ANNUAL REPORT & ACCOUNTS

2015

Manchester Building Society

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CONTENTS

CHAIRMAN'S STATEMENT

In 2015 the Board continued to focus on the prudent management of the Society in line with the strategy adopted in 2013 of reducing the size of the balance sheet in order to preserve capital. This strategy was necessary because of events, fully disclosed in the Annual Report and Accounts for the year ended 31 December 2012, that led to a material write-down of the Society's reserves following a change in the accounting treatment of certain financial assets.

In the twelve months ended 31 December 2015 the Society and its subsidiaries (the "Group") recorded an operating profit before impairments and provisions of £2.9m compared with £4.7m in the preceding twelve months. The decline in operating profit reflected the reduction in the size of the loan book which fell from £387m to £331m, and also the effect of an increased charge of £1.2m (2014: £0.2m) for regulatory non-compliance on two acquired portfolios, the administration of which was brought in-house in December 2015.

During the year the Board carried out a detailed exercise to evaluate what would be required to re-enter the residential mortgage market from which it withdrew in 2013. This exercise and consequential discussions with the Prudential Regulation Authority ("PRA") confirmed that although the Society has total capital significantly in excess of regulatory requirements, an increase in the Society's Common Equity Tier 1 capital ("CET1", a measure of the quality of capital held) would be necessary before new lending could be resumed. In the absence of this, the Society's balance sheet and scale of operations is likely to continue to decline.

As required by International Financial Reporting Standards ("IFRS"), this prospect required two non-cash accounting adjustments: the carrying value of the head office property has been written down by £2.5m to reflect the forecast under-utilisation of this asset; and the charge for taxation of £4.3m (2014: £0.2m credit) reflects a write-down of the deferred tax asset carried on the balance sheet in line with the lower level of taxable profits now forecast. Other net impairments on the loan books amounted to £0.7m.

After taking account of these charges and the compulsory Financial Services Compensation Scheme ("FSCS") levy of £0.3m, the Group recorded a post-tax loss of £4.9m (2014: £4.5m profit). At 31 December 2015, the Group had negative accounting reserves of £5.6m.

Against this background the Board are currently reviewing the strategic direction of the Society and have set out the uncertainties which exist regarding the longer term prospects of the Society in note 1 to the accounts (page 20).

Notwithstanding the difficult financial circumstances in which the Group has operated since 2012, the Society has continued to serve its members well. During 2015 the level of complaints remained low and the Society continued to offer competitive retail savings products during the unprecedented period of low interest rates. The Society has also worked closely with the small number of members whose mortgage accounts have moved into arrears in order to find a satisfactory solution to payment problems.

In the best interest of members the Board has continued to take legal advice regarding the Society's claim for damages against the previous external auditors, Grant Thornton UK LLP. The legal claim is ongoing.

Finally, on behalf of the Board, I should like to thank all members of staff for their exceptionally strong contribution during the year. I should also like to thank Mr Joe Smith, a non-executive director, who retired from the Board on 29 April 2015 after nine years' service.

D.A. Harding
Chairman
13 April 2016

STRATEGIC REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

Introduction

The directors present their 93rd Annual Report together with the Accounts and Annual Business Statement for the Group for the year ended 31 December 2015.

The Group consists of the Society and its two wholly owned subsidiaries: MBS (Mortgages) Limited and MBS (Property) Limited; further, under the terms of *IFRS 10 Consolidated Financial Statements*, this set of Financial Statements includes the consolidated position of NMB Mortgage Acquisition Company Limited (in administration) ("NMB MAC"), where the Group exerts control notwithstanding that it holds no shares in that entity.

The Group's strategy and results for the year are covered in detail in the sections that follow, along with the principal risks and uncertainties that the Group faces.

Strategy

The Society is owned by its members. The means by which its value is preserved is by providing products that meet the financial needs of both existing and potential members.

The Group's strategy since 2013 has been to reduce its risks and conserve its regulatory capital. This strategy was necessary because of events, fully disclosed in the Annual Report and Accounts for the year ended 31 December 2012, that led to a material write-down of the Society's reserves following a change in the accounting treatment of certain financial assets.

Risk reduction has been achieved via the disposal of almost all of the Society's non-strategic UK lifetime mortgage assets. Further reduction has been sought by investigating the potential for disposals of other mortgage assets (conditional on suitable offers). The Board's strategic aim in this regard has been to move the Society's risk profile away from those legacy asset positions that carried higher risks and higher regulatory capital risk weightings.

Regulatory capital conservation has continued to be a focus, the ongoing reduction in the mortgage book, as a result of the continued curtailment of new mortgage lending during 2015, being central to this. At the same time the Society has continued to explore ways in which the regulatory capital position could be improved. During 2015 this included investigating potential opportunities for further asset disposals, including the sale of the investment in New Life Home Finance Limited which completed in April 2015 at a profit of £0.7m. In the medium term, however, the regulatory capital position is dependent on profitable and sustainable growth or new sources of capital.

Accordingly, in 2015 the Society carried out a detailed evaluation of what would be required to return to growth by resuming residential mortgage lending. This included an assessment of the additional capital that would be required. At present the Society has insufficient CET1 regulatory capital to return to lending and continues to manage a "run-off" of the balance sheet. Against this background the Board is currently reviewing the strategic direction of the Society; the uncertainties which exist regarding the longer term prospects of the Society are disclosed in note 1 on page 20.

Post balance sheet event

After the year end, on 11 April 2016, the Society received new Individual Capital Guidance ("ICG") from the PRA setting out the amount of regulatory capital the Society is required to hold. The Board has reviewed the capital resources following the new guidance from the PRA and has concluded that the ICG and CRD IV buffer requirements are met. The Board also concluded that the Society meets the quantitative aspect of the PRA buffer. As previously, the Society is expected to hold a certain proportion of its capital buffers in CET1 capital; this remains challenging under the new guidance and the Society may not meet these expectations going forward.

Business Model

The principal activities of the Group remain the provision of competitive facilities for personal savings and for mortgage finance primarily to support owner occupation of residential property.

Emphasis in achieving these principal business objectives is placed on offering a secure home for retail depositors' savings and on high standards of customer services to support the Group's range of products.

Key performance indicators

Key performance indicators ("KPIs") monitored by the Board include the following:

- Capital
- Liquid assets
- Retail balances
- Mortgages and other loans
- Administration expenses
- Profit on ordinary activities before income tax

The KPIs are considered in more detail in the sections that follow below, with indications as to why each metric is considered to be of importance in assessing financial performance. Additional commentary on the Group's performance is contained within the Chairman's Statement.

Review of business performance

In 2015 the Group reported a loss for the financial year of £4.9m (2014: profit of £4.5m). This loss is after reflecting write-downs to the carrying value of certain assets, as detailed below, as a consequence of the Group's projected financial performance.

In the year the Group reported operating profit before impairments and provisions of £2.9m (2014: £4.7m).

A reconciliation of operating profit before impairments and provisions to (loss)/ profit on ordinary activities before income tax and the (loss)/ profit for the financial year is set out below:

	Group 2015 £000	Group 2014 £000
Operating profit before impairments and provisions	2,917	4,699
Impairment (losses)/gains on loans and advances to customers	(748)	33
Impairment of property, plant and equipment	(2,471)	-
Financial Services Compensation Scheme Levy	(277)	(430)
(Loss)/profit on ordinary activities before income tax	(579)	4,302
Income tax (expense)/credit	(4,295)	150
(Loss)/profit for the financial year	(4,874)	4,452

The £1.8m reduction in operating profit before impairments and provisions from 2014 is mainly due to the impact of the smaller balance sheet but also due to an increased charge for customer redress of £1.2m (2014: £0.2m) recorded in the year in relation to potential regulatory non-compliance in two acquired portfolios, the administration of which was brought in-house in December 2015. The reduction has been partially offset by the £0.7m profit on disposal of the minority share in New Life Home Finance Limited.

Net interest income in the year was £2.1m lower than in 2014, with £0.8m of the reduction being due to the increased charge for customer redress in respect of potential refunds of interest and £1.3m being due to the reduced size of the balance sheet. The loan book fell by £56.8m from £387.4m to £330.6m while total assets fell by £92.1m from £508.7m to £416.6m. Furthermore, administrative expenses increased by £0.8m mainly associated with the legal claim against Grant Thornton UK LLP, anticipated costs relating to the forthcoming customer redress exercise and project costs associated with the investigation of a possible return to lending.

Additional net loan impairment provisions of £0.7m were incurred, as explained more fully on page 4.

Without sufficient capital to return to lending, the financial projections for the Group assume a long term run-off of the balance sheet. Accordingly the carrying value of the head office property has been written down by £2.5m. For further details of the impairment of the property see the impairment losses section of this Strategic Report and Note 17.

Also as a result of applying the long term run-off financial projections, £4.3m of the deferred tax asset has been de-recognised and an income tax expense has been recognised for this amount. This results in a loss for the financial year of £4.9m (2014: profit £4.5m) being taken to Group consolidated reserves.

After having made the above adjustments the Society has a shortfall against the regulatory capital expectation for Common Equity Tier 1 Capital, with a shortfall of £1.6m as at 31 December 2015. Under the new regulatory capital regime effective 1 January 2016, at that date there is a £2.8m shortfall.

PROFITABILITY

Result for the year: The Group reported a loss for the financial year of £4.9m (2014: profit of £4.5m) and a loss on ordinary activities before income tax for the year of £0.6m (2014: profit of £4.3m).

Net interest income: The Group's net interest income was:

	Group 2015 £000	Group 2014 £000
Interest receivable and similar income	14,401	18,609
Interest payable and similar charges	(5,853)	(7,973)
Net interest income	8,548	10,636

The level of interest earned on mortgages and loans was lower at £13.9m (2014: £17.6m) due to the increased charge in the year for customer redress (in respect of potential refunds of interest) debited against interest income and the impact of reducing mortgage balances; interest on investment securities was lower (2015: £0.1m; 2014: £0.4m) owing to a reduction in the level of securities held (2015: £0.1m; 2014: £15.6m). The reduction in the level of investment securities arose through the natural maturity of instruments, with replacement instruments not being sourced.

Interest paid to savings members reduced from £5.8m in 2014 to £4.2m in 2015, reflecting the combined impact of lower interest rates paid on a reducing savings book (2015: £324.6m of balances owed to members compared with £389.5m at 31 December 2014).

Other income and other charges: Other income and charges rose slightly in the year, with exchange gains of £248k (2014: gains of £163k) arising in the year. Also, as investment securities matured, although the Society received the full principal balance and all interest due on maturity, a fair value loss on these instruments was recorded of £46k (2014: £314k loss), since the Group holds its investment securities at their fair value. Finally, the charge recorded in 2015 for the compulsory FSCS levy fell by £153k to £277k.

Income from investments: During April 2015 the Society completed the sale of its minority share in New Life Home Finance Limited to Legal and General Group plc for consideration of £995k. The profit on sale of £745k is shown under "Income from investments" in the Statements of Comprehensive Income. The shareholding had been held as a trade investment. For further information see Notes 5 and 16.

Administrative expenses: The Group's administrative activities were broadly unchanged from those of the previous year. Overhead and depreciation expenditure increased from £6.1m to £6.8m. The increase reflects additional activity carried out during the year in relation to the development of plans to return to lending, and anticipated costs provided in relation to the forthcoming customer redress exercise. Legal and professional costs were also incurred in connection with the Society's claim against Grant Thornton UK LLP.

Impairment losses: Impairment losses of £3.2m were recorded in 2015 (2014: credit of £33k), of which £2.5m (2014: nil) related to the impairment of the carrying value of the Group's head office building which is included within property, plant and equipment and which is owned by MBS (Property) Limited. The remaining impairment charge of £0.7m (2014: credit of £33k) was in respect of the Group's mortgage and loan books.

The Group's head office building was tested for impairment on a value in use basis. This indicated that the value in use of the property was lower than both its fair value less estimated costs of disposal and its carrying value. The carrying value of the property exceeded its fair value less estimated cost of disposal, which represented its recoverable amount, by £2.5m, and the property was written down to reflect this. The fair value of the property is based on an independent valuation of the property carried out in December 2015. The open market value of the property based on its current level of occupancy was assessed to be £5.5m.

All elements of the Group's mortgage and loan books were tested for impairment during the year and all impairment provisions were re-assessed. The net impairment charge of £0.7m included a charge of £1.3m in respect of the NMB MAC second charge loans where the Group holds a beneficial interest and provisioning of £1.3m in respect of the core mortgage book including one significant new account in arrears. These charges were partially mitigated by a £1.9m reduction in the provision for the Spanish lifetime portfolio following an improvement in the forecast for house prices in Spain.

FINANCIAL POSITION

Liquid Assets: The Group's liquid assets are deposited with the Bank of England and with UK "High Street" banking counterparties in instantly accessible bank accounts. Of the Society's total liquid funds at 31 December 2015, £55.9m was deposited with the Bank of England (2014: £63.1m). Only £0.1m of investment securities were held at 31 December 2015 (2014: £15.6m) as maturing instruments were not reinvested. Within investment securities at 31 December 2015 £nil was held in UK Treasury Bills (2014: £10.0m).

Mortgages and Other Loans: Group mortgage balances, after provisions, were £330.6m (2014: £387.4m), representing a year on year decrease of 14.7% (2014: 14.7% reduction). Further, to seek improvement in its regulatory capital position, the Society made no advances during the year (2014: £nil).

Overall, the performance of the core mortgage book continues to be in line with expectations. With the exception of one new significant account arising in the second half of the year, arrears levels are stable and the number of properties taken into possession has improved.

The Group has continued in its efforts to minimise mortgage arrears and to help borrowers in difficulties to resolve their situations, taking a consultative approach with borrowers who experience payment difficulties and applying forbearance as appropriate. At 31 December 2015, excluding the second charge portfolio, there were 15 mortgage accounts (2014: 14) where payments were 12 or more months in arrears. Outstanding balances on these accounts amounted to £5.5m (2014: £5.4m) with total arrears of £0.8m (2014: £0.8m), representing 1.6% of total gross mortgage balances (2014: 1.3%). The percentage of accounts 12 months or more in arrears has increased because of the declining level of total mortgage assets in the year and the absence of new lending. However, the underlying arrears performance has been stable. There were 8 properties in possession at the end of the year (2014: 9). These figures exclude the NMB MAC portfolio, where the Group only has a beneficial interest in the mortgage assets, and The Consumer Loans Company Limited ("CLC") portfolio. Arrears banding information is not presented for these second charge portfolios as there is insufficient reliable data to determine this accurately.

Provisions for potential mortgage losses have been calculated by assessing impairment indicators, arrears and forbearance positions and historic loss experience. Mortgage accounts in arrears by 3 months or more are reviewed regularly, as are impairment provision requirements.

Further information is given in Note 1.

Investment property: At the year end the Society held a small number of residential properties as a result of the settlement of an impaired mortgage asset. The properties are being held, pending their eventual sale, and have a carrying value of £0.8m (2014: £nil).

Other Assets: Included within Other Assets is a sum of £1.0m (2014: £0.5m) relating to collateral deposited in the form of cash under credit support annex agreements ("CSA") with the Group's counterparty providers of foreign exchange swaps.

Retail Balances: Retail balances reduced to £324.6m (2014: £389.5m) in proportion to the overall reduction in the balance sheet. The range of savings products available during the year was carefully managed in order to ensure that a suitable level of funding was held and that the rates offered were appropriately competitive.

Capital: The purpose of the Group's capital is to support its mortgage book and to absorb any losses that may arise, thereby offering members protection as a regulated deposit taker.

The Board manages capital within the regulatory limits set by the PRA. For regulatory capital purposes the Group is made up of the Society and MBS (Mortgages) Limited, with the regulatory capital positions at 31 December 2015 and 31 December 2014 being:

Tier 1 Capital	**Group 31 December 2014 £000**	**Movement in 2015 £000**	**Group 31 December 2015 £000**	**Regulatory Movement for 2016 £000**	**Group 1 January 2016 £000**
CET 1 Capital					
Retained Earnings	754	(3,879)	(3,125)	-	(3,125)
Deductions	(3,030)	3,029	(1)	-	(1)
Profit Participating Deferred Shares	17,461	-	17,461	-	17,461
Total CET1 Capital	15,185	(850)	14,335	-	14,335
Permanent Interest Bearing Shares					
- Nominal balance	14,788	-	14,788	-	14,788
- Amortisation	(2,958)	(1,479)	(4,437)	(1,478)	(5,915)
Net Permanent Interest Bearing Shares	11,830	(1,479)	10,351	(1,478)	8,873
Total Tier 1 Capital	27,015	(2,329)	24,686	(1,478)	23,208
Tier 2 Capital					
Subordinated Debt					
- Nominal balance	15,700	(1,500)	14,200	-	14,200
- Amortisation	(2,445)	945	(1,500)	(500)	(2,000)
Net Subordinated Debt	13,255	(555)	12,700	(500)	12,200
Collective Provisions	2,850	(695)	2,155	-	2,155
Permanent Interest Bearing Shares	2,958	1,479	4,437	1,478	5,915
Total Tier 2 Capital	19,063	229	19,292	978	20,270
Total Regulatory Capital	46,078	(2,100)	43,978	(500)	43,478

Since the start of 2015 Total Regulatory Capital under CRD IV has decreased by £2,100k made up as follows:

- the retained loss of the regulatory capital group for the year of £3,879k;
- the scheduled repayment of £1,500k of Subordinated debt, (previously amortised by £1,445k under CRD IV rules);
- the continued amortisation of Subordinated debt out of Tier 2 capital over a 9 year period, amounting to £500k in the year;
- a reduction in the allowed collectively identified provisions of £695k; and
- a partially offsetting £3,029k reduction in required deductions from CET1 Capital. This is primarily in respect of the reduction in the deferred tax asset as a result of the £4,295k deferred tax charge recorded in the year but with £250k of the reduction arising due to the sale of the investment in New Life Home Finance Limited.

Under the CRD IV rules applicable from 1 January 2016, Total Regulatory Capital is reduced by £500k compared to the position at 31 December 2015. This is due to Tier 2 Regulatory Capital being reduced by a further £500k in respect of continuing Subordinated debt amortisation.

As at 31 December 2015 the Society held sufficient capital in Tier 1 and Tier 2 to meet all of the regulatory capital requirements then in place. However, one regulatory expectation that was not met compares the Society's actual CET1 capital to the level of CET1 capital that the PRA expects the Society to hold. The Society had also fallen marginally short of this expectation as at 31 December 2014 due to the mix of capital held and during 2015 had continued to focus on rebuilding its capital position. However, the significant write downs in respect of both the intercompany loan with MBS (Property) Limited and the deferred tax asset, combined with increased customer redress provisioning, have depleted CET1 regulatory capital further. As a consequence there is a shortfall of £1.6m against this CET1 expectation as at 31 December 2015. Under the new regulatory capital regime effective 1 January 2016, at that date there is a £2.8m shortfall.

After the year end, on 11 April 2016, the Society received new Individual Capital Guidance ("ICG") from the PRA setting out the amount of regulatory capital the Society is required to hold. The Board has reviewed the capital resources following the new guidance from the PRA and has concluded that the ICG and CRD IV buffer requirements are met. The Board also concluded that the Society meets the quantitative aspect of the PRA buffer. As previously, the Society is expected to hold a certain proportion of its capital buffers in CET1 capital; this remains challenging under the new guidance and the Society may not meet these expectations going forward.

The Group's gross capital improved from 10.4% at 31 December 2014 to 11.0% at 31 December 2015. The free capital at 31 December 2015 was 12.6% (2014: 11.4%). Definitions of gross capital and free capital may be found in the Annual Business Statement.

Financial Risk Management Objectives

The Group offers mortgage and savings products. It undertakes limited interaction with the wholesale money market for cash flow and liquidity management purposes. There are formal structures in place to monitor, report and manage the risks associated with the Group's operations. The Board seeks to manage the risks that the Group faces through a suite of regularly reviewed and approved policies, covering: Credit, Liquidity, Financial Risk Management and Operational Risk.

Principal Risks and Uncertainties

Given the requirement for an increase in CET1 capital in order to return to lending, and the assessed prospects for the business and its capital position without such a return, there is a material uncertainty arising from the continued run-off of the balance sheet. The Board is assessing a number of options to develop a strategy to secure the long term future of the Group; options include plans to improve the capital position of the Group.

Every business faces risks as part of its day-to-day operation. The Board's risk management objectives are to seek to manage the risks that the Society faces, by articulating that it has a low appetite for risk and by deploying a range of risk management policies and procedures within an appropriate control environment in order to achieve such an outcome.

The principal risks and uncertainties facing the Group are credit risk, insurance risk, liquidity risk, interest rate risk and currency risk. Certain aspects of the macroeconomic environment also influence the risks that the Society faces. The principal risks that the Group faces are summarised below:

Credit Risk: The Group is exposed to the risk that it may not receive back in full any sum that has been lent (in relation to loans and advances) or any sum that it has deposited with a banking counterparty (in relation to liquid assets) when such amounts fall due. The Board monitors credit risk, underlying security values and the level of impairment provisions on a regular basis. Credit risk is more of a consideration in relation to loans and advances than in relation to the Society's liquid assets; the former involve relationships with individuals or small businesses, whilst the latter are far fewer in number, being restricted to either the Bank of England or UK High Street banks, where credit risk is assessed as being very low.

The Society's management of credit risk in respect of loans and advances recognises that as the portfolio runs off it is likely that a greater part of the residual assets will have a higher credit risk profile.

The assessment of credit risk and the related impairment provisioning is a critical accounting estimate, impacted by judgements relating to customer affordability and the impact of economic circumstances, including the level of interest rates. Prior to the current strategy of no new lending, credit risk was mitigated by appropriate mortgage underwriting and by limiting the Group's exposure to particular market sectors or loans exhibiting particular attributes. Since the cessation of new lending credit risk has been mitigated through the monitoring of management information, assessment of arrears and forbearance cases, and regular loan provision reviews. The Group holds a beneficial interest in NMB MAC a portfolio of mortgage assets, some of which are regulated by the Consumer Credit Act ("CCA"). The legal title of these loans remains with a third party business currently in administration, over which the Group exerts control. A further smaller portfolio, CLC, which had previously been beneficially owned and which is now legally owned by the Group has similarly CCA regulated mortgage assets. An assessment has been made of the estimated discounted future cash flows expected to arise from both these portfolios of loans which forms the basis for the impairment provision. Sensitivities in respect of the impairment provision required for these portfolios are given on page 34.

The administration of the NMB MAC and CLC portfolios was brought in-house in December 2015.

Insurance Risk: Impairment assessments incorporate the insurance risk attaching to the Society's lifetime mortgage contracts, which are euro-denominated. The risk arises from a contractual term within the relevant mortgage contracts which in certain circumstances precludes the Society from pursuing the borrower or their estate for any shortfall on redemption. This risk is managed through oversight of the portfolio, including monitoring valuations, the assessment of redemptions and provisioning policy. The insurance provision is a critical accounting estimate, as its assessment is based on expected future outcomes relating to the date on which an account redeems, expected to be on the death of the borrower, their move into care or through non-health related voluntary pre-payment. It is also affected by the assumptions made in relation to house price appreciation and depreciation. This means that the insurance risk provision can move by a material amount dependent upon these assumptions and market conditions.

Liquidity Risk: The Group's strategy is to maintain sufficient funds in unencumbered liquid form at all times to ensure that its liabilities can be met as they fall due. Regular stress testing of liquidity is undertaken by separately using 20 week and 3 month time horizons. The Group operates within closely monitored Board-approved liquidity policy limits, which are reviewed on a daily basis by the Group's Finance and Treasury departments, reported to the executive directors every week and considered by the Board each month. During 2015, the Group continued to have a significant proportion of its liquid assets deposited with the Bank of England. It should be noted that, by holding greater proportions of liquidity in Bank of England deposits, (for regulatory purposes) liquidity yields are lower.

Capital Risk: In order to conserve capital, the Society has continued to curtail new lending. The Society has also continued to explore ways in which the regulatory capital position could be improved, including by the sale of assets. The investment in New Life Home Finance Limited was therefore sold in April 2015, at a profit of £0.7m. In the medium term, however, the regulatory capital position is dependent on profitable and sustainable growth or new sources of capital.

Accordingly, the Society carried out a detailed evaluation of what would be required to return to growth by resuming residential mortgage lending. This included an assessment of additional CET1 capital required to resume lending. In the absence of this, the Society's balance sheet and scale of operations is likely to decline in the immediate future. The Board are currently reviewing the long term strategic direction of the Society. This review recognises that there has been and may continue to be a shortfall against the CET1 qualitative regulatory capital expectations, as explained on page 5.

Interest Rate Risk: The Group's mortgage and savings products have different interest rate types and different maturities. This means that the Group is exposed to movements in interest rates. A movement in an external interest rate (e.g. Bank of England Base Rate or LIBOR) does not always affect every mortgage and savings product that the Society holds. The Society has more fixed rate mortgage products (notably its lifetime mortgages) than it has fixed rate savings products. Presently, there are no interest rate swaps in place. The interest rate risk position is monitored by the Risk Committee and the Board and is managed via the setting of internal policy limits and through the holding of an ascribed level of capital to mitigate the risk of interest rate movement. The Board has considered this risk by its review of financial projections under differing interest rate scenarios over the long term. The Group has a natural partial hedge provided by fixed coupons on capital and some savings.

The Board does not intend to hedge its fixed rate mortgages using interest rate swaps at this time; this position is monitored regularly. A rise in interest rates gives rise to a risk of decreasing margins as a greater portion of the mortgage portfolio than the deposit portfolio is based on fixed rates. Liquidity risk can also be managed through changes in the interest rate of the deposit book.

Currency Risk: The Group faces currency movement risks on its Euro denominated mortgage balances which represent 12% of total mortgage assets as at 31 December 2015. The exchange rate risk arising on these balances is managed and mitigated by transacting exchange rate swaps. The exchange rate risk position is reported to the ALCO and Board each month.

Economic Risk: The Group faces the risk that its interest margin can become subjected to the pressure that is brought to bear from being an institution that is primarily funded through retail deposits. Within this market, there is great competition for attracting retail deposits at sustainable rates of interest. Market rates offered by retail institutions reduced following the launch of the Bank of England's Funding for Lending Scheme, however, there is a risk that as repayments are required under the Funding for Lending Scheme then there may be upward pressure on rates to prevent savings outflows.

The Society is also exposed to movements in the value of residential and commercial property in both its mortgage impairment provision requirements and those property assets held at fair value; the Society's investment property and the Group's head office building.

Regulatory Risk: As a regulated entity, the Group is exposed to risks arising from a failure to adhere to relevant regulation. In order to minimise this risk, the Group has deployed a number of risk management policies and procedures. In December 2015, the Risk Committee and Board approved a revised Risk Management Framework ("RMF"), which is designed around the present needs of the Society. The RMF includes the responsibilities of the Board, the Risk Committee, the Conduct Committee and Management as to how the Society meets, monitors and reports on its regulatory requirements. Oversight of Regulatory Risk is the responsibility of the Compliance function and is led by the Interim Chief Risk and Compliance Officer.

The majority of the regulatory requirements that the Group faces are laid down by the PRA and the Financial Conduct Authority ("FCA"). The Group monitors developments in all relevant aspects of financial service regulation and undertakes assessments of the present and future impacts of such. Appropriate actions are taken to strengthen controls and amend the Group's strategy to meet changing regulatory requirements.

Within the NMB MAC and CLC portfolios instances of non-compliance with the CCA were identified. Legal advice in this regard has been incorporated within the assessment of the estimate of discounted future cash flows expected to arise from these loans, which form the basis for the impairment provision.

In addition to considering the impact of any non-compliance on the recoverability of loan balances and thus impairment provisioning, the Group considers the conduct risk which arises from having originated regulated loans and having acquired regulated loan portfolios. As is the case for all financial institutions there is a risk that aspects of current or historic business might be considered as not being conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers.

Certain activities of the Group, particularly the NMB MAC and CLC second charge loan portfolios carry greater levels of conduct risk. The administration of the NMB MAC and CLC portfolios was brought in-house in December 2015 and following that transfer the historic conduct of these portfolios was reviewed in detail by management.

Following this review, and having incorporated legal advice received, the Group has increased its customer redress provision to £1.7m (2014: a provision of £0.5m for refunds was included in Creditors) to provide for instances of non-compliance with the CCA within the NMB MAC and CLC portfolios. The provision includes an estimate of the potential cost of interest refunds during periods of non-compliance and other costs associated with a customer redress exercise. Full details of the customer redress provision are set out in Note 32.

Although a detailed review of these portfolios has been carried out, there is no judicial certainty in the legal position and there is a risk that further conduct issues or cases of non-compliance with regulations could be identified in the future. As a result the actual results could differ materially from our estimates.

Provision has been made where the Group is aware of a specific conduct or regulatory issue and can estimate its impact reliably, further details in respect of the Group's consideration of other potential conduct and regulatory issues is provided in the contingent liabilities Note 33.

Diversity Matters

Gender Analysis: Below is a table summarising permanent, employed members of staff and directors by gender at 31 December 2015, with comparative positions for the previous year end:

	31 December 2015		31 December 2014	
	Male	Female	Male	Female
Directors	5	1	7	1
Staff	24	25	20	20
Total	29	26	27	21

Given the size and scale of the Society's operations and its head count, it does not have any members of staff that would be considered for separate disclosure as "Senior Managers" in the above table.

Social, Community and Human Rights Issues

Stakeholders: The Group's members, staff and other stakeholders are key to its success and it is committed to its policy of ensuring that all are treated fairly and equally at all times.

Employees: The Group's policies ensure that discrimination on the grounds of race, colour, religion, belief, nationality, ethnic origin, sex, sexual orientation, marital status, age, part time status and membership (or otherwise) of a trade union is not tolerated. Further, the Group also holds to its policy on disability, which is achieved via a wider policy approach to equal opportunity in the workplace. Training and development opportunities are presented to staff to allow them to acquire relevant professional qualifications, which, in turn, assist the Group in achieving its goals.

Outlook

The Board's view is that the UK mortgage and savings markets will continue to be challenging. In the short term, given uncertainty in the global economy about growth, oil prices and public finances, savings and lending institutions will develop their own responses that reflect their respective market positions. There remains the potential for interest rate rises in the UK in the medium term and the prospect of further regulation.

During 2016 the Society will continue in its claim against Grant Thornton UK LLP, the previous external auditors, taking account of external legal advice.

At present the Society has insufficient CET1 regulatory capital to return to lending and continues to manage a run-off of the balance sheet. The Board are considering a number of options to secure the future of the Society.

D.A. Harding
Chairman
13 April 2016

DIRECTORS' REPORT
FOR THE YEAR ENDED 31 DECEMBER 2015

Information presented in other sections of the Annual Report and Accounts

Certain information which is required to be included in the Directors' Report has been included in the separate Strategic Report. This information is deemed to form part of the Directors' Report:

- The Group's profitability and financial position
- The principal risks and uncertainties facing the business
- Outlook for the business
- Detailed financial risk management disclosures are provided in Note 1.

Directors

J.P. Allen	Non-executive director	
H.F. Baines	Vice Chairman	
I.A. Dewar	Non-executive director	
C.W. Gee	Finance Director	(resigned 31 March 2015)
D.A. Harding	Chairman	
P.A. Lynch	Operations Director	
F.B. Smith	Non-executive director	
J. Smith	Non-executive director	(resigned 29 April 2015)

At the Annual General Meeting Mrs Smith and Mr Dewar will retire by rotation and being eligible, will offer themselves for re-election.

At the year-end no director had an interest in any shares or debentures of the Society or its connected undertakings.

Other matters

Charitable & political donations

The Society made charitable donations totalling £5k (2014: £5k) during the year. No contributions were made for political purposes.

Pillar 3 Disclosure

The Society's Pillar 3 disclosure can be located on its website.

Supplier payment policy & practice

The Society's policy concerning the payment of its trade creditors is as follows:

a) to agree the terms of payment with a supplier;
b) to ensure that suppliers are aware of the terms of payment;
c) to pay invoices in conformity with the Society's contractual and other legal obligations.

Trade creditors at 31 December 2015 amounted to 3 days of average supplies (2014: 5 days).

Capital Requirements (Country-by-Country) Reporting

In compliance with the reporting obligations set out in Article 89 of the European Union's Capital Requirements Directive IV (CRD IV), which have been implemented in the UK by the Capital Requirements (Country-by-Country) Reporting Regulations, the Group will publish additional information in respect of the year ended 31 December 2015, by 31 December 2016. This information will be available by that date on the Society's website: www.themanchester.co.uk.

Going Concern

The directors consider that it is appropriate for the accounts to be prepared on a going concern basis of accounting as fully explained in Note 1 on page 20, which sets out the risks and uncertainties assessed as part of the preparation of the accounts.

Independent Auditors

In accordance with Section 77 of the Building Societies Act 1986 a resolution for the re-appointment of PricewaterhouseCoopers LLP will be proposed at the Annual General Meeting.

On behalf of the Board of Directors
D.A. Harding
Chairman
13 April 2016

CORPORATE GOVERNANCE

The Board is responsible for setting strategy and providing leadership within a framework of prudent and effective controls which enables risk to be assessed and managed. The Board is mindful that ownership of the Society rests with its members and that the provision of appropriate savings and mortgage products is its key aim.

In order to ensure that, as a mutual organisation, it is appropriately governed, the Society has regard to the principles of the UK Corporate Governance Code ("the Code"), which is issued by the Financial Reporting Council ("the FRC") (located at: www.frc.org.uk/Our-Work/Codes-Standards/Corporate-governance/UK-Corporate-Governance-Code.aspx). In September 2014, the FRC published its latest revision of the Code which is effective for accounting periods commencing on or after 1 October 2014.

Whilst the Code is more directly relevant to listed companies, its provisions can be adopted by a mutual organisation. The Society has been mindful of the revised Code to the extent deemed reasonable and appropriate by the Board.

At 31 December 2015, the Board consisted of one executive director and five non-executive directors. The role of Chief Executive is being filled by Allan Hodges who is not a director or an employee of the Society, as this is an interim appointment. Two different individuals hold the roles of Chairman and Chief Executive.

Chris Gee stepped down from his role as Finance Director on 31 March 2015 and took up a new non-Board role as Head of Corporate Development and Secretarial Services. Paul Gittins took on the role of Interim Finance Director on 1 April 2015 and was succeeded in that interim role by Rob Green on 16 September 2015. Graeme Honeyborne, who had held the position of Society Secretary on an interim basis, left the Society on 31 May 2015.

The senior management team was strengthened by the appointment of Ed Lord as Interim Chief Risk and Compliance Officer on 10 August 2015.

All non-executive directors are considered to be independent, except for the Chairman who, by the nature of the role that he holds, is not considered to be wholly independent. Harry Baines was nominated by the Board as the Senior Independent Director. The role of the Senior Independent Director includes being available to members, where contact through the normal channels has failed or where such contact is inappropriate.

On matters where Board approval is required, each director has a single vote; there is a majority of non-executive directors on the Board.

APPOINTMENTS TO THE BOARD

There were no new director appointments during 2015. The Remuneration and Nominations Committee's appointment process focusses on members of the business community in order to identify suitable candidates with specific, relevant skills and experience.

On joining the Board, each director is provided with an induction which includes reading material and meetings with executive directors and certain managers. Through a programme of self-managed continuing personal development, each director ensures that they maintain a level of knowledge and skill commensurate with their role within the Group.

FINANCIAL AND BUSINESS REPORTING

The respective responsibilities of the directors and the Independent Auditors for preparing and reporting on the Annual Report and Accounts are contained within the Statement of Directors' Responsibilities and the Independent Auditors' Report.

REMUNERATION

Since 1 January 2011 there have been no bonus arrangements in place for any director.

No director is involved in the discussion of, or Board voting activity, that relates to their own remuneration.

The remuneration policy for directors is contained within the Remuneration Report and service contract details may be found in the Annual Business Statement. Details of directors' remuneration are contained in Note 9 to the Accounts.

INTERACTION WITH SHAREHOLDERS

The "shareholders" of the Group are its borrowing and investing members. Unlike a PLC, each member can only have one vote and as a result there are no "major" or "significant" shareholders whose views can be canvassed for the Board. There are very few opportunities for the Group to consult with its members. The Annual General Meeting ("AGM") provides one such opportunity and all Board members are available at this Meeting in order to discuss Society matters with any attending members.

Details of the AGM are sent out to every member; all are encouraged to vote, either in person or by proxy.

THE BOARD AND ITS COMMITTEES

In order to execute its responsibilities in an efficient manner, the Board has constituted six Committees, of which three (Audit, Remuneration & Nominations and Risk) are oversight committees and three (Assets and Liabilities Committee ("ALCO"), Conduct and Credit) are executive committees. The Board retains responsibility for the setting of strategy and the approval of all policy matters. The three oversight Committees are responsible for a more detailed review of matters in their specialist areas, making recommendations to the Board as appropriate. The focus of the three executive committees is on more day-to-day operational matters, operating within the Board-approved policy framework. Operational matters are delegated to executive directors and staff, within specified mandates, in order to ensure that timely decisions can be taken in support of the Board's strategy and policy limits. In addition, the non-executive directors meet periodically to assess all aspects of governance, board responsibility and board performance.

ALCO

ALCO meets monthly to consider matters relating to liquidity and treasury management, including interest rate risk, treasury counterparty risk, exchange rate risk and interest margin management.

Membership as at 31 December 2015: A. Hodges* (Chairman), D. Callaghan*, R.H. Green*, E. Lord*, P.A. Lynch, S.J.Melbourne*.

(not a director)*

Audit Committee

The Committee's membership includes directors who are considered to be independent and its Chairman has experience in accounting and auditing matters. The Committee receives reports from the Society's internal and external auditors and from the Compliance function; its focus is in relation to compliance with statutory and regulatory requirements and systems and controls matters, including assessing the effectiveness of risk systems delivered via a rolling Internal Audit Plan which is approved on an annual basis and covers elements of the control environment.

The Committee monitors the non-audit work undertaken by the external auditors, which related to seeking professional advice on accounting and tax matters. The Audit Committee is satisfied that this non-audit work does not impair PwC's independence. The Committee monitors the financial reporting process, the statutory audit and reviews all financial information that is disclosed externally.

Membership as at 31 December 2015: I.A. Dewar (Chairman), J.P. Allen, F.B. Smith.

Conduct Committee

The Committee meets monthly and considers matters relating to the fair treatment of customers.

Membership as at 31 December 2015: P.A. Lynch (Chairman), A. Hodges*, E. Lord*, R. Mervill*.

(not a director)*

Credit Committee

The Committee meets monthly to consider all lending policy matters, loan book profile, arrears management and provisioning matters. On a return to lending it would consider lending product development.

Membership as at 31 December 2015: A. Hodges*(Chairman), D. Callaghan*, R.H. Green*, P.A. Lynch, D. Spencer*.

(not a director)*

Remuneration and Nominations Committee

The Committee is responsible for making recommendations to the Board in relation to the appointment of new directors, keeping under review the mix of skills and experience of the Board, and also in relation to the levels of remuneration for all Board members and certain managers, as well as policy matters affecting other employees of the Society.

Membership as at 31 December 2015: H.F. Baines (Chairman), D.A. Harding, F.B. Smith.

Risk Committee

In its oversight capacity, the Committee assesses, monitors and manages significant risks faced by the Group and considers strategic issues affecting all areas of risk. Throughout the year, the Committee advised the Board on treasury, balance sheet and operational risk issues.

Membership as at 31 December 2015: I.A. Dewar (Chairman), J.P. Allen, R.H.Green*, A. Hodges*, E. Lord*, P.A. Lynch, F.B. Smith.

(not a director)*

Board and Committee attendance records for 2015

Attendance at full meetings of the Board and its Committees throughout 2015 is scheduled below. Figures displayed in brackets represent the number of meetings that any individual director was due to attend.

	Board	ALCO	Audit	Conduct	Credit	Remuneration & Nominations	Risk
J.P. Allen	11 (11)	-	4 (4)	-	-	-	7 (7)
H.F. Baines	10 (11)	-	-	-	-	2 (2)	-
I.A. Dewar	11 (11)	-	4 (4)	-	-	-	7 (7)
C.W. Gee	3 (3)	3 (3)	-	-	3 (3)	-	2 (2)
D.A. Harding	11 (11)	-	-	-	-	2 (2)	-
P.A. Lynch	11 (11)	11 (11)	-	11 (11)	11 (11)	-	7 (7)
F.B. Smith	10 (11)	-	3 (3)	-	-	2 (2)	5 (7)
J. Smith	2 (3)	-	1 (1)	-	-	-	1 (2)

Figures shown for Messrs Gee and J. Smith are for the period up to the dates of their resignation from the Board in March 2015 and April 2015 respectively.

The above figures exclude instances where directors have chosen to attend a meeting where they were not a member of that committee and at which their attendance was not strictly required. Also excluded from the above are ad hoc Board and Committee meetings called at short notice and where the agenda items considered were very restricted in nature.

Internal Control

The Board is responsible for ensuring the effectiveness of the Group's systems of risk management and internal control, which are designed to identify, monitor and manage the Group's risks, rather than to eliminate them completely. Through various policies, procedures and appetite statements and with the implementation of a variety of operational control processes, the Board ensures that the Group's risks are managed proportionately.

The Society's Risk Committee assesses, monitors and manages the significant risks faced by the Group, overseeing the promotion of a risk based approach to the Group's activities.

Directed by the Audit Committee, Internal Audit reviews the control environment throughout the year and reports its findings to the Audit Committee regularly.

Following its annual review of all control activities undertaken in the year by management , internal and external auditors and the Compliance function, the Audit Committee has satisfied itself that, commensurate with the size and risk profile of the current operations of the Society, its systems are effective.

Evaluation

The non-executive directors, led by the senior independent director, are responsible for assessing the performance of the Chairman. The Chief Executive attends the Chairman's appraisal in order for executive views to be taken into consideration.

On an annual basis, the Board and its Committees undertake a process of assessing and formally documenting their performance during the year using a checklist that covers all areas of operation. Contributions are sought from both Board and Committee members and other relevant parties. The Board reviews and approves the written assessments undertaken by all Committees and where required, amendments are made to the Board Procedures as a result of the assessment processes.

DIRECTORS' REMUNERATION REPORT

Introduction

The purpose of this report is to provide details of the Group's policy on the remuneration of its executive and non-executive directors and to explain the process for setting the level of directors' remuneration.

Remuneration and Nominations Committee

The Remuneration and Nominations Committee is responsible for the remuneration policy for all of the directors; it also reviews the remuneration of certain managers. All recommendations made by the Remuneration and Nominations Committee are considered by the full Board. The Committee has regard to best practice as set out in the UK Corporate Governance Code and with the PRA Remuneration Code to the extent that it is relevant to the Society, given that the Society is a mutual institution.

Executive directors

Remuneration levels are set for executive directors so as to reward and retain the skills and commitment necessary to manage the development of the Group within a competitive and challenging business sector. In accordance with best practice, the Remuneration and Nominations Committee reviews the remuneration arrangements for the executive directors on a periodic basis and compares their range of benefits to those available within similar organisations. The Committee's objective is to promote suitable risk management arrangements, avoiding remuneration structures that promote excessive risk taking.

The executives' remuneration arrangements include:

- salaries, reviewed by the Committee on an annual basis;
- membership of the Group personal pension scheme, on the same terms as other eligible employees of the Group;
- taxable benefits which include a car allowance and private health care.

Since 1 January 2011 there have been no bonus arrangements in place for any executive director.

Non-executive directors

Non-executive directors are remunerated by way of fees, which are recommended by the Remuneration and Nominations Committee to the Board on an annual basis. The level of fees is assessed on the basis of responsibility, experience, skill and time commitment and by comparison with other building societies and regional financial institutions.

Non-executive directors do not receive any other benefits; they do not have any pension arrangements through the Group.

All directors

The Group does not make mortgage loans available to any director. The above arrangements applied throughout 2015.

Other business interests

Details of directors' other business interests are shown in the Annual Business Statement.

Directors' emoluments

The full directors' emoluments table may be found in Note 9 to the Accounts.

Summary

This report, in addition to Note 9 to the Accounts, is intended to provide a full explanation of the policy and application of directors' remuneration. A resolution will be put to the Annual General Meeting inviting members to vote on the Directors' Remuneration Report.

On behalf of the Remuneration and Nominations Committee
H.F. Baines
Chairman
13 April 2016

STATEMENT OF DIRECTORS' RESPONSIBILITIES

Directors' responsibilities for preparing the Annual Report and Accounts

The following statement, which should be read in conjunction with the statement of the Auditors' responsibilities on page 15, is made by the directors to explain their responsibilities in relation to the preparation of the Annual Report and Accounts in accordance with applicable law and regulation.

The directors are required by the Building Societies Act 1986 ("the Act") to prepare, for each financial year, financial statements which give a true and fair view of the income and expenditure of the Society and the Group for the financial year and of the state of affairs of the Society and the Group as at the end of the financial year.

In preparing the financial statements, the directors are required to:

- select appropriate accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether the financial statements have been prepared in accordance with International Financial Reporting Standards (as adopted by the European Union); and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Society and Group will continue in business.

In addition to the financial statements, the Act requires the directors to prepare, for each financial year, an Annual Business Statement and a Directors' Report, each containing prescribed information relating to the business of the Society and the Group.

Directors' responsibilities pursuant to the Disclosure and Transparency Rules

The directors confirm that to the best of each person's knowledge and belief:

- the financial statements, prepared in accordance with International Financial Reporting Standards (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 Society; and
- the Annual Business Statement and Directors' Report includes a fair review of the development and performance of the business and the position of the Group and Society, together with a description of the principal risks and uncertainties that they face.

Directors' responsibilities for accounting records and internal control

The directors are responsible for ensuring that the Society:

- keeps accounting records in accordance with the Building Societies Act 1986; and
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Prudential Regulation Authority under the Financial Services and Markets Act 2000.

The directors have general responsibility for safeguarding the assets of the Society and the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

In so far as each of the directors is aware:

- There is no relevant audit information of which the Society's auditors are unaware; and
- The directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information.

The directors are responsible for the maintenance and integrity of the Society's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

On behalf of the Board of Directors
D.A. Harding
Chairman
13 April 2016

INDEPENDENT AUDITORS' REPORT
TO THE MEMBERS OF MANCHESTER BUILDING SOCIETY

Report on the financial statements

Our opinion

In our opinion, Manchester Building Society's Group and Society financial statements (the "financial statements"):

- give a true and fair view of the state of the Group's and of the Society's affairs as at 31 December 2015 and of the Group's and the Society's income and expenditure and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Emphasis of matter-Group and Society: Going concern

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of the disclosures made in note 1 to the financial statements concerning the Society and Group's ability to continue as a going concern. The directors have set out the risks and uncertainties for the business given its continued run-off and the ongoing development of plans to secure the business. These conditions, along with the other matters explained in note 1 to the financial statements, indicate the existence of a material uncertainty which may cast significant doubt about the Society and Group's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Society and Group were unable to continue as a going concern.

What we have audited

Manchester Building Society's financial statements comprise:

- the Group and Society Statements of Financial Position as at 31 December 2015;
- the Group and Society Statements of Comprehensive Income for the year then ended;
- the Group and Society Statements of Changes in Equity for the year then ended;
- the Group and Society Statements of Cash Flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and International Financial Reporting Standards as adopted by the European Union.

In applying the financial reporting framework the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinions on other matters prescribed by the Buildings Societies Act 1986

In our opinion:

- the Annual Business Statement and the Directors' Report have been prepared in accordance with the requirements of the Building Societies Act 1986;
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the accounting records and the financial statements; and
- the information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Building Societies Act 1986 we are required to report to you if, in our opinion:

- proper accounting records have not been kept by the Society; or
- the Society financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations and access to documents we require for our audit.

We have no exceptions to report arising from this responsibility.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Director's Responsibilities set out on page 14, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK & Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Society's members as a body in accordance with Section 78 of the Building Societies Act 1986 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of financial statements involves

We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Group's and Society's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report and Accounts to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Heather Varley (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Manchester

13 April 2016

STATEMENTS OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2015

	Note	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Interest receivable and similar income	2	14,401	18,609	14,832	18,220
Interest payable and similar charges	3	(5,853)	(7,973)	(5,853)	(7,973)
Net interest income		8,548	10,636	8,979	10,247
Fees and commission income		318	370	318	370
Fees and commission expense		(34)	(45)	(34)	(45)
Other operating income	4	295	173	871	870
Other operating charges	4	(58)	(58)	(201)	(201)
Income from investments	5	745	-	745	-
(Loss)/profit from derivatives	6	(10)	9	(11)	9
Net loss on financial assets designated at fair value through profit and loss	12	(46)	(314)	(46)	(314)
Total operating income		9,758	10,771	10,621	10,936
Administrative expenses	7	(6,599)	(5,845)	(5,817)	(5,421)
Depreciation	17	(242)	(227)	(101)	(87)
Operating profit before impairments and provisions		2,917	4,699	4,703	5,428
Impairment (losses)/gains	15	(3,219)	33	(2,258)	(3,750)
Financial Services Compensation Scheme Levy	32	(277)	(430)	(277)	(430)
(Loss)/profit on ordinary activities before income tax		(579)	4,302	2,168	1,248
Income tax (expense)/ credit	10	(4,295)	150	(4,295)	376
(Loss)/profit for the financial year		(4,874)	4,452	(2,127)	1,624

The Group and the Society have no other comprehensive income.

The notes on pages 20 to 54 form part of these accounts.

STATEMENTS OF CHANGES IN EQUITY

	Group 2015				Society 2015			
	Retained Earnings £000	Subscribed Capital £000	PPDS £000	Total £000	Retained Earnings £000	Subscribed Capital £000	PPDS £000	Total £000
Balance at 1 January 2015	(141)	9,788	17,461	27,108	(486)	9,788	17,461	26,763
Transactions with equity holders - interest on PIBS	(675)	-	-	(675)	(675)	-	-	(675)
Tax credit relating to interest on PIBS	135	-	-	135	135	-	-	135
(Loss) and total comprehensive income for year	(4,874)	-	-	(4,874)	(2,127)	-	-	(2,127)
Balance at 31 December 2015	(5,555)	9,788	17,461	21,694	(3,153)	9,788	17,461	24,096

	Group 2014				Society 2014			
	Retained Earnings £000	Subscribed Capital £000	PPDS £000	Total £000	Retained Earnings £000	Subscribed Capital £000	PPDS £000	Total £000
Balance at 1 January 2014	(4,053)	9,788	17,461	23,196	(1,570)	9,788	17,461	25,679
Transactions with equity holders - interest on PIBS	(675)	-	-	(675)	(675)	-	-	(675)
Tax credit relating to interest on PIBS	135	-	-	135	135	-	-	135
Profit and total comprehensive income for year	4,452	-	-	4,452	1,624	-	-	1,624
Balance at 31 December 2014	(141)	9,788	17,461	27,108	(486)	9,788	17,461	26,763

STATEMENTS OF FINANCIAL POSITION
AS AT 31 DECEMBER 2015

	Note	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
ASSETS					
Liquid assets					
Cash and balances with the Bank of England		55,861	63,053	55,861	63,053
Loans and advances to credit institutions	11	20,838	26,206	20,787	26,155
Investment securities	12	74	15,561	74	15,561
		76,773	104,820	76,722	104,769
Derivative financial instruments	13	403	2,146	403	2,134
Loans and advances to customers					
Loans fully secured on residential property	14	302,441	354,437	295,265	345,872
Loans fully secured on land	14	26,802	31,278	26,802	31,278
Other loans	14	1,375	1,657	1,375	1,657
		330,618	387,372	323,442	378,807
Investments					
Subsidiary undertakings	16	-	-	13,160	15,905
Trade investments	16	-	250	-	250
		-	250	13,160	16,155
Property, plant and equipment	17	5,920	8,313	470	275
Investment property	18	781	-	781	-
Current tax assets		356	356	335	335
Deferred tax assets	19	382	4,542	382	4,542
Other assets	20	1,343	948	1,322	922
Total assets		416,576	508,747	417,017	507,939
LIABILITIES					
Due to members	21	324,630	389,475	324,630	389,475
Deposits from banks	22	2,002	1,508	2,002	1,508
Other deposits	23	44,957	66,946	44,957	66,946
Derivative financial instruments	13	679	-	627	-
Other liabilities	25	1,582	2,796	1,291	2,333
Provisions for liabilities and charges	32	1,832	214	214	214
Subordinated liabilities	24	14,200	15,700	14,200	15,700
Subscribed capital	26	5,000	5,000	5,000	5,000
		394,882	481,639	392,921	481,176
Equity					
Retained earnings		(5,555)	(141)	(3,153)	(486)
Subscribed capital	26	9,788	9,788	9,788	9,788
Profit participating deferred shares	28	17,461	17,461	17,461	17,461
		21,694	27,108	24,096	26,763
Total equity and liabilities		416,576	508,747	417,017	507,939

The accounts on pages 17 to 54 were approved by the Board of Directors on 13 April 2016.

D.A. Harding
Chairman

A. Hodges
Chief Executive

I.A. Dewar
Director

STATEMENTS OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2015

	Note	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Cash flows from operating activities					
Interest and commission receivable		12,175	14,797	11,611	15,534
Interest expense payable		(5,453)	(7,577)	(5,453)	(7,577)
Fees and commission payable		(68)	(74)	(68)	(74)
Settlement of derivative contracts		2,412	(2,175)	2,347	(2,163)
Net trading and other income		5,137	1,053	4,945	1,043
Cash payments to employees and suppliers		(6,626)	(6,275)	(6,094)	(5,851)
Income taxes paid		-	-	-	-
Cash flows from operating activities before changes in operating assets and liabilities		7,577	(251)	7,288	912
Changes in operating assets and liabilities					
Net decrease in loans and advances to credit institutions		13	5	13	5
Net decrease in loans and advances to customers		53,869	69,977	54,512	66,154
Net (increase)/decrease in other assets		(383)	585	(400)	599
Net increase/(decrease) in deposits from banks		494	(4,035)	494	(4,035)
Net decrease in other deposits		(21,989)	(24,339)	(21,989)	(24,339)
Net decrease in amounts due to members		(64,845)	(113,111)	(64,845)	(113,111)
Net (decrease)/increase in other liabilities		(1,210)	575	(1,181)	283
Net decrease in liabilities and charges		386	(61)	13	(61)
Net cash used in operating activities		(26,088)	(70,655)	(26,095)	(73,593)
Cash flow from investing activities					
Investments in subsidiary undertakings		-	-	(17)	2,945
Sale of trade investment		995	-	995	-
Purchase of property and equipment	17	(320)	(182)	(296)	(190)
Sale of securities		15,941	17,203	15,941	17,203
Investment in securities		(500)	(10,021)	(500)	(10,021)
Net cash from investing activities		16,116	7,000	16,123	9,937
Cash flow from financing activities					
Repayment of subordinated loan	24	(1,500)	-	(1,500)	-
Interest paid on subscribed capital		(1,075)	(1,071)	(1,075)	(1,071)
Net cash used in financing activities		(2,575)	(1,071)	(2,575)	(1,071)
Net movement in cash and cash equivalents		(12,547)	(64,726)	(12,547)	(64,727)
Cash and cash equivalents at start of year		89,233	153,959	89,182	153,909
Cash and cash equivalents at end of year	27	76,686	89,233	76,635	89,182

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2015

1. Accounting policies and financial risk management

a) Summary of significant accounting policies

The principal accounting policies applied consistently in the preparation of these financial statements are set out below.

Basis of preparation: going concern

The Group's financial statements have been prepared on a going concern basis as explained below.

The long term continuing operation of the Society and the Group is dependent on successfully returning to lend to grow the balance sheet in order to maintain profitability and rebuild regulatory capital. At present the Society has insufficient capital to return to lending and continues to manage a long term run-off of the balance sheet.

The Board is developing a number of options which individually or in combination are reasonably expected to secure the future of the Society, enable it to continue to meet capital requirements and improve the quality of its regulatory capital. These options include improving its capital position, including through a capital injection from other parties, or securing its future through merger or alternative means.

The Board expects to develop these plans over the next few months. These plans may involve third parties and as such carry execution risk. Whilst an assessment of the different options has not yet been completed the Board is satisfied that it is reasonable to expect a successful outcome. Although these represent material uncertainties which may cast significant doubt about the Society's and Group's ability to continue as a going concern in the longer term, in the Board's opinion the going concern basis is appropriate.

In order to satisfy themselves that the Society and Group have adequate resources to continue to operate for the foreseeable future as a going concern, the directors have taken into account the following:

- The Group's profitable financial performance, before the head office property impairment and write-down of the recognised deferred tax asset, for the year ended 31 December 2015;
- The Group's current level of liquidity;
- The Group's financial position as at 31 December 2015 after having applied a write-down to the carrying value of the head office property and the recognised deferred tax asset in the light of the medium to long term financial projections;
- The Group's financial projections for the next 2 years, in particular for income, expenditure, assets, liabilities, liquidity and regulatory capital, including sensitivity analysis. These projections, based on a managed run-off of the balance sheet without a return to lending, indicate that the underlying operations of the Group, before costs associated with the development of its capital plans, will remain profitable in the short to medium term. In the medium term it is likely that the net interest margin will be insufficient to cover operating costs and loan impairment charges, resulting in operating losses;
- The ongoing legal claim against and prospects of recovery from Grant Thornton UK LLP, the previous external auditors;
- The planned redress of customers in respect of the acquired NMB MAC and CLC portfolios;
- The challenge of continuing to meet the CET1 qualitative regulatory capital expectation;
- Ongoing discussions with the PRA and other stakeholders regarding the development of a plan to secure the future of the Society and its strategic direction;
- The operational risks faced by the Society to develop and deliver the strategic plans;
- The Group's principal risks and uncertainties as set out in the Strategic Report on pages 6 to 7.

Should there be a material stress event in the economy or to financial markets that adversely impacts the Society, or the current options available to the Society are shown to not be viable, then there is less certainty as to the going concern position of the Society.

Having due regard to these matters and after taking into consideration the material uncertainties above the Board continues to adopt the going concern basis of accounting in preparing the financial statements.

Basis of preparation: accounting standards

The Group's financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Financial Reporting Interpretations Committee ("IFRIC") pronouncements as issued by the International Accounting Standards Board and as adopted by the European Union and with those parts of the Building Societies (Accounts and Related Provisions) Regulations 1998 applicable to building societies reporting under IFRS. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of all derivative contracts and certain other assets.

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 1c.

No further IFRS accounting standards and pronouncements identified as being relevant to the Group were adopted with effect from 1 January 2015.

The Group has noted that there are a number of further new accounting standards, which are neither adopted by the EU nor effective at 31 December 2015, but which are likely to be adopted over the coming years. The only one of these which is likely to have a significant impact on the Group is *IFRS 9 – Financial instruments*, which will replace *IAS39- Financial Instruments: Recognition and Measurement*

The final version of IFRS 9 has been issued by the International Accounting Standards Board but has not yet been endorsed by the EU. The effective date will be 1 January 2018, although it will be available for early adoption.

The standard includes changes for classification and measurement of the Group's financial assets and liabilities, the recognition of impairment, and hedge accounting.

The most significant impact on the Group is likely to be in respect of the measurement of impairment of financial assets. Under IFRS 9, impairment will be based on expected credit losses ("ECL") rather than incurred credit losses which is the methodology the Group currently adopts under IAS39. At initial recognition, an ECL provision is required for default events in the next 12 months, whilst following a significant increase in credit risk, a lifetime ECL is required. The review of credit risk and the calculation of ECL are required to be unbiased and probability weighted, and should include all available relevant information, with assessments of current conditions and forecasts of future economic conditions. As a result the recognition and measurement of impairment is more forward looking than is the case under IAS39. Consequently, it is likely to lead to an increase in the total level of provision in many businesses.

The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet on transition to IFRS 9, with no requirement to restate comparative periods.

The directors do not expect the other standards to have a material impact on the financial statements of the Society and Group.

Basis of consolidation

The Group's accounts include the accounts of the Society, its subsidiary undertakings and for the period up to 7 December 2015 two entities, NMB Mortgage Acquisition Company Limited ("NMB MAC") and The Consumer Loans Company Limited ("CLC"), in which the Group held no shares but over which, per IFRS 10, it exerted control. The way in which the Group met the definition of control over these two entities, as set out in IFRS 10, is described more fully in Note 16.

On 7 December 2015, the Group acquired legal title to the loans owned by CLC over which it had previously had a beneficial interest. As a result the Group no longer benefits from the cash flows of CLC or exerts significant influence over it and since it does not then meet the definition of a connected undertaking it does not consolidate CLC after that date. The Group now receives the cash flows from these loans directly. NMB MAC is still consolidated at 31 December 2015.

The Society and its subsidiaries have accounting periods ending on 31 December, whilst NMB MAC has an accounting period ending on 28 February. For consolidation purposes, the accounting records of NMB MAC have been prepared at 31 December and consolidated for the 12 months ended 31 December. CLC has been consolidated until 7 December 2015. The accounting policies of the subsidiary undertakings are materially consistent with the Group accounting policies. The accounting policies for the two other entities, where different from those of the Group, have been brought in line with those of the Group on consolidation. The Society's statement of financial position includes the investment in the subsidiary undertakings at cost, less any provision for impairment.

Interest income and expense

Interest income and expense are recognised in the Statements of Comprehensive Income for all financial instruments measured at amortised cost using the effective interest rate method. The effective interest rate method is a method of allocating the income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated cash flows (excluding future expected credit losses) to the net carrying amount of the asset over the expected life of the instrument.

In calculating the effective interest rate all contractual terms of the financial instrument are taken into account, along with all fees paid or received, all transaction costs and any other premia or discounts.

Charges in respect of the estimated interest refund element of the customer redress provision are debited against interest income, when the provision is established.

Insurance contracts

The Society has a portfolio of lifetime mortgage loans secured on Spanish residential property. A particular clause of the mortgage contract meets the definition of an insurance contract; where a borrower dies or goes into long term care and a redemption receipt is less than the contractual sum owed the Society does not have any further ability to recover amounts from the borrower or the estate.

Under IFRS 4 the Society has continued to account for these mortgage contracts using its existing accounting policies. The mortgage contract has been classified as being not unbundled. The impact of assessing the contracts as being "not unbundled" is that the income earned on the mortgage contracts is not split between interest and insurance premium and that the mortgage asset is included within loans and advances at the present value of future cash flows.

Measurement and recognition of the income earned on the mortgage contract has been undertaken in line with the Society's other mortgage contracts; the income earned has been included in the Income Statement within the Interest and Similar Income category. Within the Statement of Financial Position the mortgage asset and any impairment which has been calculated is disclosed in line with IAS 39.

The insurance risk liability associated with the no-negative equity guarantee is calculated by estimating potential shortfalls arising at redemption, discounted at the effective interest rate, and is represented by the impairment provision. The assessment incorporates assumptions relating to future house price values at the time of account redemption. Its assessment is also based on expected future outcomes relating to the date on which an account redeems which, given the nature of the product is expected to be on death of the borrower, but can be affected by health issues that would see borrowers move into care; it can also be affected by non-health related voluntary pre-payment. The insurance liability arising as a result of the no negative equity guarantee is presented within Note 14 to the financial statements, under the heading "Insurance risk provisions".

Fees and commissions

Fees and commissions relating to the creating of loans and advances to members are recognised within interest income using the effective interest rate method.

Other operating income

The Group recognises foreign exchange gains and losses and rents receivable as other operating income. The Society recognises other operating income relating to the interest that it charges on the loans made to its subsidiary undertakings.

Income from investments

Income from investments is recognised when an irrevocable agreement to sell the investment is in place.

Financial assets

The Group classifies its financial assets in the following categories under IAS 39:

(i) Financial assets at fair value through profit or loss

Derivative financial instruments. These instruments hedge the exchange rate risk on the Group's Euro denominated Spanish mortgages. These instruments are carried at their fair value with changes in their fair value reflected in profit or loss as part of total operating income. Hedge accounting has not been applied by the Group.

Investment securities. These instruments are carried at their market value which reflects the fair value of the asset. Changes in their fair value are recognised in profit or loss as part of total operating income. Any gain or loss on disposal is taken through profit or loss.

Financial assets at fair value through profit or loss are subsequently carried at fair value. Fair values are obtained in line with the three tier hierarchy described in IFRS 7 from quoted market prices in active markets, revaluation techniques using specialist tools and confirmations from counterparties.

Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss category are included in the profit or loss in the period in which they arise.

The fair values of financial assets as at 31 December 2015 and 31 December 2014 are detailed in the fair values of financial assets and liabilities section on page 32.

(ii) Loans and receivables

Loans and advances to credit institutions. These are sums deposited in instantly accessible bank accounts with major high street banks, used for liquidity purposes.

Loans and advances to customers. These are sums advanced to the Group's borrowers, secured on property, land or (in a very restricted number of instances) unsecured.

Loans and receivables are carried at amortised cost using the effective interest method.

Purchases and sales of financial assets at fair value through profit or loss are recognised on the trade-date being the date on which the Group legally commits to purchase or sell the asset. Loans are recognised when cash is advanced to the borrowers. Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets are no longer recognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership.

Impairment

With regard to mortgage assets, the Group assesses at each financial position date whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence of impairment includes events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that a financial asset or group of assets is impaired includes accounts going into arrears and other observable data that comes to the attention of the Group about the following loss events:

i. the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
ii. it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
iii. observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the Group, including:

   – adverse changes in the payment status of borrowers in the Group; or

   – national or local economic conditions that correlate with defaults on the assets in the Group. The above assessment includes those mortgage assets which are subject to forbearance arrangements.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables 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 impairment value is then reflected in a separate account from the underlying assets in the Group's financial records and is recognised in the Statement of Comprehensive Income.

The Group's policy in relation to any properties that it has taken into possession is that it will seek their disposal with a view to minimising the losses that it may incur.

Investment in subsidiary undertakings

Subsidiaries are all entities over which the Group has control. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Investments in the Society's subsidiary undertakings are recorded in the Statement of Financial Position at historic cost less any provision for impairment. Impairment is assessed in line with *IAS 36 – Impairment of Assets* comparing the carrying value of the investment against future cash flows from the subsidiary undertakings.

Property, plant and equipment

All property, plant and equipment is stated at historical cost less depreciation and any provision for impairment. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in each asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives, as follows:

- Freehold office premises: over 50 years.
- Office premises structural alterations: over 20 years.
- Office fixtures and fittings: over 10 years.
- Computer and sundry equipment: over 5 years.
- Other assets: over 4 years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each financial reporting date. The freehold head office property has been tested for impairment and written down to fair value less estimated cost of disposal.

Investment property

Investment property is residential property acquired as a result of the settlement of an impaired mortgage asset. The properties are being held, pending their eventual sale, and are carried at their fair value after taking into account estimated costs to sell. Changes in their fair value are recognised in profit or loss as part of total operating income. Any gain or loss on disposal is taken through profit or loss.

Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition including: cash in hand and non-restricted balances with central banks, loans and advances to banks and amounts due from other banks.

Corporation tax

Corporation tax is charged at the current rate calculated on the basis of the profit on ordinary activities as adjusted in line with HMRC requirements for taxation purposes.

Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the financial position date and are expected to apply when the deferred tax asset is realised or the liability is settled.

Deferred tax assets ("DTAs") are recognised to the extent that it is probable that future taxable profit will be available against which deductible temporary differences can be utilised.

Pensions - Group defined contribution scheme

The Group operates a defined contribution pension scheme for its employees. All the costs incurred by the employer are included in profit or loss.

Foreign currency

Foreign currency transactions are translated into sterling, using the exchange rates prevailing at the dates of the transactions (spot exchange rate). Foreign exchange gains and losses resulting from the settlement of such transactions and from the re-measurement of monetary items at year-end exchange rates are recognised in the Statement of Comprehensive Income.

Leases

The Group has entered into operating lease agreements. Rental income and expenditure is recognised in profit or loss on a straight line basis over the term of the lease in other income and charges in the Statement of Comprehensive Income.

Financial Liabilities

All financial liabilities including shares, deposits, derivative financial instruments, debt securities and subordinated liabilities are recognised initially at fair value, being the issue proceeds, net of transaction costs incurred as appropriate. Financial liabilities, except for derivative financial instruments, are subsequently measured at amortised cost using the effective interest rate method. Following initial recognition derivative financial instruments continue to be recognised at fair value.

Offsetting

For the financial assets and liabilities subject to enforceable master netting arrangements or similar arrangements, each agreement between the Group and the counterparty allows for net settlement of the relevant financial assets and liabilities when both elect to settle on a net basis. In the absence of such an election, financial assets and liabilities will be settled on a gross basis. However, each party to the master netting agreement or similar agreement will have the option to settle all such amounts on a net basis in the event of default of the other party.

Provisions for liabilities and charges

A provision is recognised in the balance sheet if the Group has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made.

Financial Services Compensation Scheme ("FSCS")

During 2008, claims were made on the FSCS following the failure of Bradford & Bingley plc, Heritable Bank plc, Kaupthing Singer and Friedlander Limited and London Scottish Bank plc. In order to fund the claims made under its terms of operation, the FSCS has borrowed from the Bank of England and HM Treasury. The FSCS pays interest on its borrowings, it incurs operating expenses in its own right and incurs capital losses where shortfalls arise on the realisations of assets that it is managing from the failed banks listed above. The costs of the FSCS are passed on to all UK banks and building societies.

The Society makes provision for the charge based on estimates of its share of the total levy that the FSCS will raise by comparing its level of "protected deposits" with those of all deposit taking institutions covered by the FSCS. The Society's estimates are sensitive to the level of estimated management expenditure incurred by the FSCS and the level of capital losses that will arise in future periods as the FSCS undertakes the management of the assets of the failed banks.

In accordance with *IFRIC 21 - Levies* the trigger date for recognition of a provision in respect of the FSCS levy is 1 April each year and at 31 December the Society holds an accrual for one year's interest levy.

Customer redress provision

Provision for customer redress is made when the Group is aware of a specific historic conduct or regulatory issue and it is probable that customer remediation will be required to settle the obligation. Provision is made for the estimated cost of interest refunds, which is debited against interest income, and other associated costs which are debited against other administrative expenses.

Permanent Interest Bearing Shares

The Society has two tranches of Permanent Interest Bearing Shares in issue. Both sets were issued with the intention of enhancing the Society's regulatory capital position. The PIBS issued in 2005 confer unconditional discretion on the Society's Board to cancel in part or in whole any interest payment due. Interest on the 1999 PIBS can only be cancelled in a restricted number of circumstances; the Board does not have an unconditional right to cancel this interest. Therefore, in accordance with *IAS 32 - Financial Instruments: Presentation*, within the Financial Statements the 2005 PIBS are classified as equity and the 1999 PIBS are classified as a liability. Interest paid on the 1999 PIBS issue is shown in the Statement of Comprehensive Income whereas interest paid on the 2005 PIBS issue is shown in the Statement of Changes in Equity.

Profit Participating Deferred Shares

The Society has £18m of Profit Participating Deferred Shares, issued during 2013 (see Note 28). These instruments qualify as equity within the Statement of Financial Position. Whilst no coupon has been paid on the PPDS, any such cost would be recorded through the Statement of Changes in Equity.

b) Financial risk management

Strategy in using financial instruments

The Group accepts deposits from customers at both fixed and floating rates of interest, some of which are for fixed periods and others are open-ended; it seeks to enhance its interest margins by investing these funds in high-quality mortgages, liquidity instruments and liquid assets.

The Society has more fixed rate mortgages than fixed rate savings accounts. In order to manage the interest rate risk that arises, the Society may enter into simple-form interest rate swap arrangements with the intention of gaining some economic certainty as to its net interest margin position.

The Group uses financial instruments to invest liquid asset balances and raise funding. The Group also uses derivative financial instruments (derivatives) to manage the risks arising from its operations.

The Board has authorised the use of derivatives by the Group to reduce the risk of loss arising from changes in market risks in accordance with Section 9A (4) of the Building Societies Act 1986 and derivatives are used by the Group for economic hedging purposes only. The Group does not run a trading book.

The principal derivatives used by the Group are foreign exchange contracts that are used to economically hedge Group Statement of Financial Position exposures.

The Board does not intend to hedge its fixed rate mortgages using interest rate swaps at this time; this position is monitored regularly.

Credit risk - exposure

Credit risk is the risk that an individual or institutional counterparty to whom the Society has lent money will be unable to re-pay the sums in full when they fall due.

The Group manages the levels of credit risk it accepts by placing limits on the amount available in relation to individual borrowers and groups of borrowers. Such risks are monitored on a revolving basis and are subject to a regular review. Policy limits on the level of credit risk by product, industry sector and by country are approved half yearly by the Board. The exposure to any one borrower, including banking counterparties, is further restricted by sub-limits covering on and off balance sheet exposures. Actual exposures against limits are monitored daily.

The Group's most significant concentration of credit risk is within the loans secured on residential property in the UK. The following table shows the credit exposure, which is the maximum potential exposure before provisions and including committed facilities.

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Financial assets				
Loans and advances to credit institutions	20,838	26,206	20,787	26,155
Investment securities	74	15,561	74	15,561
Gross loans and advances - on residential property and land	307,423	361,696	292,322	346,458
Gross loans and advances - lifetime mortgages	39,819	42,953	39,819	42,953
Gross loans and advances - other loans	1,388	1,678	1,388	1,678
Loans to subsidiary undertakings	-	-	13,158	18,613
Derivatives - exchange rate swaps	403	2,146	403	2,134
	369,945	450,240	367,951	453,552

Impairment provisions are provided for losses that have been incurred at the financial position date. The figure for lifetime mortgages is stated after deduction of an effective interest rate provision.

Credit risk - forbearance

The Society's forbearance strategy is to seek to agree with borrowers in financial difficulty the provision of short to medium term assistance with their monthly mortgage payments, in order to avoid or mitigate the risk of financial loss. The range of forbearance options available in certain circumstances includes arrangements to clear the arrears over a reasonable period of time, payment concessions, and capitalisation of arrears. For mortgages that are not past due, conversion to interest only payment terms, an extension of term, or suspension of monthly payments pending sale of the property are available as options to reduce the monthly payment due and these seek to avoid a mortgage entering arrears and becoming past due, allowing time for a borrower to regularise their financial position.

As at 31 December 2015, the Society had 42 accounts (2014: 47) with balances of £5.0m (2014: £5.6m) where conversion to interest only or an extension of term had taken place. Of these, 35 accounts (2014: 29) were neither past due nor impaired, and 7 (2014: 18) were past due and/or impaired. The aggregate capital balance was £2.0m (2014: £3.0m); aggregate arrears £21k (2014: £28k); and aggregate impairment provision was £nil (2014: £5k).

The forbearance strategy seeks to avoid arrears arising or further increasing and to allow account performance to be restored by supporting the mortgage payments being brought up to date or to provide a period of time for repayment of the amount owed. The assessment of impaired loans incorporates management work-out strategies in relation to a number of credit exposures. If expectations were to change then this would affect the impairment risk. This is incorporated into the assessment of impairment provisions.

There are no specific concentrations of accounts in forbearance in relation to portfolios or geographical areas.

Credit risk – Loans and advances to customers

The analysis shown below, in relation to loans and advances to customers is based on the Group's balances. Information is disclosed for the Society where there is significant variance between the Group and Society figures.

- Of the £348.6m of gross mortgage assets in this class £316.0m (90.6%) (2014: 91.1%) is fully secured on residential property and £31.2m (9.0%) (2014: 8.4%) is fully secured on land.
- £1.4m (0.4%) (2014: 0.4%) is unsecured personal loans.
- With balances of £39.8m Lifetime mortgages represent 11.4% of this class (2014:10.7%).

Secured lending – fully secured on residential property

The average loan to valuation ("LTV") of the Group's lending that is fully secured on residential property is estimated at 36% (2014: 39%). Further analysis of the Group's residential property lending is detailed below.

	2015 %	2014 %
<70%	72	73
70% - 80%	13	13
80% - 90%	7	7
90% - 100%	3	3
>100%	5	4
Average loan to value of stock - UK mortgages	33	37
Average loan to value of stock - Spanish mortgages	78	74

Estimates of current LTV are obtained by indexing the valuation at the last physical inspection of the property, by reference to externally published data. At 31 December 2015, 28% of the loan book had an LTV of 70% or greater (2014: 27%). In the event that valuations were to increase by 5%, at 31 December 2015 this would reduce the proportion of the loan book that had an LTV of 70% or greater to 23% (2014: 22%); in the event that House Price Indices ("HPIs") decreased by 5% at 31 December 2015, the proportion of the loan book with an LTV of 70% or greater would increase to 34% (2014: 34%).

The Group continues to review regularly the quality of its loans that are fully secured on residential property. The proportion of these loans more than 3 months in arrears is 3% (2014: 3%). There are no lifetime mortgages which are past due.

The table below provides further information on the payment due status of gross loans fully secured on residential property.

	2015 £m	2015 %	2014 £m	2014 %
Not impaired:				
Neither past due nor impaired	278.0	88	324.5	88
Past due up to 3 months	13.1	4	16.1	4
Past due 3 to 6 months	2.3	1	4.2	1
Past due 6 to 12 months	0.4	-	2.2	1
Past due over 12 months	0.7	-	0.3	-
Impaired:				
Not past due and up to 3 months	2.1	1	2.1	-
Past due 3 to 6 months	0.1	-	-	-
Past due 6 to 12 months	-	-	0.1	-
Past due over 12 months	2.1	1	2.2	1
Possessions *	2.3	1	2.5	1
	301.1	96	354.2	96
NMB MAC mortgage book - beneficial interest is held **	13.5	4	13.4	4
CLC mortgage book **	1.4	-	1.4	-
	316.0	100	369.0	100

* For properties in possession, £2.7m (2014: £2.4m) of collateral is held. In the analysis above, for all past due loans, £38.9m (2014: £50.0m) of collateral is held.

** The NMB MAC and CLC mortgage books of second charge loans were initially acquired at a deep discount and are considered impaired. Arrears banding information is not presented for these portfolios as there is insufficient reliable data to determine this accurately. The net book value of these loan books after impairment provisions is £6.6m (2014: £7.8m).

In the analysis above, loans which are not impaired and are less than 3 months past due and which have collective impairment provisions total £11.9m (2014: £12.6m).

At 31 December 2015 the Group held individually identified impairment provisions of £1.7m (2014: £2.0m).

Geographical Analysis

The table below provides information on the geographical split of the Group's gross lending on residential property.

	2015 £m	2015 %	2014 £m	2014 %
East Midlands	4.6	1	6.0	2
Greater London	18.8	6	23.1	6
London	43.5	14	51.6	14
North	7.5	2	7.9	2
North West	121.7	39	139.2	38
Other	10.8	3	12.5	3
South East	25.4	8	31.4	9
South West	9.8	3	12.8	3
Wales	7.9	3	9.6	3
West Midlands	9.9	3	12.1	3
Yorkshire	16.3	5	20.8	6
Total UK properties	276.2	87	327.0	89
Spain (lending is lifetime mortgages)	39.8	13	42.0	11
	316.0	100	369.0	100

Secured lending – fully secured on land

The constitution of gross loans fully secured on land by industry type is as follows:

	2015 £m	2015 %	2014 £m	2014 %
Offices	8.9	29	10.1	29
Shops	7.1	23	7.7	23
Industrial	4.8	15	5.4	16
Restaurants, Hotels and other	10.4	33	11.2	32
	31.2	100	34.4	100

The table below provides further information on the payment due status of gross loans that are fully secured on land:

	2015 £m	2015 %	2014 £m	2014 %
Not impaired:				
Neither past due nor impaired	22.5	72	26.8	78
Past due up to 3 months	1.5	5	1.1	3
Past due 3 to 6 months	0.7	2	0.7	2
Past due 6 to 12 months	0.3	1	0.1	-
Past due over 12 months	-	-	0.3	1
Impaired:				
Not past due and up to 3 months	0.7	2	0.9	3
Past due 3 to 6 months	1.2	4	-	-
Past due 6 to 12 months	-	-	-	-
Past due over 12 months	2.1	7	2.1	6
Possessions *	2.2	7	2.4	7
	31.2	100	34.4	100

* For properties in possession £1.9m of collateral is held (2014: £2.1m). In the analysis above, for all past due loans £5.1m of collateral is held (2014: £5.9m).

In the analysis above, loans which are not impaired and are less than 3 months past due have collective impairment provisions of £18k (2014: £20k).

At 31 December 2015 the Group held individually identified impairment provisions of £4.4m (2014: £3.1m).

Unsecured lending

The table below provides further information on the payment due status of gross unsecured loans:

	2015 £m	2015 %	2014 £m	2014 %
Not impaired:				
Neither past due nor impaired	0.9	64	1.5	88
Past due up to 3 months	0.5	36	0.1	6
Past due 3 to 6 months	-	-	0.1	6
	1.4	100	1.7	100

In the analysis above, loans which are not impaired and are less than 3 months past due have collective impairment provisions of £13k (2014: £nil).

At 31 December 2015 the Group held individually identified impairment provisions of £nil (2014: £21k).

Credit risk – loans and advances to banks and investment securities

Credit risk relating to liquid assets arises from the investments held by the Group in order to meet business-as-usual liquidity requirements. This aspect of credit risk is managed by the Group's Risk Committee, which sets and monitors compliance with policy and limits. The equivalent information has not been disclosed for the Society as there is no significant variance between the Group and Society figures.

The maximum individual counterparty exposure at the financial position date was £56m (2014: £63m) which was on deposit with the Bank of England. The number of active counterparties at the financial position date was 5 (2014: 6). All counterparties are UK 'High Street' blue chip banks whose registered address is within the UK and who are authorised by the PRA and regulated by the FCA and PRA as lead regulators; this is in support of the Board's low risk appetite approach to banking counterparty risk.

For credit purposes, the liquid asset portfolio comprises the following sub-portfolios as at 31 December:

	2015 £m	2015 %	2014 £m	2014 %
Financial institutions	76.7	100	104.7	100
Mortgage backed securities	0.1	-	0.1	-
	76.8	100	104.8	100

The Group's Risk Committee monitors exposure concentrations against a variety of criteria including industry sector / asset class and country of counterparty.

Geographical exposure, assessed by reference to the registered address of the counterparty and the lead regulator of the entity, is solely within the UK.

Industry sector/asset class exposure:

	2015 £m	2015 %	2014 £m	2014 %
UK financial institutions	76.7	100	104.7	100
Asset backed securities	0.1	-	0.1	-
	76.8	100	104.8	100

Collateral held as security for liquid assets is determined by the nature of the instrument. Loans and debt securities are generally unsecured with the exception of asset backed securities which are secured by pools of financial assets.

Credit risk – foreign exchange derivatives and offsetting

Foreign exchange derivative financial assets are subject to offsetting, enforceable, master netting agreements. The gross amounts of these assets on the balance sheet is £403k (2014: £2,146k). Related amounts not set off are £679k (2014: £nil) financial liabilities with cash collateral received of £230k (2014: £600k).

Foreign exchange derivative financial liabilities are subject to offsetting, enforceable, master netting agreements. The gross amounts of these liabilities on the balance sheet is £679k (2014: £nil). Related amounts not set off are £403k (2014: £2,146k) financial assets with cash collateral paid of £955k (2014: £525k).

Cash flow and fair value interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. The Board sets limits on the level of mismatch of interest rate repricing that may be undertaken, which are monitored monthly.

The table below summarises the Group's exposure to interest rate risks. Included in the table are the Group's assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates. The equivalent information has not been disclosed for the Society as there is no significant variance between the Group and Society figures.

The Group's interest rate sensitivity exposure at 31 December 2015 and 31 December 2014 was:

	Effective interest rate %	0-3 months £000	3-6 months £000	6-12 months £000	1-5 years £000	5-10 years £000	10-20 years £000	20-30 years £000	Over 30 years £000	Non-interest bearing £000	Total £000
At 31 December 2015											
Assets											
Cash and central banks balances	0.50	55,844	-	-	-	-	-	-	-	17	55,861
Due from other banks	0.71	20,825	-	-	-	-	-	-	-	13	20,838
Investment securities	0.99	74	-	-	-	-	-	-	-	-	74
Loans to customers	3.82	266,430	2,417	2,965	4,197	2,513	11,094	4,354	119	-	294,089
Lifetime mortgages	6.76	-	-	353	2,979	2,903	18,031	12,263	-	-	36,529
Other assets		1,346	12	-	-	-	-	-	-	7,827	9,185
Total assets		344,519	2,429	3,318	7,176	5,416	29,125	16,617	119	7,857	416,576
Liabilities											
Due to other banks	0.65	1,000	1,000	-	-	-	-	-	-	2	2,002
Other deposits	0.84	42,016	500	2,216	-	-	-	-	-	225	44,957
Due to members	1.21	301,703	3,958	9,243	8,910	-	-	-	-	816	324,630
Subordinated liabilities	4.07	9,200	-	-	-	-	5,000	-	-	-	14,200
Other liabilities		308	283	318	-	-	-	-	-	3,184	4,093
Subscribed capital		-	-	-	-	-	-	-	-	14,788	14,788
Profit participating deferred shares		-	-	-	-	-	-	-	-	17,461	17,461
Reserves		-	-	-	-	-	-	-	-	(5,555)	(5,555)
Total liabilities		354,227	5,741	11,777	8,910	-	5,000	-	-	30,921	416,576
Cumulative interest rate sensitivity gap		(9,708)	(3,312)	(8,459)	(1,734)	5,416	24,125	16,617	119	(23,064)	-

	Effective interest rate %	0-3 months £000	3-6 months £000	6-12 months £000	1-5 years £000	5-10 years £000	10-20 years £000	20-30 years £000	Over 30 years £000	Non-interest bearing £000	Total £000
At 31 December 2014											
Assets											
Cash and central banks balances	0.50	63,028	-	-	-	-	-	-	-	25	63,053
Due from other banks	0.66	26,154	-	-	-	-	-	-	-	52	26,206
Investment securities	1.48	10,057	5,050	-	-	-	-	-	-	454	15,561
Loans to customers	3.88	314,849	1,703	3,513	10,935	2,007	11,315	6,207	239	-	350,768
Lifetime mortgages	7.02	-	-	1,733	1,041	2,125	14,423	16,309	973	-	36,604
Other assets		1,285	877	716	76	-	-	-	-	13,601	16,555
Total assets		415,373	7,630	5,962	12,052	4,132	25,738	22,516	1,212	14,132	508,747
Liabilities											
Due to other banks	0.93	1,000	-	500	-	-	-	-	-	8	1,508
Other deposits	1.24	52,973	5,500	8,214	-	-	-	-	-	259	66,946
Due to members	1.26	363,901	6,625	2,892	15,065	-	-	-	-	992	389,475
Subordinated liabilities	4.38	10,700	-	-	-	-	5,000	-	-	-	15,700
Other liabilities		-	-	-	-	-	-	-	-	3,010	3,010
Subscribed capital		-	-	-	-	-	-	-	-	14,788	14,788
Profit participating deferred shares		-	-	-	-	-	-	-	-	17,461	17,461
Reserves		-	-	-	-	-	-	-	-	(141)	(141)
Total liabilities		428,574	12,125	11,606	15,065	-	5,000	-	-	36,377	508,747
Cumulative interest rate sensitivity gap		(13,201)	(4,495)	(5,644)	(3,013)	4,132	20,738	22,516	1,212	(22,245)	0

The Society's financial performance is sensitive to changes in interest rates in respect of the interest it earns. Based on the assets and liabilities in the balance sheet at 31 December 2015 an increase of 1% in market interest rates across all maturities would reduce income and equity by £4.8m (2014: £5.2m reduction). These amounts are for indication only, and represent the impact of an unexpected overnight 1% parallel shift in the yield curve, without any subsequent management action, and consequently do not represent amounts that are at risk. ALCO monitor a variety of interest rate shocks from 0.5% to 2%.

Liquidity risk

The Group is exposed to daily calls on its available cash resources from customer withdrawals, maturing deposits, loan draw-downs and guarantees, and from margin and other calls on cash-settled derivatives. The Group does not maintain immediately available cash resources to meet instantly all of these needs, as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty.

The Board sets limits on the minimum proportion of maturing funds available to meet such calls and on the nature of the funds that are available to the Society on an instantly accessible basis; with the latter, the Board strategy has been to place notable sums with the Bank of England and with other UK "High Street" banks in order to ensure that it meets its objectives of ensuring that all such funds are highly liquid.

The liquidity profile throughout 2015 has aligned with the Board's low risk appetite in this area and day-to-day operations of the liquidity portfolio saw compliance with all policy limits throughout the period. Such policy limits are reviewed on a daily basis and it should be noted that the Group has consistently maintained cash resources in excess of the policy minimum.

The equivalent information has not been disclosed for the Society as there is no significant variance between the Group and Society figures.

In absolute terms liquidity has reduced in line with the overall reduction in the balance sheet. The Society has continued to hold liquidity levels well in excess of the regulatory thresholds during the year. This has contributed to downward pressure on net interest income.

The table below analyses the Group's contractual cash flows under financial liabilities.

	On demand £000	0-3 months £000	3-12 months £000	1-5 years £000	5-10 years £000	10-15 years £000	Over 15 years £000	Total £000
At 31 December 2015								
Due to members	153,744	148,776	6,957	15,153	-	-	-	324,630
Due to other banks and depositors	3,947	39,308	3,749	-	-	-	-	47,004
Derivative financial instruments	-	78	601	-	-	-	-	679
Other liabilities	1,155	268	1,991	-	-	-	-	3,414
PIBS interest	-	-	400	1,600	2,000	2,000	2,000	8,000
Subordinated liabilities	-	145	434	2,313	11,272	1,675	5,605	21,444
Total outflow	158,846	188,575	14,132	19,066	13,272	3,675	7,605	405,171
	£000	£000	£000	£000	£000	£000	£000	£000
At 31 December 2014								
Due to members	238,751	137,772	7,496	5,456	-	-	-	389,475
Due to other banks and depositors	11,866	37,358	19,419	-	-	-	-	68,643
Other liabilities	2,128	295	587	-	-	-	-	3,010
PIBS interest	-	-	400	1,600	2,000	2,000	2,000	8,000
Subordinated liabilities	-	1,664	433	2,307	11,511	1,675	5,977	23,567
Total outflow	252,745	177,089	28,335	9,363	13,511	3,675	7,977	492,695

The table below analyses the Group's assets and liabilities into relevant maturity groupings based on the remaining period at the financial position date to the contractual maturity date. The equivalent information has not been disclosed for the Society as there is no significant variance between the Group and Society figures.

	0-3 months £000	3-6 months £000	6-12 months £000	1-5 years £000	5-10 years £000	10-20 years £000	20-30 years £000	Over 30 years £000	Total £000
At 31 December 2015									
Assets									
Cash and central banks balances	55,861	-	-	-	-	-	-	-	55,861
Due from other banks	20,838	-	-	74	-	-	-	-	20,912
Derivative financial instruments	391	12	-	-	-	-	-	-	403
Loans to customers	10,417	3,479	6,962	57,771	54,739	141,194	18,258	1,269	294,089
Lifetime mortgages	-	-	353	2,979	2,903	18,031	12,263	-	36,529
Other assets	350	-	1,349	1,163	-	-	-	5,920	8,782
Total assets	87,857	3,491	8,664	61,987	57,642	159,225	30,521	7,189	416,576
Liabilities									
Due to other banks	1,000	1,002	-	-	-	-	-	-	2,002
Other deposits	42,241	500	2,216	-	-	-	-	-	44,957
Derivative financial instruments	78	283	318	-	-	-	-	-	679
Due to members	302,521	3,958	2,999	15,152	-	-	-	-	324,630
Subordinated liabilities	-	-	-	-	9,200	5,000	-	-	14,200
Other liabilities	1,423	-	1,991	-	-	-	-	-	3,414
Total liabilities	347,263	5,743	7,524	15,152	9,200	5,000	-	-	389,882
Net liquidity gap	(259,406)	(2,252)	1,140	46,835	48,442	154,225	30,521	7,189	26,694
At 31 December 2014									
Total assets	111,119	9,252	10,452	69,211	66,941	183,929	47,204	10,639	508,747
Total liabilities	428,512	12,754	15,717	5,456	9,200	5,000	-	-	476,639
Net liquidity gap	(317,393)	(3,502)	(5,265)	63,755	57,741	178,929	47,204	10,639	32,108

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. The Society does not expect to be completely matched, as transacted business is often of uncertain term and of different types. An unmatched position potentially enhances profitability but could also increase the risk of losses.

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 and exchange rates.

Currency risk

At 31 December 2015 the Group had a currency exposure of €58.2m (2014: €57.7m) in loans and receivables. At the balance sheet date this exposure is predominantly matched with exchange rate swaps. The Board sets limits on the level of exposures to foreign currency and these are monitored daily.

Foreign Exchange Sensitivity

The Group has assessed, on an indicative basis, the effect that a 10bp depreciation of the Euro would have on the Group's income, as a result of a revaluation of the balance sheet assets and liabilities.

	2015	**2014**
	£000	**£000**
Effect on income with no Euro forward contracts	(2,928)	(3,231)
Effect on income with Euro contracts fully matching Euro denominated assets	17	1

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 knowledgeable, willing market participants at the measurement date.

Wherever possible, fair values have been calculated using unadjusted quoted market prices in active markets for identical instruments held by the Group. Where quoted market prices are not available, or are unreliable, fair values have been determined using valuation techniques which, to the extent possible, use market observable inputs, but in some cases use non-market observable inputs.

Valuation techniques used include discounted cash flow analysis and pricing models and, where appropriate, comparison to instruments with characteristics similar to those of the instruments held by the Group.

Because a variety of estimation techniques are employed and significant estimates made, comparisons of fair values between financial institutions may not be meaningful. Readers of these financial statements are thus advised to use caution when using this data to evaluate the Group's financial position.

The fair value measurement basis used is as follows:

Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Valuation techniques where all inputs are taken from observable market data, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 Valuation techniques where significant inputs are not based on observable market data. None of the Group's financial assets or liabilities are valued using this technique.

Fair values of financial assets and liabilities

The following methods and assumptions have been applied in determining the fair value of the financial instruments in these reports:

i. Trade investments are measured at cost as the fair value cannot be estimated reliably.
ii. The fair value of derivatives and investment securities are calculated by utilising internal valuation models using a discounted cash flow model based on a current yield curve appropriate for the remaining term to maturity. External market data is used within these internal valuation models. Derivatives are held for trading. Investment securities are designated at fair value through profit or loss. Movements in the valuations of derivatives and investment securities are treated as fair value through profit and loss, and these financial assets and liabilities are grouped into the fair value hierarchy under level 2.
iii. The fair value of loans and advances to customers at a variable rate of interest is assumed to approximate to their carrying amounts. The fair value of loans and advances at a fixed rate of interest is estimated by internal valuation models. External market data is used within these internal valuation models.

All other financial assets and liabilities are held at amortised cost.

The Group has disclosed within these financial statements all the assets and liabilities for which fair values are required.

All financial assets are classified as loans and receivables, with the exception of derivative financial instruments and investment securities which are classified as fair value through profit and loss.

All financial liabilities are classified as other financial liabilities at amortised cost, with the exception of derivative financial instruments which are classified as fair value through profit and loss.

The fair values of the Group and Society's financial instruments are as follows:

Group	2015 Carrying value £000	2015 Fair value £000	2014 Carrying value £000	2014 Fair value £000
Financial assets				
Cash and balances with the Bank of England	55,861	55,861	63,053	63,053
Loans and advances to credit institutions	20,838	20,838	26,206	26,206
Investment securities	74	74	15,561	15,561
Derivative financial instruments	403	403	2,146	2,146
Loans and advances to customers	330,618	324,374	387,372	382,068
Investments	-	-	250	250
	407,794	401,550	494,588	489,284
	£000	£000	£000	£000
Financial liabilities				
Due to members	324,630	324,645	389,475	389,512
Deposits from banks	2,002	2,002	1,508	1,508
Other deposits	44,957	44,957	66,946	66,946
Derivative financial instruments	679	679	-	-
Subordinated liabilities	14,200	14,200	15,700	15,700
Subscribed capital	5,000	5,975	5,000	6,000
	391,468	392,458	478,629	479,666

Society	2015 Carrying value £000	2015 Fair value £000	2014 Carrying value £000	2014 Fair value £000
Financial assets				
Cash and balances with the Bank of England	55,861	55,861	63,053	63,053
Loans and advances to credit institutions	20,787	20,787	26,155	26,155
Investment securities	74	74	15,561	15,561
Derivative financial instruments	403	403	2,134	2,134
Loans and advances to customers	323,442	317,198	378,807	373,503
Investments	-	-	250	250
	400,567	394,323	485,960	480,656
	£000	£000	£000	£000
Financial liabilities				
Due to members	324,630	324,645	389,475	389,512
Deposits from banks	2,002	2,002	1,508	1,508
Other deposits	44,957	44,957	66,946	66,946
Derivative financial instruments	627	627	-	-
Subordinated liabilities	14,200	14,200	15,700	15,700
Subscribed capital	5,000	5,975	5,000	6,000
	391,416	392,406	478,629	479,666

The basis of the calculation of fair value is as follows:

a. Loans and advances to customers
The fair value of loans and advances to customers has been calculated on an individual basis taking into account the fixed interest rate attached to each mortgage.

b. Deposits and borrowings
The estimated fair value of variable interest deposits is based on their carrying value, as they are deemed to be issued at market rates.

c. Investment securities
The fair value of each individual investment security is calculated using a discounted cash flow model using a current yield curve appropriate for the remaining term to maturity.

The following table summarises the carrying values of financial assets and liabilities presented on the Group's balance sheet, according to the fair value measurement basis used. The fair values presented in the table are at a specific date and may be significantly different from the amounts which will actually be paid or received on the maturity or settlement date.

Group	2015 Level 1 £000	2015 Level 2 £000	2015 Level 3 £000	2015 Total £000
Financial assets				
Cash and balances with the Bank of England	-	55,861	-	55,861
Loans and advances to credit institutions	-	20,838	-	20,838
Investment securities	-	74	-	74
Derivative financial instruments	-	403	-	403
Loans and advances to customers	-	324,374	-	324,374
Investments	-	-	-	-
	-	401,550	-	401,550
Financial liabilities				
Due to members	-	324,645	-	324,645
Deposits from banks	-	2,002	-	2,002
Other deposits	-	44,957	-	44,957
Derivative financial instruments	-	679	-	679
Subordinated liabilities	-	14,200	-	14,200
Subscribed capital	5,975	-	-	5,975
	5,975	386,483	-	392,458

Group	2014 Level 1 £000	2014 Level 2 £000	2014 Level 3 £000	2014 Total £000
Financial assets				
Cash and balances with the Bank of England	-	63,053	-	63,053
Loans and advances to credit institutions	-	26,206	-	26,206
Investment securities	-	15,561	-	15,561
Derivative financial instruments	-	2,146	-	2,146
Loans and advances to customers	-	382,068	-	382,068
Investments	-	250	-	250
	-	489,284	-	489,284
Financial liabilities				
Due to members	-	389,512	-	389,512
Deposits from banks	-	1,508	-	1,508
Other deposits	-	66,946	-	66,946
Derivative financial instruments	-	-	-	-
Subordinated liabilities	-	15,700	-	15,700
Subscribed capital	6,000	-	-	6,000
	6,000	473,666	-	479,666

c) Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the financial year. The most significant areas where judgements and assumptions are made are as follows:

(i) Impairment losses on loans and advances

The Group reviews its portfolio of loans to assess potential impairment periodically. Save for lifetime mortgages (discussed further below), forbearance matters, arrears positions and indexed LTVs are reviewed on all loan accounts in order to identify potential impairment indicators. For all accounts where impairment may have occurred, the recoverability of the balance due at the financial statement date is assessed by reference to the discounted cash flows associated with the loan. The assessment of these cash flows includes periodic interest and capital repayments and a redemption amount. Within this impairment assessment, assumptions are made concerning sale disposal costs, any loss that may arise from discounts incurred at the point of sale and, in instances where the Society is not the primary charge holder, any payment that must be made to other lenders by the borrower. Values at redemption are assessed as follows:

- loans secured on residential property – assessed by reference to regional HPI data published by Nationwide Building Society and economic forecast data published by Oxford Economics.

- loans secured on land (a category which includes commercial property) – historic valuation data is supplemented with periodic updated desktop, drive-by or full inspection valuation information.

Assumptions are built in to the discounted cash flows regarding any work-out strategies on particular impaired accounts.

If the value of current house prices were 5% higher than that currently estimated, then the total impairment provision required for the Group would decrease from £18.0m to £17.1m. If current prices were 5% lower, then the provision requirement would increase by £1.0m to £19.0m.

The Group holds a beneficial interest in NMB MAC a portfolio of mortgage assets, some of which are CCA regulated. The legal title of these loans remains with this third party business to which the Group provided funding and over which it holds a debenture; under IFRS 10 this third party entity, which is currently in administration, is consolidated within the Group Financial Statements. A further smaller portfolio, CLC, which had previously been beneficially owned and which is now legally owned by the Group has similarly CCA regulated mortgage assets. The impact of non-compliance with the CCA has been assessed and included in the estimate of discounted future cash flows that forms the basis of the impairment provision. This has been assessed based on recent historic cash flow receipts, experience of redemptions and using estimates of the likely future redemption dates. The value of the mortgage assets, post impairment provision in these two portfolios, is £6.6m (2014: £7.8m) of which approximately one third (2014: one third) relates to CCA regulated mortgages.

A 5% uplift in cash flows from the mortgage assets in these NMB MAC and CLC portfolios, associated with greater levels of recoverability than currently estimated, would result in the provision being reduced from £8.3m to £8.0m whilst a 10% reduction in cash flows would see the provision requirement increase from £8.3m to £8.9m.

The expected date of redemption is an important assumption in determining the level of impairment provision for the NMB MAC and CLC portfolios. If the average date of redemption was one year earlier than estimated this would result in the impairment provision being reduced from £8.3m to £8.1m, whilst a one year delay in the expected redemption cash flows would see the provision requirement increase from £8.3m to £8.5m.

The Board monitors its credit risk exposures, underlying security values and the level of impairment provisions on a regular basis.

(ii) Provisions for customer redress and regulatory issues

In addition to considering the impact of any non-compliance on the recoverability of loan balances and thus impairment provisioning, the Group considers the conduct risk which arises from having originated regulated loans and having acquired regulated loan portfolios. As is the case for all financial institutions there is a risk that aspects of current or historic business might be considered as not being conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers.

Certain activities of the Group, particularly the NMB MAC and CLC second charge loan portfolios carry greater levels of conduct risk. These portfolios are under regular review and assessment as part of the risk management processes within the Group. The administration of the NMB MAC and CLC portfolios was brought in-house in December 2015 and following that transfer the historic conduct of these portfolios was reviewed in detail by management.

Following this review, and having incorporated legal advice received, the Group has increased its customer redress provision to £1.7m (2014: a provision of £0.5m for refunds was included in Creditors) to provide for instances of non-compliance with the CCA within the NMB MAC and CLC portfolios. The provision includes an estimate of the potential cost of interest refunds during periods of non-compliance and other costs associated with a customer redress exercise. Full details of the customer redress provision are set out in Note 32.

Although a detailed review of these portfolios has been carried out, there is no judicial certainty in the legal position and there is a risk that further conduct issues or cases of non-compliance with regulations could be identified in the future. As a result the actual results could differ materially from our estimates.

Provision has been made where the Group is aware of a specific conduct or regulatory issue and can estimate its impact reliably, further details in respect of the Group's consideration of other potential conduct and regulatory issues is provided in the contingent liability Note 33.

(iii) Insurance risk

The Society's lifetime mortgages total £39.8m (2014: £43.0m). All loans are at rates of interest that are fixed for the duration of the mortgage; at inception LTVs were low and borrowers were above the age of 60. Borrowers do not make monthly repayments; instead under their contractual terms, interest is capitalised within the balance and becomes repayable on redemption of the loan.

The mortgage contracts contain a clause that behaves like an insurance policy, where in certain circumstances, if the redemption receipt is less than the contractual sum due, the Society cannot pursue the borrower or the estate for the shortfall. This exposes the Society to the risk that the redemption balance may not be recovered fully. Impairment provisions are calculated using: projection data regarding the expected remaining term of the loan and both historic and forecast Spanish HPI data. As redemption dates can be 25+ years in the future, the impairment provision is most sensitive to the value of the property at redemption, where a small change in property value assumptions in the earlier years can have a notable impact on the estimated redemption receipt.

Projection data obtained from external UK sources indicates average long term year-on-year Spanish HPI appreciation at 3.53% (2014: 2.80%) over a 25 year period. If this HPI were to decrease by 0.5% per annum, the insurance provision would increase from its current level of £3.3m to £4.0m; an increase in HPI of 0.5% per annum would see the provision reduce to £2.5m. Mortality rates are based on a third party actuarial assessment. The provision is not particularly sensitive to the date of redemption; in the event that borrowers were to live for 5 years longer than current predictions, the insurance provision would increase by £0.3m. Pre-payment rates are estimated to be 5.5% (2014: 5.5%), based on experience to date. A 0.5% decrease in the pre-payment rate would see the insurance risk provision increase from £3.3m to £3.6m whilst a 0.5% increase in pre-payment would result in a reduction in the insurance risk provision from £3.3m to £3.0m.

(iv) Deferred tax

An asset is recognised to the extent that it is considered probable that future taxable profits will be available to utilise its carrying value. The most critical element of judgement applied is that relating to the Society's forecast profitability and the certainty of that profitability in the medium term in order to meet the requirements of *IAS 12 – Income Taxes*. This includes a consideration of the likely changes in economic conditions and the extent of new lending, or otherwise, in the business. The Group's long term financial projections, based on a managed run-off of the balance sheet without a return to lending, indicate that the underlying operations of the Group will remain profitable in the short to medium term. In the medium to long term it is likely that the net interest margin will be insufficient to cover operating costs and loan impairment charges, resulting in operating losses.

As a result the recoverability of the Group's deferred tax asset has been reassessed and £4.3m of deferred tax has been de-recognised in the year. Further details may be found in Note 19.

(v) Property, plant and equipment

The Group's land and building, being its head office, is owned by MBS (Property) Limited. The value of this property was tested for impairment by reference to *IAS 36 Impairment of Assets*.

The impairment test indicated that the carrying value of the property at 31 December 2015 exceeded its recoverable amount, as represented by fair value less estimated costs of disposal, by £2.5m. Accordingly, an impairment loss for this amount was recognised in the Group Statement of Comprehensive Income.

The fair value of the property is based on an independent valuation of the property carried out in December 2015. The open market value of the property based on its current level of occupancy was assessed to be £5.5m.

The Society holds an investment in MBS (Property) Limited. This is also tested for impairment using value in use assessment techniques to ascertain the future cash flows associated with the property. These cash flows were discounted using the rate of financing in place between the two entities and were based on expectations of future rental arising from the property and void periods. A discount rate of 5.63% (2014:5.63%) was applied and an impairment of £1.6m (2014:£2.7m) was recognised in the year. If rentals are not achieved in line with expectations then the investment may be further impaired. A 5% decrease in rental experience would increase the charge by £0.4m, while a 5% increase in rental experience would reduce the charge by £0.4m. The value of the property has been assumed to grow at 2% per annum up to a future date of disposal. If the growth rate was only 1% per annum this would lead to additional impairment of £0.7m, while if the growth rate was 3% per annum the charge would be reduced by £1.0m. Assumptions have been made in the impairment test about occupancy and void periods, if the assumed date of occupancy of vacant floors was delayed by 12 months then a further impairment of £0.2m would be required.

d) Segmental Analysis

The Group's results are predominately derived from the Society's principal activities. The Group's other income streams are not sufficiently material to require segmental reporting. The chief operating decision maker of the Group and the Society is deemed to be the Group Board.

2. Interest receivable and similar income

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
On loans fully secured on residential property	12,634	16,200	13,065	15,811
On other loans	1,223	1,383	1,223	1,383
On investment securities	69	427	69	427
On other liquid assets	475	599	475	599
	14,401	18,609	14,832	18,220

Interest receivable and similar income, on loans fully secured on residential property, has been reduced in the year by a charge of £1.0m (2014: £0.2m) in respect of a provision for customer redress, see Note 32 for further details.

Other than £2.6m (2014: £3.1m) generated on loans originating in Spain, all interest receivable and similar income has been generated within the United Kingdom.

3. Interest payable and similar charges

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
On amounts due to members	4,204	5,756	4,204	5,756
On deposits and other borrowings				
Subordinated liabilities	598	845	598	845
Subscribed capital (Note 26)	400	396	400	396
Other	651	976	651	976
	5,853	7,973	5,853	7,973

4. Other operating income and charges

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Income				
Rents receivable	47	10	22	-
Interest from subsidiaries	-	-	603	716
Other income from subsidiaries	-	-	10	-
Exchange gains and losses	248	163	236	154
	295	173	871	870
Charges				
Rents payable	51	51	194	194
Other	7	7	7	7
	58	58	201	201

Exchange gains and losses arise principally in respect of the Spanish lifetime mortgage book.

Rent payable by the Society under operating leases is payable to the Society's subsidiary MBS (Property) Limited. Rent payable by the Group under operating leases is payable to 3rd parties.

5. Income from investments

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Profit on sale of shareholding in New Life Home Finance Limited	745	-	745	-

During April 2015 the Society completed the sale of its minority share in New Life Home Finance Limited ("NLHF") to Legal and General Group plc. For further information see Note 16.

6. (Loss)/profit from derivatives

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Net (loss)/profit from derivatives	(10)	9	(11)	9

Net (loss)/profit from derivatives included above are solely in respect of exchange rate swaps.

7. Administrative expenses

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Employee costs (including Executive Directors)				
Wages & salaries	1,726	1,358	1,726	1,358
Social security costs	185	139	185	139
Pension costs	149	133	149	133
	2,060	1,630	2,060	1,630
Other administrative expenses	4,539	4,215	3,757	3,791
	6,599	5,845	5,817	5,421

The increase in employee costs reflects additional activity carried out during the year in relation to the development of plans to return to lending. Legal and professional costs were also incurred in connection with the Society's claim against Grant Thornton UK LLP.

Other administrative expenses includes a charge in respect of costs associated with the customer redress exercise, see Note 32 for further details.

Remuneration of the auditors

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Fees payable to the auditors for audit of the annual accounts				
Current year	322	289	322	289
Additional fees in relation to the audit of the prior year	48	288	48	288
Fees payable to the auditors for other services				
Audit of the accounts of subsidiaries	10	12	-	-
Tax compliance services	73	94	71	94
Other assurance services	16	13	16	13
	469	696	457	684

8. Employees

The average number of persons employed during the year was:

	Group 2015 Number	Group 2014 Number	Society 2015 Number	Society 2014 Number
Full-time	41	32	41	32
Part-time	5	6	5	6
	46	38	46	38

9. Directors' emoluments

Executive directors

	Salary £000	Pension Contributions £000	Benefits £000	Total £000
2015				
C.W. Gee (resigned 31 March 2015)	29	3	3	35
P.A. Lynch	117	14	11	142
	146	17	14	177
2014				
C.W. Gee	117	14	11	142
P.A. Lynch	117	14	11	142
	234	28	22	284

Non-executive directors

	Fees 2015 £000	Fees 2014 £000
J.P. Allen	29	29
H.F. Baines	36	32
I.A. Dewar	29	29
R.W. Dyson (resigned 16 June 2014)	-	13
D.A. Harding	72	72
F.B. Smith	29	28
J. Smith (resigned 29 April 2015)	9	32
	204	235

Total directors' emoluments

	2015 £000	2014 £000
Executive directors	177	284
Non-executive directors	204	235
Total directors' emoluments	381	519

During the year a number of appointments to the executive management team were made on an interim basis. Further details regarding Key Management Personnel may be found in Note 29.

10. Income tax (expense)/credit

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
(Loss)/profit for the year before tax	(579)	4,302	2,168	1,248
Tax rate	20.25%	21.50%	20.25%	21.50%
Expected tax expense	(117)	925	439	268
Adjustment for non-deductible items	517	28	559	583
Income not taxable	(146)	-	(146)	-
Deferred tax movement closing rate/average rate difference	(11)	(67)	(11)	(60)
Current year losses for which no deferred tax asset recognised	587	-	-	-
Fixed asset timing differences for which no deferred tax asset recognised	11	-	-	-
Adjustment in respect of prior years - deferred tax	-	233	-	-
Decrease/(increase) in deferred tax asset recognised	3,454	(1,269)	3,454	(1,167)
Actual tax expense/(credit), net	4,295	(150)	4,295	(376)
Comprising				
Deferred tax origination and reversal of timing difference	4,295	(383)	4,295	(376)
Deferred tax adjustment in respect of prior years	-	233	-	-
	4,295	(150)	4,295	(376)

11. Loans and advances to credit institutions

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Accrued interest	13	26	13	26
Repayable on demand	20,825	26,180	20,774	26,129
	20,838	26,206	20,787	26,155

12. Investment securities

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Government investment securities	-	9,989	-	9,989
Listed private sector investment securities	74	5,572	74	5,572
	74	15,561	74	15,561
Investment securities have remaining maturities as follows:				
In not more than three months	-	9,989	-	9,989
In more than three months but not more than one year	-	5,490	-	5,490
In more than one year but not more than five years	74	82	74	82
	74	15,561	74	15,561

The directors of the Society consider that the primary purpose of holding investment securities is prudential. The securities are held as liquid assets with the intention of use on a continuing basis in the Group's activities.

The movement in investment securities is summarised as follows:

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
At 1 January	15,561	23,057	15,561	23,057
Additions	500	10,021	500	10,021
Fair value adjustment	(46)	(314)	(46)	(314)
Disposals	(15,941)	(17,203)	(15,941)	(17,203)
At 31 December	74	15,561	74	15,561

13. Derivative financial instruments and trading liabilities - Group and Society

Exchange rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currency rates (for example, Sterling for Euros). No exchange of principal takes place. The Group's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligations. This risk is monitored by reference to the fair value of the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Group assesses counterparties using techniques including credit ratings. The fair value is based on the current discounted cash flows of the swaps when compared with the current exchange rate yields.

The Group uses foreign exchange forward contracts and swaps for hedging purposes. All derivative financial instruments are held for economic purposes.

The following table describes the significant activities undertaken by the Group, the risks associated with such activities and the types of derivatives which are typically used in managing such risks.

Activity	Risk	Type of derivative instruments used
Mortgage lending in Euros	Sensitivity to changes in exchange rates	Exchange rate swaps

	Notional amount £000	Fair value Assets £000	Fair value Liabilities £000
Derivatives held at 31 December 2015			
Exchange rate swaps	42,760	403	679
	42,760	403	679
Derivatives have remaining maturities as follows:			
Up to three months	15,392	391	78
Three to six months	14,291	12	283
Six to twelve months	13,077	-	318
	42,760	403	679
Derivatives held at 31 December 2014			
Exchange rate swaps	44,861	2,146	-
	44,861	2,146	-

14. Loans and advances to customers

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Loans fully secured on residential property	302,441	354,437	295,265	345,872
Loans fully secured on land	26,802	31,278	26,802	31,278
Other loans	1,375	1,657	1,375	1,657
	330,618	387,372	323,442	378,807

At 31 December 2015 the Group had €58.3m (2014: €57.7m) of loans denominated in Euros. These were converted into Sterling at a rate of €1.3611 to the £ (2014: €1.2873).

Maturity analysis

The remaining maturity of loans and advances to customers from the date of the financial position is as follows:

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Repayable on demand	8,635	8,180	8,635	8,180
Other loans and advances secured by residual maturity repayable:				
In not more than three months	2,103	2,408	1,830	2,123
In more than three months but not more than one year	10,906	10,611	10,088	9,562
In more than one year but not more than five years	61,735	70,534	57,263	65,975
In more than five years	265,251	313,428	255,713	304,083
	348,630	405,161	333,529	389,923
Less: impairment provisions	(18,012)	(17,789)	(10,087)	(11,116)
	330,618	387,372	323,442	378,807

The Group's experience is that, in many cases, mortgages are redeemed before their natural or contractual redemption dates. As a consequence the maturity analysis above may not reflect actual experience.

Impairment losses on loans and advances

	Loans fully secured on residential property £000	Other loans fully secured on land £000	Other loans £000	Total £000
Group				
At 1 January 2015				
Individually identified				
Credit risk provisions	1,981	3,147	21	5,149
Total individually identified	1,981	3,147	21	5,149
Collectively identified				
Credit risk provisions	7,438	20	-	7,458
Insurance risk provisions	5,182	-	-	5,182
Total collectively identified	12,620	20	-	12,640
Total opening provisions	14,601	3,167	21	17,789
Amounts utilised during the year				
Individually identified				
Credit risk provisions	(332)	(39)	-	(371)
Total individually identified	(332)	(39)	-	(371)
Collectively identified				
Insurance risk provisions	(39)	-	-	(39)
Total collectively identified	(39)	-	-	(39)
Transferred to Investment property during the year (Note 18)				
Individually identified				
Credit risk provisions	(115)	-	-	(115)
Total individually identified	(115)	-	-	(115)
Statement of Comprehensive Income				
Individually identified				
Credit risk provisions	172	1,262	(21)	1,413
Total individually identified	172	1,262	(21)	1,413
Collectively identified				
Credit risk provisions	1,177	(2)	13	1,188
Insurance risk provisions	(1,853)	-	-	(1,853)
Total collectively identified	(676)	(2)	13	(665)
Total	(504)	1,260	(8)	748
At 31 December 2015				
Individually identified				
Credit risk provisions	1,706	4,370	-	6,076
Total individually identified	1,706	4,370	-	6,076
Collectively identified				
Credit risk provisions	8,615	18	13	8,646
Insurance risk provisions	3,290	-	-	3,290
Total collectively identified	11,905	18	13	11,936
Total closing provisions	13,611	4,388	13	18,012

	Loans fully secured on residential property £000	Other loans fully secured on land £000	Other loans £000	Total £000
Society				
At 1 January 2015				
Individually identified				
Credit risk provisions	1,981	3,147	21	5,149
Total individually identified	1,981	3,147	21	5,149
Collectively identified				
Credit risk provisions	765	20	-	785
Insurance risk provisions	5,182	-	-	5,182
Total collectively identified	5,947	20	-	5,967
Total opening provisions	7,928	3,167	21	11,116
Amounts utilised during the year				
Individually identified				
Credit risk provisions	(332)	(39)	-	(371)
Total individually identified	(332)	(39)	-	(371)
Collectively identified				
Insurance risk provisions	(39)	-	-	(39)
Total collectively identified	(39)	-	-	(39)
Transferred to Investment property during the year (Note 18)				
Individually identified				
Credit risk provisions	(115)	-	-	(115)
Total individually identified	(115)	-	-	(115)
Statement of Comprehensive Income				
Individually identified				
Credit risk provisions	172	1,262	(21)	1,413
Total individually identified	172	1,262	(21)	1,413
Collectively identified				
Credit risk provisions	(75)	(2)	13	(64)
Insurance risk provisions	(1,853)	-	-	(1,853)
Total collectively identified	(1,928)	(2)	13	(1,917)
Total	(1,756)	1,260	(8)	(504)
At 31 December 2015				
Individually identified				
Credit risk provisions	1,706	4,370	-	6,076
Total individually identified	1,706	4,370	-	6,076
Collectively identified				
Credit risk provisions	690	18	13	721
Insurance risk provisions	3,290	-	-	3,290
Total collectively identified	3,980	18	13	4,011
Total closing provisions	5,686	4,388	13	10,087

Total impairment losses in the Statement of Comprehensive Income of the Group and Society are disclosed in Note 15

15. Impairment losses/(gains)

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Impairment losses/(gains) on loans and advances to customers on residential property and land	2,601	(294)	1,349	779
Impairment (gains)/losses on loans and advances to customers on lifetime mortgages	(1,853)	261	(1,853)	261
Impairment on loan to subsidiaries:				
- MBS(Property) Limited	-	-	1,564	2,710
- MBS(Mortgages) Limited	-	-	1,198	-
Impairment of property, plant and equipment	2,471	-	-	-
	3,219	(33)	2,258	3,750

The value of the Group's head office was tested for impairment and an impairment loss of £2.5m was recognised to reduce the carrying value of the property. For further details of the impairment test see Note 17.

In 2015, following a further reassessment of the recoverability of the Society's investment in MBS (Property) Limited, an impairment provision of £1.6m (2014: £2.7m) was reflected in the Society's separate financial statements reducing the net investment in this subsidiary. For further details of the impairment test see Note 16.

The recoverability of the Society's investment in MBS (Mortgages) Limited was also reassessed in 2015, and an impairment provision of £1.2m (2014: £nil) was reflected in the Society's separate financial statements reducing the net investment in this subsidiary. For further details of the impairment test see Note 16.

16. Investments

Subsidiary undertakings	Shares £000	Loans £000	Total £000
At 1 January 2015	2	15,903	15,905
Impairment	-	(2,762)	(2,762)
Advances	-	17	17
At 31 December 2015	2	13,158	13,160

The Society's investment in its subsidiaries has been tested for impairment and appropriate reductions in the carrying balances have been made.

A further impairment of £1.6m was made to the investment held in MBS (Property) Limited in the year. The investment valuation was assessed based on the discounted cash flows associated with the property, requiring an assessment of rentals, void rates and long term property values. A discount rate of 5.63% (2014: 5.63%) was applied being the rate associated with the financing arrangement in place. A 5% decrease in rental experience would increase the charge by £0.4m, while a 5% increase in rental experience would reduce the charge by £0.4m. The value of the property has been assumed to grow at 2% per annum up to a future date of disposal. If the growth rate was only 1% per annum this would lead to additional impairment of £0.7m, while if the growth rate was 3% per annum the charge would be reduced by £1.0m. Assumptions have been made in the impairment test about occupancy and void periods, if the assumed date of occupancy of vacant floors was delayed by 12 months then a further impairment of £0.2m would be required.

The Group holds a beneficial interest in a portfolio of mortgage assets, NMB MAC, some of which are regulated by the CCA. The administration of this portfolio was brought in-house in December 2015 and following a review of the portfolio a significant charge was booked in the separate financial statements of MBS (Mortgages) Limited to provide for potential refunds and other costs associated with customer redress where cases of non-compliance with CCA regulations had been identified. Further details of this review and the charge in the year are set out in Note 1c(ii) and Note 32. Also a reassessment of the recoverability of these assets was carried out (as detailed in Note 1c (i)) and an additional impairment provision has been booked in the financial statements of MBS (Mortgages) Limited who consolidate these assets. These charges impair the ability of the subsidiary to repay the Society's investment in it and therefore an impairment provision of £1.2m has been made in the Society's separate financial statements, reducing the net investment in the subsidiary.

The directors consider that the carrying value of the investment in subsidiaries is supported by their net assets, less impairment provisions.

Subsidiaries	**Nature of Business**	**Country of Incorporation and place of business**	**Proportion of Ordinary shares held**
MBS (Mortgages) Limited	Mortgage lending	England	100%
MBS (Property) Limited	Property ownership	England	100%

MBS (Mortgages) Limited and MBS (Property) Limited are wholly owned and wholly funded by the Society. The Society's ability to recover its investment in these subsidiaries is based upon the cash flows that these subsidiaries can generate.

Connected undertakings

In 2014 and up until 7 December 2015, there were two other entities the results of which had been consolidated with the Group position under the terms of IFRS 10: NMB Mortgage Acquisition Company Limited ("NMB MAC") and The Consumer Loans Company Limited ("CLC"). Both companies had been funded by the Group and were in administration. The Group benefited from the cash flows arising from NMB MAC and CLC, save for those used by the administrator of the businesses to meet their day-to-day running costs, and the Group had significant influence over these companies. The Group had no shareholding or voting rights in either company but was exposed to variable returns from the companies. There were no material non-controlling interests in either NMB MAC or CLC. These arrangements met the definition of control under IFRS 10 and so the results of NMB MAC and CLC had been consolidated in accordance with that standard.

On 7 December 2015, the Group acquired legal title to the loans owned by CLC over which it had previously had a beneficial interest. As a result it now receives the cash flows from these loans directly rather than having a beneficial interest in the cash flows of CLC. As a result CLC no longer meets the definition of a connected undertaking and is no longer consolidated.

The arrangements in respect of NMB MAC remain unchanged.

Connected undertakings	Nature of Business	Country of Incorporation and place of business	Proportion of Ordinary shares held
NMB Mortgage Acquisition Company Limited*	Mortgage lending	England	0%

* in administration

As NMB MAC is in administration, the Group's ability to use this entity's assets or settle its liabilities is restricted by the cash flows that the entity is able to generate alongside the administrator's statutory duty to manage the entity. Save for the above, there are no other significant restrictions on the Group's ability to use assets or settle liabilities in any of the subsidiaries listed above.

Trade investments - Group and Society	2015 £000	2014 £000
At 31 December	-	250

During April 2015 the Society completed the sale of its minority share in New Life Home Finance Limited to Legal and General Group plc for consideration of £995k. The profit on sale of £745k is shown under "Income from investments" in the Statements of Comprehensive Income, see Note 5. The shareholding had been held as a trade investment.

17. Property, plant and equipment

Group	Land and buildings £000	Alterations fixtures and equipment £000	Total £000
Cost			
At 1 January 2015	8,519	1,453	9,972
Additions	(7)	327	320
Disposals	-	(36)	(36)
At 31 December 2015	8,512	1,744	10,256
Accumulated depreciation			
At 1 January 2015	871	788	1,659
Charge for the year	110	132	242
Impairment loss	2,275	196	2,471
Eliminated on disposal	-	(36)	(36)
At 31 December 2015	3,256	1,080	4,336
Carrying amount			
At 31 December 2015	5,256	664	5,920
At 31 December 2014	7,648	665	8,313

Society	Land and buildings £000	Alterations fixtures and equipment £000	Total £000
Cost			
At 1 January 2015	-	875	875
Additions	-	296	296
Disposals	-	(36)	(36)
At 31 December 2015	-	1,135	1,135
Accumulated depreciation			
At 1 January 2015	-	600	600
Charge for the year	-	101	101
Eliminated on disposal	-	(36)	(36)
At 31 December 2015	-	665	665
Carrying amount			
At 31 December 2015	-	470	470
At 31 December 2014	-	275	275

The Group's land and building, being its head office, is owned by MBS (Property) Limited. The value of this property was tested for impairment on a value in use basis by reference to *IAS 36 Impairment of Assets*. The impairment test indicated that the value in use of the property was lower than both its fair value less estimated costs of disposal and its carrying value. The carrying value of the property exceeded its fair value less estimated cost of disposal, which represented its recoverable amount, by £2.5m and an impairment loss for this amount was recognised in the Group Statement of Comprehensive Income.

The fair value of the property is based on an independent valuation of the property carried out in December 2015. The open market value of the property based on its current level of occupancy was assessed to be £5.5m.

18. Investment property - Group and Society

The movement on Investment property is as follows:

	Residential property £000
Fair value	
At 1 January 2015	-
Transfer from loans and advances to customers	781
At 31 December 2015	781

During the year the Society acquired a small number of residential properties as a result of the settlement of an impaired mortgage asset. The properties are being held, pending their eventual sale, as investment properties and are stated at their fair value after taking in to account estimated costs to sell.

19. Deferred tax assets

Deferred income taxes are calculated on all temporary differences under the liability method using effective tax rates of 19.0% to 20.0% depending on when the timing difference are expected to reverse (2014: 20.0%). The movement on the deferred income tax account is as follows:

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
At 1 January	4,542	4,257	4,542	4,031
Statement of comprehensive income	(4,295)	150	(4,295)	376
Statement of changes in equity	135	135	135	135
At 31 December	382	4,542	382	4,542
Deferred tax assets are attributable to the following items:				
Other provisions	2	(6)	2	(6)
Accelerated tax depreciation	(70)	(37)	(65)	(19)
Tax losses	5	349	-	331
Deferred tax asset on timing differences on derivative contracts	445	4,236	445	4,236
	382	4,542	382	4,542

The movement in the deferred tax account is shown below:

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Other provisions	8	8	8	8
Tax losses	(479)	(1,618)	(466)	(1,396)
Accelerated tax depreciation	(33)	(32)	(46)	(28)
Deferred tax movement on timing differences on derivative contracts	(3,791)	1,792	(3,791)	1,792
Deferred income tax (expense)/credit in statement of comprehensive income	(4,295)	150	(4,295)	376
Deferred income tax credit in statement of changes in equity	135	135	135	135
	(4,160)	285	(4,160)	511

IAS 12 - Income Taxes, requires that a deferred tax asset ("DTA") can only be recognised to the extent that it is probable that it will be recovered through future profitability.

The proposed reductions in the future main rates of corporation tax announced by the Chancellor of the Exchequer in the 2015 Summer budget were included in the Finance Bill 2015, which was substantively enacted on 26 October 2015. As a result, the main rate of corporation tax in the UK will fall from 20% to 19% on 1 April 2017, and by a further 1% to 18% on 1 April 2020.

The carrying value of the deferred tax asset has been re-measured to take account of these reductions in rate.

Further proposed reductions in the main rate of corporation tax were announced in the 2016 budget.The deferred tax asset has not been re-measured in respect of these changes as they are not substantively enacted.

The Group's long term financial projections, based on a managed run-off of the balance sheet without a return to lending, indicate that the underlying operations of the Group will remain profitable in the short to medium term. In the medium to long term it is likely that the net interest margin will be insufficient to cover operating costs and loan impairment charges, resulting in operating losses.

As a result the recoverability of the Group's deferred tax asset has been reassessed and £4.3m of deferred tax has been de-recognised in the year.

If the future profits of the Group were 10% higher than those envisaged in the Group's long term financial projections referred to above, then the amount of deferred tax asset recognised in the balance sheet would not be significantly increased, as the Group only remains profitable in the short to medium term.

It should be noted that the de-recognised element of the DTA is still available for tax relief purposes, as tax losses can be carried forward indefinitely under UK tax rules and can be used subject to the availability of future taxable profits.

In addition to the recognised deferred taxation assets and liabilities, certain deferred tax assets have not been recognised.

At 31 December 2015 for the Group, these were:

- £2,207k arising from timing differences on derivative contracts (2014: £1,718k) and
- £4,732k arising from losses (2014: £1,560k)

At 31 December 2015 for the Society, these were:

- £2,207k arising from timing differences on derivative contracts (2014: £1,718k) and
- £2,755k arising from losses (2014: £173k).

20. Other assets

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Amounts due within one year				
Credit support annex	955	525	955	525
Prepayments	349	401	336	375
Other assets	39	22	31	22
	1,343	948	1,322	922

The Credit support annex balances represent the sums deposited by the Society with its derivative counterparties to collateralise the derivatives issued. The balances, whilst in cash form, are not included within Liquid Assets.

21. Due to members

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Held by individuals	324,630	389,475	324,630	389,475
Shares are repayable from the financial position date in the ordinary course of business as follows:				
Accrued interest	816	992	816	992
Repayable on demand	153,744	238,750	153,744	238,750
Other shares by residual maturity repayable:				
In not more than three months	147,961	136,781	147,961	136,781
In more than three months but not more than one year	6,957	7,496	6,957	7,496
In more than one year but not more than five years	15,152	5,456	15,152	5,456
	324,630	389,475	324,630	389,475

22. Deposits from banks

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Amounts owed to credit institutions are repayable from the financial position date in the ordinary course of business as follows:				
Accrued interest	2	8	2	8
Other amounts owed to credit institutions by residual maturity repayable:				
In not more than three months	1,000	1,000	1,000	1,000
In more than three months but not more than one year	1,000	500	1,000	500
	2,002	1,508	2,002	1,508

23. Other deposits

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Amounts owed to other deposit customers are repayable from the financial position date in the ordinary course of business as follows:				
Accrued interest	225	259	225	259
Repayable on demand	3,783	11,809	3,783	11,809
Other amounts owed to other deposit customers by residual maturity repayable:				
In not more than three months	38,233	36,164	38,233	36,164
In more than three months but not more than one year	2,716	18,714	2,716	18,714
	44,957	66,946	44,957	66,946

At 31 December 2015 the Group had £nil (2014: £23m) nominal value of mortgages pledged as collateral for £nil (2014: £10m) of deposits placed by other customers.

24. Subordinated liabilities

	Group and Society 2015 £000	Group and Society 2014 £000
Subordinated loans		
Loan repayable 2015 (fixed interest rate of 7.362%)	-	1,500
Loan repayable 2022 (variable interest rate of 3 months LIBOR plus 1.75%)	5,000	5,000
Loan repayable 2023 (variable interest rate of 3 months LIBOR plus 2.45%)	4,200	4,200
Loan repayable 2032 (fixed interest rate of 6.70%)	5,000	5,000
	14,200	15,700

The subordinated loans were taken to assist the financing of future development. The loans exist for a fixed period and the Society has the option to prepay the loans at par 5 years prior to the final repayment dates. The 2015 subordinated loan at 7.362% was repaid in full on 9 March 2015.

25. Other liabilities

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Amounts falling due within one year:				
Income tax - deducted from interest payments to customers	178	233	178	233
Taxation and social security	90	62	90	62
Creditors	569	1,338	402	875
Interest accrued on subordinated liabilites	124	160	124	160
Accruals	621	1,003	497	1,003
	1,582	2,796	1,291	2,333

Other liabilities includes interest accrued on PIBS of £70k (2014: £70k).

26. Subscribed capital

The Society has two tranches of PIBS in issue. The first tranche was issued in 1999 and is remunerated at 8.00% and the other was issued in 2005 and is remunerated at 6.75%.

The two tranches are accounted for differently as they are subject to differing legal arrangements. Both tranches of PIBS are unsecured and rank pari passu with each other. In priority terms, the PIBS holders rank behind the Society's depositing members, its wholesale counterparties and all subordinated note holders.

Classified as a liability:	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
8.00% Permanent Interest Bearing Shares	5,000	5,000	5,000	5,000
	5,000	5,000	5,000	5,000

Under the terms of offer, the Board may, subject to a resolution, cancel in whole or in part any scheduled interest payment due to holders of the 8.00% PIBS in restricted circumstances, when the Society were to have in issue other shares or deposits (save for deferred shares) on which the Board could cancel interest at its discretion. As no such class of share or deposit was in issue at either of the financial statement dates, it has been assessed that the terms of the PIBS confer a contractual obligation on the Society to deliver cash in the form of interest payments and as such, the 8.00% PIBS are treated as a liability on the part of the Society and interest is booked to income and expenditure (Note 3).

Classified as equity:	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
6.75% Permanent Interest Bearing Shares	9,788	9,788	9,788	9,788
	9,788	9,788	9,788	9,788

Under the terms of offer, the Board may at its sole discretion, subject to a resolution, cancel in whole or in part any scheduled interest payment due to holders of the 6.75% PIBS. Whilst the Board does not intend to avail itself of this discretion, the facility to do so results in the assertion that the PIBS should be considered not to confer a contractual obligation on the Society to deliver cash in the form of interest payments. As such, the 6.75% PIBS are treated as forming a part of the Society's equity and interest is booked to Statement of Changes in Equity.

27. Cash and cash equivalents

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
For the purposes of the cash flow statement, cash and cash equivalents comprises the following balances with less than three months maturity from the date of acquisition:				
Cash and balances with central banks	55,861	63,053	55,861	63,053
Loans and advances to credit institutions	20,825	26,180	20,774	26,129
	76,686	89,233	76,635	89,182

28. Profit Participating Deferred Shares

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Nominal value - proceeds received	18,000	18,000	18,000	18,000
Less: issue costs	(539)	(539)	(539)	(539)
Book value	17,461	17,461	17,461	17,461
PPDS Reserve Account at 1 January (memo)	(506)	(1,680)		
Share of (loss)/profit for the year	(1,624)	1,174		
PPDS Reserve Account at 31 December (memo)	(2,130)	(506)		

The Society issued £18m of PPDS in April 2013. The PPDS are deferred shares for the purposes of Section 119 of the Building Societies Act 1986 (as amended). They are perpetual instruments with no maturity date or right to repayment other than on a winding-up; in the event of a winding-up, the PPDS would rank below claims in respect of the Society's PIBS. The PPDS are not protected deposits for the purposes of the Financial Services Compensation Scheme. They are eligible as Common Equity Tier 1 Capital for regulatory purposes.

Save as described below, the holders of the PPDS are eligible to receive a dividend, at the discretion of the Board of the Society, of up to 30% (the "Participation Percentage") of the annual consolidated post-tax profits of the Society and its subsidiaries (calculated prior to payment of the PPDS dividend and subject to certain other adjustments).

The PPDS will also absorb the Participation Percentage of any consolidated post-tax losses recorded by the Society and its subsidiaries, any such amount being debited to a reserve account maintained by the Society for the purpose of the PPDS (the "PPDS Reserve Account"). Any net profits which are eligible to be paid to holders of PPDS as dividends but which are not so paid will be credited to the PPDS Reserve Account.

No dividends may be paid on the PPDS when the PPDS Reserve Account is in deficit as a result of previous years' losses.

No dividend has been declared in the year.

29. Related party transactions

Key Management Personnel. The directors, the Chief Executive, the Interim Finance Director, the Interim Chief Risk and Compliance Officer and the Head of Corporate Development and Secretarial Services are considered to be the Key Management Personnel as defined by *IAS 24 – Related Party Disclosures*. In line with the Board's continuing policy, there were no loans provided to any of these individuals or their close family members (2014: nil). None of the directors, or their close family members held any of the Society's PIBS (2014: nil).

In 2015 and 2014 the Group made a number of appointments to Key Management Personnel roles on an interim basis. The Remuneration and Nominations Committee reviewed these appointments and assessed the level of fees or remuneration payable, for further details of the work of this Committee see page 10. Where the services of these Key Management Personnel are provided by entities controlled by them, then the amounts paid to the entities by the Group for their services (inclusive of VAT) and any balances outstanding at year end are disclosed below.

The total remuneration of Key Management Personnel was as follows:

	Group 2015 £000	Group 2014 £000
Executive directors (per note 9)	177	284
Non-executive directors (per note 9)	204	235
Key Management Personnel	657	492
	1,038	1,011

Transactions with other related parties.

The Society had the following transactions with other related parties:

	Group 2015 £000	Group 2014 £000
Purchases of interim executive services from entities controlled by Key Management Personnel	516	492

The following balances are outstanding at 31 December in relation to transactions with other related parties:

	Group 2015 £000	Group 2014 £000
Current payables for purchases from entities controlled by Key Management Personnel	10	40

Register. In accordance with sections 68 and 69 of the Building Societies Act 1986 a register of transactions is maintained at the Society's head office which shows details of all transactions and arrangements with directors and connected persons.

Subsidiaries. The Group is controlled by Manchester Building Society; details of the subsidiary undertakings may be found in Note 16.

The Society had the following transactions with its subsidiary undertakings during the year:

(i) Current loan accounts - unsecured	Society 2015 £000	Society 2014 £000
As at 1 January	15,903	18,848
Loans issued during the year	1,376	1,274
Loan repayments during the year	(1,359)	(1,509)
Impairment of subsidiary loans	(2,762)	(2,710)
At 31 December	13,158	15,903

(ii) Interest income charged to subsidiaries	603	716

Interest is charged at pre-agreed rates which are either fixed, track the Bank of England base rate, or track LIBOR

(iii) Other income charged to subsidiary for management of NMB MAC loan book	10	-
(iv) Society recharge to subsidiaries of head office expenses	66	79
(v) Subsidiary recharge to Society on rent for head office	143	143
(vi) Cash received from borrowers by connected undertakings		
NMB MAC - cash received and paid through to MBS (Mortgages) Limited	636	1,126
CLC - cash received and paid through to Society	117	123

30. Financial commitments

(i) Capital commitments:

	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Capital expenditure contracted for but not provided	10	-	10	-

(ii) Lease commitments

At the financial position date the Group had outstanding commitments as lessee under operating leases. The financial commitments are shown below.

Lease commitments:	Lessee 2015 £000	Lessee 2014 £000
Less than one year	50	50
One to five years	41	91
	91	141

Contingent liabilities are considered in Note 33.

31. Capital management

Regulatory capital requirements are laid down by the Society's regulator; they are calculated, forecast and stress tested on a regular basis for the Board and period end positions are reported to the regulator. For regulatory capital purposes the Group is made up of the Society and MBS (Mortgages) Limited, with the regulatory capital positions under CRD 1V at 31 December 2015 and 31 December 2014 being:

Tier 1 Capital	Group 31 December 2014 £000	Movement in 2015 £000	Group 31 December 2015 £000	Regulatory Movement for 2016 £000	Group 1 January 2016 £000
CET 1 Capital					
Retained Earnings	754	(3,879)	(3,125)	-	(3,125)
Deductions	(3,030)	3,029	(1)	-	(1)
Profit Participating Deferred Shares	17,461	-	17,461	-	17,461
Total CET1 Capital	15,185	(850)	14,335	-	14,335
Permanent Interest Bearing Shares					
- Nominal balance	14,788	-	14,788	-	14,788
- Amortisation	(2,958)	(1,479)	(4,437)	(1,478)	(5,915)
Net Permanent Interest Bearing Shares	11,830	(1,479)	10,351	(1,478)	8,873
Total Tier 1 Capital	27,015	(2,329)	24,686	(1,478)	23,208
Tier 2 Capital					
Subordinated Debt					
- Nominal balance	15,700	(1,500)	14,200	-	14,200
- Amortisation	(2,445)	945	(1,500)	(500)	(2,000)
Net Subordinated Debt	13,255	(555)	12,700	(500)	12,200
Collective Provisions	2,850	(695)	2,155	-	2,155
Permanent Interest Bearing Shares	2,958	1,479	4,437	1,478	5,915
Total Tier 2 Capital	19,063	229	19,292	978	20,270
Total Regulatory Capital	46,078	(2,100)	43,978	(500)	43,478

Since the start of 2015 Total Regulatory Capital under CRD IV has decreased by £2,100k made up as follows:

- the retained loss of the regulatory capital group for the year of £3,879k;
- the scheduled repayment of £1,500k of Subordinated debt, (previously amortised by £1,445k under CRD IV rules);
- the continued amortisation of Subordinated debt out of Tier 2 capital over a 9 year period, amounting to £500k in the year;
- a reduction in the allowed collectively identified provisions of £695k; and
- A partially offsetting £3,029k reduction in required deductions from CET1 Capital. This is primarily in respect of the reduction in the deferred tax asset as a result of the £4,295k deferred tax charge recorded in the year but with £250k of the reduction arising due to the sale of the investment in New Life Home Finance Limited.

Under the CRD IV rules applicable from 1 January 2016, Total Regulatory Capital is reduced by £500k compared to the position at 31 December 2015. This is due to Tier 2 Regulatory Capital being reduced by a further £500k in respect of continuing Subordinated debt amortisation.

As at 31 December 2015 the Society held sufficient capital in Tier 1 and Tier 2 to meet all of the regulatory capital requirements then in place. However, one regulatory expectation that was not met compares the Society's actual CET1 capital to the level of CET1 capital that the PRA expects the Society to hold. The Society had also fallen marginally short of this expectation as at 31 December 2014 due to the mix of capital held and during 2015 had continued to focus on rebuilding its capital position. However, the significant write downs in respect of both the intercompany loan with MBS (Property) Limited and the deferred tax asset, combined with increased customer redress provisioning, have depleted CET1 regulatory capital further. As a consequence there is a shortfall of £1.6m against this CET1 expectation as at 31 December 2015. Under the new regulatory capital regime effective 1 January 2016, at that date there is a £2.8m shortfall.

After the year end, on 11 April 2016, the Society received new Individual Capital Guidance ("ICG") from the PRA setting out the amount of regulatory capital the Society is required to hold. The Board has reviewed the capital resources following the new guidance from the PRA and has concluded that the ICG and CRD IV buffer requirements are met. The Board also concluded that the Society meets the quantitative aspect of the PRA buffer. As previously, the Society is expected to hold a certain proportion of its capital buffers in CET1 capital; this remains challenging under the new guidance and the Society may not meet these expectations going forward.

32. Provisions for liabilities and charges

2015	**Group FSCS Levy £000**	**Group Customer redress £000**	**Group Total £000**	**Society FSCS Levy £000**	**Society Customer redress £000**	**Society Total £000**
At 1 January 2015	214	-	214	214	-	214
Transferred from creditors	-	463	463	-	90	90
Charge/(release) for the year	277	1,232	1,509	277	(13)	264
Provision utilised	(354)	-	(354)	(354)	-	(354)
At 31 December 2015	137	1,695	1,832	137	77	214

2014	**Group FSCS Levy £000**	**Group Customer redress £000**	**Group Total £000**	**Society FSCS Levy £000**	**Society Customer redress £000**	**Society Total £000**
At 1 January 2014	275	-	275	275	-	275
Charge for the year	430	-	430	430	-	430
Provision utilised	(491)	-	(491)	(491)	-	(491)
			-			
At 31 December 2014	214	-	214	214	-	214

(i) Financial Services Compensation Scheme ("FSCS") Levy

The Society's provision for FSCS charges arises from its operation as a UK deposit taker.

The FSCS levy consists of two parts - a management expenses levy, which covers the interest cost of running the scheme, and a capital levy to cover the cost of the compensation paid, net of any recoveries.

The charge for 2015 and the provision at the end of the year include the expected management expenses levy for the FSCS scheme year 2015-16.

In 2013 the FSCS announced that there was likely to be a shortfall in their overall level of recoverability and indicated that it would levy this shortfall on deposit-taking institutions over the three years 2013-14 to 2015-16. The shortfall capital levy for the FSCS scheme year 2014-15 was received during 2015 and recognised as a charge in the Statements of Comprehensive Income for 2015. No provision is made in respect of the capital levy for scheme years beyond this period. The levy is paid during the third quarter of each year and the Society does not expect to recover any sums paid.

(ii) Customer redress provision

As is the case for all financial institutions there is a risk that aspects of current or historic business might be considered as not being conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers.

Certain activities of the Group, particularly the NMB MAC and CLC second charge loan portfolios carry greater levels of conduct risk .The administration of these portfolios was brought in-house in December 2015 and following that transfer the historic conduct of these portfolios was reviewed in detail by management.

Following this review, and having incorporated legal advice received, the Group has increased its customer redress provision to £1.7m (2014: a provision of £0.5m for refunds was included in Creditors) to provide for instances of non-compliance with the CCA within the NMB MAC and CLC portfolios. The provision includes an estimate of the potential cost of interest refunds during periods of non-compliance and other costs associated with a customer redress exercise.

Although a detailed review of these portfolios has been carried out, there is no judicial certainty in the legal position and there is a risk that further conduct issues or cases of non-compliance with regulations could be identified in the future. As a result the actual results could differ materially from our estimates.

The Directors consider the customer redress provision to be a critical accounting estimate.

Provision has been made where the Group is aware of a specific conduct or regulatory issue and can estimate its impact reliably, further details in respect of the Group's consideration of other potential conduct and regulatory issues is provided in the contingent liabilities Note 33.

33. Contingent liabilities and assets

(i) Contingent liabilities:

Given the high level of scrutiny regarding financial institutions' treatment of customers and business conduct from regulatory bodies and other sources there is a risk that certain aspects of the Group's current or historic business, including, amongst other things, CCA regulated loans, may be determined by the FCA and other regulatory bodies or the courts as, in their opinion, not being conducted in accordance with applicable laws or regulations, or fair and reasonable treatment.

As detailed in Note 32 provision has been made, following a detailed analysis, for the costs of customer redress in respect of identified cases in periods of non-compliance with CCA regulations.

There is a risk that other aspects of the Group's business might be considered as not having been conducted in accordance with all relevant regulation, or the fair and reasonable treatment of customers. It is also not possible to rule out the possibility of other instances of non-compliance with CCA or other regulations which have not been identified. No provisions against these risks are included in these accounts.

(ii) Contingent assets:

The Society continues, based on legal advice, with the claim against Grant Thornton UK LLP for breach of contract, negligence and breach of statutory duty relating to audit services and advice provided between 2006 and 2013.

34. Post balance sheet event

After the year end, on 11 April 2016, the Society received new Individual Capital Guidance ("ICG") from the PRA setting out the amount of regulatory capital the Society is required to hold. The Board has reviewed the capital resources following the new guidance from the PRA and has concluded that the ICG and CRD IV buffer requirements are met. The Board also concluded that the Society meets the quantitative aspect of the PRA buffer. As previously, the Society is expected to hold a certain proportion of its capital buffers in CET1 capital; this remains challenging under the new guidance and the Society may not meet these expectations going forward.

ANNUAL BUSINESS STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2015

1. Statutory limits

	2015	Statutory
	%	% limit
Lending limit	10.19	25.0
Funding limit	12.64	50.0

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986, as amended by the Building Societies Act 1997.

The Lending limit measures the proportion of business assets not in the form of loans fully secured on residential property and is calculated as (X - Y) ÷ X where:

X = business assets, being the total assets of the Group plus provisions for bad and doubtful debts less liquid assets, tangible fixed assets and intangible assets as shown in the Group accounts.

Y = the principal of, and interest accrued on, loans owed to the Group which are fully secured on residential property and mortgage loss provisions.

The Funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals and is calculated as (X - Y) ÷ X where:

X = shares and borrowings, being the aggregate of:

(i) the principal value of, and interest accrued on, shares in the Society;
(ii) the principal value of, and interest accrued on, sums deposited with the Society or any subsidiary undertaking of the Society;
(iii) the principal value of, and interest accrued under, bills of exchange, instruments or agreements creating or acknowledging indebtedness and accepted, made, issued or entered into by the Society or any such undertaking less any amounts qualifying as own funds.

Y = the principal value of, and interest accrued on, shares in the Society held by individuals otherwise than as bare trustees (or, in Scotland, simple trustees) for bodies corporate or for persons who include bodies corporate.

The statutory limits are laid down under the Building Societies Act 1986 as amended by the Building Societies Act 1997 and ensure that the principal purpose of a Building Society is that of making loans which are secured on residential property and are funded substantially by its members.

Other ratios

As a percentage of shares and borrowings:

	2015	2014
	%	%
Gross capital	11.0	10.4
Free capital	12.6	11.4
Liquid assets	20.7	22.9
Leverage ratio	5.6	4.6

As a percentage of mean total assets:

(Loss)/profit after taxation	(1.05)	0.77
Group management expenses	1.48	1.05
Society management expenses	1.28	0.95

The above percentages have been prepared from the Group accounts and in particular:

'Shares and borrowings' represent the total of amounts due to customers, amounts owed to banks, amounts owed to other depositors and debt securities in issue in the Group statement of financial position.

'Gross capital' represents the aggregate of reserves, other borrowed funds, profit participating deferred shares and subscribed capital as shown in the Group statement of financial position.

'Free capital' represents the aggregate of gross capital and general loss provisions for bad and doubtful debts less property, plant and equipment in the Group statement of financial position.

'Mean total assets' represent the amount produced by halving the aggregate of total assets at the beginning and end of the financial year for the Group/Society.

'Liquid assets' represent the total of cash and balances with central banks, loans and advances to banks and debt trading securities in the Group statement of financial position.

'Leverage ratio' is the ratio of Tier 1 capital divided by total exposure, which includes the sum of on balance sheet exposures, derivative exposures and off balance sheet items.

'Management expenses' represent the aggregate of administrative expenses and depreciation taken from the Group/Society Statements of Comprehensive Income.

ANNUAL BUSINESS STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2015

2. Information relating to the directors and officers as at 31 December 2015

Name	Date of Birth	Date of appointment	Occupation	Other directorships
Directors				
J.P. Allen	3.6.1953	Nov 2009	Consultant	Emerson Developments (Holdings) Limited J & JA Associates Limited Jones Homes Limited Pallet-Track Limited
H.F. Baines	12.3.1957	Aug 2013	Consultant	Halifax Pension Nominees Limited Harry Baines Consulting Limited HBOS Final Salary Trust Limited Lloyds Banking Group Pension Trustees Limited PACE Trustees Limited
I.A. Dewar	14.9.1957	Aug 2013	Chartered Accountant	Aldenham Foundation Brewin Dolphin Limited Brewin Dolphin Holdings plc Arbuthnot Banking Group plc Arbuthnot Latham & Co Limited
D.A. Harding	29.7.1947	Apr 2013	Company Director	
P.A. Lynch	31.8.1969	Apr 2002	Building Society Executive	MBS (Mortgages) Limited MBS (Property) Limited
F.B. Smith	3.1.1959	Jan 2014	General Counsel	
Officers				
C.W. Gee			Head of Corporate Development & Society Secretary	
R.H. Green			Interim Finance Director	
A. Hodges			Interim Chief Executive	Lamjam Limited
I.A. Johnson			IT Manager	
J. C. Johnson			Operations Manager	
E. Lord			Interim Chief Risk & Compliance Officer	
R. Mervill			TCF Conduct & Operations Manager	
A.C. Pradena			Savings Customer Services Manager	
D. Spencer			Lending Manager	
G.C. Worthington			HR & Administration Manager	Buzybakson Enterprises Limited

Executive Director		Position	Date of signing service contract
P.A. Lynch	31.8.1969	Operations Director	3.4.2002

The executive director has an employment contract which is terminable by the Society by giving 12 months' notice. The executive director is required to give 6 months' notice to the Society to terminate his contract.

ANNUAL BUSINESS STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2015

Non-Executive Directors

Non-executive directors are not appointed under service contracts. Their appointment is terminable by 1 month's notice on either side. In the event of the Society merging with another society whilst D.A. Harding is the Chairman of the Board, he is entitled to 6 months fees under his letter of appointment.

It is indicated to each non-executive director that they would not be expected to serve more than nine years on the board, although for the avoidance of doubt this is not a contractual commitment to the directors. Accordingly, by reference to a full nine year term, the unexpired part of each non executive director's term at 31 December 2015 would be:

J.P. Allen	2 years and 10 months
H.F. Baines	6 years and 8 months
I.A. Dewar	6 years and 8 months
D.A. Harding	6 years and 4 months
F.B. Smith	7 years

Any documents may be served on the above named directors at the following address: Lyons Wilson, 1 Central Street, Manchester M2 5WR.

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