Code') during 2018. Reference is also made to changes in Corporate Governance resulting from the implementation of the 2018 UK Corporate Governance Code (the '2018 Code') which has effect from 1 January 2019.

2018 was another year of change and development in the Corporate Governance of the Group. As the Group has grown the governance has had to adapt. Public and regulatory expectations continue to evolve and require increasing standards of governance which we have embraced.

There have been some significant developments during 2018. In particular:-

- **Strategy**: The Board adopted a different approach to the review of the strategy of the Group culminating in Board Strategy Away Days in September 2018 at which the strategy was approved.

- **Composition of Board**: There have been changes to the composition of the Board during 2018 which have reinforced its independence while bringing additional skills and experience to the Board.

- **Remuneration**: The remuneration-related arrangements of the Group have been the subject of considerable focus and I am most grateful for the work that the Chairman of the Remuneration Committee and the other members of the Remuneration Committee have done in 2018 in developing this aspect of our Corporate Governance.

- **Oversight**: We have taken steps to strengthen the oversight exercised by the Board including the development of our governance framework, particularly in relation to the Risk Committee and its sub-committees - the Model Governance Committee, the Assumptions Committee and the Assets and Liabilities Committee. The Risk Committee has spent a considerable amount of time in relation to oversight of management actions in relation to Information Security (including Cyber Security and Operational Resilience) which are important areas of risk for any financial institution.

- **Auditor change**: 2018 was also the year in which we replaced our auditors and dealt with the implementation of a major new accounting standard and I am grateful to the Audit Committee for their work in ensuring a smooth transition to our new Auditors and in relation to the implementation of IFRS 9.

We have also had to adapt to the arrangements contemplated in the 2018 Code and this has resulted in changes to the composition of Board Committees which took effect at the end of January 2019. The 2018 Code removed the exemption for smaller public companies and we are now complying with all the provisions of the 2018 Code and, for the first time in 2019, all the Directors will present themselves for re-election at the 2019 Annual General Meeting.

The composition of the Board is kept under review and we had already initiated a process for the identification and appointment of additional independent Non-Executive Directors before Sir Henry Angest and Andrew Salmon resigned as Directors. I was delighted to welcome Baroness Neville-Rolfe and Paul Myers as additional independent Non-Executive Directors at the end of November 2018. Further information on the composition of the Board and its Committees is set out in the following pages of this report. I am pleased that we have a diverse Board: the membership of the Board is kept under review and we are mindful of the importance of succession planning.

We have also given consideration to the way in which we engage with our employees and I look forward to more engagement with our Group Employee Council in 2019.

Corporate governance report

Chairman's introduction

I am most grateful for the efforts of my colleagues in performing their roles as Directors of the Company, both Non-Executive and Executive. I have stated elsewhere in this report my thanks and appreciation of the support provided by Sir Henry Angest and Andrew Salmon over many years.

We have reviewed the effectiveness of the Board and its Committees and conducted an assessment of our Corporate Governance. There is always room for improvement but we can look back on 2018 as a year in which we strengthened the governance of the Group. There remains more to be done in 2019 as our Corporate Governance evolves further.

The Board looks forward to engaging the shareholders at the Annual General Meeting to be held on 15 May 2019.

Lord Forsyth
Chairman of the Board

Corporate governance report

Board of Directors

1. **The Rt Hon Lord Forsyth of Drumlean PC Kt – Non-Executive Chairman**

Appointed to the Board on 1 March 2014 as an Independent Non-Executive Director and appointed Chairman of the Company on 19 October 2016. ●●

Skills and experience

Lord Forsyth is a former Chairman of Hyperion Insurance Group, and former Deputy Chairman of JP Morgan UK and Evercore Partners International. He was appointed to the Privy Council in 1995, knighted in 1997, and joined the House of Lords in 1999. He was a member of the House of Commons for 14 years and served in Government for 10 years, latterly as a Cabinet Minster. His background in the public and private sectors has given Lord Forsyth a broad experience of matters relevant to the business of the Group including strategy, governance, operations, marketing, risk and human capital.

Other appointments include:

Lord Forsyth is a director of J&J Denholm Limited and Denholm Logistics Limited and Chairman of the House of Lords Economic Affairs Committee.

2. **Ann Berresford ACA – Independent Non-Executive Director**

Appointed to the Board on 22 November 2016 and appointed Chairman of the Audit Committee on 23 September 2017 and a member of the Risk Committee on 25 July 2018. ●●●

Skills and experience

Ann Berresford is a Chartered Accountant with a background in the financial services and energy sectors. She has held positions at Bath Building Society, the Pensions Regulator, Hyperion Insurance Group, Triodos Renewables plc, the Pension Protection Fund, Bank of Ireland Group, Clyde Petroleum plc and Grant Thornton. Her career has given Ann experience in mortgages, pensions, operations, accounting, finance and risk.

Other appointments include:

Ann is a non-executive director of Albion Venture Capital Trust PLC.

3. **Neeraj Kapur B.Eng, ACGI, FCA, CF, FCIBS – Chief Financial Officer**

Appointed to the Board on 31 May 2011. ●

Skills and experience

Neeraj Kapur has over 25 years' financial services experience spent in both the accounting and banking industries. He holds a degree in Aeronautical Engineering from Imperial College, London, is a fellow of the Chartered Institute of Bankers in Scotland, a fellow of the Institute of Directors, a fellow and a member of the Council of the Institute of Chartered Accountants in England & Wales ('ICAEW'), and Chair of the ICAEW Financial Services Faculty. Neeraj qualified as a Chartered Accountant in 1993 at Arthur Andersen and spent 11 years working in professional practice. He joined Royal Bank of Scotland ('RBS') in 2001 where he performed a number of roles which included Chief Financial Officer of Lombard North Central PLC. His background has given Neeraj experience in accounting, finance, professional services, governance, operations, marketing and risk.

Other appointments include:

Member of the Council of the ICAEW.

Corporate governance report

Board of Directors

4. **Paul Lynam ACIB, AMCT, Fifs – Chief Executive Officer**

Appointed to the Board on 13 September 2010. Chairman of the Assets and Liabilities Committee. ●

Skills and experience

Paul Lynam joined Secure Trust Bank as Chief Executive Officer, having spent 22 years working for NatWest and RBS. Prior to leaving RBS, Paul was the Managing Director, Banking, for RBS/NatWest's SME banking business across the UK. Before that Paul spent four years as the Managing Director of Lombard North Central PLC. During his career Paul has undertaken roles in branch banking, business banking, corporate and commercial banking, asset finance, invoice finance, strategy, performance management, lending and central head office functions. Paul is a non-executive director of UK Finance, the recognised trade body for the finance industry, leading on Challenger Banks and SME customer interests. He also chairs the Specialist Bank Strategic Advisory Committee. He is a Fellow of the IFS University College and an Associate of the Chartered Institute of Bankers and the Association of Corporate Treasurers.

On 30 January 2019 Paul resigned as a member of the Risk Committee.

Other appointments include:

Paul is a non-executive director of UK Finance, as well as a member of the faculty of the School for CEOs.

5. **Paul Marrow ACIB – Independent Non-Executive Director and Senior Independent Director.**

Appointed to the Board on 3 March 2011. Chairman of the Risk Committee and a member of the Audit, Remuneration and Nomination Committees. ●●●●

Skills and experience

Paul Marrow has over 40 years' banking experience and has, in the past, been responsible for the Commercial Banking and Specialist Corporate Banking business divisions of RBS Group in the UK and been the chair of JCB Finance Limited. Paul served for a number of years as Chair of the Audit Committee and was Chairman of the Everyday Loans Group during the period that it was part of the Group. During his career, Paul has gained experience in governance, risk, finance, accounting, operations and corporate strategy across a wide range of banking disciplines. Paul is an Associate of the Chartered Institute of Bankers.

Other appointments include:

Paul is an independent non-executive director of Arbuthnot Latham & Co. Limited, a wholly owned subsidiary of Arbuthnot Banking Group.

6. **Paul Myers ACIB – Independent Non-Executive Director**

Appointed to the Board on 28 November 2018 and a member of the Risk and Nomination Committees. ●●

Skills and experience

Paul Myers has many years of banking experience, gained initially in Barclays where he spent 24 years in a variety of retail banking roles. He was part of the small team that founded and built Aldermore Bank, where he served as Chief Operating Officer, Corporate Development Director and on the board as an executive director. Paul had a wide range of responsibilities at Aldermore, including IT, operations, transformation, marketing and digital as well as building and developing the retail and SME savings operations. Paul is an Associate of the Chartered Institute of Bankers.

Paul joined the Risk and Nomination Committees on 30 January 2019.

Other appointments include:

Paul was until February 2019 the chief executive officer and an executive director of GKBK Limited, which is a new banking venture.

7. **Baroness Lucy Neville-Rolfe DBE CMG – Independent Non-Executive Director**

Appointed to the Board on 28 November 2018 and a member of the Audit and Nomination Committees. ●●

Skills and experience

Baroness (Lucy) Neville-Rolfe DBE CMG has had a distinguished career in business and in public service. She became a member of the House of Lords in 2013 and was a minister in the Business and Culture Departments and in HM Treasury from 2014-2017. Lucy was an executive at Tesco plc for 15 years including serving for over six years on the main board. Her experience includes customer facing businesses and financial services, communications, corporate strategy and M&A, economic issues, regulation and governance experience as a company secretary and a non-executive director and chair.

Lucy joined the Audit and Nomination Committees on 30 January 2019.

Other appointments include:

Lucy is currently a Non-executive Director of Capita plc and Chairman of Assured Food Standards (Red Tractor). In the period 2010-14 she was a Non-Executive Director of ITV plc, of Metro AG, of 2 Sisters Food Group, of PWC's Advisory Board and Chairman of EuroCommerce in Brussels. Earlier in her career she was a civil servant in No 10 Downing St and the Director of the Deregulation Unit in the Cabinet Office. On 31 December 2018, Lucy was appointed a Director and Trustee of Thomson Reuters Founders Share Company Limited.

8. **Victoria Stewart – Independent Non-Executive Director**

Appointed to the Board on 22 November 2016, appointed Chairman of the Remuneration Committee on 21 July 2017 and appointed as a member of the Nomination Committee on 28 February 2018. ●●

Skills and experience

Victoria Stewart was for many years a fund manager and investor in UK small companies. Victoria has knowledge of corporate structures and capital markets with particular experience in smaller companies listed on the Main Market and AIM. She has held a number of positions at Royal London Group and Chiswell Associates (formerly Cantrade Investment Management Limited and now part of Sarasin & Partners). Her background has given Victoria experience in remuneration, governance, operations, investor relations, accounting, finance and risk.

Other appointments include:

Member of the ICAEW Corporate Governance Committee.

The Company Secretary is:

Alan Karter LLB (Hons) – Company Secretary

Alan Karter is a Scottish and English qualified solicitor and a former partner of Simmons & Simmons LLP. He joined Arbuthnot Banking Group as Head of Legal Affairs in February 2012 and was appointed Company Secretary of Secure Trust Bank PLC on 31 August 2014. On 1 September 2016 he transferred his employment from Arbuthnot Banking Group to the Company and was appointed to the dual role of General Counsel and Company Secretary of Secure Trust Bank.

Corporate governance report

Board of Directors

- Audit Committee members
- Risk Committee members
- Assets and Liabilities Committee members
- Remuneration Committee members
- Nomination Committee members

Corporate governance report

Board of Directors

Former Directors who served during the year.

Sir Henry Angest LLL – Non-Executive Director
Appointed to the Board on 28 January 1982. Resigned on 8 August 2018.

Skills and experience

Sir Henry Angest is an experienced and respected banker. He is a past Master of the Worshipful Company of International Bankers, Chairman and Chief Executive of Arbuthnot Banking Group and Chairman of Arbuthnot Latham & Co., Limited. He gained extensive national and international experience as an executive of The DOW Chemical Company and DOW Banking Corporation. He was chairman of the banking committee of the London Investment Banking Association and a director of the Institute of Directors. He has a law degree from the University of Basel. During his career, Sir Henry has gained extensive experience in leadership, general management, corporate strategy, acquisitions, banking operations, human capital, legal and risk.

Other appointments include:

Sir Henry is Chairman of Arbuthnot Banking Group PLC and of its subsidiary Arbuthnot Latham & Co., Limited. Sir Henry was originally appointed by Arbuthnot Banking Group to the Board of Secure Trust Bank PLC.

Andrew Salmon ACA – Non-Executive Director
Appointed to the Board on 8 July 2003. Resigned on 8 August 2018.

Skills and experience

Andrew Salmon joined Arbuthnot Banking Group in 1997 and is its Chief Operating Officer and Head of Business Development and the Chief Executive Officer of Arbuthnot Latham & Co., Limited. He was previously a director of Hambros Bank Limited and qualified as a Chartered Accountant with KPMG. His professional qualification and background in the financial services sector has given Andrew experience in remuneration, governance, operations, accounting, finance, marketing, risk and compliance.

Other appointments include:

Andrew is a Director of Arbuthnot Banking Group PLC and its subsidiary Arbuthnot Latham & Co., Limited. Andrew was originally appointed by Arbuthnot Banking Group to the Board of Secure Trust Bank PLC.

Corporate governance report

Corporate governance statement

2016 UK Corporate Governance Code (the 'Code') – Statement of Compliance

The Code sets out principles relating to good governance of companies. The Code is available at www.frc.org.uk. Throughout the period under review, the Company was subject to the Code.

The Board confirms that from 1 January 2018 to 31 December 2018 the Group complied with the requirements of the Code.

The Board has taken steps to ensure compliance with the 2018 UK Corporate Governance Code (the '2018 Code') which came into effect from 1 January 2019 and these are described in the Nomination Committee Report.

The following sections of this report describe how the Board has applied the principles of the Code and describes the Group's governance arrangements with particular reference to leadership, effectiveness, accountability, remuneration and relations with shareholders.

Section A: Leadership

Role of the Board

The Board is led by the Chairman. The Board provides strategic leadership to the Group, sets the Group's long term strategic objectives and exercises oversight over the implementation of the strategy and the activities of management. The Board is responsible for promoting the long term success of the Group. The setting of a risk appetite and the oversight of risk management practices is an important part of the role of the Board both directly and through the Risk Committee.

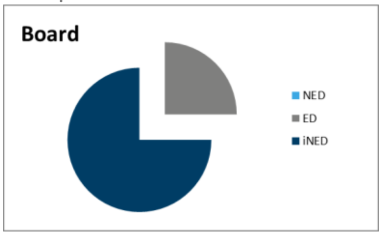
The Board meets regularly and, both as a Board and through its committees, provides direction, oversight and challenge of and to management. The Board has delegated specific authorities to its committees as set out in each Committee's terms of reference. The Board exercises oversight of the work of its committees and receives updates on the work of each committee at Board meetings.

There is a schedule of matters reserved for consideration by the Board. Matters reserved for exclusive determination by the Board include the determination of dividends, material acquisitions or disposals and the issue of new shares.

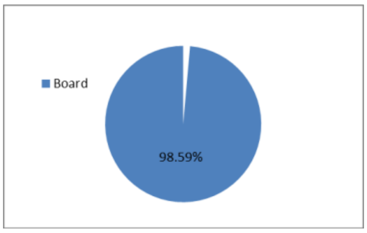
The Board has delegated authority to executive management to run the business and to implement the strategy set by the Board. Two members of executive management, the CEO and the CFO, are members of the Board.

Board composition

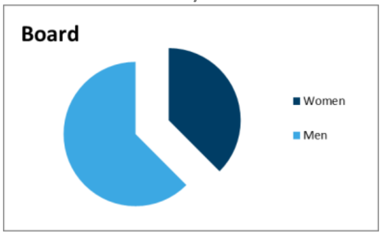
Composition



Meeting attendance



Gender Diversity

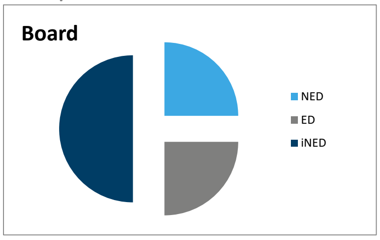


Corporate governance report

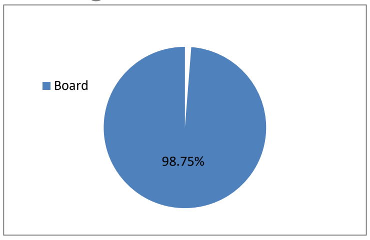
Corporate governance statement

Metrics for 2017:

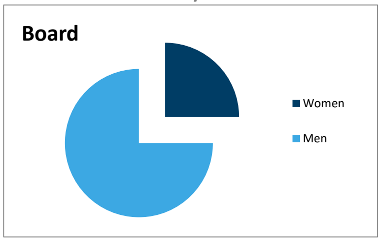
Composition



Meeting attendance



Gender Diversity



The Board meets formally at least eight times a year and otherwise as required. The number of planned meetings held during 2018 and the attending Directors are shown in the table below:

	Board
Number of meetings during 2018	9
Lord Forsyth (Chairman)	9/9
Ann Berresford	9/9
Neeraj Kapur	8/9
Paul Lynam	9/9
Paul Marrow (Senior Independent Director)	8/9
Paul Myers[1]	0/0
Baroness Lucy Neville-Rolfe[1]	0/0
Victoria Stewart	9/9
Former Directors	7
Sir Henry Angest	6/7
Andrew Salmon	7/7

[1] Baroness Neville-Rolfe and Paul Myers attended the Board meeting in November 2018 as observers, their appointment being effective from the close of the meeting.

There are eight members of the Board as set out in the chart above. Biographical details for each director can be found on pages 64 to 67 together with their roles and membership of Committees. Further information on Board effectiveness, Non-Executive Director evaluation and independence can be found on page 72.

The Code recommends that the Board should appoint one of the independent Non-Executive Directors as Senior Independent Director. The Senior Independent Director should be available to shareholders if they have concerns which contact through the normal channels of Chairman, Chief Executive Officer or other Executive Directors has failed to resolve or for which such contact is inappropriate. The Board has appointed Paul Marrow as the Senior Independent Director.

Role of the Chairman

The Chairman's role is to ensure good corporate governance and the smooth and effective operation of the Board. His responsibilities include leading the Board, ensuring the effectiveness of the Board, supporting effective communication with shareholders, setting the Board's agenda and ensuring that all Directors are encouraged to participate fully in the activities and decision making process of the Board.

Corporate governance report

Corporate governance statement

The Chairman of the Board and the Chairmen of the Remuneration, Risk and Audit Committees and the Senior Independent Director, together with the Chief Executive Officer and Chief Financial Officer, are all Senior Managers for the purposes of the Senior Manager Regime.

Separation of roles of Chairman and Chief Executive

The roles of the Chairman and the Chief Executive Officer are separate, clearly defined in writing and have been approved by the Board.

Meetings

The Board meets at regular intervals. There is a comprehensive Board pack and agenda which is circulated in advance of the meeting and minutes and actions are documented. There is an annual Board calendar at which certain items are considered by the Board at certain times of the year, including the report and accounts, regulatory filings and review of risk appetite. Additional meetings of the Board are held as required and, in addition to the standing committees of the Board, the Board may appoint ad hoc committees to deal with particular matters from time to time. Charts in the Corporate Governance Report show scheduled meeting attendance.

Company Secretary

The Company Secretary or the Deputy Company Secretary acts as Secretary to the Board and its Committees and is responsible for ensuring that Board processes and procedures are followed and support effective decision making. All Directors have access to the Company Secretary's advice and services. Directors may obtain independent professional advice in the course of their duties, if necessary, at the Company's expense in order to assist them in carrying out their duties.

The Company Secretary provides support and acts as a first point of contact for the Chairman and Non-Executive Directors. The Company Secretary is also responsible for the induction of new independent Non-Executive Directors.

The role of the members of the Board

The Chairman leads the Board and sets the Board's agenda with the support of the Company Secretary.

The Chief Executive Officer is responsible for the day-to-day management of the Group within the delegated authorities and risk appetite approved by the Board. He recommends the Group strategy and leads the executive management team in the execution of the strategy approved by the Board. He leads the relationship with institutional shareholders and ensures that timely and accurate information is disclosed to the market.

The Chief Financial Officer manages the Group's financial affairs and supports the Chief Executive Officer in the management of the business. He has particular responsibility for the financial and regulatory reporting of the Group and balance sheet and liquidity management.

The Senior Independent Director acts as a sounding board for other Non-Executive Directors and the Chairman. The Senior Independent Director also conducts the Chairman's annual performance evaluation, collecting views from the other Directors.

The Non-Executive Directors provide independent and constructive challenge of the Executive Directors and scrutinise the delivery of the strategy within the risk and control framework set by the Board. Non-Executive Directors also determine Executive Director remuneration.

Executive management

The Chief Executive Officer and Chief Financial Officer are supported by an executive team who sit on an Executive Committee which operates under authorities delegated from the Board.

Below the Executive Committee there is a comprehensive governance structure involving a number of committees linked to business lines and functions. Details of that structure can be found on the Company's website www.securetrustbank.com.

Committees

The Board has established Audit, Nomination, Remuneration and Risk Committees. There is also an Assets and Liabilities Committee ('ALCO') a Model Governance Committee and an Assumptions Committee all of which ultimately report to the Risk Committee. Each committee has formally delegated duties and responsibilities and written terms of reference. The terms of reference of the Board committees are available on www.securetrustbank.com.

All Board committees have access to independent advice and the services of the Company Secretary.

Further information about the Board committees is set out later in this governance report, including information about membership of the committees, meetings held during the year and the attendance of committee members.

Election of Directors

The Articles of Association contain provisions for the retirement by rotation of Directors. The Board has decided to follow the provisions of the 2018 Code and to require each director who is not already standing for election at the first AGM since their appointment, to stand for re-election.

The Board recommends the election or re-election of each of the Directors at the 2019 Annual General Meeting. Further information about each director standing for election or re-election can be found on page 116 and in the circular containing the Notice of Annual General Meeting.

Section B: Effectiveness

Appointments to the Board

Appointments to the Board are the responsibility of the full Board, on the recommendation of the Nomination Committee. On appointment, new Non-Executive Directors enter into a formal appointment letter which sets out the terms and conditions of their appointment as Non-Executive Directors. The terms and conditions of appointment of the Non-Executive Directors and the service contracts of Executive Directors are available for inspection at the Group's registered office during normal business hours. The letters of appointment of the Non-Executive Directors were amended in January 2019 to reflect changes to the composition of the Board's Committees, associated changes to individual Non-Executive Director responsibilities and amendments to their fees.

Induction, training and professional development

On appointment, all new Directors receive a comprehensive and tailored induction. The induction involves provision of information about the Group as well as face-to-face meetings with Directors and senior management. New Directors have access to historic Board material, including the prospectus and other Admission related documentation. New Directors are also provided with briefing notes on regulatory and legal matters, including their duties and responsibilities under the Companies Act 2006.

Further information on Board training and development can be found on page 79.

Board effectiveness

The composition of the Board and its committees and the performance of Directors were rigorously evaluated during the year. More details can be found on pages 78 to 79.

Formal evaluations of the performance of the Audit, Nomination, Remuneration and Risk committees took place during the year and the result of those evaluations was that the performance of each committee was considered to be satisfactory. Where actions to improve the committee performance have been identified, these are disclosed in the respective committee report.

The Board conducted a formal self-evaluation of the effectiveness of the Board to assess its effectiveness and how it performs, along with other Board related governance matters, including the provision of information to the Board. Further details can be found on page 78.

Diversity

The Board has adopted a Board policy on diversity, which addresses gender, race, ethnicity, age, disability, religious belief, sexual orientation, marital status, gender reassignment and pregnancy (together 'Diversity').

The Board embraces the benefits of Diversity in the boardroom and considers that Diversity benefits governance. In considering the appointment of new Directors, the Board gave careful consideration to Diversity as well as the skill, experience and knowledge of the candidates. The Board approved Board Diversity Policy operates in conjunction with the Equality and Diversity Policy applicable throughout the Group. Appointments to the Board are made on merit and having regard to the balance of skills and experience of the Board and the candidates. The Board has not set targets for representation of any particular group on the Board. Female membership of the Board currently stands at 37.5%. BAME membership currently stands at 12.5%.

Section C: Accountability

The Board has delegated authority to the Audit, Nomination, Remuneration and Risk Committees to exercise oversight of aspects of the operations of the Group.

Conflicts of Interest

All Directors are required to disclose to the Board any outside interests which may pose a conflict with their duties to the Group. The Board is required to approve any actual or potential conflicts of interest. On appointment new Directors are required to disclose their other interests. Conflicts of interest are also governed by the Articles of Association of the Company and company law.

Financial reporting

A description of the responsibilities of the Directors in relation to the preparation of the annual report and accounts is set out on page 120.

The approach taken by the Board to ensuring that the annual report and accounts are fair, balanced and understandable is set out on page 118 and the information necessary for shareholders to assess the Company's position and performance is set out in the Strategic Report starting on page 2. An explanation of the business model and the strategy for delivering the objectives of the Company is set out on pages 2 to 5.

Corporate governance report

Corporate governance statement

A statement of the responsibility of the external auditors in relation to the report and accounts is set out on page 130.

The basis on which the Board reached its decision to adopt the going concern basis of accounting is described on page 52.

Internal Control

The Board has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against the risk of material misstatement or loss.

The Board has adopted a Group risk appetite statement which sets out the Board's attitude to risk and internal control. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board and are also reviewed by the Risk Committee at its meetings. Key business risks are also identified, evaluated and managed on an ongoing basis by management. The Board and the Risk Committee also receive regular reports on any material risk matters. Significant risks identified in connection with the development of new activities are considered by the Board and the Risk Committee in conjunction with the approval of any such new activity.

The effectiveness of the internal control system is reviewed regularly by the Board and the Audit Committee, which also receives reports of reviews undertaken by the internal audit function. The Audit Committee also receives reports from the external auditors, Deloitte LLP, which include details of internal control matters that they have identified. Certain aspects of the system of internal control are also subject to regulatory supervision, the results of which are monitored closely by the Board and its Committees.

Key elements of the Group's system of internal control include regular meetings of the executive and business unit risk committees, together with annual budgeting, monthly financial and operational reporting for all businesses within the Group. Conduct and compliance are monitored by management, the Risk team, Internal Audit and Compliance and, to the extent necessary to support its audit report, the external auditor. Oversight is also exercised by the Board and the Audit and Risk Committees.

During 2018 the Group continued to invest in its Treasury management capability and this on-going investment will continue during 2019.

The Board regularly reviews actual and forecast performance compared with annual plans as well as other key performance indicators as described on page 18.

Lines of responsibility and delegated authorities are clearly defined.

The Group's policies and procedures are reviewed and regularly updated and a training programme applies in relation to the roll-out of policies.

Section D: Remuneration

Details regarding the remuneration of the Directors, the governance processes connected with remuneration and the operation of the Directors Remuneration Policy can be found on pages 92 to 113.

Corporate governance report

Corporate governance statement

Section E: Relations with shareholders

The Company maintains a regular dialogue with its principal shareholders and makes full use of the Annual General Meeting to communicate with investors. All Directors are expected to make themselves available to shareholders at the Annual General Meeting. The Chairmen of the Board Committees will be available at the Annual General Meeting to answer questions about the work of their committees.

The Board recognises the importance of maintaining good relationships with shareholders. The Chief Executive Officer and the Chief Financial Officer would normally expect to meet with institutional shareholders on a regular basis, including following the publication of financial information or updates by the Group. The Chairman has joined them in some meetings throughout 2018 and 2019. The Group's brokers also facilitate communication between the Group and its institutional shareholders.

The Chairman is responsible for ensuring that appropriate channels of communication are established between the Directors (and in particular the Chief Executive Officer and Chief Financial Officer) and shareholders and that the views of shareholders are made known to the Board.

The Chief Executive Officer provides written reports prepared by the Group's brokers to all Directors on meetings held with institutional shareholders.

The Group recognises the importance of ensuring effective communication with its shareholders. An annual financial report is distributed to all shareholders. This report, together with the half-yearly financial report, regulatory announcements and current details of the Group's share price are made available on the Company's website.

Annual General Meeting

The Group's Annual General Meeting will be held at Arbuthnot House, 7 Wilson Street, London, EC2M 2SN at 3.00 p.m. on Wednesday 15 May 2019. The Notice of Annual General Meeting, together with an explanation of the items of business to be discussed at the meeting will be posted to shareholders and made available at www.securetrustbank.com.

Members of the Board will be in attendance at the 2019 Annual General Meeting which will provide an opportunity to engage with shareholders and to respond to any questions from shareholders.

Approval

This corporate governance statement was approved by the Board on 27 March 2019 and signed on its behalf by:

A J Karter
Secretary

Corporate governance report

Statement by the Chairman of the Nomination Committee

I am pleased to present the report of the Nomination Committee in respect of 2018, which was an important year for the Company.

In February 2018 we assessed the composition of the Board and its Committees and the balance between independent Non-Executive Directors and Non-Executive Directors in line with the proposals of the draft 2018 Code. The Committee recommended to the Board that it consider a search for further independent Non-Executive Directors and that Victoria Stewart be invited to join the Committee, which the Board approved on 28 February 2018. Sir Henry Angest and Andrew Salmon stepped down from Audit, Risk and Remuneration Committee duties on 31 March 2018 and the Committee, at the request of the Board, commenced a search for up to three additional independent Non-Executive Directors. With the assistance of the Secretary, we conducted a competitive tender process for the appointment of a recruitment agent and determined that Korn Ferry should be appointed to assist in the search. None of the Directors or the Company had an existing relationship with Korn Ferry.

The Committee worked with Korn Ferry to determine the search criteria for the recruitment process, having regard to both the Board's Diversity Policy and the Board and Committee effectiveness evaluations conducted in 2017. We determined that at least one of the candidates should have significant banking experience and that at least one of the candidates should have significant corporate governance and listed company experience, in addition to the other skills identified. The search culminated in the appointment of Baroness Lucy Neville-Rolfe and Paul Myers on 28 November 2018. In the intervening period Ann Berresford was appointed to the Risk Committee with effect from 25 July 2018 and Sir Henry Angest and Andrew Salmon resigned as Directors on 8 August 2018.

Following the appointment of Baroness Lucy Neville-Rolfe and Paul Myers in November 2018 and having regard to the effectiveness evaluations conducted by the Board and its Committees in September and October 2018, we recommended that Lucy be appointed to the Nomination and Audit Committees and that Paul be appointed to the Nomination and Risk Committees. Noting the changes in the 2018 Code, we also recommended that I should step down from my role as a member of the Audit Committee and Paul Lynam from his role as a member of the Risk Committee. The Board accepted all these recommendations at its meeting of 30 January 2019 and the changes were made with immediate effect.

Both Lucy and Paul have received thorough inductions into their respective roles and have had the opportunity to meet senior members of the leadership team and other employees. Their induction will continue throughout the first half of 2019 and it is expected to have been completed by the AGM in May 2019.

The Board underwent a questionnaire based performance evaluation in September and October 2018 which was conducted by the Company Secretary under my direction. In addition I have conducted individual evaluations with each of the Non-Executive Directors; and Paul Marrow, as Senior Independent Director, has undertaken an evaluation of me as Chairman, seeking feedback from both the Executive and Non-Executive Directors.

The outcomes of those various evaluations are consistent with a Board evolving and adapting to a new dynamic in terms of personnel and being listed on the Main Market. I am pleased to report, however, that the Board has concluded it is both performing well and is effective. Further information on the evaluations can be found on page 78, together with information on the activities of the Committee throughout 2018.

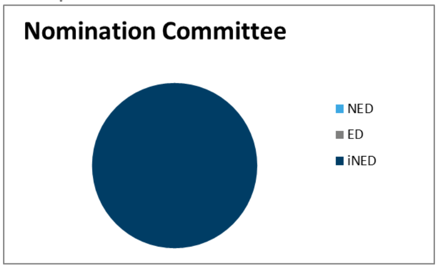
Lord Forsyth, Chairman of the Nomination Committee

Corporate governance report

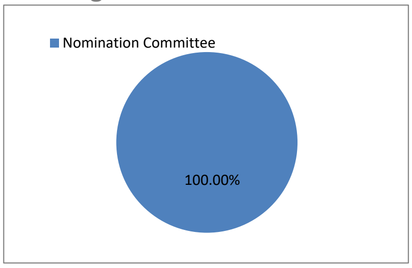
Nomination Committee report

Nomination Committee membership and meetings

Composition

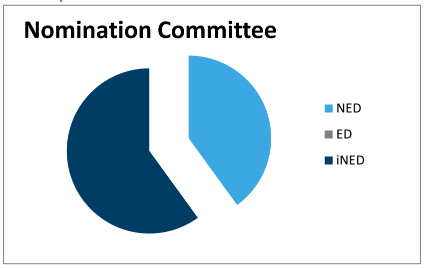


Meeting attendance

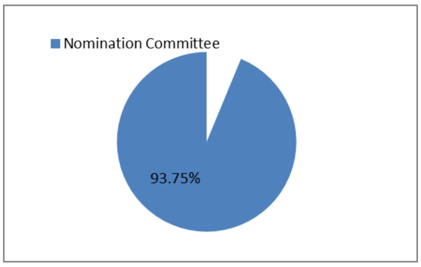


Metrics for 2017:

Composition



Meeting attendance



As at 31 December 2018 the Nomination Committee was composed of four members and was compliant with the Code provision regarding the composition of the Nomination Committee throughout 2018. The Chairman of the Committee is Lord Forsyth.

The Nomination Committee meets as frequently as its chairman may require and also at regular intervals to deal with routine matters and in any event not less than twice in each financial year. The Committee held four scheduled meetings during 2018 and one ad hoc meeting. The attending Directors are shown in the table below:

	Nomination Committee
Number of meetings during 2018	4
Lord Forsyth	4/4
Ann Berresford	4/4
Paul Marrow	3/4
Victoria Stewart[1]	3/3
Former Directors	3
Sir Henry Angest	2/3
Andrew Salmon	3/3

[1] Victoria Stewart attended the February Nomination Committee meeting and was appointed as a member of the Committee at the Board meeting following the conclusion of the Board meeting.

The Company Secretary or the Deputy Secretary acts as Secretary to the Nomination Committee. Other individuals attend at the request of the Nomination Committee Chairman when appropriate and during the year the Chief Executive Officer and the Chief Financial Officer attended meetings.

Corporate governance report

Nomination Committee report

The Chairman of the Nomination Committee reports to the Board on the outcome of Committee meetings and any recommendations made by the Committee.

Role and activities of the Nomination Committee

The Nomination Committee assists the Board in discharging its responsibilities relating to the structure, size and composition of the Board. The Nomination Committee is responsible for, amongst other matters, evaluating the balance of skills, knowledge, independence, experience and diversity of the Board, and makes recommendations to the Board on such matters. The Nomination Committee also considers succession planning, both for the Executive and Non-Executive Directors, taking into account the skills and expertise that will be needed on the Board in the future.

Board effectiveness and Non-Executive Director evaluation

During 2018 the Board conducted an internally facilitated review of the effectiveness of the Board, its Committees and individual Directors using a combination of questionnaires and face-to-face meetings. The Committee reviewed the results of the effectiveness reviews and the individual Director's performance evaluations when assessing the composition of the Board Committees and the contribution made by the individual Directors. The Committee noted that the conclusion to the Board effectiveness review was that the Board was performing well and exercising the right level of judgement with due regard to the duties placed on Directors under company law.

As with all Boards that have undergone change, there were areas for improvement. The 2017 effectiveness review highlighted that there could be improvement in the quality of information coming to the Board and its Committees; and that this would assist the Board in moving towards an enhanced view on forward looking strategic direction rather than backward facing historic performance. As a consequence the Executive Directors enhanced the information provided to the Board at the strategy sessions leading up to and at the Strategy Away Day held in September and this assisted the Board in their deliberations. The Board will continue to monitor this area and make suggestions for improvement over time.

The 2018 Board effectiveness review highlighted that the process for reviewing potential strategic acquisitions could be streamlined and improved. Steps have been taken to improve the process.

The Committee also noted that the Directors had been mindful of the provisions of the Code and their responsibilities as Directors and, where applicable, as senior managers under the Senior Managers Regime when reaching their assessment of Board effectiveness and individual Director contributions.

The Committee reviewed the independence of each Non-Executive Director. The Committee, following a rigorous review and evaluation, considers Paul Marrow to be independent in both character and judgement, and his judgement unaffected by his appointments at other companies. The Board, upon the recommendation of the Committee, is satisfied that each of the other Non-Executive Directors is independent within the meaning of the Code and that Lord Forsyth, on his appointment as Chairman, met the independence criteria set out in the Code. As a smaller company within the meaning of the Code, the Company is required to have at least two independent Non-Executive Directors.

Following the resignation of Sir Henry Angest and Andrew Salmon in August 2018 and the appointment of Baroness Neville-Rolfe and Paul Myers in November 2018, the Committee recommended to the Board that the composition of the Audit and Risk Committees could be strengthened and recommended that Lucy and Paul be appointed to the Audit and Risk Committees respectively. Following their appointment, the Nomination Committee concluded that the composition of each Committee was appropriate, with each Committee having the right balance of skills and experience. Further information on the individual Director's experience can be found on pages 64 to 68. The Committee contemplates conducting a further internally facilitated review of the effectiveness of the Board, its Committees and individual Directors during 2019.

Board training and development

The Board receives detailed reports from executive management on the performance of the Group at its meetings. Updates are provided on relevant legal, corporate governance and financial reporting developments.

In addition, the Board, upon the recommendation of the Committee, adopted a training programme during 2018 and received formal training from both internal and external experts on diverse topics ranging from Cyber attacks and security awareness, the economic outlook for 2019 and beyond, IFRS 9 Model Governance and assumptions, Senior Managers Regime responsibilities and threats and opportunities from FINtech.

Directors are also encouraged to attend external seminars on areas of relevance to their role and to keep a record of their external training.

A training plan for 2019 has been developed with a focus both on strategic and governance matters.

Succession Planning

The Nomination Committee has considered the Company's succession plans and focused on Board (executive and non-executive) and senior manager succession. Consideration has been given to potential internal candidates, short term solutions in the event of unanticipated changes in circumstances and external recruitment as well as re-allocating responsibilities on a short term or longer basis. The need for regulatory approval of the persons performing Senior Manager functions under the Senior Managers Regime has also been taken into account.

The Nomination Committee also reviewed the Board policy on diversity, including gender. The policy is described on page 73.

A full copy of the terms of reference for the Nomination Committee can be obtained by request to the Company Secretary or via the Group's website at www.securetrustbank.com.

Corporate governance report

Statement by the Chairman of the Audit Committee

I am pleased to present the report of the Audit Committee for the financial year ended 31 December 2018, my first full year as the Committee Chairman. 2018 has been an active year for the Audit Committee. As well as routine 'business as usual items', we have monitored the transition to IFRS 9 and overseen a change in the external auditor.

The transition to IFRS 9 was a key matter for the Committee and received significant focus in both 2017 and 2018. With the close of the 2017 audit, discussed by the Committee at the February and March 2018 meetings, we shifted our focus to the review and evaluation of the judgements made in determining the starting IFRS 9 position and in evaluating the model outputs once reporting of results under the new standard had commenced. I am pleased to say that the reviews of model outputs and associated assumptions over the course of 2018 have validated the initial model choices and judgements made. The Committee did not have to revisit the substantive decisions made when presented with actual reported results in the monthly MI reports, with any adjustments to assumptions made being minor.

To assist with our oversight of IFRS 9, the Committee and the wider Board received training on specific aspects of the IFRS 9 model assumptions including the macro economic scenarios used in the model and their effect on the Group's ICAAP and ILAAP models. The Risk Committee has oversight of these areas via the Model Governance Committee and the Assumptions Committee, and more detail can be found on the Group's website: www.securetrustbank.com/our-corporate-information/risk-management.

I have also met regularly with the external audit partner. The 2018 financial year was the first year of Deloitte LLP's engagement as external auditor and they observed the 2017 audit close conducted by KPMG LLP. The transition from KPMG to Deloitte went smoothly and I wish to thank KPMG, Deloitte and the Finance team on behalf of the Committee for managing this process so seamlessly. The cooperation between all parties was germane when the Company issued Fixed Rate loan notes in July 2018, with Deloitte and KPMG each providing support in different areas, as needed to be the case in this transitional year. Deloitte reviewed the 2018 Interim Financial statements and carried out the 2018 year-end audit. The Committee will be carrying out a formal assessment of the effectiveness of the external audit process in Q2 2019 and based upon progress to date we have recommended to the Board the reappointment of Deloitte as auditors for 2019 at the 2019 AGM.

The transition to Deloitte presented the Finance team with an opportunity to reassess and align their focus and processes with the new audit team. Those changes also presented the Committee with an opportunity to review the structure, format and timing of the Committee meetings and to reflect on our focus in 2018 and also 2019 and beyond. We intend to meet four times in 2019, having changed the standing agenda and meeting schedule accordingly.

I met with the Chief Internal Auditor every month to discuss past and planned internal audit activity and I have also met regularly with the Chief Risk Officer. Internal audit activity continues to address all categories of risk across the business. The Committee has agreed with the internal audit function that particular areas of focus in 2019 will include the motor transformation change programme and operational resilience.

Lord Forsyth stepped down from the Committee with effect from 30 January 2019 and we welcomed Baroness Neville-Rolfe to the Committee on the same date. I would like to thank Michael, on behalf of the Committee and myself, for his sage counsel during his tenure as a member of the Committee.

Further information on the activities of the Audit Committee is provided in the following report and I will be available at the AGM to answer any questions about our work.

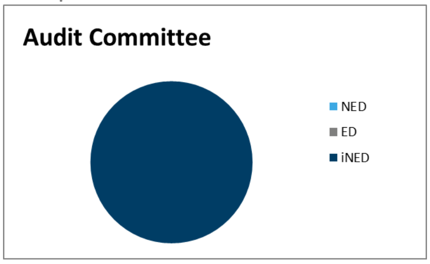
Ann Berresford, Chairman of the Audit Committee

Corporate governance report

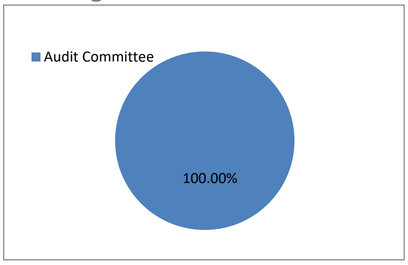
Audit Committee report

Audit Committee membership and meetings

Composition

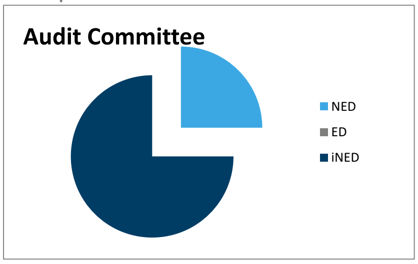


Meeting attendance

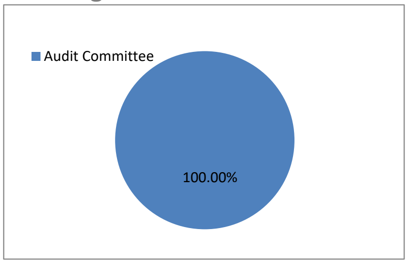


Metrics for 2017:

Composition



Meeting attendance



As at 31 December 2018 the Audit Committee was composed of three members with Ann Berresford as the Chairman of the Committee. Ann is considered by the Board to have recent and relevant financial experience and the Audit Committee as a whole has competence relevant to the sector in which the Group operates.

The Code provides that for smaller companies, such as the Company, the Board should establish an Audit Committee of at least two independent Non-Executive Directors. In addition, the Chairman of the Company may be a member of, but not chair, the Committee if he was considered independent on appointment as Chairman. The Company complied with this provision throughout 2018. As set out on page 80 Lord Forsyth retired from the Committee on 30 January 2019 and Baroness Neville-Rolfe joined the Committee with effect from the same date.

The Audit Committee meets formally at least four times a year and otherwise as required. The number of planned meetings held during 2018 and the attending members are shown in the table below:

	Audit Committee
Number of meetings during 2018	6
Ann Berresford	6/6
Lord Forsyth	6/6
Paul Marrow	6/6
Former Directors	2
Andrew Salmon	2/2

Corporate governance report

Audit Committee report

The Company Secretary or the Deputy Company Secretary acts as Secretary to the Audit Committee. Other individuals attend at the request of the Audit Committee Chairman and during the year the external auditor lead partner, Chief Executive Officer, Chief Financial Officer and Chief Internal Auditor and a number of senior members of the Finance department attended meetings to report to the Audit Committee. The Chairman of the Audit Committee reports to the Board on the outcome of Committee meetings and any recommendations arising from the Committee.

Role of the Audit Committee

The Audit Committee assists the Board in, amongst other matters, discharging its responsibilities with regard to regulatory reporting, financial reporting, including reviewing the Company's annual financial statements, reviewing and monitoring the extent of the non-audit work undertaken by external auditors, advising on the appointment, reappointment, removal and independence of external auditors and reviewing the effectiveness of the Company's internal audit activities, internal controls and risk management systems. The ultimate responsibility for reviewing and approving the Annual Report and Accounts and the half-yearly report remains with the Board. The Board ensures the Annual Report, taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position, performance, business model and strategy. The Audit Committee assists the Board in reaching those conclusions, including an assessment that the narrative reporting in the front of the Annual Report accurately reflects the financial statements in the back.

A full copy of the terms of reference for the Audit Committee can be obtained by request to the Company Secretary or via the Group's website at www.securetrustbank.com/ investor-information.

Matters discussed at Audit Committee meetings since 1 January 2018

The Audit Committee has a schedule of meetings with standing agenda items. Meetings are planned to coincide with key dates in the Group's financial reporting cycle, enabling the Committee to deal with matters on a timely basis over the course of the year. In addition to standing agenda items the Committee also deals with other matters as they arise including, in 2018, assumptions used in the IFRS 9 model and other matters relating to IFRS 9, the application of IFRS 16 and the transition of auditor.

The Audit Committee reviewed and approved its Terms of Reference, the schedule of standing agenda items, the Internal Audit Charter and the engagement contract with the external auditors. Other principal matters considered are set out below.

Financial reporting

The Audit Committee has reviewed the following matters in connection with the annual and interim financial statements and considers that the Company has adopted appropriate accounting policies and made appropriate estimates and judgements:

Corporate governance report

Audit Committee report

Subject area	Matters considered
Accounting policies, key judgements and assumptions used in preparing interim and annual financial statements	The Audit Committee reviewed the key accounting judgements made by management in preparing the financial statements for the year ended 31 December 2018, the interim financial statements for the six months ended 30 June 2018, and the press releases and investor presentations that were prepared when the financial statements were released. In particular the Committee considered at its meeting in February 2018 a paper on the key accounting judgements relating to the 2017 annual report and accounts. These included effective interest rate accounting, impairments and expected value of share option schemes. In relation to impairment provisions the Committee considered the adequacy of provision cover, including the emergence period for different products, factors relevant to the loss given default assumptions used for Consumer Finance products and the level of overlay to the modelled impairment provision to reflect increased uncertainty in the UK economy and the remaining sub prime motor book. At this meeting, the Committee approved the Group's accounting policy in respect of IFRS 9, which became effective from 1 January 2018. The Committee considered key accounting judgements in respect of the 2018 Interim Report at its meeting in July 2018. In particular, it considered the transition to IFRS 9 and the impact of the standard on the balance sheet as at 1 January 2018. The provision charge for the period to 30 June 2018 was also compared to the equivalent charge calculated on the basis of the previous relevant standard, IAS 39. The Committee reviewed and challenged key assumptions used in the calculation of provisions under IFRS 9, including in respect of the improvement in probability of default noted over the first half of the year and the loss given default in respect of Consumer Finance products. In its meeting in November 2018, the Committee considered the key judgements and assumptions that were expected to be applied in respect of the 2018 Annual Report and Accounts. This focused on an update to the assumptions used in the IFRS 9 provision modelling, including the use of forward looking macroeconomic scenarios and the probability weightings applied to these scenarios. A Board training session was held in respect of macroeconomic scenarios, including those used for IFRS 9 and the Group's ICAAP and ILAAP. The Committee considered updates to these judgements and assumptions at its meeting in March 2019. In making its recommendations to the Board to approve the annual and interim financial statements the Committee has taken into account matters raised by the external auditor on matters of judgment and disclosures in relation to non-recurring or sensitive items.
Use of the going concern basis in preparing the financial statements and long term viability of the Group	The financial statements are prepared on the basis that the Group and Company are each a going concern. The Audit Committee has reviewed management's explanations as to the appropriateness of the going concern basis in preparing the Group and Company financial statements. The financial statements for 2018 also include statements that provide shareholders with the Board's views on the long term viability of the Group. The Audit Committee has reviewed and challenged the basis for assessing long term viability, including the period by reference to which viability is assessed, the principal risks to long term viability and actions taken or planned to manage those risks.
Presentation of a 'fair, balanced and understandable' Annual Report and Accounts	The Audit Committee, having reviewed the content of the Annual Report and considering relevant matters including the presentation of material sensitive items, the representation of significant issues, the consistency of the narrative disclosures in the 'front half' with the financial statements, the overall structure of the Annual Report and the steps taken to ensure the completeness and accuracy of the matters included, has advised the Board that the 2018 Annual Report and Accounts include a 'fair, balanced and understandable' assessment of the Group and Company's businesses.

The potential impact of future accounting changes	The Committee has considered changes to financial reporting requirements that were not yet effective as at 31 December 2018 but that are likely to impact the reported results or financial position of the Group in the future. In its November meeting a paper setting out the impact of IFRS 16 "Leases", which became effective from 1 January 2019, was reviewed. Having considered the expected impact of the standard on the Group's financial position and results, the Committee approved a number of decisions in respect of the transition to this standard. These are disclosed in Note 1.3.

The table above is not a complete list of matters considered by the Committee but highlights the most significant matters for the period in the opinion of the Audit Committee.

External audit

In last year's Annual Report the external audit tender which resulted in Deloitte LLP being appointed as statutory auditor for the year ended 31 December 2018 was described. The 2018 audit was the first audit completed by Deloitte.

The Committee reviewed and approved the external audit terms of engagement, the scope of the external audit, timetable, materiality, audit strategy and fees. The Committee maintains a close dialogue with the external auditor and meets with them without management at every Committee meeting.

The Audit Committee reviews written reports prepared by the external auditors setting out their audit approach and conclusions on matters of judgment impacting the financial statements, disclosures in relation to non-recurring or sensitive items, any internal control findings identified during the course of the external audit and their independence.

The Audit Committee has monitored Deloitte in their approach to their first audit of the Group and has considered the effectiveness of the work of the external auditors, the quality of the team, the scope of the work and communications and fees following the completion of the Interim Review. The Committee also met with management, including without Deloitte present, to hear their views on the effectiveness of the external auditors. The Committee will conduct a formal assessment of the first audit completed by Deloitte during 2019 and has so far informally concluded that the external auditors are performing well.

The Audit Committee was satisfied that the level of audit fees payable in respect of the audit services provided, being £270,000 (KPMG LLP 2017: £338,000) was appropriate and that an effective audit could be conducted for such a fee. The existing authority for the Audit Committee to determine the current remuneration of the external auditors is derived from shareholder approval granted at the AGM held in May 2018.

Independence of the external auditor

Deloitte has also confirmed to the Audit Committee that it has policies and procedures in place to satisfy the required standards of objectivity, independence and integrity and that these comply with the Auditing Practices Board's Ethical Standards for Auditors.

The Group has agreed a policy on the provision of non-audit services by its external auditor. The policy ensures that the engagement of the external auditor for such services requires pre-approval by appropriate levels of management or the Audit Committee and does not impair the independence of the external auditor, and that such engagements are reported to the Audit Committee on a regular basis. The external auditor will only be selected for such services when they are best suited to undertake the work and there is no conflict of interest.

Corporate governance report

Audit Committee report

The provision of any non-audit services provided by the external auditors requires prior approval, as set out in the table below.

	Approval required
Services not previously pre-approved regardless of fee	Audit Committee
Any engagement > £100,000	Audit Committee
Pre-approved services < £100,000	CEO or CFO

The total of audit and non-audit fees paid to Deloitte during the period is set out in Note 5 on page 161. The non-audit services fee of £235,000 (KPMG LLP 2017: £101,000) was in respect of, but not limited to, the review of the half-year accounts and work relating to the raising of subordinated debt and other ad hoc advice. In the case of each engagement, management considered it appropriate to engage Deloitte for the work because of their existing knowledge and experience or the organisation.

The Audit Committee has also considered matters that might impair the independence of the external auditor, including the non-audit fees paid to the external auditor, and has confirmed that it was satisfied as to the independence of the external audit firm Deloitte. Matthew Perkins is the audit partner from Deloitte and can continue in this role until the completion of the 2022 audit at the latest.

Internal audit

The Group has an independent Internal Audit function led by the Chief Internal Auditor. The Chief Internal Auditor reports to the Chairman of the Audit Committee and they meet each month.

The Audit Committee reviewed and approved the internal audit plan for the year and monitored the activity of the Internal Audit function throughout the year. It also:

- Reviewed other matters which are not currently contemplated in the audit plan but which may be appropriate for inclusion in the future.
- Considered the risk and control matters identified in internal audit reports issued since the previous meeting along with management's responses to those points and progress in taking action to resolve control weaknesses.
- Approved the Internal Audit budget and resource plan for the year.
- Reviewed and approved the Internal Audit Charter.
- Reviewed the annual assessment of the overall effectiveness of the governance and risk and control framework provided by the Internal Audit function.
- Reviewed Internal Audit's conclusions on staff behaviours in the context to the Group's framework of values and culture.

In addition the Audit Committee assesses the effectiveness and independence of the Internal Audit Function each year. In 2016 it commissioned an independent external party to carry out a full external effectiveness review which highlighted a number of particular strengths as well as some areas for further enhancement. During 2018 the Committee reviewed the performance of the Internal Audit function taking into account an updated assessment carried out by the Chief Internal Auditor and the progress made addressing areas for enhancement identified in the 2016 review, and was satisfied as to the effectiveness and independence of the Internal Audit function. The next external effectiveness review is scheduled for 2021.

The Committee was satisfied that Internal Audit has the appropriate resources to deliver the 2018 and 2019 internal audit plan. In addition to the internal resource it is also able to draw on a panel of external subject matter experts.

Corporate governance report

Audit Committee report

Internal controls and risk management

The Audit Committee monitors the effectiveness of the Group's governance, risk and control framework. A statement approved by the Committee regarding the operation of the risk and control framework is set out on page 74.

During 2018 the Committee reviewed the procedures for detecting fraud affecting financial reporting.

Whistleblowing

The Audit Committee has reviewed the effectiveness of whistleblowing arrangements in place within the Group and adherence to the Financial Conduct Authority Rules on Whistleblowing. During the year the Committee received a report on a review and test of the Whistleblowing framework, which included the results of mandatory training provided for staff and the provision of a confidential hotline by an external third party.

The Chairman of the Risk Committee is the Whistleblowers' Champion for the Group and the Risk Committee received a report each quarter on the operation of the Whistleblowing arrangements.

In compliance with the 2018 Code, the reporting on effectiveness of whistleblowing arrangements in place within the Group and adherence to the Financial Conduct Authority Rules on Whistleblowing will move to the Board for 2019, forming part of the wider reporting of concerns raised by the workforce.

Audit Committee effectiveness

During the year the Committee considered and evaluated its performance. It did this by means of a questionnaire which members of the Committee completed and by taking soundings from other attendees, including the external auditor. The Chairman of the Committee then collected the responses and produced a report to the Committee. The result of the evaluation was that the Committee considered that it was performing effectively.

Corporate governance report

Statement by the Chairman of the Risk Committee

I am pleased to present the report of the Risk Committee for the financial year ended 31 December 2018. The Group has had separate Audit and Risk Committees since 2011 and both Committees have overseen the development and evolution of the risk management and internal control frameworks during that period and to date.

Management of risk is a key part of what the Group does. As a Committee, we have been involved both with assessing the principal risks that impact the Group at a macro-economic and strategic level; and also in assessing risk at a business level when the Group seeks to develop new business opportunities or products. We had significant focus on our ICAAP for 2018 in the first half of the year, reviewing our model outputs and assumptions and how we have calculated the various elements of our capital requirements given changes in regulation and guidance. We also reviewed the positive progress made with the quality and effectiveness of the Group's Operational Risk Framework and following discussion, we recommended to the Board that the Group should move from the Basic Indicator Approach to The Standardised Approach for determining our Operational Risk Capital. The PRA have approved this.

Operational resilience, including cyber and data security has become a standing agenda item for the Committee as the Group seeks to mitigate the risk in this area, both by reviewing current preventative measures and by reviewing plans for enhancements in 2019/2020. As well as receiving updates from the Committee, the Board participated in a specific cyber security training session in 2018, noting both the risks and opportunities this area brings to the Group. During the year we also reviewed significant changes to our now separate Recovery Plan as required under the new regulation. Assumptions in both our Recovery Plan and Resolution Plan were also reviewed for correlation with our ICAAP and ILAAP documents, ensuring that the scenarios aligned both for the modelled 'event' and the expected outcome. The Committee is also overviewing on behalf of the Board the implementation and progress of the motor transformation programme.

We have also considered the risks and opportunities arising from Brexit and the actions the Group may choose to take, noting the limited direct impact Brexit will have on a largely UK focused business. We have also modelled likely scenarios and will continue to monitor the risk to the Group once more detail is known. More detail can be found on page 49.

The Risk and Compliance teams continue to meet the challenge of developing regulation and have provided the Committee with effective oversight of the risk landscape within the Group. We have also considered regulatory updates through regular reporting which includes the outputs of the Compliance monitoring programme and emerging regulatory requirements.

The membership of the Committee has also changed, and I would like to thank Andrew Salmon and Paul Lynam for their contributions during their tenure and to welcome Ann Berresford and Paul Myers to the Committee, the latter joining the Committee on 30 January 2019.

Further information on the activities of the Committee during the year is provided in the following report and further information about risk related matters can be found in the sections of the report and accounts on pages 40 to 51.

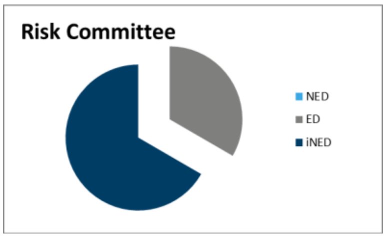
Paul Marrow
Chairman of the Risk Committee

Corporate governance report

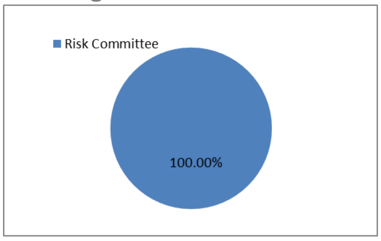
Risk Committee report

Risk Committee membership and meetings

Composition

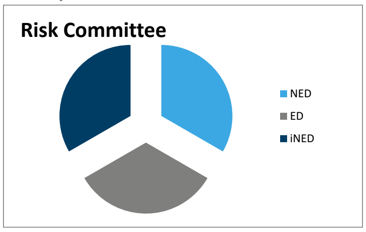


Meeting attendance

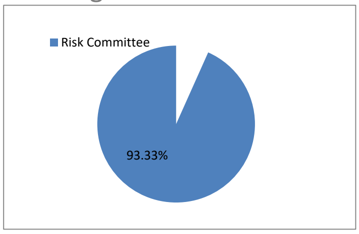


Metrics for 2017:

Composition



Meeting attendance



The Risk Committee is composed of three members and Paul Marrow is the Chairman of the Committee. As set out on page 87 Paul Lynam retired from the Committee on 30 January 2019 and Paul Myers joined the Committee on the same date.

The Risk Committee meets formally at least four times a year and otherwise as required. The number of planned meetings held during 2018 and the attending Directors are shown in the table below:

	Risk Committee
Number of meetings during 2018	5
Paul Marrow	5/5
Ann Berresford	3/3
Paul Lynam	5/5
Former Directors	3
Andrew Salmon	3/3

The Company Secretary or the Deputy Company Secretary acts as Secretary to the Risk Committee. Other individuals attend at the request of the Risk Committee Chairman and during the year the Chief Risk Officer, Chief Internal Auditor, Chief Compliance Officer, Group Head of Operational Risk, Chief Information Security Officer and other senior managers attended meetings to report to the Committee.

The Chairman of the Risk Committee reports to the Board on the outcome of Committee meetings and any recommendations arising from the Committee.

Corporate governance report

Risk Committee report

Role of the Risk Committee

The Risk Committee reviews the design and implementation of risk management policies and risk related strategies and the procedures for monitoring the adequacy and effectiveness of this process; considers the Group's risk appetite in relation to the current and future strategy of the Group; oversees the Group's ICAAP and ILAAP and outputs from these; and exercises oversight of the risk exposures of the Group.

The Committee exercises its internal control and risk management role through the reports it receives from the ALCO, the Chief Risk Officer, the Chief Internal Auditor, the Chief Executive Officer, the Chief Financial Officer and other members of management and its engagement with executive management, internal and external auditors and consultants.

Other matters within the remit of the Committee are the risk profile of the Group, risk appetite, frameworks and limits, the risk management operating model, the technology infrastructure supporting the risk management framework, operational risk and regulatory and compliance matters.

Matters discussed at Risk Committee meetings since 1 January 2018

The Risk Committee has a schedule of meetings with standing agenda items so that all relevant matters are dealt with over the course of the year. In addition to standing agenda items the Committee also deals with other matters that arise during the year. In 2018 this included, for example, increasing the focus on cyber security, a review and oversight of a related party transaction, key regulatory developments such as the PRA/FCA Discussion Paper on Operational Resilience and the oversight of the risks arising from the implementation and execution of the motor transformation programme.

During the year the Risk Committee reviewed its Terms of Reference and approved the schedule of standing agenda items, the Compliance monitoring plan for 2019, the business continuity plan and the operational risk management policy.

The principal matters discussed during the year and up to the date of this report were as follows:

Subject area	Matters considered
Group risk appetite statement and key risk indicators	The Group's key risk appetite metrics, which are reviewed and approved on an annual basis. The Committee reviews exceptions to the last quarter's performance by reference to the key risk indicator metrics provided to each meeting.
Strategic risks	Strategic risks (those arising from the internal environment and the external environment that could have an effect on management's ability to deliver on the Group strategic plan) are discussed and challenged on an annual basis.
Credit risk	Credit risk performance for all businesses and 'deep dive' reviews on status and plans for individual account balances or portfolios that warrant specific focus. The Committee has a mandate to approve some Group-wide mandates and policies including single counterparty limits and credit risk policies set for individual business areas.

Risk Committee report

Operational Risk/Resilience risk, including Cyber resilience risk	Oversight of the operational risk policy including metrics and KPI reporting and business unit management risk and control self-assessment. Complaints data, governance, including review of the Group Governance Manual. Oversight of the business continuity plan and other operational resilience reporting/KPIs. Oversight of the biannual Operational Risk and Control Assessments. The strategies undertaken within the Group to understand, identify, monitor and respond to cyber threats including the current state and planned activity.
Capital and Liquidity risk	The Committee has primary responsibility for reviewing and making a recommendation to the Board on the Bank's ICAAP and ILAAP and the Resolution and Recovery Plans. Specific matters such as the Pillar 2A capital requirement and the results of stress testing were reviewed and debated.
Regulatory and conduct risk	The Committee receives regular reports on the key risk indicators for regulatory, reputational and conduct risk. The Committee reviews the regulatory risk assessment on an annual basis and approves the annual compliance monitoring programme.
Whistleblowing	The Chair of the Committee has the role of Whistleblowers' Champion. The Committee has validated through oversight and regular reporting that the arrangements for whistleblowing remain effective.

Regulatory, Compliance and Conduct Risk Monitoring

The Committee oversees the management of regulatory risk for the Group. The Chief Compliance Officer presents an Annual Compliance Report to the Committee and responds to any challenge from the Committee on the effectiveness of the Compliance function.

The Committee receives regular reports on key risk indicators for regulatory, reputational and conduct risk, regulatory incidents and key advisory activity of note, horizon scanning and actions to implement new and revised regulations or legislation, and the outputs of the compliance monitoring programme. The Committee reviews the Regulatory Risk Assessment on an annual basis, and approves the annual compliance monitoring programme.

In addition, the Committee receives a detailed review of financial crime focussed on Anti-Money Laundering in the Money Laundering Reporting Officer's ('MLRO') Annual Report, which is then presented to the Board.

The Group has an externally managed whistleblowing 'hotline' and quarterly reports are provided to the Committee and the Whistleblowers' Champion; tests have been completed validating the adequacy of the framework, service provider and internal procedures.

During 2018, regulatory changes have included the implementation of the new prescribed responsibility for Conduct Rules and of the enhanced requirements of the Insurance Distribution Directive; improvements to the management information provided to the Committee in response to the PRA's 'Dear Chair' letter which highlighted areas of improvement in Consumer Credit lending; planning for the extension of the Senior Managers and Certification Regime to the regulated subsidiaries (Debt Managers (Services) Ltd, V12 Retail Finance Ltd and STB Leasing Ltd); the major project for the General Data Protection Regulation implementation, which required changes to the management of personal data across the Group; implementation of the FCA's revised Creditworthiness and Affordability rules; and implementation of the Payment Services Directive II.

Conduct risk and culture remain a key focus within the Group and are managed through the Customer Focus Committee which reports to the Board through the Executive Committee.

Risk Committee report

Strategic and Operational Risk

The Committee oversees the management of strategic and operational risk across the Group. The Group Head of Operational Risk presents annually an Operational Risk Management Policy to the Committee and responds to any challenge from the Committee on the effectiveness of risk management and risk governance throughout the Group.

To assist in understanding how the risk framework has embedded within the Group and to challenge the effectiveness of the risk management function, the Committee receives a quarterly review of material operational risk events/losses, performance against the key Operational Risk Appetite Metrics, together with the key findings from bi-annual Risk and Control Self Assessments. This will include a key focus on the effectiveness of the Operational Resilience control framework and plan.

The Committee conducts an annual review of the Group risk appetite statement and the supporting metrics and recommends the Group risk appetite statement to the Board for approval.

In assessing strategic risk the Committee has regard to the identified strategic risks, which the Committee reviews annually. In assessing strategic risks, the Committee has due regard to the existing process and internal controls in operation and reviews the recommendations from the Risk and Compliance functions on how to adapt the controls to mitigate those risks.

Credit Risk

The Committee receives reports on key risk indicators for credit risk, together with quarterly assessments of each portfolio's credit profile including impairments, bad debts, watch-lists, and any policy exceptions. These assessments are underpinned by the associated credit risk policies which, together with the Responsible Lending policy, set out the credit risk framework which is reviewed by the Committee at least annually.

Risk Committee effectiveness

During the year the Committee considered and evaluated its own performance. It did this by means of a questionnaire which members of the Committee completed. The Chairman of the Committee then collected the responses and produced a report to the Committee. The result of the evaluation was that the Committee considered that it was performing effectively.

A full copy of the terms of reference for the Risk Committee can be obtained by request to the Company Secretary or via the Group's website at www.securetrustbank.com.

Corporate governance report

Statement by the Chairman of the Remuneration Committee

On behalf of the Committee I am pleased to present the Remuneration Committee report, including the Directors' Remuneration Report, for the 2018 financial year. This has been a busy year for the Committee in which we have strengthened our oversight of remuneration practice across the Group in a number of areas and in particular:

- **Employee Remuneration:** Our focus for the majority of 2018 has been on reviewing, and assisting in the production and implementation of, the All Employee Remuneration Policy ('Policy') and in the governance and oversight of the processes which underpin employee remuneration. The implementation of the Policy will lead to a standardised approach to remuneration for employees across the Group throughout 2019 and complements the role grading structure implemented in September 2018, which provides staff with clarity for their future career path. We will continue to monitor these structures throughout 2019 and intend to review these later in the year.
- **Material Risk Takers:** As part of the Policy approval process we took the opportunity to review the methodology used to determine and identify Material Risk Takers ("MRTs") and to strengthen our processes and remuneration practices regarding this cohort. For 2019 and onwards staff identified as MRTs will be subject to malus, clawback and bonus deferral rules.
- **Review of Executive Remuneration:** The Committee has reviewed its role in the oversight and decision making processes concerning the Executive Directors, Senior Management and MRTs and has strengthened the information we receive and review in relation to these individuals. Executive Remuneration outcomes are detailed below.
- **Planning for 2019 and 2020:** The Committee will be required to seek shareholder approval for the Directors' Remuneration Policy at the AGM in 2020. We identified that the Committee would require assistance, in updating the current policy, from a Remuneration Consultant in H2 2019 and, with the assistance of the Secretary, we conducted a competitive tender to appoint the Executive Compensation practice of Aon plc as advisors to the Committee. We have also taken preparatory steps to fulfil our responsibilities under the 2018 Corporate Governance Code in anticipation of having a 'deep dive' on workforce matters, and other elements of the Code which impact Directors' Remuneration Policy, during 2019.

Performance and variable pay outcomes for the year ended 31 December 2018

For the financial year ended 31 December 2018, Executive Directors were eligible for an annual bonus award of up to 100% of salary, subject to stretching performance metrics based on a balanced business scorecard of financial, risk, strategic, customer, operational and staff metrics. 60% of the bonus was subject to financial and risk performance metrics and 40% of the bonus was subject to a mixture of strategic, customer, operational and staff performance metrics.

The Board agreed the 2018 financial year budget at its meeting in December 2017, which included targets relating to the Financial KPIs set out in the Strategic Report on page 18. The performance objectives set for the Executive Directors for the 2018 financial year reflected elements of those KPIs. Additional strategic targets were set, specifically relating to the non-financial performance metrics, for each of the Executive Directors. Performance against those objectives is set out on page 100.

With this in mind, and taking into account performance in the year against the annual bonus performance metrics, the CFO will receive a bonus of £300,694 equivalent to 73.34% of his maximum opportunity. The CEO will receive a bonus of £600,000 equivalent to 50% of his maximum opportunity which is lower than the outcome he would have achieved applying a formulaic calculation. The Remuneration Committee, in agreement with the CEO, has reduced the total amount to be paid to the equivalent of an 'on-target' assessment. Further details are set out on page 99.

Statement by the Chairman of the Remuneration Committee

There were no share-based performance plans which were eligible to vest in respect of the financial year ended 31 December 2018.

As a Committee, we are satisfied that the variable remuneration for the 2018 financial year for each of the Executive Directors is in line with business performance.

Executive remuneration arrangements for 2019

Further detail on the intended operation of the Remuneration Policy in 2019 is set out on page 107.

In outline:

- It is proposed that the CEO will not receive a salary increase in 2019 (2018: nil), for the third consecutive year.
- It is proposed that the CFO's salary will increase by 3.66% (2018: 2.5%) to £425,000, broadly in line with the staff salary increases across the Group.
- The maximum annual bonus opportunity for the year ending 31 December 2019 will be equal to 100% of salary. The bonus will be subject to stretching performance metrics based on a balanced business scorecard of financial, risk, strategic, customer, operational and staff metrics. Up to an additional 100% of salary may be awarded under the annual bonus in exceptional circumstances (such as in order to recognise exceptional performance during the year).
- 50% of any bonus earned will be deferred into shares under the Deferred Bonus Plan. Deferred shares will vest in equal tranches after one, two and three years following deferral and will be subject to malus and clawback.
- Long term incentive awards of 50% of salary for the CEO and 61% for the CFO are expected to be granted in 2019, which are substantially below the maximum limit of 100% of salary set out in our approved Directors' Remuneration Policy. Whilst the CFO's award of 61% of salary is 39 percentage points below the maximum permitted under the policy, it is 11 percentage points higher than the 50% awarded last year. This modest increase in the LTIP for the CFO is to marginally improve his total remuneration compared to peers, through long-term variable pay rather than fixed pay.

The above proposals are intended to assist in driving the delivery of our business plan for 2019, and are aligned with shareholders' interests.

We encourage an active interest from our investors in our Remuneration Policy and practices, we welcome dialogue with shareholders on remuneration, and seek to engage regularly with shareholders on this important subject.

As set out in the Chairman's Statement, Sir Henry Angest and Andrew Salmon stepped down from their roles on the Committee on 31 March 2018. I would like to thank Sir Henry and Andrew for their advice and counsel to the Committee during their tenure.

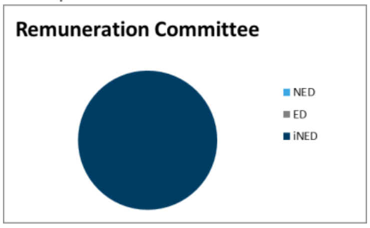
Victoria Stewart
Chairman of the Remuneration Committee

Corporate governance report

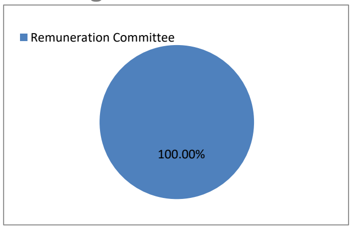
Operation of the Remuneration Committee

Remuneration Committee membership and meetings

Composition

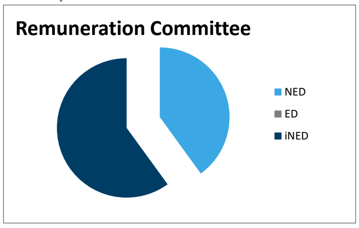


Meeting attendance

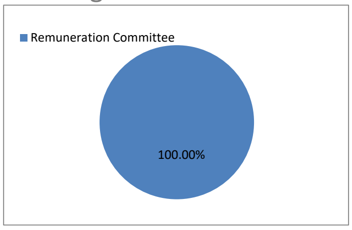


Metrics for 2017:

Composition



Meeting attendance



As at 31 December 2018 the Remuneration Committee was comprised of three members and was compliant with the Code provision regarding the composition of the Remuneration Committee throughout 2018. The Code contemplates that, in relation to the Company, the Board should establish a Remuneration Committee of at least two independent Non-Executive Directors. The Company chairman may also be a member of the Committee where, as is the case with STB, he was considered independent on appointment as chairman.

The Remuneration Committee meets at least twice and ordinarily four times a year and when required to address non-routine matters. The number of planned meetings held during 2018 and the attending Directors are shown in the table below:

	Remuneration Committee
Number of meetings during 2018	4
Victoria Stewart	4/4
Lord Forsyth	4/4
Paul Marrow	4/4
Former Directors	2
Sir Henry Angest	2/2
Andrew Salmon	2/2

The Company Secretary or the Deputy Company Secretary acts as Secretary to the Remuneration Committee. Other individuals attend at the request of the Remuneration Committee Chairman and during the year the Chief Executive Officer, HR Director, Chief Internal Auditor and other senior managers attended meetings to report to the Committee.

The Chairman of the Remuneration Committee reports to the Board on the outcome of Committee meetings and any recommendations arising from the Committee.

Corporate governance report

Operation of the Remuneration Committee

During the year the Committee reviewed and approved its terms of reference. A full copy of the terms of reference of the Remuneration Committee can be obtained by request to the Company Secretary or via the Group's website at www.securetrustbank.com.

Role of the Remuneration Committee

The Remuneration Committee assists the Board in fulfilling its responsibilities in relation to remuneration including, amongst other matters, determining the individual remuneration and benefits package of each of the Executive Directors and the senior management below Board level.

Key Matters considered by the Committee from 1 January 2018 to 31 December 2018.

Item	Comment
Executive Directors bonus arrangements	The Remuneration Committee considered the bonus arrangements in relation to the Executive Directors for 2017 and 2018 in accordance with the Directors' Remuneration Policy and the targets set as part of a balanced business scorecard. In doing so the Remuneration Committee took into account the financial performance of the Group and personal performance. Details of the 2018 bonus earned by Directors during the year can be found on page 92.
Internal Audit reward and incentives governance review	The Committee reviewed the results of the Internal Audit of the reward and incentives governance review and the audit actions arising from that review and will monitor their implementation throughout 2019.
All Employee Group Remuneration Policy (Policy)	The Committee reviewed and approved for recommendation to the Board the All Employee Group Remuneration Policy, having received advice on the Policy from the HR Director, the Risk Committee, the Head of Compliance and the Company Secretary. The Policy was approved by the Board and became effective 1 January 2019.
Material Risk Takers (MRTs)	The Committee reviewed the processes for the classification and identification of MRTs and the remuneration and bonus arrangements for this cohort, with the subsequent strengthening of reporting to the Committee on the review process.
Proposed Grading Structure for 2018	The Committee reviewed the new grading structure within the Group. The structure is backed by a robust analytical job evaluation system, supported by industry based market benchmarking and is intended to provide greater clarity and transparency for staff, allowing individuals to map how their career could develop within the Group. The new structure was implemented in Q3 2018.
Gender Pay Gap Reporting (GPG)	The Committee reviewed the GPG between staff and discussed disclosure of the figures and the differences between Equal Pay and GPG.
Directors Remuneration Report (DRR) and other disclosures in the Annual Report and Accounts.	The Committee considered the disclosures required in the Annual Report and Accounts. The Committee received advice from the Company Secretary, HR Director and Deloitte LLP when compiling the DRR and the additional disclosures in the Notes.
Annual review of terms of reference	The Committee reviewed its term of reference and approved these for recommendation to the Board.
Forward calendar and items for 2019	The Committee agreed a standing agenda and calendar of meetings for 2019. Four meetings are planned to be held in 2019 to address routine matters.

The table above is not a complete list of matters considered by the Committee but highlights the most significant matters for the period in the opinion of the Remuneration Committee.

Remuneration Consultants and Committee advice

Throughout the period 1 January 2018 to 31 December 2018 the Committee had not appointed a Remuneration Consultant. The Committee received advice on specific matters from internal advisers and management, including the Group HR Director and the Company Secretary. Management received advice from McLagan, part of the Talent, Rewards & Performance practice at Aon plc, PwC LLP and from Deloitte LLP, such advice forming the basis for Management's advice to the Committee. The Committee is satisfied that the advice provided by McLagan, PwC and

Deloitte in relation to remuneration matters is objective and independent and, in respect of Deloitte, did not adversely affect their independence as auditor.

In early 2019 the Committee commenced a competitive tender process to seek to appoint a Remuneration Consultant, culminating in the appointment of the Executive Compensation practice of Aon plc. This team from Aon is a signatory to the Remuneration Consultants' Code of Conduct, which requires its advice to be objective and impartial, and the team is not involved in marketing or selling other Aon services. Further information on the outcome of this process will be provided in the 2019 Annual Report and Accounts.

Corporate Governance Report

Directors' Remuneration Report

The information contained in the Directors' Remuneration Report is subject to audit, where indicated in the Report, in accordance with The Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended).

On behalf of the Board, as Chairman of the Remuneration Committee, I am pleased to present our Directors' Remuneration Report.

The Directors' Remuneration Report contains the Annual Remuneration Report which explains the operation of remuneration related arrangements for 2018 and a summary of the intended operation of the Remuneration Policy in 2019. An extract of the Remuneration Policy for Executive and Non-Executive Directors and an illustration of the application of the Remuneration Policy in 2019 are included at the end of this Report.

A full copy of the Remuneration Policy, which was approved by shareholders at the 2017 Annual General Meeting, can be found on the Company's website at www.securetrustbank.com.

How we link executive remuneration to our strategy

The key principles behind the Group's Remuneration Policy are:

- to be simple and transparent in order to reflect the Group's mission statement of straightforward, transparent banking,
- to promote the long term success of the Group, with transparent and demanding performance conditions,
- to provide alignment between executive reward and the Group's values, risk appetite and shareholder returns, and
- to have a competitive mix of base salary and short and long term incentives, with an appropriate proportion of the package linked to the delivery of sustainable long term growth.

In developing and implementing the Remuneration Policy we have also had regard to regulatory requirements with regard to senior managers under the Senior Manager Regime. The Group is currently a Level 3 firm within the classifications applied by the financial regulators for regulated entities. That means that the Group is not required to satisfy in full all elements of the remuneration codes. Notwithstanding this, in formulating and applying the Remuneration Policy the Committee has had regard to the remuneration codes when looking at existing and proposed remuneration. The Committee has been compliant with the remuneration requirements of the 2016 UK Corporate Governance Code throughout the year.

Corporate governance report

Directors Remuneration Report for 2018

Single figure table (audited information)

The following table sets out total remuneration earned for each Director in respect of the year ended 31 December 2018 and the prior year.

	Salary and fees		Benefits		Annual bonus		Pension		Shares[1]		Total remuneration	
	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's	£'000's
Executive Directors												
P Lynam	1,200	1,200	22	28	600[7]	400[7]	35	35	-	-	1,857	1,663
N Kapur	410	400	29	35	300[7]	160[7]	25	25	-	-	764	620
Non-Executive Directors												
M Forsyth	200	200	1	1	-	-	-	-	-	-	201	201
A Berresford[2]	88	74	1	1	-	-	-	-	-	-	89	75
P Marrow[3]	115	126	-	-	-	-	-	-	-	-	115	126
P Myers[4]	6	-	-	-	-	-	-	-	-	-	6	-
L Neville-Rolfe[4]	6	-	-	-	-	-	-	-	-	-	6	-
V Stewart[5]	75	72	1	1	-	-	-	-	-	-	76	73
Former Directors									-	-		
H Angest[6]	40	60	-	-	-	-	-	-	-	-	40	60
A Salmon[6]	40	60	-	-	-	-	-	-	-	-	40	60
	2,180	2,192	54	66	900	560	60	60	-	-	3,194	2,878

[1] No shares were eligible to vest under the LTIP based upon performance for the year ending 2018 (2017:nil). Further details of awards made under the LTIP can be found on page 184.
[2] Ann Berresford was appointed Audit Committee Chairman on 23 September 2017 and a member of the Risk Committee on 25 July 2018.
[3] Paul Marrow stepped down as Chair of the Audit Committee with effect 23 September 2017.
[4] Baroness Neville-Rolfe and Paul Myers were appointed to the Board on 28 November 2018.
[5] Victoria Stewart was appointed Remuneration Committee Chairman on 21 July 2017.
[6] Fees for the services of Sir Henry Angest and Andrew Salmon as Non-Executive Directors were paid to Arbuthnot Banking Group by whom they are employed. Fees of £5,000 per director per month were paid. These figures exclude VAT.
[7] The bonus amount for Paul Lynam and Neeraj Kapur is the total bonus earned in respect of the year, of which 50% was deferred into shares under the 2017 Deferred Bonus Plan. Further details are disclosed on page 186.

The figures in the single figure tables above are derived from the following:

Salary and fees	The amount of salary / fees received in the year.
Benefits	The taxable value of benefits received in the year. These are principally private medical health insurance, car allowances and the value of Sharesave Scheme options granted during the year. Sharesave Scheme options are valued based on the difference between the market value of the shares at grant and the exercise price and were granted for the first time in 2017.
Annual bonus	The value of the bonus earned in respect of the financial year (including the proportion of the amount earned which is subject to deferral).
Pension	The amount of payments in lieu of Company pension contributions received in the year.

Additional disclosures in respect of the single figure table (audited information)

Base salary and fees

Base salaries for the Executive Directors in respect of the year ended 31 December 2017 and 31 December 2018 are as follows:

	2017 base salary £000	2018 base salary £000
P Lynam	1,200	1,200
N Kapur	400	410

The Committee considered it appropriate to increase Neeraj Kapur's base salary for 2018 by 2.5% to £410,000 in line with the basic salary increases for broader staff and to reflect the position of his salary compared to peers.

Bonus arrangements

For the financial year ended 31 December 2018 Executive Directors were eligible for an annual bonus award of up to 100% of salary, subject to stretching performance metrics based on a balanced business scorecard of financial, strategic, customer, operational and staff metrics. 60% of the bonus was subject to financial and risk performance ("Financial") metrics and 40% of the bonus was subject to a mixture of strategic, customer, operational and staff performance ("Non-financial") metrics. Details of the annual bonus outturn are shown below.

	Financial % of salary opportunity	Financial % of salary outturn	Non-financial % of salary opportunity	Non-financial % of salary outturn	Total % of salary outturn	£000
Paul Lynam	60	41.4	40	24.63	66.03	792
Neeraj Kapur	60	48.8	40	24.5	73.3	300

50% of the bonus earned is deferred into shares under the Deferred Bonus Plan. Deferred shares will vest in equal tranches after one, two and three years following deferral. The CFO's objectives differ in weighting and target to those of the CEO and, whilst no less challenging, had a different outturn to that of the CEO.

The Chairman and the CEO discussed the objective assessment of the financial and non-financial performance of the Group relative to the targets set at the beginning of 2018. The Group has made good progress in a number of strategic areas during 2018 as set out in the Chairman's and CEO's statements, and has delivered adjusted profits above target. This warrants an 'above target' rating for the CEO, which in turn would drive a formulaic 'above target' reward. However, despite this strong performance across a number of financial and non-financial KPIs, including profitability and customer measures, given the market wide reduction in banking sector share prices and specifically the reduction in the share price of the Company over the course of 2018, and being cognisant of the overall level of his remuneration, the CEO indicated that, if he were awarded a bonus in respect of 2018, he would not wish this to exceed an 'on-target' level. The Remuneration Committee, in agreement with that assessment, has applied an overlay to the formulaic calculation to reduce the total amount to be paid to the equivalent of an 'on-target' assessment of 50% of salary, half of which is deferred into shares over three years. This further aligns the CEO's interests with those of shareholders.

Set out below are the high level financial and non-financial performance metrics applied in respect of the financial year ended 31 December 2018.

Financial and risk performance metrics

The financial and risk performance metrics were based on the delivery of Board agreed KPIs in accordance with the schedule below.

					CEO		CFO	
Objective	**Threshold (0% payable)**	**On-target (50% payable)**	**Stretch (100% payable)**	**Achieved**	**Weight**	**Bonus payable**	**Weight**	**Bonus payable**
Grow Statutory Profit Before Tax.	£30m	£33m	£36m	£36.7m	15%	11.8%	15%	11.8%
Adjusted Return on Average Equity.	10.4%	11.8%	13.2%	13.1%	15%	14.9%	15%	14.9%
Sustain Underlying Cost Income ratio as determined by the Board.	57.1%	51.9%	46.7%	53.8%	10%	3.2%	5%	1.6%
Maintain strong compliance with risk appetite and legal and regulatory obligations across the Group, including maintaining sufficient capital to meet the strategic plan	Range of capital required set at the minimum capital requirement through to a level, which included a capital buffer, as determined by the Board. Regulatory capital as assessed by the Board is above the agreed target as detailed on page 24. The Group's risk appetite was maintained within tolerance, including budgeted cost of risk in line with the KPIs set out on page 18 (Threshold; 2.6%; On target; 2.0% Stretch; 1.6%).; no material negative issues identified by Board, Risk or Audit Committee during the year; mandatory training was completed by all relevant staff.				10%	7.5%	10%	7.5%
Deliver other key financial objectives	Assessed by reference to improving the profitability of the mortgage business and ensuring a smooth transition and run off of the asset finance business or such other route as agreed - both measures were delivered at between threshold and on-target performance.				10%	4%	n/a	n/a
Successful execution of capital diversification plans.	Assessed by the raising of debt capital before 31 December 2018 at an attractive coupon.				n/a	n/a	15%	13%
Total					**60%**	**41.4%**	**60%**	**48.8%**

Non-financial performance metrics

The high level objectives and targets (together with commentary on their achievement) for both Executive Directors are set out on the following page.

Corporate governance report

Directors Remuneration Report for 2018

Objective	Targets	Achievement	CEO Weight	CEO Bonus payable
Grow				
Strategic M&A activity	Explore M&A opportunities to augment the organic plan or achieve a strategic objective as agreed.	The Committee was satisfied that we have engaged in a number of discussions relating to inorganic business opportunities in support of our strategy throughout 2018. None of the opportunities has progressed to a conclusion that was acceptable to us or our disciplined approach to opportunities. The Committee was therefore satisfied that on-target performance was achieved during the year.	5%	2.5%
Delivery of long-term strategic plan and objectives throughout the year	Measured by reference to the presentation of and direction in line with the three year strategic plan.	The Committee was satisfied that the strategic plan delivered in terms of quality, vision and deliverable financial targets, including the quality of financial data within Board papers, merited an on-target performance outcome.	10%	5%
Love				
Placing the customer at the heart of what we do	Measured by reference to the FEEFO and overall customer rating for STB.	Aggregate scores of 4.7/5 for the period were just below the stretch performance target set.	5%	4.38%
Focusing on our investor relations	Measured by reference to sustaining strong relationships with shareholders, assessed via feedback direct to the Chairman from shareholders and from the post shareholder roadshow feedback.	The Committee was satisfied that the feedback received from the Chairman and our corporate brokers and advisers merited a between on-target and stretch performance outcome during the year.	5%	3%
Investing in the future and development of the senior talent pipeline	Measured by reference to the development of the Senior Management and Executive Committee members to fully contribute to the Group Strategy and in the execution of the agreed plan.	Individual Executive Committee and Senior Manager objectives were set to deliver key targets of the Group Strategy, with these cascaded into the Senior Management team via their individual performance management documents. The Committee was therefore satisfied that on-target performance was achieved during the year.	7.5%	3.75%
Being an employer of choice.	Expanding plans to address staff engagement at all levels and in contemplation of regulatory changes and so as to increase employee retention, decrease employee attrition and promote employee development.	Achieved Great Places to Work accreditation meaning STB is in top 3% of all firms surveyed. Attrition and turnover reduced. Established an Employee Council aligned with the requirements of the 2018 Corporate Governance Code.	7.5%	6%
Total			**40%**	**24.63%**

Corporate governance report

Directors Remuneration Report for 2018

			CFO	
Objective	**Targets**	**Achievement**	**Weight**	**Bonus payable**
Grow				
Strategic M&A activity	Explore M&A opportunities to augment the organic plan or achieve a strategic objective as agreed	The Committee was satisfied that we have engaged in a number of discussions relating to inorganic business opportunities in support of our strategy throughout 2018. None of the opportunities has progressed to a conclusion that was acceptable to us or our disciplined approach to opportunities. The Committee was therefore satisfied that on-target performance was achieved during the year.	5%	2.5%
Delivery of long-term strategic plan and objectives throughout the year.	Measured by reference to the presentation of and direction in line with the three year strategic plan.	The Committee was satisfied that the strategic plan delivered in terms of quality, vision and deliverable financial targets, including the quality of financial data within Board papers, merited an on-target performance outcome.	10%	5%
Sustain				
Auditor Migration	Measured by the effective and efficient migration of external auditors from KPMG LLP to Deloitte LLP.	The Committee was satisfied that the migration delivered in terms of quality, efficiency, management of key risks, timeliness and deliverable targets for the Finance team, and merited a performance outcome between on-target and stretch.	10%	7.5%
Love				
Focusing on our investor relations	Measured by reference to sustaining strong relationships with shareholders, assessed via feedback direct to the Chairman from shareholders and from the post shareholder roadshow feedback.	The Committee was satisfied that the feedback received from the Chairman and our corporate brokers and advisers merited a between on-target and stretch performance outcome during the year.	5%	3%
Investing in the future and development of the wider Finance Team.	Measured by reference to the development of the Finance team and Target Operating Mode, staff engagement and developing talent and planning for succession	The Committee was satisfied that the future capability of the Finance team and the plans developed and implemented merited a between on-target and stretch performance outcome during the year.	5%	4%
Strengthening the Treasury capabilities.	Measured by the successful implementation of Treasury plans, including the creation of effective hedging strategies and execution capabilities.	The Committee was satisfied that the future capability of the Treasury team and the plans developed and implemented merited an on-target performance outcome during the year.	5%	2.5%
Total			**40%**	**25.5%**

Vesting of the non-financial performance element of the annual bonus was based on the Committee's view of the relative importance and impact of each of the objectives during the year.

Awards granted during the financial year (audited information)

2017 Long Term Incentive Plan ('LTIP')

Nominal-cost share options were granted to Executive Directors on 20 April 2018 in accordance with the rules of the LTIP as follows.

Recipient	Date of grant	Basis of award	Number of shares	Face value of award £000[1]	Performance period
Paul Lynam	20 April 2018	33.3% of salary	20,986	400	1 January 2018 to 31 December 2020
Neeraj Kapur	20 April 2018	44% of salary	9,443	180	1 January 2018 to 31 December 2020

[1]Based on a share price of 1906p per share which was the mid market price on the 19 April 2018.

Vesting of the share options is subject to EPS, Relative TSR and risk management performance metrics, assessed over a three year performance period. The EPS and relative TSR performance targets are set out in the table below:

Vesting (% of maximum)	EPS growth (40% of award)	Relative TSR[1] (40% of award)
0%	Less than 10% per annum	Below Median
25%	10% per annum	Median
100%	30% per annum	Upper quartile
Straight-line vesting between points.		

[1]As at the grant date, the TSR comparator group consisted of the following constituents: Arbuthnot Banking Group, Charter Court Financial Services Group plc, Close Brothers, OneSavings Bank, Metro Bank, Paragon Banking Group, Provident Financial, S&U and Virgin Money.

The remaining 20% of the award will be assessed on risk management performance objectives during the Performance Period aligned with the Company's risk management framework, including but not limited to:

- the number of customer complaints received;
- the number and nature of material risk events within the Group;
- credit losses compared to the Board's assessment of the Group's risk appetite; and
- management of regulatory capital limits.

Vesting will be determined based on the Committee's view of the relative importance and impact of each of the objectives over the performance period. Awards vest to the extent that the performance metrics are achieved, and are subject to a further two-year holding period.

2017 Deferred Bonus Plan (DBP)

Nominal-cost share options were granted to Executive Directors on 20 April 2018 in accordance with the rules of the DBP as set out below:

Recipient	Date of grant	Number of shares	Tranche 1	Tranche 2	Tranche 3	Face value of award £000[1]
Paul Lynam	20 April 2018	10,493	3,497	3,497	3,499	200
Neeraj Kapur	20 April 2018	4,197	1,399	1,399	1,399	80

[1]Based on a share price of 1906p per share which was the mid market price on the 19 April 2018.

Each award has been granted in the form of an option with an exercise price per share equal to the nominal value of a share and, subject to the rules of the Plan will vest:

- on 20 April 2019 as regards one third of the shares subject to it (Tranche 1);
- 20 April 2020 as regards one third of the shares subject to it (Tranche 2); and
- 20 April 2021 as regards one third of the shares subject to it (Tranche 3).

Each option once vested remains capable of exercise until 20 April 2028. The awards are subject to malus and clawback provisions as detailed in the rules of the DBP but not subject to further performance conditions.

Statement of Directors' shareholding and share interests (audited information)

No formal shareholding guidelines are currently in place. However, Paul Lynam has committed to building up and maintaining a shareholding of at least 100% of base salary, over time, by retaining all awards under the LTIP that vest (net of income tax and National Insurance).

The interests of the Directors and their connected persons in the Company's ordinary shares as at 31 December 2018 were as set out below. Any changes to a Directors' shareholding are set out in the notes below the table.

Director	Type	Owned outright	Vested but unexercised	Vested and exercised during the year	Unvested, not subject to performance conditions	Unvested, subject to performance conditions	Total as at 31 December 2018
P Lynam	Shares	19,012[5]	-	-	-	-	19,012
	2011 Share Options	-	141,667	-	-	-	141,667
	2017 LTIP	-	-	-	-	26,335	26,335
	2018 LTIP[1]	-	-	-		20,986	20,986
	2018 DBP[1]	-	-	-	10,493	-	10,493
	2017 SAYE[2]	-	-	-	1,364	-	1,364
	Phantom share options[3]	-	187,500	-	-	-	187,500
							407,357 [6]
N Kapur	Shares	1,000	-	-	-	-	1,000
	2011 Share Options	-	35,417	-	-	-	35,417
	2017 LTIP	-	-	-	-	7,132	7,132
	2018 LTIP[1]	-	-	-	-	9,443	9,443
	2018 DBP[1]	-	-	-	4,197	-	4,197
	2017 SAYE[2]	-	-	-	1,364	-	1,364
	Phantom share options[3]	-	31,250	-	-	-	31,250
							89,803 [6]
M Forsyth	Shares	3,000[7]	-	-	-	-	**3,000**
A Berresford	Shares	-	-	-	-	-	-
P Marrow	Shares	5,440	-	-	-	-	**5,440**
P Myers	Shares	-	-	-	-	-	-
L Neville-Rolfe[4]	Shares	-	-	-	-	-	-
V Stewart	Shares	-	-	-	-	-	-
Former Directors							
H Angest	Shares	-	-	-	-	-	-
A Salmon	Shares	7,500	-	-	-	-	**7,500**

[1] Awards were granted under the LTIP and DBP rules on 20 April 2018 as set out on pages 184 and 186.

[2] Each of Paul Lynam and Neeraj Kapur participated in the 2017 SAYE scheme to the maximum monthly saving amount and did not participate in the 2018 SAYE scheme.

[3] Each Phantom Share Option was granted on 23 March 2015 and was subject to the satisfaction of a performance condition. That performance condition had been met by the end of the performance period; the option price was below the market price, however, and a £nil value has been attributed to the awards.

[4] Baroness Neville-Rolfe purchased 1,271 shares on 9 January 2019.

[5] On 18 December 2018 Paul Lynam purchased 4,012 shares.

[6] Assuming a full vesting of awards as disclosed in the table above (excluding Phantom Share Options, see 3 above) and a market value as at 31 December 2018 of 1190p the value of Paul Lynam's total interest in shares is £2.62m and the value of Neeraj Kapur's total interest in shares is £0.7m.

[7] On 18 October 2018 Lord Forsyth purchased 1,000 shares.

Payments made to former Directors during the year (audited information)

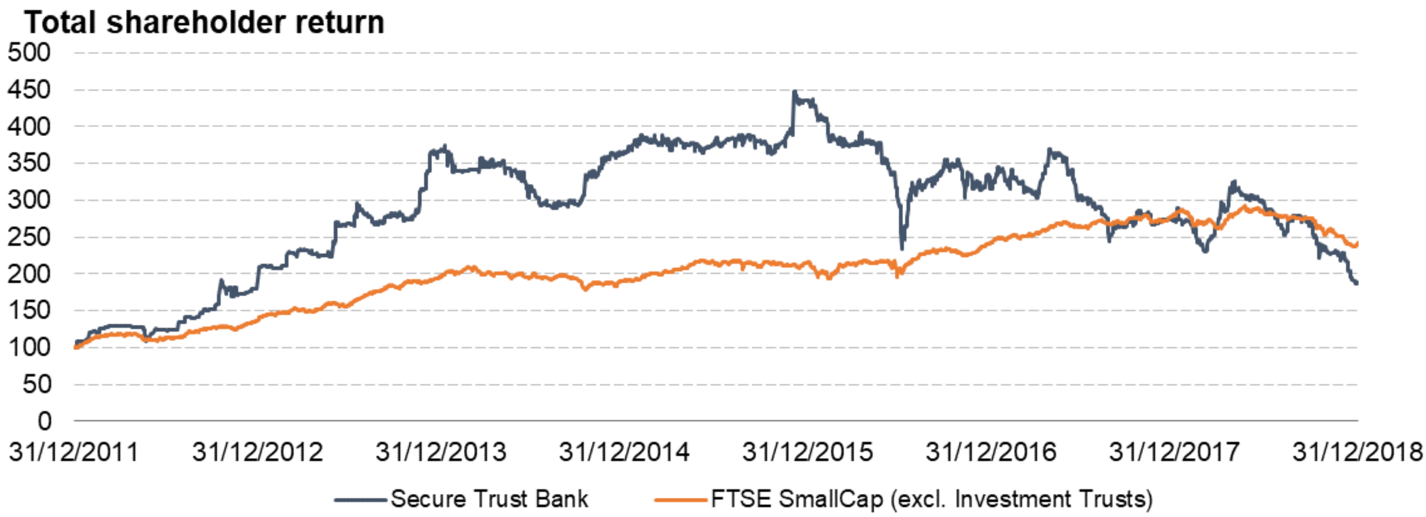
No payments were made in the year to any former Director of the Company.

Payments for loss of office made during the year (audited information)

No payments for loss of office were made in the year to any Director of the Company.

Performance graph and historical CEO remuneration outcomes

The graph below shows the total shareholder return (TSR) performance for the Company's shares in comparison to the FTSE SmallCap Index (excluding Investment Trusts) for the period from 1 January 2012 to 31 December 2018. For the purposes of the graph, TSR has been calculated as the percentage change during the period in the market price of the shares, assuming that dividends are reinvested. The graph shows the value, by 31 December 2018, of £100 invested in the Group over the period compared with £100 invested in the FTSE SmallCap Index (excluding Investment Trusts). The FTSE SmallCap Index (excluding Investment Trusts) has been chosen as a comparator as this is the most appropriate reference point given the capitalisation of the Company.



The table below shows details of the total remuneration, bonus and share options vesting (as a percentage of the maximum opportunity) for the CEO over the last seven financial years.

Corporate governance report

Directors Remuneration Report for 2018

	Total remuneration £'000	Bonus as a % of maximum opportunity[1]	Share options as a % of maximum opportunity[2]
2018	1,857	50	N/A
2017	1,657	33.3	N/A
2016	5,542	N/A	100%
2015	1,459	N/A	N/A
2014	3,671	N/A	100%
2013	1,031	N/A	N/A
2012	870	N/A	N/A

1. Pre Main Market Admission bonuses were determined by the Committee on a discretionary basis taking into account Group financial and individual performance during the financial year.
2. No share options were eligible to vest in respect of the years 2012, 2013, 2015, 2017 and 2018.

CEO pay increase in relation to all employees

The table below sets out the percentage change (from the financial year ended 31 December 2017) in base salary, value of taxable benefits and bonus for the CEO compared with the average percentage change for all employees.

Percentage change	CEO	Wider workforce
Salary	0%	3.0%
Taxable benefits	0%	13.6%
Annual bonus	50.0%	0.9%

Paul Lynam earned a bonus equal to £600,000 in respect of performance for the financial year ended 31 December 2018 (2017: £400,000).

Spend on pay

The following table sets out the percentage change (from the financial year ended 31 December 2017) in dividends and the overall expenditure on pay (as a whole across the organisation).

	2018 £million	2017 £million	Change %
Dividends, excluding special dividends, and share buybacks	14.8	14.0	5.7
Dividends, Including special dividends, and share buybacks	14.8	14.0	5.7
Overall expenditure on pay continuing operations[1]	47.3	39.0	21.3

[1] Further information can be found in Note 5 set out on page 161.

The increase in overall expenditure on pay is driven primarily by the increased size of Group's workforce, as set out in Note 6.

Service agreements and letters of appointment

Details of the Directors' service agreements, letters of appointment and notice periods are set out below:

Directors Remuneration Report for 2018

Name	Commencement of current service agreement/letter of appointment[2,3,4]	Notice period
P Lynam	28 July 2010	12 months
N Kapur	27 October 2011	12 months
M Forsyth[1]	6 October 2016	6 months
A Berresford	22 November 2016	6 months
P Marrow[1]	6 October 2016	6 months
P Myers	28 November 2018	6 months
L Neville-Rolfe	28 November 2018	6 months
V Stewart	22 November 2016	6 months

[1]Entered into new letters of appointment prior to the Company's transition from the AIM to the Main Market.
[2]Each of the Non-Executive Directors' letter of appointment was amended in January 2019 by a side letter confirming their respective Committee membership and their total fee. No other changes were made to their existing letter of appointment.
[3]All Non-Executive Directors are subject to re-election at intervals of not more than three years. For 2019 and future years, all Directors will be subject to annual re-election.
[4]Those Non-Executive Directors who are members of the Remuneration Committee are set out on page 94.

Implementation of Directors' Remuneration Policy for the financial year ending 31 December 2019

Details on how Secure Trust intends to implement the Directors' Remuneration Policy for the financial year ending 31 December 2019 are set out below.

Salary

Paul Lynam will not receive a salary increase in 2019. Neeraj Kapur's salary was increased by 3.66% to £425,000 with effect from 1 January 2019.

Fees

The following table sets out the Non-Executive Director fee structure effective from 1 January 2019.

Role	2019 fee £'000's
Chairman[1]	204[2]
Non-Executive Director (basic fee)[2]	67[2]
Senior Independent Director	20
Chairman of Audit Committee	20
Chairman of Risk Committee	20
Chairman of Remuneration Committee	10
Member of Audit Committee	5
Member of Risk Committee	5
Member of Remuneration Committee	5

1. The Chairman does not receive any additional fees for his membership of any of the Board's committees.
2. With effect from 2019 the base fee payable to the Chairman and the NEDs increased in line with the average increase of remuneration for staff implemented within the annual review of remuneration in the previous year. The increase takes effect from 1 January each year starting with 2019. For 2019 the increase was 2.4%.

Annual bonus

The proposed maximum annual bonus opportunity for the year ending 31 December 2019 will be equal to 100% of salary. The bonus will be subject to stretching performance metrics based on a balanced business scorecard. 55% of the bonus will be subject to financial performance metrics, 15% risk metrics and 30% of the bonus will be subject to a mixture of non-financial strategic, customer, operational and staff performance metrics. The financial metrics will include PBT (15%), ROAE (15%), Cost Income Ratio (10%), and capital ratios (15%). The risk measures will include risk appetite (7.5%) and risk culture (7.5%). The non-financial metrics will include strategic programmes (15%), stakeholder management (5%) and governance (5%).

The Committee considers that the targets are commercially sensitive. A description of the performance targets will be disclosed in the Annual Report on Remuneration for the year ending 31 December 2019 or at such time when the targets are no longer considered commercially sensitive.

Up to an additional 100% of salary may be awarded in exceptional circumstances (such as in order to recognise exceptional performance during the year). To the extent that any additional bonus is awarded, full details of the award and rationale will be disclosed in the Annual Report on Remuneration for the year ending 31 December 2019.

50% of any bonus earned will be deferred into shares under the Deferred Bonus Plan. Deferred shares will vest in equal tranches after one, two and three years following deferral.

LTIP

The Company proposes to grant LTIP awards to the Executive Directors in the form of nominal share options at the level of up to 61% of salary for the CFO and 50% of salary for the CEO. The LTIP awards will be subject to EPS, Relative TSR and risk management performance metrics as in 2018. Performance will be assessed over a three year performance period.

The proposed EPS and Relative TSR performance targets are set out below.

Vesting (% of maximum)	EPS growth (40% of award)	Relative TSR[1] (40% of award)
0%	Less than 10% per annum	Below Median
25%	10% per annum	Median
100%	30% per annum	Upper quartile
Straight-line vesting between points.		

1. The Committee intends to use the following group of selected peers for assessing TSR performance: Arbuthnot Banking Group, Charter Court Financial Services Group plc, Close Brothers, OneSavings Bank, Metro Bank, Paragon Banking Group, Provident Financial, S&U and PCF Group plc.

20% of the award will be based on risk management performance objectives aligned with the Company's risk management framework.

Statement of voting at AGM

The Remuneration Policy and Directors' Remuneration Report were approved by shareholders at the AGM in 2017 and 2018 respectively; the votes cast were as detailed below.

Resolution	Proxy votes for	% of proxy votes cast	Proxy votes against	% of proxy votes cast
To approve the directors' remuneration policy (2017)	13,454,036	96.04	554,865	3.96
To receive and approve the directors' remuneration report (2018)	15,753,799	100	72	0

Corporate governance report

Directors Remuneration Report for 2018

Approval

This Report was approved by the Board on 27 March 2019 and signed on its behalf by:

Victoria Stewart
Chairman of the Remuneration Committee

Corporate governance report

Summary remuneration policy

The Directors' Remuneration Policy was approved by shareholders at the 2017 AGM and took effect from the end of that meeting. A summary of the Directors' Remuneration Policy is set out below. A full copy of the Directors' Remuneration Policy can be found within the 2016 Report and Accounts, which are on the website at www.securetrustbank.com, and that document should be used when evaluating Directors Remuneration.

Summary Directors' Remuneration Policy table for Executive Directors

Base salary	
Operation	Salaries are usually reviewed annually taking into account: • underlying Group performance; • role, experience and individual performance; • competitive salary levels and market forces; and • pay and conditions elsewhere in the Group.
Maximum opportunity	No maximum salary; increases will normally be in line with the typical range of salary increases awarded (in percentage of salary terms) to other employees in the Group. Salary increases above this level may be awarded to take account of individual circumstances.
Benefits	
Operation	Executive Directors receive benefits in line with market practice, and these include a car allowance, medical insurance, life assurance and disability insurance. Other benefits may be provided based on individual circumstances. These may include, for example, relocation and travel allowances.
Maximum opportunity	Whilst the Committee has not set an absolute maximum on the level of benefits Executive Directors may receive, the value of benefits is set at a level which the Committee considers to be appropriately positioned taking into account relevant market levels based on the nature and location of the role and individual circumstances.
Pension	
Operation	Executive Directors are eligible to participate in the Group defined contribution pension plan. In appropriate circumstances, such as where contributions exceed the annual or lifetime allowance, Executive Directors may be permitted to take a cash supplement in lieu of contributions to a pension plan.
Maximum opportunity	Employer pension contributions are limited to 5% of base salary. The maximum cash supplement in lieu of pension is 5% of base salary (less any employer pension contribution).
Annual bonus	
Operation	Awards are based on performance (measured over a year) against metrics determined by the Committee. Pay-out levels are determined by the Committee after the year end based on performance against those targets. The Committee has discretion to amend the pay-out should any formulaic output not reflect the Committee's assessment of overall business performance. Executive Directors are required to defer 50% of any bonus earned into shares under the Deferred Bonus Plan (DBP). Deferred share awards vest in equal tranches after one, two and three years following deferral. The Committee may decide to pay the whole of the bonus earned in cash where the amount to be deferred is less than £50,000. Clawback provisions will apply to annual bonus awards and malus and clawback provisions will apply to deferred share awards.
Maximum opportunity	The normal maximum annual bonus opportunity is 100% of base salary. An additional annual bonus opportunity of up to 100% of base salary may be awarded in exceptional circumstances.

Summary remuneration policy

Performance Metrics	Targets are set annually reflecting the Group's strategy and aligned with key financial, strategic and/or individual targets. The annual bonus will be assessed against key financial performance metrics of the business and non-financial strategic/personal objectives, in such proportions as the Committee considers appropriate. **Financial metrics** At least 50% of the maximum potential will be paid for on-target performance and all of the maximum potential will be paid for maximum performance. **Non-financial strategic or individual metrics** Vesting of the non-financial strategic or individual metrics will apply on a scale between 0% and 100% based on the Committee's assessment of the extent to which a non-financial performance metric has been met. Deferred share awards are not subject to any additional performance metrics.
Long Term Incentive Scheme (LTIP)	
Operation	Awards are in the form of nil-cost / nominal-cost share options, conditional shares or other such form as has the same economic effect. Awards will be granted with vesting dependent on the achievement of performance conditions set by the Committee, normally over at least a three year performance period. Awards will usually be subject to a two year holding period following the end of the performance period (with the exception that sufficient awards may be sold to meet any income tax and National Insurance liabilities). The holding period does not apply to awards with a face value of £150,000 or less at the time of grant. Awards may be settled in cash (or granted as a right to a cash amount) at the election of the Committee. Malus and clawback provisions will apply to awards.
Maximum opportunity	The normal maximum award is 100% of salary in respect of a financial year. The Committee will take into account Company and personal performance during the preceding financial year when determining the maximum award to be granted.
Performance Metrics	Performance metrics are selected that reflect underlying business performance. Performance metrics and their weighting where there is more than one metric are reviewed annually to maintain appropriateness and relevance. Awards will vest between 25% and 100% for performance between 'threshold' performance (the minimum level of performance that results in any level of vesting) and 'maximum' performance.
All employee share schemes	
Operation	Executive Directors are entitled to participate in a HMRC tax-qualifying all-employee Sharesave Scheme under the same terms as other Group employees.
Maximum opportunity	Participant limits are those set by the UK tax authorities from time to time.

Application of malus and clawback

Malus and clawback provisions will apply over the following time periods:

Element	Malus	Clawback
Annual bonus award	To such time as payment is made.	Up to three years following payment.
Deferred bonus award	To such time as the award vests.	Tranche of award deferred for one year: Up to two years following vesting. Tranche of award deferred for two years: Up to one year following vesting. Tranche of award deferred for three years: No clawback provisions apply.
LTIP award	To such time as the award vests.	Up to two years following vesting.

Summary remuneration policy

Malus may apply in the following circumstances:

- The Executive Director's service agreement is terminated for gross misconduct or the Executive Director receives a formal written warning for gross misconduct, as defined by the Company's disciplinary policy.
- The Company suffers a material loss arising from the Executive Director operating outside of agreed risk policy parameters and as such the Committee considers a material failure in risk management has occurred.
- The level of the award is not considered sustainable when assessing the overall financial viability of the Company.
- The Executive Director is subject to regulatory censure in respect of a material failure in control.

Clawback may apply in the following circumstances:

- Discovery of a material misstatement resulting in an adjustment in the audited consolidated accounts of the Company.
- The assessment of any performance target or condition in respect of an award was based on material error or materially inaccurate or misleading information.
- The discovery that any information used to determine the DBP and/or LTIP was based on material error, or materially inaccurate or misleading information.
- Action or conduct of an Executive Director which, in the reasonable opinion of the Board, amounts to fraud or gross misconduct.
- The Executive Director is subject to regulatory censure in respect of a material failure in control.

Non-Executive Directors

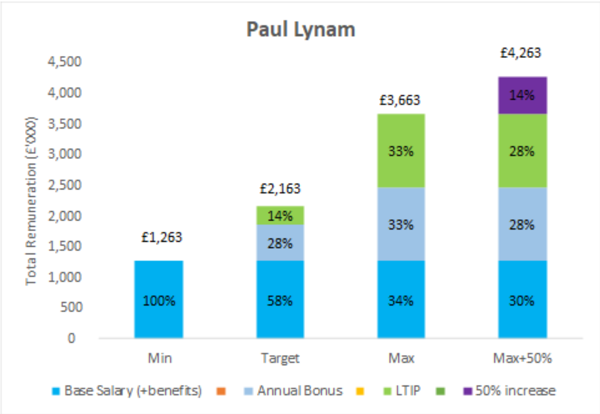
Element and purpose	Approach of the Company
Chairman and Non-Executive Director fees To enable the Group to recruit and retain Non-Executive Directors of a suitable calibre.	Fees are normally reviewed annually. Fees paid to Non-Executive Directors for their services are approved by the Board. Fees may include a basic fee and, for Non-Executive Directors excluding the Chairman, additional fees for further responsibilities (for example, chairmanship and membership of Board committees or holding the office of Senior Independent Director). Fees are based on the level of fees paid to Non-Executive Directors serving on the board of similar-sized UK listed companies and the time commitment and contribution expected for the role. Non-Executive Directors cannot participate in any of the Company's share schemes or annual bonus and are not eligible to join the Company's pension scheme. Non-Executive Directors may be eligible to receive benefits such as private medical insurance, the use of secretarial support, travel costs or other support that may be appropriate.

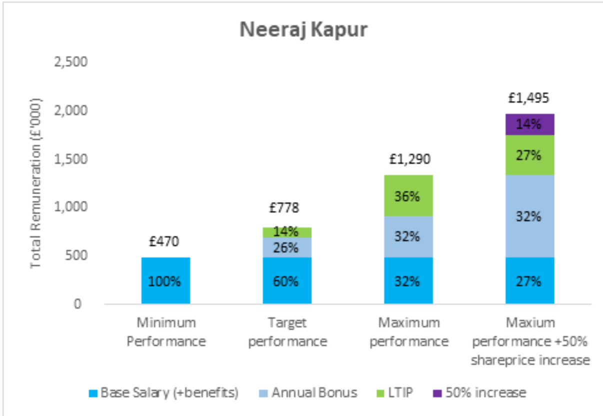
Illustrations of application of remuneration policy

The charts below set out for each Executive Director an illustration of the application for 2019 of the remuneration policy. The charts show the split of remuneration between fixed pay, annual bonus (including amounts deferred under the DBP) and LTIP on the basis of minimum remuneration, remuneration receivable for performance in line with the Company's expectations, maximum remuneration (not allowing for any share price appreciation) and maximum remuneration allowing for a 50% appreciation in the share price calculated at 31 December 2018.

Corporate governance report

Summary remuneration policy





In illustrating the potential reward, the following assumptions have been made:

Scenario	Description	Assumptions
Minimum performance	Minimum remuneration receivable.	Fixed elements of remuneration only – salary as at 1 January 2018, benefits and pension. No payments under incentive plans.
Target performance	Remuneration receivable for achieving performance in line with expectations.	Fixed elements of remuneration (as above). 50% of maximum annual bonus earned. 25% of maximum LTIP award vesting.
Maximum performance	Remuneration receivable for achieving performance in excess of the maximum performance targets.	Fixed elements of remuneration (as above). 100% of maximum annual bonus earned. 100% of maximum LTIP award vesting.
Maximum performance + 50% shareprice increase	Remuneration receivable for achieving performance in excess of the maximum performance targets and a 50% increase in share price.	Fixed elements of remuneration (as above). 100% of maximum annual bonus earned. 100% of maximum LTIP award vesting and 50% increase in share price.

Corporate governance report

Directors' report

Report and financial statements

The Directors submit their report, the related Strategic Report and Corporate Governance Report and the audited financial statements of Secure Trust Bank PLC and its subsidiaries (the 'Group') for the year ended 31 December 2018. The Strategic Report is set out beginning on page 2. This Directors' Report also includes additional disclosures required by the UKLA's Disclosure and Transparency Rules and Listing Rules. Some of the matters normally included in the Directors' Report are included by reference as indicated below.

Principal activities and review

The principal activity of the Group is banking including deposit taking and secured and unsecured lending.
The business review and information about future developments, key performance indicators and principal risks are contained in the Strategic Report.

Corporate governance

The Corporate Governance report, on pages 62 to 113, contains information about the Group's corporate governance arrangements, including the Group's compliance with the Code. A statement relating to the Group's compliance with the Code throughout the year ending 31 December 2018 is set out on page 69.

Results

The results for the year are shown on page 134. The Group made a profit for the period of £28.3 million (2017: £23.8 million, being profit after tax from continuing operations of £19.9 million and profit from discontinued operations of £3.9 million). The reconciliation of statutory results to adjusted results is set out in the Financial Review in the Strategic Report.

For the purposes of DTR 4.15R2 and DTR 4.1.8 this Directors' Report and the Strategic Report on pages 2 to 61 comprise the management report.

Dividends

The Directors recommend the payment of a final dividend of 64 pence per share which, together with the interim dividend of 19 pence per share paid on 28 September 2018, represents total dividends for the year of 83 pence per share (2017: 79 pence per share). The final dividend, if approved by members at the Annual General Meeting, will be paid on 24 May 2019 to shareholders on the register at the close of business on 26 April 2019.

Dividend Policy

The Directors reviewed the dividend policy of the Company and have adopted a progressive dividend policy which takes into account the Company's capital requirements, earnings and cash flow in the long term.

The Directors will have regard to current and projected capital, liquidity, earnings and market expectations in determining the amount of the dividend. On occasion, the Company may declare and pay a special dividend resulting from special circumstances, however no such special dividend is currently envisaged.

Share capital

The share capital of the Company comprises one class of ordinary shares with a nominal value of 40p each. As at 31 December 2018 the Company had 18,475,229 ordinary shares in issue. Each ordinary share entitles the holder to one vote.

All the ordinary shares are fully paid and rank equally in all respects and there are no special rights to dividends or in relation to control of the Company. No shares were issued during 2018 (2017: nil).

Details of the Company's share capital and movements in the Company's issued share capital during the year are provided in Note 26 of the consolidated financial statements.

The Company operates a Long Term Incentive Plan, Sharesave Plan and a Deferred Bonus Share Plan as set out in the Remuneration Report on pages 97 to 109. Upon exercise, shares awarded under these plans have the same rights and rank pari passu with existing ordinary shares.

The powers of the Directors, including in relation to the issue or buyback of the Company's shares are set out in the Companies Act 2006 and the Company's Articles of Association. Shareholders will be asked to grant authority to the Directors to issue and allot shares at the 2019 Annual General Meeting.

Under section 551 of the Companies Act 2006, the Directors may allot equity securities only with the express authorisation of shareholders which may be given in General Meeting, but which cannot last more than five years. Under section 561 of the Companies Act 2006, the Board may also not allot shares for cash (otherwise than pursuant to an employee share scheme) without first making an offer to existing shareholders to allot such shares to them on the same or more favourable terms in proportion to their respective shareholdings, unless this requirement is waived by special resolution of the shareholders.

Resolutions permitting such actions will be proposed at the 2019 Annual General Meeting. Details of the resolutions for such authority are included in the Notice of the 2019 Annual General Meeting and in the related explanatory notes.

The Notice of the 2019 Annual General Meeting also includes resolutions specifically relating to the issue of shares associated with an issue of Additional Tier 1 Securities. These resolutions are in a similar form to the resolutions proposed and passed at the 2018 AGM.

Under section 701 of the Companies Act 2006 a company may make a market purchase of its own shares if the purchase has first been authorised by a resolution of the company.

The Company did not repurchase any of the issued ordinary shares during the year or up to the date of this report, although it was granted authority to do so by shareholders at the 2018 Annual General Meeting on 16 May 2018. That authority expires on 31 May 2019 or, if earlier, the conclusion of the 2019 Annual General Meeting.

At the 2019 Annual General Meeting a special resolution will be proposed authorising the Company to make market purchases of ordinary shares within the limits set out in the resolution. The resolution is in a similar form to that proposed at the 2018 Annual General Meeting. The Directors have no present intention of exercising the authority granted by the resolution, but regard it as a useful tool to have available.

On a show of hands, each member has the right to one vote at General Meetings of the Company. On a poll, each member is entitled to one vote for every share held. The shares carry no rights to fixed income. No person has any special rights of control over the Company's share capital and all issued shares are fully paid. Voting at the 2019 AGM will be conducted on a poll.

Directors' report

There are no specific restrictions on the transfer of the shares in the Company which are governed by the general provisions of the Articles of Association and prevailing legislation.

Substantial shareholders

In accordance with Disclosure and Transparency Rules DTR5, the Company as at 26 March 2019 (being the latest practicable date before publication of this report), has been notified of the following disclosable interests in its issued ordinary shares:

Significant Shareholders	No.of Ordinary Shares	%
Invesco Perpetual Asset Management	3,544,465	19.18%
Columbia Threadneedle Investments	2,902,234	15.71%
Arbuthnot Banking Group PLC	2,869,538	15.53%
Wellington Management Company	1,547,994	8.38%
Ruffer	1,532,247	8.29%
Mr Steven A Cohen	1,510,412	8.18%
Unicorn Asset Management	1,257,410	6.81%
BAE Systems Pension Fund Investment Management	845,753	4.58%

Directors

A full list of Directors who served on the Board throughout the financial year, including their biographical information, is shown on pages 64 to 68. All the Directors will be retiring and standing for either election or re-election at the Annual General Meeting to be held on 15 May 2019.

Directors' Interests

The Directors' interests (and those of any persons connected with them) in the share capital of the Company as at 31 December 2018 are set out on page 104 in the Directors' Remuneration Report.

Powers of Directors

The Directors' powers are conferred on them by UK legislation and by the Company's Articles of Association. Changes to the Company's Articles of Association must be approved by shareholders by way of a special resolution and must comply with the provisions of the Companies Act 2006 and the Financial Conduct Authority's Disclosure and Transparency Rules.

Appointment and retirement of Directors

The appointment and retirement of the Directors is governed by the Company's Articles of Association, the UK Corporate Governance Code and the Companies Act 2006. Further details can be found on page 72 and in the explanatory notes included in the Notice of 2019 Annual General Meeting.

Directors' indemnities

The Company's Articles of Association provide that, subject to the provisions of the Companies Act 2006, the Company may indemnify any director or former director of the Company or any associated company against any liability and may purchase and maintain for any director or former director of the Company or any associated company insurance against any liability.

The Group has maintained directors and officers liability insurance throughout 2018.

The letters of appointment of the Non-Executive Directors incorporate by reference the provisions of the Articles of Association in relation to the indemnity of Directors into the contract established by the letter of appointment between the Non-Executive Director and the Company.

Disclosure of information under Listing Rule 9.8.4R

Additional information, where not already contained in the Directors' Report, where applicable to the Company, can be found in the following sections of the Annual Report.

Item	Page reference
Details of any long term incentive schemes	Page 103
Allotments of cash of equity securities otherwise than to shareholders in proportion to their holdings	Note 27, Page 183

Related party transactions and conflicts of interest

Details of related party transactions are set out in Note 36 to the Financial Statements. Directors are invited to declare new conflicts of interest at each Board meeting and where an actual or potential conflict of interest has been identified appropriate steps are taken to deal with the conflict. A separate register of Directors' conflicts of interest is maintained by the Company.

Significant contracts

Details of related party transactions are set out in Note 36 to the financial statements. There are no contracts of significance in which a director is interested.

There are no agreements between any Group company and any of its employees or any director of any Group company which provide for compensation to be paid to an employee or a director for termination of employment or for loss of office as a consequence of a takeover of the Company.

There are no significant agreements to which the Company is party that take effect, alter or terminate upon a change of control following a takeover bid for the Company.

Employment policies and equal opportunities

The Group is an inclusive and equal opportunities employer and opposes all forms of discrimination. Applications from people with disabilities will be considered fairly and if existing employees become disabled, every effort is made to retain them within the workforce wherever reasonable and practicable. The Group also endeavours to provide equal opportunities in the training, promotion and general career development of disabled employees.

Group policies seek to create a workplace that has an open atmosphere of trust, honesty and respect. Harassment or discrimination of any kind is not tolerated. This principle applies to all aspects of employment from recruitment and promotion, through to termination and all other terms and conditions of employment.

The Group has processes in place for communicating with its employees. Employee communications include information about the performance of the Group, on major matters affecting their work, employment or workplace and to encourage employees to get involved in social or community events. These communications aim to achieve a common awareness for all employees of the financial and economic factors affecting the performance of the Group. Further information on the ways in which the Group communicates with its employees are set out in the Corporate Responsibility Report starting on page 54.

Directors' report

Research and development

The Group does not undertake research and development activities.

Political donations and expenditure

The Group made no political donations and incurred no political expenditure during the year (2017: £nil).

Post balance sheet events

There have been no significant events between 31 December 2018 and the date of approval of the financial statements which would require a change to or additional disclosure in the financial statements.

Disclosure of information to auditor

Each director in office at the date of this Directors' Report confirms that so far as the director is aware, there is no relevant audit information of which the Company's auditor is unaware and each director has taken all the steps that they ought to have taken as a director to make themselves 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 the Companies Act 2006.

Going concern and viability

The financial statements have been prepared on a going concern basis. Further information about this, and the Group's ongoing viability, is to be found on page 52.

Fair, Balanced and Understandable

The Directors are satisfied that the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable, and provide the information necessary for members and other stakeholders to assess the Group's position and performance, strategy and business model.

Future developments and financial risk management objectives and policies

Information about future developments, internal control and financial risk management systems in relation to financial reporting and financial risk management objectives and policies in relation to the use of financial instruments can be found in the following sections of the annual report which are incorporated into this report by reference:

Future developments – see Strategic Report on pages 2 to 61.

Internal control and financial risk management systems in relation to financial reporting – see Corporate Governance Report on pages 62 to 113. Financial risk management objectives and policies in relation to the use of financial instruments can be found on the Group's website: www.securetrustbank.com/our-corporate-information/risk-management and Note 29 to the financial statements.

Greenhouse Gas emissions from our operations

The Group's Greenhouse Gas emissions, required under the Companies Act 2006 (Strategic Report and Directors' Report) Regulation 2013, are detailed on page 54.

Auditor

Deloitte LLP was appointed as auditor at the Annual General Meeting held in 2018. As detailed on page 80 in the Audit Committee Report, the Board is recommending the reappointment of Deloitte LLP as auditor at the 2019 Annual General Meeting.

Annual General Meeting

The 2019 Annual General Meeting will be held at 3pm on 15 May 2019 at Arbuthnot House, 7 Wilson Street, London, EC2M 2SN.

By order of the Board
A J Karter
Secretary
27 March 2019

Directors’ responsibility statement

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. As required by the Listing Rules they are required to prepare the Group financial statements in accordance with IFRS 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 and prudent;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- state whether they have been prepared in accordance with IFRS as adopted by the EU;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group and parent company's financial position and financial performance;
- 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 Group and parent company’s transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its 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 to safeguard the assets of the Group and parent company and for taking such steps as are reasonably open to them 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, Directors’ Remuneration Report and Corporate Governance Statement 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.

We confirm that to the best of our knowledge:

- The financial statements, prepared in accordance with IFRS as adopted by the European Union, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and parent company and the undertakings included in the consolidation taken as a whole;
- The strategic report includes a fair review of the development and performance of the business and the position of the Group and parent 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; and

Directors' responsibility statement

- The annual report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group and parent company's performance, business model and strategy.

This responsibility statement was approved by the Board of Directors on 27 March 2019 and is signed on their behalf by:

Paul Lynam
Chief Executive Officer

Neeraj Kapur
Chief Financial Officer

Independent Auditor's report to the members of Secure Trust Bank PLC

Report on the audit of the financial statements

In our opinion:

- **the financial statements of Secure Trust 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 2018 and of the Group's profit for the year then ended;**
- **the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;**
- **the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and**
- **the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.**

We have audited the financial statements which comprise:

- the consolidated statement of comprehensive income;
- the consolidated and parent company statement of financial position;
- the consolidated and parent company statement of changes in equity;
- the consolidated and parent company statement of cash flows; and
- the related notes 1 to 40.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as issued by European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the 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 the 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.

Independent Auditor's report to the members of Secure Trust Bank PLC

Report on the audit of the financial statements

Key audit matters	The key audit matters that we identified in the current year were: • revenue recognition; and • impairment of receivables.
Materiality	We determined materiality using 5% of profit before tax. The materiality that we used for the Group financial statements was £1.7 million and the materiality used for the parent company was £1.3 million.
Scoping	All entities in the Group are within our audit scope and audited to a local materiality for the purpose of individual entity reporting. Audit work to respond to the risks of material misstatement was performed directly by the Group audit engagement team.

Conclusions relating to going concern, principal risks and viability statement

Going concern

We have reviewed the directors' statement in note 1 to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Group's and Company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements.

We considered as part of our risk assessment the nature of the Group, its business model and related risks including where relevant the impact of Brexit, the requirements of the applicable financial reporting framework and the system of internal control. We evaluated the directors' assessment of the Group's ability to continue as a going concern, including challenging the underlying data and key assumptions used to make the assessment, and evaluated the directors' plans for future actions in relation to their going concern assessment.

We are required to state whether we have anything material to add or draw attention to in relation to that statement required by Listing Rule 9.8.6R(3) and report if the statement is materially inconsistent with our knowledge obtained in the audit.

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

Independent Auditor's report to the members of Secure Trust Bank PLC
Report on the audit of the financial statements

Principal risks and viability statement

Based solely on reading the directors' statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the directors' assessment of the Group's and the Company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to:

- the disclosures on pages 40 to 51 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation on page 40 that they have carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity; or
- the directors' explanation on page 52 as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We are also required to report whether the directors' statement relating to the prospects of the Group required by Listing Rule 9.8.6R (3) is materially inconsistent with our knowledge obtained in the audit.

We confirm that we have nothing material to report, add or draw attention to in respect of these matters.

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.

Report on the audit of the financial statements

Revenue recognition	
Key audit matter description	The Group recognised interest income of £169.2 million (2017: £141.3 million) against loans and advances to customers during the year. The Group has implemented IFRS 9: Financial Instruments, which was effective from 1 January 2018. This is a new and complex accounting standard which has required considerable judgement and interpretation in its implementation. The Group holds loans and advances to customers which meet the criteria of financial assets under IFRS 9. The recognition of interest income on loans under IFRS 9 requires the use of an effective interest rate method. Judgement is applied by management to determine key assumptions related to the behavioural lives, with our specific focus placed on the Motor and Retail Finance portfolios, being the principal income streams for the Group. Any changes to such assumptions during the life of the loan can have a significant impact on the amount of interest income recognised during the year. Given the degree of judgement and estimation involved in determining the behavioural life, as well as the cash flows directly attributable to each loan (primarily fee and interest cash flows), we also identified that there is a potential for fraud through possible manipulation of this balance. Management's associated accounting policies are detailed on pages 144 to 145. The corresponding area in the Audit Committee report is on page 83.
How the scope of our audit responded to the key audit matter	We first understood management's process and key controls around recognition of interest income through discussions and walkthroughs, we then evaluated the associated design and implementation of the key controls. Specifically, we assessed the Assumption Committee control, which is used as a forum for members to present analysis, discuss and challenge key assumptions, such as the estimate of behavioural lives adopted within revenue recognition. We challenged the behavioural life assumptions used by management by reference to the Group's historical behavioural life experience and the macroeconomic environment. We utilised our data analytics specialists to translate the SAS code used to determine the behavioural lives from the historical settlement data and tested the accuracy and completeness of these data alongside management's extraction process from the underlying lending systems. As part of our wider assessment of revenue recognition we also reviewed the treatment of fees and charges arising on loans and advances to customers and the appropriateness of their inclusion or exclusion in the Group's EIR model.

Report on the audit of the financial statements

Key observations	The results of our testing were satisfactory and the underlying methodology used for the calculation of EIR for the Motor and Retail Finance portfolios is considered materially compliant in the context of the accounting policies and the requirements of the relevant accounting standards. We determine the behavioural lives adopted by management to be reasonable.
Impairment of receivables	
Key audit matter description	The Group held allowances for impairment of loans and advances to customers of £67.1 million (2017: £39.9 million in accordance with IAS 39) against loans and advances to customers of £2,096.0 million (2017: £1,638.2 million). The transition adjustment on adoption of IFRS 9 at 1 January 2018 was an increase of £31.8 million, resulting in a total allowance for impairment of £71.7 million at 1 January 2018. For financial assets held at amortised cost, IFRS 9 requires the carrying value to be assessed for impairment using unbiased forward-looking information. The measurement of expected credit losses is complex and involves a number of judgements and estimates relating to customer default rates, exposure at default, loss given default, assessing significant increases in credit risk and macroeconomic scenario modelling. These assumptions are informed using historical behaviour and management's experience. They are also affected by management's consideration of the future economic environment including the potential effect of the withdrawal of the United Kingdom from the European Union. In order to determine the key assumptions within the model, we performed sensitivity analysis and considered the impact each assumption had on the level of recorded provision. The most significant assumptions and judgements applied in the impairment model are: • The determination of the loss given default ('LGD') on the Motor Finance portfolio, in particular the vehicle recovery rate and the valuation of forecast auction proceeds; • The completeness of the Real Estate Finance ('REF') allowance for impairment; and • The completeness and accuracy of post-model overlays made by management. As such our significant risk focussed on the validity of these particular assumptions and judgements. Given the degree of judgement involved in determining key assumptions, we also identified that there is a potential for fraud through possible manipulation of this balance. Management's associated accounting policies are detailed within note 1.10 on pages 148 to 153. The corresponding area in the Audit Committee report is on page 83.

How the scope of our audit responded to the key audit matter	We first understood management's process and key controls around allowances for impairment by undertaking a walkthrough. Following identification of the key controls, we evaluated the associated design and implementation of such controls. Specifically, we assessed: • the review control over the determination of the LGD assumptions within Motor Finance, as part of management's judgement paper; • the credit grading review performed within the REF business; and • the Assumption Committee control which is used as a forum for members to present analysis, discuss and challenge key assumptions, such as the completeness and validity of management overlays. For the Motor Finance LGD we have assessed and tested both the historical and forecast data used to support both the vehicle recovery rate and the valuation of forecast auction proceeds, whilst also re-performing the calculation to assess its mechanical accuracy. In order to assess completeness of the REF allowance for impairment, we reviewed cases where a significant increase in credit risk had been observed, as well as customers that had been placed on a Watchlist by management. Additionally we performed testing across the remainder of the REF portfolio to identify whether there are any customers who may be experiencing signs of financial distress. We engaged our valuation specialists to challenge the collateral valuations utilised by the Group within the LGD calculation for all cases where financial distress had been observed. We utilised peer benchmarking to assess the reasonableness of the forced sale discounts applied to the collateral valuations. For post-model overlays we reviewed the accuracy of management's overlay provisions by reference to the supporting calculations and challenged their completeness through our understanding of model enhancements, the external environment and analysis of key performance indicators. Additionally we reviewed whether overlays identified as part of the transitional assessment and interim balance sheet date had been incorporated into the models. We challenged management's consideration of the future economic environment within the macroeconomic scenarios, including the potential effect of the withdrawal of the United Kingdom from the European Union by comparing modelled assumptions to publicly available data from the Office of National Statistics and comparable peer data. As part of our wider assessment of impairment of receivables we engaged accounting specialists to assess compliance of the modelling approach with the requirements of the standard and credit risk specialists to determine whether the documented modelled approach was implemented in practice.

Independent Auditor’s report to the members of Secure Trust Bank PLC

Report on the audit of the financial statements

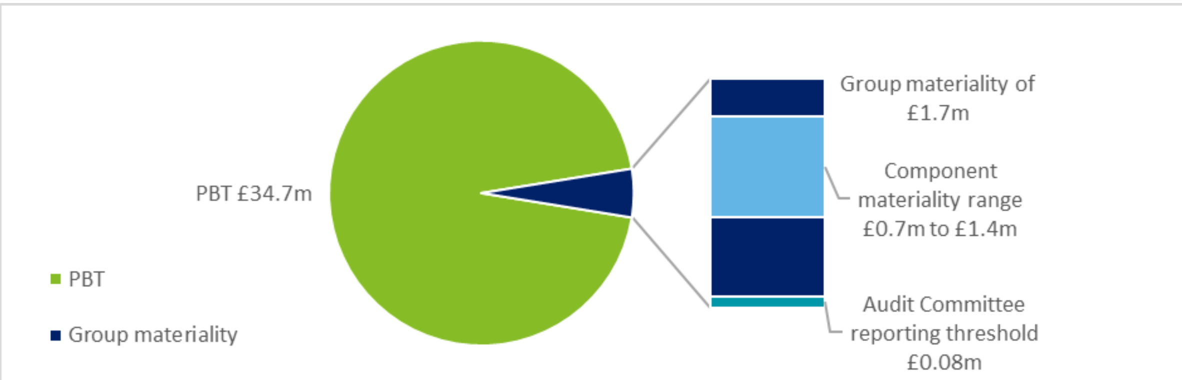
	We reconciled the allowances for impairment models to the general ledger and substantively tested a sample of loans to assess whether the data used in the provision calculation were complete and accurate.
Key observations	Based on the evidence obtained, we found that the assumptions underpinning the allowances for impairment models were determined and applied appropriately and the recognised provision was reasonably stated.

Our application of 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	£1.7 million (2017 under predecessor auditor: £1.2 million)	£1.3 million (2017 under predecessor auditor: £1.2 million)
Basis for determining materiality	5% of profit before tax	5% of profit before tax
Rationale for the benchmark applied	We determined materiality using profit before tax as we considered this to be the most appropriate measure to assess the performance of the Group. As the majority of the Group’s operations are carried out by the parent company, the same materiality basis was used for both.	



Independent Auditor's report to the members of Secure Trust Bank PLC

Report on the audit of the financial statements

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £86,500k (2017 under predecessor auditor: £60,000), 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.

An overview of the scope of our audit

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. Based on that assessment, our Group audit scope focused on all entities within the Group and covered 100% of the material balances in the consolidated financial statements of the Group. We have performed testing over the consolidation of Group entities. These audits were performed directly by the Group audit team and executed at levels of materiality ranging from £0.05m to £1.3m, which are applicable to each individual entity and are lower than Group materiality.

Other information

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

We have nothing to report in respect of these matters.

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.

In connection with our audit of the financial statements, 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 audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. 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.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

- Fair, balanced and understandable – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's position and performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or
- Audit committee reporting – the section describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee; or
- Directors' statement of compliance with the UK Corporate Governance Code – the parts of the directors' statement required under the Listing Rules relating to the Company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R (2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.

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 parent company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud are set out below.

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.

Independent Auditor's report to the members of Secure Trust Bank PLC

Report on the audit of the financial statements

Extent to which the audit was considered capable of detecting irregularities, including fraud

We identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and then design and perform audit procedures responsive to those risks, including obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion.

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, our procedures included the following:

- enquiring of management, internal audit and the Audit Committee, including obtaining and reviewing supporting documentation, concerning the Group's 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;
    - the internal controls established to mitigate risks related to fraud or non-compliance with laws and regulations;
- discussing among the engagement team and involving relevant internal specialists, including tax, data analytics, valuations, share based payment, information technology, prudential regulatory and credit risk specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud. As part of this discussion, we identified potential for fraud in the following areas: revenue recognition and impairment of receivables; and
- obtaining an understanding of the legal and regulatory frameworks that the Group operates in, focusing on those laws and regulations that had a direct effect on the financial statements or that had a fundamental effect on the operations of the Group. The key laws and regulations we considered in this context included the UK Companies Act, listing rules and tax legislation. In addition, we considered the regulation set by the Prudential Regulatory Authority relating to regulatory capital and liquidity requirements, which are fundamental to the Group's ability to continue as a going concern.

Audit response to risks identified

As a result of performing the above, we identified revenue recognition and impairment of receivables as key audit matters. 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 relevant laws and regulations discussed above;
- enquiring of management, the Audit Committee and in-house 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 Financial Conduct Authority and Prudential Regulation Authority; and

- 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 and regulations and potential fraud risks to all engagement team members including internal specialists, 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

Opinions on other matters prescribed by the Companies Act 2006

In our opinion the part of the directors' remuneration report to be audited has been properly prepared in accordance with 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 of 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.

Opinion on other matter prescribed by the Capital Requirements (Country-by-Country Reporting) Regulations 2013

In our opinion the information given in note 40 to the financial statements for the financial year ended 31 December 2018 has been properly prepared, in all material respects, in accordance with the Capital Requirements (Country-by Country Reporting) Regulations 2013.

Independent Auditor's report to the members of Secure Trust Bank PLC

Report on the audit of the financial statements

Matters on which we are required to report by exception

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.

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 made or the part of the directors' remuneration report to be audited is not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Other matters

Auditor tenure

Following the recommendation of the Audit Committee, we were appointed by the Board of Directors on 16 May 2018 to audit the financial statements for the year ending 31 December 2018 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is one year.

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).

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.

Matthew Perkins (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
Birmingham, United Kingdom
27 March 2019

Consolidated statement of comprehensive income

	Note	2018 Total £million	2017 Continuing £million	2017 Discontinued £million	2017 Total £million
Income statement					
Interest income and similar income	4.1	169.2	141.3	8.0	149.3
Interest expense and similar charges	4.1	(35.5)	(26.7)	-	(26.7)
Net interest income	4.1	**133.7**	**114.6**	**8.0**	**122.6**
Fee and commission income	4.2	19.4	16.0	-	16.0
Fee and commission expense	4.2	(1.5)	(1.1)	-	(1.1)
Net fee and commission income	4.2	**17.9**	**14.9**	**-**	**14.9**
Operating income		**151.6**	**129.5**	**8.0**	**137.5**
Net impairment losses on loans and advances to customers		(32.4)	(33.5)	(3.4)	(36.9)
Operating expenses	5	(84.5)	(71.3)	(0.3)	(71.6)
Profit on sale of equity instruments available-for-sale		-	0.3	-	0.3
Profit before income tax		**34.7**	**25.0**	**4.3**	**29.3**
Income tax expense	7	(6.4)	(5.1)	(0.8)	(5.9)
Profit after income tax		**28.3**	**19.9**	**3.5**	**23.4**
Gain recognised on disposal after tax		-	-	0.4	0.4
Profit for the period		**28.3**	**19.9**	**3.9**	**23.8**
Other comprehensive income					
Items that will not be reclassified to the income statement					
Revaluation reserve		(0.3)	0.1	-	0.1
Taxation		0.1	-	-	-
		(0.2)	0.1	-	0.1
Items that may subsequently be reclassified to the income statement					
Available-for-sale reserve		-	2.8	-	2.8
Taxation		-	-	-	-
		-	2.8	-	2.8
Other comprehensive income for the period, net of income tax		**(0.2)**	**2.9**	**-**	**2.9**
Total comprehensive income for the period		**28.1**	**22.8**	**3.9**	**26.7**
Profit attributable to:					
Equity holders of the Company		**28.3**	**19.9**	**3.9**	**23.8**
Total comprehensive income attributable to:					
Equity holders of the Company		**28.1**	**22.8**	**3.9**	**26.7**
Earnings per share for profit attributable to the equity holders of the Company during the period (pence per share)					
Basic earnings per share	8.1	**153.2**	**107.7**	**21.1**	**128.8**
Diluted earnings per share	8.2	**150.9**	**106.4**	**20.9**	**127.3**

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Consolidated statement of financial position

	Note	At 31 December 2018 £million	2017 £million
ASSETS			
Cash and balances at central banks		169.7	226.1
Loans and advances to banks	10	44.8	34.3
Loans and advances to customers	11	2,028.9	1,598.3
Debt securities	14	149.7	5.0
Property, plant and equipment	15	11.0	11.5
Intangible assets	16	9.9	10.4
Deferred tax assets	18	7.9	0.6
Other assets	19	22.4	5.4
Total assets		**2,444.3**	**1,891.6**
LIABILITIES AND EQUITY			
Liabilities			
Due to banks	20	263.5	113.0
Deposits from customers	21	1,847.7	1,483.2
Current tax liabilities		4.2	3.0
Other liabilities	22	40.1	41.9
Provisions for liabilities and charges	23	1.3	1.4
Subordinated liabilities	24	50.4	-
Total liabilities		**2,207.2**	**1,642.5**
Equity attributable to owners of the parent			
Share capital	26	7.4	7.4
Share premium		81.2	81.2
Revaluation reserve		1.1	1.3
Retained earnings		147.4	159.2
Total equity		**237.1**	**249.1**
Total liabilities and equity		**2,444.3**	**1,891.6**

The financial statements on pages 134 to 216 were approved by the Board of Directors on 27 March 2019 and were signed on its behalf by:

Paul Lynam
Chief Executive Officer

Neeraj Kapur
Chief Financial Officer

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Company statement of financial position

	Note	At 31 December 2018 £million	2017 £million
ASSETS			
Cash and balances at central banks		169.7	226.1
Loans and advances to banks	10	41.9	32.3
Loans and advances to customers	11	1,980.3	1,565.5
Debt securities	14	149.7	5.0
Property, plant and equipment	15	6.0	6.1
Intangible assets	16	8.1	8.5
Investments	17	3.9	3.7
Deferred tax assets	18	7.8	0.6
Other assets	19	65.6	33.2
Total assets		**2,433.0**	**1,881.0**
LIABILITIES AND EQUITY			
Liabilities			
Due to banks	20	263.5	113.0
Deposits from customers	21	1,847.7	1,483.2
Current tax liabilities		3.6	1.9
Other liabilities	22	49.1	44.4
Provisions for liabilities and charges	23	1.3	1.4
Subordinated liabilities	24	50.4	-
Total liabilities		**2,215.6**	**1,643.9**
Equity attributable to owners of the parent			
Share capital	26	7.4	7.4
Share premium		81.2	81.2
Revaluation reserve		0.6	0.5
Retained earnings		128.2	148.0
Total equity		**217.4**	**237.1**
Total liabilities and equity		**2,433.0**	**1,881.0**

The Company has elected to take the exemption under section 408 of the Companies Act 2006 not to present the parent company income statement. The profit for the parent company for the year of £20.8 million is presented in the Company statement of changes in equity.

The financial statements on pages 134 to 216 were approved by the Board of Directors on 27 March 2019 and were signed on its behalf by:

Paul Lynam
Chief Executive Officer

Neeraj Kapur
Chief Financial Officer

Registered number: 00541132

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Consolidated statement of changes in equity

	Share capital £million	Share premium £million	Revaluation reserve £million	Available-for-sale reserve £million	Retained earnings £million	Total £million
Balance at 1 January 2017	**7.4**	**81.2**	**1.2**	**(2.8)**	**149.0**	**236.0**
Total comprehensive income for the period						
Profit for 2017	-	-	-	-	23.8	23.8
Other comprehensive income, net of income tax						
Revaluation reserve	-	-	0.1	-	-	0.1
Available-for-sale reserve	-	-	-	2.8	-	2.8
Total other comprehensive income	**-**	**-**	**0.1**	**2.8**	**-**	**2.9**
Total comprehensive income for the period	**-**	**-**	**0.1**	**2.8**	**23.8**	**26.7**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.0)	(14.0)
Tax on share-based payments	-	-	-	-	0.4	0.4
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**(13.6)**	**(13.6)**
Balance at 31 December 2017 (as previously stated)	**7.4**	**81.2**	**1.3**	**-**	**159.2**	**249.1**
IFRS 9 transition adjustment	-	-	-	-	(25.8)	(25.8)
Balance at 1 January 2018	**7.4**	**81.2**	**1.3**	**-**	**133.4**	**223.3**
Total comprehensive income for the period						
Profit for 2018	-	-	-	-	28.3	28.3
Other comprehensive income, net of income tax						
Revaluation reserve	-	-	(0.3)	-	-	(0.3)
Tax on revaluation reserve	-	-	0.1	-	-	0.1
Total other comprehensive income	**-**	**-**	**(0.2)**	**-**	**-**	**(0.2)**
Total comprehensive income for the period	**-**	**-**	**(0.2)**	**-**	**28.3**	**28.1**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.8)	(14.8)
Share-based payments	-	-	-	-	0.8	0.8
Tax on share-based payments	-	-	-	-	(0.3)	(0.3)
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**(14.3)**	**(14.3)**
Balance at 31 December 2018	**7.4**	**81.2**	**1.1**	**-**	**147.4**	**237.1**

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Company statement of changes in equity

	Share capital £million	Share premium £million	Revaluation reserve £million	Available-for-sale reserve £million	Retained earnings £million	Total £million
Balance at 1 January 2017	**7.4**	**81.2**	**0.5**	**(2.8)**	**135.5**	**221.8**
Total comprehensive income for the period						
Profit for 2017	-	-	-	-	26.1	26.1
Other comprehensive income, net of income tax						
Available-for-sale reserve	-	-	-	2.8	-	2.8
Total other comprehensive income	-	-	-	**2.8**	-	**2.8**
Total comprehensive income for the period	-	-	-	**2.8**	**26.1**	**28.9**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.0)	(14.0)
Tax on share-based payments	-	-	-	-	0.4	0.4
Total contributions by and distributions to owners	-	-	-	-	**(13.6)**	**(13.6)**
Balance at 31 December 2017 (as previously stated)	**7.4**	**81.2**	**0.5**	-	**148.0**	**237.1**
IFRS 9 transition adjustment	-	-	-	-	(26.3)	(26.3)
Balance at 1 January 2018	**7.4**	**81.2**	**0.5**	-	**121.7**	**210.8**
Total comprehensive income for the period						
Profit for 2018	-	-	-	-	20.8	20.8
Other comprehensive income, net of income tax						
Revaluation reserve	-	-	0.1	-	-	0.1
Total other comprehensive income	-	-	**0.1**	-	-	**0.1**
Total comprehensive income for the period	-	-	**0.1**	-	**20.8**	**20.9**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends	-	-	-	-	(14.8)	(14.8)
Share-based payments	-	-	-	-	0.8	0.8
Tax on share-based payments	-	-	-	-	(0.3)	(0.3)
Total contributions by and distributions to owners	-	-	-	-	**(14.3)**	**(14.3)**
Balance at 31 December 2018	**7.4**	**81.2**	**0.6**	-	**128.2**	**217.4**

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Consolidated statement of cash flows

	Note	Year ended 31 December 2018 £million	Year ended 31 December 2017 £million
Cash flows from operating activities – Continuing operations			
Profit for the year		28.3	19.9
Adjustments for:			
Income tax expense	7	6.4	5.1
Depreciation of property, plant and equipment	15	1.3	0.8
Loss on disposal of computer software		0.1	-
Amortisation of intangible assets	16	1.8	2.0
Impairment losses on loans and advances to customers		32.4	33.5
Share based compensation	27	0.8	-
Profit on sale of equity instruments available-for-sale		-	(0.3)
Cash flows from operating profits before changes in operating assets and liabilities		71.1	61.0
Changes in operating assets and liabilities:			
- net (increase)/decrease in debt securities		(144.7)	15.0
- net increase in loans and advances to customers		(494.8)	(378.3)
- net increase in other assets		(17.0)	(1.0)
- net increase in deposits from customers		364.5	331.4
- net decrease in other liabilities		(0.5)	(7.0)
Income tax paid		(6.4)	(5.1)
Net cash (outflow)/inflow from operating activities – Continuing operations		**(227.8)**	**16.0**
Cash flows from investing activities			
Sale of discontinued operation		-	37.1
Proceeds from sale of equity instruments available-for-sale		-	16.6
Purchase of property, plant and equipment	15	(1.1)	(0.8)
Purchase of computer software	16	(1.4)	(3.4)
Net cash (outflow)/inflow from investing activities – Continuing operations		**(2.5)**	**49.5**
Cash flows from financing activities			
Increase in amounts due to banks		150.0	43.0
Issue of subordinated liabilities	24	50.0	-
Subordinated liabilities issue costs	24	(0.8)	-
Dividends paid	9	(14.8)	(14.0)
Net cash inflow from financing activities – Continuing operations		**184.4**	**29.0**
Net (decrease)/increase in cash and cash equivalents – Continuing operations		**(45.9)**	**94.5**
Net increase in cash and cash equivalents – Discontinued operations		-	35.7
Cash and cash equivalents at 1 January		260.4	130.2
Cash and cash equivalents at 31 December		**214.5**	**260.4**

Proceeds from sale of equity instruments available-for-sale and net increase in amounts due to banks have been moved from operating activities to investing activities and financing activities respectively, as this better represents the nature of the underlying activity.

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Company statement of cash flows

	Note	Year ended 31 December 2018 £million	Year ended 31 December 2017 £million
Cash flows from operating activities – Continuing operations			
Profit for the year		20.8	22.2
Adjustments for:			
Income tax expense		4.9	2.7
Depreciation of property, plant and equipment	15	0.7	0.4
Loss on disposal of computer software		0.1	-
Amortisation of intangible assets	16	1.6	1.0
Impairment losses on loans and advances to customers		33.1	35.1
Share based compensation	27	0.6	-
Profit on sale of equity instruments available-for-sale		-	(0.3)
Cash flows from operating profits before changes in operating assets and liabilities		61.8	61.1
Changes in operating assets and liabilities:			
- net (increase)/decrease in debt securities		(144.7)	15.0
- net increase in loans and advances to customers		(480.3)	(378.9)
- net (increase)/decrease in other assets		(32.4)	0.6
- net increase in deposits from customers		364.5	331.4
- net increase/(decrease) in other liabilities		6.0	(11.5)
Income tax paid		(4.3)	(2.6)
Net cash (outflow)/inflow from operating activities – Continuing operations		**(229.4)**	**58.1**
Cash flows from investing activities			
Sale of discontinued operation		-	37.1
Proceeds from sale of equity instruments available-for-sale		-	16.6
Purchase of property, plant and equipment	15	(0.5)	(0.3)
Purchase of computer software	16	(1.3)	(3.3)
Net cash (outflow)/inflow from investing activities – Continuing operations		**(1.8)**	**50.1**
Cash flows from financing activities			
Increase in amounts due to banks		150.0	43.0
Issue of subordinated liabilities	24	50.0	-
Subordinated liabilities issue costs	24	(0.8)	-
Dividends paid	9	(14.8)	(14.0)
Net cash inflow/(outflow) from financing activities – Continuing operations		**184.4**	**(14.0)**
Net (decrease)/increase in cash and cash equivalents		**(46.8)**	**94.2**
Net increase in cash and cash equivalents – Discontinued operations		-	35.7
Cash and cash equivalents at 1 January		258.4	128.5
Cash and cash equivalents at 31 December		**211.6**	**258.4**

Proceeds from sale of equity instruments available-for-sale and net increase in amounts due to banks have been moved from operating activities to investing activities and financing activities respectively, as this better represents the nature of the underlying activity.

The notes on pages 141 to 216 are an integral part of these consolidated financial statements

Notes to the financial statements

1. Accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

1.1. Reporting entity

Secure Trust Bank PLC is a public limited company incorporated in England and Wales in the United Kingdom (referred to as 'the Company') and is limited by shares. The Company is registered in England and Wales and has the registered number 00541132. The registered address of the Company is One Arleston Way, Solihull, West Midlands, B90 4LH. The consolidated financial statements of the Company as at and for the year ended 31 December 2018 comprise Secure Trust Bank PLC and its subsidiaries (together referred to as 'the Group' and individually as 'subsidiaries'). The Group is primarily involved in banking and financial services.

1.2. Basis of presentation

The Group's consolidated financial statements and the Company's financial statements have been prepared in accordance with International Financial Reporting Standards, as adopted by the Group and endorsed by the EU and the Companies Act 2006 applicable to companies reporting under IFRS. They have been prepared under the historical cost convention, as modified by the revaluation of land and buildings and equity instruments available-for-sale. The consolidated financial statements are presented in pounds sterling, which is the functional and presentational currency of the entities within the Group.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 2.

The directors have assessed, in the light of current and anticipated economic conditions, the Group's ability to continue as a going concern. The directors confirm they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future. For this reason, they continue to adopt the 'going concern' basis for preparing accounts, as set out in the going concern and viability section of the Strategic Report starting on page 2.

The consolidated financial statements were authorised for issue by the Board of Directors on 27 March 2019.

1.3. IFRS 16 'Leases'

IFRS 16 'Leases' has been issued, and endorsed by the EU, but is not yet effective. It is effective for annual periods beginning on or after 1 January 2019, and has not been adopted early.

The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract i.e. the customer ('lessee') and the supplier ('lessor'). It replaces the previous leases standard, IAS 17 'Leases', and related interpretations.

IFRS 16 uses a new single model that applies to all leases, thus eliminating the classification of leases as either operating leases or finance leases for a lessee. Applying that model, on commencement of a lease, the lessee recognises a liability to make lease payments ('the lease liability'), an asset representing the right to use the underlying asset during the lease term ('the right-of-use asset'), and depreciation of right-of-use assets is shown separately from interest on lease liabilities in the income statement.

The lease liability is initially measured based on the net present value of the lease payments to be made over the remaining lease term, using the lessee's incremental borrowing rate as the discount rate. After commencement of the lease, the lease liability is measured on an amortised cost basis, with interest being calculated on an effective interest rate basis on the remaining balance of the liability, and lease payments reducing the lease liability when paid.

The right-of-use asset is initially measured at cost, being the amount of the initial measurement of the lease liability, adjusted for any prepaid rentals less any lease incentives plus any initial direct costs incurred by the lessee and dismantling or restoration costs. Subsequently, the right-of-use asset is amortised on a straight-line basis over the remaining term of the lease.

Transition choices

The Group has elected to recognise the cumulative effect of implementing IFRS 16 as an adjustment to the opening balance of retained earnings at 1 January 2019. Accordingly, prior year comparatives shall not be restated. As a practical expedient, the Group will apply the new standard only to contracts that had previously been identified as leases. Therefore, the new standard will not be applied to contracts that had not previously been identified as leases.

The Group has also elected not to apply IFRS 16 to the following:

- Short term leases of 12 months or less.
- Leases for which the underlying asset is of low value.

This has resulted in the new standard only being applicable to a number of property leases and motor vehicle leases.

The Group has chosen to measure the initial right of use asset for property leases at its carrying amount as if the standard has been applied since the commencement date, but discounted using the incremental borrowing rate as at 1 January 2019. The initial right of use asset for all other leases is measured at an amount equal to the lease liability.

The Group's IFRS 16 implementation project is substantially complete, and based on assessments undertaken to date, the estimated adjustments (net of tax) arising from the adoption of IFRS 16 on 1 January 2019 are expected to be an increase in assets and liabilities of approximately £6 million, and there will be no material impact on shareholders' equity at 1 January 2019. Additionally, it is not expected that implementation of IFRS 16 will have any material impact on profit before tax for the year ended 31 December 2019.

Lessor accounting

Lessor accounting remains unchanged from IAS 17.

1.4. Consolidation

Subsidiaries

Subsidiaries are all investees controlled by the Group. The Group controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to the Group.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

The parent company's investments in subsidiaries are recorded at cost less, where appropriate, provision for impairment in value.

Inter-company transactions, balances and unrealised gains and losses on transactions between Group companies are eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

Discontinued operations

Subsidiaries are de-consolidated from the date that control ceases. Discontinued operations are a component of an entity that has been disposed of, and represents a major line of business and is part of a single co-ordinated disposal plan.

1.5. IFRS 9 'Financial instruments'

The new standard, effective for the period beginning 1 January 2018, has replaced IAS 39 'Financial Instruments: Recognition and Measurement'. Adoption of the standard has resulted in new accounting policies for interest income and expense, the classification and measurement of financial instruments and the impairment of financial assets and loan commitments which are presented below.

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as noted below:

- The comparatives for the year ended 31 December 2017 have not been restated. Information presented for 2017 will not therefore be comparable. Differences in the carrying amounts of financial instruments resulting from adoption of IFRS 9 are recognised in retained earnings at 1 January 2018
- The determination of the business model within which a financial asset is held has been assessed based on facts that existed at the date of initial application and
- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Group has assumed that the credit risk of the asset had not increased significantly since initial recognition. A financial asset is considered to have low credit risk when its credit risk rating is equivalent to the widely understood definition of investment grade.

Additionally, the Group has adopted the consequential amendments to IFRS 7 'Financial Instruments: Disclosures'. These disclosures have been applied to information presented for the year ended 31 December 2018 and have not been applied to comparative information.

Implementation of IFRS 9 resulted in a £25.8 million reduction in the Group's opening equity at 1 January 2018, being £32.1 million net of £6.3 million related to associated deferred tax impacts. There has been no change in the carrying amount of financial instruments on the basis of their measurement categories. All adjustments have arisen solely due to a replacement of the IAS 39 incurred loss impairment approach with an expected credit loss ('ECL') approach. Further details are provided in Note 38.

1.6. Interest income and expense

Applicable from 1 January 2018 – IFRS 9 basis

For all financial instruments measured at amortised cost, the effective interest rate method is used to measure the carrying value and allocate interest income or expense. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- the gross carrying amount of the financial asset or
- the amortised cost of the financial liability.

In calculating the effective interest rate for financial instruments, other than assets that were credit impaired on initial recognition, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, early redemption penalty charges and broker commissions) and anticipated customer behaviour but does not consider future credit losses. For financial assets that were impaired on initial recognition (also referred to as purchased or originated credit impaired assets – 'POCI'), a credit adjusted effective interest rate is calculated using estimated future cash flows, including expected credit losses.

The calculation of the effective interest rate includes all fees received and paid that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial instrument.

For financial assets that are not considered to be credit impaired ('stage 1' and 'stage 2' assets), interest income is recognised by applying the effective interest rate to the gross carrying amount of the financial asset. For financial assets that become credit impaired subsequent to initial recognition ('stage 3' assets), interest income is recognised by applying the effective interest rate to the amortised cost of the financial asset. The credit risk of financial assets that become credit impaired are not expected to improve such that they are no longer considered credit impaired, however, if this were to occur the calculation of interest income would revert back to the gross basis. The Group's definition of stage 1, stage 2 and stage 3 assets is set out in Note 1.10.

For financial assets that were credit impaired on initial recognition (POCI assets), income is calculated by applying the credit adjusted effective interest rate to the amortised cost of the asset. For such financial assets the calculation of interest income will never revert to a gross basis, even if the credit risk of the asset improves.

Further details regarding when an asset becomes credit impaired subsequent to initial recognition is provided within Note 1.10.

Applicable prior to 1 January 2018 – IAS 39 basis

Interest income and expense was recognised in the income statement for all instruments measured at amortised cost using the effective interest method.

The effective interest method calculates the amortised cost of a financial asset or a financial liability and allocates the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group takes into account all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

1.7. Net fee and commission income

Fees and commission income and expenses that are an integral part of the effective interest rate of a financial instrument are included in the effective interest rate and presented in the Statement of Comprehensive Income as interest income or expense.

Fees and commission income that are not considered an integral part of the effective interest rate of a financial instrument are recognised when the Group satisfies performance obligations by transferring promised services to customers.

1.8. Financial assets and financial liabilities

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all of the risks and rewards of ownership. There have not been any instances where assets have only been partially derecognised. The Group derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

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, minus principal payments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

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. The fair value of assets and liabilities traded in active markets are based on current bid and offer prices respectively. If the market for a financial instrument is not active the Group establishes a fair value by using an appropriate valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis.

Applicable from 1 January 2018 – IFRS 9 basis

Financial Assets

The Group classifies its financial assets at inception into three measurement categories; ‘amortised cost’, ‘fair value through other comprehensive income’ (‘FVOCI’) and ‘fair value through profit and loss’ (‘FVTPL’). A financial asset is measured at amortised cost if both the following conditions are met and it has not been designated as at FVTPL:

- the asset is held within a business model whose objective is to hold the asset to collect its contractual cash flows; and
- the contractual terms of the financial asset give rise to cash flows on specified dates that represent payments of solely principal and interest on the outstanding principal amount.

The Group's current business model for all financial assets is to hold to collect contractual cash flows and all assets held give rise to cash flows on specified dates that represent solely payments of principal and interest on the outstanding principal amount. All the Group's assets are therefore currently classified as amortised cost. Loans are recognised when funds are advanced to customers and are carried at amortised cost using the effective interest method.

The amortised cost of an instrument is the amount at which it is measured at initial recognition, less principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, less any expected credit loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

A debt instrument would be measured at FVOCI only if both the below conditions are met and it has not been designated as FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting its contractual cash flows and selling the financial asset; and
- the contractual terms of the financial asset give rise to cash flows on specified dates that represent payments of solely principal and interest on the outstanding principal amount.

The Group currently has no financial instruments classified as FVOCI.

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election would be made on an investment by investment basis. The Group currently holds no such investments.

All other assets are classified as FVTPL. The Group currently has no financial assets classified as FVTPL.

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Group changes its business model for managing financial assets. The Group has not reclassified any financial assets during the reporting period.

Deposits from customers

The Group classifies its financial liabilities as measured at amortised cost. Such financial liabilities are recognised when cash is received from depositors and carried at amortised cost using the effective interest method.

Other financial liabilities

The subordinated liabilities comprise of 6.75% Fixed Rate Reset Callable Subordinated Notes due 2028 (the 'Notes'):

- The notes are redeemable for cash at their principal amount on a fixed date.
- The Company has a call option to redeem the securities early in the event of a 'tax event' or a 'capital disqualification event', which is at the full discretion of the Company.
- Interest payments are paid at six monthly intervals and are mandatory.
- The notes give the holders rights to the principal amount on the notes, plus any unpaid interest, on liquidation. Any such claims are subordinated to senior creditors, but rank pari passu with holders of other subordinated obligation and in priority to holders of share capital.

The above features provide the issuer with a contractual obligation to deliver cash or another financial asset to the holders, and therefore the notes are classified as financial liabilities. Further information in respect of the Notes is provided in Note 24.

Transactions costs that are directly attributable to the issue of the notes and are incremental costs that would not have been incurred if the notes had not been issued are deducted from the financial liability, and expensed to the income statement on an effective interest rate basis over the expected life of the notes.

The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the statement of financial position date.

The Group has not elected to measure any financial liabilities at fair value.

Applicable prior to 1 January 2018 – IAS 39 basis

The Group classified its financial assets as fair value through profit or loss, loans and receivables, held-to-maturity or available-for-sale and classifies its financial liabilities as other financial liabilities. Management determines the classification of its investments at initial recognition. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(a) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. Loans are recognised when the funds are advanced to customers. Loans and receivables are carried at amortised cost using the effective interest method (see below).

(b) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. Held-to-maturity investments are carried at amortised cost using the effective interest method.

(c) Available-for-sale

Available-for-sale ('AFS') investments are those not classified as another category of financial assets. These comprised equity investments in a quoted company. They may be sold in response to liquidity requirements or equity price movements. AFS investments are initially recognised at cost, which is considered as the fair value of the investment including any acquisition costs. AFS investments are subsequently measured at fair value in the statement of financial position. Fair value changes on the AFS securities are recognised in the statement of other comprehensive income and in equity (AFS reserve), until the investment is sold or impaired. Once sold or impaired, the cumulative gains or losses previously recognised in the AFS reserve are recycled to the income statement.

(d) Other financial liabilities

Other financial liabilities are non-derivative financial liabilities with fixed or determinable payments. Other financial liabilities are recognised when cash is received from the depositors. Other financial liabilities are carried at amortised cost using the effective interest method. The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the statement of financial position date.

1.9. Foreign currencies

Transactions in foreign currencies are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated into the Company's functional currency at the rates prevailing on the balance sheet date. Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in the income statement for the period.

1.10. Impairment of financial assets and loan commitments

Applicable from 1 January 2018 – IFRS 9 basis

The Group recognises loss allowances for ECLs on all financial assets carried at amortised cost, including lease receivables and loan commitments.

Credit loss allowances are measured as an amount equal to lifetime ECL, except for the following assets, for which they are measured as 12 month ECL:

- Financial assets determined to have low credit risk at the reporting date
- Financial assets which have not experienced a significant increase in credit risk since their initial recognition; and
- Financial assets which have experienced a significant increase in credit risk since their initial recognition but have subsequently met the Group's cure policy, as set out below.

Such assets are classified as stage 1 assets.

Assets which have experienced a significant increase in credit risk since their initial recognition and have not subsequently met the Group's cure policy are classified as stage 2 assets. The Group's definitions of a significant increase in credit risk and default are set out below.

A financial asset is considered to have low credit risk when its credit risk rating is equivalent to the widely understood definition of 'investment grade' assets. The Group has assessed all its debt securities, which represents UK Treasury bills, and loans held in STB Leasing Limited, for which credit risk is retained by its partner RentSmart, to be low credit risk.

Definition of default/credit impaired financial assets (Stage 3 loans)

At each reporting date, the Group assesses whether financial assets carried at amortised cost are credit impaired (stage 3). A financial asset is considered to be credit impaired when an event or events that have a detrimental impact on estimated future cash flows have occurred. Evidence that a financial asset is credit impaired includes the following observable data:

- Initiation of bankruptcy proceedings
- Notification of bereavement
- Identification of loan meeting debt sale criteria or
- Initiation of repossession proceedings.

In addition, a loan that is 90 days or more past due is considered credit impaired for all portfolios. The credit risk of financial assets that become credit impaired are not expected to improve such that they are no longer considered credit impaired.

For Commercial Finance facilities that do not have a fixed term or repayment structure, evidence that a financial asset is credit impaired includes:

- The client ceasing to trade; and
- Unpaid debtor balances that are dated at least 6 months past their normal recourse period.

Notes to the financial statements

Significant increase in credit risk (Stage 2 loans)

For Consumer Finance, the credit risk of a financial asset is considered to have experienced a significant increase in credit risk since initial recognition where there has been a significant increase in the remaining lifetime probability of default of the asset. The Group may also use its expert credit judgement and where possible relevant historical and current performance data, including bureau data, to determine that an exposure has undergone a significant increase in credit risk.

For Business Finance, the credit risk of a financial asset is considered to have experienced a significant increase in credit risk where certain early warning indicators apply. These indicators may include notification of county court judgements or, specifically for the Real Estate Finance portfolio, cost over-runs and timing delays experienced by borrowers.

As a backstop, the Group considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due for all portfolios.

Performing assets which have experienced a significant increase in credit risk since initial recognition are reclassified from stage 1, for which loss allowances are measured at an amount equal to 12 month ECL, to stage 2, for which ECL is measured as lifetime ECL.

Cure policy

The credit risk of a financial asset may improve such that it is no longer considered to have experienced a significant increase in credit risk if it meets the Group's cure policy. The Group's cure policy for all portfolios requires sufficient payments to be made to bring an account back within less than 30 days past due and for such payments to be maintained for six consecutive months.

The Group has determined stage 3 to be an absorbing state. Once a loan is in default it is not therefore expected to cure back to stage 1 or 2.

Calculation of expected credit loss

ECLs are probability weighted estimates of credit losses which are measured as the present value of all cash shortfalls. Specifically, this is the difference between the contractual cash flows due and the cash flows expected to be received, discounted at the original effective interest rate or, for portfolios purchased outside of the Group by Debt Managers (Services) Limited, the credit adjusted effective interest rate. For undrawn loan commitments ECL is measured as the difference between the contractual cash flows due if the commitment is drawn and the cash flows expected to be received.

Lifetime ECL is the ECL that results from all possible default events over the expected life of a financial asset.

12 month ECL is the portion of lifetime ECL that results from default events on a financial asset that are possible within 12 months after the reporting date.

ECLs are calculated by multiplying three main components; the probability of default ('PD'), exposure at default ('EAD') and loss given default ('LGD') discounted at the original effective interest rate of an asset. These variables are derived from internally developed statistical models and historical data, adjusted to reflect forward looking information and are discussed in turn further below. Management adjustments are made to modelled output to account for situations where known or expected risk factors have not been considered in the modelling process.

Notes to the financial statements

Probability of default (PD) and credit risk grades

Credit risk grades are a primary input into the determination of the PD for exposures. The Group allocates each exposure to a credit risk grade at origination and at each reporting period to predict the risk of default. Credit risk grades are determined using qualitative and quantitative factors that are indicative of the risk of default e.g. arrears status and loan applications scores. These factors vary for each loan portfolio. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. In monitoring exposures information such as payment records, request for forbearance strategies and forecast changes in economic conditions are considered for Consumer Finance. Additionally, for Business Finance information obtained during periodic client reviews, for example audited financial statements, management accounts, budgets and projections are considered, with particular focus on key ratios, compliance with covenants and changes in senior management teams.

Exogenous, Maturity, Vintage ('EMV') modelling is used in the production of forward looking lifetime PDs. This method entails modelling the effects of external (exogenous) factors against cohorts of lending and their time on the books creating a clean relationship to best demonstrate the movement in default rates as macroeconomic variables are changed. These models are extrapolated to provide PD estimates for the future, based on forecasted economic scenarios.

Exposure at default (EAD)

EAD represents the expected exposure in the event of a default. EAD is derived from the current exposure and potential changes to the current amount allowed under the terms of the contract, including amortisation overpayments and early terminations. The EAD of a financial asset is its gross carrying amount. For loan commitments the EAD includes the amount drawn as well as potential future amounts that may be drawn under the terms of the contract, estimated based on historical observations and forward looking forecasts.

For Commercial Finance facilities that have no specific term, an assumption is made that accounts close 36 months after the reporting date for the purposes of measuring lifetime ECL. This assumption is based on industry experience of average client life. These facilities do not have a fixed term or repayment structure but are revolving and increase or decrease to reflect the value of the collateral i.e. receivables or inventory. The Group can cancel the facilities with immediate effect, although this contractual right is not enforced in the normal day to day management of the facility. Typically, demand would only be made on failure of a client business or in the event of a material event of default, such as a fraud. In the normal course of events, the Group's exposure is recovered through receipt of remittances from the client's debtors rather than from the client itself.

The ECL for such facilities is estimated taking into account the credit risk management actions that the Group expects to take to mitigate against losses. These include a reduction in advance rate and facility limits or application of reserves against a facility so as to improve the likelihood of full recovery of exposure from the debtors. Alternative recovery routes mitigating ECL would include refinance by another funding provider, taking security over other asset classes or secured personal guarantees from the client's principals.

Loss given default (LGD)

LGD is the magnitude of the likely loss in the event of default. This takes into account recoveries either through curing or, where applicable, through auction sale of repossessed collateral and debt sale of the residual shortfall amount. For loans secured by retail property, loan-to-value ratios are key parameters in determining LGD. LGDs are calculated on a discounted cash flow basis using the financial instrument's origination effective interest rate as the discount factor.

Incorporation of forward looking data

The Group incorporates forward looking information into both its assessment of whether the credit risk of a financial asset has increased significantly since initial recognition and its measurement of expected credit loss. This is achieved by developing a number of potential economic scenarios and modelling expected credit losses for each scenario. To ensure material non-linear relationships between economic factors and credit losses are reflected in the calculation of ECL a deeper stress scenario is used as one of these scenarios. The outputs from each scenario are combined using the estimated likelihood of each scenario occurring to derive a probability weighted expected credit loss. The four scenarios adopted and probability weighting applied are approved by the Assumptions Committee and are set out in Note 2.

The Group has considered which economic variables impact credit risk and credit losses. The key drivers of credit risk and credit losses included in the macroeconomic scenarios for all portfolios, with the exception of Real Estate Finance, have been identified as annual unemployment rate growth and annual house price index growth. In addition, for Asset Finance and Commercial Finance, changes to the consumer price index are also included in the macro economic scenarios. For the Real Estate Finance portfolio the key drivers have been identified as unemployment rate growth and Bank of England base rates. Base case assumptions applied for each of these variables, with the exception of the annual house price index growth, have been sourced from external consensus forecasts. The annual house price index is assumed to increase 2% per annum until December 2021 and 4% thereafter. Further details of the assumptions applied to other scenarios is presented in Note 2.

Presentation of loss allowance

Loss allowances for ECL are presented in the statement of financial position as follows with the loss recognised in the statement of comprehensive income:

- Financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets.
- Other loan commitments: generally, as a provision.

For the Real Estate Finance and Commercial Finance portfolios, where a loan facility is agreed that includes both drawn and undrawn elements and the Group cannot identify the ECL on the loan commitment separately, a combined loss allowance for both drawn and undrawn components of the loan is presented as a deduction from the gross carrying amount of the drawn component, with any excess of the loss allowance over the gross drawn amount presented as a provision.

A customer's account may be modified to assist customers who are in or have recently overcome financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. Where the terms of a financial asset have been modified and the modification has not resulted in derecognition, the expected cash flows arising from the modified financial asset are included in calculating any cash shortfalls from the existing asset. Any change in the carrying value of the modified asset would be recognised immediately in the income statement.

When a loan is uncollectible, it is written off against the related ECL allowance. Such loans are written off after all necessary procedures have been completed and the amount of the loss has been determined.

Motor voluntary termination provision

In addition to recognising allowances for ECLs the Group holds a provision for voluntary terminations ('VT') for all Motor Finance financial assets. VT is a legal right provided to customers who take out hire purchase agreements. The provision is calculated by multiplying the probability of VT of an asset by the expected shortfall on VT discounted back at the original effective interest rate of the asset. VT allowances are not held against loans in default (stage 3 loans).

The VT provision is presented in the statement of financial position as a deduction from the gross carrying amount of Motor Finance assets with the loss recognised in the statement of comprehensive income.

Applicable prior to 1 January 2018 – IAS 39 basis

Assets carried at amortised cost

On an ongoing basis the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence is the occurrence of a loss event, after the initial recognition of the asset, that impacts on the estimated future cash flows of the financial asset or group of financial assets, and can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include, but are not limited to, the following:

- Delinquency in contractual payments of principal or interest;
- Breach of financial covenants or contractual obligations;
- Cash flow difficulties experienced by the borrower; and
- Initiation of bankruptcy proceedings.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

The Group considers evidence of impairment for loans and advances at both an individual asset and collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. In assessing collective impairment the Group uses historical trends of the probability of default, emergence period, the timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be significantly different to historic trends.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

Business Finance

In assessing objective evidence of a loss event for business loans, the following factors are considered:

- If any contractual repayment date has been missed;
- Covenant breaches; and
- In Commercial Finance, a loan may be considered for potential impairment if the financial prospects of the borrower's customers deteriorates.

Consumer Finance

For Consumer loans, cash flows are estimated based on past experience combined with the Group's view of the future considering the following factors:

- The Group's exposure to the customer;
- Based on the number of days in arrears at the statement of financial position date, the likelihood that a loan will progress through the various stages of delinquency and ultimately be written off; and
- The amount and timing of expected receipts and recoveries.

Modification of loans

A customer's account may be modified to assist customers who are in or have recently overcome financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. Loans that have renegotiated or deferred terms, resulting in a substantial modification to the cash flows, are no longer considered to be past due but are treated as new loans recognised at fair value, provided the customers comply with the renegotiated or deferred terms.

1.11. Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of the acquisition over the fair value of the Group's share of the net identifiable assets acquired at the date of acquisition. Goodwill is held at cost less accumulated impairment losses and is deemed to have an infinite life.

The Group reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. Impairment losses are recognised in the income statement if the carrying amount exceeds the recoverable amounts.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software.

Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred unless the technical feasibility of the development has been demonstrated, and it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance, in which case they are capitalised.

These costs are amortised on the basis of the expected useful lives, which are between three to ten years.

(c) Other intangibles

The acquisition of subsidiaries was accounted for in accordance with IFRS 3 'Business Combinations', which requires the recognition of the identifiable assets acquired and liabilities assumed at their acquisition date fair values. As part of this process, it was necessary to recognise certain intangible assets which are separately identifiable and which are not included on the acquiree's balance sheet, which are amortised over their expected useful lives, as set out in Note 16.

1.12. Property, plant and equipment

Property is held at its revalued amount, being its fair value at the date of valuation less any subsequent accumulated depreciation. Revaluations are carried out annually at the reporting date, and movements are recognised in Other Comprehensive Income, net of any applicable deferred tax.

Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Pre-installed computer software licences are capitalised as part of the computer hardware it is installed on. Depreciation is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, which are subject to regular review:

Land	not depreciated
Freehold buildings	50 years
Leasehold improvements	shorter of life of lease or 7 years
Computer equipment	3 to 5 years
Other equipment	5 to 10 years

Gains and losses on disposals are determined by comparing proceeds with carrying amounts. These are included in the income statement.

1.13. Leases

(a) As a lessor

Assets leased to customers under agreements which transfer substantially all the risks and rewards of ownership, with or without ultimate legal title, are classified as finance leases. When assets are held subject to finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

(b) As a lessee

Rentals made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease.

1.14. Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise cash in hand and demand deposits, and cash equivalents comprise highly liquid investments which are convertible into cash with an insignificant risk of changes in value with a maturity of three months or less at the date of acquisition, including certain loans and advances to banks and short-term highly liquid debt securities.

1.15. Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issuance costs. Any amounts received over nominal value are recorded in the share premium account, net of direct issuance costs. Costs associated with the listing of shares are expensed immediately.

Notes to the financial statements

1.16. Employee benefits

(a) Post-retirement obligations

The Group contributes to defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees. The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. There are no post-retirement benefits other than pensions.

(b) Share-based compensation

The fair value of equity settled share-based payment awards are calculated at grant date and recognised over the period in which the employees become unconditionally entitled to the awards (the vesting period). The amount is recognised as personnel expenses in the income statement, with a corresponding increase in equity. Further details of the valuation methodology is set out in Note 27.

The fair value of cash settled share-based payments is recognised as personnel expenses in the income statement with a corresponding increase in liabilities over the vesting period. The liability is remeasured at each reporting date and at settlement date based on the fair value of the options granted, with a corresponding adjustment to personnel expenses.

1.17. Taxation

Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise.

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the statement of financial position date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, when they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

1.18. Dividends

Final dividends on ordinary shares are recognised in equity in the period in which they are approved by Shareholders. Interim dividends on ordinary shares are recognised in equity in the period in which they are paid.

2. Critical accounting judgements and key sources of estimation uncertainty

2.1 Judgements

No critical judgements have been identified.

2.2 Key sources of estimation uncertainty

Estimations which could have a material impact on the Group's financial results and are therefore considered to be key sources of estimation uncertainty are outlined below.

2.2.1 Impairment losses on loans and advances to customers

As discussed in Note 1.10 ECLs are calculated by multiplying three main components: the PD, EAD and LGD. These variables are derived from internally developed statistical models and historical data, adjusted to reflect forward looking information. The determination of both the PD and LGD require estimation which is discussed further below.

2.2.2 Probability of default (PD)

As set out in Note 1.10 Exogenous, Maturity, Vintage (EMV) modelling is used in the production of forward looking lifetime PDs in the calculation of ECLs. As the Group's performance data does not go back far enough to capture a full economic cycle, the proxy series of the quarterly rates of write offs for UK unsecured lending data is used to build an economic response model ('ERM') to incorporate the effects of recession.

The portfolios for which external benchmark information represents a significant input into the measurement of ECL are Real Estate Finance, Asset Finance and Commercial Finance. The benchmarks used for all three portfolios are Standard & Poor's Ratings and Bank of England UK Possessions as proxy data for ERM.

With the exception of the Motor Finance portfolio, sensitivity to reasonably possible changes in PD is not considered to result in material changes in the ECL allowance. The Motor Finance portfolio has seen improvements in PD since implementation of IFRS 9 due to the Group's move away from writing subprime Motor loans in January 2017 and improvements in the collections process. During the year the Motor Finance PD reduced by 9.6% resulting in an £2.3 million reduction in ECL. A 10% change in the PD for Motor Finance would impact the ECL allowance by £1.8 million.

The composition of the Retail Finance portfolio remains stable with minimal movement in PDs and the ECL allowance held for the Business Finance, Consumer Mortgages and Other portfolios remains low. Reasonably possible changes in the PD for these portfolios are not considered to result in a material change in the ECL allowance.

2.2.3 Loss given default (LGD)

The Group's policy for the determination of LGD is outlined in Note 1.10.

With the exception of the Motor Finance portfolio, the sensitivity of the ECL allowance to reasonably possible changes in the LGD is not considered material. For the Motor Finance portfolio a 10% change in the LGD is considered reasonably possible due to historic data showing movements in vehicle collection rates once a loan is in repossession stage. A 10% change in the vehicle recovery rate assumption element of the LGD for Motor Finance would impact the ECL allowance by £1.6 million. Vehicle collection rates and proceeds received on sale of vehicles at auction remained broadly stable over 2018, and therefore there was no material change to ECL as a result of LGD changes.

Notes to the financial statements

2.2.4 Incorporation of forward looking data

The Group incorporates forward looking information into both its assessment of whether the credit risk of a financial asset has increased significantly since initial recognition and its measurement of expected credit loss by developing a number of potential economic scenarios and modelling expected credit losses for each scenario. Further detail on this process is provided in Note 1.10. Whilst not material and therefore not required by IAS 1, the Group has included the disclosure below as it is considered useful to readers of the Annual Report and Accounts.

The macro economic scenarios and weightings applied on adoption of IFRS 9 on 1 January 2018 and at 31 December 2018 are summarised below:

Scenario	Derivation	Weighting 31 December 2018	Weighting 1 January 2018
Base case	Derived from external consensus forecasts and used in the Group's strategic planning and budgeting processes.	65%	80%
Benign case	Assumes macroeconomic variables will move with a more positive trajectory than the base case.	10%	5%
Stressed case	Management's assessment, based on historic data, of an adverse scenario that could occur once every 7 to 8 years.	20%	10%
Deeper stress	Based on the scenario used by the PRA for the H1 2018 ICAAP. This can be found on the Bank of England's website: www.bankofengland.co.uk	5%	5%

Weightings applied to the macro economic scenarios were reviewed at the October 2018 Assumptions Committee and reconfirmed at the January 2019 Assumptions Committee. After taking into consideration current economic conditions and emerging industry practice it was agreed to revise the weightings applied. The impact of this change was £0.4 million increase to the Group's ECL.

The sensitivity of the ECL allowance to reasonably possible changes in macro-economic scenario weighting is presented below:

	Increase in stressed case weighting by 5% and reduction in base case £million	Increase in deeper stress case weighting by 5% and reduction in base case £million
Motor Finance	0.1	0.3
Retail Finance	0.1	0.8

The sensitivity of other portfolios to reasonably possible changes in macro-economic scenario weightings is not considered material.

Notes to the financial statements

3. Operating segments

The Group is organised into seven operating segments, which consist of the different products available, disclosed below:

Business Finance

1) Real Estate Finance: residential and commercial investment and development loans secured by UK real estate.
2) Asset Finance: loans to small and medium sized enterprises to acquire commercial assets.
3) Commercial Finance: invoice discounting and invoice factoring.

Consumer Finance

4) Motor Finance: hire purchase agreements secured against the vehicle being financed.
5) Retail Finance: point of sale unsecured finance for in-store and online retailers.
6) Debt Management: debt collection.

Consumer Mortgages

7) Residential mortgages for the self-employed, contract workers, those with complex income and those with a recently restored credit history, sold via select mortgage intermediaries.

Other

Other includes principally OneBill and RentSmart. OneBill has been closed to new customers since 2009.

Discontinued operations

Personal Lending: Unsecured consumer loans sold to customers via broker aggregators and business partners.

Currently, the Debt Management and Consumer Mortgages segments both fall below the quantitative threshold for separate disclosure, but the directors consider that they represent sufficiently distinct types of business to merit separate disclosure. The prior year figures have been restated accordingly, in order to separately disclose Debt Management.

Management review these segments by looking at the income, size and growth rate of the loan books, impairments and customer numbers. Except for these items no costs or balance sheet items are allocated to the segments.

	Interest income and similar income	Fee and commission income	Revenue from external customers	Net impairment losses on loans and advances to customers	Loans and advances to customers
	£million	£million	£million	£million	£million
31 December 2018					
Business Finance					
Real Estate Finance	41.1	0.1	**41.2**	0.5	**769.8**
Asset Finance	6.6	-	**6.6**	2.2	**62.8**
Commercial Finance	5.5	7.9	**13.4**	-	**194.7**
Consumer Finance					
Retail Finance	58.7	4.1	**62.8**	19.3	**597.0**
Motor Finance	47.4	1.1	**48.5**	11.3	**276.4**
Debt Management	6.1	0.9	**7.0**	-	**32.3**
Consumer Mortgages	1.5	-	**1.5**	0.2	**84.7**
Other	2.3	5.3	**7.6**	(1.1)	**11.2**
	169.2	**19.4**	**188.6**	**32.4**	**2,028.9**

Notes to the financial statements

	Interest income and similar income £million	Fee and commission income £million	Revenue from external customers £million	Net impairment losses on loans and advances to customers £million	Loans and advances to customers £million
31 December 2017					
Business Finance					
Real Estate Finance	32.1	0.2	**32.3**	(0.2)	**580.8**
Asset Finance	8.5	-	**8.5**	1.0	**116.7**
Commercial Finance	2.5	4.7	**7.2**	0.1	**126.5**
Consumer Finance					
Retail Finance	47.5	3.2	**50.7**	13.8	**452.3**
Motor Finance	46.2	0.9	**47.1**	20.8	**274.6**
Debt Management	3.3	1.6	**4.9**	-	**15.6**
Consumer Mortgages	0.1	-	**0.1**	-	**16.5**
Other	1.1	5.4	**6.5**	(2.0)	**15.3**
Continuing operations	141.3	16.0	**157.3**	33.5	**1,598.3**
Discontinued operations					
Personal Lending	8.0	-	**8.0**	3.4	-
	149.3	**16.0**	**165.3**	**36.9**	**1,598.3**

The 'other' segment above includes products which are individually below the quantitative threshold for separate disclosure and fulfils the requirement of IFRS 8.28 by reconciling operating segments to the amounts reported in the financial statements.

Funding costs and operating expenses are not aligned to operating segments for day to day management of the business, so they cannot be allocated on a reliable basis. Accordingly, profit by operating segment has not been disclosed.

All of the Group's operations are conducted wholly within the United Kingdom and geographical information is therefore not presented.

Notes to the financial statements

4. Operating income

4.1 Net interest income

	2018 £million	2017 £million
Loans and advances to customers	167.4	140.7
Cash and balances at central banks	1.0	0.4
Debt securities	0.8	-
Loans and advances to banks	-	0.2
Interest income and similar income	**169.2**	**141.3**
Deposits from customers	(32.8)	(26.7)
Due to banks	(1.5)	-
Subordinated liabilities	(1.2)	-
Interest expense and similar charges	**(35.5)**	**(26.7)**
Net interest income	**133.7**	**114.6**

The net interest income shown above excludes £8.0 million in 2017 of interest on loans and advances to customers in respect of discontinued operations, as shown in the income statement as set out on page 134.

4.2 Net fee and commission income

	2018 £million	2017 £million
Fee and disbursement income	16.3	12.4
Commission income	2.0	2.7
Other income	1.1	0.9
Fee and commission income	**19.4**	**16.0**
Other expenses	(1.5)	(1.1)
Fee and commission expense	**(1.5)**	**(1.1)**
Net fee and commission income	**17.9**	**14.9**

Fees and commissions income consists principally of the following:

- weekly and monthly fees from the OneBill product
- associated insurance commissions and commissions earned on debt collection activities in DMS
- discounting, service and arrangement fees in Commercial Finance, and
- account management and administration fees from retailers in Retail Finance.

Fee and commission expenses consist primarily of fees payable in respect of Motor Finance.

5. Operating expenses

	Total 2018 £million	Continuing 2017 £million	Discontinued 2017 £million	Total 2017 £million
Staff costs, including those of directors:				
Wages and salaries	39.1	33.8	0.3	34.1
Social security costs	6.0	4.2	-	4.2
Pension costs	1.4	1.2	-	1.2
Share based payment transactions	0.8	(0.2)	-	(0.2)
Depreciation of property, plant and equipment (Note 15)	1.3	0.8	-	0.8
Amortisation of intangible assets (Note 16)	1.8	2.0	-	2.0
Operating lease rentals	1.7	1.5	-	1.5
Other administrative expenses	32.4	28.0	-	28.0
Total operating expenses	**84.5**	**71.3**	**0.3**	**71.6**

As described in Note 3, operating expenses are not aligned to operating segments for day-to-day management of the business, so they cannot be allocated on a reliable basis. Accordingly, discontinued operating expenses above relates only to those costs that are directly attributable to the discontinued business.

Remuneration of the auditor and its associates, excluding VAT, was as follows:

	2018 £'000	2017 £'000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	233	270
Fees payable to the Company's auditor for other services:		
The audit of the Company's subsidiaries, pursuant to legislation	37	68
Audit related assurance services	-	100
Other assurance services	95	62
All other non-audit services	140	39
	505	**539**

Other assurance services related to the half year review.

All other non-audit services related to profit certification, accounting opinion relating to the issue of the subordinated liabilities, recovery plan support, review of share scheme documentation and Financial Services Compensation Scheme reporting health check (2017: profit certification, work relating to entry into the Term Funding Scheme and advice on a potential corporate acquisition).

Notes to the financial statements

6. Average number of employees

	2018 Number	2017 Number
Directors	7	8
Management	88	116
Administration	766	610
	861	**734**

During the year, the Group updated its grading and pay structure. The analysis above is therefore not directly comparable between 2017 and 2018.

7. Income tax expense

	Total 2018 £million	Continuing operations 2017 £million	Discontinued operations 2017 £million	Total 2017 £million
Current taxation				
Corporation tax charge - current year	7.3	5.5	0.8	6.3
Corporation tax charge - adjustments in respect of prior years	0.3	-	-	-
	7.6	**5.5**	**0.8**	**6.3**
Deferred taxation				
Deferred tax charge - current year	(1.0)	(0.5)	-	(0.5)
Deferred tax charge - adjustments in respect of prior years	(0.2)	0.1	-	0.1
	(1.2)	**(0.4)**	**-**	**(0.4)**
Income tax expense	**6.4**	**5.1**	**0.8**	**5.9**
Tax reconciliation				
Profit before tax	34.7	25.0	4.3	29.3
Tax at 19.00% (2017: 19.25%)	6.6	4.8	0.8	5.6
Permanent differences	-	0.2	-	0.2
Banking surcharge	0.3	-	-	-
Rate change on deferred tax assets	(0.6)	-	-	-
Prior period adjustments	0.1	0.1	-	0.1
Income tax expense for the year	**6.4**	**5.1**	**0.8**	**5.9**

The Government substantively enacted a reduction in the main rate of UK corporation tax from 20% to 19% (effective from 1 April 2017) and a further reduction to 17% (effective 1 April 2020). The Government also introduced an 8% surcharge on the profits of banking companies in excess of £25 million effective from 1 January 2016 that is reflected in the 2018 tax charge and reconciliation.

Notes to the financial statements

8. Earnings per ordinary share

8.1 Basic

Basic earnings per ordinary share are calculated by dividing the profit attributable to equity holders of the parent by the weighted average number of ordinary shares as follows:

	2018	2017
Profit attributable to equity holders of the parent (£ millions)		
Continuing operations	28.3	19.9
Discontinued operations	-	3.9
	28.3	**23.8**
Weighted average number of ordinary shares (number)	**18,475,229**	**18,475,229**
Earnings per share (pence)		
Continuing operations	153.2	107.7
Discontinued operations	-	21.1
	153.2	**128.8**

8.2 Diluted

Diluted earnings per ordinary share are calculated by dividing the profit attributable to equity holders of the parent by the weighted average number of ordinary shares in issue during the year, as noted above, as well as the number of dilutive share options in issue during the year, as follows:

	2018	2017
Weighted average number of ordinary shares	18,475,229	18,475,229
Number of dilutive shares in issue at the year end	277,234	219,007
Fully diluted weighted average number of ordinary shares	18,752,463	18,694,236
Dilutive shares being based on:		
Number of options outstanding at the year end	511,706	368,063
Weighted average exercise price (pence)	678	799
Average share price during the period (pence)	1,489	1,974
Diluted earnings per share (pence)		
Continuing operations	150.9	106.4
Discontinued operations	-	20.9
	150.9	**127.3**

9. Dividends

	2018	2017
	£'000	£'000
2016 final dividend - 58 pence per share (paid May 2017)	-	10.7
2017 interim dividend – 18 pence per share (paid September 2017)	-	3.3
2017 final dividend – 61 pence per share (paid May 2018)	11.3	-
2018 interim dividend – 19 pence per share (paid September 2018)	3.5	-
	14.8	**14.0**

The directors recommend the payment of a final dividend of 64 pence per share which, together with the interim dividend of 19 pence per share paid on 28 September 2018, represents total dividends for the year of 83 pence per share (2017: 79 pence per share). The final dividend, if approved by members at the Annual General Meeting, will be paid on 24 May 2019 to shareholders on the register at the close of business on 26 April 2019.

10. Loans and advances to banks

	Group	Group	Company	Company
	2018	2017	2018	2017
	£million	£million	£million	£million
Placements with banks included in cash and cash equivalents (Note 28)	44.8	34.3	41.9	32.3

Moody's long-term ratings are as follows:

	Group	Group	Company	Company
	2018	2017	2018	2017
	£million	£million	£million	£million
A1	11.2	6.1	11.1	6.0
A1*/A2	28.6	-	25.8	-
A3	-	23.2	-	21.3
Arbuthnot Latham & Co., Limited - No rating	5.0	5.0	5.0	5.0
	44.8	**34.3**	**41.9**	**32.3**

None of the loans and advances to banks are either past due or impaired.

11. Loans and advances to customers

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Gross loans and advances	2,096.0	1,638.2	2,048.9	1,605.4
Less: allowances for impairment on loans and advances (Note 13)	(67.1)	(39.9)	(68.6)	(39.9)
	2,028.9	**1,598.3**	**1,980.3**	**1,565.5**

The fair value of loans and advances to customers is shown in Note 35. For a maturity profile of loans and advances to customers, refer to Note 34.

Group and Company

At 31 December 2018 loans and advances to customers of £326.5 million (2017: £200.7 million) were pre-positioned under the Bank of England's Term Funding Scheme, and were available for use as collateral within the scheme.

The following loans are secured upon real estate:

	2018 Loan balance £million	2018 Loan-to-value %	2017 Loan balance £million	2017 Loan-to-value %
Real Estate Finance	769.8	57%	580.8	57%
Consumer Mortgages	84.7	59%	16.5	59%
	854.5		**597.3**	

Under its credit policy, the Real Estate Finance business lends to a maximum loan-to-value of 70% for investment loans and 60% for residential development loans and up to 65% for pre-let commercial development loans (based on gross development value), and the Consumer Mortgages business lends to a maximum of 90%.

None of these loans are impaired. All property valuations at loan inception, and the majority of development stage valuations, are performed by independent Chartered Surveyors, who perform their work in accordance with the Royal Institution of Chartered Surveyors Valuation – Professional Standards.

Group

£1.9 million (2017: £2.5 million) of collateral is held from RentSmart, against loans of £10.8 million (2017: £14.9 million). This collateral is included in trade payables at 31 December 2018. This is based upon the balance of customer receivables and expected new agreements during the following month.

12. Finance lease receivables

Loans and advances to customers include finance lease receivables as follows:

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Gross investment in finance lease receivables:				
- No later than 1 year	175.3	189.9	168.7	180.7
- Later than 1 year and no later than 5 years	326.9	374.2	322.0	367.7
- Later than 5 years	0.2	1.2	0.2	1.2
	502.4	565.3	490.9	549.6
Unearned future finance income on finance leases	(135.8)	(162.5)	(132.8)	(158.4)
Net investment in finance leases	**366.6**	**402.8**	**358.1**	**391.2**
The net investment in finance leases may be analysed as follows:				
- No later than 1 year	112.0	117.5	107.6	111.3
- Later than 1 year and no later than 5 years	254.4	284.2	250.3	278.8
- Later than 5 years	0.2	1.1	0.2	1.1
	366.6	**402.8**	**358.1**	**391.2**

13. Allowances for impairment of loans and advances

Group

	Not credit impaired Stage 1: Subject to 12 month ECL	Stage 2: Subject to lifetime ECL	Credit impaired Stage 3: Subject to lifetime ECL	Total provision	Gross loans and receivables	Provision cover
	£million	£million	£million	£million	£million	%
31 December 2018						
Business Finance:						
Real Estate Finance	0.6	-	-	0.6	770.4	0.1%
Asset Finance	0.2	0.1	2.7	3.0	65.8	4.6%
Commercial Finance	0.2	0.2	0.4	0.8	195.5	0.4%
Consumer Finance:						
Retail Finance	8.9	9.8	4.3	23.0	620.0	3.7%
Motor Finance:						
Voluntary termination provision	6.0	-	-	6.0		
Other impairment	4.2	13.8	15.4	33.4		
	10.2	13.8	15.4	39.4	315.8	12.5%
Debt Management	-	-	-	-	32.3	0.0%
Consumer Mortgages	0.2	-	-	0.2	84.9	0.2%
Other	-	-	0.1	0.1	11.3	0.9%
	20.3	**23.9**	**22.9**	**67.1**	**2,096.0**	**3.2%**

Total provisions above include expert credit judgements over the Group's IFRS 9 model results of £2.0 million, of which £1.4 million are specific overlays held against credit impaired secured assets held within the Business Finance portfolio. These specific overlays have been estimated on an individual basis by assessing the recoverability and condition of the secured asset, along with any other recoveries that may be made. The remaining £0.6 million primarily relates to the estimated impact of planned enhancements to LGD elements of the models of £0.8 million, offset by a net decrease in the ECL due to management judgements in respect of the PD elements of the models.

Within this Note, provision charges and balances in respect of 2018 are prepared on an IFRS 9 basis. In accordance with the transitional provisions of the standard comparatives set out in the tables below have not been restated. Refer to Notes 1 and 38 for further information.

	Individual provision £million	Collective provision £million	Total provision £million	Gross loans and receivables £million	Provision cover %
31 December 2017 (IAS 39 basis)					
Business Finance					
Real Estate Finance	-	0.3	0.3	581.1	0.1%
Asset Finance	1.0	0.2	1.2	117.9	1.0%
Commercial Finance	0.4	0.2	0.6	127.1	0.5%
Consumer finance					
Retail Finance	6.5	1.1	7.6	459.9	1.7%
Motor Finance					
Voluntary termination provision	1.0	-	1.0		
Other impairment	23.3	2.6	25.9		
	24.3	2.6	26.9	301.5	8.9%
Debt Management	-	-	-	15.6	0.0%
Consumer Mortgages	-	-	-	16.5	0.0%
Other	3.3	-	3.3	18.6	17.7%
	35.5	**4.4**	**39.9**	**1,638.2**	**2.4%**

Provisions included in 'Other' are in respect of various legacy products. This segment also includes loans of £10.8 million (2017: £14.9 million) held in STB Leasing Limited. The credit risk associated with those loans is retained by its partner, RentSmart. Accordingly, no provision is held against the RentSmart loans.

The impairment losses disclosed in the income statement, for continuing operations, can be analysed as follows:

	2018 (IFRS 9) £million	2017 (IAS 39) £million
IFRS 9 ECL/ IAS 39 incurred loss individual provision: charge for impairment losses	30.4	36.4
IAS 39 incurred loss collective provision: charge for impairment losses	-	(0.4)
Loans written off, net of amounts utilised	4.3	1.4
Recoveries of loans written off	(2.3)	(0.5)
	32.4	36.9
Less Personal Lending	-	(3.4)
	32.4	**33.5**

Reconciliations of the opening to closing impairment allowance for losses on loans and advances are presented below:

	Not credit impaired Stage 1: Subject to 12 month ECL £million	Stage 2: Subject to lifetime ECL £million	Credit impaired Stage 3: Subject to lifetime ECL £million	Total £million
At 1 January 2018	18.9	24.9	27.9	71.7
Increase/(decrease)due to change in credit risk				
- Transfer to stage 2	(6.3)	33.0	-	26.7
- Transfer to stage 3	(0.1)	(23.4)	30.8	7.3
- Transfer to stage 1	1.5	(3.2)	-	(1.7)
Passage of time	(6.7)	(1.7)	(3.9)	(12.3)
New loans originated	17.4	-	-	17.4
Derecognised loans	(1.8)	(4.0)	-	(5.8)
Changes to model methodology	(1.3)	(0.2)	-	(1.5)
Changes to credit risk parameters	(1.2)	(1.5)	0.6	(2.1)
Other adjustments	2.4	-	-	2.4
Charge to income statement	3.9	(1.0)	27.5	30.4
Allowance utilised in respect of write offs	(2.5)	-	(32.5)	(35.0)
31 December 2018	**20.3**	**23.9**	**22.9**	**67.1**

Passage of time represents the impact of accounts maturing through their contractual life and the associated reduction in PDs. For stage 3 assets it represents the unwind of the discount applied in calculating the ECL.
Changes to model methodology represents movements that have occurred due to enhancements made to the models during the year.
Changes to credit risk parameters represents movements that have occurred due to the Group updating model inputs. This would include the impact of, for example, updating the macro economic scenarios applied to the models.
Other adjustments represents the movement in the Motor voluntary termination provision.

The table above has been prepared based on monthly movements in the ECL. Stage 1 write offs arise on Motor accounts that have exercised their right to voluntarily terminate their agreements.

	£million
31 December 2017 (IAS 39 basis)	
Individual allowances for impairment	
At 1 January	23.1
Charge for impairment losses	36.4
Amounts utilised	(13.5)
Changes to presentation in respect of debt sales	(3.6)
Sale of personal lending	(6.9)
At 31 December	**35.5**
Collective allowances for impairment	
At 1 January	5.3
Charge for impairment losses	(0.4)
Sale of personal lending	(0.5)
At 31 December	**4.4**
Total allowances for impairment	**39.9**

Notes to the financial statements

Interest income on loans classified as impaired totalled £2.0 million (2017: £2.6 million).

Company

	Not credit impaired Stage 1: Subject to 12 month ECL £million	Stage 2: Subject to lifetime ECL £million	Credit impaired Stage 3: Subject to lifetime ECL £million	Total provision £million	Gross loans and receivables £million	Provision cover %
31 December 2018						
Business Finance:						
Real Estate Finance	0.6	-	-	0.6	770.4	0.1%
Asset Finance	0.2	0.1	2.7	3.0	65.8	4.6%
Commercial Finance	0.2	0.2	0.4	0.8	191.4	0.4%
Consumer Finance:						
Retail Finance	9.2	9.8	4.4	23.4	620.0	3.8%
Motor Finance:						
Voluntary termination provision	6.0	-	-	6.0		
Other impairment	4.3	14.2	16.0	34.5		
	10.3	14.2	16.0	40.5	315.8	12.8%
Consumer Mortgages	0.2	-	-	0.2	84.9	0.2%
Other	-	-	0.1	0.1	0.6	16.7%
	20.7	**24.3**	**23.6**	**68.6**	**2,048.9**	**3.3%**

Total provisions above include expert credit judgements over the Group's IFRS 9 model results of £2.0 million, of which £1.4 million are specific overlays held against credit impaired secured assets held within the Business Finance portfolio. These specific overlays have been estimated on an individual basis by assessing the recoverability and condition of the secured asset, along with any other recoveries that may be made. The remaining £0.6 million primarily relates to the estimated impact of planned enhancements to LGD elements of the models of £0.8 million, offset by a net decrease in the ECL due to management judgements in respect of the PD elements of the models.

	Individual provision £million	Collective provision £million	Total provision £million	Gross loans and receivables £million	Provision cover %
31 December 2017 (IAS 39 basis)					
Business Finance					
Real Estate Finance	-	0.3	0.3	581.1	0.1%
Asset Finance	1.0	0.2	1.2	117.9	1.0%
Commercial Finance	0.4	0.2	0.6	124.8	0.5%
Consumer Finance					
Retail Finance	6.5	1.1	7.6	459.9	1.7%
Motor Finance					
Voluntary termination provision	1.0	-	1.0		
Other impairment	23.3	2.6	25.9		
	24.3	2.6	26.9	301.5	8.9%
Consumer Mortgages	-	-	-	16.5	0.0%
Other	3.3	-	3.3	3.7	89.2%
	35.5	**4.4**	**39.9**	**1,605.4**	**2.5%**

Notes to the financial statements

The impairment losses disclosed in the income statement, for continuing operations, can be analysed as follows:

	2018 (IFRS 9) £million	2017 (IAS 39) £million
IFRS 9 ECL/ IAS 39 incurred loss individual provision: charge for impairment losses	33.9	38.8
IFRS 9 impairment losses in respect of off balance sheet loan commitments	0.1	-
IAS 39 incurred loss collective provision: charge for impairment losses	-	(0.4)
Loans written off, net of amounts utilised	1.7	1.4
Recoveries of loans written off	(2.4)	(0.5)
Profit on sale of debt	(0.2)	(0.3)
	33.1	39.0
Less Personal Lending	-	(3.4)
	33.1	**35.6**

Reconciliations of the opening to closing impairment allowance for losses on loans and advances are presented below:

	Not credit impaired Stage 1: Subject to 12 month ECL £million	Stage 2: Subject to lifetime ECL £million	Credit impaired Stage 3: Subject to lifetime ECL £million	Total £million
At 1 January 2018	19.0	25.1	28.2	72.3
Increase/(decrease)due to change in credit risk				
- Transfer to stage 2	(6.5)	33.9	-	27.4
- Transfer to stage 3	(0.1)	(24.0)	31.6	7.5
- Transfer to stage 1	1.5	(3.2)	-	(1.7)
Passage of time	(6.7)	(1.6)	(4.6)	(12.9)
New loans originated	17.9	-	-	17.9
Derecognised loans	(1.8)	(4.1)	2.8	(3.1)
Changes to model methodology	(1.3)	(0.2)	-	(1.5)
Changes to credit risk parameters	(1.2)	(1.5)	0.6	(2.1)
Other adjustments	2.4	-	-	2.4
Charge to income statement	4.2	(0.7)	30.4	33.9
Allowance utilised in respect of write offs	(2.5)	(0.1)	(35.0)	(37.6)
31 December 2018	**20.7**	**24.3**	**23.6**	**68.6**

Passage of time represents the impact of accounts maturing through their contractual life and the associated reduction in PDs. For stage 3 assets it represents the unwind of the discount applied in calculating the ECL.
Changes to model methodology represents movements that have occurred due to enhancements made to the models during the year.
Changes to credit risk parameters represents movements that have occurred due to the Group updating model inputs. This would include the impact of, for example, updating the macro economic scenarios applied to the models.
Other adjustments represents the movement in the Motor voluntary termination provision.

The table above has been prepared based on monthly movements in the ECL. Stage 1 write offs arise on Motor accounts that have exercised their right to voluntarily terminate their agreements.

	£million
31 December 2017 (IAS 39 basis)	
Individual allowances for impairment	
At 1 January	22.4
Charge for impairment losses	38.8
Utilised	(13.5)
Release of allowance for impairment on the sale of debt	(5.3)
Sale of personal lending	(6.9)
At 31 December	**35.5**
Collective allowances for impairment	
At 1 January	5.3
Charge for impairment losses	(0.4)
Sale of personal lending	(0.5)
At 31 December	**4.4**
Total allowances for impairment	**39.9**

Interest income on loans classified as impaired totalled £1.1 million (2017: £2.6 million).

14. Debt securities

Debt securities of £149.7 million (2017: £5.0 million) represent UK Treasury Bills. The Company's intention is to hold them to maturity and, therefore, they are stated in the statement of financial position at amortised cost.

All of the debt securities had a rating agency designation at 31 December 2018, based on Moody's long-term ratings of Aa2 (2017: Aa2). None of the debt securities are either past due or impaired.

15. Property, plant and equipment

Group

	Freehold land and buildings £million	Leasehold property	Computer and other equipment £million	Total £million
Cost or valuation				
At 1 January 2017	9.0	-	10.9	19.9
Additions	-	-	0.8	0.8
At 31 December 2017	**9.0**	**-**	**11.7**	**20.7**
Additions	-	0.1	1.0	1.1
Disposals	-	-	(2.0)	(2.0)
Revaluation	(0.8)	-	-	(0.8)
At 31 December 2018	**8.2**	**0.1**	**10.7**	**19.0**
Accumulated depreciation				
At 1 January 2017	-	-	**(8.5)**	**(8.5)**
Depreciation charge	(0.1)	-	(0.7)	(0.8)
Revaluation	0.1	-	-	0.1
At 31 December 2017	**-**	**-**	**(9.2)**	**(9.2)**
Depreciation charge	(0.5)	-	(0.8)	(1.3)
Disposals	-	-	2.0	2.0
Revaluation	0.5	-	-	0.5
At 31 December 2018	**-**	**-**	**(8.0)**	**(8.0)**
Net book amount				
At 31 December 2017	9.0	-	**2.5**	**11.5**
At 31 December 2018	**8.2**	**0.1**	**2.7**	**11.0**

Company

	Freehold property £million	Computer and other equipment £million	Total £million
Cost or valuation			
At 31 December 2017	4.6	9.8	14.4
Additions	-	0.3	0.3
At 31 December 2017	**4.6**	**10.1**	**14.7**
Additions	-	0.5	0.5
Disposals	-	(2.0)	(2.0)
At 31 December 2018	**4.6**	**8.6**	**13.2**
Accumulated depreciation			
At 1 January 2017	-	(8.2)	(8.2)
Depreciation charge	-	(0.4)	(0.4)
At 31 December 2017	-	**(8.6)**	**(8.6)**
Depreciation charge	(0.4)	(0.3)	(0.7)
Disposals	-	2.0	2.0
Revaluation	0.1	-	0.1
At 31 December 2018	(0.3)	**(6.9)**	**(7.2)**
Net book amount			
At 31 December 2017	**4.6**	**1.5**	**6.1**
At 31 December 2018	**4.3**	**1.7**	**6.0**

The Group's freehold properties comprise:

- the Registered Office of the Company, which is fully utilised for the Group's own purposes.
- Secure Trust House, Boston Drive, Bourne End, SL8 5YS, which is only partially used for the Group's own purposes.
- 25 and 26 Neptune Court, Vanguard Way, Cardiff, CF24 5PJ, which is fully utilised for the Group's own purposes.

Freehold properties are stated at fair value as at 31 December 2018 based on external valuations performed by professionally qualified valuers Knight Frank LLP. These valuations have been undertaken in accordance with International Valuations Standards, and were arrived at by reference to market evidence of the transaction prices paid for similar properties. In estimating the fair value of the properties, the valuers consider the highest and best use of the properties. Knight Frank LLP were paid a fixed fee for the valuations. Knight Frank LLP also undertakes some professional work in respect of the Group's Real Estate Finance business, although this is limited in relation to the activities of the Group as a whole. A decrease in the fair value of freehold property has been recognised and its carrying value has been adjusted accordingly. Movements in the fair value of freehold property are recognized in other comprehensive income, to the extent that any reductions do not exceed the initial increase.

The carrying value of freehold land which is included in the total carrying value of freehold land and buildings and which is not depreciated is £1.9 million (2017: £1.9 million).

Notes to the financial statements

The historical cost of freehold property included at valuation is as follows:

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Cost	7.9	7.9	4.1	4.1
Accumulated depreciation	(1.6)	(1.5)	(0.2)	(0.1)
	6.3	**6.4**	**3.9**	**4.0**

16. Intangible assets

Group

	Goodwill £million	Computer software £million	Other intangible assets £million	Total £million
Cost or valuation				
At 1 January 2017	1.0	12.9	2.2	16.1
Additions	-	3.3	0.1	3.4
At 31 December 2017	**1.0**	**16.2**	**2.3**	**19.5**
Additions	-	1.4	-	1.4
Disposals	-	(0.6)	(0.1)	(0.7)
At 31 December 2018	**1.0**	**17.0**	**2.2**	**20.2**
Accumulated amortisation				
At 1 January 2017	-	(6.1)	(1.0)	(7.1)
Amortisation charge	-	(1.8)	(0.2)	(2.0)
At 31 December 2017	-	**(7.9)**	**(1.2)**	**(9.1)**
Amortisation charge	-	(1.6)	(0.2)	(1.8)
Disposals	-	0.6	-	0.6
At 31 December 2018	-	**(8.9)**	**(1.4)**	**(10.3)**
Net book amount				
At 31 December 2017	**1.0**	**8.3**	**1.1**	**10.4**
At 31 December 2018	**1.0**	**8.1**	**0.8**	**9.9**

Goodwill above relates to the following cash generating units, which are part of the Retail Finance operating segment:

	2018 £million	2017 £million
Music business	0.3	0.3
V12	0.7	0.7
Total	**1.0**	**1.0**

The recoverable amount of these cash generating units are determined on a value in use calculation which uses cash flow projections based on financial forecasts covering a three year period, and a discount rate of 8%. Cash flow projections during the forecast period are based on the expected rate of new business. A zero growth based scenario is also considered. The directors believe that any reasonably possible change in the key assumptions on which recoverable amount is based would not cause the aggregate carrying amount to exceed the aggregate recoverable amount of the cash-generating unit.

Other intangible assets were recognised as part of the V12 Finance Group acquisition. These were recorded at fair value, and are being amortised on a straight line basis as follows:

	Years
IT system	5
Distribution channel	10
Brand name	5

Company

	Goodwill £million	Computer software £million	Total £million
Cost or valuation			
At 1 January 2017	0.3	9.0	9.3
Additions	-	3.3	3.3
At 31 December 2017	**0.3**	**12.3**	**12.6**
Additions	-	1.3	1.3
Disposals	-	(0.7)	(0.7)
At 31 December 2018	**0.3**	**12.9**	**13.2**
Accumulated amortisation			
At 1 January 2017	-	(3.1)	(3.1)
Amortisation charge	-	(1.0)	(1.0)
At 31 December 2017	-	**(4.1)**	**(4.1)**
Amortisation charge	-	(1.6)	(1.6)
Disposals	-	0.6	0.6
At 31 December 2018	-	**(5.1)**	**(5.1)**
Net book amount			
At 31 December 2017	**0.3**	**8.2**	**8.5**
At 31 December 2018	**0.3**	**7.8**	**8.1**

Goodwill above relates to the music business cash generating unit, which is part of the Retail Finance operating segment. The recoverable amount is determined on the same basis as for the Group.

17. Investments
Company

	£million
Cost and net book value	
At 31 December 2017 and 1 January 2018	3.7
Equity contributions to subsidiaries in respect of share options	0.2
At 31 December 2018	**3.9**

Shares in subsidiary undertakings of Secure Trust Bank PLC at 31 December 2018 are stated at cost less any provision for impairment. All subsidiary undertakings are unlisted and none are banking institutions. All are 100% owned by the Company. The subsidiary undertakings were all incorporated in the UK and wholly owned via ordinary shares. All subsidiary undertakings are included in the consolidated financial statements and have an accounting reference date of 31 December.

Details are as follows:

	Principal activity
Owned directly	
Debt Managers (Services) Limited	Debt collection company
Secure Homes Services Limited	Property rental
STB Leasing Limited	Leasing
V12 Finance Group Limited	Holding company
Owned indirectly via intermediate holding companies	
V12 Personal Finance Limited	Dormant
V12 Retail Finance Limited	Sourcing and servicing of unsecured loans

The registered office of the Company, and all subsidiary undertakings, is One Arleston Way, Shirley, Solihull, West Midlands, B90 4LH.

Notes to the financial statements

18. Deferred taxation

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Deferred tax liabilities:				
Unrealised surplus on revaluation of freehold property	-	(0.2)	-	-
Other short term timing differences	-	0.2	-	-
Deferred tax liabilities	-	-	-	-
Deferred tax assets:				
Other short term timing differences	7.9	0.6	7.8	0.6
Deferred tax assets	**7.9**	**0.6**	**7.8**	**0.6**
Deferred tax liabilities:				
At 1 January	-	(0.2)	-	-
Income statement	-	0.2	-	-
Other comprehensive income	-	-	-	-
At 31 December	-	-	-	-
Deferred tax assets:				
Prior period closing (IAS 39 basis)	0.6	-	0.6	0.1
Tax on IFRS 9 transition adjustment	6.3	-	6.4	-
At 1 January	6.9	-	7.0	0.1
Income statement	1.2	0.2	1.1	0.1
Other comprehensive income	(0.2)	0.4	(0.3)	0.4
At 31 December	**7.9**	**0.6**	**7.8**	**0.6**

The Government substantively enacted a reduction in the main rate of UK corporation tax from 20% to 19% (effective from 1 April 2017) and a further reduction to 17% (effective 1 April 2020). The Government also introduced an 8% surcharge on the profits of banking companies in excess of £25 million effective from 1 January 2016. Deferred tax has been calculated based on the enacted rates to the extent that the related temporary differences are expected to reverse in future periods. A deferred tax asset was recognised on the IFRS 9 transition adjustment on 1 January 2018 and the current year credit includes a reassessment of the rates at which it is projected to reverse over the period to 31 December 2027.

19. Other assets

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Other receivables	16.2	1.2	16.1	1.0
Amounts due from related companies	-	-	44.5	29.7
Prepayments and accrued income	6.2	4.2	5.0	2.5
	22.4	**5.4**	**65.6**	**33.2**

20. Due to banks

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Amounts due to other credit institutions	263.0	113.0	263.0	113.0
Accrued interest	0.5	-	0.5	-
	263.5	113.0	263.5	113.0

Amounts due to banks for the current year represent monies arising from drawings under the Term Funding Scheme. These are due for repayment between May 2021 and February 2022 (2017: May 2021 and November 2021).

21. Deposits from customers
Group and Company

	2018 £million	2017 £million
Current/demand accounts	14.5	14.5
Term deposits	1,833.2	1,468.7
	1,847.7	**1,483.2**

For a maturity profile of deposits from customers, refer to Notes 31, 32 and 34.

22. Other liabilities

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Other payables	25.8	29.5	22.8	24.5
Amounts due to related companies	-	-	14.1	9.7
Accruals and deferred income	14.3	12.4	12.2	10.2
	40.1	**41.9**	**49.1**	**44.4**

Financial Services Compensation Scheme Levy

The Financial Services Compensation Scheme has confirmed that it has repaid the remaining £4.68 billion it owed to HM Treasury relating to the Bradford and Bingley failure in 2008. Accordingly, no accrual was held for this item as at 31 December 2018.

In the prior year, the liability for the Financial Services Compensation Scheme levy was included in accruals and deferred income of both Group and Company.

In common with all regulated UK deposit takers, the Company paid a levy to the Financial Services Compensation Scheme to enable it to meet claims against it. The levy consists of a compensation levy which covers the amount of compensation and a management expenses levy, which covers the costs of running the scheme and interest associated with compensation which the scheme pays.

The Company's Financial Services Compensation Scheme accrual at 31 December 2017 of £0.2 million reflected market participation up to the date of the last payment to the scheme in September 2018. This amount was calculated on the basis of the Company's share of protected deposits and the Financial Services Compensation Scheme's estimate of total interest levies payable for the last scheme year.

Notes to the financial statements

23. Provisions for liabilities and charges
Group and Company

	Customer redress £million	ECL allowance on loan commitments £million	Fraud £million	Total £million
Balance at 1 January 2017	1.3	-	-	1.3
Charged to income statement	0.4	-	0.2	0.6
Utilised	(0.5)	-	-	(0.5)
Balance at 31 December 2017	1.2	-	0.2	1.4
IFRS 9 transition adjustment	-	0.3	-	0.3
Balance at 1 January 2018	1.2	0.3	0.2	1.7
(Credited)/charged to income statement	(0.4)	0.1	(0.1)	(0.4)
Balance at 31 December 2018	**0.8**	**0.4**	**0.1**	**1.3**

Customer redress provision
The Group provides for its best estimate of redress payable in respect of historical sales of accident, sickness and unemployment insurance, by considering the likely future uphold rate for claims, in the context of confirmed issues and historical experience. The likelihood of potential new claims is projected forward to 2019, as management believe this to be an appropriate time horizon, recognising the significant decline in recent claims experience and the increasing subjectivity beyond that. The accuracy of these estimates would be affected, were there to be a significant change in either the number of future claims or the incidence of claims upheld by the Financial Ombudsman Service.

The Financial Conduct Authority has announced a deadline for making these customer redress claims, which would give consumers until 29 August 2019 to make a claim.

Fraud
The fraud provision relates to cases where the Bank has reasonable evidence of suspected fraud, but further investigation is required before the cases can be dealt with appropriately.

ECL allowance on loan commitments
In accordance with the requirements of IFRS 9 the Group holds an ECL allowance against loans it has committed to lend but have not yet been drawn. For the Real Estate Finance and Commercial Finance portfolios, where a loan facility is agreed that includes both drawn and undrawn elements and the Group cannot identify the ECL on the loan commitment separately, a combined loss allowance for both drawn and undrawn components of the loan is presented as a deduction from the gross carrying amount of the drawn component, with any excess of the loss allowance over the gross drawn amount presented as a provision. At 31 December 2018 no provision was held for losses in excess of drawn amounts.

24. Subordinated liabilities

	£million
At 1 January 2018	-
Issued during the year	50.0
Unamortised issue costs	(0.8)
Accrued interest	1.2
At 31 December 2018	**50.4**

During the year, Secure Trust Bank PLC issued two tranches of 6.75% Fixed Rate Reset Callable Subordinated Notes due 2028 (the Notes):

- £25 million on 17 July 2018
- £25 million on 2 October 2018.

The Notes mature in 2028 but the issuer may at its discretion redeem the Notes in 2023. The Notes are listed on the Global Exchange Market of the Irish Stock Exchange plc trading as Euronext Dublin.

The Notes are treated as Tier 2 regulatory capital which is used to support the continuing growth of the business taking into account increases in regulatory capital buffers. The issue of the Notes is part of an on-going programme to diversify and expand the capital base of the Bank.

25. Contingent liabilities and commitments

25.1 Contingent liabilities

As a financial services business, the Group must comply with numerous laws and regulations, which significantly affect the way it does business. Whilst the Group believes there are no material unidentified areas of failure to comply with these laws and regulations, there can be no guarantee that all issues have been identified.

25.2 Capital commitments

At 31 December 2018, the Group had no capital commitments (2017: £nil).

The Company had no capital commitments (2017: £nil).

25.3 Credit commitments

Commitments to extend credit to customers were as follows:

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Business Finance				
Real Estate Finance	173.4	98.6	173.4	98.6
Asset Finance	-	15.5	-	15.5
Commercial Finance	45.6	35.5	45.6	35.5
Consumer Finance				
Retail Finance	28.3	20.1	28.3	20.1
Motor Finance	0.5	0.6	0.5	0.6
Consumer Mortgages	15.3	7.7	15.3	7.7
Other	-	0.6	-	0.5
	263.1	**178.6**	**263.1**	**178.5**

25.4 Operating lease commitments

The future aggregate lease payments for non-cancellable operating leases are as follows:

Group	2018 Land and buildings £million	2018 Other £million	2017 Land and buildings £million	2017 Other £million
Within 1 year	1.1	0.2	0.3	0.1
Between 1 year and 5 years	3.9	0.2	0.8	0.1
Over 5 years	2.0	-	-	-
	7.0	**0.4**	**1.1**	**0.2**

Company	2018 Land and buildings £million	2018 Other £million	2017 Land and buildings £million	2017 Other £million
Within 1 year	0.8	0.1	0.1	0.1
Between 1 year and 5 years	3.0	0.1	0.4	-
Over 5 years	1.4	-	-	-
	5.2	**0.2**	**0.5**	**0.1**

There are seven leases classified as land and buildings in the Group (2017: 3). Other leases include motor vehicles and computer hardware.

26. Share capital

	2018 Number	2018 £ million	2017 Number	2017 £ million
At start and end of year	**18,475,229**	**7.4**	**18,475,229**	**7.4**

Share capital comprises ordinary shares with a par value of 40 pence each.

27. Share based payments

At 31 December 2018, the Group had five share based payment schemes in operation:

- Share option Scheme
- 2017 long term incentive plan
- 2017 sharesave plan
- 2017 deferred bonus plan
- 'Phantom' share option scheme.

A summary of the key details of each scheme is set out below:

	Outstanding at the start of the year	Granted during the year	Leavers during the year	Outstanding at the end of the year	Vested and exercisable	Vesting	Exercise price
	Number	Number	Number	Number	Number	Date	£
Equity settled							
Share option scheme	177,084	-	-	177,084	177,084	2 November 2016	7.20
						1 June 2020	0.40
2017 long term incentive plan	67,992	94,504	(899)	161,597	-	20 April 2021	0.40
						1 November 2020	13.19
2017 sharesave plan	125,947	34,449	(15,387)	145,009	-	1 November 2021	14.03
						20 April 2019	0.40
						20 April 2020	0.40
2017 deferred bonus plan	-	14,690	-	14,690	-	20 April 2021	0.40
	371,023	143,643	(16,286)	498,380	177,084		
Cash settled							
'Phantom' share option scheme	312,917	-	-	312,917	-	16 March 2019	25.00

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Expense incurred in relation to share-based payments	**0.8**	-	**0.6**	-

27.1 Share option scheme

The share option scheme was established on 17 October 2011.

On 2 November 2011, 934,998 share options were granted at an exercise price of £7.20 per share, entitling three directors and certain senior employees to purchase shares in the Company. Approximately half of the share options vested and were exercised on 2 November 2014, with the remainder vesting and becoming exercisable on 2 November 2016. The bulk of the remainder were exercised on 7 November 2016, leaving 177,084 share options of 2 directors unexercised. Vested options are exercisable for a period of 10 years from the date of grant.

The intrinsic value of unexercised options is £0.8 million (2017: £1.8 million).

27.2 Long term incentive plan

The long term incentive plan was established on 3 May 2017.

Awards under this plan are subject to three performance conditions, which are based on:

- Annual compound growth in earnings per share ('EPS') over the performance period
- Rank of the total shareholder return ('TSR') over the performance period against the TSR of the comparator group of peer group companies
- Maintaining appropriate risk practices over the performance period reflecting the longer term strategic risk management of the Group.

The awards will vest on the date on which the board determines that these conditions have been met.

The awards have a performance term of 3 years. Those awards granted to the Executive Directors are subject to a holding period of 2 years following the vesting date. Those awards not subject to a holding period will be released to the participants on the vesting date. Vested options are exercisable for a period of 10 years from the date of grant.

The following awards have been granted under the plan, entitling two Executive Directors and certain other key senior employees to purchase shares in the Company. The exercise price is £0.40 per share. The original grant date valuation was determined using a Black-Scholes model for the EPS and risk management tranches, and a Monte Carlo model for the TSR tranche:

	Subject to a holding period of two years Awards granted	Subject to a holding period of two years Grant date valuation	Subject to no holding period Awards granted	Subject to no holding period Grant date valuation	Total Awards granted
	Number	£	Number	£	Number
Granted on 1 June 2017	33,467	12.19	34,525	14.82	67,992
At 31 December 2017	33,467		34,525		67,992
Granted on 20 April 2018	30,429	14.26	64,075	15.47	94,504
Leavers	-		(899)		(899)
At 31 December 2018	**63,896**		**97,701**		**161,597**

Measurement inputs and assumptions used for the grant date valuation were as follows:

	Awards granted on 20 April 2018	Awards granted on 1 June 2017
Share price at grant date	£20.85	£22.45
Expected dividend yield	4.05%	3.80%
Awards subject to a holding period		
Expected stock price volatility	25.2%	24.6%
Risk free interest rate	1.15%	0.42%
Average expected life (years)	5.00	5.00
Discount for lack of marketability during holding period	nil	10.00%
Awards not subject to a holding period		
Expected stock price volatility	26.9%	25.1%
Risk free interest rate	0.89%	0.19%
Average expected life (years)	3.00	3.00
Assumptions applicable to TSR tranche only		
Expected stock price volatility	27.1%	25.50%
Grant date TSR performance of the Company compared to comparator group	Upper quartile	Below median
Correlation	22%	37%

In calculating the charge to the income statement, an expected leaver rate has been assumed of nil% for the Executive Directors and 10% for other employees.

27.3 Sharesave plan

The sharesave plan was established on 3 May 2017.

This plan allows all employees with more than 12 months service to save for three years, subject to a maximum monthly amount of £500, with the option to buy shares in Secure Trust Bank PLC when the plan matures. Participants cannot change the amount that they have agreed to save each month but they can suspend payments for up to six months. Participants can withdraw their savings at any time but, if they do this before the completion date, they lose the option to buy shares at the Option Price, and if participants cease to hold plan-related employment before the third anniversary of the grant date, then the options are also lost. The options ordinarily vest approximately three years after grant date, and are exercisable for a period of six months following vesting.

The following awards have been granted under the plan, entitling all eligible employees to purchase shares in the Company. The original grant date valuation was determined using a Black-Scholes model:

	Awards granted	Grant date valuation	Exercise price
	Number	£	£
Granted on 20 September 2017	125,987	3.53	13.19
Leavers	(40)		
At 31 December 2017	125,947		
Granted on 18 September 2018	34,449	3.67	14.03
Leavers	(15,387)		
At 31 December 2018	**145,009**		

Measurement inputs and assumptions used were as follows:

	Awards granted on 18 September 2018	Awards granted on 20 September 2017
Share price at grant date	£17.53	£17.51
Expected stock price volatility	28.14%	25.55%
Expected dividend yield	4.57%	4.34%
Risk free interest rate	0.89%	0.58%
Average expected life (years)	3.36	3.36

In calculating the charge to the income statement, an expected leaver rate of 10% has been assumed.

27.4 Deferred bonus plan

The deferred bonus plan was established on 3 May 2017.

As disclosed in the 2017 annual report and accounts, 50% of the bonus earned by two Executive Directors, amounting to £280,000, was deferred into shares under the deferred bonus plan. The award will vest in three equal tranches after one, two and three years following deferral.

Accordingly, the following awards have been granted under the plan, entitling the two Executive Directors to purchase shares in the Company. The exercise price is £0.40 per share. The original grant date valuation was determined using a Black-Scholes model:

	Awards granted Vesting after 1 year	Grant date valuation Vesting after 1 year	Awards granted Vesting after 2 years	Grant date valuation Vesting after 2 years	Awards granted Vesting after 3 year	Grant date valuation Vesting after 3 years	Awards granted Total
	Number	£	Number	£	Number	£	
Granted on 20 April 2018	4,896	19.64	4,896	18.87	4,898	18.12	14,690
At 31 December 2018	**4,896**		**4,896**		**4,898**		**14,690**

Measurement inputs and assumptions used were as follows:

	Awards vesting after one year	Awards vesting after two years	Awards vesting after three years
Share price at grant date	£20.85	£20.85	£20.85
Expected dividend yield	3.96%	3.96%	3.96%
Expected stock price volatility	25.25%	30.90%	27.68%
Risk free interest rate	0.69%	0.77%	0.82%
Average expected life (years)	1.00	2.00	3.00

27.5 Cash settled share based payments

On 16 March 2015, a four year 'phantom' share option scheme was established in order to provide effective long-term incentive to senior management of the Group. Under the scheme, no actual shares would be issued by the Company, but those granted awards under the scheme would be entitled to a cash payment. The amount of the award is calculated by reference to the increase in the value of an ordinary share in the Company over an initial value set at £25 per ordinary share, being the price at which the shares resulting from the exercise of the first tranche of share options under the share option scheme were sold in November 2014.

As at 31 December 2018, 312,917 (2017: 312,917) share options remained outstanding. The options will vest on 16 March 2019, and be exercisable for a period of 10 years after grant date.

As at 31 December 2018, the estimated fair value has been prepared using the Black-Scholes model. Measurement inputs and assumptions used were as follows:

	2018	2017
Share price at reporting date	£11.80	£17.97
Expected stock price volatility	24.76%	24.49%
Expected dividend yield	7.12%	4.45%
Risk free interest rate	0.76%	0.59%
Average expected life (years)	3.71	4.03
Fair value	**£0.05**	**£0.79**

As the options can be exercised at any point during the seven years after vesting, and given high levels of share price volatility, management has concluded that it is appropriate to hold the accrual at the same level as 2017. This resulted in the following being recognised in the financial statements:

	2018 £million	2017 £million
Liability at 1 January	0.2	0.6
Credit for the year	-	(0.4)
Liability at 31 December	**0.2**	**0.2**

28. Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with less than three months' maturity from the date of acquisition.

	Group 2018 £million	Group 2017 £million	Company 2018 £million	Company 2017 £million
Cash and balances at central banks	169.7	226.1	169.7	226.1
Loans and advances to banks (Note 10)	44.8	34.3	41.9	32.3
	214.5	**260.4**	**211.6**	**258.4**

29. Financial risk management strategy

By their nature, the Group's activities are principally related to the use of financial instruments. The directors and senior management of the Group have formally adopted a Group risk appetite statement which sets out the Board's attitude to risk and internal controls. Key risks identified by the directors are formally reviewed and assessed at least once a year by the Board, in addition to which key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

A more detailed description of the risk governance structure is contained in the Strategic Report beginning on page 40.

The principal financial risks inherent in the Group's business are credit risk (Note 30), market risk (Note 31), liquidity risk (Note 32), and capital risk (Note 33).

30. Credit risk

The Company and Group take on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. A formal Credit Risk Policy has been agreed by the Board whilst credit risk is monitored on a monthly basis by the Credit Risk Committees which review performance of key portfolios including new business volumes, collections performance, provisioning levels and provisioning methodology. A credit risk department within the Group monitors adherence to the Credit Risk Policy, implements risk tools to manage credit risk and evaluates business opportunities and the risks and opportunities they present to the Group whilst ensuring the performance of the Group's existing portfolios is in line with expectations.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to individual borrowers or groups of borrowers. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. The limits on the level of credit risk are approved periodically by the Board of Directors and actual exposures against limits monitored daily.

Impairment provisions are provided for expected credit losses at the statement of financial position date. Significant changes in the economy could result in losses that are different from those provided for at the statement of financial position date. Management therefore carefully manages the Group's exposures to credit risk as it considers this to be the most significant risk to the business.

Exposure to Consumer Finance and Consumer Mortgages credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing lending limits where appropriate. Exposure to credit risk for these portfolios is also managed in part by obtaining collateral, principally motor vehicles on Motor Finance loans, residential property on Consumer Mortgages and a credit support balance provided by RentSmart. The assets undergo a scoring process to mitigate risk and are monitored by the Board.

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For Real Estate Finance and Commercial Finance, lending decisions are made on an individual transaction basis, using expert judgement and assessment against criteria set out in the lending policies. Asset Finance lending is outsourced to Haydock, who operate in line with the Group's credit policies and risk appetite, and is currently closed to new business. The loans are secured against the assets lent against (real estate, trade receivables and commercial plant and equipment, respectively). Disclosures relating to collateral and arrears on loans and advances to customers are disclosed in Notes 11 and 13 respectively.

The Board monitors the ratings of the counterparties in relation to the Group's loans and advances to banks. Disclosures of these at the year end are contained in Note 10. There is no direct exposure to the Eurozone and peripheral Eurozone countries.

Group

With the exception of loans and advances to customers, the carrying amount of financial assets represents the Group's maximum exposure to credit risk. The Group's maximum exposure to credit risk for loans and advances to customers by portfolio and IFRS 9 stage without taking account of any collateral held or other credit enhancements attached was as follows:

	Stage 1	Stage 2			Stage 3			Total
		<= 30 days past due	> 30 days past due	Total	Excl. purchased credit impaired	Purchased credit impaired	Total	
	£million	£million	£million	£million	£million	£million	£million	£million
31 December 2018								
Business Finance								
Real Estate Finance	723.3	47.1	-	47.1	-	-	-	770.4
Asset Finance	55.6	6.5	0.5	7.0	3.2	-	3.2	65.8
Commercial Finance	186.1	8.8	-	8.8	0.6	-	0.6	195.5
Consumer Finance								
Retail	537.1	74.1	3.9	78.0	4.9	-	4.9	620.0
Motor	200.2	92.7	2.4	95.1	20.5	-	20.5	315.8
Debt Management	-	-	-	-	9.3	23.0	32.3	32.3
Consumer Mortgages	84.9	-	-	-	-	-	-	84.9
Other	11.3	-	-	-	-	-	-	11.3
Total drawn exposure	1,798.5	229.2	6.8	236.0	38.5	23.0	61.5	2,096.0
Off balance sheet								
Loan commitments	263.1	-	-	-	-	-	-	263.1
Total gross exposure	2,061.6	229.2	6.8	236.0	38.5	23.0	61.5	2,359.1
Less:								
Impairment allowance	(20.3)	(19.9)	(4.0)	(23.9)	(22.9)	-	(22.9)	(67.1)
Provision for loan commitments	(0.4)	-	-	-	-	-	-	(0.4)
Total net exposure	**2,040.9**	**209.3**	**2.8**	**212.1**	**15.6**	**23.0**	**38.6**	**2,291.6**

The above table is prepared on an IFRS 9 basis. In accordance with the transitional provisions of the standard comparatives have not been restated. Refer to Notes 1 and 13 for further information. An analysis of the Group's opening loans and advances to customers by IFRS 9 stage and portfolio is presented in Note 38. The Group has not disclosed exposures and impairment allowance split by risk rating as this split is not used internally by the Group to monitor loan book performance.

A reconciliation of opening to closing impairment allowance for losses on loans and advances to customers is presented in Note 13.

The tables below summarise the December 2017 loans and advances to customers on an IAS 39 basis:

	£million	%
31 December 2017 (IAS 39 basis)		
Neither past due nor impaired	1,545.6	94.3%
Not past due but impaired	5.4	0.3%
Past due but not impaired	0.3	0.0%
Past due up to 90 days and impaired	37.8	2.3%
Past due after 90 days and impaired	49.1	3.0%
Gross	1,638.2	100.0%
Less: allowance for impairment	(39.9)	
Net	**1,598.3**	

Gross amounts of loans and advances to customers that were past due up to 90 days and impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	24.5
Past due 30 - 60 days	8.6
Past due 60 - 90 days	4.7
Total	**37.8**

Gross amounts of loans and advances to customers that were past due but not impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	0.2
Past due 30 - 60 days	0.1
Total	**0.3**

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Company

The Group's maximum exposure to credit risk for loans and advances to customers by portfolio and IFRS 9 stage without taking account of any collateral held or other credit enhancements attached was as follows:

	Stage 1	Stage 2			Stage 3			Total
		<= 30 days past due	> 30 days past due	Total	Excl. purchased credit impaired	Purchased credit impaired	Total	
	£million	£million	£million	£million	£million	£million	£million	£million
31 December 2018								
Business Finance								
Real Estate Finance	723.3	47.1	-	47.1	-	-	-	770.4
Asset Finance	55.6	6.5	0.5	7.0	3.2	-	3.2	65.8
Commercial Finance	182.0	8.8	-	8.8	0.6	-	0.6	191.4
Consumer Finance								
Retail	537.1	74.1	3.9	78.0	4.9	-	4.9	620.0
Motor	200.2	92.7	2.4	95.1	20.5	-	20.5	315.8
Consumer Mortgages	84.9	-	-	-	-	-	-	84.9
Other	0.6	-	-	-	-	-	-	0.6
Total drawn exposure	1,783.7	229.2	6.8	236.0	29.2	-	29.2	2,048.9
Off balance sheet								
Loan commitments	263.1	-	-	-	-	-	-	263.1
Total gross exposure	2,046.8	229.2	6.8	236.0	29.2	-	29.2	2,312.0
Less:								
Impairment allowance	(20.7)	(20.2)	(4.1)	(24.3)	(23.6)	-	(23.6)	(68.6)
Provision for loan commitments	(0.4)	-	-	-	-	-	-	(0.4)
Total net exposure	**2,025.7**	**209.0**	**2.7**	**211.7**	**5.6**	**-**	**5.6**	**2,243.0**

The above table is prepared on an IFRS 9 basis. In accordance with the transitional provisions of the standard comparatives have not been restated. Refer to Notes 1 and 13 for further information. The average IFRS 9 probability of default (PD) is based on 12 month PDs at the reporting date.

The tables below summarise the December 2017 loans and advances to customers on an IAS 39 basis:

	£million	%
31 December 2017 (IAS 39 basis)		
Neither past due nor impaired	1,529.0	95.3%
Not past due but impaired	5.4	0.3%
Past due but not impaired	-	0.0%
Past due up to 90 days and impaired	37.5	2.3%
Past due after 90 days and impaired	33.5	2.1%
Gross	1,605.4	100.0%
Less: allowance for impairment	(39.9)	
Net	**1,565.5**	

Gross amounts of loans and advances to customers that were past due up to 90 days and impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	24.4
Past due 30 - 60 days	8.5
Past due 60 - 90 days	4.6
Total	**37.5**

Gross amounts of loans and advances to customers that were past due but not impaired were as follows:

	£million
31 December 2017 (IAS 39 basis)	
Past due up to 30 days	-
Past due 30 - 60 days	-
Total	-

30.1 Concentration risk

Management assesses the potential concentration risk from geographic, product and individual loan concentration. Due to the nature of the Group's lending operations the directors consider the lending operations of the Group as a whole to be well diversified. Details of the Group's loan and advances to customers and loan commitments by product is provided in Note 3.

Geographical concentration

The Group's Real Estate Finance and Consumer Mortgages are secured against UK property only. The Directors consider that the key risk is the location of the security, rather than location of the borrower. Accordingly, the geographical concentration of these business loans and advances to customer, for 2018, has been presented by location of the security as follows:

Group and Company

	Real Estate Finance £million	Consumer Mortgages £million
31 December 2018		
Central England	35.1	16.2
Greater London	451.5	12.2
Northern England	37.6	16.6
South East England (excl. Greater London)	209.0	26.3
South West England	9.6	9.3
Scotland, Wales and Northern Ireland	27.6	4.3
Gross loans and receivables	770.4	84.9
Allowance for impairment	(0.1)	(0.2)
Total	**770.3**	**84.7**

The geographical concentration of these business loans and advances to customer at 31 December 2017, by location of the borrower, is set out below:

	Real Estate Finance £million	Consumer Mortgages £million
31 December 2017		
Central England	6.8	2.1
Greater London	384.2	4.1
Northern England	12.1	2.1
Scotland	-	-
South East England (excl. Greater London)	154.9	5.2
South West England	3.3	1.9
Wales and Northern Ireland	-	1.1
Other	19.8	-
Gross loans and receivables	581.1	16.5
Allowance for impairment	(0.3)	-
Total	**580.8**	**16.5**

30.2 Forbearance

At year end, all customers within the Group's Consumer Mortgage business were up to date with their monthly payments. Should customers face financial difficulties, the Group may, depending on individual circumstances, offer customers one of a number of forbearance options. The types of forbearance the Group may be prepared to offer include the following:

- Temporary interest only concessions are offered to customers in financial difficulty on a temporary basis with formal periodic review. The concession allows the customer to reduce monthly payments to cover interest only, and if made, the arrears status will not increase.
- Arrangement payment plans are agreed to enable customers to reduce their arrears balances by an agreed amount per month which is paid in addition to their standard monthly repayment.
- Payment concessions can be agreed on a temporary basis whereby the customer may pay less than the contractual monthly payment, in line with their individual affordability. If a customer is within this type of concession, their arrears position will increase.
- In exceptional circumstances, capitalisations of arrears may occur or an interest rate adjustment may be applied. These are used under strict controls, explicitly where the customer circumstances offer no other option.

All forbearance arrangements are formally discussed and agreed with the customer. By offering customers in financial difficulty the option of forbearance the Group potentially exposes itself to an increased level of risk through prolonging the period of non-contractual payment and/or potentially placing the customer into a detrimental position at the end of the forbearance period.

All forbearance arrangements are reviewed and monitored regularly to assess the ongoing potential risk, suitability and sustainability to the Group.

Where forbearance measures are not possible or are considered not to be in the customer's best interests, or where such measures have been tried and the customer has not adhered to the forbearance terms that have been agreed, the Bank will consider realising its security and taking possession of the property in order to sell it and clear the outstanding debt.

Other than Consumer Mortgages, the Group does not routinely reschedule contractual arrangements where customers default on their repayments. It may offer the customer the option to reduce or defer payments for a short period, in which cases the loan will retain the normal contractual payment due dates and will be treated the same as any other defaulting cases for impairment purposes. Arrears tracking will continue on the account with any impairment charge being based on the original contractual due dates for all products.

31. Market risk

Market risks arise from open positions in interest rate and currency products, all of which are exposed to general and specific market movements. There are no significant exposures to foreign currencies and therefore there is no significant currency risk. The Group does not operate a trading book.

31.1 Interest rate risk

Group and Company

Interest rate risk is the risk of potential loss through unhedged or mismatched asset and liability positions, which are sensitive to changes in interest rates. When interest rates change, the present value and timing of future cash flows change. This in turn changes the underlying value of the Group's assets, liabilities and off-balance sheet instruments and hence its economic value. Changes in interest rates also affect the Group's earnings by altering interest sensitive income and expenses, affecting its net interest income.

The Group seeks to 'match' interest rate risk on either side of the statement of financial position. However, this is not a perfect match and interest rate risk is present on the mismatch between fixed rate loans and savings products and variable rate assets and liabilities.

The Group monitors the interest rate mismatch on at least a monthly basis. The main test employed is a 200bps interest rate shock across all interest indices on a parallel basis. The Group maintained such exposures within the risk appetite set by the Board throughout the year.

The Group measures primarily Earnings at Risk, Market Rate Sensitivity and Economic Value of Equity, through monitoring an interest rate sensitivity gap. Interest rate risks inherent in new products or through changes to the terms and conditions of existing products were assessed over the course of the year.

This potential exposure is managed by the Group Treasury function and overseen by ALCO. The policy is not to take significant unmatched positions.

31.2 Interest rate sensitivity gap

The following tables summarise the re-pricing periods for the assets and liabilities in the Company and Group. Items are allocated to time bands by reference to the earlier of the next contractual interest rate re-price and the maturity date.

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Group

	Within 3 months	More than 3 months but less than 6 months	More than 6 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years	Non interest bearing	Total
	£million	£million	£million	£million	£million	£million	£million
As at 31 December 2018							
ASSETS							
Cash and balances at central banks	169.7	-	-	-	-	-	169.7
Loans and advances to banks	44.8	-	-	-	-	-	44.8
Debt securities	-	149.7	-	-	-	-	149.7
Loans and advances to customers	719.6	119.4	196.1	954.8	5.4	33.6	2,028.9
Other assets	-	-	-	-	-	51.2	51.2
Total assets	**934.1**	**269.1**	**196.1**	**954.8**	**5.4**	**84.8**	**2,444.3**
LIABILITIES AND EQUITY							
Due to banks	263.0	-	-	-	-	0.5	263.5
Deposits from customers	640.2	94.9	281.5	820.1	11.0	-	1,847.7
Subordinated liabilities	-	-	-	50.0	-	0.4	50.4
Other liabilities	-	-	-	-	-	45.6	45.6
Equity	-	-	-	-	-	237.1	237.1
Total liabilities and equity	**903.2**	**94.9**	**281.5**	**870.1**	**11.0**	**283.6**	**2,444.3**
Interest rate sensitivity gap	**30.9**	**174.2**	**(85.4)**	**84.7**	**(5.6)**	**(198.8)**	
Cumulative gap	**30.9**	**205.1**	**119.7**	**204.4**	**198.8**	**-**	

	Within 3 months	More than 3 months but less than 6 months	More than 6 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years	Non interest bearing	Total
	£million	£million	£million	£million	£million	£million	£million
As at 31 December 2017							
ASSETS							
Cash and balances at central banks	226.1	-	-	-	-	-	226.1
Loans and advances to banks	34.3	-	-	-	-	-	34.3
Debt securities	5.0	-	-	-	-	-	5.0
Loans and advances to customers	581.2	121.3	181.9	696.0	2.3	15.6	1,598.3
Other assets	-	-	-	-	-	27.9	27.9
Total assets	**846.6**	**121.3**	**181.9**	**696.0**	**2.3**	**43.5**	**1,891.6**
LIABILITIES AND EQUITY							
Due to banks	113.0	-	-	-	-	-	113.0
Deposits from customers	577.2	28.2	269.9	581.4	6.5	20.0	1,483.2
Other liabilities	-	-	-	-	-	46.3	46.3
Equity	-	-	-	-	-	249.1	249.1
Total liabilities and equity	**690.2**	**28.2**	**269.9**	**581.4**	**6.5**	**315.4**	**1,891.6**
Interest rate sensitivity gap	**156.4**	**93.1**	**(88.0)**	**114.6**	**(4.2)**	**(271.9)**	
Cumulative gap	**156.4**	**249.5**	**161.5**	**276.1**	**271.9**	**-**	

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Company

	Within 3 months £million	More than 3 months but less than 6 months £million	More than 6 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million	Non interest bearing £million	Total £million
As at 31 December 2018							
ASSETS							
Cash and balances at central banks	169.7	-	-	-	-	-	169.7
Loans and advances to banks	41.9	-	-	-	-	-	41.9
Debt securities	-	149.7	-	-	-	-	149.7
Loans and advances to customers	714.1	118.3	194.1	948.4	5.4	-	1,980.3
Other assets	-	-	-	-	-	91.4	91.4
Total assets	**925.7**	**268.0**	**194.1**	**948.4**	**5.4**	**91.4**	**2,433.0**
LIABILITIES AND EQUITY							
Due to banks	263.0	-	-	-	-	0.5	263.5
Deposits from customers	640.2	94.9	281.5	820.1	11.0	-	1,847.7
Subordinated liabilities	-	-	-	50.0	-	0.4	50.4
Other liabilities	-	-	-	-	-	54.0	54.0
Equity	-	-	-	-	-	217.4	217.4
Total liabilities and equity	**903.2**	**94.9**	**281.5**	**870.1**	**11.0**	**272.3**	**2,433.0**
Interest rate sensitivity gap	**22.5**	**173.1**	**(87.4)**	**178.3**	**(5.6)**	**(180.9)**	
Cumulative gap	**22.5**	**195.6**	**108.2**	**186.5**	**180.9**	**-**	

	Within 3 months £million	More than 3 months but less than 6 months £million	More than 6 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million	Non interest bearing £million	Total £million
As at 31 December 2017							
ASSETS							
Cash and balances at central banks	226.1	-	-	-	-	-	226.1
Loans and advances to banks	32.3	-	-	-	-	-	32.3
Debt securities	5.0	-	-	-	-	-	5.0
Loans and advances to customers	576.6	119.2	178.3	689.1	2.3	-	1,565.5
Other assets	-	-	-	-	-	52.1	52.1
Total assets	**840.0**	**119.2**	**178.3**	**689.1**	**2.3**	**52.1**	**1,881.0**
LIABILITIES AND EQUITY							
Due to banks	113.0	-	-	-	-	-	113.0
Deposits from customers	577.2	28.2	269.9	581.4	6.5	20.0	1,483.2
Other liabilities	-	-	-	-	-	47.7	47.7
Equity	-	-	-	-	-	237.1	237.1
Total liabilities and equity	**690.2**	**28.2**	**269.9**	**581.4**	**6.5**	**304.8**	**1,881.0**
Interest rate sensitivity gap	**149.8**	**91.0**	**(91.6)**	**107.7**	**(4.2)**	**(252.7)**	
Cumulative gap	**149.8**	**240.8**	**149.2**	**256.9**	**252.7**	**-**	

32. Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. The liquidity requirements of the Group are met through withdrawing funds from its Bank of England Reserve Account to cover any short-term fluctuations and longer term funding to address any structural liquidity requirements.

The Company has a formal governance structure in place to manage and mitigate liquidity risk on a day to day basis. The Board sets and approves the Company's liquidity risk management strategy. The ALCO, comprising senior executives of the Company, monitors liquidity risk. Key liquidity risk management information is reported by the Treasury function and monitored by the Chief Executive Officer and Chief Financial Officer on a daily basis. The ALCO meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and ILAAP metrics.

The Company raised fixed rate deposit bonds during the year as set out below:

	2018	2017
Amount	£448.4 million	£347.9 million
Term	1 to 7 years	1 to 5 years

These were issued to broadly match the term lending by the Company.

The PRA requires a firm to maintain at all times liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. There is also a requirement that a firm ensures its liquidity resources contain an adequate buffer of high quality, unencumbered assets (i.e. Government Securities in the liquidity asset buffer); and it maintains a prudent funding profile. The liquidity assets buffer is a pool of highly liquid assets that can be called upon to create sufficient liquidity to meet liabilities on demand, particularly in a period of liquidity stress. The liquidity resources outside the buffer must either be marketable assets with a demonstrable secondary market that the firm can access, or a credit facility that can be activated in times of stress.

The Group has a Board approved ILAAP. The ILAAP rules require the Group to identify, measure, manage and monitor liquidity and funding risks across different time horizons and stress scenarios, consistent with the Group's risk appetite as established by the Board. The ILAAP seeks to document the Group's approach to liquidity and funding, and demonstrate that it complies with the Overall Liquidity Adequacy Rule. The PRA's approach to liquidity supervision is based on the principle that a firm must have adequate levels of liquidity resources and a prudent funding profile, and that it comprehensively manages and controls liquidity and funding risks. The liquidity buffer required by the ILAAP has been put in place and maintained since that time. Liquidity resources outside of the buffer are made up of deposits placed at the Bank of England. The ILAAP is updated annually.

The primary measures used by management to assess the adequacy of liquidity is the Overall Liquidity Adequacy Rule, which is the Board's own view of the Group's liquidity needs as set out in the Board approved ILAAP. The Group maintained liquidity in excess of the Overall Liquidity Adequacy Rule throughout the year ended 31 December 2018.

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The LCR regime has applied to the Group from 1 October 2016, requiring management of net 30 day cash outflows as a proportion of High Quality Liquid Assets. The Group has set a more prudent internal limit. The actual LCR has significantly exceeded both limits throughout the year.

The Group is exposed to daily calls on its available cash resources from maturing deposits and loan draw-downs. The Group maintains significant cash resources to meet all of these needs as they fall due.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates.

The tables below analyse the contractual undiscounted cash flows for the financial liabilities and assets into relevant maturity groupings:

Group

	Carrying amount	Gross nominal inflow/ (outflow)	Not more than 3 months	More than 3 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years
	£million	£million	£million	£million	£million	£million
At 31 December 2018						
Non-derivative financial liabilities						
Due to banks	(263.5)	(263.5)	(263.5)	-	-	-
Deposits from customers	(1,847.7)	(1,916.3)	(644.3)	(404.7)	(855.8)	(11.5)
Other financial liabilities	(26.3)	(26.3)	(26.3)	-	-	-
Subordinated liabilities	(50.4)	(66.9)	(0.8)	(2.5)	(63.6)	-
	(2,187.9)	**(2,273.0)**	**(934.9)**	**(407.2)**	**(919.4)**	**(11.5)**
Non-derivative financial assets						
Cash and balances at central banks	169.7	169.7	169.7	-	-	-
Loans and advances to banks	44.8	44.8	44.8	-	-	-
Debt securities	149.7	149.7	149.7	-	-	-
Loans and advances to customers	2,028.9	2,476.4	841.1	523.8	1,110.1	1.4
Other financial assets	16.1	16.1	16.1	-	-	-
	2,409.2	**2,856.7**	**1,221.4**	**523.8**	**1,110.1**	**1.4**
Liquidity mismatch	**221.3**	**583.7**	**286.5**	**116.6**	**190.7**	**(10.1)**

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2017						
Non-derivative financial liabilities						
Due to banks	(113.0)	(115.1)	(0.1)	(0.4)	(114.6)	-
Deposits from customers	(1,483.2)	(1,517.2)	(580.8)	(318.6)	(611.1)	(6.7)
Other financial liabilities	(29.5)	(29.5)	(29.5)	-	-	-
	(1,625.7)	**(1,661.8)**	**(610.4)**	**(319.0)**	**(725.7)**	**(6.7)**
Non-derivative financial assets						
Cash and balances at central banks	226.1	226.1	226.1	-	-	-
Loans and advances to banks	34.3	34.3	34.3	-	-	-
Debt securities	5.0	5.0	5.0	-	-	-
Loans and advances to customers	1,598.3	2,054.4	667.8	420.8	965.3	0.5
Other financial assets	1.2	1.2	1.2	-	-	-
	1,864.9	**2,321.0**	**934.4**	**420.8**	**965.3**	**0.5**
Liquidity mismatch	**239.2**	**659.2**	**324.0**	**101.8**	**239.6**	**(6.2)**

Company

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2018						
Non-derivative financial liabilities						
Due to banks	(263.5)	(263.5)	(263.5)	-	-	-
Deposits from customers	(1,847.7)	(1,916.3)	(644.3)	(404.7)	(855.8)	(11.5)
Other financial liabilities	(37.4)	(37.4)	(37.4)	-	-	-
Subordinated liabilities	(50.4)	(66.9)	(0.8)	(2.5)	(63.6)	-
	(2,199.0)	**(2,284.1)**	**(946.0)**	**(407.2)**	**(919.4)**	**(11.5)**
Non-derivative financial assets						
Cash and balances at central banks	169.7	169.7	169.7	-	-	-
Loans and advances to banks	41.9	41.9	41.9	-	-	-
Debt securities	149.7	149.7	149.7	-	-	-
Loans and advances to customers	1,980.3	2,427.1	801.3	519.2	1,105.2	1.4
Other financial assets	60.6	16.1	16.1	-	-	-
	2,402.2	**2,804.5**	**1,178.7**	**519.2**	**1,105.2**	**1.4**
Liquidity mismatch	**203.2**	**520.4**	**232.7**	**112.0**	**185.8**	**(10.1)**

	Carrying amount £million	Gross nominal inflow/ (outflow) £million	Not more than 3 months £million	More than 3 months but less than 1 year £million	More than 1 year but less than 5 years £million	More than 5 years £million
At 31 December 2017						
Non-derivative financial liabilities						
Due to banks	(113.0)	(115.1)	(0.1)	(0.4)	(114.6)	-
Deposits from customers	(1,483.2)	(1,517.2)	(580.8)	(318.6)	(611.1)	(6.7)
Other financial liabilities	(34.2)	(34.2)	(34.2)	-	-	-
	(1,630.4)	**(1,666.5)**	**(615.1)**	**(319.0)**	**(725.7)**	**(6.7)**
Non-derivative financial assets						
Cash and balances at central banks	226.1	226.1	226.1	-	-	-
Loans and advances to banks	32.3	32.3	32.3	-	-	-
Debt securities	5.0	5.0	5.0	-	-	-
Loans and advances to customers	1,565.5	2,017.5	646.6	413.1	957.3	0.5
Other financial assets	30.7	30.7	30.7	-	-	-
	1,859.6	**2,311.6**	**940.7**	**413.1**	**957.3**	**0.5**
Liquidity mismatch	**229.2**	**645.1**	**325.6**	**94.1**	**231.6**	**(6.2)**

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing financial liabilities as they mature are important factors in assessing the liquidity of the Company and Group and its exposure to changes in interest rates and exchange rates.

Other financial liabilities, as shown above, do not include non-interest accruals as these are not classed as financial liabilities.

33. Capital risk

The Group’s capital management policy is focused on optimising shareholder value, in a safe and sustainable manner. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

In accordance with CRD IV and the required parameters set out in the Capital Requirements Regulation, the Group’s ICAAP is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, as a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a ‘Pillar 1 plus’ approach to determine the level of capital the Group needs to hold. This method takes the Pillar 1 capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequate to cover management’s view of anticipated risks. Where it is considered that the Pillar 1 calculations do not reflect the risk, an additional capital add-on in Pillar 2 should be applied, in line with the Total Capital Requirement issued by the PRA.

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Pillar 3 complements the minimum capital requirements (Pillar 1) and the supervisory review process (Pillar 2). Its aim is to encourage market discipline by developing a set of disclosure requirements which would allow market participants to assess key pieces of information on a firm's capital, risk exposures and risk assessment processes. Pillar 3 disclosures for the Group for the year ended 31 December 2018 are published as a separate document on the Group's website.

The following table, which is unaudited and therefore not in scope of the independent auditor's report, shows the regulatory capital resources for the Group. The Group has elected to adopt the IFRS 9 transitional rules. For 2018 this allowed 95% of the initial IFRS 9 transition adjustment, net of attributable deferred tax, to be added back to eligible Tier 1 capital. Tier 2 capital comprises solely subordinated debt issued during the year net of unamortised issue costs and excluding accrued interest, capped at 25% of the capital requirement. At 31 December 2017, Tier 2 capital comprised the collective allowance for loan impairment. Under IFRS 9, there is no longer a collective allowance.

	2018 £million (unaudited)	2017 £million (unaudited)
Tier 1		
Share capital	7.4	7.4
Share premium	81.2	81.2
Retained earnings	147.4	159.2
Revaluation reserve	1.1	1.3
IFRS 9 transition adjustment	24.5	-
Goodwill	(1.0)	(1.0)
Intangible assets net of attributable deferred tax	(8.8)	(9.2)
CET1 capital	**251.8**	**238.9**
Tier 2		
Subordinated liabilities	50.4	-
Less ineligible portion	(4.7)	-
Collective allowance for impairment of loans and advances	-	4.4
Total Tier 2 capital	**45.7**	**4.4**
Own Funds	**297.5**	**243.3**
Reconciliation to total equity:		
IFRS 9 transition adjustment	(24.5)	-
Eligible subordinated liabilities	(45.7)	-
Goodwill and other intangible assets net of attributable deferred tax	9.8	10.2
Collective allowance for impairment of loans and advances	-	(4.4)
Total equity	**237.1**	**249.1**

The Group ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The PRA sets a Total Capital Requirement ('TCR') for each UK bank calibrated by reference to its Capital Resources Requirement, which is broadly equivalent to 8% of risk weighted assets and thus representing the capital required under Pillar 1 of the Basel III framework. The ICAAP is a key input into the PRA's TCR setting process, which addresses the requirements of Pillar 2 of the Basel II framework. The PRA's approach is to monitor the available capital resources in relation to the TCR. The Group maintains an extra internal buffer and capital ratios are reviewed on a monthly basis to ensure that external and internal requirements are adhered to. The PRA reviewed the Group's ICAAP in 2017 and issued its updated TCR in March 2018.

The Group is also subject to further capital requirements imposed by the PRA on all financial services firms. During the periods, the Group complied with these requirements.

The Group raised Tier 2 capital in 2018. Further details of the capital issuance are given in Note 24.

34. Maturity analysis of consolidated assets and liabilities

Group

	Due within one year	Due after more than one year	No contractual maturity	Total
	£million	£million	£million	£million
Contractual maturity analysis at 31 December 2018				
ASSETS				
Cash and balances at central banks	169.7	-	-	169.7
Loans and advances to banks	44.8	-	-	44.8
Loans and advances to customers	1,035.1	960.2	33.6	2,028.9
Debt securities	149.7	-	-	149.7
Property, plant and equipment	-	-	11.0	11.0
Intangible assets	-	-	9.9	9.9
Deferred tax assets	-	-	7.9	7.9
Other assets	-	-	22.4	22.4
Total assets	**1,399.3**	**960.2**	**84.8**	**2,444.3**
LIABILITIES				
Due to banks	263.5	-	-	263.5
Deposits from customers	1,016.6	831.1	-	1,847.7
Current tax liabilities	4.2	-	-	4.2
Other liabilities	-	-	40.1	40.1
Provisions for liabilities and charges	-	-	1.3	1.3
Subordinated liabilities	1.2	50.0	(0.8)	50.4
Total liabilities	**1,285.5**	**881.1**	**40.6**	**2,207.2**

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2017				
ASSETS				
Cash and balances at central banks	226.1	-	-	226.1
Loans and advances to banks	34.3	-	-	34.3
Loans and advances to customers	884.4	698.3	15.6	1,598.3
Debt securities	5.0	-	-	5.0
Property, plant and equipment	-	-	11.5	11.5
Intangible assets	-	-	10.4	10.4
Deferred tax assets	-	-	0.6	0.6
Other assets	-	-	5.4	5.4
Total assets	**1,149.8**	**698.3**	**43.5**	**1,891.6**
LIABILITIES				
Due to banks	113.0	-	-	113.0
Deposits from customers	875.3	587.9	20.0	1,483.2
Current tax liabilities	3.0	-	-	3.0
Other liabilities	-	-	41.9	41.9
Provisions for liabilities and charges	-	-	1.4	1.4
Total liabilities	**991.3**	**587.9**	**63.3**	**1,642.5**

The directors have reviewed behavioural maturity of the loan book and have concluded that it would not significantly affect the analysis above.

Company

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2018				
ASSETS				
Cash and balances at central banks	169.7	-	-	169.7
Loans and advances to banks	41.9	-	-	41.9
Loans and advances to customers	1,026.5	953.8	-	1,980.3
Debt securities	149.7	-	-	149.7
Property, plant and equipment	-	-	6.0	6.0
Intangible assets	-	-	8.1	8.1
Investments	-	-	3.9	3.9
Deferred tax assets	-	-	7.8	7.8
Other assets	-	-	65.6	65.6
Total assets	**1,387.8**	**953.8**	**91.4**	**2,433.0**
LIABILITIES				
Due to banks	263.5	-	-	263.5
Deposits from customers	1,016.6	831.1	-	1,847.7
Current tax liabilities	3.6	-	-	3.6
Other liabilities	-	-	49.1	49.1
Provisions for liabilities and charges	-	-	1.3	1.3
Subordinated liabilities	1.2	50.0	(0.8)	50.4
Total liabilities	**1,284.9**	**881.1**	**49.6**	**2,215.6**

	Due within one year £million	Due after more than one year £million	No contractual maturity £million	Total £million
Contractual maturity analysis at 31 December 2017				
ASSETS				
Cash and balances at central banks	226.1	-	-	226.1
Loans and advances to banks	32.3	-	-	32.3
Loans and advances to customers	874.1	691.4	-	1,565.5
Debt securities	5.0	-	-	5.0
Property, plant and equipment	-	-	6.1	6.1
Intangible assets	-	-	8.5	8.5
Investments	-	-	3.7	3.7
Deferred tax assets	-	-	0.6	0.6
Other assets	-	-	33.2	33.2
Total assets	**1,137.5**	**691.4**	**52.1**	**1,881.0**
LIABILITIES				
Due to banks	113.0	-	-	113.0
Deposits from customers	875.3	587.9	20.0	1,483.2
Current tax liabilities	1.9	-	-	1.9
Other liabilities	-	-	44.4	44.4
Provisions for liabilities and charges	-	-	1.4	1.4
Total liabilities	**990.2**	**587.9**	**65.8**	**1,643.9**

The directors have reviewed behavioural maturity of the loan book and have concluded that it would not significantly affect the analysis above.

35. Classification of financial assets and liabilities

Group

	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2018 (IFRS 9 basis)			
Cash and balances at central banks	169.7	169.7	Level 1
Loans and advances to banks	44.8	44.8	Level 2
Loans and advances to customers	2,028.9	2,032.5	Level 3
Debt securities	149.7	149.7	Level 1
Other financial assets	16.2	16.2	Level 3
	2,409.3	**2,412.9**	
Due to banks	263.5	263.5	Level 2
Deposits from customers	1,847.7	1,859.7	Level 3
Other financial liabilities	26.3	26.3	Level 3
Subordinated liabilities	50.4	50.4	Level 2
	2,187.9	**2,199.9**	

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	Debt securities £million	Loans and receivables £million	Other financial assets and liabilities £million	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2017 (IAS 39 basis)						
Cash and balances at central banks	-	226.1	-	226.1	226.1	Level 1
Loans and advances to banks	-	34.3	-	34.3	34.3	Level 2
Loans and advances to customers	-	1,598.3	-	1,598.3	1,641.1	Level 3
Debt securities	5.0	-	-	5.0	5.0	Level 1
Other financial assets	-	-	1.2	1.2	1.2	Level 3
	5.0	**1,858.7**	**1.2**	**1,864.9**	**1,907.7**	
Due to banks	-	-	113.0	113.0	113.0	Level 2
Deposits from customers	-	-	1,483.2	1,483.2	1,481.6	Level 3
Other financial liabilities	-	-	29.5	29.5	29.5	Level 3
	-	**-**	**1,625.7**	**1,625.7**	**1,624.1**	

All assets and liabilities are carried at amortised cost. Therefore for these assets and liabilities, the fair value hierarchy noted above relates to the disclosure in this note only.

Company

	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2018 (IFRS 9 basis)			
Cash and balances at central banks	169.7	169.7	Level 1
Loans and advances to banks	41.9	41.9	Level 2
Loans and advances to customers	1,980.3	1,983.9	Level 3
Debt securities	149.7	149.7	Level 1
Other financial assets	60.6	60.6	Level 3
	2,402.2	**2,405.8**	
Due to banks	263.5	263.5	Level 2
Deposits from customers	1,847.7	1,859.7	Level 3
Other financial liabilities	37.4	37.4	Level 3
Subordinated liabilities	50.4	50.4	Level 2
	2,199.0	**2,211.0**	

Notes to the financial statements

	Debt securities £million	Loans and receivables £million	Other financial assets and liabilities £million	Total carrying amount £million	Fair value £million	Fair value hierarchy level
At 31 December 2017 (IAS 39 basis)						
Cash and balances at central banks	-	226.1	-	226.1	226.1	Level 1
Loans and advances to banks	-	32.3	-	32.3	32.3	Level 2
Loans and advances to customers	-	1,565.5	-	1,565.5	1,608.3	Level 3
Debt securities	5.0	-	-	5.0	5.0	Level 1
Other financial assets	-	-	30.7	30.7	30.7	Level 3
	5.0	**1,823.9**	**30.7**	**1,859.6**	**1,902.4**	
Due to banks	-	-	113.0	113.0	113.0	Level 2
Deposits from customers	-	-	1,483.2	1,483.2	1,481.6	Level 3
Other financial liabilities	-	-	34.2	34.2	34.2	Level 3
	-	-	**1,630.4**	**1,630.4**	**1,628.8**	

All assets and liabilities are carried at amortised cost. Therefore for these assets, the fair value hierarchy noted above relates to the disclosure in this note only.

Fair value classification

The tables above include the fair values and fair value hierarchies of the Group and Company's financial assets and liabilities. The Group measures fair value using the following fair value hierarchy that reflects the significance of the inputs used in making measurements:

- Level 1: Quoted prices in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Cash and balances at central banks

The fair value of cash and balances at central banks was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date.

At the end of each year, the fair value of cash and balances at central banks was calculated to be equivalent to their carrying value.

Loans and advances to banks

The fair value of loans and advances to banks was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date.

Loans and advances to customers

The fair value of loans and advances to customers was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date, and the same assumptions regarding the risk of default were applied as those used to derive the carrying value.

Debt securities
The fair value of debt securities is based on the quoted mid-market share price.

At the end of December 2018 the fair value of debt securities was calculated to be equivalent to their carrying value.

Due to banks
The fair value of amounts due to banks was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date.

At the end of each year, the fair value of amounts due to banks was calculated to be equivalent to their carrying value due to the short maturity term of the amounts due.

Deposits from customers
The fair value of deposits from customers was calculated based upon the present value of the expected future principal and interest cash flows. The rate used to discount the cash flows was the market rate of interest at the balance sheet date for the notice deposits and deposit bonds. The fair value of instant access deposits is equal to book value as they are repayable on demand.

Dividends and other financial liabilities
The fair value of dividends and other financial liabilities was calculated based upon the present value of the expected future principal cash flows.

At the end of each year, the fair value of dividends and other financial liabilities was calculated to be equivalent to their carrying value due to their short maturity. The other financial liabilities include all other liabilities other than non-interest accruals.

Subordinated liabilities
The fair value of subordinated liabilities was calculated based upon the present value of the expected future principal cash flows.

36. Related party transactions
Related parties of the Company and Group include subsidiaries, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits as set out below. Except for the directors' disclosures, there were no other Key Management Personnel disclosures, therefore the tables below relate to directors and close members of their family only.

Notes to the financial statements

	Directors	
	2018	2017
	£million	£million
Loans		
Loans outstanding at 1 January	3.7	3.2
Loans advanced	0.4	0.4
Interest applied	0.1	0.1
Loans outstanding at 31 December	**4.2**	**3.7**
Deposits		
Deposits outstanding at 1 January	0.4	0.3
Additional deposits made during the year	-	0.1
Deposits outstanding at 31 December	**0.4**	**0.4**

The loans outstanding above comprise the following:

- A £0.4 million advance (2017: £0.4 million) as part of a £2.5 million facility agreed with a company in which a director holds 50% of the voting shares, which is secured by property and personal guarantees.
- A £3.8 million advance (2017: £3.3 million) as part of a revised £4.4 million facility agreed with a director, which is secured by property and certain other undertakings.

Both of these transactions were agreed by the Group's Real Estate Finance business and arose during the normal course of business. Both loans were subject to the usual Board governance and Credit Committee approval procedures and are on substantially the same terms as for comparable transactions with third parties.

The Company undertook the following transactions with other companies in the Secure Trust Bank Group:

	2018	2017
	£million	£million
Debt Managers (Services) Limited - income from sale of debt portfolio	(0.2)	(0.3)
Debt Managers (Services) Limited - debt collection services	1.0	0.2
Secure Homes Services Limited - building rental paid	0.4	0.4
V12 Finance Group Limited - dividend received	-	(13.9)
V12 Retail Finance Limited - fees and commission	21.4	20.8
	22.6	**7.2**

During the year, the basis of the fees and commission charged by V12 Retail Finance Limited was changed. A breakdown of the charges is set out below:

	2018	2017
	£million	£million
Fees and commission		
Loan management services	14.9	-
Sales commission	6.5	-
Financial intermediary charges		
Applications proposed	-	5.1
Applications accepted	-	2.3
Loan set-up and processing	-	4.5
Loan book management and servicing fees	-	8.9
	21.4	**20.8**

The loans and advances with, and amounts receivable and payable to, related companies are noted below:

	Company 2018 £million	Company 2017 £million
Amounts receivable from subsidiary undertakings	44.5	29.7
Amounts due to subsidiary undertakings	(14.1)	(9.7)
	30.4	**20.0**

Directors' remuneration

The directors' emoluments (including pension contributions and benefits in kind) for the year are disclosed in the Directors’ Remuneration Report beginning on page 97.

At the year end the ordinary shares held by the directors are disclosed in the Directors’ Report beginning on page 114. Details of the directors’ holdings of share options, as well as details of those share options exercised during the year, are also disclosed in the Directors’ Report.

37. Immediate parent company and ultimate controlling party

The Company has had no immediate parent company or ultimate controlling party.

38. Implementation of IFRS 9

Group

The table below summarises the adjustments arising on adoption of IFRS 9 on the Group's balance sheet at 1 January 2018. There has been no change in the carrying amount of financial instruments on the basis of their measurement categories. All adjustments have arisen solely due to a replacement of the IAS 39 incurred loss impairment approach with an expected credit loss approach. The Group's classification and measurement and loss impairment accounting policies are provided in Note 1.

	IAS 39 measurement category	IFRS 9 measurement category	IAS 39 carrying amount	ECL adjustment	IFRS 9 carrying amount
			£million	£million	£million
At 1 January 2018					
ASSETS					
Cash and balances at central banks	Loans and receivables	Amortised cost	226.1	-	226.1
Loans and advances to banks	Loans and receivables	Amortised cost	34.3	-	34.3
Loans and advances to customers	Loans and receivables	Amortised cost	1,598.3	(31.8)	1,566.5
Debt securities	Held to maturity	Amortised cost	5.0	-	5.0
Property, plant and equipment	N/A	N/A	11.5	-	11.5
Intangible assets	N/A	N/A	10.4	-	10.4
Deferred tax asset	N/A	N/A	0.6	6.3	6.9
Other assets	N/A	N/A	5.4	-	5.4
Total assets			**1,891.6**	**(25.5)**	**1,866.1**
LIABILITIES AND EQUITY					
Due to banks	Other financial assets and liabilities	Amortised cost	113.0	-	113.0
Deposits from customers	Other financial assets and liabilities	Amortised cost	1,483.2	-	1,483.2
Current tax liabilities	N/A	N/A	3.0	-	3.0
Other liabilities	N/A	N/A	41.9	-	41.9
Provisions for liabilities and charges	N/A	N/A	1.4	0.3	1.7
Total liabilities			**1,642.5**	**0.3**	**1,642.8**
Equity attributable to owners of the parent					
Share capital	N/A	N/A	7.4	-	7.4
Share premium	N/A	N/A	81.2	-	81.2
Revaluation Reserve	N/A	N/A	1.3	-	1.3
Retained earnings	N/A	N/A	159.2	(25.8)	133.4
Total equity			**249.1**	**(25.8)**	**223.3**
Total liabilities and equity			**1,891.6**	**(25.5)**	**1,866.1**

Notes to the financial statements

The following table reconciles the Group's closing IAS 39 impairment allowance to the opening IFRS 9 allowance as at 1 January 2018:

	Closing IAS 39 balance at 31 December 2017	ECL adjustment	Opening IFRS 9 balance at 1 January 2018
	£million	£million	£million
Specific allowances for impairment	35.5	36.2	71.7
Collective allowances for impairment	4.4	(4.4)	-
Impairment against on balance sheet assets	**39.9**	**31.8**	**71.7**
Provision for loan commitments	-	0.3	0.3
Total impairment and provision	**39.9**	**32.1**	**72.0**

Total provisions above include expert credit judgements over the Group's IFRS 9 model results of £2.5 million, of which £1.2 million are specific overlays for the Business Finance portfolio.

An analysis of the Group's opening gross loans and advances to customers and ECL impairment allowance by IFRS 9 stage is provided below:

	Not credit impaired		Credit impaired			
	Stage 1: Subject to 12 month ECL	Stage 2: Subject to lifetime ECL	Stage 3: Excl. purchased credit impaired	Stage 3: Purchased credit impaired	Total	Provision cover
	£million	£million	£million	£million	£million	%
1 January 2018						
Gross loans and advances						
Business Finance						
Real Estate Finance	516.5	64.6	-	-	581.1	
Asset Finance	103.1	11.3	3.5	-	117.9	
Commercial Finance	125.4	1.2	0.5	-	127.1	
Consumer Finance						
Retail Finance	398.4	57.4	3.6	-	459.4	
Motor Finance	182.0	94.0	25.5	-	301.5	
Debt Management	-	-	7.8	7.8	15.6	
Consumer Mortgages	16.5	-	-	-	16.5	
Other	15.8	0.2	3.1	-	19.1	
Total on balance sheet	**1,357.7**	**228.7**	**44.0**	**7.8**	**1,638.2**	
Loan commitments	**178.6**	**-**	**-**	**-**	**178.6**	
ECL Impairment allowance						
Business Finance						
Real Estate Finance	0.1	-	-	-	0.1	0.0%
Asset Finance	0.3	0.1	1.0	-	1.4	1.2%
Commercial Finance	0.2	0.2	0.4	-	0.8	0.6%
Consumer Finance						
Retail Finance	6.8	7.4	3.1	-	17.3	3.8%
Motor Finance:						
ECL allowance	5.9	16.9	20.1	-	42.9	
Voluntary termination provision	5.6	-	-	-	5.6	
	11.5	16.9	20.1	-	48.5	16.1%
Debt Management	-	-	-	-	-	0.0%
Consumer Mortgages	-	-	-	-	-	0.0%
Other	-	0.3	3.3	-	3.6	18.8%
Impairment allowance against on balance sheet assets	**18.9**	**24.9**	**27.9**	**-**	**71.7**	**4.4%**
Provision for loan commitments	**0.3**	**-**	**-**	**-**	**0.3**	**0.2%**

Company

The table below summarises the adjustments arising on adoption of IFRS 9 on the Company's balance sheet at 1 January 2018. There has been no change in the carrying amount of financial instruments on the basis of their measurement categories. All adjustments have arisen solely due to a replacement of the IAS 39 incurred loss impairment approach with an expected credit loss approach.

Notes to the financial statements

	IAS 39 measurement category	IFRS 9 measurement category	IAS 39 carrying amount £million	ECL adjustment £million	IFRS 9 carrying amount £million
At 1 January 2018					
ASSETS					
Cash and balances at central banks	Loans and receivables	Amortised cost	226.1	-	226.1
Loans and advances to banks	Loans and receivables	Amortised cost	32.3	-	32.3
Loans and advances to customers	Loans and receivables	Amortised cost	1,565.5	(32.4)	1,533.1
Debt securities	Held to maturity	Amortised cost	5.0	-	5.0
Property, plant and equipment	N/A	N/A	6.1	-	6.1
Intangible assets	N/A	N/A	8.5	-	8.5
Investments	N/A	N/A	3.7	-	3.7
Deferred tax asset	N/A	N/A	0.6	6.4	7.0
Other assets	N/A	N/A	33.2	-	33.2
Total assets			**1,881.0**	**(26.0)**	**1,855.0**
LIABILITIES AND EQUITY					
Due to banks	Other financial assets and liabilities	Amortised cost	113.0	-	113.0
Deposits from customers	Other financial assets and liabilities	Amortised cost	1,483.2	-	1,483.2
Current tax liabilities	N/A	N/A	1.9	-	1.9
Other liabilities	N/A	N/A	44.4	-	44.4
Provisions for liabilities and charges	N/A	N/A	1.4	0.3	1.7
Total liabilities			**1,643.9**	**0.3**	**1,644.2**
Equity attributable to owners of the parent					
Share capital	N/A	N/A	7.4	-	7.4
Share premium	N/A	N/A	81.2	-	81.2
Revaluation Reserve	N/A	N/A	0.5	-	0.5
Retained earnings	N/A	N/A	148.0	(26.3)	121.7
Total equity			**237.1**	**(26.3)**	**210.8**
Total liabilities and equity			**1,881.0**	**(26.0)**	**1,855.0**

The following table reconciles the Company's closing IAS 39 impairment allowance to the opening IFRS 9 allowance as at 1 January 2018:

	Closing IAS 39 balance at 31 December 2017 £million	ECL adjustment £million	Opening IFRS 9 balance at 1 January 2018 £million
Specific allowances for impairment	35.5	36.8	72.3
Collective allowances for impairment	4.4	(4.4)	-
Impairment against on balance sheet assets	**39.9**	**32.4**	**72.3**
Provision for loan commitments	-	0.3	0.3
Total impairment and provision	**39.9**	**32.7**	**72.6**

Notes to the financial statements

Total provisions above include expert credit judgements over the Company's IFRS 9 model results of £2.5 million, of which £1.2 million are specific overlays for the Business Finance portfolio.

An analysis of the Company's opening gross loans and advances to customers and ECL impairment allowance by IFRS 9 stage is provided below:

	Not credit impaired		Credit impaired			
	Stage 1: Subject to 12 month ECL	Stage 2: Subject to lifetime ECL	Stage 3: Excl. purchased credit impaired	Stage 3: Purchased credit impaired	Total	Provision cover
	£million	£million	£million	£million	£million	%
1 January 2018						
Gross loans and advances						
Business Finance						
Real Estate Finance	516.5	64.6	-	-	581.1	
Asset Finance	103.1	11.3	3.5	-	117.9	
Commercial Finance	123.1	1.2	0.5	-	124.8	
Consumer Finance						
Retail Finance	398.4	57.4	3.6	-	459.4	
Motor Finance	182.0	94.0	25.5	-	301.5	
Consumer Mortgages	16.5	-	-	-	16.5	
Other	0.8	0.2	3.2	-	4.2	
Total on balance sheet	**1,340.4**	**228.7**	**36.3**		**1,605.4**	
Loan commitments	**178.5**	**-**	**-**	**-**	**178.5**	
ECL Impairment allowance						
Business Finance						
Real Estate Finance	0.1	-	-	-	0.1	0.0%
Asset Finance	0.3	0.1	1.0	-	1.4	1.2%
Commercial Finance	0.2	0.2	0.4	-	0.8	0.6%
Consumer Finance						
Retail Finance	6.8	7.5	3.2	-	17.5	3.8%
Motor Finance:						
ECL allowance	6.0	17.0	20.3	-	43.3	
Voluntary termination provision	5.6	-	-	-	5.6	
	11.6	17.0	20.3	-	48.9	16.2%
Consumer Mortgages	-	-	-	-	-	0.0%
Other	-	0.3	3.3	-	3.6	85.7%
Impairment allowance against on balance sheet assets	**19.0**	**25.1**	**28.2**	**-**	**72.3**	**4.5%**
Provision for loan commitments	**0.3**	**-**	**-**	**-**	**0.3**	**0.2%**

Group and Company

As set out in Note 1 for the Real Estate Finance and Commercial Finance portfolios, where a loan facility is agreed that includes both a drawn and undrawn element and the Group cannot identify the ECL on the loan commitment separately, a combined loss allowance for both the drawn and undrawn component of the loan is recognised as an impairment allowance and deducted from the gross carrying amount of the drawn component. At 1 January 2018 loan commitments held for the Real Estate Finance and Commercial Finance portfolios were £98.6 million and £35.5 million respectively.

39. Discontinued operations

On 21 December 2017, the Bank agreed to sell its remaining portfolio of unsecured personal loans to Alpha Credit Solutions 8 S.à.r.l., a company owned by AnaCap Credit Opportunities III LP. As previously highlighted, the Group made the decision to withdraw from the unsecured personal loan market in 2016, and the sale of this portfolio represents a full exit by the Group from this market.

The net proceeds of sale, after transaction costs, amounted to £36.6 million, which was used for general corporate purposes including other forms of lending. The cash purchase consideration for the portfolio was calculated based on an agreed price for the portfolio as at 30 June 2017, adjusted for cash receipts the Group had already received from the portfolio during the period up to the date of completion.

The effect of the transaction is to accelerate capital realisation to reinvest into the Group's core business while removing any future credit risk associated with the portfolio. The profit arising on sale of the portfolio was £0.5 million before tax. The Group continued to administer the portfolio until the completion of a migration of the portfolio to a third party administrator appointed by the purchaser, which was completed in the first half of 2018.

Details of the income statement, net assets disposed of and consequential gain recognised on disposal, and cash flow of the discontinued operation are set out below:

Income statement	2017 £million
Interest income and similar income	8.0
Interest expense and similar charges	-
Net interest income	**8.0**
Fee and commission income	-
Fee and commission expense	-
Net fee and commission income	**-**
Operating income	**8.0**
Net impairment losses on loans and advances to customers	(3.4)
Operating expenses	(0.3)
Profit before income tax	**4.3**
Income tax expense	(0.8)
Profit after income tax	**3.5**
Gain recognized on disposal after tax (see below)	0.4
Profit for the period	**3.9**

As described in Note 3, funding costs and operating expenses are not aligned to operating segments for day to day management of the business, so they cannot be allocated on a reliable basis. Accordingly, funding costs are not included above, and operating expenses above relates only to those costs that are directly attributable to the discontinued business.

Notes to the financial statements

	Assets sold on 21 December 2017 £million
Net assets disposed of:	
Loans and advances to customers	36.1
Consideration	
Cash	37.1
Less selling costs	(0.5)
	36.6
Gain recognised on disposal before tax	**0.5**
Tax	(0.1)
Gain recognised on disposal after tax	**0.4**

Cash flow statement	Year ended 31 December 2017 £million
Cash flows from discontinued operations	
Cash flows from operating activities	
Profit for the year	3.5
Adjustments for:	
Income tax expense	0.8
Impairment losses on loans and advances to customers	3.4
Cash flows from operating profits before changes in operating assets and liabilities	7.7
Changes in operating assets and liabilities:	
- net decrease in loans and advances to customers	28.0
Net cash inflow from operating activities and net increase in cash and cash equivalents	**35.7**

40. Country by Country reporting

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 introduced reporting obligations for institutions within the scope of CRD IV. The requirements aim to give increased transparency regarding the activities of institutions.

The Country-by-Country Information is set out below:

Name	Nature of activity	Location	Turnover £million	Number of FTE employees	Profit before tax £million	Tax paid on profit £million
31 December 2018						
Secure Trust Bank PLC	Banking services	UK	188.6	861	34.7	6.4

Name	Nature of activity	Location	Turnover £million	Number of FTE employees	Profit before tax £million	Tax paid on profit £million
31 December 2017						
Secure Trust Bank PLC	Banking services	UK	165.3	734	29.3	6.0

Five year summary (unaudited)

	2018 £million	2017 £million	2016 £million	2015 £million	2014 £million
Profit for the year					
Interest and similar income	169.2	149.3	141.1	139.7	93.6
Interest expense and similar charges	(35.5)	(26.7)	(26.3)	(21.6)	(14.2)
Net interest income	**133.7**	**122.6**	**114.8**	**118.1**	**79.4**
Net fee and commission income	17.9	14.9	14.5	14.4	18.5
Operating income	**151.6**	**137.5**	**129.3**	**132.5**	**97.9**
Impairment losses on loans and advances	(32.4)	(36.9)	(30.3)	(24.3)	(15.3)
Arbuthnot Banking Group recharges	-	-	-	(0.8)	(0.2)
Operating expenses	(84.5)	(71.6)	(71.5)	(70.9)	(56.3)
Profit on sale of equity instruments available-for-sale	-	0.3	-	-	-
Profit before income tax	**34.7**	**29.3**	**27.5**	**36.5**	**26.1**

	2018 £million	2017 £million	2016 £million	2015 £million	2014 £million
Earnings per share for profit attributable to the equity holders of the Group during the year					
(expressed in pence per share)					
- basic	153.2	128.8	754.1	157.8	122.3

	2018 £million	2017 £million	2016 £million	2015 £million	2014 £million
Financial position					
Cash and balances at central banks	169.7	226.1	112.0	131.8	81.2
Loans and advances to banks	44.8	34.3	18.2	11.5	39.8
Loans and advances to customers	2,028.9	1,598.3	1,321.0	1,074.9	622.5
Debt securities	149.7	5.0	20.0	3.8	16.3
Other assets	51.2	27.9	38.8	25.4	22.5
Total assets	**2,444.3**	**1,891.6**	**1,510.0**	**1,247.4**	**782.3**
Due to banks	263.5	113.0	70.0	35.0	15.9
Deposits from customers	1,847.7	1,483.2	1,151.8	1,033.1	608.4
Subordinated liabilities	50.4	-	-	-	-
Other liabilities	45.6	46.3	52.2	38.1	33.1
Total shareholders' equity	237.1	249.1	236.0	141.2	124.9
Total liabilities and shareholders' equity	**2,444.3**	**1,891.6**	**1,510.0**	**1,247.4**	**782.3**

Appendix to the Annual Report (unaudited)

Key performance indicators

All revenue, income, impairments, and expenses used in the calculations below are stated on a continuing operations basis.

(i) Margin ratios

Net interest margin is calculated as interest income and similar income less interest expense and similar charges for the financial period as a percentage of the average loan book, net revenue margin is calculated as operating income for the financial period as a percentage of the average loan book and gross revenue margin is calculated as interest income and similar income plus fee and commission income for the financial period as a percentage of the average loan book. The calculation of the average loan book is the average of the monthly balance of loans and advances to customers, net of provisions and discontinued operations, over thirteen months:

	2018 £million	2017 £million
Net interest margin		
Interest income and similar income	169.2	141.3
Interest expense and similar charges	(35.5)	(26.7)
Net interest income	133.7	114.6
Net revenue margin		
Net interest income	133.7	114.6
Net fee and commission income	17.9	14.9
Operating income	151.6	129.5
Gross revenue margin		
Interest income and similar income	169.2	141.3
Fee and commission income	19.4	16.0
Gross revenue	188.6	157.3
Opening loan book (after IFRS 9 transition adjustment see Note (vi))	1,566.5	1,255.5
Closing loan book	2,028.9	1,598.3
Average loan book	1,818.2	1,418.1
Net interest margin	**7.4%**	**8.1%**
Net revenue margin	**8.3%**	**9.1%**
Gross revenue margin	**10.4%**	**11.1%**

A reconciliation of the loan book figures used above to the statement of financial position is as follows:

	2016 £million
Balance sheet loan book	1,321.0
PLD loans	(65.5)
	1,255.5

The margin ratios all measure the yield of the loan book.

(ii) Cost ratios

Cost of risk is calculated as impairment losses on loans and advances to customers for the financial period as a percentage of the average loan book, cost of funds is calculated at interest expense for the financial period as a percentage of average loan book and cost to income ratio is calculated as operating expenses for the financial period as a percentage of operating income for the financial period:

	2018 £million	2017 £million
Net impairment losses on loans and advances to customers	32.4	33.5
Average loan book	1,818.2	1,418.2
Cost of risk	**1.8%**	**2.4%**
Interest expense	35.5	26.7
Average loan book	1,818.2	1,418.2
Cost of funds	**2.0%**	**1.9%**
Operating expenses	84.5	71.3
Operating income	151.6	129.5
Cost to income ratio	**55.7%**	**55.1%**

The cost of risk measures how effective the Group has been in managing its impairment losses. The cost of funds measures the cost of money being lent to customers. The cost to income ratio measures how efficiently the Group is utilising its cost base in producing income.

(iii) Return ratios

Annualised adjusted return on average assets is calculated as the adjusted profit after tax for the previous 12 months as a percentage of average assets, annualised adjusted return on average equity is calculated as the adjusted profit after tax for the previous 12 months as a percentage of average equity and annualised adjusted return on required equity is calculated as the adjusted profit after tax for the previous 12 months as a percentage of average required equity.

Adjusted profit after tax is profit after tax attributable to continuing operations, adjusted for items that are non-controllable items or other items that fall outside of the Group's core business activities. A reconciliation of adjusted profit after tax to statutory profit after tax is provided on page 17.

Average assets is calculated as the average of the monthly assets balances, net of discontinued operations, average equity is calculated as the average of the monthly equity balances and average required equity is calculated as the average of the monthly balances of total required equity. Total required equity is calculated as the equity required to achieve a CET1 ratio of 12%, excluding equity required against discontinued operations:

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	2018 £million	2017 £million
Adjusted profit after tax	29.9	21.5
Opening assets (after IFRS 9 transition adjustment – see below)	1,866.1	1,444.5
Closing assets	2,444.3	1,891.6
Average assets	2,182.4	1,639.9
Opening equity	223.3	236.0
Closing equity	237.1	249.1
Average equity	228.9	242.0
Opening required equity	173.3	146.1
Closing required equity	220.9	173.3
Average required equity	201.7	159.8
Annualised adjusted return on average assets	**1.4%**	**1.3%**
Annualised adjusted return on average equity	**13.1%**	**8.9%**
Annualised adjusted return on required equity	**14.8%**	**13.5%**

A reconciliation of assets to the balance sheet is as follows:

	2018 (opening balance) £million	2016 £million
Balance sheet assets	1,891.6	1,510.0
PLD assets	-	(65.5)
IFRS 9 transition adjustment	(25.5)	-
	1,866.1	**1,444.5**

A reconciliation of equity to the balance sheet is as follows:

	2018 (opening balance) £million
Equity	249.1
IFRS 9 transition adjustment	(25.8)
	223.3

Return on average assets demonstrates how profitable the Group's assets are in generating revenue. Return on average equity is a measure of the Group's ability to generate profit from the equity available to it. Return on required equity relates profitability to the capital that the Group is required to hold.

(iv) Funding ratios

The loan to deposit ratio is calculated as the loan book, net of discontinued operations, at the year end, divided by deposits from customers at the year end, and the total funding ratio is calculated as the total funding at the year end, being the sum of deposits from customers, borrowings under the Term Funding Scheme, and equity, divided by the loan book, net of discontinued operations, at the year end:

	2018 £million	2017 £million
Loan book	2,028.9	1,598.3
Deposits from customers	1,847.7	1,483.2
Borrowings under the Term Funding Scheme	263.5	113.0
Tier 2 capital (including accrued interest)	50.4	-
Equity	237.1	249.1
Total funding	2,398.7	1,845.3
Loan to deposit ratio	**109.8%**	**107.8%**
Total funding ratio	**118.2%**	**115.5%**

The funding ratios measure the Group's liquidity.

(v) Adjusted earnings per share

Adjusted earnings per ordinary share are calculated by dividing the adjusted profit attributable to equity holders of the parent by the weighted average number of ordinary shares as follows:

	2018	2017
Adjusted profit attributable to equity holders of the parent (£ millions)	29.9	21.5
Weighted average number of ordinary shares (number)	18,475,229	18,475,229
Adjusted earnings per share (pence)	**161.8**	**116.4**

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(vi) Loans to customers

The impact of the IFRS 9 transition adjustments on the opening balances by segment are set out in the table below:

	31 December 2017 (on an IAS 39 basis)	IFRS 9 transition adjustment	1 January 2018 (on an IFRS 9 basis)
	£million	£million	£million
Business Finance			
Real Estate Finance	580.8	0.2	581.0
Asset Finance	116.7	(0.2)	116.5
Commercial Finance	126.5	(0.2)	126.3
Consumer Finance			
Retail Finance	452.3	(9.7)	442.6
Motor Finance	274.6	(21.6)	253.0
Debt Management	15.6	-	15.6
Consumer Mortgages	16.5	-	16.5
Other	15.3	(0.3)	15.0
	1,598.3	**(31.8)**	**1,566.5**

(vii) Adjusted profit and effective adjusted tax rate

Adjusted profit before tax was £36.7 million (2017: £27.0 million). **Adjusted profit after tax** was £29.9 million (2017: £21.5 million).

The Group uses adjusted profit for planning and reporting purposes, as it improves the comparability of information between reporting periods. The adjustments to profit relate to non-controllable items or other items that fall outside of the Group's core business activities.

Fair value amortisation relates to the acquisition of V12 Finance Group. The acquisition accounting required identifiable assets and liabilities to be adjusted to their fair value, and these adjustments are subject to amortisation.

Transformation costs comprise principally costs of closing the unsecured personal lending product, the cost of potential corporate acquisition work and treasury development (31 December 2017: comprised the costs of setting up the Group's Consumer Mortgage operation and of closing the current account and unsecured personal lending products).

Bonus payments of £1.3 million (2017: £0.6 million) relate to a long term incentive plan that was set up for a small number of employees on the creation of the Commercial Finance business. The scheme is based on profits earned by that business up to the end of 2019, and is payable in 2020.

Profit on sale of Non-Standard Finance plc shares and discontinued activities represented non-core activities.

Glossary

Term	Explanation
AIM	The Alternative Investment Market is the London Stock Exchange's international market for smaller growing companies. A wide range of businesses including early stage, venture capital backed as well as more established companies join AIM seeking access to growth capital.
ALCO	The Assets and Liabilities Committee. The remit of the Committee can be found on the Group's website: www.securetrustbank.com/our-corporate-information/risk-management.
Bank of England	The Bank of England promotes the good of the people of the United Kingdom by maintaining monetary and financial stability. It also performs a supervisory role of the banking system via the Prudential Regulation Authority.
CET 1 capital	Common Equity Tier 1 capital comprises a bank's core capital and includes common shares, stock surpluses resulting from the issue of common shares, retained earnings, common shares issued by subsidiaries and held by third parties, and accumulated other comprehensive income.
CET 1 capital ratio	The Common Equity Tier 1 capital ratio is the ratio of the bank's CET 1 capital to its Total Risk Exposure. This signifies a bank's financial strength. The CET 1 capital ratio is utilised by regulators and investors because it shows how well a bank can withstand financial stress and remain solvent.
CRD IV	Capital Requirements Directive IV is intended to implement the Basel III agreement in the EU. This includes enhanced requirements for the quality and quantity of capital; a basis for new liquidity and leverage requirements; new rules for counterparty risk; and new macroprudential standards including a countercyclical capital buffer and capital buffers for systemically important institutions.
Credit impaired assets	Financial assets that are considered to be in default or 'stage 3' assets. There are no material differences in the Group's definition of 'stage 3', credit impaired or default assets. Financial assets are considered to be stage 3 when an event or events have occurred that have a detrimental impact on estimated future cash flows. Evidence may include initiation of bankruptcy proceedings, notification of bereavement, loan meeting debt sale criteria or initiation of repossessions proceedings. As a backstop a loan that is 90 days or more past due is considered credit impaired for all portfolios.
Capital Requirement Regulation	The EU regulation implementing CRD IV directly across the EU.
DBP	Deferred Bonus Plan.

Glossary

Default	Refer to definition of credit impaired assets above.
DMS	Debt Managers (Services) Limited, the wholly owned subsidiary of Secure Trust Bank PLC, responsible for carrying out market leading debt recovery services to the credit industry.
Expected credit loss ('ECL')	ECLs are probability weighted estimates of credit losses which are measured as the present value of all cash shortfalls. Specifically this is the difference between the contractual cash flows due and the cash flows expected to be received, discounted at the original effective interest rate or, for portfolios purchased outside of the Group by DMS, the credit adjusted effective interest rate.
EU	European Union.
FEEFO	The Feedback Forum collects independent reviews from the customers of over 2,500 businesses.
Financial Conduct Authority	The Financial Conduct Authority is the conduct regulator for 58,000 financial services firms and financial markets in the UK. Its aims are to protect consumers, enhance market integrity and promote competition.
The Financial Ombudsman Service	Set up by Parliament, the Financial Ombudsman Service is the UK's official expert in sorting out problems with financial services.
Financial Services Compensation Scheme	The Financial Services Compensation Scheme protects consumers when authorised financial services firms fail.
General Data Protection Regulation or GDPR	The General Data Protection Regulation (Regulation (EU) 2016/679) is a regulation by which the European Parliament, the European Council and the European Commission intend to strengthen and unify data protection for individuals within the European Union. It also addresses export of personal data outside the European Union.
High Quality Liquid Assets	High Quality Liquid Assets are assets with a high potential to be converted easily and quickly into cash. This is comprised of cash and balances at central banks and treasury bills that are the subject of a repurchase agreement (see below).
IAS	International Accounting Standard.
ICAAP	Internal Capital Adequacy Assessment Process. A firm must carry out an ICAAP in accordance with the PRA's ICAAP rules. These include requirements on the firm to undertake a regular assessment of the amounts, types and distribution of capital that it considers adequate to cover the level and nature of the risks to which it is or might be exposed.
IFRS	International Financial Reporting Standard.

Glossary

ILAAP	The Internal Liquidity Adequacy Assessment Process allows firms to assess the level of liquidity and funding that adequately supports all relevant current and future liquidity risks in their business. In undertaking this process, a firm should be able to ensure that it has appropriate processes in place to ensure compliance with the CRD IV. This requires firms to develop and use appropriate risk and liquidity management techniques.
LCR	The Liquidity Coverage Ratio regime requires management of net 30 day cash outflows as a proportion of High Quality Liquid Assets. The Group has set a more prudent internal limit than that proposed in guidance from the regulator.
LTIP	Long term incentive plan.
MREL	Minimum Requirement for Own Funds and Eligible Liabilities regime.
OLAR	The Overall Liquidity Adequacy Rule is the Board's own view of the Group's liquidity needs as set out in the Board approved ILAAP.
Pillar 1, Pillar 2 and Pillar 3	Basel III uses a 'three pillars' concept – (1) Pillar 1 - minimum capital requirements (addressing risk) using a standardised approach for credit, market and operational risk, (2) Pillar 2 - supervisory review process and (3) Pillar 3 - market discipline and enhanced disclosures. Basel II is the second of the Basel Accords, (now extended and partially superseded by Basel III), which are recommendations on banking laws and regulations issued by the Basel Committee on Banking Supervision.
PLD	A portfolio of legacy unsecured personal loans sold to Alpha Credit Solutions 8 S.à.r.l., a company owned by AnaCap Credit Opportunities III LP, on 21 December 2017.
PRA	The Prudential Regulation Authority was created as a part of the Bank of England by the Financial Services Act (2012) and is responsible for the prudential regulation and supervision of around 1,700 banks. The PRA's objectives are set out in the Financial Services and Markets Act 2000, but the main objective is to promote the safety and soundness of the firms it regulates.
Repurchase agreement	A repurchase agreement is a form of short-term borrowing for dealers in government securities. The dealer sells the government securities to investors, and buys them back at an agreed point in the future.
SME	Small to medium sized enterprises.

Glossary

Stage 1 assets	Financial assets which have: • been determined to be low credit risk at the reporting date; • not experienced a significant increase in credit risk since their initial recognition; or • have experienced a significant increase in credit risk since initial recognition but have since met the Group’s cure policy (refer to Note 1 for the Group’s cure policy. Credit losses for such assets are measured as an amount equal to 12 month ECL.
Stage 2 assets	Financial assets that have experienced a significant increase in credit risk since their initial recognition and have not subsequently met the Group’s cure policy (refer to Note 1 for further detail). As a backstop, the Group considers a significant increase in credit risk occurs no later than when an asset is more than 30 days past due for all portfolios. Credit losses for such assets are measured as an amount equal to lifetime ECL.
Stage 3 assets	Refer to definition of credit impaired assets above.
Term Funding Scheme	The Term Funding Scheme is designed to reinforce the transmission of Bank Rate cuts to those interest rates actually faced by households and businesses by providing term funding to banks at rates close to Bank Rate. The Term Funding Scheme allows participants to borrow central bank reserves in exchange for eligible collateral.
Tier 2 capital	Tier 2 capital is the secondary component of bank capital, in addition to Tier 1 capital, that makes up a bank's required reserves. Tier 2 capital is designated as supplementary capital, and is composed of subordinated liabilities, net of issue costs.
Total Capital Requirement	Guidance given to a firm about the amount and quality of capital resources that the PRA considers that firm should hold at all times under the overall financial adequacy rule as it applies on a solo level or a consolidated level.
Total Risk Exposure	Total Risk Exposure is the total of the bank’s risk-weighted assets.
V12	V12 Retail Finance Limited, the wholly owned subsidiary of Secure Trust Bank PLC, responsible for retail lending.

Corporate contacts and advisers

Secretary & Registered Office

A J Karter LLB (Hons)
One Arleston Way
Solihull
West Midlands
B90 4LH
T 0121 693 9100
F 0121 693 9124

Independent Auditor

Deloitte LLP
Four Brindleyplace
Birmingham
B1 2HZ

Principal Banker

Barclays Bank PLC
38 Hagley Road
Edgbaston
Birmingham
B16 8NY

Stockbrokers

Canaccord Genuity Limited
88 Wood Street
London
EC2V 7QR

Stifel Nicolaus Europe Limited
150 Cheapside
London
EC2V 6ET

Registrar

Link Asset Services
The Registry
34 Beckenham Road
Beckenham
Kent
BR3 4TU