Shawbrook Bank

Shawbrook Group plc
Annual Report & Accounts 2019

Proudly different.

Contents

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Shawbrook – Proudly different.

Shawbrook is a leading specialist bank providing lending and savings products to small and medium enterprises (SMEs) and consumers. We have an established reputation for providing products and services in sectors we know and understand, that deliver quality and consistency for our customers, either directly or through our partnership models.

We remain committed to the simple quality of good sense, adopting traditional values with a modern delivery. This is a big part of who we are.

Communication matters. We listen, we understand and we talk to one another. We care about our customers and their specialist needs. People are the life force of our business, so our approach is to blend human judgement with data and technology when it comes to decision-making.

That's why ensuring a deep understanding of our customers is a top priority.

The difference in being different.

How we've done
2019 key highlights

How we have delivered against our strategic pillars:

Maintain excellent credit quality

47bps
Cost of risk

Progressively increase originations

15%
Increase in loan book to £6.8 billion

Maintain conservative foundations

12.0%
CET1

16.4%
Total capital ratio

Enhance customer focus

In 2019 we served over
420,500
personal and business customers

Achieve strong risk adjusted returns

6.4%
Gross asset yield

Our business

What we do

Shawbrook is a specialist UK lending and savings bank focused on Property Finance, Business Finance, Consumer Lending and Savings. We differentiate ourselves by concentrating on markets where our expert knowledge, judgement and personalised approach to underwriting offer us a competitive advantage.

Our divisions

Property Finance
Our Property Finance division is comprised of our Commercial Property and Residential Mortgages teams. Aimed at serving professional landlords and property traders in residential and commercial asset classes, and personal customers through specialist second charge mortgages.

£4.4bn
Loan book

Business Finance
Our Business Finance division offers a wide range of products to serve the UK SME market. Whether it is replacing essential equipment or investing for growth, when it comes to funding, we understand that speed, flexibility and certainty matter the most.

£1.7bn
Loan book

Consumer Lending
Our Consumer Lending division provides digital unsecured personal loans to consumers for a variety of purposes including home improvement and holiday ownership.

£0.7bn[1]
Loan book

Savings
Our Savings division provides a wide range of cash savings solutions, both directly and through partners, to our personal and SME customers.

£6.1bn
Customer deposits

[1] Includes loans classified as assets held for sale of £104.1 million.

Our differentiated approach

The Shawbrook way
A customer led approach...

- Specialists.
- Thoughtful decision making through judgement.
- Driven by customer needs.
- Innovative and tailored products.
- Focus on quality.

Our five strategic pillars

- Achieve strong risk adjusted returns
- Enhance customer focus
- Maintain excellent credit quality
- Progressively increase originations
- Maintain conservative foundations

Our values

We are expert:
we are quietly confident and enabling.

We are driven:
we are ambitious and passionate.

We are practical:
we are down to earth and pragmatic.

We act with integrity:
we are thoughtful and responsible.

Our people and community

814
Employees (average on a full-time equivalent basis)

45
Charities supported

Gender split

56% male

44% female

Chairman's statement
John Callender

We firmly believe that good corporate governance provides the foundation for a successful organisation and in 2019 we continued to evolve Shawbrook's governance framework.

It is with great pleasure that I introduce Shawbrook's 2019 Annual Report and Accounts, reviewing the strong progress we have made throughout the year against both our strategic and financial objectives.

I am pleased to report that the Group has continued to deliver impressive and balanced growth through supporting our customers' growth ambitions, achieving both loan growth of 15% and an encouraging 11% year on year increase in profit before tax to £122.4 million for the year ended 31 December 2019. This was driven by an enhanced focus on our SME propositions.

Business model and strategy

2019 was an important year in the evolution of Shawbrook's business model and strategy. The Board and Executive team have worked closely together to agree the strategy that will best drive value for all our stakeholders, while also ensuring continued development of a safe and sustainable business model.

We have reviewed our various revenue streams with the aim of simplifying the business and to ensure that we focus on products where we can support our customers' needs most effectively whilst generating value for Shawbrook. A number of changes have been successfully implemented which are detailed in this report, including the sale of our offshore business, Shawbrook International Limited and the rationalisation of our Consumer Lending offering and partner relationships.

The changes provide increased clarity on where and how we will play in our chosen markets, with a greater focus on the attractive SME segments, where our expert knowledge, judgement and human touch give us a competitive advantage. These strengthen our business model and give our stakeholders a clear sense of purpose, setting us up for further success as we head into 2020.

Good corporate governance

We firmly believe that good corporate governance provides the foundation for a successful organisation and in 2019 we continued to evolve Shawbrook's governance framework. This included commissioning a further independent Board effectiveness review, details of which can be found in the Corporate Governance Report on page 45.

In October 2019, we welcomed Michele Turmore to the Board as a Non-Executive Director. Michele brings with her an impressive track record across both retail and commercial banking. Formerly a Chief Operating Officer at the SME bank Allica, her insights have been welcomed by the Board and Executive team alike.

Roger Lovering, David Gagie and Sally Ann Hibberd stepped down from the Board in 2019 and I would like to take this opportunity to thank them for their support and dedication to the Group and wish them well for their future endeavours.

Further information about our stakeholders and how the Board and Group engaged with them can be found on pages 15 to 18.

Our approach to sustainability

We understand that in order to deliver truly sustainable returns, the Group's social, environmental and economic impact must be embedded into our day to day business activity. Our approach to sustainability is delivered through four key segments: environment, community, marketplace and workplace. Further information on these segments and progress made in 2019 can be found on pages 33 to 37.

Investing in our employees

Now with more than 800 talented Shawbrook employees, the culture in which our people work remains critical to our success. We know that to attract and maintain this high-level talent, we must remain committed to prioritising employee satisfaction and development whilst maintaining a positive workplace culture.

Key to our culture is inclusion and diversity, ensuring we access the widest talent pool available and that our employees feel welcome and included and can bring their 'whole-selves' to work. In 2019, we introduced several initiatives including an employee-led inclusion network and a new employee mentoring programme. These have the added benefit of bank wide collaboration by broadening internal networks.

Looking ahead

I would like to take this opportunity to extend my thanks to all Shawbrook's employees as well as the Board and Executive team for their continued commitment to the Group. We have made extensive headway from where we were a year ago and it would not have been achievable without their tireless support.

I see an exciting future for Shawbrook, as we continue to closely align our model to support our customers and deliver our specialist propositions in line with our ambition to be recognised in our markets as the specialist SME lender of choice.

Since the year end, the Covid-19 outbreak has been classified as a pandemic by the World Health Organization. We have been monitoring its impacts closely and have taken all precautions as advised by the government to ensure the safety of our employees, whilst ensuring continuity of operations. We have implemented our Incident Management Plan within the business and are continually assessing the impacts against our operating model and future business plans.

At this stage, we are satisfied with how the Group has responded to this unprecedented event, with the majority of our staff now working from home and our material outsourced suppliers providing their critical services successfully under the current conditions. Whilst the full effects are not known, at the time of publishing these accounts, the Group continues to be fully operational and profitability for the first quarter of 2020 is in line with our financial forecasts.

John Callender
Chairman

Chief Executive Officer's statement
Ian Cowie

2019 has been another year of strong performance for Shawbrook, driven through an increased focus on our core markets and further development of our specialist propositions, whilst continuing to invest in our franchise for the future.

I am delighted to be presenting Shawbrook's 2019 Annual Report and Accounts following my first full year as Chief Executive Officer. We are reporting another strong and progressive set of results, further endorsing our continued emphasis on the specialist segments we serve.

Continued growth

An increased focus on our core propositions has helped drive strong lending volumes with our loan book increasing by 15%, or £0.9 billion, to £6.8 billion[1] at the end of 31 December 2019. This growth was particularly evident across our Property Finance and Business Finance divisions, where loan balances increased to £4.4 billion and £1.7 billion respectively.

Our cost to income ratio decreased to 48.5% and is on an improving trend as we begin to benefit from improved operational efficiencies, underpinned by investment in automation. We expect a continued positive trajectory as we head through 2020, whilst still managing to balance a progressive investment plan. Profit before tax increased 11% year on year to £122.4 million, or 26% excluding the one-off insurance recovery recognised in 2018. We maintain our focus on delivering strong risk adjusted returns in our chosen markets, with an improvement in the cost of risk to 0.47% also present. The Group experienced some competitive pricing pressures in certain markets which, when combined with a shift in asset mix, has put pressure on gross asset yield. Notwithstanding this, we delivered a net interest margin of 4.6%.

[1] Includes loans classified as assets held for sale of £104.1 million.

Building out our specialist SME capabilities

In 2019, we set out our strategic aspirations to place greater emphasis on providing specialist solutions to the SME markets, in particular where we have deep expertise and can offer a truly differentiated proposition to serve our customers' needs.

We have simplified our business, our propositions and our processes, exiting certain product lines and markets where these no longer fit our strategic rationale. Shawbrook International Limited (our offshore Jersey entity), for example, lacked the scale required and in October 2019 we successfully sold the business via a management buy-out transaction. I wish the team every success for the future.

As part of a detailed strategic review of our Consumer Lending franchise, we have rationalised our footprint in this space, for example withdrawing the buy-now-pay-later product and exiting the retail point-of-sale market. This will enable us to focus on those consumer lending segments where we have a unique selling point, delivering straightforward lending products through customer-centric propositions.

We also entered some new markets and developed new services such as our unitranche loan and buy-to-let product switch portal. We will continue to build on these foundations in the short to medium-term, to deliver sustainable growth across the franchise while improving customer experience.

Funding our growth

Our deposit franchise is key to our lending growth and in 2019 we stepped up our investment in our Savings business, serving more than 147,000 customers with our simple, straightforward and consistently competitive savings products. To provide a more rounded SME offering, we also successfully launched our new digital SME deposit range.

We also continued to diversify our funding sources more broadly, successfully completing our maiden securitisation – further information can be found in the Chief Financial Officer's review on pages 9 to 12.

Strengthening the team

The strong performance achieved in 2019 is the result of the experience and effort that everyone at Shawbrook demonstrates on a daily basis and for this, I'd like to express my thanks to all staff.

During the year, I was delighted to welcome two new members to the Executive team. John Eastgate joined as the Managing Director of our Property Finance division and Julian Hynd joined as Chief Operating Officer.

Both John and Julian have tremendous experience and proven ability in their fields and it is a real testament to the business and the progress we have made that we can attract such high calibre individuals who share our vision and are already playing a pivotal part in driving sustainable growth.

Looking to the future

We are mindful of the economic uncertainty that continues to exist, primarily in relation to trading conditions following the UK's exit from the EU and, most recently, the Covid-19 pandemic. In relation to Covid-19, we are taking all appropriate steps in line with government advice and reviewing the most up-to-date information available. We have implemented our Incident Management Plan and our priority during this period continues to be on ensuring the safety of our people, whilst keeping our business operational to meet the needs of our customers. Alongside this, we will continually assess the possible impacts to our operating model and future business plans and adapt them to ensure we remain within our risk appetite.

As this report describes, we have made significant progress over the last year and I am confident that our ongoing investment plan is leading to improvements for customers whilst creating long-term sustainability and value for our business. I believe we are uniquely placed to lead the market as the specialist SME lender of choice.

Ian Cowie
Chief Executive Officer

Chief Financial Officer's review
Dylan Minto

2019 has seen continued growth with profit before tax increasing 11% year on year to £122.4 million and excluding the one-off insurance recovery recognised in 2018, growth was 26%. Our strategic focus on our specialist propositions enabled strong asset growth of 15% whilst also exiting our offshore business.

Key performance indicators[1]	**2019**	2018	% change
Assets and liabilities			
Loan book (£m)	**6,781.7[2]**	5,880.0	15.3
Average principal employed (£m)	**6,372.6**	5,351.8	19.1
Customer deposits (£m)	**6,109.4**	4,977.9	22.7
Wholesale funding (£m)	**1,122.3**	1,029.4	9.0
Profitability metrics			
Gross asset yield (%)	**6.4**	6.8	(0.4)
Liability yield (%)	**(1.8)**	(1.6)	(0.2)
Net interest margin (%)	**4.6**	5.1	(0.5)
Management expenses ratio (%)	**(2.2)**	(2.6)	0.4
Cost to income ratio (%)	**48.45**	51.2	(2.7)
Cost of risk (%)	**(0.47)**	(0.43)/(0.68)[3]	(0.04)/(0.21)
Return on lending assets before tax (%)	**1.9**	2.1	(0.2)
Return on tangible equity (%)	**15.7**	16.1	(0.4)
Liquidity			
Liquidity coverage ratio (%)	**274.5**	244.9	29.6
Capital and leverage			
Common Equity Tier 1 capital ratio (%)	**12.0**	12.3	(0.3)
Total Tier 1 capital ratio (%)	**14.5**	15.2	(0.7)
Total capital ratio (%)	**16.4**	17.0	(0.6)
Leverage ratio (%)	**8.6**	9.2	(0.6)
Risk-weighted assets (£m)	**4,974.5**	4,206.8	18.2

Progressively increasing originations

A progressive increase in originations drove strong net lending of £0.9 billion across the portfolio and resulted in the loan book increasing by 15% to £6.8 billion (2018: £5.9 billion). Strong demand for our SME led customer propositions saw higher levels of growth across Property Finance, up 20% to £4.4 billion and Business Finance, up 16% to £1.7 billion. As discussed on page 18, the Board undertook a strategic review of our lending proposition during 2019 and we chose to dispose of Shawbrook International Limited, our Jersey specialist lending business (assets of c.£28 million). Following the strategic review of our Consumer Lending proposition, we also agreed the sale of a legacy unsecured personal lending portfolio as we refocus our unsecured offering inside our proprietary underwriting scorecards.

Diversifying our funding base

Our funding base remains predominantly retail and SME deposit led with a significant component being from the Term Funding Scheme (TFS).

Customer deposits increased 23% to £6.1 billion (2018: £5.0 billion). Wholesale funding increased 9% to £1.1 billion and was supported by the Group's successful inaugural securitisation in June of a £250 million mortgage backed security to external investors.

We issued an additional £20 million in Tier 2 capital through a private placement in September at a coupon of 6.5% and ensured we maintained an optimal hybrid capital position. In order to position the balance sheet for the maturity of the TFS, we chose to early redeem £118 million of our initial tranches from the scheme and following this we had £757 million drawn under the scheme with contractual maturities spread across 2021 and 2022. We are now reviewing our options following recent announcements regarding the Term Funding Scheme with additional incentives for SMEs.

[1] Key performance indicators are defined on page 216

[2] Includes loans classified as assets held for sale of £104.1 million.

[3] 2018 cost of risk excluding £13.0 million insurance recoveries was 68 basis points.

Chief Financial Officer's review

Achieving strong risk adjusted returns

During the year, operating income grew by 13% to £408.3 million (2018: £361.4 million) reflecting net loan growth. Our gross asset yield of 6.4% (2018: 6.8%) fell slightly as the loan book shifted away from the Consumer Lending loan book to 10% of the portfolio at 31 December 2019 (2018: 13%) and against the backdrop of a highly competitive rate environment. Interest expense increased by 30% to £113.2 million with the liability yield increasing to 1.8% (2018: 1.6%) driven by our increased wholesale funding and early TFS repayment. Retail deposit costs increased slightly to 1.5%[1] for the year ended 31 December 2019 (2018: 1.4%). As a result, the Group's net operating income increased by 8% to £295.1 million (2018: £274.1 million) while the net interest margin reduced to 4.6% (2018: 5.1%).

Maintaining excellent credit quality

Whilst we continued to experience economic uncertainty throughout 2019, our cost of risk remained low at 0.47% (2018: 0.43%) reflecting our robust approach to risk management. Adjusting for the insurance recoveries received in 2018, our cost of risk reduced against 0.68% recognised in 2018. Of the total 2019 impairment charge, £8.1 million, (2018: £15.5 million) related to the £104.1 million portfolio of loans which the Group sold post year-end.

Continued investment in people and technology

Careful cost management remains a key objective of the Group, however, we continued to invest in technology solutions to support our business priorities.

Total administrative expenses increased to £138.5 million (2018: £130.3 million), an increase of 6% reflecting further investment in the business including growth in our teams, costs incurred to meet regulatory developments such as GDPR, and enhancements to our customer proposition and service as we seek to sustainably grow the Group in our chosen segments.

We continue to provide for conduct matters in relation to liabilities under the Consumer Credit Act where suppliers have become insolvent. However, the charge for the year reduced to £4.5 million (2018: £10.1 million).

The cost to income ratio decreased to 48.5% (2018: 51.2%) and the management expenses ratio reduced to 2.2% (2018: 2.6%) as we begin to benefit from the solid foundations we have invested in during previous years.

	2019 £m	2018 £m	% change
Operating income[2]	**408.3**	361.4	13.0%
Interest expense and similar charges	**(113.2)**	(87.3)	(29.7%)
Net operating income	**295.1**	274.1	7.7%
Administrative expenses	**(138.5)**	(130.3)	(6.3%)
Impairment losses on financial assets[3]	**(29.9)**	(23.2)	(28.9%)
Provisions for liabilities and charges	**(4.5)**	(10.1)	55.4%
Total operating expenses	**(172.9)**	(163.6)	(5.8%)
Share of results of associate	**(0.1)**	(0.5)	80.0%
Gain on disposal of subsidiary	**0.3**	–	–
Profit before tax	**122.4**	110.0	11.3%
Tax	**(28.8)**	(25.9)	(11.2%)
Profit after tax	**93.6**	84.1	11.3%

Maintaining conservative foundations

As at 31 December 2019, the Group maintained a robust capital position with a total capital ratio of 16.4% (2018: 17.0%) and a Common Equity Tier 1 ratio of 12.0% (2018: 12.3%). The reduction in capital ratios over the year reflect the profit after tax of £93.6 million and a private issuance of £20 million Tier 2 capital, offset by growth in risk-weighted assets of £768 million and payment of AT1 coupons totalling £9.8 million. We continue to optimise our capital resources while maintaining a robust and prudent risk appetite.

The Group is not required to comply with the PRA leverage ratio framework, however the Group maintains its returns with prudent levels of leverage. The leverage ratio for the Group is 8.6% (2018: 9.2%), compared to the minimum requirement of 3.0% with risk-weighted assets as a proportion of customer loans having remained stable at c.73% (2018: c.72%).

Outlook

During 2019, we reviewed the strategic ambitions of the Group and aligned our proposition, positioning the Group well to navigate the known challenges ahead. These challenges include a continuation of low interest rates, ongoing uncertainty as the UK government negotiates a post-Brexit trade relationship with the EU and continued pricing competition in many of our markets. The recent Covid-19 pandemic, whilst still developing, will create further challenges to the economy and, alongside any government and regulatory responses, we will take the appropriate steps to support our customers whilst ensuring our capital and liquidity remains within appetite.

Dylan Minto
Chief Financial Officer

[1] Calculated as interest expense on customer deposits divided by average principal employed.

[2] Includes interest income calculated using the effective interest rate method, other interest and similar income, net income from operating leases, net fee, commission income, net gains/(losses) on financial instruments mandatorily at fair value through profit or loss and other operating (expense)/income.

[3] During the year ended 31 December 2018, the Group received £13.0 million from the Group's insurance claim in respect of a controls breach identified in the Business Finance division in 2016.

Our business model
A unique model for a ‘proudly different bank’...

At Shawbrook, we provide specialist solutions to both the UK SME and consumer markets by challenging the conventional approach of the mainstream banks. When it comes to serving our customers, our approach is to combine human judgement with data and technology to offer a truly differentiated proposition and generate sustainable attractive returns.

Our people

The Shawbrook way.
A customer led approach...

Specialists

Thoughtful decision making

Innovative and tailored products

Driven by customer needs

Focus on quality

We use our expertise and judgement to make individual decisions that balance risk and return with customer needs.

Our customers

SMEs | **Landlords** | **Homeowners** | **Consumers** | **Savers**

Across our carefully selected markets...

Business

Property

Consumer

Our channels to market

Through direct and indirect channels...

KBIs
Key business introducers in professional services are primarily utilised by our Business Finance division.

Sponsors
Working with private equity and venture capital firms to support their financial goals.

Direct
Our customers can access our services directly via our website, call centres and relationship staff.

Brokers
We have a selected panel of brokers and for certain products we utilise broker networks.

Supported through the prudent management of liquidity and capital

Our specialist savings franchise

A primarily deposit funded model through the deployment of our personal and business savings products.

c.85%
funding liabilities

Wholesale funding

We also utilise the wholesale funding market to strengthen our capital base:

- TFS
- Securitisation
- Bilateral Secured Funding

c.15%
funding liabilities

Creating value for our stakeholders

The Board of Directors understand their duties and responsibilities under the Companies Act 2006 (2006 Act). This section of the Strategic Report describes how the Directors have had regard to the matters set out in section 172(1) (a) to (f) of the 2006 Act. Detail of how the Board has engaged with the Group's stakeholders is set out below. Further information on how Board members have fulfilled their Directors' duties can be found in the Corporate Governance Report.

The Board believes that effective stakeholder engagement is central to ensuring responsible and balanced outcomes, while also helping to both shape Shawbrook's strategy and align business activities with stakeholder expectations. Throughout the year, the Board engaged with each of our stakeholder groups, both directly and indirectly, in order to bring their views and insights into the room.

Customers

Our customer base is comprised primarily of UK SMEs and consumers seeking specialist finance and savings solutions. Customers are at the core of our business, so our engagement with customers facilitates our ability to ensure a continued understanding of their needs and required outcomes.

The Board regularly reviews customer management information (MI), for example complaints data, to understand trends and enable continuous improvement to the Shawbrook proposition. The Executive Directors and broader Executive team also continually engage with customers to understand areas for improvement, reporting this information back to the wider Board.

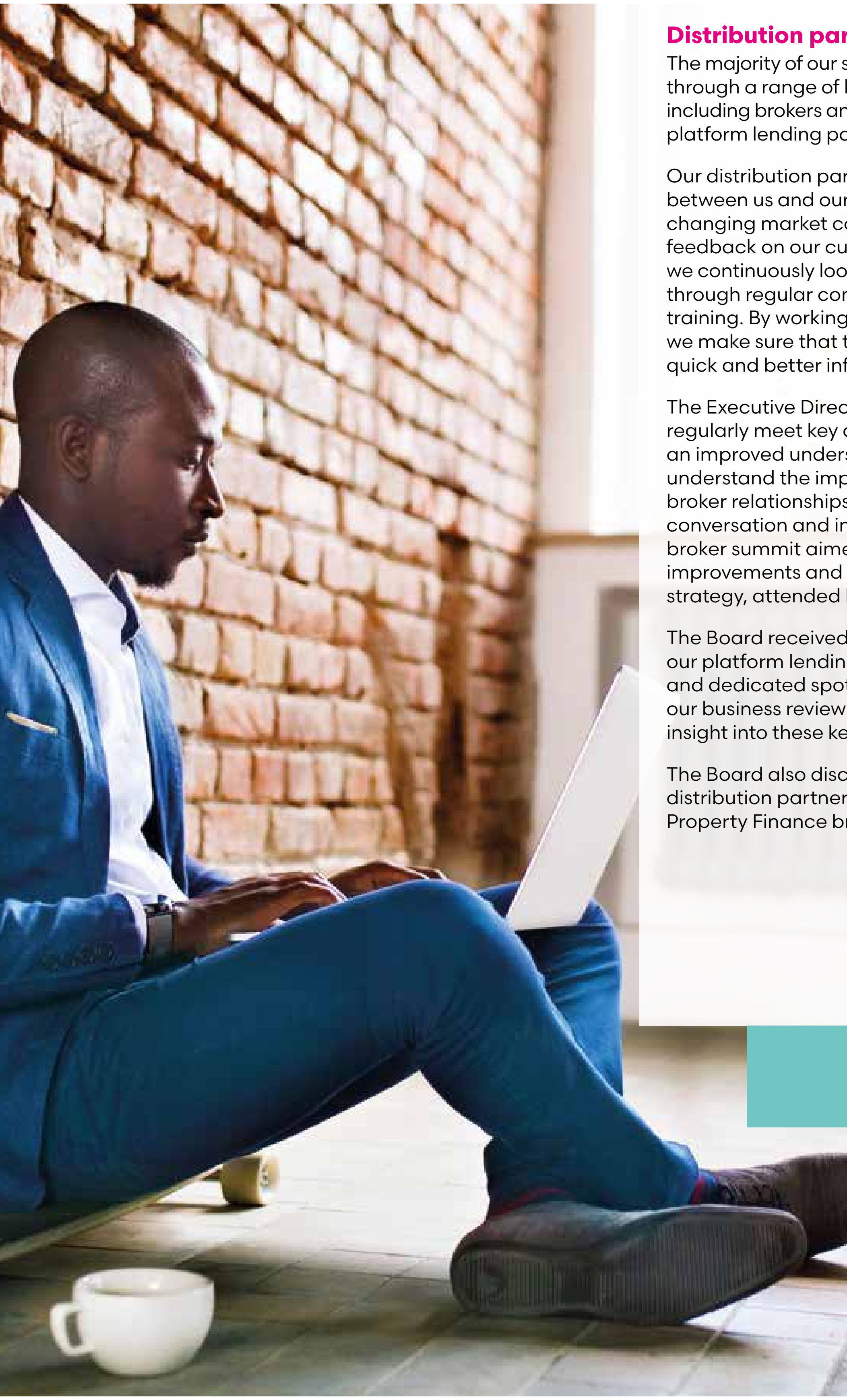
One of the agreed Shawbrook business 'enabler' areas is to enhance focus on customer needs – this entails encouraging all staff to bring customer views and insights into day to day business operations and decisions, especially when designing new products. More detail on how the Board received these insights to inform a key investment decision is included in the commercial property re-engineering case study.

Case Study

Commercial property re-engineering

During the year, the Group made platform improvements to benefit our commercial property customers. Utilising technology to improve the end to end customer journey. The relevant investment proposal presented to the Board by the employee project team contained key outputs from a customer journey mapping exercise evidencing customer, broker and employee 'pain points' arising from the previous process. The Board's review of stakeholder MI played a fundamental role in the decision to support the improvements and agree the investment. Approval was provided subject to the business initiating regular progress meetings with the Group's majority shareholders to monitor the project status.

Following launch of our new product switch portal, a demonstration of the end to end customer journey was presented by employees at a Board meeting and support was subsequently given to commence with the next stage of the project. The platform changes also underwent governance reviews by the Board's risk and product sub-committees to ensure they sat within the Group's risk appetite and were in the best interests of our customers.



Distribution partners

The majority of our specialist propositions are deployed through a range of like-minded distribution partners; including brokers and networks, key business introducers, platform lending partners and digital partners.

Our distribution partners provide a crucial interface between us and our customers, keeping us informed on changing market conditions and sentiment including feedback on our customer propositions. As a result, we continuously look for ways to deepen relationships through regular communications, feedback and training. By working collaboratively with our partners, we make sure that the right tools are in place to enable quick and better informed decisions for our customers.

The Executive Directors and Executive team regularly meet key distribution partners to enable an improved understanding of their businesses. We understand the importance of providing all strategic broker relationships with an opportunity to join our conversation and in 2019, we held our first property broker summit aimed at updating brokers on business improvements and aligning them with our 2020 strategy, attended by the Chief Executive Officer.

The Board received detailed MI on performance of our platform lending solutions partner propositions, and dedicated spotlight discussions were also held at our business review offsite sessions which gave further insight into these key relationships.

The Board also discussed feedback received from our distribution partners, including the results of our 2019 Property Finance broker barometer.

Creating value for our stakeholders

Employees

Our employees are critical to the successful delivery of our strategy, so we are committed to prioritising employee engagement, satisfaction and development.

We ran two engagement surveys over the course of the year, providing the opportunity for the Board to understand and act on our key employee engagement drivers. This was complemented by regular feedback shared with the Board by our Group Human Resources Director, acting as the representative for employee voice, including designated people and culture sessions at Board meetings and business review offsite sessions.

During 2019, we hosted a range of employee events, such as our annual staff conference, updating employees on the Group's strategy, performance and priorities. Board members have been present at a number of these events, for example our Chairman provided the introduction to our all staff conference as well as presenting our 2019 employee recognition awards.

Board meetings were hosted across three different Shawbrook office locations. These included 'Director walkabouts', which covered both business and functional areas, facilitating direct dialogue between the Board and employees.

Throughout 2019, the Board also supported the introduction of several employee initiatives to promote a culture of inclusion, for example our newly launched mentoring scheme and staff recognition tool.

Suppliers

Our business is supported by more than 700 suppliers, ranging from small local fruit providers to our larger loan servicing partners, and our supplier network provides us with the tools required to better serve our customers.

Underpinning our desire to improve cultural alignment, we regularly engage with our supplier community to ensure they are acting in accordance with our ethical requirements, acting responsibly and our supply chain remains aligned to our core values.

The Executive Directors and Management conduct regular meetings with our suppliers including our material outsourcing partners. In 2019, this included a dedicated offsite session with our major servicing partner which focused on all aspects material to the Group's operations.

During the year, the Board also received regular MI on supplier performance and reports on specific supplier issues, complemented by dedicated spotlight sessions at Board meetings presented by the Chief Operating Officer, who is responsible for third party oversight arrangements.

Regulators

As a regulated UK bank, we are subject to the regulation of both the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) and the Board understands the importance of further developing relationships with both, liaising regularly on a range of topics.

The Chairman and Executive Directors met regularly with the PRA in 2019, to provide updates on strategic changes. Individual meetings were also held with a number of the Non-Executive Directors, as well as the PRA presenting at a Board meeting during the year.

We also had contact with the FCA throughout the year on topics such as culture and our compliance and broader strategy.

Investors

Our Investors include both our private equity Shareholders and our debt Investors.

Our Shareholders are central to Shawbrook's success, bringing a different perspective and expertise to the business. As such, there is regular dialogue and engagement with both major Shareholders on key performance, strategic and business matters. The Board composition also includes two Institutional Directors, who ensure that the views of our Shareholders are brought into the Boardroom. In 2019, additional Shareholder representatives also attended the dedicated business review offsite sessions, bringing additional insights to strategic topics.

The Executive Directors also hold one-to-one meetings with a range of our debt investors to keep them informed of Shawbrook's progress.

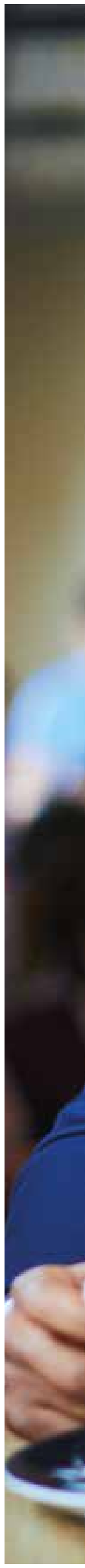
Community

Our Community stakeholder group includes both the local community and wider environment.

As a business we feel strongly about giving back to the community we operate in, and therefore continue to support local causes with charitable donations. During the year, the Board reviewed and approved the Group's annual charity budget to be put to a good cause and donated to employee nominated charities.

In addition, the Group's Chairman had direct engagement with one of the chosen charities that subsequently received donations.

The Group is also committed to functioning as a sustainable business and therefore closely manages its wider social and environmental impacts. During the year, the Board engaged in the production of the Group's Climate Change Plan, including approving the finalised plan prior to submission to the PRA. The Board recognises that climate change considerations will have greater prominence in business operations going forward.



Case study

Shawbrook International Limited disposal

During 2019, the Board and Executive team undertook a strategic review of our Shawbrook International operations in Jersey and Guernsey, leading to a decision to exit this business. This decision was aligned to our strategic aspiration to simplify the Group's business, enabling increased focus on our core value creation activities.

Stakeholder impact was central when determining the optimal outcome of the Group's exit from the Channel Islands and future of the Shawbrook International business. The focus was therefore on finding a purchaser who planned to continue the business and to build on the solid foundations laid, with the same customers, in the same community and working with the same local suppliers and distribution partners, while minimising the impact on Shawbrook International's staff. Investors' and regulators' views were also sought and taken into account, with our Shareholders and regulators in both the UK and Channel Islands engaged throughout the process.

The successful completion of a management buy-out transaction of Shawbrook International resulted in the continued employment of all its staff and its business operations remaining aligned, providing continuity to its customers, distribution partners and suppliers.

Business review
Property Finance

Activity

The Property Finance division offers a diverse range of commercial and residential mortgage products. Within these broad markets, we specialise in the following areas:

- **Commercial:** provides term and bridging finance to professional landlords and property investors in residential investment and commercial investment and owner-occupied asset classes.
- **Residential:** provides specialist residential second charge mortgages to owner occupiers for a variety of purposes including home improvements, loan consolidation and high-value consumer purchases.

Buy-to-let

Our specialist buy-to-let proposition forms a core part of the Property Finance division, providing experienced landlords with a range of term-finance options.

In September 2019, the business launched '*My Shawbrook Portal*', an online tool that significantly reduces the time taken for our buy-to-let customers to switch to a new product when nearing the end of their current mortgage term. This innovative platform differentiates Shawbrook in the specialist space, enhancing the retention experience by giving control of the application process to the customer whilst keeping the broker involved at all times.

In response to customer demand, we simplified our product range in December 2019. This represented the first step in a journey that will be an ongoing priority for the business which is to provide greater clarity of our offering to brokers and borrowers alike.

Commercial investment

In April 2019, the Group relaunched its commercial investment offering, aiming to build an industry-leading proposition, underpinned by skilful execution through a highly experienced underwriting team. The refocused proposition has been well received and has enabled us to grow our pipeline in this asset class, in support of our continued desire to serve specialist markets and deliver strong growth and good risk-adjusted returns.

Bridging finance

In March 2019, the Group extended the reach of its award-winning online application platform to include bridging finance. The platform enables efficient online management of bridging loan applications, driving a more efficient operation and improved customer service These improvements, along with other several revisions to our bridging finance proposition helped Shawbrook to win 'Short Term Lender of the Year' at the 2019 NACFB Awards.

Residential

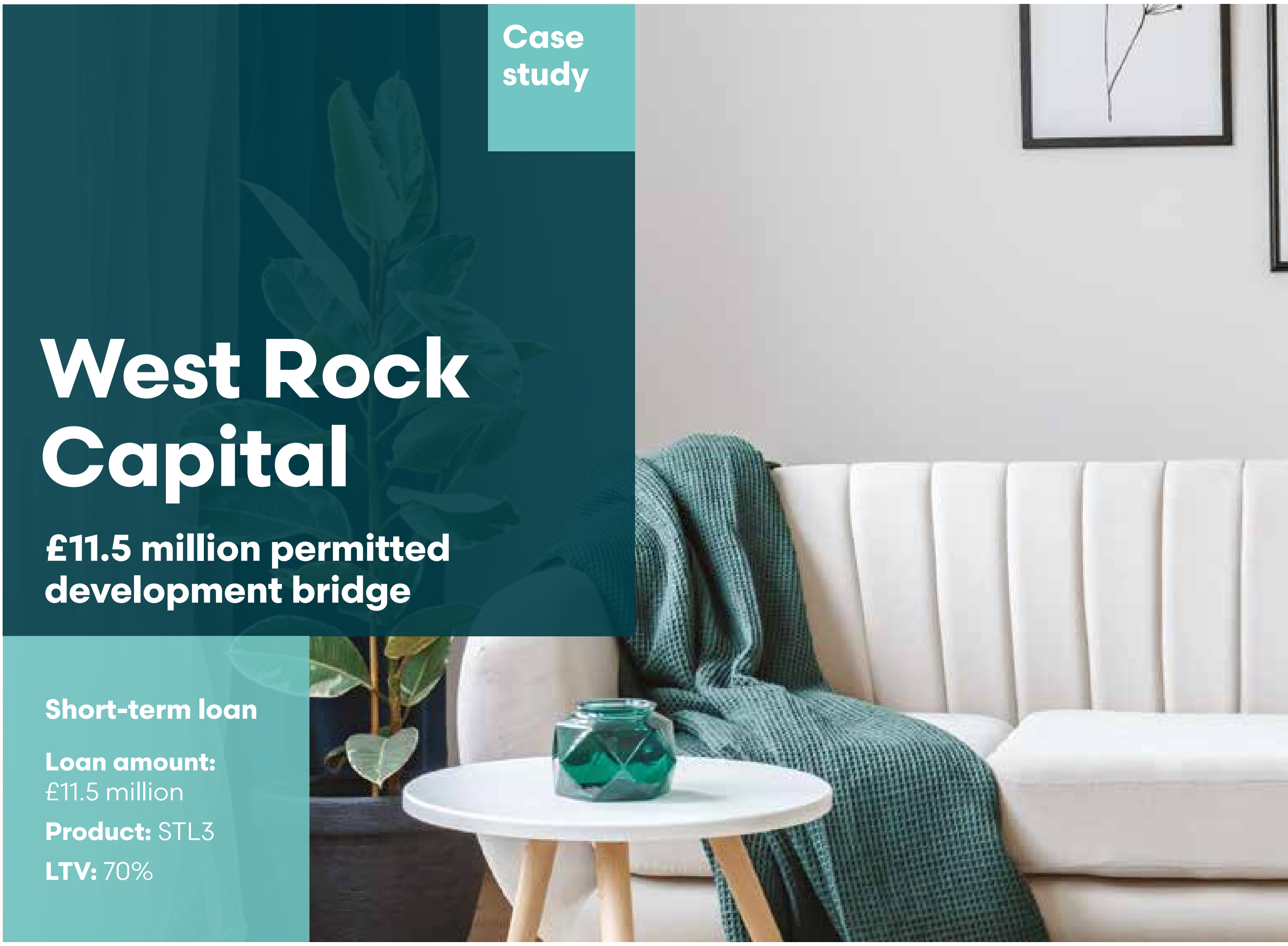
Following a substantial review of its products and proposition, the Group successfully returned to the second charge residential mortgage market in the second half of 2019. The business saw significant strengthening of new business volumes, especially through Q4 2019. The outlook for 2020 is robust and we believe there to be significant opportunity to grow market share at attractive returns.

Outlook

There is a well-established shift towards a more professionalised private rental sector, however our core markets have been constrained by the political and economic uncertainty that has prevailed since 2016. Whilst we anticipated that investors would return to the market in 2020, due to the recent outbreak of Covid-19 we will continue to closely monitor the associated market impacts and where necessary review our business model to align with the government and regulatory responses, ensuring support for our customers.

While political and economic turbulence creates market uncertainty, we believe many opportunities remain for tailored solutions to be delivered by a specialist lender focused on relationships and execution. Our focus on delivering relevant propositions, underpinned by a technology enabled service proposition, is starting to pay dividends and we believe that we are becoming increasingly better situated to support our customers in the specialist markets we know so well.

Case study



West Rock Capital

£11.5 million permitted development bridge

Short-term loan

Loan amount: £11.5 million

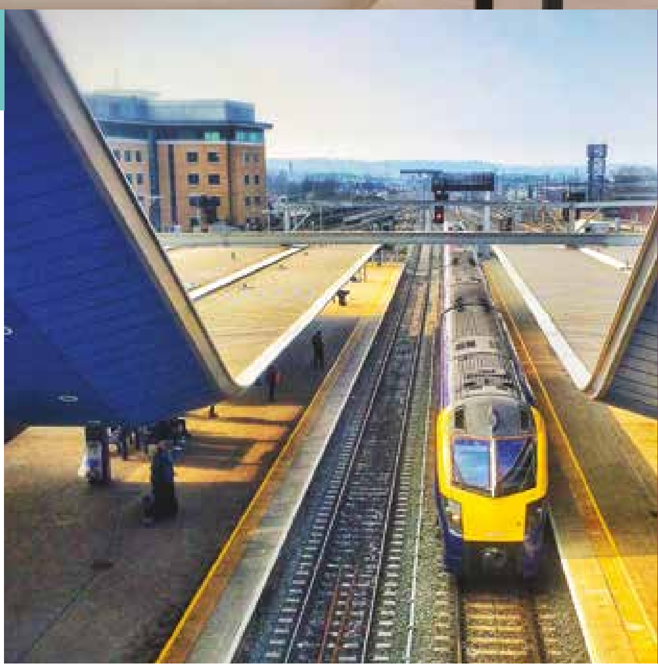
Product: STL3

LTV: 70%

Our Commercial Property team was approached by broker partner, West Rock Capital, and a long-established client who specialises in permitted developments. The client was looking for a 24-month bridging loan to purchase a commercial premises at Milton Keynes train station.

Worth £16 million, the client required a £11.5 million facility for the acquisition of this unusual property with the aim to sell in 18 to 24 months and with the potential of redeveloping into residential units. There were a few hurdles to navigate with this bridge, including risks associated with the premises being located at a train station. However, following a detailed review of this complex case, our team of specialist underwriters were comfortable that they saw no issues arising with the purchase or potential planning issues regarding converting the property into residential units, and as a result the team proceeded with the application.

Using our STL3 product, providing the ability to service the interest, the short-term team were able to fund this purchase at 70% LTV across a 24-month term, allowing additional time in case of any refurbishment or planning delays. Our Business Development Manager and underwriting team worked seamlessly with the broker and the case completed in 6 weeks.



"I am delighted to have successfully enabled our client to secure this exciting opportunity. Our extensive experience in property finance and long-term relationship with Shawbrook ensured our client was able to complete this complicated acquisition on time. This was a great team effort with Shawbrook and I am looking forward to working on more opportunities going forward."

Westley Richards, Director at West Rock Capital

Business review
Business Finance

Activity

The Business Finance division provides debt-based financing solutions to UK SMEs. Our portfolio of lending products are delivered through the following four distinct business propositions:

- **Asset finance:** offers leasing and instalment credit finance to UK based SMEs.
- **Corporate lending:** provides asset-based lending and commercial loans.
- **Structured finance:** provides finance to non-bank specialist lenders, either through wholesale funding or block discounting in addition to funding for UK SMEs with institutional ownership.
- **Development finance:** provides finance to established regional mid-size developers looking to build and refurbish properties in residential and commercial sectors for sale or investment.

Shawbrook International: as referenced on page 18, in October 2019 the Group carefully exited its Shawbrook International business.

Asset finance

During the year, the business initiated a strategic restructure of its asset finance proposition, resulting in the combination of all our asset finance activities into one business unit. Asset finance continues to originate business through both direct sales and broker partners with a focus on unregulated lease and instalment credit products.

In 2020, we will continue to work with third party providers to explore alternative technology opportunities to automate and simplify processes, making for a modern and efficient experience for our specialist asset finance customers.

Corporate lending

Following the creation of our central asset finance business we have focused our regional business centres on the direct delivery of asset based lending and our new commercial loan product under the new name of corporate lending. Focusing on these specific products, we have also highlighted London, Birmingham and Manchester as our key locations. In 2020, the business will work closely with the key business introducer community to support the deployment of our expertise in servicing our specialist customers across the UK.

Structured finance

Our structured finance proposition remained well received in its chosen markets throughout the year as we continued to serve UK SMEs throughout their lifecycle. The established wholesale finance and block discounting products maintained strong positions in supporting alternative lenders build their loan books and superseded their 2019 annual origination targets.

During the year, we introduced our new unitranche product which, sitting alongside our growth capital product, provides diversification to our offering and recognises the need for flexible funding for fast growth SMEs. Having spent a lot of time listening to key intermediaries and investors to accurately understand market conditions we are confident that we can now focus on growing our share in this specialist space.

Development finance

Throughout the year, our development finance business has continued to build on the momentum of prior years, providing secured senior financing for the development of residential and mixed-use property assets. The business has started to see the benefits of our investment in sales force and brand positioning, exceeding the £0.5 billion of committed facilities mark for the first time.

Outlook

Market conditions during 2019 were characterised by economic and political uncertainty which weighed on the confidence levels of UK SMEs and the residential property sector, however our focus on delivering a high-quality service in specialist markets enabled growth in our originations, loan book and profits. Having further positioned our business for growth through the divestment of sub-scale activities and organising our market proposition into clear product lines, we move into 2020 with a focus on modernising our proposition through the deployment of technology to improve our customer experience and operating efficiencies.

In light of the Covid-19 outbreak we also continue to explore how to adapt our business model to support our customers as we navigate through this difficult and unprecedented time.

Shawbrook Bank makes history with income streaming app Wagestream

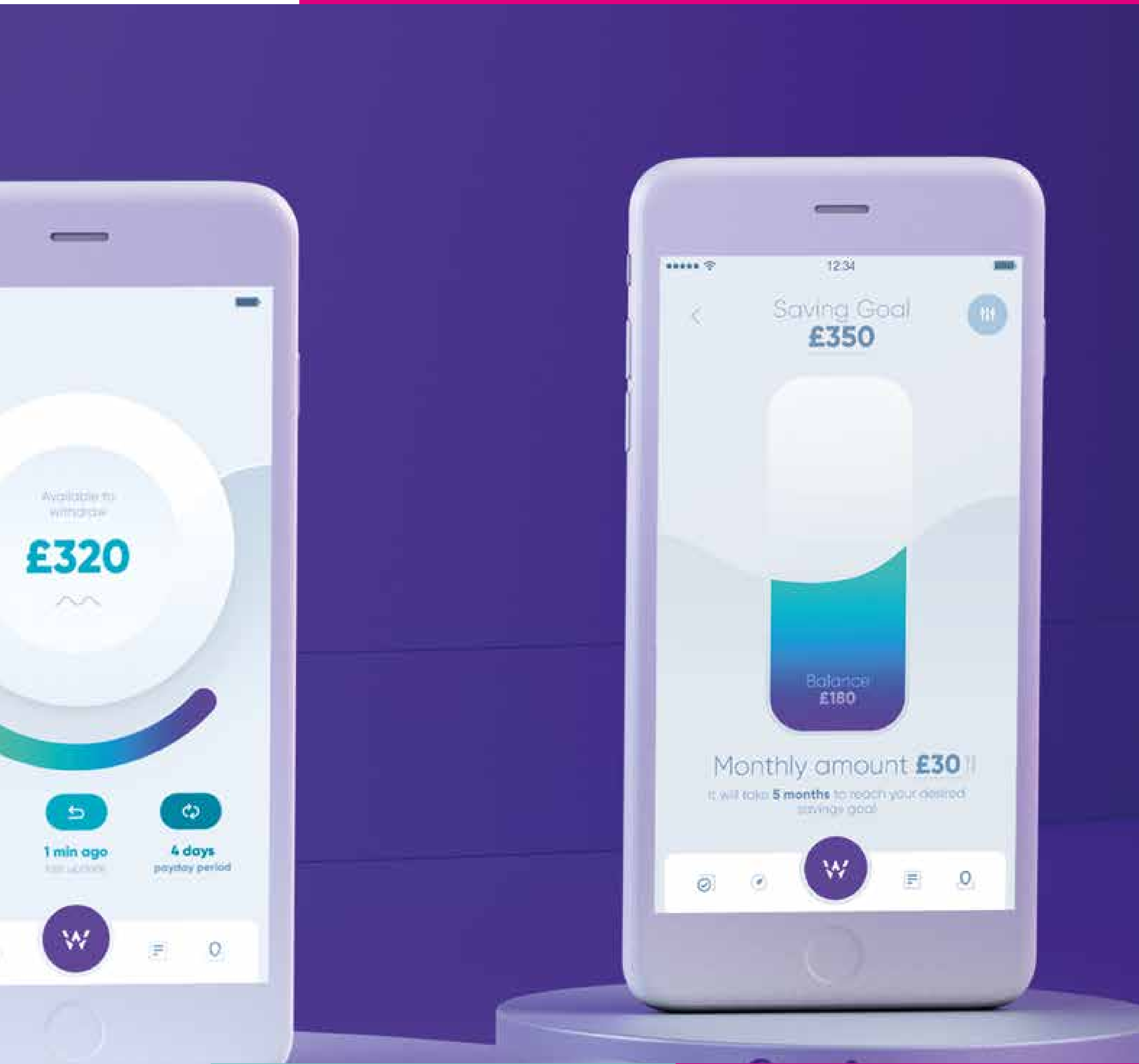
Case study

Shawbrook Bank provides a wholesale funding facility of up to £25 million to support the rapid growth of Wagestream's income streaming platform. The funding line from Shawbrook adds to the £40 million Series A investment funding raised by Wagestream from lead investors QED, Balderton and Northzone. The funding total from Shawbrook and other finance providers means that Wagestream has attracted the largest pool of social impact investment in UK history.

Wagestream is on a mission to bring better financial health to employees across the globe. By putting workplace data into the hands of workers, Wagestream's financial wellness software allows employees to track, budget, save and stream their earnings, all in real time. Wagestream unlocks the constraints of the monthly pay cycle and eradicates the debt issues and financial stress many workers face between pay day. Wagestream are now working with over 110 brands, including Bupa, Rentokil, David Lloyd Gyms and The NHS with 210,000 employees on the platform.

The focus that Wagestream have on improving consumer financial wellbeing was a key factor in why Shawbrook were keen to support the firm. With considerable expertise in structuring wholesale funding facilities, combined with their knowledge of venture debt and fast growth businesses, Shawbrook was the go-to specialist bank for the Wagestream team.

WAGESTREAM



"We're excited to rapidly grow our business, and with the funding from Shawbrook, we can do just that. The expertise of the team and the flexible structure the team proposed really demonstrated that they knew our business well, meaning they can deliver exactly what we need, right when we need it."

Peter Briffett, Chief Executive Officer and Co-Founder at Wagestream

"Shawbrook is delighted to collaborate with Wagestream to structure this specialised wholesale facility, and we are excited at the opportunity to support the growth of such an innovative business."

Jake Francis, Associate Director, Structured Finance at Shawbrook Bank

Business review
Consumer Lending

Activity
The Consumer Lending division focuses on two key product areas, building on our approach to transparency and fairness for customers:

- **Personal loans:** provides unsecured loans to personal customers, across a number of key partners, via our digital real-rate pre-approval journey.
- **Partner finance:** provides unsecured loans to consumers through strategic partnerships, funding specific purchases across a range of home improvements and timeshare holidays.

Personal loans
Our personal loans proposition is deployed through a digital pre-approved loan platform, developed organically by the business in 2018 to enhance our decisioning capability. During 2019, we continued to build on the foundations laid and made additional enhancements to our bespoke application scorecard. This enabled the ongoing optimisation of both risk and pricing strategies, driving improved early arrears performance and strengthening front-book yields. We further strengthened our distribution capabilities, improving our integration process and enhancing customer journeys through providing quicker loan decisions and smoother data collection.

The year also saw us launch a proof of concept, using open banking data within our loan decisioning, via our direct to consumer offering on the Shawbrook website. We are working with Account Score to provide the data to us and we will work to understand how this new customer data can help us to improve our lending decisions and the customer journey.

We continue to have excellent coverage of our real-rate proposition across all key digital marketplaces, such as ClearScore, MoneySuperMarket, Compare the Market and Totally-Money. Meanwhile, there was notable success for our team as we received several industry award nominations, picking up the 'MoneyComms Award for Best Personal Loans Provider 2019' and 'Feefo's Gold Trusted Service Award 2019'.

Partner finance
Our focus for the partner finance business during the year was to simplify and streamline our approach, as we faced a challenging regulatory and competitive environment. We successfully exited the point-of-sale retail finance market, concluding relationships with c.3,000 individual retailers, with minimal operational losses. In addition, we made the decision to fully exit the solar market and remove the buy-now-pay-later product from front-book sales, allowing us to focus on core home improvement and timeshare holiday markets, while maintaining strong relationships with key partners.

Case study

TotallyMoney

"We've worked with the Personal Loans team at Shawbrook for over two years. Since then, we've created and developed opportunities with Shawbrook to help TotallyMoney customers move on up to a better financial future and prevent them paying more than they need to when they borrow. We've combined our expertise to provide the right kinds of products, to the right customers, at the right time.

When we began working with Shawbrook Personal Loans, they were one of the first in the market to offer a rate for risk personal loan, based on an individual's credit profile, by using a direct integration. Not only has this been invaluable for TotallyMoney in terms of showing customers whether they're pre-approved, it has also helped reshape the market, something we're very passionate about. Now, more lenders promote the value of transparency in their propositions, creating better long-term value for customers and lenders alike."

Qin Su, Head of Cards and Loans, TotallyMoney

Outlook

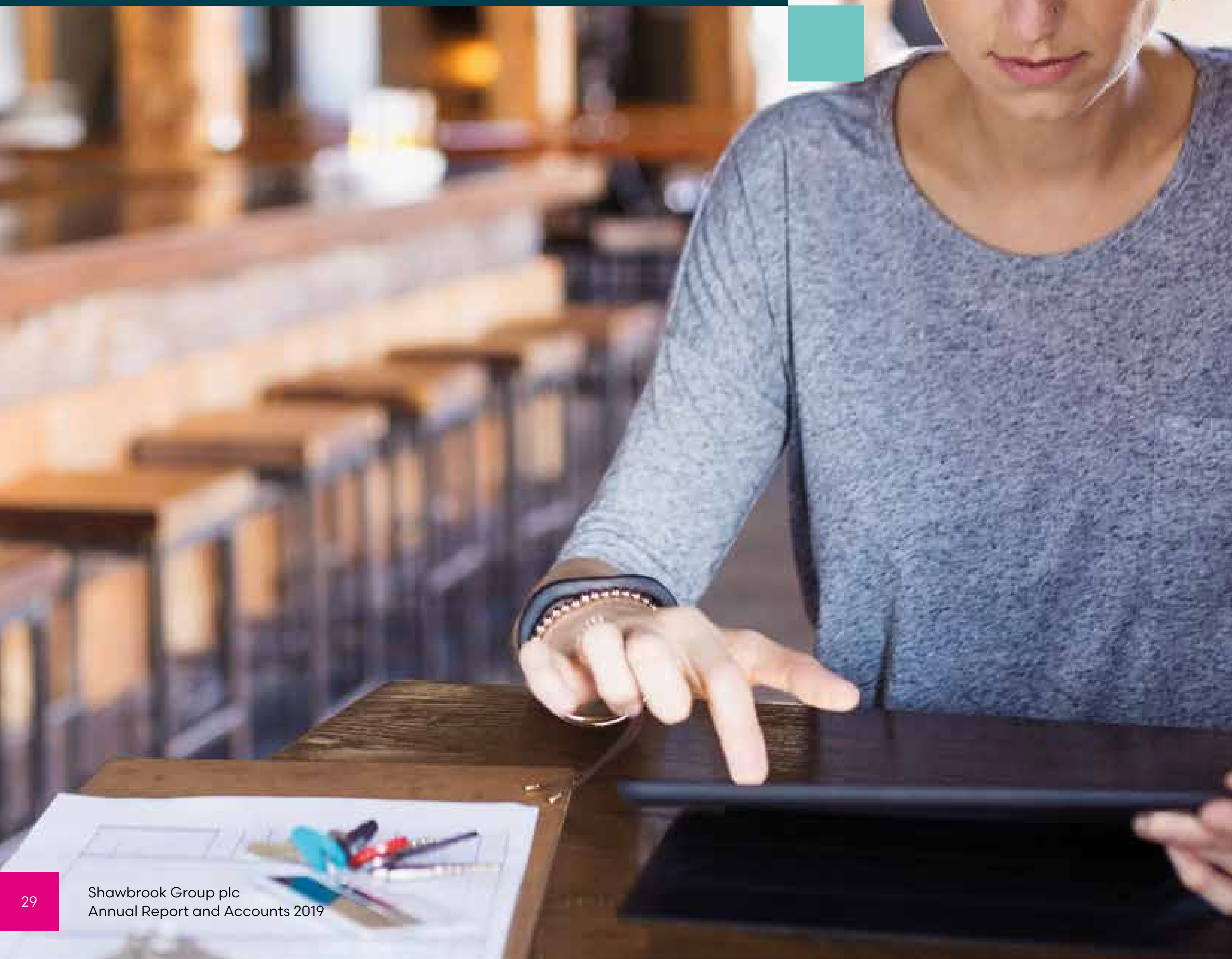
Looking forward, focus will be on safe and sustainable growth through a continued approach of optimising our risk and pricing strategies, supported by investment in people, data and a technology capability. We will also continue to seek out new distribution opportunities within the markets we operate in, both in terms of marketplaces and strategic partnerships.

Business review
Savings and Central

Savings activity

Our Savings business offers a wide range of personal and business savings products, underpinned by consistently strong rates and customer service. Our proposition is split into the following two product areas:

- **Personal savings:** provides a range of savings products to personal customers, including Easy Access, Notice, Fixed Term Bonds and both Easy Access and Fixed Term Cash ISAs.
- **Business savings:** provides a range of savings products for SMEs, including Easy Access, Notice and Fixed Term Bonds.



Personal savings

The business saw continued, sustainable growth in its personal savings deposits throughout the year which resulted in us ending 2019 with a deposit book of over £6 billion. This deposit book will serve to support the continued progressive growth of our specialist lending book.

During the year, we extended our partner distribution through the introduction of new relationships with cash management platforms Insignis and Octopus and the online bank, Monzo. All three organisations come with customer focused propositions complementing Shawbrook's direct offering. Partnerships, particularly in this form, will provide the business with exciting opportunities going forward as we continue to deepen and extend our market presence.

Business savings

In 2019, we took the opportunity to upgrade our banking platform, which allowed us to digitise our SME savings proposition with a suite of new products, enabling limited companies, partnerships and sole traders to apply for our products online.

Following the platform refresh we successfully launched our revamped SME savings proposition. This was supported by the publication of our SME Savings Monitor in conjunction with the Centre for Economics and Business Research, which showed increasing demand for more accessible business savings products.

Outlook

In 2020, the business will continue to make incremental changes to its proposition, increasing the use of digitalisation and automation to empower customers, improve customer experience and bolster operational capacity. Serving the needs of SME and personal customers through a straightforward, value driven proposition, our ambition is to be recognised as a 'go-to' savings provider in the market which in turn will be used to support our lending customer's growth ambitions through the provision of specialist financing facilities.

Case study

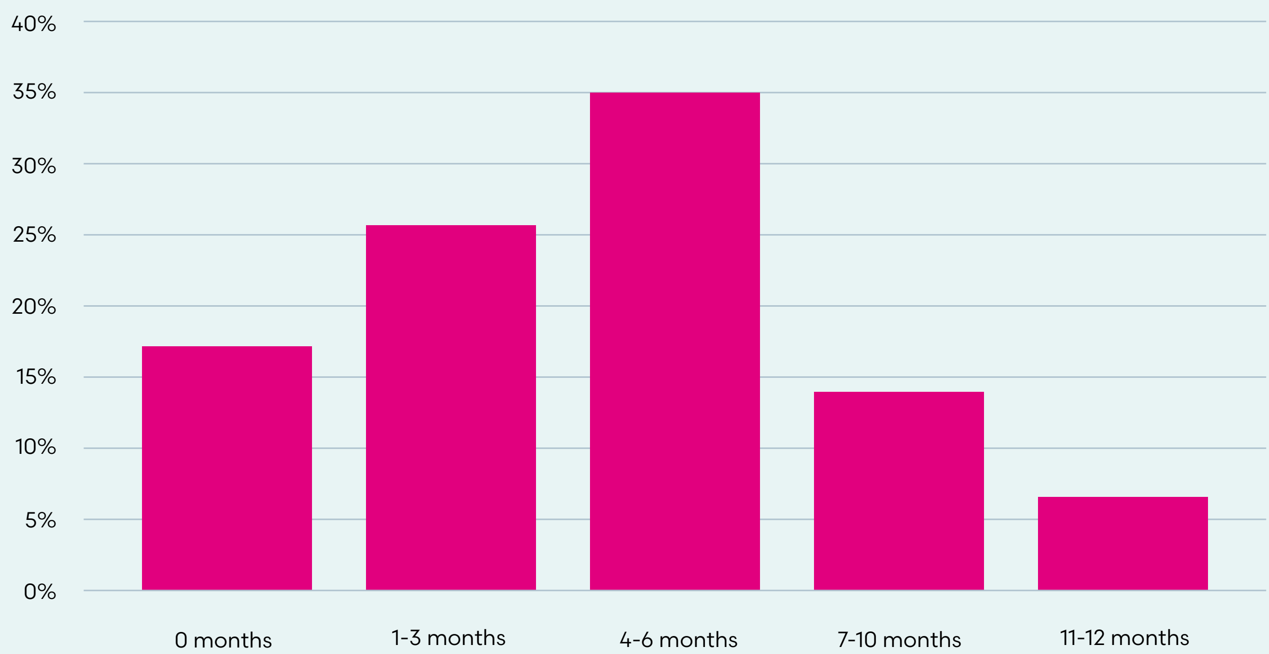
UK economy missing out on vital boost as SMEs stockpile £86 billion of 'dormant cash' in lower or zero-interest accounts

The amount of money SMEs are keeping in accounts paying little or no interest is indicative of the cautious nature of many firms in the current economic and political climate. Whilst, of course, it is prudent for firms to keep some cash within easy reach to cover the daily costs of running a business, having too much money that is earning next to no interest can have an adverse impact on finances.

"Small and medium-sized businesses are the backbone of UK plc and the savings industry needs to provide greater incentives to those firms to maximise the interest they receive on their cash reserves. Quicker access to better paying accounts, more innovative and flexible products and improved mobile and online services are just some of the ways providers can help tackle inertia in the market and encourage greater engagement from SMEs."

Julian Hynd, Chief Operating Officer

Number of months in the past year where SMEs have had a cash surplus



Source: 3Gem research, Cebr analysis

Only around one in five (21%) survey respondents said that their business' monthly revenue exceeded its monthly operating expenditures in more than 6 out of the past 12 months. Meanwhile, 35% reported that their business had a surplus of cash during 4 – 6 of the past 12 months, and a further 26% said that they ran a surplus during just 1 – 3 of the past 12 months. The volatility of many SMEs' cash flows underlines the importance of building a cash buffer and maximising the associated opportunities to generate a stream of interest income.

Central functions activity

The Group's central functions include our treasury operations as well as common costs which are not directly attributable to the operating segments. Central function costs include, amongst other things, finance, IT, marketing, legal, risk and human resources.

During the year, the Group's IT function received substantial investment to support the upgrade of key business platforms to enhance online productivity and security, contributing to more efficient and streamlined processes. In support of this, the Group also reviewed and enhanced its approach to operational resiliency and as a result, established a new team within the central business services division, to manage and improve our operational resiliency across the business.

The business also continued to invest in headcount throughout the year, to not only improve capacity and capability across the business, but also encourage a more inclusive and diverse workplace. As a result of these investments, the Group's administrative expenses naturally increased during 2019.

Wholesale funding

As the Group's loan book continues to grow, it is important that we diversify our funding channels. So, whilst our funding strategy continues to be principally deposit-led through our specialist savings franchise, in 2019 we continued to add further wholesale funding capabilities. As an example, in June 2019, we successfully completed our first securitisation, utilising the excellent credit quality of our buy-to-let business to complete our first public residential mortgage backed securitisation. In addition to providing cost efficient diversification to our funding model, the positive investor response received demonstrates the continued market confidence in Shawbrook as the Group continues to grow.

Corporate Responsibility Report

At Shawbrook, operating as a responsible business is important to us, so we make sure we continue to act with integrity and adhere to high ethical standards. We understand that in order to deliver truly sustainable returns, continuous consideration of our social, environmental and governance impacts must be embedded into our day to day business activity.

Our approach to Corporate Responsibility is split between the following four key stakeholder segments:

Environment	Community	Marketplace	Workplace

Our environment

We understand embedding sustainability in all aspects of our business model is the right thing to do and are committed to creating a strong business that is not achieved at the expense of our environment. Whether it be our carbon footprint, our waste and energy consumption or the way we do business, Shawbrook strives to entrench sustainability across all aspects of our business operations.

Climate Change Plan

The UK financial services industry has a crucial role to play in tackling climate change, which has the potential to directly impact our product offering and customers' behaviour, desire to invest, finance and, ultimately, their ability to repay.

In this context, and in response to the supervisory statement introduced by the PRA, which laid out the regulator's expectations for firms, during the year our Board and Executive team established a Climate Change Working Group. In October 2019, following Board approval, we submitted our plan to the PRA focusing on the development of the bank wide climate change strategy, risk appetite and management and governance arrangements to ensure appropriate decision-making, and disclosures. Recognising the impact of climate change stretches far wider than the financial risks outlined in the plan, the Climate Change Working Group will continue to consider other initiatives to help reduce Shawbrook's impact on the environment.

Energy Savings Opportunity Scheme
Over the past 12 months we have been looking at ways to reduce our energy consumption. During the year, we submitted phase two of the Energy Savings Opportunity Scheme assessment. The findings revealed that since completing phase one in 2015, our head office electricity consumption decreased significantly. This drove several energy saving opportunities to be identified and in 2020 we will formulate an actionable plan to introduce more sustainable elements across our new offices.

Emissions
During 2019, our head office experienced a 21% decrease in kilowatts per hour (kWh) despite employee headcount increasing, improving our employee to kWh ratio. Our second largest office in Redhill also performed exceptionally well during the year compared to industry benchmarks and following the consolidation of our two legacy offices to one central Redhill hub a 49% reduction in kwh was revealed. In total, Shawbrook experienced a 21% decrease across our combined estate.

Sustainable lending
Across all of our product propositions sustainability is a key consideration and we strive to ensure our actions will provide a lasting benefit for both our customers and the wider community.

Our specialist agriculture and renewable energy product propositions provide us with the opportunity to not only support the UK's farming industry with finance solutions, but also support the reduction of carbon emissions through investment in renewable technologies. In 2019, Shawbrook provided financing to green energy provider Olympus Power Ltd, to complete one of the largest commercial solar installations in the UK and all without any Feed-in Tariff funding.

The energy generated from this installation will be in excess of

500,000 kWh

every single year,

in layman's terms this is enough energy to power around **135 average households for a year**

and has the carbon off set equivalent to planting **832 football fields worth of trees**.

The carbon dioxide equivalent is 390 tonnes which is around the weight of **1.5 full-grown blue whales**.

This is all just over a single year of use!

Our community

Dedication to our community is embedded in our core values, so we recognise the importance of investing time and support into the communities we touch so we can continue to make a difference.

Banking and business community
Through our active involvement with industry bodies, we class ourselves a responsible member of the banking and businesses community. This provides Shawbrook with the opportunity to collaborate with other members on industry initiatives and remain informed with relevant policy updates.

Financial education
We believe educating our community about the financial services industry is an important way to encourage change and bolster interest in our space. In 2019, we actively promoted the benefits of a career in financial services in our local communities through attendance at career fairs and providing work experience opportunities to those who might not traditionally get the opportunity to do so.

"Fiona gave us emotional support during the hardest time of our lives. We had no certainty the girls would make it, and this support made the world of difference to us. The magnitude of difficulty and the overwhelming rollercoaster that comes with having two sick children is unimaginably hard. We are eternally grateful to the Rainbow Trust for helping us get through."

Elle-Mae, mother of premature twins Bella and Ruby, born 14 weeks early.

Employee fundraising
We are proud of the significant charity and community work that continued to take place across the Group in 2019. The growth of our employee-led charity committee encouraged even broader involvement, resulting in an increase in employee fundraising activities, with donations being awarded to 43 worthy causes. Employee charity activity ranged from staff football matches, quiz nights and cake sales to running marathons and completing a 192 mile bike ride. Solely through Shawbrook's gift matching benefit scheme, which in most cases resulted in Shawbrook replicating the amount raised by our employees, Shawbrook donated a total of £36,000.

Make a difference days
As a way of encouraging Shawbrook employees to engaged with our local communities, we offer each staff one paid working day to be put to good use and make a difference. In 2019, we are proud to say employee volunteer days utilised increased. Our healthcare finance team set a great example of doing their bit by helping a local care home renovate its garden, whilst also seeing first-hand how the kind of facilities the team typically finance improve residents' lives.

Charitable donations
Every year we ask all Shawbrook employees to nominate their favoured charities, providing an opportunity to support those close to their hearts. Due to popular employee demand, in June 2019 we picked our top two national charities to sponsor throughout the year - Mind and the Rainbow Trust. Our £10,000 donation to the Rainbow Trust in 2019 will provide support to five families throughout 2020, providing emotional and practical support whenever, wherever and however it is needed, through treatment and beyond.

Our marketplace

At Shawbrook, we strive to achieve mutually advantageous supplier relationships, built on common values and expectations. It is the commitment to conduct business in a responsible and sustainable manner that underpins our engagement with third party suppliers, only working with those that resonate with our values.

Supplier performance

The growth of our third-party network has driven us to actively improve internal controls regarding how we source, onboard and manage supplier relationships. Continuously improving our policies, we introduced our new Group procurement and supplier performance management policy setting out how we will operationally and economically effectively manage and monitor our third party suppliers, whilst adhering to regulatory requirements, including the new European Banking Authority third party governance guidelines.

Human rights and Modern Slavery Act

Shawbrook has zero-tolerance to any modern slavery and by having the correct tools and regularly reviewing our policies, we can ensure that any occurrences are swiftly addressed.

In 2019, we continued to take the appropriate steps to prevent slavery and human trafficking from both our business and supply chain through a database utilised to monitor Modern Slavery Act compliance. This built upon our established outsourcing policy which ensures that there is a framework which is followed to efficiently manage potential and contracted third party relationships and comply with regulatory obligations. A full copy of our modern slavery statement can be viewed on our company website.

Our workplace

We are committed to remaining a great place to work, where all colleagues feel respected, engaged and supported to be their best selves. Our people really matter so we work hard to ensure this ethos is translated into the Shawbrook culture. We pride ourselves on creating an environment where talent is rewarded, employees are supported, and we all feel included.

Diversity and inclusion (D&I)
In 2019, Shawbrook's inclusion network was introduced to encourage an inclusive culture. Now, with over 130 members, ideas, experiences and opinions are regularly shared across the business. This also drove us to host several inclusion events across our sites, offering all colleagues the opportunity to hear first-hand from some of our D&I advocates and senior leaders about their approach to D&I in both their professional and personal lives. We have built an extensive calendar of internal events that will continue into 2020.

Mentoring our stars of the future
In addition to our structured management development programmes, 2019 saw the launch of our first Group wide employee mentoring programme, aimed at encouraging some of our existing leaders to provide support and guidance to their colleagues from across the business. Whilst we hope this will help grow our female leadership, we intentionally opened this initiative up to all as we recognise the important role mentoring can play for everyone.

"As a first-time mentee, the experience to date has been even better than expected! The mentor I have been matched with is someone I would have never approached myself but is a perfect fit and in the short space of time I have been meeting with him, I have been given the extra confidence that I needed to develop my career."

Becca Shawyer, Shawbrook Mentee

Employee engagement
We understand that listening to our employees is key in order to retain, motivate and make Shawbrook an employer of choice. In this regard, in 2019, we launched two employee surveys to help us determine which factors drive our employees to perform at their best. During our last survey conducted in 2019, we received 85% employee participation, our best response rate to date.

Recognising our talent
We are keen to embed a culture of continuous recognition to ensure all employees feel their efforts and contributions do not go un-noticed. Following the success of our annual *Proudly Shawbrook* Awards, designed to highlight and celebrate the successes of our colleagues, in 2019 we introduced the online Proudly Different recognition tool. Making it easier to say thank you on a regular basis, the tool acknowledges those living our values and allows a simple 'thank you' to small acts of kindness.

Health and wellbeing
We want all Shawbrook employees to be the best they can be and feel comfortable at work. With that in mind, in 2019, we launched a series of mental health awareness workshops to all Shawbrook employees, in a bid to raise awareness and support colleagues who may need support with their physical and mental wellbeing. As a result, we introduced several certified mental health first aiders to the business, to provide confidential support to those that may need it and promote the recovery of good health.

The Strategic Report was approved by the Board and signed on its behalf by the Chief Executive Officer.

Ian Cowie
Chief Executive Officer

Corporate Governance

Corporate Governance.

Chairman's introduction

On behalf of the Board, I am pleased to present the Corporate Governance Report for the year ended 31 December 2019.

Our commitment to good corporate governance

The Board recognises that high standards of governance and effective Board oversight are vital to a successful organisation. This report explains how the Board has dealt with ensuring that we have effective corporate governance in place to help support the creation of long-term sustainable value for our Shareholders and wider stakeholders.

Board meetings and activity

In 2019, the Board considered several key areas. These areas can broadly be categorised into the following themes: strategy and execution, financial performance, risk management, and corporate governance. Further details about these themes can be found on page 50 of this report.

The Board's Committees also continued to play an important role in the governance and oversight of the Group by ensuring adherence to strong governance practice and principles. This section contains a report from the Board's principal Committees, which sets out their approach and considerations.

Effectiveness and evaluation

During 2019, one of my priorities was to ensure that the Board was effective and possessed the right balance of skills and expertise.

When I joined the Board in 2018, I commissioned a Board effectiveness review to be undertaken by an independent consultant, Egon Zehnder. This review was completed in 2018 and in 2019 Egon Zehnder was commissioned to undertake a further review to assess the progress made against the actions from the 2018 review. Further details of this review can be found on page 45 of this report.

Succession planning and Board changes

Following the departures of Sally-Ann Hibberd, David Gagie and Roger Lovering in 2019, and taking into consideration the results of Egon Zehnder's 2019 review, the Board launched a search for a new Independent Non-Executive Director.

The Nomination Committee, with the support of Ridgeway Partners, conducted a thorough interview and assessment programme, which is described in more detail on page 75, culminating in its recommendation to the Board that Michele Turmore be appointed. Michele joined the Board and became a member of the Audit and Risk Committees on 1 October 2019. Further information about Michele's appointment and induction can be found on page 76.

The Nomination Committee reviews succession plans for the Board, Executive and Senior Management each year. The Board has female representation of 22% and the Board remains committed to continuing to be a member of the Women in Finance Charter. Further information on our approach to diversity, succession planning and Board appointments can be found on pages 75 to 76.

Culture and values

The Board recognises the importance of its role in setting the tone of Shawbrook's culture and embedding it throughout the Group. The Board aims to create an open and collaborative culture that encourages the Group to make decisions that are best for our Shareholders, whilst having regard to the interest of our wider stakeholders. The values set by the Board are central to the Group's culture and contribute to its objectives of long-term sustainable success and Shareholder value.

Looking forward

Our corporate governance priorities for the year ahead will be to reflect and further embed the learnings from the 2018 and 2019 effectiveness reviews, resulting in the continued strengthening of the governance framework across the Group.

John Callender
Chairman

16 April 2020

Board of Directors

A Audit Committee

N Nomination Committee

R Remuneration Committee

RI Risk Committee

Committee Chair

John Callender
Chairman

N R

Appointed to the Board in March 2018.

Skills and experience
John was appointed to the Board as Chairman in March 2018. John brings extensive financial services experience to the Board, gained through both his Executive and Non-Executive careers. John has previously served as Non-Executive Director of Aldermore Group plc, Non-Executive Director of Motability Operations plc and Non-Executive Chair of ANZ Bank Europe Ltd for a 10-year term retiring in 2019. John also sat on the Regulatory Decisions Committee for the FCA for 6 years finishing his two statutory terms in January.

External appointments
John is currently a Senior Independent Director and Chair of the Risk Committee of FCE Bank plc, Director of Inglewood Amenity Management Company Limited and Director of Camberley Heath Limited.

Ian Cowie
Chief Executive Officer

Appointed to the Board in February 2019.

Skills and experience
Ian joined Shawbrook in April 2017, initially leading the Business Finance division. Ian was appointed permanent Chief Executive Officer in February 2019 having served as Interim Chief Executive Officer from July 2018. Ian has a wealth of SME banking experience, after leading the largest business banking franchise in the UK via a number of senior roles at RBS. These included: Chief Executive Officer Business and Commercial Banking, Chairman of SME Banking at NatWest and Director of Lombard Asset Finance and RBS Invoice Finance.

External appointments
None.

Dylan Minto
Chief Financial Officer

Appointed to the Board in February 2017.

Skills and experience
Dylan joined Shawbrook in 2013 from KPMG where he spent 11 years in their Financial Services practice advising large UK and European banks. Dylan was appointed permanent Chief Financial Officer in February 2017 having been Interim Chief Financial Officer from June 2016. He is a Fellow of the ICAEW and holds a dual BA Honours degree in German and Business Studies from Sheffield University.

External appointments
None.

Robin Ashton
Senior Independent Director

A N R RI

Appointed to the Board in March 2015.

Skills and experience
Robin has comprehensive experience of retail financial services both in the UK and internationally. He is a chartered accountant and holds a Bachelor of Arts (Hons) degree in Economics and Law from Durham University.

External appointments
Robin is a Non-Executive Director of Domestic & General Limited.

Andrew Didham
Independent Non-Executive Director

A R RI

Appointed to the Board in February 2017.

Skills and experience
Andrew has extensive financial services experience. He is a qualified accountant, having enjoyed a successful career at KPMG, becoming a partner in 1990, and subsequently as Group Finance Director of the international Rothschild investment banking group.

External appointments
Andrew is currently Executive Vice-Chairman for Rothschild, a Non-Executive Director of Charles Stanley Group plc and is also Non-Executive Chairman of its principal operating company Charles Stanley & Co Limited. He is also Non-Executive Director of IG Group Holdings plc.

Paul Lawrence
Independent Non-Executive Director

A N R RI

Appointed to the Board in August 2015.

Skills and experience
Paul has considerable experience in financial services having had a successful career within HSBC Group. Paul has particular strengths in managing risk and internal audit across a number of business lines and previously served as a member on the IIA Committee for Internal Audit Guidance for Financial Services.

External appointments
Paul is currently an Independent Director of HSBC Bank Oman and Chairman of Uley Community Stores Limited.

Michele Turmore
Independent Non-Executive Director

A RI

Appointed to the Board in October 2019.

Skills and experience
Michele has comprehensive experience in operations, transformation, IT and distribution leadership, with focus on the customer. She has operated across blue chip, mid-scale and start-up entities, including Private Equity backed banks. Most recently Michele held the position of Chief Operating Officer at Allica Limited.

External appointments
Michele is currently a Director of Ambant Limited, Ambant Underwriting Services Limited and KMT Management Limited (in voluntary liquidation).

Lindsey McMurray
Institutional Director

A N R RI

Appointed to the Board in April 2010.

Skills and experience
Lindsey has over 20 years of experience as a private equity investor with a particular focus on the financial services sector. She holds a first class honours degree in Accounting and Finance from Strathclyde University.

External appointments
Lindsey is managing partner of private equity fund manager Pollen Street Capital, an affiliate of Marlin Bidco Limited of which she is also a Director. She is also currently an Executive Director of Pollen Street Capital Limited and a Director of 1st Stop Group Limited, 1st Stop Funding Limited, Cashflows Europe Limited, Freedom Acquisitions Limited, Honeycomb Holdings Limited, Honeycomb Finance Limited and Kingswood Holdings Limited.

Cédric Dubourdieu
Institutional Director

A N R RI

Appointed to the Board in September 2017.

Skills and experience
Cédric has close to 20 years of private equity experience, having led a number of investments in a variety of sectors across Europe. He holds a degree from Ecole Polytechnique, Paris.

External appointments
Cédric is a Partner of private equity firm BC Partners and sits on BC Partners' investment committee. BC Partners is an affiliate of Marlin Bidco Limited of which Cédric is also a Director. Cédric is also a board member of iQera, the French leader of credit management services .

Daniel Rushbrook
General Counsel and Company Secretary

Appointed Company Secretary to the Board in March 2015.

Skills and experience
Daniel has over 25 years of legal experience. He has experience in private practice having worked for both Linklaters LLP and Macfarlanes LLP. Daniel became the first in-house lawyer for Commercial First Mortgages Limited, later joining its Board as Legal Director in 2005. In 2011 Daniel transferred to Shawbrook becoming General Counsel and Company Secretary. Daniel holds a first-class law degree from Oxford University and a Masters law degree from the University of Pennsylvania.

External appointments
None.

Resignations

Roger Lovering resigned as a Director on 31st August 2019

David Gagie and Sally-Ann Hibberd both resigned as Directors on 31st January 2019

Corporate Governance Report

This report explains the Board's role and activities, and how corporate governance operates throughout the Group.

The UK Corporate Governance Code

During the financial year ended 31 December 2019 the Company has given due consideration to the spirit of the UK Corporate Governance Code 2018 (the 'Code') published in July 2019 by the Financial Reporting Council.

Where required, sections of the Financial Conduct Authority's (FCA) Disclosure and Transparency Rules have been applied in line with obligations in relation to the Group's Listed Debt.

The Board

The Board takes account of the views of the Company's Shareholder and has regard to wider stakeholder interests and other relevant matters in its discussions and decision-making. The Board recognises that stakeholders' interests are integral to the promotion of the Company's long-term success. Further information about how the Board considers the interests of its stakeholders can be found on page 15.

A Framework Agreement is in place with Marlin Bidco Limited (the 'Shareholder') which includes a formal schedule of matters reserved for the Board and those matters which require recommendation to the Shareholder for approval. This document is supported by a Memorandum of Understanding, which preserves the Board's independence when making significant decisions. The Board delegates specific powers for some matters to Board Committees, with the outputs from each Committee meeting reported to the Board regularly, thus ensuring the Board maintains the necessary oversight. More detail on the committees and their work is described in the separate committee reports on pages 55 to 76.

Composition, Board balance and time commitment

The Board currently consists of nine members, namely the Chairman, four Independent Non-Executive Directors, two Executive Directors and two Institutional Directors. Biographical details of all Directors are on pages 41 to 42.

The Independent Non-Executive Directors have substantial experience across all aspects of banking, including relevant skills in financial management, regulatory matters, credit assessment and pricing, liability management, technology, operational and conduct matters. The Independent Non-Executive Directors are considered to be of sufficient calibre and experience to bring significant influence to bear on the decision-making process.

The Board considers that the balance of skills and experience is appropriate to the requirements of the Group's business and that the balance between Executive and Independent Non-Executive Directors allows it to exercise objectivity in decision-making and proper control. Each member of the Board has had access to all information relating to the Group, the advice and services of the Company Secretary (who is responsible for ensuring that governance procedures are followed) and, as required, external advice at the expense of the Group.

The Board with the assistance of the Nomination Committee keeps under review the structure, size and composition of the Board (and undertakes regular evaluations to ensure it retains an appropriate balance of skills, knowledge and experience). The membership of the various Board Committees and the expected time commitment of the Directors is closely monitored.

The terms of appointment of the Independent Non-Executive Directors specify the amount of time they are expected to devote to the Group's business. They are currently required to commit at least four days per month which is calculated based on the time required to prepare for and attend Board and Committee meetings, meetings with the Shareholder and with Management and training.

Meetings and attendance

The Board holds joint meetings of Shawbrook Group plc and Shawbrook Bank Limited at regular intervals, at which standing items such as the Group's financial and business performance, risk, compliance, human resources and strategic matters are reviewed and discussed. There is a comprehensive Board pack and agenda which is circulated beforehand so that Directors have the opportunity to consider the issues to be discussed. Detailed minutes and any actions arising out of discussions are documented.

The Board and Board Committees held a number of scheduled meetings in 2019 at which senior executives, external advisors and independent advisors were invited, as required, to attend and present on business developments and governance matters. The Company Secretary and/or his deputy attended all Board meetings and he, or his nominated deputy, attended all Board Committee meetings. The table below sets out the attendance at scheduled meetings in 2019. Additional Board and Committee meetings were convened during the year to discuss ad hoc business development, governance, and regulatory matters.

Number of scheduled meetings attended*					
	Board	**Audit Committee**	**Risk Committee**	**Remuneration Committee**	**Nomination Committee**
John Callender (Chair)	8/8			5/5	5/5
Ian Cowie	8/8				
Dylan Minto	8/8				
Robin Ashton(1)	7/8	5/6	4/5	5/5	5/5
Lindsey McMurray(2)	8/8	6/6	5/5	4/5	5/5
Cedric Dubourdieu(3)	8/8	6/6	5/5	5/5	4/5
Paul Lawrence	8/8	6/6	5/5	5/5	5/5
Andrew Didham(4)	8/8	6/6	5/5	2/4	
Michele Turmore(5)	2/2	2/2	2/2		
David Gagie(6)		1/1			
Sally-Ann Hibberd(7)				1/1	
Roger Lovering(8)	4/6	3/3	2/3		

The attendance above reflects the number of scheduled Board and Committee meetings held during the financial year. During the year there were also a number of ad-hoc Board and Committee meetings to deal with matters arising outside of the usual meeting schedule. The majority of Directors made themselves available at short notice for these meetings.

Notes

* Meetings were held from January 2019 to December 2019

(1) Due to a family bereavement, Robin Ashton was unable to attend the Board meeting on the 19 March, and due to illness, the Audit and Risk Committee meetings held on the 16 November 2019.

(2) Due to a prior commitment, Lindsey McMurray was unable to attend the 8 October 2019 Remuneration Committee meeting.

(3) Due to a prior commitment, Cedric Dubourdieu was unable to attend the 23 January 2019 Nomination Committee meeting.

(4) Andrew Didham was appointed to the Remuneration Committee on the 1 February 2019. Due to prior commitments, Andrew was unable to attend the 28 February and 13 May 2019 Remuneration Committee meetings.

(5) Michele Turmore was appointed to the Group on the 1 October 2019.

(6) David Gagie stepped down on the 31 January 2019.

(7) Sally-Ann Hibberd stepped down on the 31 January 2019.

(8) Due to prior commitments, Roger Lovering was unable to attend the Board meeting on 1 April and 7 May 2019 and the 23 January 2019 Risk Committee meeting. Roger stepped down on the 31 August 2019.

Corporate Governance Report

Board effectiveness review

2018	2019	2020
Externally facilitated evaluation conducted by Egon Zehnder	Externally facilitated evaluation conducted by Egon Zehnder	Internal evaluation

In 2018, independent consultants Egon Zehnder were appointed following a tender process to conduct an evaluation of the effectiveness of the Board. In 2019, Egon Zehnder were commissioned to undertake a further review to assess the progress made against the actions from the 2018 review.

Evaluation process

I Phase I (background and familiarisation)

A briefing meeting was held with the Chairman on the scope and approach of the evaluation. A questionnaire was then circulated to Board members and the Executive team.

II Phase II (formal interviews and board observation)

One-to-one meetings were held with each member of the Board, key members of the Executive team and the Prudential Regulation Authority. Egon Zehnder also attended and observed a full Board meeting to further understand the dynamics of the Board.

III Phase III (feedback and reflection)

Draft findings of the evaluation were shared with the Chairman and a final Board evaluation report was prepared and shared with the Board.

Board effectiveness results 2019

The conclusion of the 2019 Board evaluation was that the Board operated effectively throughout the year. Directors and the Executive Management team had engaged fully with the evaluation and commented positively in relation to many aspects of the Board's operations. Since the 2018 evaluation the Board has undergone a significant transformation not only structurally but also operationally. Areas of significant improvement included Chairmanship and leadership, the size and composition of the Board, Board papers and agendas of meetings and enhanced boardroom dynamics.

The following were agreed as areas of focus for the Board to consider during 2020:

Board pack and presentations
Action: A review of Board meeting reporting would be undertaken, and metrics developed that more readily highlight key points for discussion and enable an improved level of preparation, questions, debate and challenge.

Board training
Action: Work will continue to strengthen the Board training programme to enhance the Board and Executive Management's understanding of market insights and views of our wider stakeholders.

Feedback and reflection
Action: The Board will spend a dedicated amount of time reviewing key projects and decisions. Time will be spent reflecting on what worked well and what areas could be strengthened in order to apply any lessons learned to future projects and decisions.

Relationship with Shareholders
Action: Time would be added to the annual Board calendar for the Independent Non-Executive Directors to meet with the Shareholders outside of the boardroom.

Structure of the Board, Board Committees and Executive Management

The diagrams on pages 46 and 49 summarise the role of the Board, its Committees and the responsibilities of the Chairman, the Senior Independent Director, the Non-Executive Directors, the CEO and the Executive Committee. The Board and Board Committees have unrestricted access to Management and external advisors to help discharge their responsibilities. The Board and Board Committees are satisfied that, in 2019, sufficient, reliable and timely information was received to enable them to perform their responsibilities effectively. Each Committee plays a vital role in helping the Board to operate efficiently and consider matters appropriately. The Board Committees terms of reference can be found on the website at: **https://www.shawbrook.co.uk/investors/.**

Board

Leadership
- The Board has clear divisions of responsibility and seeks the long-term sustainable success of the Group.

Stakeholder engagement
- The Board organises and directs the Group's affairs in a way that it believes will help the Group succeed for the benefit of its Shareholder and in consideration of the Group's wider stakeholders. More information about the Group's stakeholders is on pages 15 to 18.

Operations
- The Board supervises the Group's operations, with a view to ensuring that they are effectively managed, that effective controls and IT systems are in place, and that risks and operational resiliency are assessed and monitored appropriately.

Financial performance
- The Board sets the financial plans, annual budgets and key performance indicators and monitors the Group's results and levels of capital and liquidity against them.

Strategy
- The Board oversees the development of the Group's strategy, and monitors performance and progress against the strategic aims and objectives.

Culture
- The Board develops and promotes the collective vision of the Group's purpose, culture, values and behaviours.

Information and support
- The Board accesses assistance and advice from the Company Secretary. The Board may seek external independent professional advice at the Company's expense, if required to discharge its duties.

Board Committees

The Audit Committee
- Monitors the integrity of the Group's financial statements.
- Oversees and challenges the effectiveness of the Group's financial controls.
- Monitors the work and effectiveness of the Group's internal and external auditors.

The Risk Committee
- Provides oversight and advice to the Board in relation to current and potential future risk exposures of the Group and the future risk strategy, including determination of risk appetite and tolerance.
- Responsible for reviewing and approving various formal reporting requirements and promoting a risk awareness culture within the Group.

The Remuneration Committee
- Oversees how the Group implements its remuneration policy.
- Monitors the level and structure of remuneration arrangements for the Board, Executive and material risk takers, approves share incentive plans, and recommends them to the Board and Shareholder.

The Nomination Committee
- Reviews the Board's structure, size, composition, and balance of skills, experience, independence and knowledge of the Directors.
- Leads the process for Board appointments and Senior Management Function holder appointments and makes recommendations to the Board.
- Provides guidance to Management on executive succession planning.

Corporate Governance Report

Board and Executive Management roles

Each Director brings different skills, experience and knowledge of the Company, with the Non-Executive Directors contributing additional independent thought and judgement. There is a clear division of responsibilities between the Chairman, Chief Executive Officer and Senior Independent Director. Their roles have been clearly defined in writing and agreed by the Board. Depending on business needs, the Non-Executive Directors and the Chairman commit at least four days per month to discharge their duties effectively in accordance with their letters of appointment.

The Chairman

- Guides, develops and leads the Board, ensuring its effectiveness in all aspects of its role as well as being responsible for its governance.
- Helps to ensure effective communication and information flows with key stakeholders (such as employees, regulators and investors).
- Sets the tone for the Group and ensures effective relationships between Management, the Board and stakeholders.
- Helps to ensure effective communication and flow of information between Executive and Non-Executive Directors.
- Chairs the Board and Nomination Committee.

The Senior Independent Director

- Acts as a sounding board for the Chairman and serves as an intermediary for the other Directors when necessary.
- Is available to the Shareholder if they have any concerns, which the normal channels of Chairman, CEO or other Executive have failed to resolve, or for which such contact is appropriate.
- Leads the planning for the succession of the Chairman of Board.
- Meets with other Non-Executive Directors to appraise the Chairman's performance.
- Provides feedback to the Chairman, Shareholder and Executive Directors on the Non-Executive Directors' views.

The Non-Executive Directors

- Provide constructive challenge to Management and bring experience to the Board's discussions and decision-making.
- Monitor the delivery of the Group's strategy against the governance, risk and control framework established by the Board.
- Ensure the integrity of financial information and ensure that the financial controls and systems of risk management are effective.
- Led by the Senior Independent Director, the Non-Executive Directors are also responsible for evaluating the performance of the Chairman and Senior Management.

The CEO
As authorised by the Board, the CEO manages the Group's day-to-day operations and delivers its strategy. The CEO delegates certain elements of his authority to members of the Executive Committee to help ensure that senior executives are accountable and responsible for managing their perspective business and functional units. The CEO chairs the Executive Committee, which meets no less than three times a month.

The Executive Committee
The Executive Committee is responsible for developing the business and delivering against a Board approved strategy, putting in place effective monitoring, control mechanisms and setting out a framework for reporting to the Board.

- **Chief Operating Officer**
- **MD Business Finance**
- **Chief Financial Officer**
- **MD Consumer**
- **Chief Risk Officer**
- **MD Property Finance**
- **Chief Technology Officer**
- **Group HR Director**
- **General Counsel and Company Secretary**

Corporate Governance Report

The Executive Committee

The Board delegates daily management responsibility for the Group to the Chief Executive Officer who discharges this responsibility through the Executive Committee. The Executive Committee is responsible for developing the business and delivering against a Board approved strategy, putting in place effective monitoring, control mechanisms and setting out a framework for reporting to the Board.

There are currently ten (including the CEO) members of the Executive Committee and their biographical details can be viewed on the Group's website at **https://www.shawbrook.co.uk/investors/.**

To discharge its duties, the Executive Committee operates four executive level committees. Details of these executive level committees and their responsibilities are set out below.

Enterprise Risk Management Committee (ERMC)

Purpose
The ERMC has oversight responsibility for all operational aspects of measuring, monitoring, reporting and management of the Group's Risk Management Framework (RMF).

Frequency and membership
The ERMC meets twice a month and is chaired by the Chief Risk Officer or the Enterprise Risk Director as their alternate. Other key members are the Chief Executive Officer, Chief Financial Officer and divisional Risk Directors.

Group Product Committee (GPC)

Purpose
The GPC is responsible for all aspects of product governance including approval of new, and changes to existing, products.

Frequency and membership
The GPC meets monthly and is chaired by the Chief Operating Officer, with the other members comprising the Chief Executive Officer, Chief Risk Officer, Chief Financial Officer, General Counsel and Company Secretary, Chief Compliance Officer, Group Head of Marketing and Product Governance and the divisional Managing Directors.

Asset and Liability Committee (ALCo)

Purpose
The ALCo oversees asset, liability and other solvency risks, specifically market risk, treasury wholesale credit risk and liquidity risk.

Frequency and membership
The ALCo meets monthly and is chaired by the Chief Financial Officer, or either of the Chief Executive Officer or Chief Risk Officer as their alternate, each of whom are members, with the other members comprising the Chief Operating Officer, Group Treasurer, Head of Financial Planning and Analysis, Head of Financial Control and Head of Market and Liquidity Risk.

Operations Committee (OPCo)

Purpose
The OPCo provides operational oversight and organisational alignment to deliver an efficient, consistent, and effective operating model, ensuring that operational procedures and business processes are relevant.

Frequency and membership
The OPCo meets monthly and is chaired by the Chief Operating Officer or the Chief Technology Officer as their alternate with the other members comprising the Chief Executive Officer, Enterprise Risk Director, Group HR Director, Head of Financial Control and divisional Managing and Risk Directors.

Board meetings and activity in 2019

Board meetings
The activities undertaken by the Board in 2019 were intended to help promote the long-term sustainable success of the Company. Scheduled Board meetings focussed on five main themes in 2019:

Strategy and execution, including: approving and overseeing the Group's key strategic targets and monitoring the Group's performance against these targets; reviewing and approving key projects aimed at developing the business; reviewing the strategy of individual divisions.

Financial performance, including: setting financial plans, annual budgets and key performance indicators and monitoring the Group's results against them; approving financial results for publication; and monitoring and approving the approach to the Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP).

Risk management, regulatory and other related governance, including: reviewing and agreeing the Group's policies; setting risk appetites; reviewing the Group's solvency position and forecast and agreeing the Group's approach to climate change in light of the PRA's supervisory statement published in April 2019.

Spotlights, including: deep dive sessions on investments, consumer lending, platform lending and partnerships, savings, employee engagement survey and culture and the exit from Shawbrook International Limited.

Board and Board Committee governance, including: receiving reports from the Board's Committees; updating terms of reference for the Committees; implementing an independent annual review of Board effectiveness; and commencing an annual review of the Group's governance framework.

In addition to routine business, the Board considers and discusses key issues that impact on the business as they arise. The CEO and CFO spend a considerable amount of time with the different divisions and business areas ensuring that the Board's aims are being correctly disseminated throughout the Group, and that our employees' views and opinions are reported back to the Board and Board Committees.

Strategy days
The Board sets aside time each year outside the annual Board calendar to hold strategy days giving the Directors the opportunity to focus solely on strategic matters. In February and October 2019, the Board held offsite sessions to set and monitor progress against the Group's strategy and to discuss the strategic challenges and opportunities within the Group and its divisions. Sessions focussing on the savings proposition, modernisation of business functions, optimisation of resources and further enhancing the RMF were also held.

Board induction
All new Directors appointed to the Board undertake an induction programme aimed at ensuring they develop a solid understanding of the Group, its divisions, people and processes, and of their roles and responsibilities as Directors of the Company. The programmes are tailored to suit each Director and include:

- provision of relevant current and historical information about the Group;
- visits to business units around the Group;
- one-to-one meetings with Board members, Senior Management and the Company's advisors.

Michele Turmore, who joined the Board as an Independent Non-Executive Director in October 2019, received such an induction programme, which was completed in November 2019.

Board effectiveness review
To reflect upon the progress since the 2018 Board effectiveness review, Egon Zehnder were invited to undertake a follow up review in 2019. More information about the nature and outcomes of their review are on page 45.

Corporate Governance Report

Conflicts of interest

All Directors have a duty to avoid situations that may give rise to a conflict of interest (in accordance with s175 of Companies Act 2006). Formal procedures are in place to deal with this. Directors are responsible for notifying the Chairman and the Company Secretary as soon as they become aware of any actual or potential conflict of interest for discussion. This will then be considered by the Board which, will take into account the circumstances of the conflict when deciding whether to permit it (or whether to impose any conditions). Any actual or potential conflicts of interest are recorded in a central register and Directors are also required, on an annual basis, to confirm that they are not aware of any circumstances which may affect their fitness and propriety and therefore their ability to continue to serve on the Board. In addition, Directors are required to seek the Board's approval of any new appointments or material changes in external commitments.

Induction, training and professional development

On appointment, all new Directors receive a comprehensive and tailored induction, having regard to any previous experience they may have as a Director of a financial services company. The Group also provides additional induction materials and training for those Directors who are also Committee Chairs. The content of our Director induction programmes is tailored, with input from the new Director. The induction information is delivered in a variety of formats; including face to face meetings with the Chairman, Board Directors, Executive Management and key members of staff, and input from external advisers as appropriate. This is supplemented by the provision of key governance documents as reading material, including policies, procedures, Board and Committee minutes, the Board meeting schedule, the Group structure chart and copies of the Code, the FCA Handbook, regulatory codes/requirements and information on Directors' duties and responsibilities under the Companies Act 2006 and other relevant legislation.

An ongoing programme of training is available to all members of the Board which includes professional external training and bespoke Board training on relevant topics such as regulatory and governance developments, changes to the Companies Act 2006 or accounting requirements. Directors are also encouraged to devote an element of their time to self-development, including attendance at relevant external seminars and events. This is in addition to any guidance that may be given from time to time by the Company Secretary.

The Chairman is responsible for reviewing the training needs of each Director, and for ensuring that Directors continually update their skills and knowledge of the Group. All Directors are advised of changes in relevant legislation, regulations and evolving risks, with the assistance of the Group's advisers where appropriate.

The Board receives detailed reports from Executive Management on the performance of the Group at its meetings and other information as necessary. Regular updates are provided on relevant legal, corporate governance and financial reporting developments. The Board frequently reviews the actual and forecast performance of the business compared against the annual plan, as well as other key performance indicators.

Risk management and internal control systems

The Board has overall responsibility for the Group's system of internal control and for monitoring its effectiveness. The Audit Committee and Risk Committee have been in operation throughout the relevant period and oversee the Group's system of internal control. Material risk or control matters are reported by the Audit Committee and Risk Committee to the Board. The Board monitors the ongoing process by which 'top risks' affecting the Group are identified, measured, managed, monitored, reported and challenged. This process is consistent with both the Group RMF and with internal control and related financial and business reporting guidance issued by the Financial Reporting Council. The key elements of the Group's system of internal control include regular meetings of the Executive Management and risk governance committees, together with annual budgeting, and monthly financial and operational reporting for all businesses within the Group. Conduct and compliance are monitored by Management, the Group risk function, internal audit and, to the extent it considers necessary to support its audit report, the external auditor.

The Board assesses the effectiveness of the Group's system of internal controls (including financial, operational and compliance controls and risk management systems) based on:

- established procedures, including those already described, which are in place to manage perceived risks;
- reports by Management to the Audit Committee and Risk Committee on the adequacy and effectiveness of the Group's system of internal control and significant control issues;
- under the direction of the Chief Risk Officer, the continuous Group wide process for formally identifying, evaluating and managing the significant risks to the achievement of the Group's objectives; and
- reports from the Audit Committee on the results of internal audit reviews and work undertaken by other departments.

The Group's system of internal controls is designed to manage, rather than eliminate, the risk of failure to achieve the Group's objectives and can only provide reasonable, and not absolute, assurance against material misstatement or loss. In assessing what constitutes reasonable assurance, the Board considers the materiality of financial and non-financial risks and the relationship between the cost of, and benefit from, the system of internal controls. During 2019, the Group continued to strengthen its risk management and internal controls capability to ensure that it remained relevant, appropriate and scalable to support the Group's objectives over the duration of the strategic plan and continued to embed improvements into the Group's RMF.

Lines of responsibility and delegated authorities are clearly defined. The Group's policies and procedures are regularly updated and distributed throughout the Group. The Audit Committee and Risk Committee receive reports on a regular basis on compliance with the Group's policies and procedures.

Shawbrook Bank Limited (the main operating subsidiary of the Group) is subject to regulation by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) and as such undertakes an ILAAP and ICAAP on an annual basis. The ICAAP process benefited from ongoing improvements during 2019; the process involves an assessment of all the risks that the Group faces in its operating environment, the likelihood of those risks crystallising and their potential materiality and the effectiveness of the control framework in mitigating each risk. This includes a thorough evaluation of how the Group would be impacted by severe, but plausible, periods of stress in its stress testing programme.

The purpose of the process is to establish the level and quality of capital resources that the business should maintain, both under current market conditions and under a range of stressed scenarios, to ensure that financial resources are enough to successfully manage the effects of any risks that may crystallise.

Corporate Governance Report

Cyber resilience

The Group recognises the importance of cyber resilience. The Board oversees the Group's cyber resilience approach and the level of investment into cyber security, providing robust challenge and scrutiny to ensure that the Group is adequately mitigating the threats it faces. The Board recognises that specialist knowledge is required in this area and therefore seeks relevant advice from third parties where appropriate. The cyber resilience strategy is routinely monitored by the Risk Committee and reviewed by the Board on an annual basis. The review considers the latest cyber threat intelligence assessment, the specialist nature of cyber threats and any outsourcing risks faced by the Group in this area. This ensures that the strategy remains fit for purpose to combat the potential cyber threats the Group may face.

Remuneration

The Board has delegated responsibility to the Remuneration Committee for the remuneration arrangements of the Group's Executive Directors, certain individuals considered to be material risk takers and the Group's Chairman. You can find out more about this in the Directors' Remuneration Report which starts on page 66.

Relationship with Marlin Bidco Limited (the 'Shareholder')

The Group is committed to maintaining a constructive relationship with the Shareholder whilst not compromising the independence of the Board.

The Chief Executive Officer and the Chief Financial Officer meet with the Shareholder and their representatives on a regular basis outside of Board and Committee meetings. The Shareholder also meets with the Chairman and has the option to meet with other Non-Executive Directors on request.

To ensure that governance arrangements with the Shareholder are formalised, a Framework Agreement and Memorandum of Understanding outlining the responsibilities of each party was established following the change in ownership. The Framework Agreement ensures that information flows are clear, that the independent judgement of the Board is not impacted and that the Board retains its oversight of the business in respect of strategy, performance, risk appetite and assessment of the control framework and governance arrangements. The Memorandum of Understanding seeks to support and protect the independence of the Board, particularly in relation to the appointment of Non-Executive Directors to the Board and its Committees. It ensures that there will always be a majority of independent Non-Executive Directors in line with the Code. As set out in the Framework Agreement the Shareholder has appointed two Directors to the Board, both of whom are considered Institutional Directors.

The Group recognises the importance of ensuring effective communication with all of its stakeholders. This report, together with a wide range of other information, including financial reports and regulatory announcements are made available on the Investor section of the Group's website at **https://www.shawbrook.co.uk/investors/.**

Other Committees

The Board has delegated authority to its principal Committees to carry out certain tasks as defined in each Committee's respective terms of reference. The written terms of reference in respect of the Audit, Risk, Remuneration and Nomination Committees are available on the Company's website. In addition to the principal Committees the Board is supported by the work of the Disclosure Committee and the Acquisitions and Divestments Committee, which meet on an as needed basis.

Annual General Meeting

Shawbrook Group plc's Annual General Meeting will be held on 12 May 2020.

Audit Committee Report

Membership, attendance and responsibilities of the Committee can be found on pages 44 and 46.

The terms of reference for the Committee can be found on the Group's website at: **shawbrook.co.uk/investors/.**

I am pleased to present the Audit Committee Report. The Committee possesses recent and relevant financial experience in line with good governance practice across the sector and included within the Code.

The Committee has continued to focus on the issues relevant to the Group's financial reporting, considering emerging trends and overseeing the Group's internal control framework to ensure it remains robust and fit for purpose.

The Committee's annual work plan is framed around the Group's financial reporting cycle which ensures that the Committee considers all matters delegated to it by the Board and covers a review and challenge of the critical accounting estimates and judgements, which are set out in Note 1.9 of the Financial Statements.

We also received reports from the internal audit function, which in 2019 covered responsible lending, arrears and forbearance, IT security, operational resilience, procurement and identity and access management.

During the year, IFRS 9 was further embedded across the Group with the changing macroeconomic environment in relation to Brexit continuing to be at the forefront of the Committee's discussions when considering our modelling judgements and the macroeconomic scenarios used within the expected credit loss calculation.

Work has also been undertaken to commence the transition to establish an in-house internal audit function. A Head of Internal Audit has been appointed who will work closely with Deloitte, our present outsourced provider of internal audit services to build an independent and effective in-house function.

Andrew Didham
Chair of the Audit Committee

16 April 2020

Main activities during the year

Throughout the year, the Committee discussed a range of topics including financial reporting, internal controls and risk management, external audit, internal audit and whistleblowing. You can find out more about this in the following sections.

Financial reporting

The Committee considered the integrity of the Group financial statements and all external announcements in relation to its financial performance. In 2019, this included the Group's 2018 Annual Report and Accounts, its Financial Reports and Pillar 3 disclosures together with any related management letters, letters of representation and reports from the external auditors. Significant financial reporting issues and judgements were considered together with any significant accounting policies and proposed changes to them.

Going concern and long-term viability

The Committee reviewed a detailed paper presented by Management setting out the assumptions underlying the going concern statement. The paper covered the capital position of the Group, embedding of the Group's RMF and governance and the work performed on the Group's ICAAP and ILAAP. The Committee also considered an additional Covid-19 stress test scenario prepared to examine the immediate implications of the government actions to contain the spread of Covid-19 along with the support provided by the government and the Bank of England to individuals and businesses to support the economy and the more severe 'Rates Down' scenario specified by the Bank of England as a severe but plausible outcome for the UK economy. The Committee also considered reports from Management concerning the operational resilience of the business having effectively and efficiently converted to remote home working in compliance with government advice. Based on the work performed and having regard for the additional work performed by Management concerning the post year end Covid-19 pandemic, the Committee concluded that there was a reasonable expectation that the Group will have adequate resources to continue in operational existence for the period of assessment of 12 months from the date of signing the accounts. The Committee reported accordingly to the Board, which also considered going concern in detail.

In order to support the Board's approval of the statement on page 141 as to the longer-term viability of the Group, the Committee reviewed papers from Management setting out the intended approach to the disclosures and providing details in support of the statement based in particular on the Group's medium-term plan and the results of stress testing, including both the Covid-19 and 'Rates Down' stress tests referred to above, the reverse stress tests included in the ICAAP and the effective operational resilience apparent following the invocation of the Group's Incident Management Plan.

Audit Committee Report

Significant areas of judgement

During 2019, the following significant issues and accounting judgements were considered by the Committee:

Significant financial and reporting issue	How the Committee addressed the issue
Impairment of loans and advances	The Committee received presentations from Executive Management explaining the impairment methodology across the Group's lending operations ahead of both the interim and full year results. The Committee considered and challenged the impairment methodology applied by Management and also subsequently impacted by IFRS 9 (discussed further below), including the inputs to the statistical loan loss models prepared by the Group risk function. The Committee also considered the calibration of model parameters in the light of economic indicators and underlying book performance. The Committee reviewed the movements in impairment coverage ratios and non-performing loan ratios throughout the year and concluded that these had been appropriately monitored during the year. The Committee reviewed the net asset values recognised in relation to investment made in strategic change programmes, concluding that on balance the various remaining economic benefits supported the continued recognition of net asset balance with several immaterial legacy projects being impaired where economic benefit to be realised was insufficient to support the net asset value. The Committee also reviewed the development of the control environment and tools to develop the Group's approach to forecasting. The Committee concluded that the impairment provisions, including Management's judgements, were appropriate. Refer to Note 1.9(d) of the Financial Statements for further details.
Effective interest rate	Interest earned on loans and receivables is recognised using the effective interest rate (EIR) method. The EIR methodology of accounting uses a discounted cash flow model to spread interest and fee income and expenses attributable to loan assets, including costs and other premium and discounts, over the estimated life of the asset. EIR is calculated on the initial recognition of loan lending through a discounted cash flow model that incorporates fees, costs and other premiums or discounts. There have been no changes to the EIR accounting policies during the year. The Committee considered and challenged the EIR methodology applied by Executive Management, including expected future customer behaviours, redemption profiles and changes to existing redemption profiles and concluded that the EIR methodology was appropriate as at 31 December 2019. Refer to Note 1.9(a) of the Financial Statements for further details.
Impairment assessment of goodwill	The Committee considered and challenged the annual assessment of the carrying value of goodwill. Following the review and challenge of the Group's value in use calculations and key assumptions, the Committee agreed with Management's conclusion that the Group's carrying value of goodwill as at 31 December 2019 was reasonably stated. Refer to Note 1.9(b) of the Financial Statements for details of impairment testing of goodwill.

Significant financial and reporting issue	How the Committee addressed the issue
Conduct risk	The Group's Consumer Lending division is exposed to risk under s. 75 of the Consumer Credit Act (CCA), in relation to any misrepresentations or breaches of contract by suppliers of goods and services to customers where the purchase of those goods and services is financed by the Group. While the Group would have recourse to the supplier in the event of such liability, if the supplier becomes insolvent then that recourse would have limited value. The Committee considered the increase in exposures to insolvent suppliers, specifically in the case of the Group's exposure to s.75 of the CCA relating to solar panels. Throughout 2019 the Group's Consumer Lending division has worked to ensure that all complaints relating to solar panels are being fairly addressed. The Committee concluded that the provisioning against conduct risk exposures was appropriate as at 31 December 2019. Refer to Note 1.9(c) of the Financial Statements for further details.
Risk-weighted asset assurance	The Committee has engaged a third party to provide assurance to the Board with regards to the completeness and accuracy of the risk-weighted asset balances reported to the Bank's regulators. The Committee continues to monitor developments in this regard across the UK banking sector and will consider in due course whether to incorporate formal attestation in the Annual Report and Accounts.
Post balance sheet events	The Committee carefully considered the implications of the Covid-19 pandemic upon the preparation of the 2019 Annual Report and Accounts. The Committee agreed with Management that the declaration of the pandemic and the various protective actions by government and their immediate impact on economic activity were matters that arose during 2020 and did not pertain to the conditions that existed as at 31 December 2019. As such, it was agreed that the matter should be regarded as a non-adjusting post balance sheet event and no adjustment made to the financial statements. Refer to Note 43 of the Financial Statements for further details. The Committee also carefully considered the implications of the Covid-19 pandemic upon the going concern and viability statements contained within the Annual Report and Accounts on pages 56 and 141, respectively. Additional work was commissioned to examine the possible implications of the Covid-19 pandemic, the extent and duration of social distancing measures, the impact on the economy and asset prices generally and the countervailing support being provided by the government and Bank of England to individuals and the economy at large.

In addition to the matters described above, the Committee considered matters relating to provisions for contingent liabilities, hedge accounting, LIBOR transition and external audit performance.

Internal controls and risk management

The Committee annually assesses principal risks and uncertainties on a financial control basis. Details of the risk management systems in place and principal risks and uncertainties are provided within the Risk Management Report which starts on page 80. The Group's system of internal control has been designed to manage risk and whilst risk cannot be eliminated, the systems assist with the provision of reasonable assurance against material misstatement or loss.

The Committee receives reports on a regular basis on compliance with the Group's policies and procedures and the effectiveness of the Group's systems and controls.

The risk and internal audit functions review the extent to which the system of internal control is effective; is adequate to manage the Group's principal risks; safeguards the Group's assets; and, in conjunction with the Company Secretary and the Group's legal and compliance functions, ensures compliance with legal and regulatory requirements.

Audit Committee Report

Internal audit

The internal audit function as the third line of defence is outsourced to Deloitte LLP providing assurance to the Group that the specialist nature of the Group's activities can be fully assessed. The role of the internal audit function and the scope of its work continue to evolve to take account of changes within the business and emerging best practice.

The work of the internal audit function is focused on the areas of greatest risk to the Group, as determined by a structured risk assessment process involving Executive Management. The output from the process is summarised in an internal audit plan, which is approved by the Committee annually.

On behalf of the Board, the Committee undertakes regular reviews of the effectiveness of the Group's systems of internal control as detailed in the section above. The Group has outsourced the internal audit function to Deloitte LLP since June 2013. For several years, the Committee had been satisfied with an outsourced internal audit function. More recently, work has been undertaken to ascertain whether it would be appropriate to bring the function in-house. In 2019, the Committee agreed that it was the right time to begin taking steps to establish an in-house internal audit function and appointed a new Head of Internal Audit. The new Head of Internal Audit will work closely with Deloitte to ensure the establishment of an effective in-house function. Further detail about this work will be reported on in the 2020 Annual Report and Accounts.

The terms of reference of the internal audit function are set out in the Internal Audit Charter. The Committee approves the annual audit plan and audit methodology for internal audit and monitors progress against the plan during the year. The internal audit Partner agrees the programme of work and reports directly to the Committee on the outcomes. Additional project assurance reviews are undertaken, which include follow up audits to test internal controls as required and requested by the Committee.

Internal audit carried out a significant number of audits during 2019 of varying size and complexity. Thematic audits focused on, amongst other things, model risk, responsible lending, operational resilience, project portfolio governance, arrears and forbearance, solar complaints, block discounting, procurement, corporate criminal offences, identity and access management, forward flow and treasury management system and operational controls. Internal audit reports are circulated to the Committee members prior to each scheduled meeting and the Committee monitors progress against actions identified in these reports.

The Committee monitors and reviews internal audit's effectiveness annually, using feedback from the Board, Senior Management and other stakeholders of the internal audit process. Additionally, the Committee ensures that there are sufficient resources available to internal audit to complete its remit. Internal audit has unrestricted access to all Group documentation, premises, functions and employees as required to enable it to perform its functions. The appointment and removal of the internal audit function is the responsibility of the Audit Committee.

External audit

The Committee oversees the relationship with the external auditor and considers the external auditor's engagement (including remuneration), its effectiveness, its continued independence and objectivity. The Committee also considers the audit and audit strategy (including the planned levels of materiality). The external auditor attends the Committee meetings as appropriate and meets at least annually with the Committee without Executive Management. The Chairman of the Committee also meets privately with the external auditor before each Committee meeting.

During the year, the Committee received regular detailed reports from the external auditor including formal written reports dealing with the audit objectives; and reports on: the auditors' qualifications, expertise and resources; the effectiveness of the audit process; procedures and policies for maintaining independence; and compliance with the ethical standards issued by the Auditing Practices Board. The external auditor's management letter is reviewed, as is Management's response to issues raised and progress is monitored against actions identified in these reports. The Committee monitors the provision of non-audit services by the external auditor throughout the year.

External audit independence and objectivity

The Committee is responsible for reviewing the independence of the Group's external auditor, KPMG LLP and making a recommendation to the Board on their engagement. KPMG LLP has a policy of partner rotation which complies with regulatory standards. The Committee monitors the latest ethical guidance regarding rotation of audit partners.

The Group's external auditor is KPMG LLP and Simon Ryder, the audit partner was appointed to the Group in 2017. Tenure for the audit partner is currently set at 5 years after which point KPMG LLP will appoint a new audit partner in consultation with the Group.

Maintaining an independent relationship with the Group's auditor is a critical part of assessing the effectiveness of the audit process. The Committee has a formal policy on the use of the auditor for non-audit services. It ensures that work is only awarded when permissible and if the auditor's knowledge, skills or experience are a decisive factor and therefore clearly preferred over alternative suppliers.

Each year, the Committee receives and reviews an analysis of all non-audit work and reviews the level of audit and non-audit fees paid to KPMG LLP and ensures that significant assignments are not awarded without first being subject to the scrutiny of the Committee. The fees paid to KPMG LLP for audit and non-audit services are set out in Note 7 of the Financial Statements.

Non-audit services policy

The key principles of the policy on non-audit services are:

- Prohibited services include services remunerated on a success fee or participation in activities normally undertaken by Management.
- The Committee approved a list of permitted audit related reviews of the Group's interim results or any other review of its accounts for regulatory purposes. (Details of the services provided by the external auditor can be found in Note 7 of the Financial Statements).
- The Committee maintains a list of prohibited services which is aligned to the 'blacklist' of services set out in the European Union Audit regulations and directives.
- Pre-approved services up to £100,000 require approval by the Chief Financial Officer, the Chief Executive Officer or the Chair of the Audit Committee. All services that are not pre-approved or are discretional or exceed the monetary threshold of £100,000 should be referred to the Audit Committee for approval.

The Committee reviewed payments for non-audit services and confirms that no prohibited services were provided by the external auditor and it is satisfied that the policy on the supply of non-audit services could not lead to audit objectivity and independence being compromised.

During the year, the Committee assessed the effectiveness of the external auditor. The review included seeking the views of Committee members and Executive Management. The review concluded that the external audit process was effective.

The Committee is satisfied with the performance of the external auditor in 2019 and the policies and procedures in place to maintain their objectivity and independence and has recommended that they be re-appointed at the forthcoming Annual General Meeting.

Whistleblowing

The Committee annually reviews the arrangements by which employees may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters (whistleblowing). The Committee also reviewed reports relating to whistleblowing including cases (anonymised) to ensure arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow up action. The Committee probed Management and was satisfied that the whistleblowing process met the necessary standards and that it was adequately designed, operated effectively and adhered to regulatory requirements.

Governance

The Committee undertakes an annual review of its terms of reference to ensure that they remain relevant and apply any changes or updates in respect of appropriate regulatory requirements.

Fair, balanced and understandable

The Committee reviewed and concluded that the Annual Report and Accounts taken as a whole is fair, balanced and understandable, and provided enough information to enable the reader to assess the Group's position and performance, business model and strategy. When considering the Annual Report and Accounts, the Committee focused on the significant judgements and issues that could be material to the financial statements. This included the matters set out in the table on pages 57 to 58. The Committee challenged the judgements being made and also discussed these matters with the external auditor.

Additional information

The Committee has unrestricted access to Management and external advisors to help discharge its duties. It is satisfied that in 2019 it received sufficient, reliable and timely information to perform its responsibilities effectively.

The Chair reports on matters dealt with at each Committee meeting to the subsequent Board meeting.

The Board reviewed and approved this report on 16 April 2020.

Andrew Didham
Chair of the Audit Committee

Risk Committee Report

Membership, attendance and responsibilities of the Committee can be found on pages 44 and 46.

The terms of reference for the Committee can be found on the Group's website at: **shawbrook.co.uk/investors/.**

I am pleased to present the Risk Committee Report for the financial year-ended 31 December 2019. The Committee's key role is to provide oversight of and advice to the Board on the management of risk across the organisation, balancing the agenda between risk exposure and the future risk strategy of the Group. The Committee has further provided oversight, review and challenge of the suitability of the Group's RMF.

During the year, the Committee continued to focus on the oversight of current areas of risk management whilst ensuring emerging risks are appropriately addressed. We have continued to evolve and embed an appropriate risk culture across the Group providing consistent challenge to the suitability of scenarios and stress testing in light of the changing macroeconomic environment and its impact on the Group's wider risk profile and appetite.

The Committee reviewed and recommended to Board for approval the 2019 Risk and Compliance Plan and the RMF, which included consideration of the emerging risk associated with climate change. The Committee has also focussed on third party risk management and the maturity of the control environment in technology and information security. External challenges have included uncertainty in relation to the direction of the UK's future relationship with the European Union and the political environment. The Committee challenged the Group's preparedness for an uncertain economic environment through the Chief Risk Officer's report to the Board. The Committee reviewed and recommended to Board the annual Money Laundering Reporting Officer report and a report from the Group's Data Protection Officer.

The Committee oversaw progress in the annual review of the Group's risk appetite and the risk assessment that underpins the Group ICAAP which included a number of enhancements in 2019 including a new stress testing approach for the Group's customer loans and advances. The Committee oversaw the development of the Liquidity Contingency Plan and the review and recommendation to Board for approval of the ILAAP. The Committee also received the plan for the update to the Recovery Plan and Resolution Pack (collectively the RRP) that will be completed in 2020.

The Committee has focussed on the oversight of its financial crime controls and maintaining operational resilience and welcomed the appointment of a new Chief Operating Officer and Head of Operational Resiliency to oversee the Group's operational resiliency requirements and management information.

In recognition and support of the Group's zero tolerance appetite to unfair outcomes for its customers, the Committee receives reports from the Chief Compliance Officer of the number of employees who have completed the face to face conduct risk training that has been rolled out to all employees. Progress is also being made towards refining the Group's conduct risk appetite measures and to strengthen the Group's first line of defence financial crime capability, the Committee supported the Board's decision to approve the prioritisation of the automation of standard customer due diligence.

I am also pleased to report that data privacy has been integrated within the Group's RMF as a conduct and compliance risk and 2019 also saw the continued development of the Group's Privacy Framework.

The Risk Committee is mindful of the economic uncertainty that continues to exist, primarily in relation to trading conditions following the UK's exit from the EU and, most recently, the Covid-19 pandemic. The Committee will keep under review the more immediate risks of Covid-19 and Brexit, whilst also reviewing other risks on the horizon which could have a material impact on the Group. During 2019, these included the oversight of the Group's plans in response to the announcement from the LIBOR regulators regarding the decision to transition away from sterling LIBOR to Sterling Overnight Index Average Rate (SONIA) or any other selected alternative benchmark or rate and the Group's Climate Change Plan. Moving into 2020, the Committee will continue to monitor and assess the risks facing the Group and provide guidance in what is looking to be a challenging operating environment.

Paul Lawrence
Chair of the Risk Committee

16 April 2020

Main activities during the year

Risk monitoring and oversight

During 2019, the Committee considered a wide range of risks facing the Group both existing and emerging, across all areas of risk management. At each scheduled meeting, the Committee received regular reports from the Chief Risk Officer detailing the key activities undertaken by the Group risk function to oversee the embedding of risk management across the Group, was provided with outputs of regular risk monitoring and details of specific risk issues, received details of the Group's current and forward looking solvency position and monitored performance against the Group's risk appetite statement.

Risk management and controls

Throughout the year the Committee monitored the effectiveness of the Group's risk management and internal control systems and reviewed their effectiveness through the RMF. The RMF sits across the business with a particular focus on quality assurance and control.

Top and emerging risks

The Group's top and emerging risks are considered regularly by the Committee. Further information about the Group's top and emerging risks can be seen in the Risk Management Report starting on page 80.

Risk Committee Report

Significant risks and primary areas of focus

During 2019, the following significant risk and primary areas of focus were considered by the Committee:

Significant risks and primary areas of focus	Risk Committee review
Enterprise risk management	■ The Committee reviewed and recommended for the Board's approval the RMF for the Group including the introduction of the emerging risks associated with climate change. ■ The Committee reviewed and recommended for the Board's approval the 2019 Risk and Compliance Plan which included the key areas of focus for the risk function and the divisions. ■ The Committee received regular summaries of the enterprise risk profile of the Group through the Chief Risk Officer's Report. ■ The Committee reviewed the top and emerging risks for the Group prior to the Interim Financial Report and the Annual Report and Accounts. ■ The Committee reviewed the effectiveness of the RMF throughout the year through the Chief Risk Officer's Report. ■ The Committee received updates on the three lines of defence through the Chief Risk Officer's Report and challenged the effectiveness of quality control and assurance across the divisions.
Board risk appetite	■ The Committee reviewed progress on the annual review of the Board's risk appetite including material risk appetite limits. ■ The Committee received regular updates on the evolving risk appetite framework, including the provision of a monthly risk appetite dashboard which accompanies the Chief Risk Officer's Report at each meeting.
Credit risk	■ The Committee received regular updates on the Group's implementation of IFRS 9, to understand the impact of future expected credit losses across the divisions. ■ The Committee reviewed and recommended for the Board's approval a number of new asset class policies as part of the annual policy review cycle.
Operational risk	■ The Committee received regular reports across the spectrum of operational risks and information security. The Committee received a summary of the findings from a full Cyber Incident Response Plan which forms an important part of the Group's crisis management framework. These reports cover incidents that have arisen to allow the Committee to assess Management's response and proposed remedial actions. Although a number of incidents were raised during the course of 2019, the Committee was satisfied that the action taken was appropriate and that the control of operational incidents continued to improve. ■ The Committee reviewed a maturity assessment of the control environment within technology and recommended to Board a number of changes to improve control and resiliency. The Committee also received a report and updated policies to improve the risk management approach to third parties.

Significant risks and primary areas of focus	Risk Committee review
Conduct, legal and compliance risk	■ The Committee continually reviews the Group's risk management approach to reflect the regulatory and legal environment in which the Group operates. ■ The Committee received updates on various conduct risk and legal liability risk matters, including details of the conduct risk training that had been rolled out to all staff. ■ The Committee reviewed the Group's approach to conduct risk throughout the year in relation to insolvent suppliers through the Chief Risk Officer's Report. ■ The Committee regularly received updates on the Group's investment in financial crime and received the annual Money Laundering Reporting Officer report and the annual Data Protection Officer's report from the Group's new Data Protection Officer.
Liquidity and market risk	■ The Committee reviewed and recommended to the Board approval of the ILAAP. ■ The Committee reviewed and recommended to the Board approval of the Liquidity Contingency Plan. ■ The Committee reviewed the Group's plans in response to the announcement from the LIBOR regulators regarding the decision to transition away from sterling LIBOR and the Group's Climate Change Plan prior to recommendation to Board for review and submission to the PRA.
Stress testing and capital	■ The Committee reviewed material parts of the Group's ICAAP throughout 2019 and was actively engaged in the oversight of the risk assessment leading to the recommendation for the Total Capital Requirement, macroeconomic stress testing and the oversight of a new stress testing approach for customer loans and advances and the development of idiosyncratic stress tests. The ICAAP includes the Group's assessment of the impact of the PRA's Policy Statement, PS22/17 Refining the PRA's Pillar 1A Capital Framework.
Recovery and resolution plan	■ The Committee received the plan to redevelop the Recovery Plan and Resolution Pack (collectively the RRP) during 2020.

Risk Committee Report

Priorities for 2020

The key projects which the Group risk function are accountable for delivering in 2020 include:

- Delivery of a programme to implement a new credit risk application system.
- Delivery of the ICAAP.
- Development and delivery of the Recovery and Resolution Plan.
- Managing and assessing the key risks to the business and our customers from Covid-19.
- Delivery of the customer due diligence automation project in partnership with the Chief Compliance Officer.
- Delivery of the Climate Change Plan.
- Delivery of a refreshed and targeted data privacy training programme.
- Delivery of face to face financial crime training to the wider Group.

Governance

The Committee undertakes an annual review of its terms of reference to ensure that they remain relevant and apply any changes or updates in respect of appropriate regulatory requirements.

Other matters considered in detail by the Committee in 2019

- Brexit.
- Fast growing firms thematic review and associated actions.
- LIBOR transition.
- Material variations in product governance.
- Top and emerging risks.

Additional information

The Committee has unrestricted access to Management and external advisors to help discharge its duties. It is satisfied that in 2019 it received sufficient, reliable and timely information to perform its responsibilities effectively.

During the year, the Chair and the Committee had scheduled meetings with the Chief Risk Officer without Management being present.

The Chair reports on matters dealt with at each Committee meeting to the subsequent Board meeting.

The Board reviewed and approved this report on 16 April 2020.

Paul Lawrence
Chair of the Risk Committee

Directors' Remuneration Report

Membership, attendance and responsibilities of the Committee can be found on pages 44 and 46.

The terms of reference for the Committee can be found on the Group's website at: **shawbrook.co.uk/investors/.**

On behalf of the Remuneration Committee, I am pleased to present the Directors' Remuneration Report for the 2019 financial year. During the year, the Committee continued to oversee Shawbrook's approach to reward for senior executives, material risk takers, and the wider workforce.

In early 2019, the Committee undertook a review of the bonus arrangements and ensured that the financial and non-financial performance conditions were fully aligned with the Group's strategy. At the same time, it reviewed the on-target bonus opportunity of its Executive Directors and decided to reduce this from 80% to 60% of salary. It also oversaw the implementation and initial allocations under the Group's new Management Incentive Plan. This plan is designed to ensure that our long-term incentives appropriately reward strong performance and are aligned with the interests of our Shareholders.

During the course of the year, the Committee reviewed the alignment of its reward arrangements with the new UK Corporate Governance Code. The Committee was involved in the continued review of the reward proposition for the wider employee base, which included the introduction of a new workplace pension arrangement and a new recognition scheme. In keeping with its terms of reference, the Committee also reviewed the compensation arrangements of material risk takers who had joined or departed during the year, as well as approving year end bonus outcomes and salary increases for that population.

The Group also published its 2019 gender pay gap outcomes alongside its commitments set out under the Women in Finance Charter. Regrettably, whilst female representation has continued to grow at a bank wide level, progress against our Senior Management aspirations has been less positive. We are however encouraged by the improvements the Group is making through its wider diversity and inclusion initiatives and remain committed to the principles of the Charter.

At the end of the year, the Committee reviewed performance against the Group's 2019 financial and non-financial objectives, as well as divisional performance and risk alignment, in order to determine the overall bonus pool in 2019. In 2019, the Group continued to deliver strong financial growth alongside progress in key performance metrics relating to its people, risk management, and strategy and culture (including technology and the customer experience). These performance factors, as well as the individual's contribution to the business during the year, were taken into consideration when determining awards at an individual level.

The Committee is comfortable that the remuneration policy has operated as intended and no material changes are proposed for 2020. The Committee will continue to maintain a balanced strategy to reward our employees in a manner which drives the long-term security, soundness and success of the Group. In doing so, the Committee will continue to look at ways to ensure that the views and interests of the wider workforce are appropriately considered when setting remuneration at all levels across the Group.

Robin Ashton
Chair of the Remuneration Committee

16 April 2020

Directors' Remuneration Report

Main activities during the year

The Committee met on five occasions during 2019. In addition to cyclical agenda items, the Committee oversaw the implementation of a new Management Incentive Plan as well as enhancements to the reward proposition for the Company's wider workforce including the introduction of a new workplace pension arrangement and a new recognition scheme.

Deloitte LLP provided independent advice to the Committee on all executive remuneration matters. Deloitte LLP is a member of the Remuneration Consultants Group and is a signatory to its Code of Conduct. The Committee is satisfied that the advice received from Deloitte LLP was objective and independent.

In line with the Framework Agreement and Memorandum of Understanding, the Shareholder has representation on the Committee. Where applicable decisions are escalated through the Board to the Shareholder for approval.

Guiding reward principles

The Group seeks to reward its employees fairly for their contribution and motivate them to deliver the best outcomes for all stakeholders. This is underpinned by the following principles:

- Remuneration arrangements are designed to attract, retain and motivate high calibre individuals who will assist the Group in meeting its strategy.
- Reward structures will be developed in alignment with the Group's strategy and will seek to promote long-term sustainable success, while meeting appropriate regulatory requirements.
- Remuneration will be determined within the Group's stated risk appetite defined as 'maintaining a balanced strategy to reward our employees for appropriate conduct and performance'. Safeguarding the right outcomes for customers is at the heart of this.
- There will be an appropriate mix of long term and short-term variable pay arrangements in place, which will assist in driving the long-term security, soundness and success of the Group.
- The long-term and short-term variable pay plans will be subject to appropriate performance measures, ensuring the right balance between these elements of the reward package.
- Remuneration outcomes will be determined with reference to total reward principles. For example, when making bonus decisions, the Group will take into account an employee's total aggregate remuneration.
- Eligibility for, and payment of, any remuneration will be communicated in a clear and transparent way for all colleagues and in a timely manner.
- Reward structures will be designed to avoid any conflicts of interests as set out in the Group's conflicts of interest policy. In this regard, employees in control functions will be remunerated independently from the performance of the business areas that they oversee. Furthermore, the Committee will be constituted in a way that avoids conflicts of interests and provides independent oversight of remuneration matters within the Group. No individual will be permitted to be present at the Committee when decisions are taken which concern their own remuneration.

The Group keeps its reward strategy, including the guiding reward principles, under regular review to ensure it continues to support the delivery of its strategic priorities. The Committee considers that the current framework appropriately addresses the following factors as set out in the UK Corporate Governance Code.

Clarity and simplicity	As a private company, Shawbrook is not required to produce a full Directors' Remuneration Report aligned to that of a UK-listed company. However, in the interests of transparency, the Committee provides voluntary disclosure of our remuneration policy and how this applies to Executive Directors.
Risk	As a financial institution, one of our guiding reward principles ensures that remuneration is determined within the Group's stated risk appetite defined as 'maintaining a balanced strategy to reward our employees for appropriate conduct and performance'. Safeguarding the right outcomes for customers is at the heart of this. All incentive arrangements for material risk takers are subject to malus and clawback provisions.
Predictability	The remuneration policy table contains details of maximum annual bonus opportunity levels, with actual incentive outcomes varying depending on the level of performance achieved. In terms of the Management Incentive Plan, value will only be delivered to participants if the underlying value of the Group grows by reference to the achievement of stretching hurdles set relative to the Group's business plan at the time of award. Any payment under our incentive arrangements will be subject to the committee's discretion.
Proportionality and alignment to culture	All eligible permanent and fixed-term employees are considered for an annual bonus, aligning reward to the overall financial and non-financial performance of the Group. Under the annual bonus, the Committee assesses performance against a range of objectives, including ones related to our customers, risk and our people. This ensures that reward is not determined solely on financial performance but also drives behaviours consistent with Shawbrook's culture. The Committee has the discretion in circumstances of poor financial performance to reduce the bonus outcome, including potentially to zero.

Directors' Remuneration Report

Directors' Remuneration Policy

Following the change in ownership and delisting of its shares in 2017, Shawbrook is no longer required to produce a Directors' Remuneration Report in accordance with Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended). However, for transparency the Board has produced the table below which summarises the key components of the Group's reward package and how these apply to the Executive Directors.

Element	Purpose and link to strategy	Operation
Salary	To provide a competitive level of base pay to attract and retain talent.	Base salaries are set with reference to the size and scope of the role, the external market as well as the skills and experience of the individual. Salaries are normally reviewed on an annual basis, with any changes effective 1 March each year. Where salary increases are awarded to Executive Directors, these are typically in line with the wider workforce.
Pension	To provide a competitive post-retirement benefit supporting the long-term financial wellbeing of employees.	Executive Directors may participate in the Group's workplace pension arrangement or receive a cash allowance in lieu of pension contributions. Executive Directors currently receive an allowance of 15% of salary per annum.
Benefits	To provide a suite of competitive benefits to support the wellbeing of employees.	The Group offers a wide range of benefits to support our employees' health, financial and lifestyle needs. Benefits provided to our Executive Directors include (but are not limited to) private medical cover, life assurance and permanent health insurance. Additional benefits may be provided as reasonably required.
Annual bonus	To incentivise and reward the achievement of short-term financial and non-financial objectives which are closely linked to the Group's strategy. Deferral encourages long-term focus and risk alignment.	Annual bonus awards are determined with reference to financial, non-financial and individual objectives. Specific performance measures and objectives are reviewed on an annual basis to ensure they appropriately align to the Group's ongoing strategy. When finalising individual award levels, consideration is given to the overall performance of the Group, divisional performance and individual performance against agreed objectives, including alignment with corporate values, as well as the outcome of the independent risk adjustment process. Poor financial performance can result in the bonus being reduced, including potentially to zero. The on-target opportunity for Executive Directors will be 60% of salary per annum with a normal maximum opportunity of 100% of salary per annum. Awards over a threshold level (set by the Committee each year) are subject to deferral. Deferred awards will normally be released in equal tranches after one, two and three years, subject to continued employment. Annual bonus awards are subject to the Group's malus and clawback provisions.

Element	Purpose and link to strategy	Operation
Long-term incentives	To incentivise and reward the delivery of the Group's long-term strategy and growth over a sustained period.	Following a comprehensive review, the Group introduced a new Management Incentive Plan (MIP) in early 2019. This is the only long-term incentive arrangement which Executive Directors participate in. Award levels under the MIP were determined by reference to individual performance as well as the size and scope of the role. The shares will deliver value to participants for growth in the underlying value of the Group by reference to the achievement of hurdles which have been set relative to the Group's business plan at the time of award. The value accrued under the MIP will ordinarily be released to participants at an exit event, i.e. the sale of the Group, the majority of its assets or an Initial Public Offering. The value of the MIP will depend not only on financial performance but also on the overall health of the business which will consider other non-financial factors. Awards will be subject to the Group's malus and clawback provisions. Separately, participants also had the opportunity to co-invest in the Group using their own funds. Any shares acquired via this co-investment will also be released at an exit event and will enable participants to share in the growth in value of the Group on a similar basis to the Shareholder.

Non-Executive Director Fees
The Chairman of the Board and Non-Executive Directors are entitled to an annual fee, with additional fees payable to the Senior Independent Director, the Chairs and members of the respective Committees of the Board. Fee levels are reviewed periodically, and are set out within this report.

Reasonable expenses incurred in the performance of Non-Executive duties may also be reimbursed or paid directly by the Group, as appropriate.

Directors' Remuneration Report

Directors' remuneration in 2019

The tables below set out the remuneration received by Executive and Non-Executive Directors during 2019. The numbers included in the table below have been audited.

	2019		2018	
Executive Directors[1]	**All Executive Directors £000**	**Highest paid Executive Director £000**	All Executive Directors £000	Highest paid Executive Director £000
Salary	**738**	**403**	712	361
Taxable benefits	**4**	**2**	3	1
Pension	**111**	**60**	179	126
Annual bonus	**430**	**250**	670	500
Subtotal	**1,283**	**715**	1,564	988
Payments for loss of office	**–**	**–**	1,214	983
Total	**1,283**	**715**	2,778	1,971

Non-Executive Directors[2]	**2019 £000**	2018 £000
Fees	**561**	721

[1] Following the resignation of Steve Pateman in July 2018, Ian Cowie assumed the role as Interim Chief Executive Officer in July 2018. He was not however formally appointed to the Board of the Company until February 2019. The table above therefore only includes remuneration receivable by Ian Cowie during the period he was a Board Director, with the exception of his 2019 Annual Bonus which is reflected in full given that this related to his role as Chief Executive Officer over the full year.

[2] Whilst not paid directly to the individual, the Group incurs fees of £50,000 plus VAT per annum in relation to each Institutional Director appointed to the Board by the ultimate parent company, as set out and agreed within the Framework Agreement. The Institutional Directors are not employed by the Group and their fees are not included in the above table.

Notes to the tables

Pension: all Executive Directors received their pension contributions during 2019 by way of a cash allowance.

Annual bonus: all Executive Directors were eligible to participate in the annual bonus in 2019, with an on-target opportunity of 60% of salary and a maximum opportunity of 100% of salary.

The bonus pool outcome for the Group was determined through a rounded assessment of performance against a range of the Group's objectives for 2019. For Executive Directors, this included objectives relating to:

- Financial performance
- Customer
- Risk
- People
- Strategy and culture

When determining the bonus pool outcome, the Committee carefully reviewed performance for each of the relevant objectives, whilst also taking into account broader considerations relating to overall Group and divisional performance. The Committee also considered the outcomes of the Chief Risk Officer's independent report.

Overall, whilst noting that the Group's financial and non-financial performance had generally been strong, the Committee recognised that further improvements could be made, particularly in continuing to embed its approach to risk management. As a result, the Committee set a bonus pool at a level which was below target.

The overall value of awards for the Executive Directors are included in aggregate in the emoluments table. In line with policy, 50% of any amount in excess of £100,000 payable to an individual will be subject to deferral in cash and released in three equal tranches after one, two and three years.

Share related benefits: no share related benefits were exercised during 2019.

Payments for loss of office: no payments for loss of office were made during 2019.

Wider workforce remuneration

In line with our guiding reward principles, the Group seeks to reward all its employees fairly for their contribution and motivate them to deliver the best outcomes for all our stakeholders.

The remuneration approach applied for our Executive Directors is closely aligned to how we reward all employees. All employees receive a salary, pension contribution and benefits set at a level considered appropriate taking into account their role and experience. Fixed pay is set at a competitive level to attract and retain talent. A number of enhancements were made to the 'all employee' reward proposition in 2019 including the introduction of a new workplace pension arrangement, which included an increase to the Company's highest pension contribution rate, as well as the launch of a new recognition scheme.

In terms of variable pay, all permanent and fixed-term employees are eligible to be considered for an annual bonus as appropriate to their role. We have also recently introduced a new long-term incentive (LTIP) to reward other selected senior individuals, who do not partcipate in the MIP, for their contribution to the delivery of our long-term strategy.

The Committee receives and considers internal and external information as appropriate to guide decisions on remuneration, including but not limited to, the results of employee engagement surveys and feedback sought from internal (such as the Group HR Director and Group Head of Reward) and external stakeholders. The Committee also considers the Group's gender pay gap outcomes for the year, details of which for 2019 can be found on our website.

As a private company, Shawbrook is not strictly required to disclose the CEO pay ratio. However, in line with the Board's commitment to give due consideration to the spirit of the 2018 UK Corporate Governance Code and in the interests of transparency, the Committee has chosen to voluntarily disclose the ratio of the CEO's total remuneration to the median total remuneration of our employees.

	Median ratio
Total remuneration[1]	13:1

On review of the ratio, the Committee is confident that this is reflective of our overall approach to pay and reward throughout the Group.

[1] Includes fixed remuneration, taxable benefits, pension and annual bonus awards earned in respect of the financial year ended 2019. It does not include any awards granted under the MIP and LTIP. In reaching the median total remuneration of our employees, the Group has considered the full time equivalent total remuneration of all individuals employed by the Group for the entirety of 2019 where such earnings have not been impacted by periods of absence.

Directors' Remuneration Report

Directors' remuneration in 2020

The Committee has determined that, for 2020, the remuneration policy will be implemented as follows for Executive Directors.

Executive Director salaries: the Committee reviewed Executive Director salaries on an individual basis in line with the normal annual salary review and determined that no increases would be awarded at this time.

Pension and benefits will continue to operate in line with the remuneration policy.

Annual bonus: the normal maximum annual bonus opportunity for Executive Directors will be 100% of salary. When determining the annual bonus outcomes for 2020, the Committee will give consideration to performance based on a range of key financial and non-financial measures, as well as the individual's overall performance and the outcome of the Chief Risk Officer's independent risk review.

Long-term incentive: Executive Directors were granted awards under the Management Incentive Plan in 2019, as set out within this Remuneration Report. This is the only long-term incentive arrangement in which the Executive Directors participate.

Non-Executive Director fees

There will be no changes to Non-Executive Director fees for 2020.

	Fee from 1 January 2020
Chairman fee	£200,000
Non-Executive Director base fee[1]	£65,000
Senior Independent Director fee	£10,000
Audit and Risk Committee Chair fee	£20,000
Remuneration Committee Chair fee	£5,000
Audit and Risk Committee membership fee	£5,000
Remuneration and Nomination Committee membership fee	£2,500

Additional information

The Committee has unrestricted access to Management and external advisors to help discharge its duties. It is satisfied that in 2019 it received sufficient, reliable and timely information to perform its responsibilities effectively.

The Chair reports on matters dealt with at each Committee meeting to the subsequent Board meeting.

The Board reviewed and approved this report on 16 April 2020.

Robin Ashton
Chair of the Remuneration Committee

1 Whilst not paid directly to the individual, the Group incurs fees of £50,000 plus VAT per annum in relation to each Institutional Director appointed to the Board by the ultimate parent company, as set out and agreed within the Framework Agreement.

Nomination Committee Report

Membership, attendance and responsibilities of the Committee can be found on pages 44 and 46.

The terms of reference for the Committee can be found on the Group's website at: **shawbrook.co.uk/investors/.**

I am pleased to present the 2019 report as Chair of the Nomination Committee. The Committee played a central role during the year in ensuring adequate succession planning to help contribute to the delivery of the Group's strategy by ensuring the desired mix of skills and expertise of the Board, its Committees, the Executive and the Senior Management.

The Committee oversaw the appointment of Michele Turmore as an Independent Non-Executive Director. The recruitment process involved the engagement of an external recruitment consultant who worked alongside the Committee to help ensure that the preferred candidate had the required balance of skills, knowledge and expertise whilst complementing the existing Board of the Group. Additionally, several internal promotions and external hires were made with the aim of strengthening the senior leadership team.

The Board remains committed to continuing to be a member of the Women in Finance Charter. During 2019, we reviewed the targets that the Group previously set and decided that it would be appropriate to refresh our approach. Further information about this has been provided in this report.

Looking forward to 2020, the Committee will continue to keep under review the structure, size and composition of the Board and its Committees, as well as overseeing succession of the Executive and senior leadership team. Work will also continue to embed the learnings from the 2018 and 2019 Board effectiveness reviews.

Further information about the activities of the Committee is provided in the following report.

John Callender
Chair of the Nomination Committee

16 April 2020

Nomination Committee Report

Main activities during the year

Throughout the year, the Committee considered the composition of the Board and its Committees, Board appointments, Board re-election processes, succession planning and Diversity and Inclusion. Further information about these areas can be found below.

Board composition

During the year, the Committee considered the Board's balance of skills and expertise, structure, size and composition. A review of the Non-Executive Directors' letters of appointment setting out the terms of appointment and time commitment was also undertaken.

The letters of appointment for the Chairman and Non-Executive Directors set out the time that the Group anticipates they will commit to their roles. This is at least four days per month depending on business needs.

Board and Committee changes

The Committee monitors the membership of the Board and its Committees to ensure that there is a suitable balance of diversity, skills and experience. Consideration to the length of service of the members is also given.

During the year, there were several changes to the Board and its Committees. As previously reported both David Gagie and Sally-Ann Hibberd stepped down from the Board on 31 January 2019. On 8 February 2019, following approval of the Shareholder, Andrew Didham was appointed as a member of the Remuneration Committee. On 31 August 2019, Roger Lovering stepped down from the Board and the Audit and Risk Committees. On 1 October 2019, Michele Turmore was appointed as an Independent Non-Executive Director to the Board and as a member of the Audit and Risk Committees.

Board and Senior Management Function appointment process

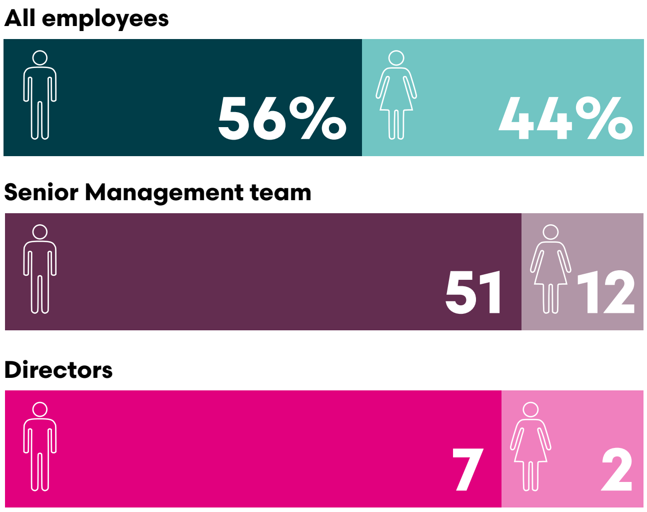
During the year, a key focus for the Committee was the review of the size, structure and composition of the Board and consideration of appointments of Senior Managers Function (SMF) holders (pursuant to the Senior Management and Certification Regime). Prior to any Board or SMF appointment, the Committee will evaluate the balance of skills, knowledge and experience and, in light of this evaluation, prepare a description of the role and capabilities required for a particular appointment (including a statement of responsibilities for SMF holders).

In consultation with the Board, it was agreed that the recruitment of a new independent Non-Executive Director with experience in operations, technology and infrastructure, would help to bolster and complement the expertise of the Board. Ridgeway Partners, who are a signatory to the Voluntary Code of Conduct for Executive Search Firms, and have no other connection to the Company, were engaged by the Board to undertake the search for a new Independent Non-Executive Director. Ridgeway Partners prepared a detailed brief setting out the required skills and experience of preferred candidates.

Ridgeway Partners prepared a list of candidates of appropriate merit from diverse backgrounds for the available position. The Committee agreed a shortlist and a series of interviews took place. Once the preferred candidate had been identified and had given their consent to act as a Director, subject to regulatory approval, the Committee recommended the appointment of Michele Turmore to the Board. Michele Turmore was subsequently appointed to the Board on 1 October 2019.

Additionally, work has been undertaken to identify internal candidates (who were ready for promotion) and recruiting external candidates into the senior leadership team to help fulfil the strategy of the Group. The Committee is pleased to report that there were several internal promotions and external hires made in 2019, which will help the Group to achieve its strategic aims.

Group Gender Metrics



Electing and re-electing Directors

Before recommending the proposed election or re-election of Directors at the 2019 Annual General Meeting, the Committee reviewed the independence of the Non-Executive Directors and concluded that Robin Ashton, Andrew Didham, Paul Lawrence and Roger Lovering met the criteria for independence set out in the Code. John Callender was independent when he was appointed as Chairman. Lindsey McMurray and Cedric Dubourdieu's re-election as Investor Non-Executive Directors was made in line with the Framework Agreement.

In February 2020, Andrew Didham's three-year term of appointment was due to come to an end. At the Board's request, Andrew agreed to continue to serve as a Non-Executive Director. The Board and the Committee is satisfied that Andrew remains independent in judgement and character and continues to make a significant contribution to the proceedings of the Board and its Committees.

Diversity and inclusion

The Group is committed to improving diversity and new appointments continue to be based on skill, experience and knowledge, with a focus on the right person being recruited for the role. Careful consideration is given to diversity of gender, race, skills, experience, as well as regional, socio-economic, educational and professional background among other differences.

Having reflected carefully, the Group reconfirmed its commitment to the Women in Finance Charter in 2019 setting itself a more realistic, longer term target of 30% of female representation in our Senior Management team (reduced from 40%) by December 2022. As part of this commitment and with the support of our main external resourcing partner, Cielo, balanced candidate shortlists and diverse interview panels for management roles, are used wherever possible. This change will allow the Group to track progress in attracting diverse talent and help remove any unconscious bias in the selection process going forward.

Succession planning

The Committee is responsible for ensuring that appropriate succession and development plans are in place for appointments to the Board. We are satisfied that the succession planning structure in place is appropriate for the size and nature of the Group.

Executive and Non-Executive Director induction

All new Directors are required to undertake an induction programme, which includes comprehensive training on their Senior Managers and Certification Regime responsibilities. In addition, Directors are required to undertake training in the regulatory and compliance frameworks and are also required to gain an understanding of relevant legal requirements such as money laundering legislation. Inductions include sessions with the Chairman, Directors, Executive Management and external advisors to gain insight into the organisation. Training is tailored to the requirements of each Director's role, knowledge and experience.

Michele Turmore received a tailored induction which included:

- understanding the role of sub-committees and governance structures;
- understanding the role of the Framework Agreement and Memorandum of Understanding;
- gaining an overview of Board Director duties, responsibilities and protocols;
- reviewing past Board packs, Committee packs and minutes;
- gaining an understanding of current issues relevant to the Board;
- receiving an overview and understanding the strategic direction of the Group;
- receiving a full briefing on UK Conduct Standards, Senior Managers Regime and Prudential Regulation;
- meeting with the key members of the Executive and senior leadership teams to consider, in depth, the key challenges facing their businesses; and
- meeting key external advisors to the Group.

Additional information

The Committee has unrestricted access to the Executive, Senior Leadership and external advisors to help discharge its duties. It is satisfied that in 2019 it received sufficient, reliable and timely information to perform its responsibilities effectively.

The Chair reports on matters dealt with at each Committee meeting to the subsequent Board meeting.

The Board reviewed and approved this report on 16 April 2020.

John Callender
Chair of the Nomination Committee

Directors' Report

Corporate governance statement
The Directors of the Group present their report together with the audited financial statements for the year ended 31 December 2019. Other information that is relevant to the Directors' Report, and which is incorporated by reference into this report, can be located as follows:

Section 414 of the Companies Act 2006 requires the Directors to present a Strategic Report in the Annual Report and Accounts. The information can be found on pages 1 to 37.

The Company has chosen, in accordance with section 414C(11) of the Companies Act 2006, and as noted in this Directors' Report, to include certain matters in its Strategic Report that would otherwise be disclosed in this Directors' Report.

Dividends
The Directors are not recommending a final dividend (2018: nil) in respect of the year ended 31 December 2019.

Employees with disabilities
Applications for employment by people with disability are given full and fair consideration bearing in mind the respective aptitudes and abilities of the applicant concerned and other ability to make reasonable adjustments to the role and the work environment. In the event of existing employees becoming disabled, all reasonable effort is made to ensure that appropriate training is given and their employment with the Group continues. Training, career development and promotion of a disabled person is, as far as possible, identical to that of an able-bodied person.

Appointment and retirement of Directors
The Group's Articles of Association set out the rules for the appointment and replacement of Directors. In accordance with the recommendations of the 2018 Code and the Companies Act 2006, all Directors shall retire from office and may offer themselves for re-appointment at the Annual General Meeting.

Powers of Directors
The Directors' powers are conferred on them by UK legislation and by the Group's Articles of Association. Changes to the Group's Articles of Association must be approved by the Shareholder passing a special resolution and must comply with the provisions of the Companies Act 2006. The Group's Articles of Association can be viewed here: **shawbrook.co.uk/investors/.**

Directors' interests
None of the Directors hold shares in the Company. Lindsey McMurray and Cedric Dubourdieu are directors of Marlin Bidco Limited, the Group's sole Shareholder.

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

The Directors of the Group have entered into individual deeds of indemnity with the Group which constituted 'qualifying party indemnity provisions' entered into by the Directors and the Company. The deeds of indemnity protect the Directors to the maximum extent permitted by the law and by the Articles of Association of the Company, in respect of any liabilities incurred in connection with the performance of their duties as a Director of the Company and any associated Group company, as defined by the Companies Act 2006.

The Group has maintained appropriate Directors' and Officers' liability insurance in place throughout 2019.

Company Secretary
All Directors have access to the services of the Company Secretary in relation to the discharge of their duties. Daniel Rushbrook is the Company Secretary of Shawbrook Group plc. He can be contacted at the Company's registered office, details of which are on page 158.

Going concern
The financial statements are prepared on a going concern basis and the Directors have a reasonable expectation that the Group has the resources to continue in business for the 12 months from the reporting date. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the balance sheet, future projections of profitability, cash flows and capital resources and the longer-term strategy of the business. The Group's capital and liquidity plans have been stress tested under a range of stressed scenarios and have been reviewed by the Directors.

The impact of Covid-19 has also been assessed and stress tested against the 2020 financial and business plans. Whilst the Covid-19 impacts are not yet fully known and will depend on many factors including the length of the enforced closure of certain businesses and social facilities, the social distancing measures and the success and continuity of the government and Bank of England measures put in place to support the economy and businesses, the Group has assessed its capital and liquidity over the going concern period. The Directors assessed the financial implications of the risks associated with Covid-19, including the expected effect of Management actions taken in response, against the most severe but plausible scenario used in the Board's assessment of the ICAAP approved in 2020. This scenario was the 'Rates Down' scenario specified by the Bank of England for use in preparing ICAAP stress tests. Having regard for the severe financial outcomes from this scenario and the reverse stress tests also conducted, the Board concluded that both capital and liquidity forecasts remained within present regulatory requirements, including use of capital buffers, over the going concern period.

After making enquiries, the Directors believe that the Group has sufficient resources to continue its activities for the 12 months from the reporting date and the Group has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the PRA.

Political and charitable donations
The Group did not make any political donations during the year (2018: £nil). Further information on charitable donations made by the Group can be found on page 35.

Share capital
Shawbrook Group plc is a non-listed public company limited by shares.

Details of the Group's issued share capital, together with details of the movements in the Group 's issued share capital during the year, are shown in Note 32 of the Financial Statements.

The Group's share capital comprises one class of ordinary share with a nominal value of £0.01 each. At 31 December 2019, 253,086,879 ordinary shares were in issue. There were no share allotments in 2019.

Restrictions on the transfer of shares
According to the Articles of Association and prevailing legislation there are no specific restrictions on the transfer of shares of the Group.

Rights attaching to shares
On a show of hands, each member has the right to one vote at General Meetings of the Group. On a poll, each member would be entitled to one vote for every share held. The shares carry no rights to fixed income. No one person has any special rights of control over the Group's share capital and all shares are fully paid.

New issues of share capital
Subject to the Framework Agreement and under section 551 of the Companies Act 2006, the Directors may allot equity securities only with the express authorisation of the Shareholder. Under section 561 of the Companies Act 2006, the Board may also not allot shares for cash (otherwise than pursuant to an employee share scheme) without first making an offer to the Shareholder to allot such shares to them on the same or more favourable terms in proportion to their respective shareholdings, unless this requirement is waived by a special resolution of the Shareholder.

Purchase of own shares by the Company
Subject to the Framework Agreement and under section 701 of the Companies Act 2006 the Group may make a purchase its own shares if the purchase has first been authorised by a resolution of the Shareholder.

Substantial shareholdings
The Group is 100% owned by Marlin Bidco Limited.

Auditor
Resolutions to reappoint KPMG LLP as the Group's auditors and to give the Directors the authority to determine the auditor's remuneration will be proposed at the Annual General Meeting.

Directors' Report

Disclosure of information to the auditor
The Directors confirm that:

1. So far as each of the Directors is aware, there is no relevant audit information of which the auditor is unaware; and
2. The Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

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

Directors' responsibility statement
The Directors are responsible for preparing the Annual Report and Accounts and the Group and Parent Company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare such financial statements for each financial year. Under that law, the Directors must prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and Article 4 of the International Accounting Standard (IAS) regulation/and applicable law and have elected to prepare the Parent Company financial statements on the same basis.

Under company law, the Directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period.

In preparing the Group's financial statements, the Directors are required to: properly select and apply accounting policies, present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information and provide additional disclosures when compliance with the specific requirements of IFRS is insufficient to enable an understanding of the impact of particular transactions, other events and conditions on the entity's financial position and financial performance. Finally, the Directors must assess the Group's ability to continue as a going concern.

The Directors are responsible for keeping adequate accounting records that: are sufficient to show and explain the Group's transactions and disclose, with reasonable accuracy, at any time the financial position of the company and enable them to ensure that its financial statements comply with the Companies Act 2006. Additionally, the Directors are responsible for safeguarding the Group's assets and, hence, taking reasonable steps to prevent and detect fraud and other irregularities. The Directors are responsible for maintaining and ensuring the integrity of the corporate and financial information included on the Group's website at **https://www.shawbrook.co.uk/.** Legislation in the UK governing and preparing and disseminating financial statements may differ from legislation in other jurisdictions.

Each of the Directors, whose names and functions are listed on pages 41 to 42, confirms that, to the best of their knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group and the undertakings included in the consolidation taken as a whole;
- the Strategic Report (on pages 1 to 37) and the Directors' Report (on pages 77 to 79) include a fair review of: (i) the business's development and performance and (ii) the position of the Group and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face;
- the Annual Report and financial statements comply with all aspects of the Guidelines for Disclosure and Transparency in Private Equity; and
- the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable, and provide the information necessary for Shareholders to assess the Group's position and performance, business model and strategy.

This responsibility statement was approved by the Board of Directors on 16 April 2020.

By order of the Board.

Daniel Rushbrook
Company Secretary

Risk Management Report

Risk Management Report.

Approach to risk management

The Group seeks to manage the risks inherent in its business activities and operations through close and disciplined risk management which quantifies the risks taken, manages and mitigates them as far as possible and prices appropriately for the residual level of risk carried in order to produce an appropriate commercial return through the cycle.

The Group's approach to risk management continues to evolve and has benefitted from further investment during 2019 in key areas such as financial crime, technology and information security. There has been further investment in the Group's key operating divisions including the appointment of a new Property Finance Risk Director and the recruitment of additional analytical resources to support the delivery of the Group's lending objectives. The Group's Risk Management Framework was further enhanced in 2019, reflecting the emergence of climate change and the realignment of key responsibilities. The Group has also developed a new approach to stress testing which is being embedded in both its Internal Capital Adequacy Assessment Process (ICAAP) and the further development of risk appetite measures and reporting. The Group appointed a new Chief Operating Officer and a Managing Director of Property Finance in April 2019 and a new Head of Operational Risk in November 2019.

The Group's approach to enterprise wide risk management is underpinned by five key elements:

Further details of these key elements are provided in the following sections.

Risk strategy

The risk strategy sets out the risk management objectives which support the achievement of the Group's commercial goals and the operation of business activities which seek to deliver those aims. The risk strategy sets out which risks are to be acquired or incurred and how they will be managed by the organisation. This is summarised in the annual Risk and Compliance Plan that is approved by the Board in February of each year.

The strategic risk management objectives are to:

- identify material risks arising in the day-to-day activities and operations of the Group;
- quantify the risks attached to the execution of the Group's business plans;
- set an appropriate risk appetite with calibrated measures and tolerance levels;
- optimise the risk/reward characteristics of business written;
- set minimum standards in relation to the acquisition, incurrence and management of risk;
- secure and organise the required level and capability of risk infrastructure and resources;
- undertake remedial action where any weaknesses are identified; and
- scan the external horizon for emerging risks.

Risk appetite

The level of risk that the Group is willing to tolerate in operating the various elements of its business are defined in a risk appetite statement, which is agreed by the Board and reviewed on a regular basis. This articulates qualitative and quantitative measures of risk which are cascaded across various areas of the Group's operations, calibrated by reference to the Group's absolute capacity for risk absorption, limit of appetite and target thresholds. During 2019, the Group completed updates to its liquidity and interest rate risk in the banking book appetite and commenced an annual review of the Group and divisional risk appetites.

The risk appetite statement is not static and evolves to reflect and support the Group's business objectives, the operating environment and risk outlook. Whilst the risk appetite statement provides an aggregated measure of performance against risk appetite, it is not just a reporting tool. Just as importantly, it also provides a framework which is used dynamically to inform strategic and operational management decisions, as well as supporting the business planning process.

The risk appetite statement is reviewed periodically by the Risk Committee and agreed with the Board on an annual basis. A dashboard with the status of each metric is monitored monthly. Executive Management and the Board exercise their judgement as to the appropriate action required in relation to any threshold trigger breach, dependent on the scenario at the time.

The risk appetite statement identifies six groups of risk appetite objectives which are further subdivided into 27 appetite dimensions as set out diagrammatically below. A suite of qualitative statements and quantitative measures have been set for each dimension, with risk limits calibrated by reference to absolute capacity, maximum risk tolerance and a threshold trigger level.

Risk appetite objectives	Strategic risk	Creditworthiness risk	Liquidity and market risk	Operational risk	Conduct risk	Reputation risk
Risk appetite dimensions	Profit volatility	Creditworthiness risk	Funding and liquidity	Technology (including systems)	Product design	Regulatory perception
	Financial strength	Concentration risk	Interest rate risk in the banking book	Physical assets and security	Sales and distribution risk	Change perception
	Lending growth			Information risk	Post sales service	Media promoter
				Operations risk	Culture	Social advocacy
				Change risk		
				Third parties		
				People		
				Financial crime		
				New product approval		
				Financial reporting		
				Model risk		
				Climate risk		

Approach to risk management

Risk Management Framework

All of the Group's business and support service activities, including those outsourced to third party providers or originated via brokers and other business intermediaries, are executed within the parameters of a single comprehensive Risk Management Framework (RMF). This sets out minimum requirements and ensures consistent standards and processes are set across the organisation. Risks are identified, measured, managed, monitored, reported and controlled using the RMF. The design and effectiveness of the framework is overseen and reviewed by the Risk Committee.

Responsibility for risk management sits at all levels across the Group from the Board and Executive Committee down through the Group's divisions, central functions, and in turn to each divisional head and their business managers and risk officers.

The Group's RMF describes the various activities, techniques and tools which are mandated to support the identification, measurement, control, management, monitoring, reporting and challenge of risk across the Group. It is designed to provide an integrated, comprehensive, consistent and scalable structure which is capable of being communicated to and clearly understood by all of the Group's employees and is described in the sections below.

The RMF also incorporates the organisational arrangements for managing risk with specific responsibilities distributed to certain functions. This ensures that there is clear accountability, responsibility and engagement at appropriate levels within the organisation which can provide robust review and challenge as well as be challenged. Operationally, the RMF is organised around the key risk categories (see page 100).

Governance

All of the Group's risk activities are subject to detailed and comprehensive governance arrangements which set out how risk-based authority is delegated from the Board to Executive Management and the various risk management committees and individuals. Risk governance and oversight is detailed further on the following page.

Culture

The Group is led by an experienced Executive Management team with a combination of significant underwriting expertise and institutional and regulatory banking experience at various major financial institutions and specialist lenders. This heritage provides the platform for a set of values and behaviour where the customer is at the heart of the decision-making process and business areas are held fully accountable for risk performance. At the individual level, this process begins with the induction programme and job descriptions, is carried into the setting of individual objectives and performance reviews and is ultimately reflected in the compensation and reward structure.

Risk governance and oversight

Risk governance describes the architecture through which the Board allocates and delegates primary accountability, responsibility and authority for risk management across the organisation.

Responsibility for risk oversight is delegated from the Board to the Risk Committee and Audit Committee. The ultimate responsibility for risk remains with the Board.

Accountability, responsibility and authority for risk management is delegated to the Chief Executive Officer and Chief Risk Officer, who in turn allocate responsibility for oversight and certain approvals across a number of management committees.

Authority and responsibility for material operational risk management, decision-making and risk assurance is vested in the Chief Risk Officer and the risk function. Lesser levels of authority are cascaded to the senior management within the support functions and business divisions.

The Group's key risk categories are detailed on page 100. Oversight of these key risk categories is illustrated below:

Oversight / Risk category	Board			
	Risk Committee			Audit Committee
	First line	Second line		Third line
Creditworthiness risk	Credit management in business divisions	Credit risk	Enterprise Risk Management Committee	Internal audit
Liquidity and market risk	Treasury	Market and liquidity risk	Asset and Liability Committee	Internal audit
Operational risk	All business divisions, functions, Chief Operating Office and Chief Technology Office	Operational risk	Enterprise Risk Management Committee	Internal audit
Conduct, legal and compliance risk	All business divisions	Compliance	Enterprise Risk Management Committee	Internal audit
Strategic risk	Executive Directors and Senior Management	Finance	Executive Committee	Internal audit
Systems and change risk	Chief Technology Office	Operational risk	Enterprise Risk Management Committee	Internal audit

These bodies and senior officers are accountable and responsible for ensuring that the day-to-day risks are appropriately managed within the agreed risk appetite and in accordance with the requirements of the RMF.

Individuals are encouraged to adopt an open and independent culture of challenge which is important in ensuring risk issues are fully surfaced and debated with views and decisions recorded. Risk governance and culture is reinforced by the provisions of the Senior Managers and Certification Regime.

Formal risk escalation and reporting requirements are set out in risk policies, individual committee terms of reference and the approved risk appetite thresholds and limits.

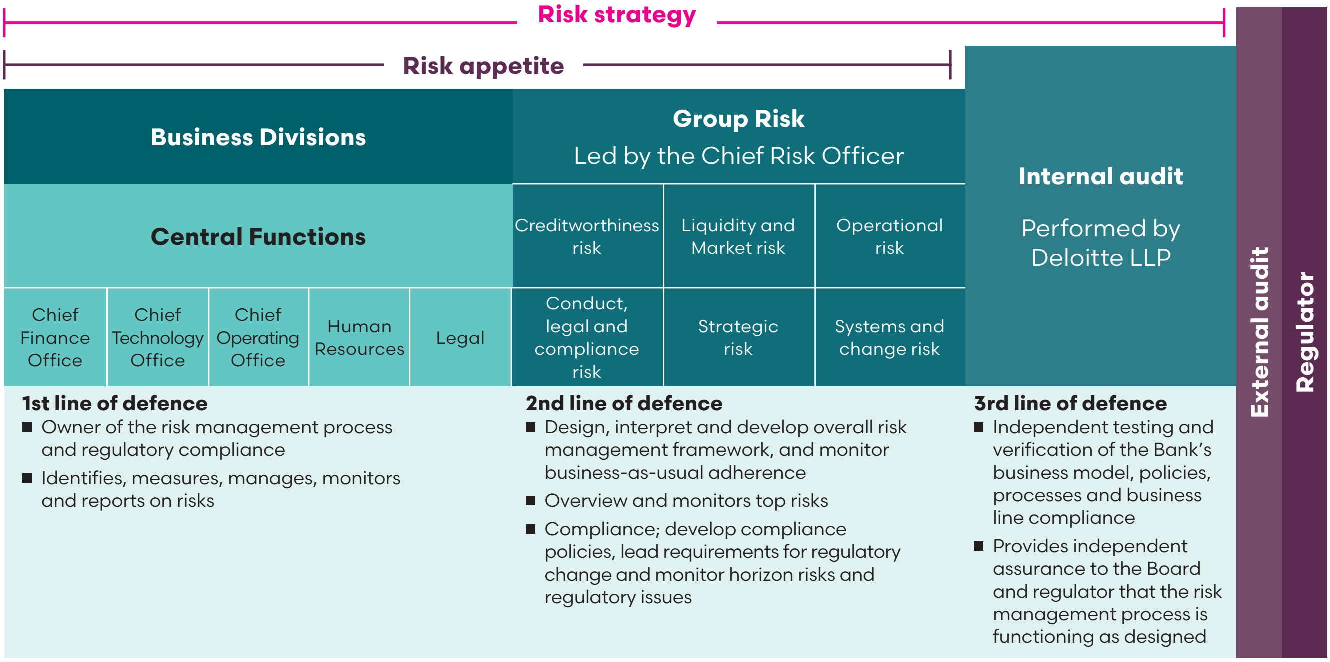
Risk governance and oversight

Committee structure and risk responsibilities

An abbreviated Board and Management Committee structure is set out in the Corporate Governance Report on pages 46 and 49. The monitoring and controlling of risk is a fundamental part of the management process within the Group. The Board oversees the management of the key risk categories across the organisation.

Three lines of defence model

The Group's RMF is underpinned by the 'three lines of defence' model which is summarised in the diagram below:



The Group implemented an organisational change in 2019 to reflect the importance of technology and operations to delivering the Group's objectives.

First line of defence

Responsibility for risk management resides in the frontline business divisions and central functions, and line management is directly accountable for identifying and managing the risks that arise in their business or functional area. They are required to establish effective controls in line with Group risk policy and act within the risk appetite parameters set and approved by the Board. The first line of defence comprises each of the three lending divisions. The first line of defence also includes the finance function led by the Chief Financial Officer, the operations function led by the Chief Operating Officer, the technology function led by the Chief Technology Officer, the human resources function led by the Group Human Resources Director and the legal function led by General Counsel and Company Secretary. Operational resiliency and outsourcing oversight is performed by the Chief Operating Officer and the Chief Technology Officer. Whilst the human resources and legal functions are not customer facing themselves, they provide support and back up to the customer facing divisions and have insight into many operational factors that could ultimately impact on Group's exposure to liquidity, market, credit, regulatory, legal, conduct, compliance and operational risk.

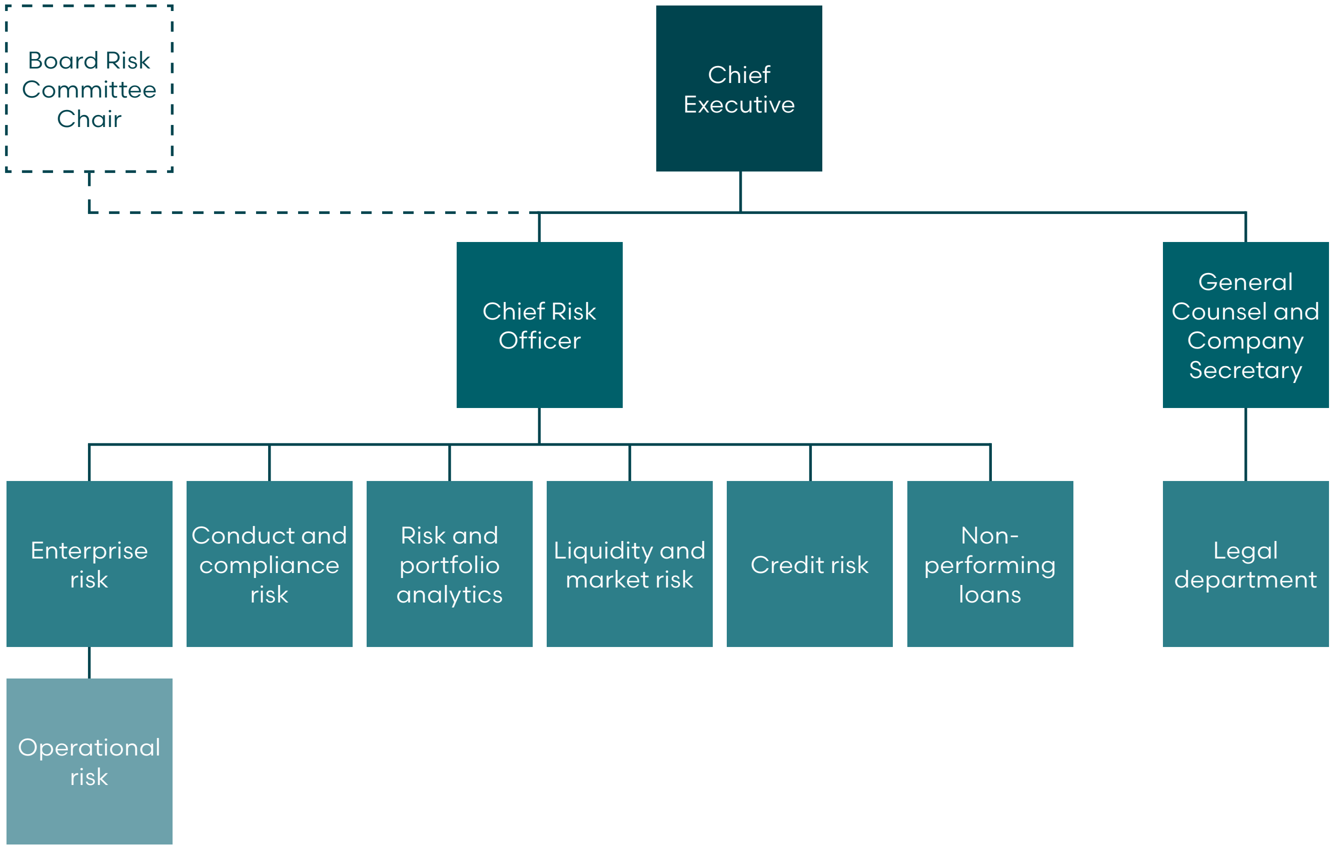
Each division and functional area operates to set risk policies to ensure that activities remain within the Board's stated risk appetite for that area of the Group. The risk policies are approved by the appropriate committee in accordance with their terms of reference and reviewed annually with any material changes requiring approval at committee level.

The first line of defence has its own operational process and procedures manuals to demonstrate and document how it conforms to the approved policies and controls. Likewise, it develops quality control programmes to monitor and measure adherence to and effectiveness of procedures. All employees within a customer facing unit are considered first line of defence. Each employee is aware of the risks to the Group of their particular activity and the divisional and function heads are responsible for ensuring there is a 'risk aware' culture within the first line of defence. For certain key policies, divisional employees complete regular online training programmes to ensure knowledge is refreshed and current.

Second line of defence

The second line of defence comprises the Group's central and independent risk management and compliance function led by the Chief Risk Officer, who reports to the Chair of the Risk Committee and to the Chief Executive Officer. The Chief Risk Officer is also provided with unfettered access to the Chairman of the Board. The second line of defence also includes the General Counsel and Company Secretary who report to the Chief Executive Officer.

The high-level risk structure is shown below:



The second line of defence is necessarily and deliberately not customer facing and has no responsibility for any business targets or performance. It is primarily responsible for:

- the design and build of the various components of the Group's RMF and embedding these, together with the risk strategy and risk appetite across the organisation;
- independent monitoring of the Group's activities against the Board's risk appetite and limits, and provision of monthly analysis and reporting on the risk portfolio to the Executive Committee and the Board;
- issuing and maintaining the suite of Group risk policies;
- undertaking physical reviews of risk management, controls and capability in the first line units and providing risk assurance reports to the Executive Committee and the Board on all aspects of risk performance and compliance with the RMF;
- providing advice and support to the first line of defence in relation to risk management activities;
- credit approvals between divisional authority and the threshold for Credit Approval Committee; and
- undertaking stress testing exercises and working with finance and treasury on the production of the Internal Capital Adequacy Assessment Process (ICAAP), Internal Liquidity Adequacy Assessment Process (ILAAP) and the Recovery Plan and Resolution Pack (collectively the RRP).

Risk governance and oversight

Third line of defence

The third line of defence, internal audit (currently outsourced to Deloitte LLP), provides independent assurance on the activities of the Group, effectiveness of the Group's RMF and internal controls directly to the Board and Audit Committee. Internal audit reports directly to the Chair of the Audit Committee as well as the Chief Executive Officer and is independent of the first and second lines of defence.

The third line of defence has access to the activities and records of both the first and second lines of defence. It can inspect and review adherence to policy and controls in the first line, the monitoring of activity in the second line and the setting of policy and controls in the second line. The third line of defence does not independently establish policy or controls itself, outside of those necessary to implement its recommendations with respect to the other two lines of defence. The third line may in some cases use as a starting point the reports and reviews compiled by the second line but is not restricted to them or necessarily influenced by their findings.

The third line of defence's scope of work is agreed with the Audit Committee to provide an independent assessment of the governance, risk management and internal control frameworks operated by the Group and to note the extent to which the Group is operating within its risk appetite. It does this by reviewing aspects of the control environment, key processes and specific risks and includes review of the operation of the second line of defence.

The Group's engagement of Deloitte LLP to carry out the functions of the third line of defence provides the Group with access to specialist capabilities beyond its current scale and provides insight into best practice.

Risk policies and controls

The RMF is enacted through a comprehensive suite of control documents and risk policies, setting out the minimum requirements and standards in relation to the acquisition and management of risk assets as well as the control of risks embedded in the Group's operations, activities and markets.

The Group's high level control documents and risk policies are owned and managed by the Group risk function, headed by the Chief Risk Officer and approved by the Board or, where delegated, the appropriate Risk Committee. The suite of policies is grouped according to importance and key risk categories.

Group level risk policies are supplemented as required by divisional risk processes and procedures, where more specific and tailored criteria are detailed. Divisional processes and procedures are required to be compliant with Group policy and dispensations or waivers are required where gaps are identified. These process and procedure manuals provide employees at all levels with day-to-day direction and guidance in the execution of their duties.

The effectiveness of and compliance with the risk policy framework is evaluated on a continuous basis through the monthly reporting requirements (including risk policy exceptions reporting). Additionally, a quarterly control self-certification process supplemented by a program of audits, thematic risk assurance reviews and quality control testing is undertaken by each of the three lines of defence.

Asset class policies

The Group controls its lending activities through 18 asset class policies and a further 13 lending policies. These have been arranged to operate on a Group wide basis rather than based upon divisional products. This is considered to provide a more stable, consistent risk standard and control across the Group's portfolio of loan assets. Asset classes can also be aligned more readily with risk-weightings, probability of default (PD), loss given default (LGD) and expected credit loss (ECL) metrics which facilitates risk reporting, risk adjusted profitability analysis and modelling for stress testing and capital adequacy purposes.

Asset class policies are structured on the basis of policy rules which must be adhered to and guidelines where an element of controlled discretion is permitted. All planned exceptions to policy rules require approval at the Group risk level and both planned and unplanned exceptions to policy rules are reported monthly to the relevant risk management committee.

Top and emerging risks

The Group's top and emerging risks are identified through the process outlined in the Risk Management Framework (see page 83) and are considered regularly by Management through the Enterprise Risk Management Committee and subsequently by the Risk Committee.

Top risks

The Group sees eight themes as its top risks:

- Geopolitical risk
- Economic and competitive environment
- Global pandemic risk
- Pace of regulatory change
- Intermediary, outsourcing and operational resiliency
- Pace, scale of change and people risk
- Credit impairment
- Information risk

Change in risk environment

- No change
- Risk decreased
- Risk increased
- New risk

These themes, together with the Group's strategy to mitigate the risk and the direction of each theme are considered further below:

Top risk	Mitigation	Change
Geopolitical risk The Group's financial position continues to improve with continued profitability and adequate capital ratios. However, increasing geopolitical risk presents a risk to the business, its financials and earnings volatility following an unprecedented political event. The UK has experienced a number of political events during 2019. Although the UK left the European Union (EU) on 31 January 2020, nothing has materially changed. The risk of a disorderly Brexit may have reduced, but there remains a risk arising from the future trading arrangements. These risks have the potential to have an impact on the Group and the impact could be wide reaching, affecting other risks such as economic, regulatory, business change, outsourcing, people, credit risk impairment and conduct risk.	The Group monitors the environment and its chosen markets on a regular basis and continues to prioritise return on tangible equity over volume. The Group operates in specialist areas where Management and employees have significant expertise and a deep understanding of customer needs, to drive a long-term relationship with its customers through the cycle. The Group undertakes a comprehensive assessment of its risk appetite and stress tests its lending and deposit portfolios to ensure that it can meet its objectives in severe but plausible economic conditions.	↔ (No change) The UK economic outlook is expected to remain favourable by historical standards but with increasing risks to the downside that may increase the potential for volatility for the Group and its customers. Developments regarding the UK's withdrawal from the EU, and in particular the reaction of households, businesses and asset prices to them, remain a significant influence on, and source of uncertainty about, the economic outlook.

Top and emerging risks

Top risk	Mitigation	Change
Economic and competitive environment A reversal in UK economic conditions, particularly in England where the majority of the Group's operations are based, could affect the Group's performance in a number of ways. These are set out below: ■ lower demand for the Group's products and services; ■ changes in funding costs resulting from ongoing political uncertainty accompanied by a loss of confidence in the market; ■ rising competition compressing Group margins below sustainable levels; and ■ higher impairments through increased defaults and/or reductions in collateral values.	The Group uses its expertise and deep understanding of its customers' needs to drive long-term relationships with its customers through the cycle. The Group monitors its chosen markets on a regular basis and during 2019 has decided to refocus on being the specialist small and medium enterprises (SME) lender of choice and has launched its first deposit account for SME's. The Group has divested its Shawbrook International Limited business and completed the divestment of a portfolio of unsecured personal loans from its Consumer Lending business in Q1 2020. The Group reviews adjacent markets where it has expertise and considers opportunities for inorganic growth that are consistent with its strategy. The Group operates in specialist areas where Management and employees have expertise and a deep understanding of customer needs to deliver superior service. As a result, loans to SMEs are subject to bespoke underwriting based on their ability to repay and sufficient security. The Group undertakes a comprehensive assessment of its risk appetite to ensure that it can meet its objectives in severe but plausible economic conditions. The Group completes comprehensive stress testing of its lending and deposit portfolios to test resilience to severe but plausible economic conditions. The Group also establishes a prudent balance sheet strategy with robust levels of capital and liquidity and a prudent funding structure.	↑ The UK economy has continued to be resilient during 2019 led by strong employment and conditions that continue to support affordability. However, the UK economy has narrowly avoided a recession in Q4 2019 and the Board expects there to be a continued period of uncertainty. As at 31 December 2019, the risk of a disorderly exit from the EU has reduced but there remains a risk arising from the nature of any future relationship with the EU. The outbreak of coronavirus (Covid-19) has now been labelled a global pandemic by the World Health Organization. If it continues to spread, it is likely to further intensify the disruptive impact on the global and UK economy resulting in falling investment and consumer spending and deteriorating market sentiments. Government actions, both fiscal and monetary, may prove to be slow to take effect and/or uncertain in their impact.

Top risk	Mitigation	Change
Global pandemic risk The outbreak of coronavirus (Covid-19) has been labelled a global pandemic by the World Health Organization and is creating disruption to the global economy. In the UK it has initially resulted in market volatility and is impacting investment through: ■ lost output because of reduced movement and dislocation in supply chains; ■ lower productivity because of travel restrictions, social distancing, self-isolation and sickness; ■ impact on employment levels, particularly for self-employed; ■ reduced consumer spending and business investment; and ■ impact on other relevant macroeconomic variables including residential and commercial property prices, interest rates and size of key markets.	The Group has taken a considered approach to minimising and managing the impact of a coronavirus related global pandemic. The Group has implemented its Incident Management Plan and has been successfully operating with the majority of employees working from home. The Group has complied with all the latest government guidance, best practice and has implemented an operating structure to ensure that the Group can deliver a sustainable service to its customers, whilst taking care of the health of its employees and families. The Group has undertaken an assessment of the risks associated with a Covid-19 pandemic scenario in a stress test to understand the impacts on its key operating divisions and third parties.	The Group has assessed the Covid-19 risk relative to the Bank of England 'Rates Down' scenario, which is used to ensure the Bank's viability through the Group's ICAAP. Based on current information available to the Group, the Board believes that the severity of the financial risks of Covid-19 are contained within, and are not as severe as, the 'Rates Down' scenario. The potential impact of the Covid-19 pandemic on the economy and the Group's operational resilience and risk appetite is subject to continuous monitoring through the Group's management committees and business continuity planning working group, with appropriate escalation to the Board and supervisory authorities.

Top and emerging risks

Top risk	Mitigation	Change
Pace of regulatory change The prudential and conduct regulatory regimes are subject to change and could lead to increases in the level and quality of capital that the Group needs to hold to meet regulatory requirements. The Financial Policy Committee (FPC) reduced the countercyclical buffer from 1% to 0% with effect from March 2020 as part of a number of special measures in response to the coronavirus pandemic and announced that it would not expect to increase the countercyclical buffer until March 2022. The Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) have undertaken a number of thematic reviews during 2019.	The regulatory environment continues to evolve and change. The Group actively engages with regulators, industry bodies and advisors to actively engage in consultation processes. The Group actively reviews regulatory publications to assess their implications for the business and oversees the impact analysis through its Regulatory Change Working Group. The Group undertakes forward capital planning and sensitivity analysis using its ICAAP to ensure that the Group has sufficient time to respond to any changes in capital requirements. The Group believes that the financial risks of Covid-19 are contained within, and are not as severe as, the Bank of England prescribed 'Rates Down' scenario.	UK financial services businesses remain subject to significant scrutiny and the current level of risk is elevated when compared to last year. The Group adopts the standardised approach to credit risk. The Basel Committee on Banking Supervision announced changes to the risk-weightings under the standardised approach in December 2017 that will lead to an increase in capital requirements over the period of the strategic plan. The Group was included in the PRA thematic review of Fast Growing Firms and has invested in addressing material observations by the 31 December 2019. The Group submitted its Climate Change Plan in October 2019 to the PRA and has submitted its responses to consultations on the retail banking review and the SME banking review. The Group also submitted its plans to manage the migration from London Inter-Bank Offered Rate (LIBOR) to the PRA in December 2019.

Top risk	Mitigation	Change
Intermediary, outsourcing and operational resiliency The Group is a specialist lending and savings bank for SMEs and consumers. The specialist nature of some of its lending through intermediaries and brokers could mean that some customers find themselves with an increased risk of an unfavourable outcome. For the Group this could also lead to increased conduct related redress, additional fraud or credit risk impairments. The Group uses a number of third parties to support the delivery of its objectives. The availability and resiliency of its core customer facing systems play a key role in supporting the Group's reputation in its chosen markets.	The Group works with carefully selected intermediary and broker partners who take on the role of advising SMEs and consumers. The Group recognises that it is ultimately accountable for the lending it originates through its partners and continually undertakes reviews of their performance. The Group continually reviews its risk management approach to intermediaries, brokers and outsource partners to reflect the regulatory environment in which the Group operates.	The Group has continued to invest in its oversight of intermediaries, brokers and outsource partners during 2019. The Group continued to invest in its relationship with Target Servicing Limited and expects to further improve the Group's outsourcing risk profile. This includes (but is not limited to) work on financial crime, arrears management, forbearance and resiliency planning. The Group continues to explore other third party relationships through which to deliver its objectives and improve operational resiliency including the use of Cloud technologies and specialist risk providers. The Group appointed a Head of Operational Resiliency in 2019 reporting to the Chief Operating Officer to oversee the Group's approach to operational resiliency.

Top and emerging risks

Top risk	Mitigation	Change
Pace, scale of change and people risk The scale and pace of change could create delivery challenges and could lead to disruption of the Group's plans and in the delivery of its objectives. The Group is a diverse specialist lending and savings bank and has a need to deliver a significant number of projects over the plan to deliver its objectives. Failure to deliver the required change may lead to a disruption in the delivery of its objectives.	The Group understands the need to manage change without disrupting the Group's operating environment and impacting customer service. The Group has further updated its change prioritisation process in 2019 to prioritise change and has increased its capability in agile working to ensure that requirements are delivered on time and within budget.	↑ The Group continues to invest in its change management processes to increase the pace and scale of change without impacting on the Group's operations and customer service. The Group continues to invest in its leadership community through an 'Inspire' leadership programme and has focused on the actions arising from its people engagement surveys and regular reviews of the succession and talent management plans.

Top risk	Mitigation	Change
Credit impairment As at 31 December 2019, the Group had customer loans (including operating leases and loans held for sale and net of loss allowances) of £6.8 billion and is exposed to credit impairment if customers are unable to repay loans and any outstanding interest and fees. In addition, the Group has exposure to a small number of counterparties with whom it places surplus funding.	The Group recognises that it will experience credit impairment in connection with its lending activities, but manages its exposure by: ■ undertaking a prudent assessment of through-the-cycle losses in pricing, forecasting and stress testing; ■ maintaining consistent and conservative loan to value ratios and avoiding material weakening of credit quality to drive volumes; ■ lending predominantly on a secured basis against identifiable and accessible assets; ■ operating strong controls and governance with effective oversight by a centralised Group credit team; and ■ maintaining a prudent treasury counterparty policy with surplus funding placed with the Bank of England and UK clearing banks.	↑ Underlying Group credit impairment has remained low by historical standards, reflecting favourable market conditions in the UK and the Group's approach to lending. The Group's counterparty exposure has remained broadly unchanged with the majority of surplus funding placed with the Bank of England and balances with UK clearing banks. The Group believes that the potential for additional credit impairment has increased with the outlook for the UK economy given recent forecasts and the potential impact of the coronavirus pandemic.

Top and emerging risks

Top risk	Mitigation	Change
Information risk The pace of technological development is changing the way in which SMEs and consumers want to engage with the Group, leading to a number of risks. These are set out below: ■ increasing customer demand could exceed the Group's ability to provide highly reliable and widely available systems and services; ■ the evolving nature and scale of criminal activity could increase the likelihood and severity of attacks on the Group's systems; and ■ franchise value and customer trust could be significantly eroded by a sustained hack of the Group's systems leading to a diversion of funds or the theft of customer data.	The Group continually reviews its control environment for information security to reflect the evolving nature of the threats to which the Group is exposed. The Group's strategy for mitigating information security risk is comprehensive, including: a documented cyber strategy, ongoing threat assessments, regular penetration testing, the wide deployment of detective controls and a programme of education and training. The Group continues to invest in its technology layer including the use of Cloud computing resources to improve resiliency and the implementation of additional controls to support the security of its core systems. This includes investment in asset management and investment in additional external resources to support systems that are approaching the end of their support.	↑ The Group appointed a Chief Information Security Officer in 2019 and has continued to invest in its capabilities to reduce its exposure to a cyber-attack and plans to adopt ISO27001 to further refine its risk appetite and controls with respect to information security. However, the risk of information security breaches, threats from cyber-crime and the impact of new technology on the Group's businesses remain.

UK withdrawal from the EU

The UK left the EU on 31 January 2020. As the Group's business model is primarily focused in the UK, the Group has very limited direct exposure to the EU. However, the Group is exposed to secondary impacts, particularly volatility in the UK economy and financial markets given the uncertain nature of both the implementation period and the future relationship between the UK and the EU. The Group has considered a number of potential outcomes, including ultimately leaving without a deal at the end of the transition period, through its stress testing programme and in its preparations for alternative economic outcomes. The Group continues to closely monitor and analyse political, economic and regulatory developments to ensure it remains well positioned to respond to any potential shocks and minimise any disruption for customers and employees. Brexit is included as one of the Group's emerging risks in the following section.

Coronavirus (Covid-19) assessment

The outbreak of coronavirus has been labelled a global pandemic by the World Health Organization. The Group has implemented its Incident Management Plan and has been successfully operating with the majority of employees working from home. The Group has complied with all the latest government guidance, best practice and has implemented an operating structure to ensure that the Group can deliver a sustainable service to its customers, whilst taking care of the health of its employees and families. The Group has good coverage of VPN and Citrix connections for its employees to access its core systems, with performance of these connections monitored by the Chief Technology Officer and escalated as appropriate.

The Group's key operating divisions have focussed on serving the needs of its existing customers and welcomes the rapid actions taken by the Bank of England and the UK government to support SME's and consumers. The key risks to the Consumer Lending division have been reduced following the placement of a portfolio of loans as held for sale in December 2019, which has left the Group with a relatively small portfolio of unsecured personal loans. The key residual risks to the Consumer Lending division relate to the solvency of suppliers within the home improvement and holiday ownership sectors, where the division has Section 75 exposure. In the Property Finance division, short-term risks relate to exposure to short-term lending and the refinance risk at the end of the loan agreement. The Property Finance division has significant exposure to buy-to-let customers where the risks relate to property prices and unemployment. In Business Finance, the key areas of emerging risk are exposure to the taxi, marine, aviation and leisure sectors within specialist asset finance.

The Group has assessed the Covid-19 risk relative to the Bank of England 'Rates Down' scenario, which is used to ensure the Bank's viability through the Group's ICAAP. Based on current information available to the Group, the Board believes that the severity of the financial risks of Covid-19 are contained within, and are not as severe as, the 'Rates Down' scenario. The Covid-19 scenarios take into consideration the following drivers and implications relevant to a pandemic crisis:

- government guidance and fiscal policy response to the crisis;
- Bank of England monetary response to the crisis;
- PRA and FPC prudential response to the crisis (specifically guidance provided on 20 March 2020 to remind firms that forward looking information used in ECL estimates needs to be both reasonable and supportable and that the PRA believes that there is very little of such information available as yet, but in any event, the PRA expects firms to reflect the temporary nature of this shock and fully take into account the significant economic support measures already announced by global fiscal and monetary authorities);
- lost output and productivity because of travel restrictions, social distancing, self-isolation and sickness;
- impact on employment levels, particularly for self-employed and flexible working segments of the labour force;
- implication for consumer spending and business investment; and
- impact on other relevant economic variables, including residential and commercial property prices, Bank of England base rate, national output and lending volumes.

The Covid-19 scenarios are designed to be extreme, but plausible, based on the assumption that the impact on the UK economy is immediate and quickly feeds through into a sharp fall in output (GDP), rising unemployment rates but from a low base by historical standards, a short-term softening of residential and commercial property prices and a slowdown in demand for lending. The Treasury and Bank of England take proactive fiscal and monetary stimulatory actions, but given the invasive nature of the pandemic, the UK economy does not show signs of recovery until 2021.

The potential impact of the Covid-19 pandemic on the economy and the Group's operational resilience and risk appetite is subject to continuous monitoring through the Group's management committees and business continuity planning working group, with appropriate escalation to the Board and supervisory authorities.

Top and emerging risks

Emerging risks

The Group has identified five emerging risks:

- Brexit
- Climate change
- Minimum requirements for own funds and eligible liabilities funding requirements
- LIBOR transition
- Financial crime

Each emerging risk, together with the Group's strategy to mitigate the risk, is detailed on the following pages:

Emerging risk	Mitigation
Brexit The UK left the EU on 31 January 2020. Although the risk of a disorderly Brexit has reduced, there remains the back stop of a disruptive Brexit following the discussions on the future trading relationship. The Group does not have operations outside of the UK so the key risk is considered to be a downturn in the UK economy. Although the imminent risk of a disorderly Brexit may have reduced there is a risk that a disruptive Brexit may occur in the event that the UK is not able to negotiate a suitable trading relationship with the EU. In the event of a disruptive Brexit, the availability of skilled workers or ability to export goods to the EU at competitive prices may impact some of the Group's customers.	The Group has retained an alternative downside scenario based on a disorderly no-deal Brexit. The scenario is based on a significant reduction in investment which helps to move the UK into a recession, increasing unemployment. In the short-term, the consumer price index remains elevated before deflationary pressures on sterling and gross domestic product start to reduce the consumer price index, presenting an opportunity for the Monetary Policy Committee to reduce interest rates. The Group has considered the first order impacts on its strategy arising from a fall in investment that may lead to a reduction in demand for its lending products and that may impact the Group's ability to grow in its SME markets. It has also considered the impact of a fall in residential and commercial property prices within its Property Finance division and the impact of an increase in default in its Consumer Lending division following an increase in unemployment. The Group considers that the current alternatives fall within its current stress testing scenarios and has considered through its ICAAP the impact on its key suppliers.

Emerging risk	Mitigation
Minimum requirements for own funds and eligible liabilities (MREL) funding requirements MREL is an EU regulation that supports orderly resolution and protects depositors and taxpayers in the event of bank failure. The Group is currently not considered in scope however, over time the Group may fall in scope for more complex resolution strategies and going concern requirements.	The Group actively monitors its position in relation to MREL and as part of its strategic decision-making. The Group will engage with the PRA during its strategic planning process to understand the point that the Group may face additional MREL requirements to ensure that the Group has plenty of time to prepare.

Emerging risk	Mitigation
Financial crime The risk of a downturn in the UK economy could result in an increased risk of financial crime activity.	The Group is enhancing its expertise in the first line of defence to ensure a continued focus on strategy and regulatory compliance. In addition, the Group is working with external parties to identify new tools to support the automation of its customer due diligence processes.

Top and emerging risks

Emerging risk	Mitigation
Climate change On 15 April 2019 the PRA published Policy Statement PS11/19 & Supervisory Statement SS3/19 both titled "Enhancing banks' and insurers' approaches to managing the financial risks from climate change" requiring Shawbrook to form a Climate Change Plan focused on: ■ the embedding of the consideration of financial risks from climate change in governance arrangements; ■ the incorporation of financial risks from climate change into the existing financial risk management practice; ■ the use of (long-term) scenario analysis to inform strategy setting, risk assessment and risk identification; and ■ the development of an approach to disclosure on the financial risks from climate change.	The Group has appointed the Chief Risk Officer as the responsible executive to oversee the embedding of climate related matters and has moved to include climate change risk within its Risk Management Framework. The Group submitted its Climate Change Plan to the regulator on 10 October 2019 and is currently working with UK Finance and other leading suppliers of climate analysis in order to develop the Group's risk appetite.

Emerging risk	Mitigation
LIBOR transition The Group like other firms supervised in the UK are required to transition away from LIBOR to alternative interest rate benchmarks ahead of the end of 2021. The Group must make sure that its customers are managed through the transition in good time to manage good customer outcomes and that new contracts are linked to alternative rates in good time.	The Group has appointed the Chief Financial Officer as the responsible executive and a LIBOR working group, reporting through to the Chief Financial Officer, has been formed. This working group manages the Group's assessment of the alternative rates for its lending divisions and the transition plan for both new and existing customers in advance of the end of 2021.

Key risk categories

The key risk categories faced by the Group are set out in the table below. Oversight of the Group's key risk categories is outlined on page 84.

Risk category	Definition	Further details
Creditworthiness risk *(Audited)*[1]	Creditworthiness risk is the risk that a borrowing client or treasury counterparty fails to repay some or all of the capital or interest advanced to them due to lack of willingness to pay (credit risk) and/or lack of ability to pay (affordability). The creditworthiness risk category also includes credit concentration risk, which is the risk of exposure to particular groups of customers, sectors or geographies that, uncontrolled, may lead to additional losses that the Shareholder or the market may not expect.	See page 101
Liquidity risk *(Audited)*[1]	Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due, or is only able to do so at excessive cost.	See page 125
Market risk *(Audited)*[1]	Market risk is the risk of financial loss through unhedged or mismatched asset and liability positions that are sensitive to changes in interest rates or currencies.	See page 129
Operational risk	Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and system failures, or from external events including strategy and reputational risks.	See page 134
Conduct, legal and compliance risk	Conduct risk is the risk that the Group's behaviour will result in poor customer outcomes and that the Group's people fail to behave with integrity. Legal and compliance risk is the risk of regulatory enforcement and sanction, material financial loss, or loss to reputation the Group may suffer as a result of its failure to identify and comply with applicable laws, regulations, codes of conduct and standards of good practice.	See page 134
Strategic risk	Strategic risk is the risk that the Group is unable to meet its objectives through the inappropriate selection or implementation of strategic plans. This includes the ability to generate lending volumes within the Group's risk appetite.	See page 134
Systems and change risk	Systems risk is the risk that new threats are introduced to the Group's critical systems resulting in them becoming unavailable during core operational times. Change risk is the risk that transition changes in the business will not be supported by appropriate change capability and be improperly implemented. It is also the risk that too many in-flight changes cause disruption to business operations.	See page 134

[1] Disclosures relating to this key risk category are covered by the Independent Auditor's Report.

Key risk categories

Creditworthiness risk

Audited: *The following section is covered by the Independent Auditor's Report.*

Creditworthiness risk is managed by the Enterprise Risk Management Committee and the Asset and Liability Committee.

The main components of creditworthiness risk are customer credit risk (from core lending activity) and treasury credit risk (from treasury activity). The Group's treasury credit risk exposure is limited to short-term deposits placed with leading UK banks and high quality covered bonds purchased for inclusion in the Group's liquid asset buffer. Treasury credit risk associated with any reverse repo or derivative transactions is mitigated by high quality collateral.

(a) Credit risk approval process

The Group operates a hierarchy of lending authorities based principally upon the size of the aggregated credit risk exposure to counterparties, group of connected counterparties or, where applicable, a portfolio of lending assets that are subject to a single transaction. In addition to maximum amounts of credit exposure, sole lending mandates may stipulate sub-limits and/or further conditions and criteria.

Each division has a maximum authority level allocated, with exposures above these levels requiring approval from an approver in the second line of defence or the Credit Approval Committee. In each lending division, at least one signatory to the loan must be a segregated first line of defence credit approver who has no responsibility for, or remuneration arrangements linked to, sales targets, ongoing sales origination or relationship responsibility with the borrower. The Board approved a change to the credit approval process in December 2019 that will result in all credit approval authorities transferring out of the Business Finance and Property Finance divisions from 1 February 2020. The transfer of the remaining limited delegations inside the Consumer Lending division will take place by 31 March 2020.

The maximum divisional mandate for Business Finance and commercial mortgages in Property Finance during 2019 was £1.25 million. The maximum divisional mandate during 2019 for residential mortgages in Property Finance was £100,000 and for Consumer Lending was £75,000. Exposures beyond these limits up to £5 million may be approved by an approver in the second line of defence and exposures up to the Group single name concentration limit of £25 million must be approved by the Credit Approval Committee. The Group has a nominal appetite for wholesale exposures above £25 million within the lending authority of the Credit Approval Committee. In addition, where transactions involve financing portfolios of lending assets in excess of £15 million, or where an individual loan is required in excess of appetite, Board approval is also required.

Lending is advanced subject to the Group lending approval policy and specific credit criteria. When evaluating the credit quality and covenant of the borrower, significant emphasis is placed on the nature of the underlying collateral. This process also includes the review of the Board's appetite for concentration risk.

The Group is a responsible lender and consumer affordability has remained a key area of focus for the Group. The Group's approach to affordability is set out in a Board approved responsible lending policy that is embedded within each lending division's lending guides.

(b) Credit monitoring

Approval and ongoing monitoring control is exercised both within the divisions and through oversight by the Group's credit risk function. This applies to both individual transactions, as well as at the portfolio level, by way of monthly credit information reporting, measurement against risk appetite limits and testing via risk quality assurance reviews.

The divisions operate collections and arrears management processes through the Chief Operating Office function. In 2019, the Group further invested in the development of new collections strategies for its Consumer Lending division and residential mortgage portfolio within the Property Finance division to ensure that the Group is well positioned for a more challenging environment.

(c) Impairment of financial assets

In accordance with the Group's accounting policy (Note 1.7(x) of the Financial Statements), impairment of financial assets is calculated using a forward looking expected credit loss (ECL) model. ECLs are an unbiased probability-weighted estimate of credit losses determined by evaluating a range of possible outcomes.

The Group calculates ECLs and records a loss allowance for all financial assets not held at fair value through profit or loss, together with financial guarantee contracts and loan commitments.

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

- **Stage 1:** when a financial asset is first recognised it is assigned to Stage 1. If there is no significant increase in credit risk from initial recognition the financial asset remains in Stage 1. Stage 1 also includes financial assets where the credit risk has improved and the financial asset has been reclassified back from Stage 2. For financial assets in Stage 1, a 12-month ECL is recognised.
- **Stage 2:** when a financial asset shows a significant increase in credit risk since initial recognition (SICR) it is moved to Stage 2. Stage 2 also includes financial assets where the credit risk has improved and the financial asset has been reclassified back from Stage 3. For financial assets in Stage 2, a lifetime ECL is recognised.
- **Stage 3:** when there is objective evidence of impairment and the financial asset is considered to be in default, or otherwise credit-impaired, it is moved to Stage 3. For financial assets in Stage 3, a lifetime ECL is recognised.

In relation to the above:

- Lifetime ECL is defined as ECLs that result from all possible default events over the expected behavioural life of a financial instrument.
- 12-month ECL is defined as the portion of lifetime ECL that will result if a default occurs in the 12 months after the reporting date, weighted by the probability of that default occurring.

For financial guarantee contracts, the Group assigns a stage using the definitions described above.

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

The following sections set out further analysis of the Group's loss allowance, details regarding the calculation of ECLs and an assessment of the critical accounting judgements and estimates associated with the impairment of financial assets.

Analysis of the Group's loss allowance

The Group calculates ECLs for its financial assets not held at fair value through profit or loss. This includes: cash and balances at central banks, loans and advances to banks, loans and advances to customers and investment securities. The Group also calculates ECLs for its financial guarantee contracts and loan commitments.

In the year ended 31 December 2019, the Group also has a portfolio of loans classified as held for sale (see Note 23 of the Financial Statements). These loans are separately presented in the Group's statement of financial position as assets held for sale and are not included in the balance of loans and advances to customers. The loans continue to be measured at amortised cost, with a loss allowance recognised.

Further analysis of the loss allowance in respect of the Group's financial assets, financial guarantee contracts and loan commitments are provided in the following sections.

Cash and balances at central banks, loans and advances to banks and investment securities

The loss allowances for cash and balances at central banks, loans and advances to banks and investment securities are immaterial, totalling less than £0.1 million in both reported years.

Creditworthiness risk continued

Loans and advances to customers

The loss allowance for loans and advances to customers is £61.1 million (2018: £67.8 million).

The following tables provide an analysis of loans and advances to customers by reportable segment and the year-end stage classification:

As at 31 December 2019	**Property Finance £m**	**Business Finance £m**	**Consumer Lending £m**	**Total £m**
Stage 1	**3,813.9**	**1,486.6**	**547.3**	**5,847.8**
Stage 2	**538.3**	**134.7**	**43.6**	**716.6**
Stage 3	**89.0**	**29.1**	**7.5**	**125.6**
Gross carrying amount	**4,441.2**	**1,650.4**	**598.4**	**6,690.0**
Stage 1	**(3.7)**	**(8.8)**	**(8.1)**	**(20.6)**
Stage 2	**(2.7)**	**(3.8)**	**(7.7)**	**(14.2)**
Stage 3	**(8.1)**	**(12.9)**	**(5.3)**	**(26.3)**
Loss allowance	**(14.5)**	**(25.5)**	**(21.1)**	**(61.1)**
Carrying amount[1]	**4,426.7**	**1,624.9**	**577.3**	**6,628.9**
Loss allowance coverage				
Stage 1	**0.1%**	**0.6%**	**1.5%**	**0.4%**
Stage 2	**0.5%**	**2.8%**	**17.7%**	**2.0%**
Stage 3	**9.1%**	**44.3%**	**70.7%**	**20.9%**
Total loss allowance coverage	**0.3%**	**1.5%**	**3.5%**	**0.9%**

As at 31 December 2018	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
Stage 1	3,051.5	1,179.7	690.8	4,922.0
Stage 2	607.8	188.5	75.3	871.6
Stage 3	60.6	54.0	6.6	121.2
Gross carrying amount	3,719.9	1,422.2	772.7	5,914.8
Stage 1	(2.0)	(5.9)	(15.6)	(23.5)
Stage 2	(5.5)	(4.0)	(11.2)	(20.7)
Stage 3	(6.2)	(13.0)	(4.4)	(23.6)
Loss allowance	(13.7)	(22.9)	(31.2)	(67.8)
Carrying amount[1]	3,706.2	1,399.3	741.5	5,847.0
Loss allowance coverage				
Stage 1	0.1%	0.5%	2.3%	0.5%
Stage 2	0.9%	2.1%	14.9%	2.4%
Stage 3	10.2%	24.1%	66.7%	19.5%
Total loss allowance coverage	0.4%	1.6%	4.0%	1.1%

The following tables provide an analysis of loans and advances to customers by type and the year-end stage classification:

As at 31 December 2019	**Loan receivables £m**	**Finance lease receivables £m**	**Instalment credit receivables £m**	**Total £m**
Stage 1	**5,437.2**	**66.4**	**344.2**	**5,847.8**
Stage 2	**680.7**	**5.5**	**30.4**	**716.6**
Stage 3	**108.7**	**9.1**	**7.8**	**125.6**
Gross carrying amount	**6,226.6**	**81.0**	**382.4**	**6,690.0**
Stage 1	**(16.8)**	**(1.0)**	**(2.8)**	**(20.6)**
Stage 2	**(12.1)**	**(0.3)**	**(1.8)**	**(14.2)**
Stage 3	**(18.5)**	**(5.1)**	**(2.7)**	**(26.3)**
Loss allowance	**(47.4)**	**(6.4)**	**(7.3)**	**(61.1)**
Carrying amount[1]	**6,179.2**	**74.6**	**375.1**	**6,628.9**
Loss allowance coverage				
Stage 1	**0.3%**	**1.5%**	**0.8%**	**0.4%**
Stage 2	**1.8%**	**5.5%**	**5.9%**	**2.0%**
Stage 3	**17.0%**	**56.0%**	**34.6%**	**20.9%**
Total loss allowance coverage	**0.8%**	**7.9%**	**1.9%**	**0.9%**

As at 31 December 2018	Loan receivables £m	Finance lease receivables £m	Instalment credit receivables £m	Total £m
Stage 1	4,470.2	77.4	374.4	4,922.0
Stage 2	834.9	8.1	28.6	871.6
Stage 3	105.3	9.5	6.4	121.2
Gross carrying amount	5,410.4	95.0	409.4	5,914.8
Stage 1	(20.5)	(0.5)	(2.5)	(23.5)
Stage 2	(18.3)	(1.1)	(1.3)	(20.7)
Stage 3	(15.3)	(5.6)	(2.7)	(23.6)
Loss allowance	(54.1)	(7.2)	(6.5)	(67.8)
Carrying amount[1]	5,356.3	87.8	402.9	5,847.0
Loss allowance coverage				
Stage 1	0.5%	0.6%	0.7%	0.5%
Stage 2	2.2%	13.6%	4.5%	2.4%
Stage 3	14.5%	58.9%	42.2%	19.5%
Total loss allowance coverage	1.0%	7.6%	1.6%	1.1%

[1] Excludes fair value adjustments for hedged risk.

Key risk categories

Creditworthiness risk continued

The reduction in total loss allowance coverage from 1.1% as at 31 December 2018 to 0.9% as at 31 December 2019 is primarily due to:

- an increase in lending in the Property Finance division which has a lower loss allowance coverage; and
- a reduction in Consumer Lending which has a higher loss allowance coverage. This is as a result of lower loan originations as the division implemented its new credit strategy and the transfer of a portfolio of unsecured personal loans to assets held for sale.

The following table provides an analysis of movements during the year in the loss allowance associated with loans and advances to customers:

				2019				2018
	Stage 1 £m	**Stage 2 £m**	**Stage 3 £m**	**Total £m**	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
As at 1 January	**23.5**	**20.7**	**23.6**	**67.8**	10.5	7.5	13.6	31.6
Impact of adopting IFRS 9	**–**	**–**	**–**	**–**	6.8	5.0	9.3	21.1
Restated balance as at 1 January	**23.5**	**20.7**	**23.6**	**67.8**	17.3	12.5	22.9	52.7
ECL charge for the year								
Transfer to Stage 1	**7.2**	**(6.3)**	**(0.9)**	**–**	4.3	(3.8)	(0.5)	–
Transfer to Stage 2	**(1.6)**	**1.9**	**(0.3)**	**–**	(1.4)	3.2	(1.8)	–
Transfer to Stage 3	**(2.1)**	**(6.0)**	**8.1**	**–**	(0.8)	(2.7)	3.5	–
New financial assets originated or purchased	**8.4**	**0.3**	**0.2**	**8.9**	13.2	1.3	0.5	15.0
Financial assets that have been derecognised	**(0.6)**	**(0.7)**	**(2.3)**	**(3.6)**	(3.2)	(1.8)	(3.9)	(8.9)
Changes in credit risk	**(7.9)**	**6.0**	**14.0**	**12.1**	(5.8)	11.4	11.1	16.7
Modifications without derecognition	**(0.7)**	**0.2**	**4.6**	**4.1**	(0.1)	0.6	2.9	3.4
Write-offs	**–**	**–**	**(18.9)**	**(18.9)**	–	–	(11.1)	(11.1)
Total ECL charge for the year	**2.7**	**(4.6)**	**4.5**	**2.6**	6.2	8.2	0.7	15.1
Loss allowance derecognised on disposal of subsidiary	**(0.3)**	**(0.3)**	**(0.2)**	**(0.8)**	–	–	–	–
Loss allowance transferred to assets held for sale	**(5.3)**	**(1.6)**	**(1.6)**	**(8.5)**	–	–	–	–
Total movement in loss allowance	**(2.9)**	**(6.5)**	**2.7**	**(6.7)**	6.2	8.2	0.7	15.1
As at 31 December	**20.6**	**14.2**	**26.3**	**61.1**	23.5	20.7	23.6	67.8

Total loss allowance decreased by £6.7 million in the year ended 31 December 2019. In the same period, the gross carrying amount of loans and advances to customers increased by £775.2 million, from £5,914.8 million to £6,690.0 million.

Movements in the gross carrying amount of loans and advances to customers that contributed to the changes in the loss allowance during the year include:

- Gross new lending of £5,529.4 million was extended. This includes new originations, increases in lending and drawdowns on revolving credit facilities.
- A portfolio of property loans totalling £137.9 million was acquired.
- Gross principle repayments of loan balances were £4,727.0 million. This includes repayments of revolving credit facilities.
- The Group continued to operate a simultaneous charge-off and write-off policy during 2019. Loan balances of £29.5 million were written off with an associated £18.9 million reduction in the loss allowance.
- Loans with a gross carrying amount of £28.6 million were derecognised on disposal of Shawbrook International Limited with an associated £0.8 million reduction in the loss allowance.
- Loans with a gross carrying amount of £112.6 million and loss allowance of £8.5 million were transferred to assets held for sale.

Movements in the gross carrying amount of loans between stages during the year ended 31 December 2019 are as follows:

	Stage 1 £m	Stage 2 £m	Stage 3 £m
Transfer to Stage 1	384.0	(381.8)	(2.2)
Transfer to Stage 2	(472.2)	475.5	(3.3)
Transfer to Stage 3	(54.5)	(32.8)	87.3

Assets held for sale
The loss allowance in respect of the portfolio of unsecured personal loans classified as held for sale is £8.5 million. These loans are separately presented in the Group's statement of financial position as assets held for sale and are not included in the loans and advances to customers balance.

The following table provides an analysis of the loans classified as held for sale by year-end stage classification:

As at 31 December 2019	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Gross carrying amount	106.6	3.1	2.9	112.6
Loss allowance	(5.3)	(1.6)	(1.6)	(8.5)
Carrying amount	101.3	1.5	1.3	104.1
Total loss allowance coverage	5.0%	51.6%	55.2%	7.5%

Financial guarantee contracts
The loss allowance for financial guarantee contracts is £nil in both reported years because the contract is fully collateralised through a first fixed charge over a blocked deposit account. As such, the amount the Group should have to pay should the guarantee be called upon is £nil.

Key risk categories

Creditworthiness risk continued

Loan commitments
The loss allowance for loan commitments is £1.0 million (2018: £1.0 million).

The following tables provide an analysis of loan commitments by reportable segment and the year-end stage classification:

As at 31 December 2019	**Property Finance £m**	**Business Finance £m**	**Consumer Lending £m**	**Total £m**
Stage 1	213.7	341.8	30.4	585.9
Stage 2	–	5.6	–	5.6
Gross loan commitments	213.7	347.4	30.4	591.5
Stage 1	–	(1.0)	–	(1.0)
Loss allowance	–	(1.0)	–	(1.0)
Total loan commitments	213.7	346.4	30.4	590.5
Loss allowance coverage				
Stage 1	–	0.3%	–	0.2%
Total loss allowance coverage	–	0.3%	–	0.2%

As at 31 December 2018	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
Stage 1	145.6	344.9	52.0	542.5
Stage 2	–	6.8	–	6.8
Gross loan commitments	145.6	351.7	52.0	549.3
Stage 1	–	(1.0)	–	(1.0)
Loss allowance	–	(1.0)	–	(1.0)
Total loan commitments	145.6	350.7	52.0	548.3
Loss allowance coverage				
Stage 1	–	0.3%	–	0.2%
Total loss allowance coverage	–	0.3%	–	0.2%

The following table provides an analysis of movements during the year in the loss allowance associated with loan commitments:

	2019		2018	
	Stage 1 £m	**Total £m**	Stage 1 £m	Total £m
As at 1 January	1.0	1.0	–	–
Impact of adopting IFRS 9	–	–	0.5	0.5
Restated balance as at 1 January	1.0	1.0	0.5	0.5
Movements in loss allowance				
New financial assets originated or purchased	0.3	0.3	0.6	0.6
Changes in credit risk	(0.3)	(0.3)	–	–
Financial assets that have been derecognised	–	–	(0.1)	(0.1)
Total movement in loss allowance	–	–	0.5	0.5
As at 31 December	1.0	1.0	1.0	1.0

Calculation of expected credit losses

ECLs are the discounted product of the probability of default (PD), exposure at default (EAD) and loss given default (LGD). Each of these components are detailed further below. ECLs are determined by projecting the PD, EAD and LGD for each future month for each exposure. The three components are multiplied together and adjusted to reflect forward looking information. This calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the current effective interest rate or the original effective interest rate if appropriate.

Twelve-month ECL (Stage 1 assets) is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL (Stage 2 and 3) is calculated by multiplying the lifetime PD by LGD and EAD.

Probability of default

PD is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio.

In relation to loans and advances to customers, the PD is based on internal and external individual customer information that is updated for each reporting period. The Group operates both a model-based PD for its high volume portfolios such as Consumer Lending and residential mortgages within Property Finance and has developed and implemented a Slotting approach for the low volume and high value obligors in Business Finance and large ticket commercial property loans. Both processes deliver a point-in-time measure of default.

For the model-based portfolios, the measure of PD is based on information available to the Group from credit reference agencies and includes information from a broad range of financial services firms and internal product performance data. For the Slotted portfolios, the measure of PD relates to attributes relating to financial strength, political and legal environment, asset/transaction characteristics, strength of sponsor and security.

For each asset class, the Group has a proprietary approach to extrapolate its best estimate of the point-in-time PD from 12 months to behavioural maturity to derive the lifetime PD. This uses economic response models that have been developed specifically to forecast the sensitivity of PD to key macroeconomic variables.

Key risk categories

Creditworthiness risk continued

Exposure at default
EAD is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.

EAD is designed to address increases in utilisation of committed limits and unpaid interest and fees that the Group would ordinarily expect to observe to the point of default, or through to the point of realisation of the collateral.

The Group determines EADs by modelling the range of possible exposure outcomes at various points in time, corresponding to the multiple scenarios.

Loss given default
LGD is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

In relation to loans and advances to customers, the Group segments its lending products into smaller homogenous portfolios as detailed below. In all cases the LGD or its components are tested against recent experience to ensure that they remain current.

- **Property Finance:** the LGD is generally broken down into two parts. These include the Group's estimate of the probability of possession given default, combined with the loss given possession. The Group has continued to focus on the proportion of accounts that have not cured over an emergence period, rather than the proportion of accounts that enter possession to be appropriately conservative. The LGD is based on the Group's estimate of a shortfall, based on the difference between the property value after the impact of a forced sale discount and sale costs, and the loan balance with the addition of unpaid interest and fees and first charge claims with regards to first charge residential mortgages.
- **Business Finance:** the LGD is based on experience of losses on repossessed assets where the Group has collateral, or Management judgement in situations where the individual loans form part of a low default portfolio.
- **Consumer Lending:** the Group uses an estimate of the probability of charge-off, defined as six or more payments in arrears, combined with an estimate of the expected write-off based on an established contractual debt sale agreement or the sale of charge-off debt. There is no recovery portfolio.

Basis of calculation
Twelve-month ECLs and lifetime ECLs are calculated on an individual or collective basis depending on the nature of the underlying portfolio and financial instruments.

Asset classes where the Group calculates ECLs on an individual basis include:

- Stage 3 assets where individual impairments are reviewed and approved by the divisional and Group Impairment Committees;
- large and unique Stage 1 and Stage 2 loans within the Business Finance and Property Finance divisions; and
- treasury and interbank relationships (such as cash and balances at central banks, loans and advances to banks and investment securities).

Asset classes where the Group calculates ECLs on a collective basis include:

- Stage 1 and Stage 2 balances relating to the Group's SME Lending;
- Stage 1, Stage 2 and certain Stage 3 exposures within the Property Finance division; and
- all loans within the Consumer Lending division.

For ECLs calculated on a collective basis, exposures are grouped into smaller homogeneous portfolios based on a combination of internal and external characteristics of the loans, as described below:

Property Finance:
- Product asset class (residential lending and commercial/semi-commercial lending);
- loan-to-value ratios;
- internal master grading scale; and
- exposure value.

Business Finance:
- Business unit (i.e. asset finance, structured finance, corporate lending and development finance);
- internal master grading scale;
- exposure value; and
- collateral type.

Consumer Lending:

- Product type (personal loans and home improvement/holiday ownership loans);
- internal master grading scale; and
- exposure value.

Where loans are assessed on a collective basis, such as loans within the Consumer Lending division, recent experience is used to assess the probability to charge-off given default and the loss given charge. For residential mortgages within the Property Finance division, recent experience of the probability of possession given default and the loss given possession is used to support the ECL. For Business Finance and commercial Property Finance, an assessment is performed on a loan-by-loan basis, which is reviewed by the Group Impairment Committee where the impairment is in excess of £75,000. Where models are used, LGDs are calculated taking into account the valuations of available collateral and the experienced forced sale discounts when collateral has been realised. These factors are applied to all the aged portfolios of debt at each statement of financial position reporting date to derive the individual impairment requirement. These judgements are reviewed at the Group Impairment Committee and the Audit Committee.

Post model adjustments

Limitations in the Group's impairment models may be identified through the ongoing assessment and validation of the outputs from the models. In certain circumstances, Management make post-model adjustments to ensure the loss allowance adequately reflects the expected outcome. These adjustments are generally modelled taking into account the particular attributes of the account which have not been adequately captured by the models. All adjustments are monitored, reviewed and where applicable incorporated into future model development.

In 2019, post model adjustments relate to individual ECL adjustments for specific cases reviewed by the Group Impairment Committee and in the treatment of acquired portfolios that have not yet been migrated into the Group's ECL scoring engine.

Critical judgements relating to the impairment of financial assets

The measurement of ECLs requires the Group to make a number of judgements. The judgements that are considered to have the most significant effect on the amounts in the financial statements are set out below. These judgements have an impact upon which stage the financial asset is held within and therefore whether a 12-month or lifetime ECL is recognised in the financial statements.

The impairment of cash and balances at central banks, loans and advances to banks and investment securities is immaterial. As such, the area where the below judgements have the most significant effect specifically relates to the impairment of loans and advances to customers.

The Group reviews and updates the following key judgements bi-annually, in advance of the Interim Financial Report and the Annual Report and Accounts. All key judgements are reviewed and recommended to the Audit Committee for approval prior to implementation.

Significant increase in credit risk assessment

If a financial asset shows a SICR, it is transferred to Stage 2. The assessment of whether there has been a SICR requires a high level of judgement.

For the purposes of the SICR assessment, the Group applies a series of quantitative, qualitative and backstop criteria:

- **Quantitative criteria:** this considers the increase in an account's remaining lifetime PD at the reporting date compared to the expected residual lifetime PD when the account was originated. The Group segments its credit portfolios into PD bands and has determined a relevant threshold for each PD band, where a movement in excess of threshold is considered to be significant. These thresholds have been determined separately for each portfolio based on historical evidence of delinquency.
- **Qualitative criteria:** this includes the observation of specific events such as short-term forbearance, payment cancellation, historical arrears or extension to customer terms (see following table for further details).
- **Backstop criteria:** IFRS 9 'Financial Instruments' includes a rebuttable presumption that 30 days past due is an indicator of a SICR. The Group considers 30 days past due to be an appropriate backstop measure and does not rebut this presumption.

Creditworthiness risk continued

As a general indicator, there is deemed to be a SICR if the following criteria are identified based on the Group's quantitative modelling:

Sector	Criteria
Property Finance	**Commercial** ■ External mortgage payments in arrears from the credit reference agencies. The external arrears information is statistically a lead indicator of financial difficulties and potential arrears on the loan book; ■ for short-term loans with a modelled PD, PD > 0.38% and the absolute movement in remaining lifetime PD is more than four times the estimate at origination; ■ for term loans with a modelled PD, PD > 0.38% and the absolute movement in remaining lifetime PD is more than two times the estimate at origination; ■ for all portfolios with a slotted PD, PD > 0.38% and the absolute movement in remaining lifetime PD is more than three times the estimate at origination; or ■ loan account is forborne. **Residential** ■ All exposures are graded under the modelled approach. Where the modelled PD > 0.38% and the absolute movement in remaining lifetime PD is more than 5.1 times the estimate at origination; ■ where the customer has ever been six or more payments in arrears on any fixed term account at the credit reference agency; ■ where the customer has missed a mortgage payment in the last six months at the credit reference agency; or ■ loan account is forborne.
Business Finance	■ Entry on to watch list; ■ loan account is forborne; ■ for accounts with a modelled PD, where the absolute movement in the remaining lifetime PD is more than 4.6 times the estimate at origination; ■ for accounts with a slotted PD, where the absolute movement in the remaining lifetime PD is more than three times the estimate at origination.;or ■ loan account is forborne.
Consumer Lending	■ Non-personal loans PD > 0.38% and the absolute movement in remaining lifetime PD is more than 3.7 times the estimate at origination; ■ personal loans PD > 038% and the absolute movement in remaining lifetime PD is more than 4.6 times the estimate at origination; ■ county court judgements registered at the credit reference agencies of > £150 or > £1,000 in last 3-years; or ■ loan account is forborne.

Stage 2 criteria are designed to be effective indicators of a significant deterioration in credit risk. As part of its bi-annual review of key impairment judgements, the Group undertakes detailed analysis to confirm that the Stage 2 criteria remain effective. This includes (but is not limited to):

- **Criteria effectiveness:** this includes the emergence to default for each Stage 2 criterion when compared to Stage 1, Stage 2 outflow as a percentage of Stage 2, percentage of new defaults that were in Stage 2 in the months prior to default, time in Stage 2 prior to default and percentage of the book in Stage 2 that are not progressing to default or curing.
- **Stage 2 stability:** this includes stability of inflows and outflows from Stage 2 and 3.
- **Portfolio analysis:** this includes the percentage of the portfolio that is in Stage 2 and not defaulted, the percentage of the Stage 2 transfer driven by Stage 2 criterion other than the back stops and back-testing of the defaulted accounts.

For low credit risk exposures, the Group is permitted to assume, without further analysis, that the credit risk on a financial asset has not increased significantly since initial recognition if the financial asset is determined to have low credit risk at the reporting date. The Group has opted not to apply this low credit risk exemption.

Loan commitments relating to the undrawn component of a facility are assigned to the same stage as the drawn component of the facility. Therefore if the drawn component of the facility shows a SICR and is transferred to Stage 2, the undrawn component will also be transferred. Loan commitments relating to pipeline loans remain in Stage 1 and are not subject to the same judgements.

The assessment of whether there has been a SICR incorporates forward looking information. The use of forward looking information is detailed on page 113.

Definition of default and credit-impaired assets

When there is objective evidence of impairment and the financial asset is considered to be in default, or otherwise credit-impaired, it is transferred to Stage 3. The Group's definition of default is fully aligned with the definition of credit-impaired.

The Group applies a series of quantitative and qualitative criteria to determine if an account meets the definition of default and should therefore be transferred to Stage 3. These criteria include:

- when the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held);
- when the borrower is more than 90 days past due on any credit obligation to the Group; and
- when a credit obligation to the Group has gone past maturity or there is doubt that the exit strategy for the obligation is likely.

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

Approach to curing

The Group considers a financial asset to be cured, and therefore reclassifies back to a lower stage, when none of the assessed criteria that caused movement into the higher stage is currently present.

For Stage 3 loans with forbearance arrangements in place, the loan must first successfully complete its 12-month curing period to be transferred to Stage 2. Following this, the loan must then successfully complete its 24-month forbearance probation period before the forbearance classification can be discontinued.

During the year ended 31 December 2019, the Group implemented curing for forborne loans. In the year ended 31 December 2018, the application of curing of forborne loans had not been applied within the ECL calculation.

Key risk categories

Creditworthiness risk continued

Critical accounting estimates relating to the impairment of financial assets

The calculation of ECLs requires the Group to make a number of assumptions and estimates. The accuracy of the ECL calculation would be impacted by movements in forward looking economic scenarios used or the probability weightings applied to these scenarios and by unanticipated changes to model assumptions which differ from actual outcomes. The key assumptions and estimates which, depending on a range of factors, could result in a material adjustment in the next financial year are set out in the following sections.

The impairment of cash and balances at central banks, loans and advances to banks and investment securities is immaterial. As such, the area where the below assumptions and estimates could have the most significant impact specifically relates to the impairment of loans and advances to customers.

Forward looking information

The Group incorporates forward looking information into the calculation of ECLs and the assessment of whether there has been a SICR. The use of forward looking information involves significant judgement and represents a key source of estimation uncertainty.

Forward looking economic scenarios used by the Group

The Group uses three forward looking economic scenarios: a base case (central view), an alternative upside scenario and an alternative downside scenario. The two alternative scenarios are chosen to be plausible alternative base cases and are not stress testing scenarios.

The Group's central view is informed by the HM Treasury Central forecast that is published quarterly and used as part of the Group's corporate planning activity. Intra-quarter, the Group considers survey-based data and lead indicators to inform whether the central view continues to be appropriate. The Group focusses its view on the next five years as part of the narrative to the scenario but has rate paths that extend out beyond the planning period for the Group and up to 20 years.

For the alternative scenarios, the Group is not large enough to have an internal economist and therefore works with a third party on the narrative of the scenarios and the rate paths to ensure that they are internally consistent using the UK Treasury model. The rate paths used in the scenarios are consistent with the core UK macroeconomic factors that are published by the Bank of England as part of the annual stress testing exercise.

The probability weightings assigned to the Group's three scenarios are a matter of judgement but are generally set to ensure that there is an asymmetry in the ECL. The weightings applied to each scenario in both reported years are as follows:

- Base: 40%
- Upside: 20%
- Downside: 40%

The Group has regularly considered Brexit within its economic scenarios and specifically the nature and probability of the alternative downside scenario. The Group has maintained the nature of the alternative downside view as a disorderly no-deal Brexit as a result of the delay in Brexit until 31 January 2020 and to reflect the remaining risk arising from the nature of any future relationship with the EU.

The Group undertakes a review of its three scenarios and the weightings applied at least quarterly and more frequently if required. The results of this review are recommended to the Audit Committee and Board prior to any changes being implemented.

The table below summarises the economic assumptions that have been used to determine the forward looking ECLs as at 31 December 2019. This reflects the aforementioned weightings applied to the three scenarios.

	2020	2021	2022	2023
GDP – % change year-on-year	Base: 1.2%	Base: 1.8%	Base: 1.6%	Base: 1.7%
	Upside: 1.9%	Upside: 2.7%	Upside: 1.9%	Upside: 1.5%
	Downside: (0.1%)	Downside: 0.8%	Downside: 1.6%	Downside: 2.1%
Bank Rate (%)	Base: 0.85%	Base: 1.08%	Base: 1.25%	Base: 1.44%
	Upside: 1.02%	Upside: 1.60%	Upside: 2.01%	Upside: 2.17%
	Downside: 0.46%	Downside: 0.20%	Downside: 0.26%	Downside: 0.64%
UK Unemployment (%)	Base: 3.9%	Base: 4.0%	Base: 4.0%	Base: 4.0%
	Upside: 3.7%	Upside: 3.4%	Upside: 3.2%	Upside: 3.1%
	Downside: 4.3%	Downside: 5.0%	Downside: 5.2%	Downside: 5.1%
Consumer Prices Index – % change year-on-year	Base: 1.9%	Base: 2.0%	Base: 2.0%	Base: 2.0%
	Upside: 1.7%	Upside: 1.9%	Upside: 2.2%	Upside: 2.1%
	Downside: 1.3%	Downside: 1.4%	Downside: 1.9%	Downside: 2.0%
UK Residential House Price Index – % change year-on-year	Base: 1.3%	Base: 2.7%	Base: 2.8%	Base: 2.3%
	Upside: 3.0%	Upside: 5.4%	Upside: 5.1%	Upside: 2.7%
	Downside (3.0%)	Downside: (2.0%)	Downside: 1.3%	Downside: 3.0%

Using forward looking information
The measurement of ECLs is required to reflect an unbiased probability weighted range of possible future outcomes. In order to do this, the Group has developed a proprietary approach to assess the impact of the changes in economic scenarios on the obligor level ECL. The Group has mapped each asset class to an external long-run benchmark series that is believed to behave in a similar way to the Group's portfolio over the economic cycle.

The Group has developed econometric models to establish how much of the historical series can be explained by movements in the UK macroeconomic factors. The models deliver an estimate of the impact of a unit increase in default arising from a 1% increase in the underlying macroeconomic factors. The models are developed in line with the Group's model governance framework and are subject to review at least every six-months. The models are tested across multiple sets of scenarios to ensure that they work in a range of scenarios, the output of the scenarios is a series of scalars by asset class and a scenario that can be applied to the underlying PDs to deliver a forward looking ECL.

The Group has developed a proprietary approach to extrapolating its 12-month PDs over the behavioural maturity of the loans that the scalars can be applied to. The nature of the scenarios means that there will be an impact on both the PD and the number of obligors moving from Stage 1 to Stage 2 in line with the SICR criteria.

Creditworthiness risk continued

Sensitivity analysis
The ECLs are sensitive to judgements and assumptions made regarding the forward looking scenarios used and the weightings applied. Sensitivity analysis is performed by Management to determine the impact on ECLs.

The table below shows the loss allowance recognised in the statement of financial position for loans and advances to customers based on the probability weighted multiple economic scenarios and the impact on this loss allowance if each forward looking scenario were weighted at 100%.

		Increase/(decrease) in loss allowance if scenario weighted at 100%		
As at 31 December 2019	Probability weighted loss allowance £m	Base £m	Upside £m	Downside £m
Property Finance	14.5	(3.7)	(4.8)	6.1
Business Finance	25.6	(1.1)	(2.2)	2.2
Consumer Lending	21.0	(1.1)	(1.8)	2.0
Total	61.1	(5.9)	(8.8)	10.3

Inputs into ECL calculations and model assumptions
ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Details of the ECL calculation are provided on page 108. The assumptions applied involve judgement and represent a key source of estimation uncertainty.

Key assumptions and sensitivity analysis
The Group considers the key assumptions impacting the ECL calculation in respect of the Group's loan and advances to customers to be those set out below. Sensitivity analysis was performed to assess the impact of changes in these key assumptions on calculated ECLs and is also set out below.

Assumption	Sensitivity analysis
PD	■ A 10% increase in the PD for each customer would increase the ECL by c.£4.0 million (2018: c.£3.9 million).
LGD: Property Finance **Property value**	■ A 10-percentage point reduction in property prices would increase the ECL in Property Finance by c.£5.9 million (2018: c.£6.1 million).
Forced sale discount	■ A 5% absolute increase in the forced sale discount would increase the ECL in Property Finance by c.£4.0 million (2018: c.£4.1 million).
LGD: Business Finance **Absolute LGD value**	■ A 5% absolute increase in the LGD applied would increase the ECL in Business Finance by c.£3.6 million (2018: c.£3.0 million).
LGD: Consumer Lending **Loss given charge-off**	■ A 10-percentage point increase in the loss given charge-off would increase the ECL in Consumer Lending by c.£2.4 million (2018: c.£2.9 million).

(d) Credit risk grading

To assess the credit risk of the Group's financial assets, financial guarantee contracts and loan commitments, a credit grading system has been developed by the Group which maps to a common master grading scale. The current risk grading framework consists of 25 grades on a master grading scale, reflecting varying degrees of risk and default as set out in the table below. The responsibility for setting risk grades lies with the approval point for the risk or committee as appropriate. Risk grades are subject to regular reviews by the Group risk function.

Grading	Master grading scale	PD range
Low risk	1-10	<=0.38%
Medium risk	11-15	>0.38% to <= 1.76%
High risk	16-25	>1.76%

(e) Credit risk exposure

Financial instruments subject to impairment
The following tables contain an analysis of the Group's credit risk exposure from its financial instruments for which a loss allowance is recognised.

The tables provide an analysis of the gross carrying amount of financial assets and the exposure to credit risk on loan commitments and financial guarantee contracts by credit risk grade and year-end stage classification. The credit risk grades are based on the grades defined in the 'credit risk grading' section above. It should be noted that the credit risk grading assessment is a point-in-time assessment whereas the stage classification is determined based on the change in credit risk from initial recognition. As such, for non-credit impaired financial assets, there is not a direct relationship between the credit risk assessment and stage classification.

The information below also provides the Group's maximum exposure to credit risk. For financial assets this is the gross carrying amount net of any loss allowance recognised. Where the loss allowance is less than £0.1 million, the Group's maximum exposure to credit risk is equal to the gross carrying amount and only this amount is presented in the table. For financial guarantee contracts, the Group's maximum exposure to credit risk is the maximum amount the Group could have to pay should the guarantee be called upon. For loan commitments, the Group's maximum exposure to credit risk is the gross amount committed.

	2019		2018	
Cash and balances at central banks	**Stage 1 £m**	**Total £m**	Stage 1 £m	Total £m
Low risk	**1,064.6**	**1,064.6**	645.2	645.2
Gross carrying amount	**1,064.6**	**1,064.6**	645.2	645.2

	2019		2018	
Loans and advances to banks	**Stage 1 £m**	**Total £m**	Stage 1 £m	Total £m
Low risk	**59.1**	**59.1**	50.6	50.6
Gross carrying amount	**59.1**	**59.1**	50.6	50.6

Creditworthiness risk continued

	2019				2018			
Loans and advances to customers	**Stage 1 £m**	**Stage 2 £m**	**Stage 3 £m**	**Total £m**	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
Low risk	**1,583.0**	**11.3**	**1.1**	**1,595.4**	1,906.5	26.2	7.7	1,940.4
Medium risk	**2,863.1**	**264.5**	**1.6**	**3,129.2**	1,910.4	464.5	33.3	2,408.2
High risk	**1,401.7**	**440.8**	**122.9**	**1,965.4**	1,105.1	380.9	80.2	1,566.2
Gross carrying amount	**5,847.8**	**716.6**	**125.6**	**6,690.0**	4,922.0	871.6	121.2	5,914.8
Loss allowance	**(20.6)**	**(14.2)**	**(26.3)**	**(61.1)**	(23.5)	(20.7)	(23.6)	(67.8)
Carrying amount[1]	**5,827.2**	**702.4**	**99.3**	**6,628.9**	4,898.5	850.9	97.6	5,847.0

	2019		2018	
Investment securities	**Stage 1 £m**	**Total £m**	Stage 1 £m	Total £m
Low risk	**200.0**	**200.0**	139.9	139.9
Gross carrying amount	**200.0**	**200.0**	139.9	139.9

	2019		2018	
Financial guarantee contracts	**Stage 1 £m**	**Total £m**	Stage 1 £m	Total £m
Low risk	**2.5**	**2.5**	2.5	2.5
Gross amount guaranteed[1]	**2.5**	**2.5**	2.5	2.5

In both reported years the Group has had one financial guarantee contract which is fully collateralised through a first fixed charge over a blocked deposit account. As such, the amount the Group should have to pay should the guarantee be called upon (i.e. the Group's maximum exposure to credit risk) is £nil.

	2019			2018		
Loan commitments	**Stage 1 £m**	**Stage 2 £m**	**Total £m**	Stage 1 £m	Stage 2 £m	Total £m
Low risk	**403.7**	**–**	**403.7**	462.1	–	462.1
Medium risk	**84.3**	**–**	**84.3**	70.5	–	70.5
High risk	**97.9**	**5.6**	**103.5**	9.9	6.8	16.7
Gross amount committed	**585.9**	**5.6**	**591.5**	542.5	6.8	549.3

[1] Excludes fair value adjustments for hedged risk.

Financial assets not subject to impairment
The following table provides an analysis of the Group's maximum exposure to credit risk from its financial assets not subject to impairment (i.e. those held at fair value through profit or loss).

	2019 £m	2018 £m
Derivative financial assets	4.4	1.6

(f) Collateral held and other credit enhancements

As a method of mitigating credit risk, the Group holds collateral and other credit enhancements against certain of its credit exposures. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty.

The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation. The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period.

Non-derivative financial assets
Collateral is generally not held against loans and advances to banks and investment securities. However, at times, certain securities are held as part of reverse repurchase agreements.

For loans and advances to customers the main types of collateral obtained are:

- **Loan receivables:** includes amounts secured by a first or second charge over commercial and residential property, debt receivables and other assets such as asset backed loans and invoice receivables.
- **Finance lease receivables and instalment credit receivables:** secured on the underlying assets which can be repossessed in the event of a default.

The following table sets out the security profile of the Group's loans and advances to customers. The amounts in the table represent gross carrying amounts:

	2019 £m	2018 £m
Secured on commercial and residential property	4,780.7	3,908.1
Secured on debt receivables	618.5	517.3
Secured on other assets	91.3	93.1
Total secured loan receivables	**5,490.5**	4,518.5
Secured by finance lease assets	81.0	95.0
Secured by instalment credit assets	382.4	409.4
Total secured loans and advances to customers	**5,953.9**	5,022.9
Unsecured loan receivables	736.1	891.9
Gross loans and advances to customers	**6,690.0**	5,914.8

Collateral held in relation to secured loans is capped, after taking into account the first charge balance, at the amount outstanding on an individual loan basis.

Creditworthiness risk continued

Derivative financial assets
Credit risk derived from derivative transactions is mitigated by entering into master netting agreements and holding collateral. Such collateral is subject to the standard industry Credit Support Annex and is paid or received on a regular basis. As at 31 December 2019, net cash collateral posted is £11.0 million (2018: £4.5 million).

Credit-impaired financial assets
The Group closely monitors collateral held for financial assets considered to be credit-impaired (Stage 3), as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses.

Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are set out below:

As at 31 December 2019	**Gross carrying amount £m**	**Loss allowance £m**	**Carrying amount £m**	**Fair value of collateral held £m**
Property Finance	**89.0**	**(8.1)**	**80.9**	**80.9**
Business Finance	**29.1**	**(12.9)**	**16.2**	**16.2**
Consumer Lending	**7.5**	**(5.3)**	**2.2**	**–**
Total credit-impaired loans and advances to customers	**125.6**	**(26.3)**	**99.3**	**97.1**

As at 31 December 2018	Gross carrying amount £m	Loss allowance £m	Carrying amount £m	Fair value of collateral held £m
Property Finance	60.6	(6.2)	54.4	54.4
Business Finance	54.0	(13.0)	41.0	41.0
Consumer Lending	6.6	(4.4)	2.2	–
Total credit-impaired loans and advances to customers	121.2	(23.6)	97.6	95.4

The following table shows the distribution of loan-to-value ratios for the Group's credit-impaired Property Finance portfolio. Loan-to-value is calculated as the ratio of the current gross carrying amount of the loan to the value of the collateral at origination.

	Gross carrying amount	
	2019 £m	2018 £m
Loan-to-value ratio		
Less than 50%	**5.8**	13.3
50-70%	**28.8**	23.6
71-90%	**33.3**	22.7
91-100%	**20.2**	0.5
More than 100%	**0.9**	0.5
Total Property Finance credit-impaired assets	**89.0**	60.6

(g) Repossessions

During the year, the Group took possession of some properties held as security against loans. As at 31 December 2019, the Group held 17 repossessed properties with a carrying amount of £3.5 million (2018: 8 repossessed properties with carrying amount of £1.7 million). The Group's policy is to pursue the realisation of collateral in an orderly manner.

(h) Forbearance

The Group maintains a forbearance policy for the servicing and management of customers who are in financial difficulty and require some form of concession to be granted, even if this concession entails a loss for the Group. A concession may be either of the following:

- a modification of the previous terms and conditions of an agreement, which the borrower is considered unable to comply with due to its financial difficulties, to allow for sufficient debt service ability, that would not have been granted had the borrower not been in financial difficulties; or
- a total or partial refinancing of an agreement that would not have been granted had the borrower not been in financial difficulties.

Forbearance in relation to an exposure can be temporary or permanent depending on the circumstances, progress on financial rehabilitation and the detail of the concession(s) agreed.

The Group applies the European Banking Authority Technical Standards on forbearance and non-performing exposures as defined in Annex V of Commission Implementing Regulation (EU) 2015/227. Under these standards loans are classified as performing or non-performing in accordance with the European Banking Authority rules.

The European Banking Authority standards stipulate that a forbearance classification can be discontinued when all of the following conditions have been met:

- the exposure is considered to be performing, including where it has been reclassified from the non-performing category, after an analysis of the financial condition of the debtor showed that it no longer met the conditions to be considered as non-performing;
- a minimum two-year probation period has passed from the date the forborne exposure was considered to be performing;
- regular payments of more than an insignificant aggregate amount of principal or interest have been made during at least half of the probation period; and
- none of the exposures to the debtor is more than 30 days past-due at the end of the probation period.

In the year ended 31 December 2018, the Group included short-term repayment plans within forborne loans. In the year ended 31 December 2019, the definition was amended to exclude short-term repayment plans. Comparative information has not been restated and as a result information is not directly comparable.

Key risk categories

Creditworthiness risk continued

Forbearance by reportable segment

The following tables provide a summary of the Group's forborne loans and advances to customers by reportable segment:

	Performing			Non-performing			
As at 31 December 2019	**Modification to terms and conditions £m**	**Refinancing £m**	**Total £m**	**Modification to terms and conditions £m**	**Refinancing £m**	**Total £m**	**Total forborne loans £m**
Property Finance	4.2	–	4.2	41.6	–	41.6	45.8
Business Finance	10.6	–	10.6	13.6	0.9	14.5	25.1
Consumer Lending	0.5	–	0.5	5.3	–	5.3	5.8
Total	15.3	–	15.3	60.5	0.9	61.4	76.7

		Gross amount of forborne loans			Loss allowance on forborne loans			
As at 31 December 2019	**Number**	**Performing £m**	**Non-performing £m**	**Total £m**	**Performing £m**	**Non-performing £m**	**Total £m**	**Coverage %**
Property Finance	703	4.2	41.6	45.8	–	(4.1)	(4.1)	9.0
Business Finance	310	10.6	14.5	25.1	(0.2)	(4.2)	(4.4)	17.5
Consumer Lending	3,564	0.5	5.3	5.8	(0.1)	(3.4)	(3.5)	60.3
Total	4,577	15.3	61.4	76.7	(0.3)	(11.7)	(12.0)	15.6

	Performing			Non-performing			
As at 31 December 2018	Modification to terms and conditions £m	Refinancing £m	Total £m	Modification to terms and conditions £m	Refinancing £m	Total £m	Total forborne loans £m
Property Finance	9.5	–	9.5	40.1	–	40.1	49.6
Business Finance	9.1	5.1	14.2	28.3	0.8	29.1	43.3
Consumer Lending	2.9	–	2.9	10.1	–	10.1	13.0
Total	21.5	5.1	26.6	78.5	0.8	79.3	105.9

		Gross amount of forborne loans			Loss allowance on forborne loans			
As at 31 December 2018	Number	Performing £m	Non-performing £m	Total £m	Performing £m	Non-performing £m	Total £m	Coverage %
Property Finance	1,011	9.5	40.1	49.6	(0.2)	(4.1)	(4.3)	8.7
Business Finance	313	14.2	29.1	43.3	(0.3)	(3.8)	(4.1)	9.5
Consumer Lending	4,687	2.9	10.1	13.0	(0.3)	(5.3)	(5.6)	43.1
Total	6,011	26.6	79.3	105.9	(0.8)	(13.2)	(14.0)	13.2

Forbearance by year-end stage

The following tables provide a summary of the Group's forborne loans and advances to customers by the year-end stage classification:

As at 31 December 2019	**Performing** Modification to terms and conditions £m	**Performing** Refinancing £m	**Performing** Total £m	**Non-performing** Modification to terms and conditions £m	**Non-performing** Refinancing £m	**Non-performing** Total £m	**Total forborne loans £m**
Stage 1	0.7	–	0.7	0.2	–	0.2[1]	0.9
Stage 2	14.6	–	14.6	7.5	0.2	7.7	22.3
Stage 3	–	–	–	52.8	0.7	53.5	53.5
Total	15.3	–	15.3	60.5	0.9	61.4	76.7

As at 31 December 2019	**Number**	**Gross amount of forborne loans** Performing £m	**Gross amount of forborne loans** Non-performing £m	**Gross amount of forborne loans** Total £m	**Loss allowance on forborne loans** Performing £m	**Loss allowance on forborne loans** Non-performing £m	**Loss allowance on forborne loans** Total £m	**Coverage %**
Stage 1	329	0.7	0.2[1]	0.9	–	–	–	–
Stage 2	433	14.6	7.7	22.3	(0.3)	(0.4)	(0.7)	3.1
Stage 3	3,815	–	53.5	53.5	–	(11.3)	(11.3)	21.1
Total	4,577	15.3	61.4	76.7	(0.3)	(11.7)	(12.0)	15.6

As at 31 December 2018	Performing Modification to terms and conditions £m	Performing Refinancing £m	Performing Total £m	Non-performing Modification to terms and conditions £m	Non-performing Refinancing £m	Non-performing Total £m	Total forborne loans £m
Stage 1	6.5	–	6.5	6.8	–	6.8[1]	13.3
Stage 2	15.0	5.1	20.1	40.5	–	40.5	60.6
Stage 3	–	–	–	31.2	0.8	32.0	32.0
Total	21.5	5.1	26.6	78.5	0.8	79.3	105.9

As at 31 December 2018	Number	Gross amount of forborne loans Performing £m	Gross amount of forborne loans Non-performing £m	Gross amount of forborne loans Total £m	Loss allowance on forborne loans Performing £m	Loss allowance on forborne loans Non-performing £m	Loss allowance on forborne loans Total £m	Coverage %
Stage 1	1,097	6.5	6.8[1]	13.3	(0.1)	(0.4)[1]	(0.5)	3.8
Stage 2	1,421	20.1	40.5	60.6	(0.7)	(2.9)	(3.6)	5.9
Stage 3	3,493	–	32.0	32.0	–	(9.9)	(9.9)	30.9
Total	6,011	26.6	79.3	105.9	(0.8)	(13.2)	(14.0)	13.2

[1] Loans that are classified as non-performing and Stage 1 are where the latest forbearance measure was extended more than a year ago and the number of days past due at the current reporting period is more than zero but less than 30.

Creditworthiness risk continued

(i) Concentrations of credit risk

The Group monitors concentrations of credit risk from its loans and advances to customers by geographic location and by loan size.

Concentrations of credit risk by geographic location
An analysis of credit risk from the Group's loans and advances to customers by geographic location is shown below:

As at 31 December 2019	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
East Anglia	134.9	77.1	24.4	236.4
East Midlands	156.0	70.2	45.2	271.4
Greater London	1,714.9	419.1	67.7	2,201.7
Guernsey/Jersey/Isle of Man	34.5	21.5	0.1	56.1
North East	74.8	42.9	24.6	142.3
North West	357.1	191.9	67.5	616.5
Northern Ireland	10.5	–	1.6	12.1
Scotland	280.2	80.4	73.4	434.0
South East	867.9	253.0	111.3	1,232.2
South West	318.8	150.3	47.6	516.7
Wales	91.9	61.5	24.0	177.4
West Midlands	179.0	171.2	56.7	406.9
Yorkshire/Humberside	220.7	111.3	54.3	386.3
Gross loans and advances to customers	4,441.2	1,650.4	598.4	6,690.0

As at 31 December 2018	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
East Anglia	117.8	69.6	32.3	219.7
East Midlands	120.6	58.2	58.8	237.6
Greater London	1,454.9	300.8	82.3	1,838.0
Guernsey/Jersey/Isle of Man	24.5	46.3	0.1	70.9
North East	52.8	31.4	35.3	119.5
North West	305.6	171.4	92.0	569.0
Northern Ireland	9.6	1.8	2.1	13.5
Scotland	222.1	93.2	89.4	404.7
South East	747.4	221.4	141.1	1,109.9
South West	263.6	113.3	61.3	438.2
Wales	80.0	95.0	31.3	206.3
West Midlands	141.6	151.4	74.9	367.9
Yorkshire/Humberside	179.4	68.4	71.8	319.6
Gross loans and advances to customers	3,719.9	1,422.2	772.7	5,914.8

Concentrations of credit risk by loan size

An analysis of credit risk from the Group's loans and advances to customers by loan size is shown below:

As at 31 December 2019	**Property Finance £m**	**Business Finance £m**	**Consumer Lending £m**	**Total £m**
0 – £50k	**258.6**	**101.9**	**598.0**	**958.5**
£50k – £100k	**458.2**	**64.8**	**0.4**	**523.4**
£100k – £250k	**1,058.1**	**121.7**	**–**	**1,179.8**
£250k – £500k	**990.5**	**112.5**	**–**	**1,103.0**
£500k – £1.0 million	**697.5**	**135.1**	**–**	**832.6**
£1.0 million – £2.5 million	**561.6**	**237.9**	**–**	**799.5**
£2.5 million – £5.0 million	**249.4**	**242.2**	**–**	**491.6**
£5.0 million – £10.0 million	**101.9**	**211.4**	**–**	**313.3**
£10.0 million – £25.0 million	**65.4**	**422.9**	**–**	**488.3**
Gross loans and advances to customers	**4,441.2**	**1,650.4**	**598.4**	**6,690.0**

As at 31 December 2018	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
0 – £50k	215.3	140.5	772.5	1,128.3
£50k – £100k	378.5	72.3	0.2	451.0
£100k – £250k	883.5	120.4	–	1,003.9
£250k – £500k	797.2	107.9	–	905.1
£500k – £1.0 million	609.3	135.6	–	744.9
£1.0 million – £2.5 million	463.8	200.2	–	664.0
£2.5 million – £5.0 million	208.7	156.1	–	364.8
£5.0 million – £10.0 million	108.4	157.3	–	265.7
£10.0 million – £25.0 million	55.2	331.9	–	387.1
Gross loans and advances to customers	3,719.9	1,422.2	772.7	5,914.8

Key risk categories

Liquidity risk

Audited: *The following section is covered by the Independent Auditor's Report.*

The Group has developed comprehensive funding and liquidity policies to ensure that it maintains sufficient liquid assets to be able to meet all of its financial obligations and maintain public confidence.

The Group's treasury function is responsible for the day-to-day management of the Group's liquidity and wholesale funding. The Board sets limits over the level, composition and maturity of liquidity and deposit funding balances, reviewing these at least annually. Compliance with these limits is monitored daily by finance and risk personnel independent of the treasury function. Additionally, a series of liquidity stress tests are performed weekly by the finance function and are formally reported to the Asset and Liability Committee and the Board to ensure that the Group maintains adequate liquidity for business purposes even under stressed conditions.

Stress testing is a major component of liquidity risk management and the Group has developed a range of scenarios covering a range of market wide and firm specific factors. A comprehensive stress testing exercise is conducted at least annually and the methodology is incorporated into the Group's statement of financial position risk management model to ensure that stress tests are run on a regular basis. The output of stress testing is circulated to the Board and to the Asset and Liability Committee who use the results to decide whether to amend the Group's risk appetite and liquidity limits.

The Group reports its liquidity position against its liquidity coverage ratio (LCR), net stable funding ratio (NSFR) and other key regulatory ratios for regulatory reporting purposes.

Maturity analysis for financial assets and liabilities

The table below segments the Group's contractual undiscounted cash flows of its non-derivative financial assets and liabilities into relevant maturity groupings. The Group's assets and liabilities may be repaid or otherwise mature earlier or later than implied by their contractual tenor.

As at 31 December 2019	Carrying amount £m	Gross nominal inflow/ (outflow) £m	Less than 1 month £m	1-3 months £m	3 months – 1 year £m	1-2 years £m	2-5 years £m	More than 5 years £m
Financial assets								
Cash and balances at central banks	1,064.6	1,064.6	1,052.1	–	–	–	–	12.5
Loans and advances to banks	59.1	59.1	59.1	–	–	–	–	–
Loans and advances to customers	6,637.7	6,743.3	307.8	265.7	889.2	752.5	1,245.7	3,282.4
Investment securities	200.0	200.3	0.3	–	–	37.7	162.3	–
Assets held for sale	104.1	55.2	55.2	–	–	–	–	–
Total financial assets	8,065.5	8,122.5	1,474.5	265.7	889.2	790.2	1,408.0	3,294.9
Financial liabilities								
Amounts due to banks	(881.6)	(887.4)	(4.2)	(7.4)	(116.8)	(488.8)	(270.2)	–
Customer deposits	(6,109.4)	(6,231.2)	(2,189.6)	(519.7)	(2,060.1)	(722.8)	(715.2)	(23.8)
Debt securities in issue	(240.7)	(328.2)	–	(0.7)	(2.2)	(2.9)	(8.6)	(313.8)
Lease liabilities	(12.4)	(13.4)	(0.1)	(0.3)	(1.3)	(1.9)	(5.6)	(4.2)
Subordinated debt liability	(95.9)	(146.4)	–	(0.7)	(7.1)	(7.7)	(23.0)	(107.9)
Total financial liabilities	(7,340.0)	(7,606.6)	(2,193.9)	(528.8)	(2,187.5)	(1,224.1)	(1,022.6)	(449.7)

As at 31 December 2018	Total carrying amount £m	Gross nominal inflow/ (outflow) £m	Less than 1 month £m	1-3 months £m	3 months – 1 year £m	1-2 years £m	2-5 years £m	More than 5 years £m
Financial assets								
Cash and balances at central banks	645.2	645.2	636.3	–	–	–	–	8.9
Loans and advances to banks	50.6	50.6	50.6	–	–	–	–	–
Loans and advances to customers	5,845.9	5,944.1	285.4	212.9	817.3	814.0	1,269.1	2,545.4
Investment securities	139.9	140.2	0.2	–	–	–	140.0	–
Total financial assets	6,681.6	6,780.1	972.5	212.9	817.3	814.0	1,409.1	2,554.3
Financial liabilities								
Amounts due to banks	(1,029.4)	(1,039.9)	(1.9)	–	–	(273.9)	(764.1)	–
Customer deposits	(4,977.9)	(5,083.8)	(1,507.3)	(292.1)	(1,800.2)	(820.2)	(598.4)	(65.6)
Subordinated debt liability	(75.5)	(120.8)	–	–	(7.5)	(6.4)	(19.1)	(87.8)
Total financial liabilities	(6,082.8)	(6,244.5)	(1,509.2)	(292.1)	(1,807.7)	(1,100.5)	(1,381.6)	(153.4)

Liquidity buffer

The Group maintains a liquidity buffer which can be called upon to create sufficient liquidity in order to meet cash and collateral outflows and PRA regulatory requirements.

The average monthly liquidity buffer throughout the year was £1,016.0 million (2018: £805.1 million).

Components of the Group's liquidity buffer as at 31 December are as follows:

	2019 £m	2018 £m
Cash and with drawable central bank reserves	**1,051.8**	636.1
Extremely high-quality covered bonds	**93.6**	129.5
Central government assets	**22.8**	–
Total liquidity buffer	**1,168.2**	765.6

All components of the Group's liquidity buffer are LCR level 1 eligible.

Central government assets are off balance-sheet UK gilts acquired as part of a security swap. See Note 28 of the Financial Statements for further details.

Key risk categories

Liquidity risk continued

Liquidity coverage ratio and net stable funding ratio

A range of early warning indicators are monitored for early signs of liquidity risk. These include a range of quantitative and qualitative measures that include the close monitoring of the LCR and NSFR.

The Group's LCR aims to monitor the resilience of the Group to a liquidity risk over a 30-day period. The following table sets out the LCR as at 31 December:

	2019	2018
Liquidity buffer (£m)	**1,168.2**	765.6
Total net cash outflows (£m)	**425.6**	312.6
Liquidity coverage ratio (%)	**274.5**	244.9

The Group's NSFR aims to ensure that the Group has an acceptable amount of stable funding to support assets over a one-year period of extended stress. Based on current interpretations of regulatory requirements and guidance, the NSFR as at 31 December 2019 is 131.9% (2018: 128.5%). This is in excess of the minimum level of 100% proposed by the Basel Committee on Banking Supervision and European Commission[1].

Assets available to support future funding

The Group's assets can be used to support collateral requirements for central bank operations or third party repurchase transactions. Assets that have been set aside for such purposes are classified as encumbered assets and cannot be used for other purposes.

All other assets are defined as unencumbered assets. These comprise assets that are readily available to secure funding or meet collateral requirements ('available as collateral'), and assets that are not subject to any restrictions but are not readily available for use ('other').

The table below sets out the availability of the Group's assets to support future funding:

	Encumbered		**Unencumbered**		
As at 31 December 2019	**Pledged as collateral £m**	**Other £m**	**Available as collateral £m**	**Other £m**	**Total £m**
Cash and balances at central banks	–	12.5	–	1,052.1	1,064.6
Loans and advances to banks	11.0	–	48.1	–	59.1
Loans and advances to customers	1,424.0	–	5,213.7	–	6,637.7
Investment securities	100.0	–	100.0	–	200.0
Derivative financial assets	–	–	–	4.4	4.4
Assets held for sale	–	–	–	104.1	104.1
Non-financial assets	–	–	39.9	113.2	153.1
Total assets	**1,535.0**	**12.5**	**5,401.7**	**1,273.8**	**8,223.0**

1 The NSFR will be implemented in the EU through the Capital Requirements Regulation 2 in June 2021. The timing of a binding NSFR in the UK remains subject to uncertainty and how and when it will be implemented depends in part on the terms and timings of the UK's withdrawal from the EU. The Basel Committee on Banking Supervision issued its final recommendations for the implementation of the NSFR in October 2016, proposing a minimum ratio of 100%. The European Commission also proposed a NSFR of at least 100% as part of the Capital Requirements Regulation 2 in November 2016.

As at 31 December 2018	Encumbered		Unencumbered		
	Pledged as collateral £m	Other £m	Available as collateral £m	Other £m	Total £m
Cash and balances at central banks	–	8.9	–	636.3	645.2
Loans and advances to banks	5.3	–	45.3	–	50.6
Loans and advances to customers	1,603.4	–	4,242.5	–	5,845.9
Investment securities	–	–	–	139.9	139.9
Derivative financial assets	–	–	–	1.6	1.6
Non-financial assets	–	–	34.1	107.6	141.7
Total assets	1,608.7	8.9	4,321.9	885.4	6,824.9

Encumbered assets pledged as collateral are:

- Loans and advances to banks totalling £11.0 million (2018: £5.3 million) which are pledged as collateral against derivative contracts.
- Loans and advances to customers totalling £1,424.0 million (2018: £1,603.4 million), of which:

  £974.2 million (2018: £1,402.7 million) are positioned with the Bank of England for use as collateral under the Term Funding Scheme.

  £163.6 million (2018: £200.7 million) are pledged as collateral against secured bank borrowings.

  £286.2 million (2018: £nil) are pledged to securitisation programmes.
- Investment securities totalling £100.0 million (2018: £nil) which are positioned with the Bank of England for use as collateral under the Term Funding Scheme.

Other encumbered assets (assets that cannot be used for secured funding due to legal or other reasons) are:

- Cash and balances at central banks totalling £12.5 million (2018: £8.9 million) which are mandatory deposits with central banks.

In the year ended 31 December 2019, the Group has also entered into self-issuance of debt securities, in which Shawbrook Mortgage Funding 2019-1 plc issued notes that were retained by Shawbrook Bank Limited (see Note 28 of the Financial Statements for details). These debt securities are eliminated in full on consolidation and are therefore not included in the above tables. Certain of these internally held notes were used as collateral as part of a security swap transacted for liquidity purposes.

Key risk categories

Market risk

Audited: *The following section is covered by the Independent Auditor's Report.*

The Group's objective is to manage and control market risk exposures, maintaining a market profile consistent with the Group's risk appetite.

The Group's treasury function is responsible for managing the Group's exposure to all aspects of market risk within the operational limits set out in the Group's treasury policies. The Asset and Liability Committee approves the Group's treasury policies and receives regular reports on all aspects of market risk exposure, including interest rate risk. All financial assets held by the Group are non-trading.

Foreign exchange risk

Foreign exchange risk is the risk that the value of, or net income arising from, assets and liabilities changes as a result of movements in exchange rates. The Group has low levels of foreign exchange risk which is managed by appropriate financial instruments including derivatives.

The table below sets out the Group's exposure to foreign exchange risk:

As at 31 December 2019	**Euros £m**	**US Dollars £m**	**Australian Dollars £m**
Loans and advances to banks	**4.4**	**6.0**	**0.4**
Loans and advances to customers	**12.6**	**17.3**	**–**
Total exposure	**17.0**	**23.3**	**0.4**

As at 31 December 2018	Euros £m	US Dollars £m	Australian Dollars £m
Loans and advances to banks	4.4	2.1	(0.1)
Loans and advances to customers	28.7	5.7	0.1
Total exposure	33.1	7.8	–

The Group estimates that a 5% movement in exchange rates would have no greater impact on the Group's profit before tax than an increase or decrease of £2.0 million (2018: £2.0 million).

Basis risk

Basis risk is the risk of loss arising from changes in the relationship between interest rates which have similar but not identical characteristics (for example, LIBOR and the Bank of England Bank Rate). This is monitored closely and regularly reported to the Asset and Liability Committee. This risk is managed within established risk limits by matching and, where appropriate and necessary, through the use of derivatives and via other control procedures.

The Group's forecasts and plans take in to account the risk of interest rate changes and are prepared and stressed accordingly, in line with PRA guidance.

Information regarding the Group's transition from LIBOR to new benchmark interest rates in advance of 2021 can be found on page 132.

Interest rate risk

Interest rate risk is the risk of loss arising from adverse movements in market interest rates. Interest rate risk arises from the loan and savings products that the Group offers. This risk is managed through the use of appropriate financial instruments, including derivatives, with established risk limits, reporting lines, mandates and other control procedures.

The following is a summary of the Group's interest rate gap position. Items are allocated to time bands by reference to the earlier of the next contractual interest rate change and the maturity date.

As at 31 December 2019	Within 3 months £m	3 months but <6 months £m	6 months but <1 year £m	1 year but <5 years £m	>5 years £m	Non – interest bearing £m	Total £m
Assets							
Cash and balances at central banks	1,052.1	–	–	–	–	12.5	1,064.6
Loans and advances to banks	59.1	–	–	–	–	–	59.1
Loans and advances to customers	3,194.2	265.7	530.9	2,536.6	177.4	(67.1)	6,637.7
Investment securities	200.0	–	–	–	–	–	200.0
Derivative financial assets	–	–	–	–	–	4.4	4.4
Assets held for sale	–	–	–	–	–	104.1	104.1
Non-financial assets	1.7	2.3	4.4	26.1	5.4	113.2	153.1
Total assets	4,507.1	268.0	535.3	2,562.7	182.8	167.1	8,223.0
Equity and liabilities							
Amounts due to banks	(881.6)	–	–	–	–	–	(881.6)
Customer deposits	(2,747.9)	(875.8)	(1,092.6)	(1,332.4)	(20.0)	(40.7)	(6,109.4)
Derivative financial liabilities	–	–	–	–	–	(14.9)	(14.9)
Debt securities in issue	(240.7)	–	–	–	–	–	(240.7)
Lease liabilities	–	–	–	–	–	(12.4)	(12.4)
Subordinated debt liability	–	–	–	(95.9)	–	–	(95.9)
Non-financial liabilities	–	–	–	–	–	(102.4)	(102.4)
Equity	–	–	–	–	–	(765.7)	(765.7)
Total equity and liabilities	(3,870.2)	(875.8)	(1,092.6)	(1,428.3)	(20.0)	(936.1)	(8,223.0)
Notional values of derivatives	972.5	(60.0)	152.0	(1,019.8)	(44.7)	–	–
Interest rate sensitivity gap	1,609.4	(667.8)	(405.3)	114.6	118.1	(769.0)	–
Cumulative gap	1,609.4	941.6	536.3	650.9	769.0	–	–

Key risk categories

Market risk continued

As at 31 December 2018	Within 3 months £m	3 months but <6 months £m	6 months but <1 year £m	1 year but <5 years £m	>5 years £m	Non – interest bearing £m	Total £m
Assets							
Cash and balances at central banks	636.3	–	–	–	–	8.9	645.2
Loans and advances to banks	50.6	–	–	–	–	–	50.6
Loans and advances to customers	2,988.5	244.8	528.8	1,994.9	175.7	(86.8)	5,845.9
Investment securities	139.9	–	–	–	–	–	139.9
Derivative financial assets	–	–	–	–	–	1.6	1.6
Non-financial assets	1.7	2.0	4.7	22.3	3.4	107.6	141.7
Total assets	3,817.0	246.8	533.5	2,017.2	179.1	31.3	6,824.9
Equity and liabilities							
Amounts due to banks	(1,027.5)	–	–	–	–	(1.9)	(1,029.4)
Customer deposits	(1,765.2)	(813.5)	(1,002.9)	(1,382.3)	(14.0)	–	(4,977.9)
Derivative financial liabilities	–	–	–	–	–	(5.7)	(5.7)
Subordinated debt liability	–	–	–	(75.5)	–	–	(75.5)
Non-financial liabilities	–	–	–	–	–	(55.3)	(55.3)
Equity	–	–	–	–	–	(681.1)	(681.1)
Total equity and liabilities	(2,792.7)	(813.5)	(1,002.9)	(1,457.8)	(14.0)	(744.0)	(6,824.9)
Notional values of derivatives	430.7	(10.0)	40.0	(433.4)	(27.3)	–	–
Interest rate sensitivity gap	1,455.0	(576.7)	(429.4)	126.0	137.8	(712.7)	–
Cumulative gap	1,455.0	878.3	448.9	574.9	712.7	–	–

The Group considers a parallel 250 basis points (bps) movement in interest rates to be appropriate for scenario testing given the current economic outlook and industry expectations.

The Group estimates that a +/ – 250 bps movement in interest rates paid/received would impact the economic value of equity as follows:

+250 bps: £12.9 million negative (2018: £10.9 million negative)

-250 bps: £28.4 million positive (2018: £31.9 million positive)

In addition, the effect of the same two interest rate shocks is applied to the statement of financial position at year end, to determine how net interest income may change on an annualised basis for one year, as follows:

+250 bps: £76.7 million positive (2018: £65.5 million positive)

-250 bps: £3.9 million positive (2018: £0.7 million positive)

In preparing the above sensitivity analyses, the Group makes certain assumptions consistent with expected and contractual repricing behaviour as well as behavioural repayment profiles, under the two interest scenarios, of the underlying statement of financial position items. The results also include the impact of hedge transactions.

Interest rate benchmark reform

The Group is closely monitoring the market and the output from the various industry working groups managing the transition to new benchmark interest rates. This includes announcements made by LIBOR regulators, including the FCA, regarding the transition away from sterling LIBOR to Sterling Overnight Index Average (SONIA). The FCA has made clear that, at the end of 2021, it will no longer seek to persuade, or compel, banks to submit to LIBOR.

As detailed in Note 1.6(c) of the Financial Statements, the Group is exposed to the sterling LIBOR interest benchmark within its hedge accounting relationships, which is subject to interest rate benchmark reform. The hedged items include fixed rate sterling mortgage lending and consumer loans and fixed rate deposits from customers. The hedging instruments for these are also exposed to sterling LIBOR. In order to mitigate LIBOR exposure, since March 2019, the Group has designated hedging relationships against SONIA and has transacted hedging instruments referencing SONIA.

In response to the announcements, the Group has set up a LIBOR transition programme which comprises the following work streams: risk management, tax, treasury, legal, finance and systems. The programme is under the governance of the Chief Financial Officer who reports to the Board. The aim of the programme is to understand where LIBOR exposures are within the business and prepare and deliver on an action plan to enable a smooth transition to alternative benchmark rates. The Group aims to have its transition and fall back plans in place by the end of 2020.

None of the Group's current sterling LIBOR linked contracts include adequate and robust fall back provisions for a cessation of the referenced benchmark interest rate. Different working groups in the industry are working on fall back language for different instruments and different LIBORs. The Group is monitoring developments closely and will look to implement these when appropriate.

For the Group's derivatives, the International Swaps and Derivatives Association's fall back clauses were made available at the end of 2019 and the Group will begin discussion with its banks with the aim to implement this language into its International Swaps and Derivatives Association agreements in early 2020 for derivatives in the banking book.

In respect of floating rate mortgage lending, wholesale finance, funds finance, block discounting, growth capital and development finance products, the Group's response is focused on treating customers fairly and considers several aspects of transition, including the reduction of clients' exposures to legacy LIBOR contracts by amending or replacing existing contracts to include robust fall back provisions or by replacing LIBOR with relevant alternative benchmark interest rates. A critical aspect of this response is also the development of new products linked to relevant alternative benchmark interest rates.

The Group has developed a detailed communication plan with a focus on communicating with customers in a way that is clear, fair and not misleading. Implementation of this plan will commence in 2020 and will include explanation of what will happen to contracts that mature beyond the end of 2021 and the effect of LIBOR replacement on the customer. Communications will be undertaken in good time to ensure that all customers have time to consider the options available before the end of 2021. Initial communications will focus on raising awareness and engagement will increase with detailed discussions with all clients taking place well in advance of the end of 2021. The Group's response also includes a rigorous training programme to ensure that relevant client-facing staff have adequate knowledge and competence to understand the implications of LIBOR replacement and can respond to customers appropriately.

Note 1.6(c) of the Financial Statements provides information regarding amendments made to IFRS 9, IAS 39 and IFRS 7 to address the issues affecting financial reporting in the period leading up to interest rate benchmark reform. The following table provides details of the hedging instruments and hedged items in scope of these amendments by hedge type. The terms of the hedged items listed match those of the corresponding hedging instruments. All of the hedge accounting relationships are fair value hedges. In total, existing exposure to LIBOR linked hedge accounted derivatives, and corresponding hedge items have a nominal amount of £2,202.3 million. The assets and derivatives have the same maturity and nominal amount as hedging is undertaken on a proportional basis.

Market risk continued

Instrument type	Maturing in	Nominal amount £m	Hedged item
Pay 3-month sterling LIBOR, receive sterling fixed interest rate swaps	2020	167.0	Sterling fixed rate mortgage lending assets and consumer loan assets of the same maturity and nominal of the swaps
	2021	93.6	
	2022	143.9	
	2023	338.7	
	2024	41.4	
	2025	3.0	
	2026	5.9	
	2027	5.6	
	2028	13.2	
Receive 3-month sterling LIBOR, pay sterling fixed interest rate swaps	2020	240.0	Sterling fixed rate customer deposits
Put option with a floor of 0.75%	2020	100.0	Sterling 3-month sterling LIBOR mortgage lending assets with an embedded floor of 0.75%
	2021	50.0	
	2022	350.0	
	2023	350.0	
	2024	200.0	
	2025	100.0	

The Group will continue to apply the amendments made to IFRS 9, IAS 39 and IFRS 7 until the uncertainty arising from the interest rate benchmark reforms with respect to the timing and amount of the underlying cash flows the Group is exposed to ends. The Group has assumed that this uncertainty will not end until the Group's contracts that reference LIBOR are amended to specify the date the interest rate benchmark will be replaced and the relevant spread adjustments to an alternative benchmark rate calculated. This will in part be dependent on the introduction of fall back clauses which have yet to be added to the Group's contracts.

Operational risk

The Risk Committee received regular reports across the spectrum of operational risks and information security. These reports cover incidents that have arisen to allow the Committee to assess Management's response and proposed remedial actions. Although a number of incidents were raised during the course of 2019, none of these were material in nature and the Risk Committee was satisfied that the action taken was appropriate and that the control of operational incidents continued to improve. The operational risk reports were further developed throughout 2019 to include more focus on forward looking risks which permits a more strategic discussion at Risk Committee level.

Conduct, legal and compliance risk

The Group continually reviews its risk management approach to reflect the regulatory and legal environment in which the Group operates.

The Group has no appetite for knowingly behaving inappropriately resulting in unfair outcomes for its customers. During 2019, the Chief Compliance Officer commenced a programme to provide face-to-face conduct risk training for all staff. This aims to improve general levels of understanding regarding the importance of effectively managing conduct risk and supports the Group's agenda to professionalise the business. Further progress has been made in refining the Group's conduct risk appetite measures, covering the conduct risks arising in product design, sales, after-sales service, data privacy, financial crime and culture, which are expected to be implemented in early 2020. The Group also invested in its first line of defence financial crime capability and has agreed as a priority to commence the automation of standard customer due diligence processes in 2020. The Group established its 'Vulnerable Customer Network' in the year, which aims to share good practice across the business divisions and wherever possible learn from external agencies which have significant expertise in dealing with specific aspects of vulnerability.

Data privacy has been integrated within the Group's Risk Management Framework as a conduct and compliance risk and 2019 also saw the continued development of the Group's Privacy Framework.

Strategic risk

Strategic risk focusses on large, long-term risks that could become a material issue for the delivery of the Group's goals and objectives. Management of strategic risk is primarily the responsibility of Executive Management. The management of strategic risk is intrinsically linked to the corporate planning and stress testing processes and is further supported by the regular provision of consolidated business performance and risk reporting to the Executive Committee and the Board. The Board received and approved a number of reports during 2019 including the strategy update. It has also been engaged actively in the formation of the Group's ICAAP, ILAAP and RRP which are critical tools to managing strategic risk.

Systems and change risk

Customer expectations for service availability are rising with the rapid pace of new technologies leading to a significantly lower tolerance for service disruption. The Group recognises that in order to continue to be recognised for very high levels of customer satisfaction it needs to continually monitor systems risk and ensure that change is delivered with minimum disruption to customers. During 2019, the Group reviewed its operational resilience and appointed a new Chief Operating Officer and Head of Operational Resiliency to oversee the Group's operational resiliency requirements and management information.

Capital risk and management

Capital risk is the risk that the Group has insufficient capital to cover regulatory requirements and/or to support its own growth plans.

The Group's objective in managing Group capital is to maintain appropriate levels of capital to support the Group's business strategy and meet regulatory requirements.

Policies and processes for managing the Group's capital

The Group's approach to capital management is driven by strategic and organisational requirements, while also taking into account the regulatory and commercial environments in which it operates.

The Group's principal objectives when managing capital are to:

- address the expectation of the Shareholders and optimise business activities to ensure return on capital targets are achieved though efficient capital management;
- ensure that the Group and Bank hold sufficient risk capital. Risk capital caters for unexpected losses that may arise, protects Shareholders and depositors and thereby supports the sustainability of the Group and Bank through the business cycles; and
- comply with capital supervisory requirements and related regulations.

The PRA supervises the Group on a consolidated basis and receives information on the capital adequacy of, and sets capital requirements for, the Group as a whole. Shawbrook Bank Limited is the only subsidiary that is regulated by the PRA and the FCA. The aim of the capital adequacy regime is to promote safety and soundness in the financial system and embed the requirements of Pillar 3 on market discipline. Under Pillar 2, the Group completes an annual self-assessment of risks known as the ICAAP. The ICAAP is reviewed by the PRA which culminates in the PRA setting a Total Capital Requirement on the level of capital the Group and its regulated subsidiaries are required to hold. Pillar 3 requires firms to publish a set of disclosures which allow market participants to assess information on that firm's capital, risk exposures and risk assessment process. The Group's Pillar 3 disclosures can be found on the Group's website.

The Group maintains an adequate capital base with the aim of supporting the development of the business and to ensure it meets the Total Capital Requirement at all times. As a result, the Group maintains capital adequacy ratios above minimum regulatory requirements. The Group's individual regulated entities complied with all of the externally imposed capital requirements to which they are subject for the year ended 2019.

Regulation

Capital Requirements Directive IV (CRD IV) requires the Group to hold Common Equity Tier 1 capital to account for capital conservation, countercyclical and systemic risk buffers. A capital conservation buffer of 0.625% was introduced on 1 January 2016 and increased each year to 2019 in line with regulations. As at 31 December 2019 the capital conservation buffer is set at 2.500% (2018: 1.875%).

CRD IV also introduced a new leverage ratio requirement. The leverage calculation determines a ratio based on the relationship between Tier 1 capital and total consolidated exposure, being the sum of on-balance sheet exposures, derivative exposures, securities financing transaction exposures and off-balance sheet exposures. This leverage ratio is a risk-based measure that is designed to act as a supplement to risk-based capital requirements.

Minimum requirements for own funds and eligible liabilities (MREL) are applicable from 1 January 2016 and will be phased in fully by 1 January 2020. Prior to 31 December 2019, MREL will be equal to an institution's minimum regulatory capital requirements. The Bank of England has provided MREL guidance to the Group, as well as guidance on the transitional arrangements until 1 January 2020.

The regulatory minimum for the Common Equity Tier 1 capital ratio and Total Tier 1 capital ratio is 4.5% and 6.0%, respectively. The Group maintains ratios well in excess of these regulatory minimums.

The minimum requirement for the leverage ratio is 3.0%. The Group is not required to comply with the PRA leverage ratio framework until its retail deposits exceed the £50 billion threshold; however, the Group maintains a prudent risk appetite for leverage.

The Total Capital Requirement of the Group in both reported years is 10.27% of risk-weighted assets.

IFRS 9 transitional arrangements

The Group has elected to use a transitional approach when recognising the impact of adopting IFRS 9 'Financial Instruments'. The transitional approach involves phasing in the full impact using transitional factors published in Regulation (EU) 2017/2395. This permits the Group to add back to their capital base a proportion of the impact that IFRS 9 has upon their loss allowances during the first five years of use. The proportion that the Group may add back in 2019 is 85% (2018: 95%). This add back is referred to throughout the capital risk disclosures as the 'transitional adjustment for IFRS 9'.

Capital risk disclosures

The following disclosures are for the Group and its principal subsidiary, Shawbrook Bank Limited ('Bank').

Capital resources

The following table shows the regulatory capital resources managed by the Group and Bank:

	Group 2019 £m	Bank 2019 £m	Group 2018 £m	Bank 2018 £m
Share capital	2.5	175.5	2.5	175.5
Share premium account	87.3	81.0	87.3	81.0
Capital redemption reserve	–	17.2	–	16.4
Merger reserve	–	1.6	–	1.6
Retained earnings	551.9	343.6	467.3	260.8
Intangible assets	(66.6)	(46.6)	(66.4)	(46.4)
Transitional adjustment for IFRS 9	22.1	22.1	25.7	25.5
Common Equity Tier 1 capital	597.2	594.4	516.4	514.4
Capital securities	124.0	125.0	124.0	125.0
Additional Tier 1 capital	124.0	125.0	124.0	125.0
Total Tier 1 capital	721.2	719.4	640.4	639.4
Subordinated debt liability[1]	94.4	94.9	74.4	75.0
Tier 2 capital	94.4	94.9	74.4	75.0
Total regulatory capital	815.6	814.3	714.8	714.4

Regulatory capital reconciles to total equity per the statement of financial position as follows:

	Group 2019 £m	Bank 2019 £m	Group 2018 £m	Bank 2018 £m
Total regulatory capital	815.6	814.3	714.8	714.4
Subordinated debt liability[1]	(94.4)	(94.9)	(74.4)	(75.0)
Intangible assets	66.6	46.6	66.4	46.4
Transitional adjustment for IFRS 9	(22.1)	(22.1)	(25.7)	(25.5)
Total equity	765.7	743.9	681.1	660.3

[1] For the purpose of regulatory capital calculations, capitalised interest of £1.5 million is excluded for both Group and Bank (2018: £1.1 million). Accrued interest is payable bi-annually and is therefore excluded from capital reserves.

Capital risk and management

The following table shows the movement in Total Tier 1 capital during the year:

	Group 2019 £m	**Bank 2019 £m**	Group 2018 £m	Bank 2018 £m
Total Tier 1 capital as at 1 January	**640.4**	**639.4**	557.4	556.4
Impact of adopting IFRS 9	**–**	**–**	(16.0)	(15.7)
Restated balance as at 1 January	**640.4**	**639.4**	541.4	540.7
Movement in Common Equity Tier 1 capital:				
Increase/(decrease) in capital redemption reserve	**–**	**0.8**	–	(0.3)
Movement in retained earnings:				
Profit for the year[1]	**93.6**	**92.6**	84.1	85.1
Share-based payments	**0.8**	**–**	(0.3)	–
Coupon paid on capital securities[1]	**(9.8)**	**(9.8)**	(9.8)	(9.8)
Increase in intangible assets	**(0.2)**	**(0.2)**	(0.7)	(1.8)
(Decrease)/increase in transitional adjustment for IFRS 9	**(3.6)**	**(3.4)**	25.7	25.5
Total movement in Common Equity Tier 1 capital	**80.8**	**80.0**	99.0	98.7
Total Tier 1 capital as at 31 December	**721.2**	**719.4**	640.4	639.4

Risk-weighted assets

	Group 2019 £m	**Bank 2019 £m**	Group 2018 £m	Bank 2018 £m
Credit risk				
Property Finance	**2,097.0**	**2,097.0**	1,660.7	1,660.7
Business Finance	**1,749.2**	**1,749.2**	1,464.3	1,476.2
Consumer Lending	**517.4**	**517.4**	560.2	560.2
Other	**155.5**	**155.4**	134.4	133.8
Total credit risk	**4,519.1**	**4,519.0**	3,819.6	3,830.9
Operational risk	**451.6**	**449.7**	383.8	383.8
Credit valuation adjustment	**3.8**	**3.8**	3.4	3.4
Total risk-weighted assets	**4,974.5**	**4,972.5**	4,206.8	4,218.1

[1] Comparatives for the year ended 31 December 2018 have been restated to reflect amendments to IAS 12 'Income Taxes'. See Note 1.6(b) of the Financial Statements for details.

Capital ratios

	Group 2019 £m	Bank 2019 £m	Group 2018 £m	Bank 2018 £m
Common Equity Tier 1 capital ratio	12.0	12.0	12.3	12.2
Total Tier 1 capital ratio	14.5	14.5	15.2	15.2
Total capital ratio	16.4	16.4	17.0	16.9

Leverage

	Group 2019 £m	Bank 2019 £m	Group 2018 £m	Bank 2018 £m
Total Tier 1 capital	721.2	719.4	40.4	639.4
Exposure measure				
Total statutory assets (excluding derivatives)	8,218.6	8,244.9	6,823.3	6,804.0
Off-balance sheet items	150.8	150.8	197.7	197.6
Exposure value for derivatives	12.8	11.5	6.3	6.3
Transitional adjustment for IFRS 9	22.1	22.1	25.7	25.5
Other regulatory adjustments	(66.6)	(46.6)	(66.4)	(46.4)
Total exposures	8,337.7	8,382.7	6,986.6	6,987.0
Leverage ratio	8.6%	8.6%	9.2%	9.2%

Off-balance sheet items comprise pipeline and committed facilities balances which have a credit conversion factor of medium risk attached to them.

Exposure values associated with derivatives have been reported in compliance with CRD IV rules. The derivative measure is calculated as the replacement cost for the current exposure plus an add-on for future exposure and is not reduced for any collateral received or grossed up for collateral provided.

Other regulatory adjustments comprise asset amounts deducted in determining Tier 1 capital.

Capital risk and management

IFRS 9 transitional arrangements impact analysis

As detailed on page 135, the Group has elected to use a transitional approach when recognising the impact of adopting IFRS 9. To illustrate the impact of using this transitional approach, the following tables provide an overview of the Group's reported capital metrics (including transitional adjustments), compared to the capital metrics if IFRS 9 transitional arrangements had not been applied (i.e. full adoption):

	2019		2018	
Group	**Including transitional arrangements**	**Transitional adjustments not applied**	Including transitional arrangements	Transitional adjustments not applied
Capital resources				
Common Equity Tier 1 capital (£m)	**597.2**	**575.1**	516.4	490.7
Total Tier 1 capital (£m)	**721.2**	**699.1**	640.4	614.7
Total regulatory capital (£m)	**815.6**	**793.5**	714.8	689.1
Risk-weighted assets				
Total risk-weighted assets (£m)	**4,974.5**	**4,955.5**	4,206.8	4,189.5
Capital ratios				
Common Equity Tier 1 capital ratio (%)	**12.0**	**11.6**	12.3	11.7
Total Tier 1 Capital Ratio (%)	**14.5**	**14.1**	15.2	14.7
Total capital ratio (%)	**16.4**	**16.0**	17.0	16.4
Leverage				
Leverage ratio total exposures (£m)	**8,337.7**	**8,315.6**	6,986.6	6,960.9
Leverage ratio (%)	**8.6**	**8.4**	9.2	8.8

	2019		2018	
Bank	**Including transitional arrangements**	**Transitional adjustments not applied**	Including transitional arrangements	Transitional adjustments not applied
Capital resources				
Common Equity Tier 1 capital (£m)	**594.4**	**572.3**	514.4	488.9
Total Tier 1 capital (£m)	**719.4**	**697.3**	639.4	613.9
Total regulatory capital (£m)	**814.3**	**792.2**	714.4	688.9
Risk-weighted assets				
Total risk-weighted assets (£m)	**4,972.5**	**4,953.5**	4,218.1	4,202.9
Capital ratios				
Common Equity Tier 1 capital ratio (%)	**12.0**	**11.6**	12.2	11.6
Total Tier 1 Capital Ratio (%)	**14.5**	**14.1**	15.2	14.6
Total capital ratio (%)	**16.4**	**16.0**	16.9	16.4
Leverage				
Leverage ratio total exposures (£m)	**8,382.7**	**8,360.6**	6,987.0	6,961.5
Leverage ratio (%)	**8.6**	**8.3**	9.2	8.8

ICAAP, ILAAP and stress testing

The ICAAP, ILAAP and associated stress testing exercises represent important elements of the Group's ongoing risk management processes. The results of the risk assessment contained in these documents is embedded in the strategic planning process and risk appetite to ensure that sufficient capital and liquidity are available to support the Group's growth plans as well as cover its regulatory requirements at all times and under varying circumstances.

The ICAAP and ILAAP are reviewed at least annually, and more often in the event of a material change in capital or liquidity. Ongoing stress testing and scenario analysis outputs are used to inform the formal assessments and determination of required buffers, the strategy and planning for capital and liquidity management as well as the setting of risk appetite limits.

The Board and Executive Management have engaged in a number of exercises which have considered and developed stress test scenarios. The analysis enables Management to evaluate the Group's capital and funding resilience in the face of severe but plausible risk shocks. In addition to the UK Annual Cyclical Scenario prescribed by the Regulator, the stress tests have included a range of Group wide, multi-risk category stress tests, generic and idiosyncratic financial shocks as well as operational risk scenario analyses. Stress testing is an integral part of the adequacy assessment processes for liquidity and capital, and the setting of tolerances under the annual review of Group risk appetite.

The Group also performed reverse stress tests to help Executive Management understand the full continuum of adverse impact and therefore the level of stress at which the Group would breach its individual capital and liquidity guidance requirements as set by the Regulator under the ICAAP and ILAAP processes.

Recovery Plan and Resolution Pack

The Group has prepared a RRP in accordance with PRA Supervisory Statements SS9/17 and SS19/13. The plan represents the Group's 'Living Will' and examines in detail:

- the consequences of severe levels of stress (i.e. beyond those in the ICAAP) impacting the Group at a future date;
- the state of preparedness and contingency plan to respond to and manage through such a set of circumstances; and
- the options available to Executive Management to withstand and recover from such an environment.

The plan is prepared annually, or more frequently in the event of a material change in the Group's status, capital or liquidity position. The Board of Directors and Executive Management are fully engaged in considering the scenarios and options available for remedial actions to be undertaken.

The Board considers that the Group's business model, its supportive owners and the diversified nature of its business markets provides it with the flexibility to consider selective business or portfolio disposals, loan book run off, equity raising or a combination of these actions. The Group would invoke the RRP in the event they are required.

Group viability statement

The Directors have assessed the outlook for the Group over a longer period than the 12 months required by the going concern statement in line with good governance practice and reporting.

The Board aims to build a sustainable lending and savings bank for SMEs and consumers over the medium to long-term. The Board monitors a five-year strategic plan that provides a robust planning tool against which strategic decisions are made. Whilst the Board has no reason to believe that the Group will not be viable for a five-year period, given the inherent uncertainty involved, the Board concluded that a three-year period is an appropriate length of time to perform a viability assessment with a greater level of certainty.

The assessment included the following:

- the Board considered updates to the strategy and five-year plan at various times during 2019 and approved the strategic update in November 2019 that outlined the business plans and financial projections from 31 December 2019 to 31 December 2024;
- the Board considered the quantity and quality of capital resources available to support the delivery of the Group's objectives, including consideration of the effects of a changing regulatory landscape on the Total Capital Requirement, Pillar 2B and the CRD IV combined buffer requirements, together with the effect of the Group's capital contingency plan to restore the capital position in scenarios of capital headwinds;
- the Board considered the Group's current and forecast liquidity and funding plan supporting the strategic objectives;
- the Board reviewed and evaluated the top and emerging risks for the business. This included a review of the cyber intelligence threat and the annual information risk assessment, together with the technology roadmap for improvements in the technology control environment in 2020; and
- the Board reviewed and approved the ICAAP and ILAAP. The Group is not large enough to participate in the annual Bank of England concurrent stress testing programme but has, as part of its ICAAP, performed a variety of equivalent stress tests and reverse stress tests of its business. The stress tests were derived through discussions with Executive Management and the Board, after considering the Group's top risks. The Group also considered its funding and liquidity adequacy in the context of the reverse stress testing. The risks associated with the UK leaving the EU have been considered and the Board believe these risks were captured within its stress testing scenarios. The stress tests enable the Group to assess the impact of a number of severe but plausible scenarios on its business model. In the case of reverse stress testing, the Board is able to assess scenarios and circumstances that would render its business model unviable, thereby identifying business vulnerabilities and ensuring the development of early warning indicators and potential mitigating actions.

The Board also reviewed and evaluated the possible impacts of Covid-19 in Q1 2020 against the original financial and business plans over the 2020-2023 period and this included the following actions:

- the Board considered the Group's operational resilience in relation to the government's mandated social distancing rules and noted that the Group has been operating successfully since March 2020, with the majority of employees working from home and the Group's material outsourced suppliers providing their critical services successfully under current conditions. The Board believe that this can operate for an extended period;
- the existing financial plans were stress tested by assessing the Group's customer and sector exposure to highlight any sectors at risk of impairment but also including the unprecedented fiscal and monetary response from the government and the Bank of England to support the UK economy and provide both capital and impairment relief from payment holidays;
- the risk that there could be an increased likelihood of an extended period of disruption in the debt financial markets preventing the Group from raising additional hybrid debt capital over the plan period was assessed; and
- the Board assessed the financial implications of the risks associated with Covid-19, including the expected effect of Management actions taken in response, against the most severe but plausible scenario used in the Board's assessment of the ICAAP approved in 2020. This scenario was the 'Rates Down'[1] scenario specified by the Bank of England for use in preparing ICAAP stress tests. Having regard for the severe financial outcomes from this scenario and the reverse stress tests also conducted, the Board concluded that both capital and liquidity remained within present regulatory requirements over the period. It is not the Board's view that the 'Rates Down' scenario is the likely economic outcome of the current Covid-19 pandemic, particularly having regard for the significant government and Bank of England support for the economy, but provides a helpful baseline for the Board's consideration of the viability of the business over the period under review.

Based on the results of these assessments, the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over a period of at least three years.

[1] The Bank of England publishes annual stress test scenarios with the 'Rates Down' scenario (an extension of the Annual Cyclical Scenario) being the most severe for the Group's forecast capital position. This scenario shows a peak-to-trough fall in UK GDP of 4.7%, unemployment peaking at 9.2%, UK residential property price falls of 33% and Bank of England Base Rate falling to 0% for the duration of the stress.

Financial Statements

Financial Statements.

Independent auditor's report

to the members of Shawbrook Group plc

1. Our opinion is unmodified

We have audited the financial statements of Shawbrook Group plc ("the Group") for the year ended 31 December 2019 which comprise the *Consolidated statement of profit and loss and other comprehensive income, Consolidated and Company statement of financial position, Consolidated statement in changes in equity, Consolidated and Company statement of cash flows*, and the related notes, including the accounting policies in note 1.

In our opinion:

— the financial statements give a true and fair view of the state of the Group's and the parent Company's affairs as at 31 December 2019 and the Group's profit for the year then ended;

— the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);

— the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and

— the financial statements have been prepared in accordance with requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were first appointed as auditor by the directors in June 2011. The period of total uninterrupted engagement is for the nine financial years ended 31 December 2019. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

Overview		
Materiality: group financial statements as a whole		£5.0m (2018: 4.5m) 4.5% (2018: 4.6%) of profit before tax
Coverage		100% (2018: 100%) of Group profit before tax
Key audit matters		**vs 2018**
Event driven	Going Concern	**New**
Recurring risks	Uncertainty due to Britain leaving the European Union	◀▶
	Expected Credit Loss provisioning	▼
	Effective interest rate accounting	◀▶
	Provisions relating to conduct matters	◀▶
	Valuation of goodwill	▼
	Recoverability of parent company's investment in subsidiaries	◀▶

2. Key audit matters: including our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

Going Concern

Refer to page 56 (Audit Committee Report), page 78 (Director's report), page 96 (Risk Management Report), page 141 (Viability statement).

Risk vs 2018: **NEW**

The risk	Our response
Disclosure quality The financial statements explain how the Board has formed a judgement that it is appropriate to adopt the going concern basis of preparation for the Group and parent Company. That judgement is based on an evaluation of the inherent risks to the Group's and Company's business model and how those risks might affect the Group's and Company's financial resources or ability to continue operations over a period of at least a year from the date of approval of the financial statements. The risk most likely to adversely affect the Group's and Company's available financial resources over this period was insufficient regulatory capital to meet minimum regulatory capital levels over the course of the next 12 months. There are also less predictable but realistic impacts, such as the impact of Coronavirus COVID-19, which could result in a rapid increase in the level of impairment in loans and advances to customers. The risk for our audit was whether or not those risks were such that they amounted to a material uncertainty that may have cast significant doubt about the ability to continue as a going concern. Had they been such, then that fact would have been required to have been disclosed.	Our procedures included: — **Our Covid-19 knowledge:** We considered the directors' assessment of Covid-19 related sources of risk for the Company's business and financial resources compared with our own understanding of the risks. We considered the directors' plans to take action to mitigate the risks; — **Sensitivity analysis:** We considered sensitivities over the level of available financial resources indicated by the Company's financial forecasts taking account of severe plausible downside effects that could arise from these risks individually and collectively. We challenged the assumptions underpinning the stress testing undertaken by the Directors of the identified critical factors in their financial forecasts. — **Evaluating Directors' intent:** We evaluated the achievability of the actions the Directors consider they would take to improve the position should the risks materialise. — **Assessing transparency:** We assessed the completeness and accuracy of the matters covered in the going concern disclosure, including those in the strategic report, by comparing the overall picture against our understanding of the risks. **Our results** We found the going concern disclosure without any material uncertainty to be acceptable (2018: acceptable).

Independent Auditor's Report

The impact of uncertainties due to Britain exiting the European Union on our audit

Refer to pages 95 and 97 (Risk Management Report).

Risk vs 2018: ◀▶

The risk	Our response
Unprecedented levels of uncertainty All audits assess and challenge the reasonableness of estimates, in particular as described in Expected credit loss provisioning, Effective interest rate accounting and Valuation of goodwill – Business Finance below, and related disclosures and the appropriateness of the going concern basis of preparation of the financial statements (see above). All of these depend on assessments of the future economic environment and the Group and parent Company's future prospects and performance. Brexit is one of the most significant economic events for the UK and its effects are subject to unprecedented levels of uncertainty of consequences with the full range of possible effects unknown.	We developed a standardised firm-wide approach to the consideration of the uncertainties arising from Brexit in planning and performing our audits. Our procedures included: — **Our Brexit knowledge:** We considered the directors' assessment of Brexit-related sources of risk for the Group and parent Company's business and financial resources compared with our own understanding of the risks. We considered the directors' plans to take action to mitigate the risks. — **Sensitivity analysis:** When addressing Expected credit loss provisioning and Valuation of goodwill – Business Finance, we compared the directors' analysis to our assessment of the full range of reasonably possible scenarios resulting from Brexit uncertainty. — **Assessing transparency:** As well as assessing individual disclosures as part of our procedures on Expected credit loss provisioning, Effective interest rate accounting and Valuation of goodwill – Business Finance, we considered all of the Brexit related disclosures together, including those in the strategic report, comparing the overall picture against our understanding of the risks. **Our results:** As reported under Expected credit loss provisioning, Effective interest rate accounting and Valuation of goodwill – Business Finance, we found the resulting estimates and related disclosures of credit impairment provisioning, effective interest rate accounting and valuation of goodwill and disclosures in relation to going concern to be acceptable. However, no audit should be expected to predict the unknowable factors or all possible future implications for a company and this is particularly the case in relation to Brexit.

Expected Credit Loss provisioning

£61.1 million; 2018: £67.8 million.

Refer to page 57 (Audit Committee Report), pages 101-124 (Risk management report), pages 173-174 (accounting policies) and page 184 (financial disclosures).

Risk vs 2018: ▼ *This risk was considered higher in 2018, as that was the first year of application of IFRS 9.*

The risk

Subjective estimate
The estimation of expected credit losses ("ECL") on financial assets involves significant judgement and estimates. The key areas where we identified greater levels of management judgement and therefore increased levels of audit focus in the Group's estimation of ECLs are:

Economic scenarios – IFRS 9 requires the Group to measure ECLs on an unbiased forward-looking basis reflecting a range of future economic conditions. Significant management judgement is applied in determining the economic scenarios used and the probability weightings applied to them.

Significant Increase in Credit Risk – For each portfolio the criteria selected to identify a significant increase in credit risk of loans, and as such the stage loans are allocated to, is a key area of judgement within the Group's ECL calculation as these criteria determine whether a 12 month or lifetime provision is recorded.

Model estimations – Inherently judgemental modelling is used to estimate ECLs, particularly in determining Probabilities of Default "PD") and Loss Given Default ("LGD"), and to a lesser extent Exposures at Default ("EAD"). These models utilise both the Group's historical data and external data inputs.

Post-model adjustments – Adjustments to the model-driven ECL results are raised by management to address known impairment model limitations or emerging trends. They represent approximately 3.4% of the ECL. Management judgement is involved in estimating these amounts especially in relation to development finance loans.

The effect of these matters is that, as part of our risk assessment, we determined that ECL provisioning has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. The risk management report (page 115) discloses the sensitivity estimated by the Group.

Disclosure quality
The disclosures regarding the Group's application of IFRS 9 are key to explaining the key judgements and material inputs to the IFRS 9 ECL results.

Our response

Our procedures included:

- **Controls testing:** We performed end to end process walk-throughs to identify the key systems, applications and controls used in the ECL processes. We tested the relevant general IT and applications controls over key systems used in the ECL process.
- **Test of details:** For a sample of loans and advances we conducted credit file reviews to assess the appropriateness of the stage allocation and associated ECL estimate.
- **Historical comparisons:** We critically assessed the Group's assumptions in respect of significant increase in credit risk; likely recoverable collateral value, including timing of recovery; and the probability of possession given default by comparing them to the Group's historical experience. For the Group's probability of default models we assessed the reasonableness of the model predictions by comparing them against actual results.
- **Benchmarking assumptions:** We compared the Group's key assumptions on significant increase in credit risk; likely recoverable collateral value, including timing of recovery; probability of possession given default; and the probability weightings attached to each economic scenario to comparable peer group organisations.
- **Our sector experience:** We challenged the Group's key assumptions on significant increase in credit risk; the definition of default; likely recoverable collateral value, including timing of recovery; probability of default; probability of possession given default based on our knowledge of the Group and experience of the industry in which it operates. We involved our own economic specialists to assist us in assessing the appropriateness of the Group's methodology for determining the economic scenarios used and the probability weightings applied to them.
- **Sensitivity analysis:** We performed sensitivity analysis over the Group's key assumptions on significant increase in credit risk; likely recoverable collateral value, including timing of recovery; probability of possession given default; and the probability weightings attached to each economic scenario.
- **Independent evaluation:** We have critically challenged and evaluated management's assumptions underpinning the post model adjustments;
- **Assessing transparency:** We evaluated whether the disclosures appropriately reflect and address the uncertainty which exists when determining the expected credit losses. As a part of this, we assessed the sensitivity analysis that is disclosed. In addition, we challenged whether the disclosure of the key judgements and assumptions made was sufficiently clear.

Our results:
We found the Group's estimate and related disclosures of the provision for expected credit loss to be acceptable (2018 result: acceptable).

Independent Auditor’s Report

Effective interest rate accounting
£396.9 million; 2018: £351.1 million.
Refer to page 57 (Audit Committee Report), pages 163 and 175-176 (accounting policy) and page 180 (financial disclosures).
Risk vs 2018: ◀▶

The risk	Our response
Subjective estimate Interest and related fee income on originated and acquired loans are recognised in line with the effective interest rate method, which spreads the income over the expected lives of the loans. The directors apply judgement in deciding and assessing the expected repayment profiles used to determine the EIR period. The most critical element of judgement in this area is the estimation of the future redemption profiles of the loans. This is informed by product mix and past customer behaviour of when loans are repaid. The effect of these matters is that, as part of our risk assessment, we determined that EIR income has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole, and possibly many times that amount. The financial statements (note 1.9(a)) disclose the sensitivity estimated by the Group.	Our procedures included: — **Our sector experience:** We assessed the key assumptions behind the expected lives and profiles of significant loan products against our own knowledge of industry experience and trends, including benchmarking with comparable lenders; — **Historical comparison:** We assessed the reasonableness of the model’s expected repayment profiles assumptions against historical experience of loan lives based on customer behaviour, product mix and recent performance; — **Sensitivity analysis:** We assessed the models for their sensitivities to changes in the key assumptions by considering different profiles to help us assess the reasonableness of the assumptions used and identify areas of potential additional focus; and — **Assessing transparency:** We assessed the adequacy of the Group’s disclosures about the degree of estimation involved in arriving at the interest income recognised. **Our results:** We found the amount of EIR income recognised in the year to be acceptable. (2018: acceptable)

Provision relating to conduct matters

£7.3 million; 2018: £10.6 million.

Refer to page 58 (Audit Committee Report), pages 177 (accounting policy) and pages 198-199 and 212 (financial disclosures).

Risk vs 2018: ◀▶

The risk

Omitted exposure
Certain of the Group's lending activities give rise to ongoing exposure under Section 75 of the Consumer Credit Act; should products be mis-sold by suppliers who subsequently become insolvent, the Group is liable for customer remediation. Whether there is a liability is inherently uncertain.

Subjective estimate
Due to the uncertainties that can arise in measuring potential obligations, the directors apply judgement in estimating the value of any associated provisions.

In particular, the Group continues to receive an inflow of customer complaints relating to its financing of solar lending products where the original supplier is no longer solvent.

During the year, the number of products reaching the six year complaints time bar increased, reducing the number of forecast future complaints and consequently the associated provision. Nevertheless, there remains significant estimation uncertainty around the year end provision.

The key elements of judgement are the estimation of future customer complaints rate, the uphold rate of complaints received and the estimated redress cost per upheld complaint. These judgements are informed by the Group's past complaint and claim experience. Given the limited historical information, there is a risk that the actual experience may differ from the Group's expectation.

The effect of these matters is that, as part of our risk assessment, we determined that the provision related to conduct matters has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (note 1.9(c)) disclose the sensitivity estimated by the Group.

Our response

Our procedures included:

— **Our sector experience:** We compared common industry issues with those areas provided for by the Group to determine whether these issues were relevant to the business and to consider completeness of the provisions assessed by the directors.

— **Independent evaluation:** We critically challenged and evaluated management's assumptions in estimating the expected exposure. This included independent estimation of the expected future customer complaint rates, claims uphold rates and redress per upheld complaint;

— **Historical comparison:** We assessed the reasonableness of the key assumptions against historical experience of customer complaint levels, complaint uphold rates and redress paid;

— **Sensitivity analysis:** We assessed and challenged the reasonableness of the model's key assumptions, by performing stress tests on the number of expected future complaints, the uphold level of complaints and the redress paid per complaint;

— **Assessing transparency:** We considered the adequacy of the Group's disclosures in detailing significant conduct related matters and potential liabilities.

Our results:
We found the resulting estimate of the conduct provisions recognised and the contingent liabilities disclosures made to be acceptable (2018: acceptable).

Valuation of goodwill – Business Finance

£34.7 million; 2018: £34.7 million

Refer to page 57 (Audit Committee Report), pages 168 and 176-177 (accounting policy) and page 194 (financial disclosures).

Risk vs 2018: ▼ *Risk of impairment of the goodwill balance reduces as the Business Finance division continues to grow, providing additional headroom.*

The risk

Forecast-based valuation
Of the total goodwill balance of £43.7 million, £34.7 million relates to Business Finance, being the area of most significant judgement in light of the size of the balance and, whilst improving, weaker than forecast financial performance in the year.

The carrying value of goodwill is tested for impairment on the occurrence of an impairment trigger or otherwise annually.

The estimated recoverable amount is subjective due to the inherent uncertainty involved in forecasting future cash flows and growth in the division, and in selecting an appropriate discount rate.

The effect of these matters is that, as part of our risk assessment, we determined that the valuation of goodwill has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (note 1.9(b)) disclose the sensitivity estimated by the Group.

Our response

Our procedures included:

— **Our sector experience:** Assessing the appropriateness of assumptions used based on market trends and events, in particular those relating to forecast revenue growth as the key driver of net operating income, discount rate and incremental capital requirements in Business Finance;

— **Benchmarking assumptions:** Comparing the Group's assumptions to external comparable data in relation to key inputs such as projected economic growth and discount rates;

— **Sensitivity analysis:** Performing breakeven analysis on the assumptions noted above using our data analytic capabilities;

— **Assessing transparency:** Assessing whether the Group's disclosures about the sensitivity of the outcome of the impairment assessment to changes in key assumptions reflected the risks inherent in the valuation of goodwill.

Our results:
We found the resulting estimate of the carrying value of goodwill to be acceptable (2018: acceptable)

Recoverability of parent Company's investment in subsidiary

Parent Company risk
£410.0 million; 2018: £409.2 million

Refer to page 197 (financial disclosures).

Risk vs 2018: ◀▶

The risk

Low risk, high value
The carrying amount of the parent company's investment in subsidiary represents 84% (2018: 84%) of the company's total assets.

Their recoverability is not at a high risk of significant misstatement or subject to significant judgement or estimate.

However, due to their materiality in the context of the parent company's financial statements, this is considered to be the area that has the greatest effect on our overall parent company audit.

Our response

Our procedures included:

— **Tests of detail:** Comparing the carrying amount of the investment with the subsidiary's financial statements to identify whether its net assets, being an approximation of its minimum recoverable amount, were in excess of the carrying amount and assessing whether the subsidiary has historically been profit-making.

Our results:
We found the Group's assessment of the recoverability of the investment in subsidiary to be acceptable (2018: acceptable)

3. Our application of materiality and an overview of the scope of our audit

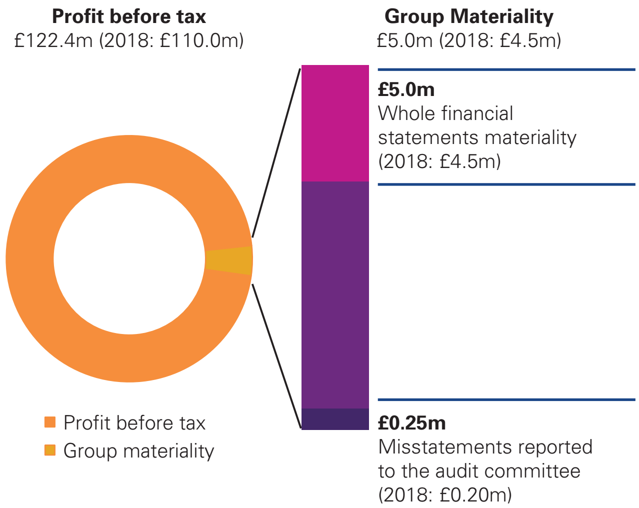
Materiality for the Group financial statements as a whole was set at £5.0m (2018: £4.5m), determined with reference to a benchmark of Group profit before tax, of which it represents 4.5% (2018: 4.6% Group profit before tax, normalised to exclude one off insurance recoveries).

Materiality for the parent Company financial statements as a whole was set at £4.0m (2018: £4.5m), determined with reference to a benchmark of company total assets, of which it represents 1.0% (2018: 0.9%).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £0.25m, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Team structure

The Group team performed the audit of the Group as if it was a single aggregated set of financial information. The audit was performed using the materiality level set out above.



4. We have nothing to report on going concern

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or the Group or to cease their operations, and as they have concluded that the Company's and the Group's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over their ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the group or the company will continue in operation.

We identified going concern as a key audit matter (see section 2 of this report). Based on the work described in our response to that key audit matter, we are required to report to you if we have anything material to add or draw attention to in relation to the directors' statement in Note 1 to the financial statements on the use of the going concern basis of accounting with no material uncertainties that may cast significant doubt over the Group and Company's use of that basis for a period of at least twelve months from the date of approval of the financial statements.

We have nothing to report in these respects.

5. We have nothing to report on other information in the Annual Report

The directors are responsible for the other information in the Annual Report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

Strategic report and directors' report

Based solely on our work on the other information:

— we have not identified material misstatements in the strategic report and the directors' report;

— in our opinion the information given in those reports for the financial year is consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. We have nothing to report on the other matters on which we are required to report by exception

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

— adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or

— the parent Company financial statements are not in agreement with the accounting records and returns; or

— certain disclosures of directors' remuneration specified by law are not made; or

— we have not received all the information and explanations we require for our audit.

— We have nothing to report in these respects.

Independent Auditor's Report

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 79, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

A fuller description of our responsibilities is provided on the FRC's website at **www.frc.org.uk/auditorsresponsibilities**.

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience through discussion with the directors and other management (as required by auditing standards), and from inspection of the group's regulatory and legal correspondence and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. The potential effect of these laws and regulations on the financial statements varies considerably.

Firstly, the Group is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies legislation), distributable profits legislation and taxation legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Group is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation or the loss of the Group's license to operate. We identified the following areas as those most likely to have such an effect: specific areas of regulatory capital and liquidity, conduct, money laundering and financial crime and certain aspects of the company legislation recognising the financial and regulated nature of the Group's activities. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and other management and inspection of regulatory and legal correspondence, if any. Through these procedures, we became aware of actual or suspected non-compliance and considered the effect as part of our procedures on the related financial statement items. Further detail in respect of conduct related matters is set out in the key audit matter disclosures in section 2 of this report.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8. The purpose of our audit work and to whom we owe our responsibilities

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

Simon Ryder (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants
15 Canada Square
London
E14 5GL
16 April 2020

Consolidated statement of profit and loss and other comprehensive income

For the year ended 31 December 2019

	Note	**2019 £m**	2018 £m
Interest income calculated using the effective interest rate method	3	**406.0**	356.0
Other interest and similar income	3	**(0.3)**	0.8
Interest expense and similar charges	4	**(113.2)**	(87.3)
Net interest income		**292.5**	269.5
Operating lease rental income		**10.3**	10.0
Depreciation of operating leases	18	**(8.6)**	(7.6)
Other operating lease income/(expense)		**0.2**	(0.6)
Net income from operating leases		**1.9**	1.8
Fee and commission income	5	**9.7**	10.7
Fee and commission expense		**(8.7)**	(8.4)
Net fee and commission income		**1.0**	2.3
Net gains/(losses) on financial instruments mandatorily at fair value through profit or loss[1]	17	**2.3**	(0.4)
Other operating (expense)/income[1]		**(2.6)**	0.9
Net operating income		**295.1**	274.1
Administrative expenses[1]	6	**(138.5)**	(130.3)
Impairment losses on financial assets[2]	11		
Impairment losses on financial assets (excluding insurance recovery)		*(29.9)*	*(36.2)*
Insurance recovery		*–*	*13.0*
		(29.9)	(23.2)
Provisions for liabilities and charges	27	**(4.5)**	(10.1)
Total operating expenses		**(172.9)**	(163.6)
Share of results of associate	21	**(0.1)**	(0.5)
Gain on disposal of subsidiary	12	**0.3**	–
Profit before tax		**122.4**	110.0
Tax[3]	13	**(28.8)**	(25.9)
Profit after tax, being total comprehensive income, attributable to owners[3]		**93.6**	84.1

The notes on pages 157 to 213 are an integral part of these financial statements.

[1] Comparatives for the year ended 31 December 2018 have been restated to reclass £0.9 million of foreign exchange losses on derivative financial instruments, from administrative expenses to net gains/(losses) on financial instruments mandatorily at fair value through profit or loss, to ensure compliance with the accounting policy set out in Note 1.3. Other foreign exchange gains of £0.9 million have been reclassified from administrative expenses to other operating expense/(income). The net impact to administrative expenses is £nil and net operating income and total operating expenses are unchanged as a result of this reclass.

[2] During the year ended 31 December 2018, the Group received £13.0 million from the Group's insurance claim in respect of a controls breach identified in the Business Finance division in 2016. To allow for meaningful comparison between the reported years, subtotals have been provided to present the insurance recovery separately.

[3] Comparatives for the year ended 31 December 2018 have been restated to reflect amendments to IAS 12 'Income Taxes'. See Note 1.6(b) for details.

Consolidated and Company statement of financial position

As at 31 December 2019

	Note	**Group 2019 £m**	**Company 2019 £m**	Group 2018 £m	Company 2018 £m
Assets					
Cash and balances at central banks		**1,064.6**	**–**	645.2	–
Loans and advances to banks		**59.1**	**–**	50.6	–
Loans and advances to customers	14	**6,637.7**	**–**	5,845.9	–
Investment securities	16	**200.0**	**–**	139.9	–
Derivative financial assets	17	**4.4**	**–**	1.6	–
Property, plant and equipment[1]	18	**57.2**	**–**	39.1	–
Intangible assets	19	**66.6**	**–**	66.4	–
Deferred tax assets	20	**14.9**	**–**	18.0	–
Investment in associate	21	**5.4**	**–**	5.5	–
Other assets	22	**9.0**	**1.4**	12.7	1.8
Assets held for sale	23	**104.1**	**–**	–	–
Investment in subsidiaries	24	**–**	**410.0**	–	409.2
Subordinated debt receivable	31	**–**	**96.4**	–	76.1
Total assets		**8,223.0**	**507.8**	6,824.9	487.1
Liabilities					
Amounts due to banks	25	**881.6**	**–**	1,029.4	–
Customer deposits	26	**6,109.4**	**–**	4,977.9	–
Provisions for liabilities and charges	27	**8.3**	**–**	11.6	–
Derivative financial liabilities	17	**14.9**	**–**	5.7	–
Debt securities in issue	28	**240.7**	**–**	–	–
Current tax liabilities		**1.0**	**–**	4.0	–
Lease liabilities[1]	29	**12.4**	**–**	–	–
Other liabilities	30	**93.1**	**0.1**	39.7	0.3
Subordinated debt liability	31	**95.9**	**95.9**	75.5	75.5
Total liabilities		**7,457.3**	**96.0**	6,143.8	75.8
Equity					
Share capital	32	**2.5**	**2.5**	2.5	2.5
Share premium account		**87.3**	**87.3**	87.3	87.3
Capital securities	33	**124.0**	**124.0**	124.0	124.0
Retained earnings		**551.9**	**198.0**	467.3	197.5
Total equity		**765.7**	**411.8**	681.1	411.3
Total equity and liabilities		**8,223.0**	**507.8**	6,824.9	487.1

The notes on pages 157 to 213 are an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 16 April 2020 and were signed on its behalf by:

Ian Cowie
Chief Executive Officer

Dylan Minto
Chief Financial Officer

Registered number 07240248

[1] Adoption of IFRS 16 'Leases' on 1 January 2019 resulted in the recognition of right-of-use assets included in property plant and equipment and lease liabilities. See Note 1.6(a) for details.

Consolidated statement of changes in equity

For the year ended 31 December 2019

Year ended 31 December 2019	**Share capital £m**	**Share premium account £m**	**Capital securities £m**	**Retained earnings £m**	**Total equity £m**
As at 1 January 2019	2.5	87.3	124.0	467.3	681.1
Profit for the year	–	–	–	93.6	93.6
Share-based payments	–	–	–	0.8	0.8
Coupon paid on capital securities	–	–	–	(9.8)	(9.8)
As at 31 December 2019	2.5	87.3	124.0	551.9	765.7

Year ended 31 December 2018	Share capital £m	Share premium account £m	Capital securities £m	Retained earnings £m	Total equity £m
As at 1 January 2018	2.5	87.3	124.0	409.3	623.1
Impact of adopting IFRS 9	–	–	–	(16.0)	(16.0)
Restated balance as at 1 January 2018	2.5	87.3	124.0	393.3	607.1
Profit for the year[1]	–	–	–	84.1	84.1
Share-based payments	–	–	–	(0.3)	(0.3)
Coupon paid on capital securities[1]	–	–	–	(9.8)	(9.8)
As at 31 December 2018	2.5	87.3	124.0	467.3	681.1

The notes on pages 157 to 213 are an integral part of these financial statements.

[1] Comparatives for the year ended 31 December 2018 have been restated to reflect amendments to IAS 12 'Income Taxes'. See Note 1.6(b) for details.

Company statement of changes in equity

For the year ended 31 December 2019

Year ended 31 December 2019	**Share capital £m**	**Share premium account £m**	**Capital securities £m**	**Retained earnings £m**	**Total equity £m**
As at 1 January 2019	**2.5**	**87.3**	**124.0**	**197.5**	**411.3**
Profit for the year	**–**	**–**	**–**	**9.5**	**9.5**
Share-based payments	**–**	**–**	**–**	**0.8**	**0.8**
Coupon paid on capital securities	**–**	**–**	**–**	**(9.8)**	**(9.8)**
As at 31 December 2019	**2.5**	**87.3**	**124.0**	**198.0**	**411.8**

Year ended 31 December 2018	Share capital £m	Share premium account £m	Capital securities £m	Retained earnings £m	Total equity £m
As at 1 January 2018	2.5	87.3	124.0	197.5	411.3
Profit for the year[1, 2]	–	–	–	10.1	10.1
Share-based payments	–	–	–	(0.3)	(0.3)
Coupon paid on capital securities[1]	–	–	–	(9.8)	(9.8)
As at 31 December 2018	2.5	87.3	124.0	197.5	411.3

The notes on pages 157 to 213 are an integral part of these financial statements.

1 Comparatives for the year ended 31 December 2018 have been restated to reflect amendments to IAS 12 'Income Taxes'. See Note 1.6(b) for details.

2 Treatment of the coupon received from the subsidiary on capital securities has been amended and it is now recognised through the statement of profit and loss rather than directly through equity. Comparatives for the year ended 31 December 2018 have been restated to reflect this amendment.

Consolidated and Company statement of cash flows

For the year ended 31 December 2019

	Note	**Group 2019 £m**	**Company 2019 £m**	Group 2018 £m	Company 2018 £m
Cash flows from operating activities[1, 2]					
Profit before tax		**122.4**	**9.5**	110.0	10.1
Adjustments for non-cash items and other adjustments included in the statement of profit and loss	34	**23.9**	**0.1**	34.0	0.1
(Increase)/decrease in operating assets	34	**(943.4)**	**0.4**	(1,050.2)	(0.3)
Increase/(decrease) in operating liabilities	34	**1,191.4**	**(0.2)**	589.2	(0.1)
Tax paid		**(28.7)**	**–**	(26.3)	–
Net cash generated from/(used by) operating activities		**365.6**	**9.8**	(343.3)	9.8
Cash flows from investing activities					
Purchase of investment securities		**(60.0)**	**–**	(139.7)	–
Purchase of property, plant and equipment		**(3.4)**	**–**	(3.6)	–
Purchase and development of intangible assets		**(8.0)**	**–**	(9.8)	–
Purchase of shares in associate		**–**	**–**	(6.0)	–
Purchase of subordinated debt		**–**	**(20.0)**	–	–
Disposal of subsidiary, net of cash disposed		**28.4**	**–**	–	–
Net cash used by investing activities		**(43.0)**	**(20.0)**	(159.1)	–
Cash flows from financing activities[1, 2]					
(Decrease)/increase in amounts due to banks		**(147.8)**	**–**	422.1	–
Issue of debt securities		**250.0**	**–**	–	–
Redemption of debt securities		**(8.2)**	**–**	–	–
Costs arising on issue of debt securities		**(1.7)**	**–**	–	–
Payment of lease liabilities		**(0.8)**	**–**	–	–
Issue of subordinated debt		**20.0**	**20.0**	–	–
Coupon paid to holders of capital securities		**(9.8)**	**(9.8)**	(9.8)	(9.8)
Net cash generated from/(used by) financing activities		**101.7**	**10.2**	412.3	(9.8)
Net increase/(decrease) in cash and cash equivalents		**424.3**	**–**	(90.1)	–
Cash and cash equivalents as at 1 January		**686.9**	**–**	777.0	–
Cash and cash equivalents as at 31 December	34	**1,111.2**	**–**	686.9	–

The notes on pages 157 to 213 are an integral part of these financial statements.

1 Presentation of interest on subordinated debt has been amended to include as a cash flow from operating activities rather than a cash flow from financing activities. This is to ensure there is consistent classification, whereby all interest that enters into the determination of profit or loss is classified within cash flows from operating activities. Comparatives for the year ended 31 December 2018 have been restated to reflect this presentation.

2 Treatment of the coupon received from the subsidiary on capital securities has been amended and it is now recognised through the statement of profit and loss rather than directly through equity. Comparatives for the year ended 31 December 2018 have been restated to reflect this amendment.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies

1.1. Reporting entity

Shawbrook Group plc (the Company) is a public limited company incorporated and domiciled in the UK. The registered office is Lutea House, Warley Hill Business Park, The Drive, Great Warley, Brentwood, Essex, CM13 3BE. The consolidated financial statements of Shawbrook Group plc, for the year ended 31 December 2019, comprise the results of the Company and its subsidiaries (together, the Group), including its principal subsidiary, Shawbrook Bank Limited. The ultimate parent company is detailed in Note 36.

The principal activities of the Group are lending and savings.

1.2. Basis of accounting and measurement

Both the consolidated and Company financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board and as adopted by the European Union, including interpretations issued by the IFRS Interpretations Committee and those parts of the Companies Act 2006 applicable to companies reporting under IFRS. No individual statement of profit and loss or related notes are presented for the Company as permitted by section 408 (4) of the Companies Act 2006.

As detailed in the Directors' Report, the Directors believe that it remains appropriate to prepare the financial statements on a going concern basis. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the balance sheet, future projections of profitability, cash flows and capital resources and the longer-term strategy of the business. The Group's capital and liquidity plans have been stress tested under a range of stressed scenarios and have been reviewed by the Directors.

The impact of Covid-19 has also been assessed and stress tested against the 2020 financial and business plans. Whilst the Covid-19 impacts are not yet fully known and will depend on many factors including the length of the enforced closure of certain businesses and social facilities, the social distancing measures and the success and continuity of the government and Bank of England measures put in place to support the economy and businesses, the Group has assessed its capital and liquidity over the going concern period. The Directors assessed the financial implications of the risks associated with Covid-19, including the expected effect of Management actions taken in response, against the most severe but plausible scenario used in the Board's assessment of the ICAAP approved in 2020. This scenario was the 'Rates Down' scenario specified by the Bank of England for use in preparing ICAAP stress tests. Having regard for the severe financial outcomes from this scenario and the reverse stress tests also conducted, the Board concluded that both capital and liquidity forecasts remained within present regulatory requirements, including use of capital buffers, over the going concern period.

After making enquiries, the Directors believe that the Group has sufficient resources to continue its activities for the 12 months from the reporting date and the Group has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the Prudential Regulation Authority.

The financial statements have been prepared on a historical cost basis, except as required in the valuation of certain financial instruments (i.e. derivative financial instruments) which are carried at fair value.

1.3. Functional and presentation currency

Both the consolidated and Company financial statements are presented in pounds sterling, which is the functional currency of the Company and all of its subsidiaries. All amounts have been rounded to the nearest million, except where otherwise indicated.

Foreign currency transactions are translated into functional currency using the spot exchange rate at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency using the spot exchange rate at the reporting date. Foreign exchange gains and losses resulting from the restatement and settlement of such transactions are recognised in the statement of profit or loss.

Non-monetary assets and liabilities that are measured on a historical cost basis and denominated in foreign currencies are translated into the functional currency using the spot exchange rate at the date of the transaction. Non-monetary assets and liabilities that are measured at fair value and denominated in foreign currencies are translated into the functional currency at the spot exchange rate at the date of valuation. Where these assets and liabilities are held at fair value through profit or loss, exchange differences are reported as part of the fair value gain or loss.

1. Basis of preparation and significant accounting policies continued

1.4. Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries. The Group's subsidiaries are detailed in Note 37.

Subsidiaries are entities controlled by the Group, including special purpose vehicles established in relation to the Group's securitisation (see Note 1.7(h)). Control is achieved when the Group has power over the entity, is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to use its power over the entity to affect its returns. The Group reassesses whether or not it controls the entity if facts and circumstances indicate that there are changes to one or more of the three elements of control.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that control ceases. Accounting policies are applied consistently across the Group. Intragroup transactions and balances are eliminated in full on consolidation.

The Group's interests in associates are detailed in Note 21. Associates are accounted for using the equity method of accounting as detailed in Note 1.7(n).

1.5. Presentation of risk and capital management disclosures

The disclosures required under IFRS 7 'Financial Instruments: Disclosures' concerning the nature and extent of risks relating to financial instruments and under IAS 1 'Presentation of Financial Statements' concerning objectives, policies and processes for managing capital have been included within the Risk Management Report. Where information in the Risk Management Report is marked as 'audited' it is covered by the Independent Auditor's Report.

1.6. Adoption of new and revised standards and interpretations

On 1 January 2019, the Group adopted the requirements of IFRS 16 'Leases' and the amendments to IAS 12 'Income Taxes'. The Group has also elected to early adopt 'Interest Rate Benchmark Reform': Amendments to IFRS 9 'Financial Instruments', IAS 39 'Financial Instruments: Recognition and Measurement' and IFRS 7 'Financial Instruments: Disclosures'. Details of these new and revised standards adopted are provided below.

A number of other new and revised standards issued by the International Accounting Standards Board, and endorsed for use in the European Union, also came into effect on 1 January 2019, but they do not have a material effect on the Group's financial statements and are not further disclosed. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

(a) IFRS 16 'Leases'

On 1 January 2019, the Group adopted the requirements of IFRS 16. The new standard replaces IAS 17 'Leases' and related interpretations. The standard applies to all leasing arrangements and sets out the principles for the recognition, measurement, presentation and disclosure of leases for both lessor and lessee accounting.

The Group has adopted IFRS 16 using the modified retrospective approach (with practical expedients). As such, the standard is applied as of 1 January 2019, with the cumulative effect recognised as an adjustment to the opening balance of retained earnings. Comparative information for 2018 is not restated and continues to be measured and presented under the requirements of IAS 17.

The key changes and impacts are outlined below:

(i) Definition of a lease

Under IFRS 16, a contract is, or contains a lease, if the contract conveys a right to control the use of an identified asset for a period of time in exchange for consideration.

Transition

On transition to IFRS 16, the Group elected to apply the practical expedient set out in IFRS 16, which means an entity is not required to reassess whether a contract is, or contains, a lease at the date of initial application. As such, the Group only applies the new requirements of IFRS 16 to contracts previously identified as leases under IAS 17 and to contracts entered into or changed on or after 1 January 2019 that meet the definition of a lease under IFRS 16. Contracts that were not previously identified as leases under IAS 17 were not reassessed.

(ii) Lessor accounting

Lessor accounting under IFRS 16 is largely unchanged from IAS 17. Lessors continue to classify leases as either operating or finance leases using similar principles as set out in IAS 17.

Transition

On adoption of IFRS 16, the accounting policies applied by the Group for leases in which it acts as a lessor, as detailed in Note 1.7(s), were unchanged and there were no other impacts.

(iii) Lessee accounting

Previously under IAS 17, the Group classified each of its leases at inception date as either a finance lease or an operating lease. A lease was classified as a finance lease if it transferred substantially all of the risks and rewards of ownership of the leased asset to the Group; otherwise it was classified as an operating lease.

Finance leases were capitalised at the commencement of the lease at the inception date fair value of the leased asset or, if lower, at the present value of the minimum lease payments. Capitalised assets were accounted for in accordance with the accounting policies detailed in Note 1.7(l). Lease payments were apportioned between finance charges and a reduction of the lease liability to achieve a constant rate of interest on the remaining balance of the liability.

In an operating lease, the leased asset was not capitalised and the lease payments were charged to administrative expenses in the statement of profit and loss on a straight-line basis over the lease term. Any prepaid or accrued lease payments were recognised in other assets or other liabilities, respectively, in the statement of financial position.

Upon adoption of IFRS 16, the Group introduced a single lessee accounting model for all leases, except for short-term leases and leases of low value items. All leases are now recognised on the statement of financial position, whereby a right-of-use asset is recognised to represent the right to use the underlying asset and a lease liability is recognised to represent the obligation to make lease payments.

New accounting policies

A summary of the significant new accounting policies applied by the Group upon adoption of IFRS 16 for leases in which it acts as a lessee is as follows:

Right-of-use assets

The Group recognises a right-of-use asset at the lease commencement date. The right-of-use asset is measured at cost, less any accumulated depreciation and impairment losses, and is adjusted for any remeasurement of the lease liability. The cost of the right-of-use asset includes the amount of the lease liability recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received.

Right-of-use assets are presented in the right-of-use leasehold property category within property, plant and equipment in the statement of financial position.

Right-of-use assets are depreciated on a straight-line basis over the shorter of the estimated useful life and the lease term. Right-of-use assets are subject to impairment and are adjusted for certain remeasurements of the lease liability. Depreciation and impairment losses are charged to administrative expenses in the statement of profit and loss.

Lease liabilities

At the lease commencement date, the Group recognises a lease liability measured at the present value of the lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating a lease, if the lease term reflects the Group exercising the option to terminate. The variable lease payments that do not depend on an index or a rate are recognised as an administrative expense in the statement of profit and loss in the period in which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Group uses the incremental borrowing rate at the lease commencement date, unless the interest rate implicit in the lease is readily determinable.

After the commencement date, lease liabilities are classified as financial liabilities measured at amortised cost. See Note 1.7(w) for details. Lease liabilities are remeasured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments, or a change in the assessment to purchase the underlying asset. When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset. If the carrying amount of the right-of-use asset has been reduced to zero, the adjustment is recognised in the statement of profit and loss.

Lease liabilities are presented as a line item on the face of the statement of financial position.

Short-term leases and leases of low value assets

The Group applies the recognition exemption to any short-term leases (i.e. those leases that have a lease term of twelve months or less from the commencement date and do not contain a purchase option). The Group also applies the recognition exemption to leases that are considered of low value. For these leases, no right-of-use asset is recognised and lease payments continue to be charged to administrative expenses in the statement of profit and loss on a straight-line basis over the lease term.

Lease term

The Group determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease if it is reasonably certain not to be exercised.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.6. Adoption of new and revised standards and interpretations continued

Transition

Leases previously classified as finance leases

At the date of transition, 1 January 2019, the Group had no lease contracts that had previously been classified as finance leases in which it acts as the lessee.

Leases previously classified as operating leases

At the date of transition, 1 January 2019, the Group had a number of lease contracts for properties that had previously been classified as operating leases in which it acts as the lessee. For such leases, upon transition the Group recognised right-of-use assets and lease liabilities, except for short-term leases (see practical expedients below). Lease liabilities were recognised at the present value of the remaining lease payments discounted using the incremental borrowing rate at the date of initial application. Right-of-use assets were recognised at an amount equal to the lease liability, adjusted for any related prepaid and accrued lease payments previously recognised.

The Group elected to apply the following practical expedients set out in IFRS 16, whereby it:

- used a single discount rate for portfolios of leases with reasonably similar characteristics;
- relied on its previous assessment of whether leases were onerous immediately before the date of initial application;
- applied the short-term lease exemption to leases with a remaining lease term of less than 12 months at the date of initial application;
- excluded initial direct costs from the measurement of the right-of-use asset at the date of initial application; and
- used hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

Impacts on transition

The effects of adopting IFRS 16 as at 1 January 2019 were as follows:

- Right-of-use assets of £10.3 million were recognised and are presented in a new right-of-use leasehold property category within property, plant and equipment in the statement of financial position.
- Lease liabilities of £10.9 million were recognised and are presented in a new line item in the statement of financial position.
- Accruals of £0.6 million included within other liabilities related to contracts previously classified as operating leases were derecognised.
- The net effect of these adjustments had no impact on opening retained earnings.

The lease liabilities recognised as at 1 January 2019 can be reconciled to the operating lease commitments as at 31 December 2018 as follows:

	£m
Operating lease commitments as at 31 December 2018	**13.7**
Weighted average incremental borrowing rate as at 1 January 2019	**2.09%**
Discounted operating lease commitments as at 1 January 2019	**12.9**
Less: Commitments relating to short-term leases	**(0.4)**
Less: VAT[1]	**(1.5)**
Less: Other adjustments	**(0.1)**
Lease liabilities as at 1 January 2019	**10.9**

Impacts for the period

There was no net impact arising from the adoption of IFRS 16 on the Group's profit for the year ended 31 December 2019. As a result of adopting IFRS 16, depreciation increased by £1.5 million and interest expense increased by £0.2 million. This was fully offset by a decrease in administrative expenses of £1.7 million.

Further disclosures relating to the Group's leases are set out in Note 29.

(b) Amendments to IAS 12 'Income taxes': 'Income Tax Consequences of Payments on Instruments Classified as Equity'

On 1 January 2019, the Group adopted the amendments to IAS 12, which were issued as part of the annual improvement cycle. The amendments clarify that an entity should recognise the tax consequences of dividends where the transactions or events that generated the distributable profits are recognised.

[1] Operating lease commitments reported under IAS 17 'Leases' in 2018 included VAT. The Group does not include VAT in the lease liability recognised under IFRS 16 'Leases'. This resulted in a £1.5 million difference.

The amendments impact the recognition of income tax relief on distributions on the Group's capital securities which are included in equity. Previously, the Group recognised the income tax relief directly in equity. Following adoption, the income tax relief is recognised in the statement of profit or loss, as this is where the transactions and events that generated the distributable profits are recognised.

Transition and impacts
The amendments are accounted for retrospectively. As such, comparatives for the year ended 31 December 2018 have been restated to reduce the tax charge and increase profit after tax by £2.5 million. The tax charge is reduced from £28.4 million to £25.9 million and profit after tax is increased from £81.6 million to £84.1 million.

In the year ended 31 December 2019, tax relief of £2.5 million is recognised in the statement of profit and loss. Prior to adopting the amendment to IAS 12, this tax relief would have been recognised directly in equity.

(c) 'Interest Rate Benchmark Reform': Amendments to IFRS 9 'Financial Instruments', IAS 39 'Financial Instruments: Recognition and Measurement' and IFRS 7 'Financial Instruments: Disclosures'

In September 2019, amendments to IFRS 9, IAS 39 and IFRS 7 were published. The amendments are effective for annual periods beginning on or after 1 January 2020, with early application permitted. The Group has elected to early adopt the amendments for the year ended 31 December 2019.

The amendments conclude phase one of the International Accounting Standards Board's work to address issues affecting financial reporting in the period leading up to interest rate benchmark reform. Specifically, the amendments provide temporary reliefs which enable hedge accounting to continue during the period of uncertainty before the replacement of an existing interest rate benchmark with an alternative nearly risk-free interest rate. The amendments are mandatory and apply to all hedging relationships directly affected by uncertainties related to interest rate benchmark reform.

Transition and impacts
The reliefs provided by the amendments that are relevant to the Group are set out below, together with the impact on the Group's accounting:

'Separately identifiable risk components' relief:
This relief means that as long as a non-contractually specified interest rate risk component meets the separately identifiable requirement at inception of the hedge accounting relationship, hedge accounting should be continued. This is applicable to the Group as follows:

- The Group has sterling denominated fixed rate advances in the form of commercial and residential mortgages, consumer lending products and fixed rate deposits from customers which it fair value hedges using sterling London Inter-Bank Offered Rate (LIBOR) to sterling fixed interest rate swaps in portfolio fair value hedge relationships. The amendments permit continuation of hedge accounting even if in the future the hedged benchmark interest rate, sterling LIBOR, may no longer be separately identifiable. However, this relief does not extend to the requirement that the designated interest rate risk component must continue to be reliably measurable. If the risk component is no longer reliably measurable, the hedging relationships will be discontinued.
- The Group has sterling denominated floating rate mortgage lending products that are referenced to three-month LIBOR, but with a minimum reference rate of 0.75%. These are hedged with sold interest rate options in a portfolio fair value hedge relationship. The amendments permit continuation of hedge accounting even if in the future the sterling LIBOR may no longer be separately identifiable.

'Prospective effectiveness' relief:
This relief means that when evaluating whether the hedging relationship is expected to be highly effective, the Group can assume that the benchmark interest rate is not altered as a result of interest rate benchmark reform and can perform the prospective hedge effectiveness assessment based on the existing interest rate benchmark on which the hedges are designated.

'Retrospective effectiveness' relief:
This relief means that when evaluating whether the actual result of a hedging relationship is outside the range of 80–125%, if the hedging relationship is subject to interest rate benchmark reforms, the Group will not discontinue hedge accounting solely because the actual effectiveness falls outside of the 80-125% range.

Further details regarding interest rate benchmark reform can be found in the market risk section of the Risk Management Report on page 132.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies

With the exception of changes to the Group's accounting policies resulting from new and revised accounting standards adopted in the year, as detailed in Note 1.6, the Group has consistently applied the following accounting policies to all periods presented in the financial statements.

(a) Operating segments

See disclosures at Note 2

Operating segments are identified on the basis of internal reports and components of the Group which are regularly reviewed by the Chief Operating Decision Maker to allocate resources to segments and to assess their performance. For this purpose, the Group Executive Committee has been determined to be the Chief Operating Decision Maker for the Group.

The Group determines operating segments according to similar economic characteristics and the nature of its products and services. No operating segments are aggregated to form the Group's reportable operating segments.

Substantially all of the Group's activities are in the United Kingdom. Consequently, segmental analysis on geographical lines is not required.

(b) Interest income and expense

See disclosures at Note 3 and Note 4

Financial instruments measured at amortised cost
Interest income and expense are recognised in the statement of profit and loss for all interest bearing financial instruments measured at amortised cost using the effective interest rate method.

The effective interest rate method calculates the amortised cost of a financial asset or financial liability and allocates the interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash flows through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset, or the amortised cost of a financial liability.

In relation to the above, amortised cost is the amount at which the financial instrument is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest rate method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any loss allowance.

With the exception of credit-impaired financial assets, when calculating the effective interest rate for financial instruments, the Group estimates future cash flows considering all contractual terms of the financial instrument but does not consider the loss allowance recognised on financial assets. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of the financial instrument.

In calculating interest income and expense, the calculated effective interest rate is applied to the gross carrying amount of the financial asset, or to the amortised cost of the financial liability, respectively.

For financial assets that become credit-impaired subsequent to initial recognition (i.e. a 'Stage 3' asset, as detailed on page 102 of the Risk Management Report), interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, the calculation of interest income reverts to the gross basis.

Derivative financial instruments
The Group recognises net interest income/expense on derivative financial instruments forming part of hedging relationships and economic hedging relationships based on the underlying hedged items. For derivative financial instruments hedging assets, the net interest income/expense is recognised in interest income. For derivative financial instruments hedging liabilities, the net interest income/expense is recognised in interest expense.

(c) Fee and commission income

See disclosures at Note 5

Fee and commission income includes amounts from contracts with customers that are not included in the effective interest rate calculation detailed in Note 1.7(b). These amounts are recognised when performance obligations attached to the fee or commission have been satisfied. The income streams included in fee and commission income all have a single performance obligation attached to them. Where income is earned from the provision of a service, such as an account maintenance fee, the performance obligation is deemed to have been satisfied when the service is delivered. Where income is earned upon the execution of a significant act, such as fees for executing a CHAPS payment, the performance obligation is deemed to have been satisfied when the act is completed.

(d) Administrative expenses

See disclosures at Note 6

Administrative expenses are recognised on an accruals basis. The Group's significant accounting policies relating to payroll costs are detailed below. Accounting policies for expenses relating to property, plant and equipment and intangible assets are set out in Note 1.7(l) and Note 1.7(m), respectively.

Payroll costs
Salaries and social security costs are recognised over the period in which the employees provide the service to which the payments relate.

Cash bonus awards are recognised to the extent that the Group has a present obligation to its employees that can be measured reliably and are recognised over the period that employees are required to provide services.

The Group operates a long-term incentive plan for a set of individuals. These benefits are recognised at the present value of the obligation at the reporting date, reflecting the Group's best estimate of the effect of the associated performance conditions. Costs are recognised over the period until which the Group considers all vesting conditions to have been reasonably achieved, which takes into account the period that employees are required to provide services.

The Group operates defined contribution pension schemes for eligible employees and does not operate any defined benefit pension schemes. Under the defined contribution pension arrangements, the Group pays fixed contributions into employees' personal pension plans, with no further payment obligations once the contributions have been paid. The Group's contributions to such arrangements are recognised as an expense when they fall due.

Employee share-based payments, which form part of payroll costs, are detailed in Note 1.7(e).

(e) Employee share-based payments

See disclosures at Note 9

The Group operates equity-settled share-based payment schemes in respect of services received from certain employees, as detailed below. The Group does not operate any cash-settled share-based payment schemes.

Equity-settled share-based payment schemes
The grant date fair value of a share-based payment transaction is recognised as a payroll cost in administrative expenses in the statement of profit and loss, with a corresponding increase in retained earnings in equity, on a straight-line basis over the period that the employees become unconditionally entitled to the awards (the vesting period). In the absence of market prices, the grant date fair value is estimated using an appropriate valuation technique.

The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that meet the related service and non-market performance conditions at the vesting date.

For share-based payment awards with market performance conditions or non-vesting conditions, the grant date fair value of the award is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

Tax on the amount recognised as an expense is recognised in the statement of profit and loss. Tax benefits that exceed the tax effected cumulative remuneration expenses are considered to relate to an equity item and are recognised directly in equity.

(f) Tax

See disclosures at Note 13 and Note 20

Tax comprises current tax and deferred tax. Tax is recognised in the statement of profit and loss except to the extent that it relates to items recognised directly in equity or other comprehensive income.

Current tax
Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. It is measured using tax rates enacted or substantively enacted at the reporting date.

Deferred tax
Deferred tax is provided in full using the liability method on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date.

A deferred tax asset is recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies continued

(g) Loans and advances

See disclosures at Note 14

Both loans and advances to banks and loans and advances to customers are classified as financial assets measured at amortised cost. See Note 1.7(w) for details.

Loans and advances to customers includes assets acquired in exchange for loans, instalment credit and finance lease receivables as part of an orderly realisation. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income.

Certain loans and advances to customers are used as collateral against bank borrowings and amounts drawn under the Bank of England's Term Funding Scheme. Certain loans and advances to banks are also used as collateral against derivative contracts. In both instances, the Group does not transfer substantially all the risks and rewards associated with these assets and as such, the derecognition criteria outlined in Note 1.7(w) are not met and the assets continue to be recognised in their entirety in the statement of financial position.

Certain loans and advances to customers are also pledged to securitisation programmes. See Note 1.7(h) for details.

(h) Securitisation transactions and debt securities in issue

See disclosures at Note 15 and Note 28

The Group has securitised certain loans included within loans and advances to customers, by transferring the beneficial interest in such loans to a bankruptcy remote special purpose vehicle (SPV). In accordance with the criteria set out in Note 1.4, the Group has assessed that it controls the SPV and as such, the SPV is treated as a subsidiary and is fully consolidated.

The terms of the securitisation are such that the Group retains substantially all the risks and rewards associated with the underlying transferred loans. As such, the criteria for derecognising financial assets, as detailed in Note 1.7(w), are not met. Accordingly, the transfer of loans to the SPV are not treated as sales by the Group and the Group continues to recognise the loans in their entirety in loans and advances to customers in the statement of financial position.

The securitisation involves the simultaneous issue of mortgage backed debt securities by the SPV to investors. Issued debt securities are classified on initial recognition as either financial liabilities or equity instruments, in accordance with the substance of the contractual arrangements. The contractual arrangements are such that the Group has an obligation to deliver the cash flows generated from the underlying securitised loans to the debt security holder. Accordingly, the debt securities are classified as financial liabilities measured at amortised cost. See Note 1.7(w) for details. Issued debt securities are presented as debt securities in issue in the statement of financial position.

Certain debt securities issued by the SPV are retained by the Group. These debt securities are eliminated in full on consolidation. Certain of these internally held debt securities are used as collateral in repurchase agreements or similar transactions. See Note 1.7(aa) for details.

(i) Investment securities

See disclosures at Note 16

Investment securities are classified as financial assets measured at amortised cost. See Note 1.7(w) for details.

Certain investment securities are used as collateral against bank borrowings or in repurchase agreements. The Group does not transfer substantially all the risks and rewards associated with these assets and as such, the derecognition criteria outlined in Note 1.7(w) are not met and the assets continue to be recognised in their entirety in the statement of financial position.

(j) Derivative financial instruments

See disclosures at Note 17

Derivatives are mandatorily classified as fair value through profit or loss. See Note 1.7(w) for details. Derivatives are classified as financial assets where their fair value is positive and financial liabilities where their fair value is negative. Where there is the legal right and intention to settle net, then the derivative is classified as a net asset or net liability, as appropriate.

To calculate fair values, the Group typically uses discounted cash flow models using yield curves that are based on observable market data. For collateralised positions, the Group uses discount curves based on overnight indexed swap rates. For non-collateralised positions, the Group uses discount curves based on term LIBOR for derivatives referencing LIBOR and Sterling Overnight Index Average rate (SONIA) for derivatives referencing SONIA.

For measuring derivatives that might change the classification from being an asset to a liability or vice versa, fair values do not take into consideration either the credit valuation adjustment or the debit valuation adjustment as the Group's portfolio is fully collateralised and it is deemed to be immaterial.

Where derivatives are not designated as part of an accounting hedge relationship, gains and losses arising from changes in fair value are recognised in net gains/(losses) on financial instruments at fair value through profit or loss in the statement of profit and loss. Where derivatives are designated within an accounting hedge relationship, the treatment of the changes in fair value are as described in Note 1.7(k).

The Group enters into master netting and margining agreements with all derivative counterparties. In general, under master netting agreements the amounts owed by each counterparty that are due on a single day in respect of all transactions outstanding under the agreement are aggregated into a single net amount payable by one party to the other. In certain circumstances, for example when a credit event such as a default occurs, all outstanding transactions under the agreement are aggregated into a single net amount payable by one party to the other and the agreements terminated.

Under margining agreements where the Group has a net asset position valued at current market values, in respect of its derivatives with a counterparty, then that counterparty will place collateral, usually cash, with the Group in order to cover the position. Similarly, the Group will place collateral, usually cash, with the counterparty where it has a net liability position.

Since October 2019, the Group has cleared its standardised over-the-counter derivatives.

(k) Hedge accounting

See disclosures at Note 17

The Group applies the exemption under IFRS 9 'Financial Instruments' to continue to apply the hedge accounting rules set out in IAS 39 'Financial Instruments: Recognition and Measurement'. However, the Group does provide the additional and more detailed hedge accounting disclosures introduced by IFRS 9's consequential amendments to IFRS 7 'Financial Instruments: Disclosures'.

In the year ended 31 December 2019, the Group has early adopted 'Interest Rate Benchmark Reform': Amendments to IFRS 9, IAS 39 and IFRS 7. This provides temporary reliefs designed to allow hedge accounting to continue during the period of uncertainty arising from interest rate benchmark reforms. Further details are provided in Note 1.6(c) and should be read in conjunction with the below accounting policy.

Hedge accounting is permitted when documentation, eligibility and testing criteria are met. As such, at the inception of the hedge relationship, the Group formally designates and documents the hedge relationship (the link between the hedging instrument and the hedged item) to which it wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The Group also documents the method that will be used to assess the effectiveness of the hedging relationship (currently the dollar-offset method).

The Group makes an assessment, both at inception and on a monthly basis, as to whether the derivatives used in hedging transactions are highly effective in offsetting the exposure to changes in the hedged item's fair value. The hedge is deemed to be highly effective where the actual results of the hedge are within a range of 80-125%.

The Group designates certain derivatives as fair value hedges, as detailed below. The Group does not designate any derivatives as cash flow hedges or net investment hedges.

Fair value hedges

The Group applies fair value hedge accounting for portfolio hedges of interest rate risk. The hedged items are portfolios that are identified as part of the risk management process. These comprise either fixed rate assets only, or fixed rate liabilities only, in respect of a benchmark interest rate. Historically the benchmark interest rate was mainly three-month sterling LIBOR. From March 2019, this changed to SONIA.

Each portfolio is grouped into repricing time periods based on expected repricing dates, by scheduling cash flows into the periods in which they are expected to occur. Interest rate swaps are used as the hedging instruments to manage this interest rate risk to swap the fixed rate interest flows to floating.

Changes in the fair value of derivatives designated as fair value hedges and changes in the fair value of the hedged asset or liability attributable to the hedged risk are recognised in net gains/(losses) on financial instruments at fair value through profit or loss in the statement of profit and loss. The hedging gain or loss on the hedged items are included in interest income in the statement of profit and loss.

If the hedge no longer meets the criteria for hedge accounting, hedge accounting is discontinued prospectively. The cumulative fair value adjustment to the carrying amount of the hedged item is amortised to the statement of profit and loss over the remaining period to maturity.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies continued

(l) Property, plant and equipment and depreciation

See disclosures at Note 18

Property, plant and equipment is divided into four asset categories: leasehold property; fixtures, fittings and equipment; assets on operating leases; and right-of-use leasehold property.

Leasehold property and fixtures, fittings and equipment
Assets are measured at cost less accumulated depreciation and any accumulated impairment losses.

Cost includes the original purchase price of the asset and any directly attributable costs of bringing the asset to the location and condition necessary for its intended use. Subsequent expenditure is only capitalised when it improves the expected future economic benefits of the asset. Ongoing repairs and maintenance are expensed to administrative expenses in the statement of profit and loss as incurred.

Depreciation is calculated to write off the cost of the asset less its estimated residual value on a straight line basis over its estimated useful life, as follows:

- Leasehold property: Life of the lease
- Fixtures and fittings: 10 years
- Office equipment: 3 – 5 years

Depreciation is recognised in administrative expenses in the statement of profit and loss. The depreciation method, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

Assets are reviewed for indicators of impairment at each reporting date. If indicators are present, an impairment review is performed. An impairment loss is recognised if the carrying amount exceeds its recoverable amount. Recoverable amount is the greater of the value in use and fair value less costs to sell. Where impairment is required, the amount is recognised in administrative expenses in the statement of profit and loss.

Gains and losses on disposals are determined by comparing the net disposal proceeds with the carrying amount of the asset and are included in administrative expenses in the statement of profit and loss.

Assets on operating leases
This asset category holds assets that are leased to customers under operating lease agreements whereby the Group acts as the lessor. The accounting policies relating to such assets are set out in Note 1.7(s).

Right-of-use leasehold property
This is a new asset category created upon adoption of IFRS 16 'Leases' on 1 January 2019. This asset category holds assets leased by the Group in which the Group acts as the lessee. The accounting policies relating to such assets are set out in Note 1.6(a.iii).

(m) Intangible assets and amortisation

See disclosures at Note 19

Computer software
Externally acquired computer software is measured at cost less accumulated amortisation and any accumulated impairment losses. Cost includes the original purchase price of the asset and any directly attributable costs of preparing the asset for its intended use.

Internally developed computer software is recognised as an asset only when the Group is able to demonstrate that the expenditure can be reliably measured, the product or process is technically and commercially feasible, future economic benefits are probable and the Group has the intention and ability to complete development and subsequently use or sell the asset. If these conditions are not met, expenditure is recognised in administrative expenses in the statement of profit and loss as incurred.

Internally developed computer software is measured at capitalised cost less accumulated amortisation and any accumulated impairment losses. Capitalised costs include all costs directly attributable in preparing the asset so that it is capable of operating in its intended manner.

Subsequent expenditure on computer software is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in administrative expenses in the statement of profit and loss as incurred.

Computer software is amortised on a straight line basis over its estimated useful life of between three and seven years. Amortisation is recognised in administrative expenses in the statement of profit and loss. The amortisation method, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

Computer software is reviewed for indicators of impairment at each reporting date. If indicators are present, an impairment review is performed. An impairment loss is recognised if the carrying amount exceeds its recoverable amount. Recoverable amount is the greater of the value in use and fair value less costs to sell. Where impairment is required, the amount is recognised in administrative expenses in the statement of profit and loss.

Gains and losses on disposals are determined by comparing the net disposal proceeds with the carrying amount of the asset and are included in administrative expenses in the statement of profit and loss.

Goodwill
Goodwill may arise on the acquisition of subsidiaries and represents the excess of the aggregate of the fair value of consideration transferred and the fair value of any non-controlling interest over the fair value of identifiable net assets at the date of acquisition. Goodwill is stated at cost less any accumulated impairment losses.

Goodwill is not amortised but is tested annually for impairment and additionally whenever there is an indication that impairment may exist. For the purpose of impairment testing, goodwill is allocated to cash generating units (CGUs). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. An impairment loss is recognised if the carrying amount of a CGU exceeds its recoverable amount. Recoverable amount is the greater of the CGUs value in use and fair value less costs to sell. Value in use is based on estimated future cash flows less a residual value, discounted at a risk-adjusted discount rate appropriate to the CGU. Where impairment is required, the amount is recognised in administrative expenses in the statement of profit and loss and cannot subsequently be reversed.

(n) Investment in associates

See disclosures at Note 21

An associate is an entity over which the Group has significant influence and that is neither a subsidiary undertaking nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in the consolidated financial statements using the equity method of accounting. Investments are initially measured at cost, which includes transaction costs, and are presented as investment in associates in the statement of financial position.

Subsequent to initial recognition, the Group includes its share of the post-acquisition profit or loss and other comprehensive income of the associate. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. Dividends receivable from associates are recognised as a reduction in the carrying amount of the investment.

Where the Group's share of losses in an associate equal or exceed its interest in the associate, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Investments in associates are reviewed for indicators of impairment at each reporting date. If indicators are present, an impairment review is performed. Where the carrying amount is not recoverable the investment is written down immediately to the estimated recoverable amount.

The Group continues to use the equity method of accounting until the date on which significant influence ceases.

(o) Assets and disposal groups held for sale

See disclosures at Note 23

The Group classifies non-current assets and disposal groups as held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through continuing use. The criteria for held for sale classification is regarded as met only when the sale is highly probable and the asset or disposal group is available for immediate sale in its present condition. Management must be committed to the plan to sell the asset or disposal group and the sale expected to be completed within one year from the date of the classification.

Non-current assets and disposal groups classified as held for sale are generally measured at the lower of their carrying amount and fair value less costs to sell with any adjustments recognised in the statement of profit and loss. An exception to this is financial assets within the scope of IFRS 9 'Financial Instruments', for example loans, which continue to be measured in accordance with this standard. Accordingly, financial instruments held for sale continue to be accounted for in accordance with the accounting policies set out in Note 1.7(w).

Depreciation and amortisation cease once classified as held for sale.

Assets and liabilities classified as held for sale are presented as separate line items in the statement of financial position and are not net off. Prior periods are not restated.

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies continued

(p) Amounts due to banks

See disclosures at Note 25

Amounts due to banks are classified as financial liabilities measured at amortised cost. See Note 1.7(w) for details.

Amounts due to banks may include liabilities recognised as part of repurchase agreements. See Note 1.7(aa) for details.

(q) Customer deposits

See disclosures at Note 26

Customer deposits are classified as financial liabilities measured at amortised cost. See Note 1.7(w) for details.

(r) Provisions for liabilities and charges

See disclosures at Note 27

Provisions are recognised when there is a present obligation arising as a result of a past event, it is probable (more likely than not) that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions for levies are recognised when the conditions that trigger the payment of the levy are met.

Provisions for liabilities and charges includes financial guarantee contracts and the loss allowance for loan commitments. See Note 1.7(z) for details.

(s) Leases

See disclosures at Note 29

As detailed in Note 1.6(a), on 1 January 2019, the Group adopted the requirements of IFRS 16 'Leases', which sets out the requirements for both lessor and lessee accounting and replaces the previous requirements set out in IAS 17 'Leases'.

Lessor accounting
Lessor accounting under IFRS 16 is largely unchanged from IAS 17. As such, the accounting policies applied in relation to lease agreements in which the Group acts as a lessor, as detailed below, are consistent in both reported years.

Group acting as a lessor – finance leases
Lease agreements in which the Group transfers substantially all the risks and rewards of ownership of the underlying asset to the lessee are classified as finance leases.

A finance lease receivable equal to the net investment in the lease (representing the future lease payments less profit and costs allocated to future periods) is recognised and is presented within loans and advances to customers in the statement of financial position.

Lease payments are apportioned between interest income in the statement of profit and loss and a reduction of the finance lease receivable to achieve a constant rate of interest on the remaining balance of the receivable.

Group acting as a lessor – operating leases
Lease agreements in which the Group does not transfer substantially all the risks and rewards of ownership of the underlying asset to the lessee are classified as operating leases.

The leased asset is included in property, plant and equipment in the statement of financial position in the assets on operating leases category. The asset is recognised at the lower of its fair value less costs to sell and the carrying amount of the lease (net of impairment allowance) at the date of exchange.

Depreciation is calculated to write off the cost of the asset less its estimated residual value on a straight line basis over the life of the lease. Depreciation is charged to depreciation of operating leases in the statement of profit and loss.

Assets are reviewed for indicators of impairment at each reporting date. If indicators are present, an impairment review is performed. An impairment loss is recognised if the carrying amount exceeds its recoverable amount. Recoverable amount is the greater of the value in use and fair value less costs to sell. Where impairment is required, the amount is recognised in other operating lease income/(expense) in the statement of profit and loss.

Operating lease rental income is recognised in the statement of profit and loss on a straight-line basis over the lease term. Where an operating lease is terminated before the lease period has expired, any payment required to be made by the lessee in compensation is charged to other operating lease income/(expense) in the statement of profit and loss in the period in which the termination is made.

Where an agreement is classified as an operating lease at inception, but is subsequently reclassified as a finance lease following a change to the agreement or an extension beyond the primary term, then the agreement is accounted for as a finance lease.

Lessee accounting
Lessee accounting has changed significantly as a result of IFRS 16 adoption. The accounting policies applied by the Group pre- and post-IFRS 16 adoption are set out in Note 1.6(a.iii).

(t) Subordinated debt

See disclosures at Note 31

The subordinated debt liability is classified as a financial liability measured at amortised cost. See Note 1.7(w) for details.

Interest costs recognised on the subordinated debt liability are capitalised in accordance with the agreed terms and are incorporated into the total debt payable.

The subordinated debt receivable in the Company is subordinated debt issued from the Group's principal subsidiary, Shawbrook Bank Limited, to the Company. It is classified as a financial asset measured at amortised cost. See Note 1.7(w) for details.

(u) Capital securities

See disclosures at Note 33

Capital instruments are classified on initial recognition as either financial liabilities or equity instruments in accordance with the substance of the contractual arrangements. The characteristics associated with redemption and interest payments of the capital securities mean the Group does not have a present obligation to deliver cash, another financial asset or a variable number of equity instruments. Accordingly, the capital securities are classified as equity instruments. The capital securities are measured at the fair value of the proceeds from the issuance less any costs that are incremental and directly attributable to the issuance (net of applicable tax).

Distributions to holders of the capital securities are recognised when they become irrevocable and are deducted from retained earnings in equity. As detailed in Note 1.6(b), in accordance with the amendments to IAS 12 'Income Taxes', income tax relief on distributions to holders of the capital securities are recognised in the statement of profit or loss.

(v) Cash flows

See disclosures at Note 34

For the purposes of the statement of cash flows, cash and cash equivalents comprise cash and balances at central banks (less mandatory deposits with central banks which are not available for use in day-to-day operations and are non-interest bearing), loans and advances to banks and short-term highly liquid debt securities with less than three months to maturity from the date of acquisition. Loans and advances to banks comprise cash balances and call deposits.

(w) Financial instruments

See disclosures at Note 35

Recognition
Financial instruments are recognised when the Group becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade date.

Classification and measurement

Financial assets
There are three principal classification categories for financial assets: amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL).

To classify financial assets the Group performs two assessments, to evaluate the business model in which financial assets are managed and their cash flow characteristics:

- **The 'business model assessment':** this assessment determines whether the Group's objective is to generate cash flows from collecting contractual cash flows (hold-to-collect), or by both collecting contractual cash flows and selling financial assets (hold-to-collect-and-sell). The assessment is performed at a portfolio level and is based on expected scenarios. If cash flows are realised in a manner that is different from the original expectation, the classification of the remaining assets in that portfolio is not changed but such information is used when assessing new financial assets going forward.
- **The 'SPPI test':** this assessment determines whether the contractual cash flows of the financial asset are solely payments of principal and interest on the principal amount outstanding (SPPI) (i.e. whether the contractual cash flows are consistent with a basic lending arrangement). For the purposes of the SPPI test, principal is defined as the fair value of the financial asset at initial recognition. Interest is defined as consideration for the time value of money and credit risk associated with the principal amount outstanding and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a reasonable profit margin. The SPPI test is performed at an instrument level based on the contractual terms of the instrument at initial recognition. Derivative financial instruments and equity instruments will always 'fail' the SPPI test.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies continued

Based on the two assessments, financial assets are classified as follows:

- **Amortised cost:** a financial asset is classified as amortised cost when it is held in a hold-to-collect business model and its contractual terms give rise on specified dates to cash flows that are SPPI.
- **FVOCI:** a financial asset is classified as FVOCI when it is held in a hold-to-collect-and-sell business model and its contractual terms give rise on specified dates to cash flows that are SPPI.
- **FVTPL:** financial assets that do not meet the criteria to be classified as amortised cost or FVOCI are classified as FVTPL.

On initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be classified as measured at amortised cost or FVOCI as FVTPL, if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

With the exception of derivatives which are mandatorily classified as FVTPL, the Group's financial assets are all classified as amortised cost. To determine the applicable business model, amongst other information assessed, the Group considers sales in prior periods, expected sales in future periods and the reasons for such sales. Whilst there may be occasional sales of certain financial assets (e.g. investment securities), such sales are not expected to be more than infrequent and the financial assets are assessed to be in a hold-to-collect business model. In performing the SPPI test, terms that could change the contractual cash flows so that they are not SPPI are considered, such as: contingent and leverage features, non-recourse arrangements and features that could modify the time value of money. No such features have been identified and contractual cash flows are assessed to be consistent with a basic lending arrangement.

The Group has not designated any financial assets as FVOCI or FVTPL.

Equity instruments are normally classified as FVTPL. However, on initial recognition of an equity instrument that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in the statement of other comprehensive income. This election is made on an investment-by-investment basis. The Group has no equity instruments for which such an election has been made.

Derivatives embedded in contracts where the host is a financial asset are never separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

Subsequent to initial recognition, financial assets are reclassified only under the rare circumstances that the Group changes its business model for managing financial assets. Where this is the case, the Group reclassifies all affected financial assets in accordance with the new business model. The reclassification is applied prospectively from the first day of the first reporting period following the change in business model.

Financial assets classified as amortised cost are initially measured at fair value plus incremental direct transaction costs. Subsequent measurement is at amortised cost using the effective interest rate method (see Note 1.7(b)). Amortised cost is reduced by impairment losses (see Note 1.7(x)). Interest income, foreign exchange gains and losses and impairment losses are recognised in the statement of profit and loss.

Financial assets classified as FVTPL are initially measured at fair value and are subsequently remeasured at fair value. Net gains and losses, including any interest or dividend income, are recognised in the statement of profit and loss.

Financial liabilities

Financial instruments are classified as a financial liability when the substance of the contractual arrangements result in the Group having a present obligation to deliver cash, another financial asset or a variable number of equity instruments.

Financial liabilities are classified at initial recognition as amortised cost or FVTPL. Financial liabilities are measured at FVTPL when they meet the definition of held for trading, or when they are designated as such to eliminate or significantly reduce an accounting mismatch that would otherwise arise. For classification purposes, derivatives are deemed to be held for trading and are therefore classified as FVTPL. Financial liabilities not classified as FVTPL are classified as amortised cost.

The Group's financial liabilities are all classified as amortised cost, with the exception of derivatives which are mandatorily classified at FVTPL.

Financial liabilities classified as amortised cost are initially measured at fair value minus incremental direct transaction costs. Subsequent measurement is at amortised cost using the effective interest rate method (see Note 1.7(b)). Interest expense is recognised in the statement of profit and loss.

Financial liabilities classified as FVTPL are initially measured at fair value and are subsequently remeasured at fair value. Net gains and losses, including any interest, are recognised in the statement of profit and loss.

Derecognition

Derecognition is the point at which the Group ceases to recognise a financial asset or financial liability on its statement of financial position.

Financial assets

The Group derecognises a financial asset (or a part of a financial asset) when:

- the contractual rights to the cash flows from the financial asset have expired;
- the Group transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred; or
- the Group transfers the financial asset in a transaction in which the Group neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the asset. If the Group retains control of the asset it continues to recognise the transferred asset only to the extent of its continuing involvement and derecognises the remainder.

On derecognition of a financial asset the difference between the carrying amount (or the carrying amount allocated to the portion being derecognised) and the sum of the consideration received (including any new asset obtained less any new liability assumed) is recognised in the statement of profit and loss.

Financial liabilities

The Group derecognises a financial liability (or a part of a financial liability) when its contractual obligations are extinguished (i.e. discharged, cancelled, or expired).

On derecognition of a financial liability, the difference between the carrying amount (or the carrying amount allocated to the portion being derecognised) and the sum of the consideration paid (including any new asset obtained less any new liability assumed) is recognised in the statement of profit and loss.

Modifications

Financial assets

The Group sometimes renegotiates or otherwise modifies the contractual cash flow of a financial asset. When this happens, the Group assesses whether or not the new terms are substantially different to the original terms. The Group does this by considering, among others, the following factors:

- if the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay;
- whether any substantial new terms are introduced that substantially affects the risk profile of the loan;
- significant extension of the loan term when the borrower is not in financial difficulty;
- significant change in the interest rate; and
- insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms and cash flows of the modified asset are deemed to be substantially different, the contractual rights to cash flows from the original financial asset are deemed to have expired. This meets the derecognition criteria outlined above and as such the original financial asset is derecognised and a 'new' financial asset is recognised at fair value. The difference between the carrying amount of the derecognised financial asset and the new financial asset with modified terms is recognised in the statement of profit and loss.

If the cash flows of the modified asset are not deemed to be substantially different, the financial asset is not derecognised and the Group recalculates the gross carrying amount of the financial asset based on the revised cash flows of the financial asset and recognises any associated gain or loss in the statement of profit and loss.

The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate.

Financial liabilities

The Group derecognises a financial liability when there is deemed to be a substantial modification of the terms. Where this is the case, the contractual obligations from the original financial liability are deemed to have been extinguished. This meets the derecognition criteria outlined above and as such the original financial liability is derecognised and a 'new' financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the derecognised financial liability and the new financial liability with modified terms is recognised in the statement of profit and loss.

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies continued

When a financial liability measured at amortised cost is modified without this resulting in derecognition, a gain or loss is recognised in the statement of profit and loss. The gain or loss is calculated as the difference between the original contractual cash flows and the modified cash flows discounted at the original effective interest rate. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and are amortised over the remaining term of the modified financial liability by recalculating the effective interest rate on the instrument.

Fair value of financial instruments
Fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

Where possible, fair value is determined with reference to quoted prices in an active market or dealer price quotations. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Where quoted prices are not available, the Group uses generally accepted valuation techniques to estimate fair value. The valuation techniques used include discounted cash flow models and Black-Scholes option pricing. Wherever possible these valuation techniques use independently sourced market parameters, such as interest rate yield curves, option volatilities and currency rates. This reduces the need for Management judgement and estimation, as well as the uncertainty related with the estimated fair value.

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

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

If an asset or a liability measured at fair value has a bid price and an ask price, the Group measures assets at bid price and liabilities at ask price.

The Group does not adjust fair value estimates derived from models for any factors such as credit risk, liquidity risk or model uncertainties.

The Group uses a fair value hierarchy that categorises financial instruments into three different levels, as detailed in Note 35. Levels are reviewed at each reporting date and this determines whether transfers between levels are required.

Further details of the fair value calculation of derivative financial instruments are set out in Note 1.7(j).

Offsetting financial instruments
Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

(x) Impairment of financial assets

See disclosures at Note 11

Measurement of expected credit losses
Impairment of financial assets is calculated using a forward looking expected credit loss (ECL) model. ECLs are an unbiased probability-weighted estimate of credit losses determined by evaluating a range of possible outcomes. They are measured in a manner that reflects the time value of money and uses reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

The Group calculates ECLs and records a loss allowance for all financial assets not held at FVTPL, together with financial guarantee contracts and loan commitments. Assets held at FVTPL and equity instruments are not subject to impairment.

Calculation of ECLs is dependent upon the 'stage' the asset is assigned to (Stage 1, 2 or 3) which is based on changes in credit risk occurring since initial recognition. Details of the 'staging' of assets, calculation of ECLs and key judgements and estimates associated with this, are provided in the creditworthiness risk section of the Risk Management Report on page 102.

A summary of ECL measurement is as follows:

- **Financial assets that are not credit-impaired at the reporting date:** as the present value of all cash shortfalls. Cash shortfalls are the difference between the contractual cash flows due to the Group and the cash flows that the Group expects to receive.
- **Financial assets that are credit-impaired at the reporting date:** as the difference between the gross carrying amount and the present value of estimated future cash flows.
- **Financial guarantee contracts:** as the expected payments to reimburse the holder less any amounts that the Group expects to recover.
- **Loan commitments:** as the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows the Group expects to receive.

In relation to the above, credit-impaired is a financial asset in Stage 3 as defined in the Risk Management Report on page 102.

The Group can elect as an accounting policy choice, to use the 'simplified approach' for trade receivables, contract assets and lease receivables. The Group has chosen not to use the simplified approach.

Modifications
If a financial asset is modified, an assessment is made to determine whether the asset should be derecognised, as detailed in Note 1.7(w). Subsequently ECLs are measured as follows:

- if the modification does not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset; or
- if the modification does result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset. The date of renegotiation is considered to be the date of initial recognition for impairment calculation purposes, including in determining whether a significant increase in credit risk has occurred and whether the new financial asset is deemed to be a purchased or originated credit-impaired asset.

Write-offs
Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. Write-offs constitute a derecognition event, as detailed in Note 1.7(w).

Financial assets that are written off can still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

Amounts subsequently recovered on assets previously written off are recognised in impairment losses on financial assets in the statement of profit and loss.

Presentation of loss allowances in the statement of financial position
Loss allowances are presented in the statement of financial position as follows:

- **financial assets measured at amortised cost:** as a deduction from the gross carrying amount of the financial asset;
- **financial guarantee contracts and loan commitments:** generally, as a provision; and
- where a financial instrument includes both a drawn and an undrawn component, and the Group cannot identify the loss allowance on the undrawn loan commitment component separately from those on the drawn component, the Group presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision.

(y) Contingent liabilities

See disclosures at Note 40

Contingent liabilities are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of the Group. Alternatively, they are present obligations that have arisen from past events where the outflow of resources is uncertain or cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed, unless the probability of settlement is remote.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.7. Significant accounting policies continued

(z) Financial guarantee contracts and loan commitments

See disclosures at Note 41

Financial guarantee contracts
Financial guarantee contracts are contracts that require the Group to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. They are included in provisions for liabilities and charges in the statement of financial position.

Initially financial guarantees are measured at their fair value, being the premium received. Subsequently, financial guarantees are measured at the higher of the amount initially recognised less the cumulative amount of income recognised in the statement of profit and loss, and the amount of loss allowance determined in accordance with the policies set out in Note 1.7(x). Loss allowances are included within provisions for liabilities and charges in the statement of financial position.

Loan commitments
Loan commitments are firm commitments to provide credit under pre-specified terms and conditions. The Group includes certain uncommitted facilities within its reported loan commitments where the terms are such that the Group has an obligation to the customer should the customer get into financial distress. The Group has not provided any commitment to provide loans at below-market interest rate, or that can be settled net in cash or by delivering or issuing another financial instrument.

The Group recognises loss allowances in accordance with the policies set out in Note 1.7(x). Loss allowances are included within provisions for liabilities and charges in the statement of financial position.

(aa) Repurchase agreements, reverse repurchase agreements and security swaps

For liquidity purposes, securities may be sold subject to a commitment to repurchase them at a predetermined price (a repurchase agreement). In accordance with Note 1.7(w), the assets are not derecognised as the risks and rewards of ownership remain with the Group. A liability is recognised in respect of the consideration received in amounts due to banks in the statement of financial position, reflecting the Group's obligation to repurchase the assets for a fixed price at a future date. The difference between the sale and repurchase price is treated as interest and recognised in net interest income over the life of the agreement.

On occasion, certain securities may be swapped via linked repurchase and reverse repurchase agreements with the same counterparty. In such circumstances, no cash consideration is exchanged. The transferred assets are not derecognised and there is no associated liability as the non-cash collateral received is not recognised on the statement of financial position (i.e. the transaction is off-balance sheet).

1.8. New and revised standards and interpretations not yet adopted

A number of new and revised standards issued by the International Accounting Standards Board have not yet come into effect. None of these are expected to have a material impact on the Group's financial statements.

1.9. Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires Management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported results and financial position. Due to the inherent uncertainty in making estimates, actual results reported in the future may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The areas involving the most complex and subjective judgements and areas where assumptions and estimates are considered to have the most significant effect on the financial statements are set out below:

(a) Effective interest rate

See accounting policies at Note 1.7(b) and disclosures at Note 3

The main source of revenue for the Group is interest income on loans and advances to customers which is recorded using the effective interest rate method. Management must estimate the expected life of each loan and the profile of loan payments over this period. This calculation involves a number of judgements and represents a source of estimation uncertainty.

Key assumptions
The key assumption applied by Management in the effective interest rate calculation is the behavioural life of the loans. Management reviews the expected lives on a segmental basis, whereby products of a similar nature are grouped into cohorts that exhibit homogenous behavioural attributes. The expected life behaviours are subject to changes in internal and external factors that may result in adjustments to the carrying amount of the loans which must be recognised in the statement of profit and loss.

The effective interest rate behavioural models are based on market trends and experience. The actual behaviour of the loan portfolios is compared to the modelled behaviour on a quarterly basis. Modelled behaviours are adjusted if the modelled behaviour materially deviates from actual behaviour, with adjustments recognised in net interest income in the statement of profit and loss.

Sensitivity analysis
Sensitivity analysis was performed to assess the impact of a 10% acceleration in the redemption curves used, which could potentially shorten the expected life.

A 10% acceleration in the redemption curves would result in a net expense to the statement of profit and loss of £0.6 million. This is attributable to the Property Finance and Consumer Lending divisions.

Property Finance would see an increase in profit of £0.2 million, which is largely due to income received from early settlement fees, offset against broker fee amortisation.

Consumer Lending would see a decrease in profit of £0.8 million, mainly attributable to the acceleration of the amortisation of broker commissions.

(b) Impairment testing of goodwill

See accounting policies at Note 1.7(m) and disclosures at Note 19

Goodwill is impaired if the carrying amount of a CGU exceeds its recoverable amount. Determining the recoverable amount of the CGU involves the calculation of its value in use, which is derived by discounting the forecast cash flows (post-tax profits) to be generated from its continuing use. This calculation is subject to judgement and estimation uncertainty, specifically:

- **Forecast cash flows:** this is based on future cash flows included in the Board approved budget and assumptions regarding the long-term pattern of sustainable cash flows thereafter. This reflects Management's view of future business prospects and is subject to significant estimation uncertainty.
- **Discount rates:** the rates used to discount forecast cash flows can have a significant effect on their valuations. Deriving the CGU specific discount rate incorporates a number of inputs, all of which are subject to estimation uncertainty.

Key assumptions
The key assumptions used in the calculation of value in use are as follows:

Cash flow period: five years of cash flows (post-tax profits) (2018: five years) are included in the discounted cash flow model based on the Board approved budget.

Terminal value growth rate: a terminal value growth rate is applied into perpetuity to extrapolate cash flows beyond the cash flow period. The terminal value growth rate of 2.0% (2018: 2.0%) is estimated by Management taking into account rates disclosed by comparable institutions.

Discount rate: the post-tax discount rate is an estimate of the return that investors would require if they were to choose an investment that would generate cash flows of amount, timing and risk profile equivalent to those that the entity expects to derive from the asset. Management calculates discount rates using the price-to-book ratio method which incorporates target return on equity, growth rate and price-to-book ratio. The discount rate for each CGU is adjusted to reflect the risks inherent to the individual CGU.

Discount rates used are as follows:

	2019		2018	
	Post-tax	**Pre-tax[1]**	Post-tax	Pre-tax[1]
Property Finance	**15.5%**	**18.1%**	12.7%	15.1%
Business Finance	**16.0%**	**18.9%**	13.2%	15.9%

[1] Management applies post-tax discount rates to post-tax cash flows when testing the CGU for impairment. The pre-tax discount rate is disclosed in accordance with IAS 36 'Impairment of Assets'.

Notes to the financial statements

For the year ended 31 December 2019

1. Basis of preparation and significant accounting policies continued

1.9. Critical accounting estimates and judgements continued

Sensitivity analysis
Sensitivity analysis was performed to assess the impact of reasonable changes in cash flows, the terminal value growth rate and the discount rate on the outcome of impairment testing.

Cash flows: a decrease in cash flows of 10.0% would not result in any impairment to goodwill.

Terminal value growth rate: a decrease in the terminal value growth rate to 0% would not result in any impairment to goodwill.

Discount rate: an increase of 2.0% to the individual CGU's discount rate would not result in any impairment to goodwill.

(c) Customer remediation and conduct issues

See accounting policies at Note 1.7(r) and disclosures at Note 27

Provisions have been recognised in respect of potential instances of misrepresentation or breaches of contract by suppliers where the suppliers have become insolvent and therefore the Group has limited recourse to those suppliers. Such provisions represent Management's best estimate of the Group's likely costs. In determining the amount of the provisions, it will often be necessary to form a view on matters which are inherently uncertain, such as the number of future complaints, the extent to which they will be upheld and the average cost of redress. This therefore represents a key source of estimation uncertainty.

Key assumptions
The key factors considered in deriving the provision are the estimated number of upheld complaints and the estimated redress costs.

Key considerations in deriving the estimated number of upheld complaints include:

- complaint volumes, taking into account both the status of current claims and Management's estimate of potential future claims based on existing complaint data;
- the origin of the claim. For example, if the claim relates to a solvent or insolvent supplier, or if the route of the claim is via a claims management company;
- the statutory limitation period; and
- Management's estimate of claim uphold rates based on existing complaint data.

Estimated redress costs are the expected average customer compensation, should claims be upheld, based on agreed redress strategies, inclusive of loan balance adjustments and cash payments.

Sensitivity analysis
Sensitivity analysis was performed to assess the impact of reasonable changes to certain key assumptions used in the provision calculation as follows:

Customer initiated complaint volume: the impact of a +/-5 percentage point change in the number of complaints would result in a £3.0 million increase or a £2.7 million decrease in the provision, respectively.

Average uphold rate per complaint: the impact of a +/-5 percentage point change in the average uphold rate per complaint would result in a £0.3 million increase or decrease in the provision, respectively.

Average redress per valid complaint: the impact of a £500 increase or decrease in the average redress per complaint would result in a £1.7 million increase or decrease in the provision, respectively.

(d) Impairment losses on financial assets

See accounting policies at Note 1.7(x) and disclosures at Note 11

The calculation and measurement of expected credit losses requires significant judgement and represents a key source of estimation uncertainty. Details of the critical judgements and accounting estimates are set out in the creditworthiness risk section of the Risk Management Report on pages 110 and 113, respectively.

2. Operating segments

See accounting policies in Note 1.7(a)

The Group has four reportable operating segments. These are the Group's three lending divisions (Property Finance, Business Finance and Consumer Lending) and a central segment ('Savings and Central') which represents the Savings business, central functions and shared central costs.

Further details of the four segments are provided in the Strategic Report on page 3 and in the business review starting on page 19.

The following tables provide information regarding the results and the assets and liabilities of each reportable segment, and their reconciliation to the Group total. All revenue for each operating segment is earned from external customers. Current taxes, deferred taxes and certain assets and liabilities are not allocated to segments as they are managed on a Group basis.

Year ended 31 December 2019	Property Finance £m	Business Finance £m	Consumer Lending £m	Savings and Central £m	Total £m
Interest income calculated using the effective interest rate method	217.3	109.9	69.9	8.9	406.0
Other interest and similar income	–	–	–	(0.3)	(0.3)
Interest expense and similar charges	(68.2)	(20.7)	(10.8)	(13.5)	(113.2)
Net interest income/(expense)	149.1	89.2	59.1	(4.9)	292.5
Operating lease rental income	–	10.3	–	–	10.3
Depreciation of operating leases	–	(8.6)	–	–	(8.6)
Other operating lease income	–	0.2	–	–	0.2
Net income from operating leases	–	1.9	–	–	1.9
Fee and commission income	0.4	8.9	0.4	–	9.7
Fee and commission expense	(3.6)	(0.2)	(4.2)	(0.7)	(8.7)
Net fee and commission income/(expense)	(3.2)	8.7	(3.8)	(0.7)	1.0
Net gains on financial instruments mandatorily at fair value through profit or loss	–	–	–	2.3	2.3
Other operating expense	–	–	–	(2.6)	(2.6)
Net operating income/(expense)	145.9	99.8	55.3	(5.9)	295.1
Administrative expenses	(20.7)	(24.0)	(17.4)	(76.4)	(138.5)
Impairment losses on financial assets	(1.2)	(8.4)	(20.3)	–	(29.9)
Provisions for liabilities and charges	0.2	–	(5.0)	0.3	(4.5)
Total operating expenses	(21.7)	(32.4)	(42.7)	(76.1)	(172.9)
Share of results of associate	(0.1)	–	–	–	(0.1)
Gain on disposal of subsidiary	–	0.3	–	–	0.3
Profit/(loss) before tax	124.1	67.7	12.6	(82.0)	122.4
Assets	4,433.7	1,664.8	683.2	1,441.3	8,223.0
Liabilities	–	–	–	(7,457.3)	(7,457.3)
Net assets/(liabilities)	4,433.7	1,664.8	683.2	(6,016.0)	765.7

Notes to the financial statements

For the year ended 31 December 2019

2. **Operating segments** continued

Year ended 31 December 2018	Property Finance £m	Business Finance £m	Consumer Lending £m	Savings and Central £m	Total £m
Interest income calculated using the effective interest rate method	194.9	87.1	69.1	4.9	356.0
Other interest and similar income	–	–	–	0.8	0.8
Interest expense and similar charges	(50.5)	(15.8)	(10.0)	(11.0)	(87.3)
Net interest income/(expense)	144.4	71.3	59.1	(5.3)	269.5
Operating lease rental income	–	10.0	–	–	10.0
Depreciation of operating leases	–	(7.6)	–	–	(7.6)
Other operating lease income/(expense)	–	(0.6)	–	–	(0.6)
Net income from operating leases	–	1.8	–	–	1.8
Fee and commission income	0.3	9.6	0.8	–	10.7
Fee and commission expense	(3.0)	(0.4)	(4.6)	(0.4)	(8.4)
Net fee and commission income/(expense)	(2.7)	9.2	(3.8)	(0.4)	2.3
Net losses on financial instruments mandatorily at fair value through profit or loss[1]	–	–	–	(0.4)	(0.4)
Other operating income[1]	–	–	–	0.9	0.9
Net operating income/(expense)	141.7	82.3	55.3	(5.2)	274.1
Administrative expenses[1]	(16.6)	(23.1)	(20.6)	(70.0)	(130.3)
Impairment losses on financial assets[2]					
Impairment losses on financial assets (excluding insurance recovery)	*(5.6)*	*(2.1)*	*(28.5)*	–	*(36.2)*
Insurance recovery	–	*13.0*	–	–	*13.0*
	(5.6)	10.9	(28.5)	–	(23.2)
Provisions for liabilities and charges	(0.2)	(0.5)	(9.3)	(0.1)	(10.1)
Total operating expenses	(22.4)	(12.7)	(58.4)	(70.1)	(163.6)
Share of results of associates	(0.5)	–	–	–	(0.5)
Profit/(loss) before tax	118.8	69.6	(3.1)	(75.3)	110.0
Assets	3,705.6	1,433.4	741.0	944.9	6,824.9
Liabilities	–	–	–	(6,143.8)	(6,143.8)
Net assets/(liabilities)	3,705.6	1,433.4	741.0	(5,198.9)	681.1

1 Comparatives for the year ended 31 December 2018 have been restated to reclass £0.9 million of foreign exchange losses on derivative financial instruments from administrative expenses to net gains/(losses) on financial instruments mandatorily at fair value through profit or loss, to ensure compliance with the accounting policy set out in Note 1.3. Other foreign exchange gains of £0.9 million have been reclassified from administrative expenses to other operating expense/(income). The net impact to administrative expenses is £nil. Net operating income and total operating expenses are unchanged as a result of this reclass.

2 During the year ended 31 December 2018, the Group received £13.0 million from the Group's insurance claim in respect of a controls breach identified in the Business Finance division in 2016. To allow for meaningful comparison between the reported years, subtotals have been provided to present the insurance recovery separately.

3. Interest and similar income

See accounting policies in Note 1.7(b)

	2019 £m	2018 £m
Interest income calculated using the effective interest rate method		
On cash and balances at central banks	**6.8**	4.7
On loans and advances to customers	**396.9**	351.1
On investment securities	**2.3**	0.2
Total interest income calculated using the effective interest rate method	**406.0**	356.0
Other interest and similar income		
On derivative financial instruments	**(0.3)**	0.8
Total other interest and similar income	**(0.3)**	0.8
Total interest and similar income	**405.7**	356.8

Interest income recognised during the year ended 31 December 2019 on credit-impaired (Stage 3) loans is £8.2 million (2018: £7.6 million).

The Group did not capitalise any interest income during the year ended 31 December 2019 (2018: £nil).

Total interest and similar income includes £406.0 million (2018: £356.0 million) of interest income on financial assets measured at amortised cost.

4. Interest expense and similar charges

See accounting policies in Note 1.7(b)

	2019 £m	2018 £m
On amounts due to banks	**9.4**	6.2
On customer deposits	**94.4**	74.3
On derivative financial instruments	**(0.7)**	(0.2)
On debt securities in issue	**3.1**	–
On lease liabilities	**0.2**	–
On subordinated debt liability	**6.8**	6.5
Other interest expense	**–**	0.5
Total interest expense and similar charges	**113.2**	87.3

The amounts reported above include £113.9 million (2018: £87.5 million) of interest expense on financial liabilities measured at amortised cost.

Notes to the financial statements

For the year ended 31 December 2019

5. Fee and commission income

See accounting policies in Note 1.7(c)

	2019 £m	2018 £m
Fee income on loans and advances to customers	**6.4**	8.3
Credit facility related fees	**3.3**	2.4
Total fee and commission income	**9.7**	10.7

6. Administrative expenses

See accounting policies in Note 1.7(d)

	2019 £m	2018 £m
Payroll costs (see Note 8)	**71.7**	65.0
Depreciation[1]	**3.4**	2.0
Loss on disposal of property, plant and equipment	**–**	0.1
Amortisation of intangible assets	**7.8**	6.1
Impairment of goodwill	**–**	1.1
Loss on disposal of intangible assets	**–**	1.9
Other administrative expenses	**55.6**	54.1
Total administrative expenses	**138.5**	130.3

Other administrative expenses include fees paid to the Group's auditor (see Note 7).

7. Auditor's remuneration

Fees payable to the Group's auditor, KPMG LLP, are as follows:

	2019 £000	2018 £000
Audit of these annual accounts	**130**	100
Audit of the annual accounts of the subsidiaries of the Company	**650**	530
Adjustments in respect of prior year and IFRS 9	**45**	45
Other tax advisory services	**23**	19
Audit related assurance services	**185**	87
All other assurance services	**341**	59
All other services	**7**	90
Total auditor's remuneration	**1,381**	930

[1] Depreciation included within administrative expenses includes depreciation of all asset categories except for assets on operating leases. Depreciation of assets on operating leases is presented as a separate line item in the statement of profit and loss. The year ended 31 December 2019 includes depreciation of right-of-use assets recognised in accordance with IFRS 16 'Leases'. As such, results are not directly comparable. See Note 1.6(a) for details.

8. Employees

See accounting policies in Note 1.7(d)

The average number of persons employed by the Group on a full-time equivalent basis (including Executive Directors) is as follows:

	2019	2018
Property Finance	**118**	99
Business Finance	**201**	170
Consumer Lending	**56**	51
Central	**439**	411
Average employees (on a full-time equivalent basis)	**814**	731

The aggregate payroll costs of these persons are shown in the table below. These payroll costs are a component of administrative expenses (see Note 6).

	2019 £m	2018 £m
Wages and salaries	**62.5**	56.7
Social security costs	**5.7**	5.2
Pension costs	**3.5**	3.1
Total payroll costs	**71.7**	65.0

Wages and salaries include share-based payment charges (see Note 9).

Pension costs represent contributions to defined contribution pension schemes. The Group does not operate any defined benefit pension schemes.

Further details of Directors' remuneration is provided in Note 10.

9. Employee share-based payment transactions

See accounting policies in Note 1.7(e)

Employee share-based payment charges are a component of payroll costs (Note 8) and are as follows:

	2019 £m	2018 £m
Management Incentive Plan	**0.8**	–
Total share-based payments	**0.8**	–

There were no share-based awards at any point during 2018. Movements in the number of share-based awards during the year ended 31 December 2019 are as follows:

		2019
	Management Incentive Plan (Number of shares)	**Total (Number of shares)**
As at 1 January	**–**	**–**
Granted	**5,275**	**5,275**
As at 31 December	**5,275**	**5,275**

Notes to the financial statements

For the year ended 31 December 2019

9. Employee share-based payment transactions continued

Details of the share-based scheme in operation are as follows:

Management Incentive Plan

In April 2019, the Management Incentive Plan was introduced for a set of individuals. The scheme is an equity-settled share-based payment scheme.

Individuals included in the Management Incentive Plan were entitled to acquire non-voting 'B' Class ordinary shares in Marlin Bidco Limited, the ultimate parent company, subject to performance conditions. All shares were issued at a price of £135.00 per share.

The performance conditions for the Management Incentive Plan relate to the equity valuation of the Company in the event of a prescribed exit event. The outcome of the performance conditions determines the vesting outcome of the awards.

The fair value of the shares issued was £580.00. The fair value of the shares was calculated using a Monte Carlo valuation model. A summary of the key data and assumptions used in measuring the fair value at grant date is as follows:

Assumptions	
Expected volatility	**28%**
Dividend yield	**0%**
Risk-free rate of return (based on government bonds)	**0.90%**
Expected life at grant date	**3.7 years**

Expected volatility is calculated based on the historical volatility of banks closely aligned to the Group.

10. Directors' remuneration

	2019 £000	2018 £000
Directors' emoluments[1]	**1,843.7**	3,499.6
Total Directors' remuneration	**1,843.7**	3,499.6

In the year ended 31 December 2019, there are no termination payments included in Directors' emoluments (2018: £1.2 million relating to termination payments.)

Further information about the remuneration of Directors is provided in the Directors' Remuneration Report on page 66.

[1] Ian Cowie assumed the role as Interim Chief Executive Officer in July 2018. He was not however formally appointed to the Board of the Company until February 2019. As such, his remuneration is not included in the figures for the year ended 31 December 2018 and is prorated for the year ended 31 December 2019 as set out in the Directors' Remuneration Report.

11. Impairment losses on financial assets

See accounting policies in Note 1.7(x)

Impairment losses on financial assets relate to the Group's loans and advances to customers, as set out in the table below. Impairment losses on the Group's cash and balances at central banks, loans and advances to banks and investment securities are immaterial in both reported years, totalling less than £0.1 million.

During the year ended 31 December 2018, the Group received £13.0 million from the Group's insurance claim in respect of a controls breach identified in the Business Finance division in 2016. To allow for meaningful comparison between the reported years, the insurance recovery has been separately presented in both the statement of profit and loss and the table below.

	2019 £m	2018 £m
Impairment losses on financial assets (excluding insurance recovery)		
ECL charge for the year	**2.6**	15.1
Loan balances written-off in the year	**34.0**	25.6
Amounts recovered in the year in respect of loan balances previously written-off (excluding insurance recovery)	**(6.7)**	(4.5)
Total impairment losses on financial assets (excluding insurance recovery)	**29.9**	36.2
Insurance recovery	**–**	(13.0)
Total impairment losses on financial assets	**29.9**	23.2

Further analysis of the ECL charge for the year is set out in the creditworthiness risk section of the Risk Management Report on page 102.

12. Gain on disposal of subsidiary

In October 2019, the sale of Shawbrook International Limited, a wholly owned subsidiary of the Group, was completed. The subsidiary was not a separate major business line and therefore is not disclosed as a discontinued operation. A gain on disposal of £0.3 million is recognised in the statement of profit and loss.

Notes to the financial statements

For the year ended 31 December 2019

13. Tax

See accounting policies in Note 1.7(f)

The tax charge recognised in the statement of profit and loss is as follows:

	2019 £m	2018[1] £m
Current tax		
Current year	**28.1**	23.1
Adjustment in respect of prior years	**(2.4)**	(0.5)
Total current tax	**25.7**	22.6
Deferred tax		
Origination and reversal of temporary differences	**0.8**	3.5
Adjustment in respect of prior years	**2.3**	(0.2)
Total deferred tax	**3.1**	3.3
Total tax charge	**28.8**	25.9

A reconciliation of profit before tax to the total tax charge is as follows:

	2019 £m	2018[1] £m
Profit before tax	**122.4**	110.0
Implied tax charge thereon at 19.00% (2018: 19.00%)	**23.3**	20.9
Adjustments		
Banking surcharge	**7.7**	6.7
Tax relief on coupon paid on capital securities	**(2.5)**	(2.5)
Adjustment in respect of prior years	**(0.1)**	(0.7)
Disallowable expenses and other permanent differences	**0.4**	0.7
Effect of tax rate changes	**–**	0.8
Total tax charge	**28.8**	25.9

Reduction in the UK corporation tax rate from 19% to 17% (effective 1 April 2020) was substantively enacted on 16 March 2016. As detailed in Note 43, in March 2020, it was announced in Budget 2020 that the main rate of corporation tax will remain at 19%, rather than reducing it to 17% from 1 April 2020.

The deferred tax asset in both reported years has been calculated based on an aggregation rate of 25%. This is based on a rate of 17% substantively enacted at the reporting date and the additional 8% of tax suffered in relation to the banking surcharge that will unwind over the remaining life of the underlying assets with which they are associated.

[1] Comparatives for the year ended 31 December 2018 have been restated to reflect amendments to IAS 12 'Income Taxes'. See Note 1.6(b) for details.

14. Loans and advances to customers

See accounting policies in Note 1.7(g)

	2019			2018		
	Gross carrying amount £m	**Loss allowance £m**	**Carrying amount £m**	Gross carrying amount £m	Loss allowance £m	Carrying amount £m
Loan receivables	**6,226.6**	**(47.4)**	**6,179.2**	5,410.4	(54.1)	5,356.3
Finance lease receivables	**81.0**	**(6.4)**	**74.6**	95.0	(7.2)	87.8
Instalment credit receivables	**382.4**	**(7.3)**	**375.1**	409.4	(6.5)	402.9
	6,690.0	**(61.1)**	**6,628.9**	5,914.8	(67.8)	5,847.0
Fair value adjustments for hedged risk			**8.8**			(1.1)
Total loans and advances to customers			**6,637.7**			5,845.9

Further analysis of the Group's loans and advances to customers and the associated loss allowance, including the movement in the loss allowance in the year, can be found in the creditworthiness risk section of the Risk Management Report on page 103.

Total loans and advances to customers include:

- £974.2 million (2018: £1,402.7 million) positioned with the Bank of England for use as collateral against amounts drawn under its Term Funding Scheme (see Note 25).
- £163.6 million (2018: £200.7 million) pledged as collateral against secured bank borrowings (see Note 25).
- £286.2 million (2018: £nil) pledged to securitisation programmes (see Note 15).

The finance lease receivables and instalment credit receivables relate to agreements issued by the Group to customers for a variety of assets including, but not limited to, plant and machinery. The underlying assets provide security against the gross receivables.

The following table provides further analysis of the Group's finance lease receivables:

	2019 £m	2018 £m
Gross amounts receivable:		
within one year	**38.9**	46.0
in the second to fifth year	**42.8**	50.0
after five years	**8.1**	10.0
Unearned finance income	**(8.8)**	(11.0)
Gross carrying amount	**81.0**	95.0
Loss allowance	**(6.4)**	(7.2)
Total finance lease receivables	**74.6**	87.8
Amounts falling due:		
within one year	**32.2**	38.0
in the second to fifth year	**35.5**	41.3
after five years	**6.9**	8.5
Total finance lease receivables	**74.6**	87.8

Notes to the financial statements

For the year ended 31 December 2019

14. Loans and advances to customers continued

The following table provides further analysis of the Group's instalment credit receivables:

	2019 £m	2018 £m
Gross amounts receivable:		
within one year	**184.8**	173.7
in the second to fifth year	**214.2**	249.2
after five years	**14.1**	26.5
Unearned finance income	**(30.7)**	(40.0)
Gross carrying amount	**382.4**	409.4
Loss allowance	**(7.3)**	(6.5)
Total instalment credit receivables	**375.1**	402.9
Amounts falling due:		
within one year	**165.9**	151.9
in the second to fifth year	**196.0**	226.1
after five years	**13.2**	24.9
Total instalment credit receivables	**375.1**	402.9

Included within instalment credit receivables are block discounting facilities of £173.5 million (2018: £157.2 million).

The cost of equipment acquired by the Group during the year for the purpose of letting to customers under finance lease and instalment credit agreements is as follows:

	2019 £m	2018 £m
Finance leases	**29.8**	58.9
Instalment credit	**102.7**	140.2
Total cost of equipment acquired during the year	**132.5**	199.1

Modifications

The Group sometimes modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximising recovery.

Details of the Group's forborne loans are set out in the creditworthiness risk section of the Risk Management Report on page 120.

Write-offs still under enforcement activity

Loans that are written off can still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due. The contractual amount outstanding on loans and advances to customers that were written off during the reporting period, and are still subject to enforcement activity, is £19.9 million (2018: £13.5 million).

15. Securitisation

See accounting policies in Note 1.7(h)

In June 2019, the Group securitised certain variable and fixed rate mortgage loans included within loans and advances to customers. The securitised loans, originated by the Group's principal subsidiary, Shawbrook Bank Limited, were transferred to a bankruptcy remote SPV, Shawbrook Mortgage Funding 2019-1 plc. The SPV is treated as a subsidiary of the Group and is fully consolidated.

The securitisation provides long-term funding to the Group through the simultaneous issue of mortgage backed debt securities by the SPV to external investors (see Note 28).

The Group continues to service the transferred loans in return for an administration fee and is entitled to any residual income from the SPV after the debt obligations and senior expenses of the securitisation programme have been met.

The transfer of loans are not treated as sales and the loans continue to be recognised in their entirety in loans and advances to customers in the statement of financial position. As such, no gains or losses have been recognised on pledging the loans to the securitisation programme.

The following table summarises the carrying amount of transferred loans and the associated debt securities in issue as at 31 December 2019:

	2019 £m
Loans securitised	**286.2**
Debt securities in issue	**240.7**

To allow for the original hedge accounting relationships relating to the securitised loans to be maintained, back-to-back balance guaranteed swaps were entered into with an external counterparty. The notional amount of these swaps will amortise in their entirety based upon the realised amortisation of the reference pool of performing fixed rate mortgage loans. Details of the nominal and carrying amounts of these swaps are presented in Note 17.

16. Investment securities

See accounting policies in Note 1.7(i)

	2019 £m	2018 £m
As at 1 January	**139.9**	–
Additions	**60.0**	139.7
Accrued interest	**0.1**	0.2
As at 31 December	**200.0**	139.9

Investment securities comprise covered bonds.

Investment securities include £100.0 million (2018: £nil) positioned with the Bank of England for use as collateral against amounts drawn under its Term Funding Scheme (see Note 25).

The loss allowance for investment securities is immaterial in both reported years, totalling less than £0.1 million.

17. Derivative financial instruments and hedge accounting

See accounting policies in Note 1.7(j) and Note 1.7(k)

Derivative financial instruments

Derivative financial instruments are used by the Group for risk management purposes in order minimise or eliminate the impact of movements in interest rates and foreign exchange rates. Derivatives are not used for trading or speculative purposes. The Group uses the International Swaps and Derivatives Association Master Agreement to document these transactions in conjunction with a Credit Support Annex.

The following table analyses the Group's derivative financial instruments by type of instrument:

	Assets		**Liabilities**	
As at 31 December 2019	**Nominal amount £m**	**Carrying amount £m**	**Nominal amount £m**	**Carrying amount £m**
Interest rate swaps	546.2	2.3	915.0	9.6
Interest rate options	–	–	1,150.0	4.0
Cross-currency swaps	40.0	0.8	–	–
Balance guaranteed swaps	236.2	1.3	236.2	1.3
Total	822.4	4.4	2,301.2	14.9

	Assets		Liabilities	
As at 31 December 2018	Nominal amount £m	Carrying amount £m	Nominal amount £m	Carrying amount £m
Interest rate swaps	431.5	1.4	559.2	1.2
Interest rate options	–	–	1,150.0	4.3
Cross-currency swaps	28.7	0.2	11.6	0.2
Total	460.2	1.6	1,720.8	5.7

Interest rate swaps are used by the Group to manage interest rate risk associated with the Group's loans and advances to customers and customer deposits. Cross currency swaps are used by the Group to manage foreign exchange risk associated with the Group's loans and advances to customers and banks.

Interest rate options are used by the Group specifically to manage interest rate risk associated with certain loans within its property loan portfolio. The property loan portfolio includes loans where interest rate terms are referenced to the three-month LIBOR index, but with a minimum reference rate of 0.75%. The Group has sold interest rate options with a nominal amount of £1,150.0 million into the wholesale market in order to hedge the Group's interest rate position against possible increases in the reference rate. Of these interest rate options, £575.0 million are forward starting, with an effective date beyond 31 December 2019.

Balance guaranteed swaps are entered into in relation to the Group's securitisation. See Note 15 for details.

From March 2019, the Group began transacting in swaps linked to SONIA for new hedges, rather than LIBOR as previously used, in order to mitigate the Group's exposure to LIBOR in preparation for LIBOR reform. Legacy hedges remain designated against LIBOR. Further information regarding interest rate benchmark reform can be found in Note 1.6(c) and in the market risk section of the Risk Management Report on page 132.

The derivatives market has been the subject of regulatory focus in recent years. Article 4 of the European Market Infrastructure Regulation requires that standardised over-the-counter (OTC) derivatives are mandatorily cleared through authorised central counterparties. The Group is classified as a Category 3 financial counterparty, the deadline for which to commence clearing OTC trades was 17 October 2019. Accordingly, since October 2019, the Group has cleared its standardised OTC derivatives via ABN Amro with London Clearing House. The table below splits out the total nominal amount of derivative financial instruments into cleared and OTC:

	Assets			Liabilities		
As at 31 December 2019	**Cleared £m**	**OTC £m**	**Total nominal amount £m**	**Cleared £m**	**OTC £m**	**Total nominal amount £m**
Interest rate swaps	73.1	473.1	546.2	69.6	845.4	915.0
Interest rate options	–	–	–	–	1,150.0	1,150.0
Cross-currency swaps	–	40.0	40.0	–	–	–
Balance guaranteed swaps	–	236.2	236.2	–	236.2	236.2
Total	73.1	749.3	822.4	69.6	2,231.6	2,301.2

Hedge accounting

The Group holds interest rate swaps and options as hedging instruments in fair value hedges. The Group's cross-currency swaps and balance guaranteed swaps are not in hedge accounting relationships. The Group does not currently designate any derivatives as cash flow hedges or net investment hedges.

Details of the Group's fair value hedges as at 31 December are presented in the following tables:

						Maturity
As at 31 December 2019	**Less than 1 month**	**1 – 3 months**	**3 months – 1 year**	**1 – 5 years**	**More than 5 years**	**Total**
Interest rate swaps						
Nominal amount (£m)	–	–	407.0	1,002.5	51.7	1,461.2
Average fixed interest rate	–	–	1.03%	0.88%	1.21%	1.04%
Interest rate options						
Nominal amount (£m)	–	–	50.0	1,000.0	100.0	1,150.0
Average fixed interest rate	–	–	0.75%	0.75%	0.75%	0.75%

						Maturity
As at 31 December 2018	Less than 1 month	1 – 3 months	3 months – 1 year	1 – 5 years	More than 5 years	Total
Interest rate swaps						
Nominal amount (£m)	–	–	50.0	913.4	27.3	990.7
Average fixed interest rate	–	–	1.20%	1.12%	1.34%	1.16%
Interest rate options						
Nominal amount (£m)	–	–	–	850.0	300.0	1,150.0
Average fixed interest rate	–	–	–	0.75%	0.75%	0.75%

17. Derivative financial instruments and hedge accounting continued

The amounts relating to items designated as hedging instruments and hedge ineffectiveness are set out in the tables below. The carrying amount of assets and liabilities included in these tables are presented in the statement of financial position on the lines derivative financial assets and derivative financial liabilities, respectively. Ineffectiveness is recognised in the statement of profit and loss on the line net gains/(losses) on financial instruments mandatorily at fair value through profit or loss. The main sources of ineffectiveness in these hedge relationships relate to the modelled prepayment/repayment behaviour and the assumptions that are used in modelling this behaviour.

As at 31 December 2019	**Nominal amount £m**	**Carrying amount £m**	**Change in fair value used for calculating ineffectiveness £m**	**Ineffectiveness recognised in statement of profit and loss £m**
Interest rate swaps				
Assets	**546.2**	**2.3**	**(8.5)**	**(0.1)**
Liabilities	**915.0**	**9.6**	**0.4**	**–**
Interest rate options				
Liabilities	**1,150.0**	**4.0**	**0.4**	**0.1**

As at 31 December 2018	Nominal amount £m	Carrying amount £m	Change in fair value used for calculating ineffectiveness £m	Ineffectiveness recognised in statement of profit and loss £m
Interest rate swaps				
Assets	431.5	1.4	(0.7)	(0.5)
Liabilities	559.2	1.2	1.7	0.2
Interest rate options				
Liabilities	1,150.0	4.3	1.6	0.3

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

As at 31 December 2019	**Carrying amount £m**	**Accumulated fair value hedge adjustments on the hedged item included in the carrying amount of the hedged item[1] £m**	**Change in fair value used for calculating ineffectiveness £m**
Assets			
Loans and advances to customers	**2,371.2**	**8.8**	**8.0**
Liabilities			
Customer deposits	**240.0**	**(0.5)**	**(0.4)**

As at 31 December 2018	Carrying amount £m	Accumulated fair value hedge adjustments on the hedged item included in the carrying amount of the hedged item £m	Change in fair value used for calculating ineffectiveness £m
Assets			
Loans and advances to customers	2,890.6	(1.1)	(1.1)
Liabilities			
Customer deposits	280.0	(0.1)	(1.4)

Net gains and losses on derivative financial instruments and hedge accounting
Gains and losses on derivative financial instruments and hedge accounting per the statement of profit and loss are summarised as follows:

	2019 £m	2018 £m
Fair value (losses)/gains on derivative financial instruments[2]	**(6.1)**	2.1
Fair value gains/(losses) on hedged risk	**8.4**	(2.5)
Net gains/(losses) on financial instruments mandatorily at fair value through profit or loss[2]	**2.3**	(0.4)

Fair value (losses)/gains on derivative financial instruments include foreign exchange gains/(losses).

[1] The accumulated amount of fair value adjustments remaining in the statement of financial position for hedged items that have been de-designated, for which the fair value hedged item adjustment is being amortised into the statement of profit and loss is £0.5 million.

[2] Comparatives for the year ended 31 December 2018 have been restated to reclass £0.9 million of foreign exchange losses on derivative financial instruments from administrative expenses to net gains/(losses) on financial instruments mandatorily at fair value through profit or loss, to ensure compliance with the accounting policy set out in Note 1.3.

Notes to the financial statements

For the year ended 31 December 2019

18. Property, plant and equipment

See accounting policies in Note 1.7(l)

Year ended 31 December 2019	Right-of-use leasehold property[1] £m	Leasehold property £m	Fixtures, fittings and equipment £m	Assets on operating leases £m	Total £m
Cost					
As at 1 January 2019	–	0.7	14.8	58.3	73.8
Impact of adopting IFRS 16	10.3	–	–	–	10.3
As at 1 January 2019 (adjusted)	10.3	0.7	14.8	58.3	84.1
Additions	2.5	1.7	1.7	18.2	24.1
Disposals	(0.2)	–	(0.3)	(8.7)	(9.2)
Transfer to finance leases	–	–	–	(7.4)	(7.4)
As at 31 December 2019	12.6	2.4	16.2	60.4	91.6
Accumulated depreciation					
As at 1 January 2019	–	0.6	9.9	24.2	34.7
Charge for the year	1.5	0.3	1.6	8.6	12.0
Disposals	–	–	–	(7.0)	(7.0)
Transfer to finance leases	–	–	–	(5.3)	(5.3)
As at 31 December 2019	1.5	0.9	11.5	20.5	34.4
Carrying amount					
As at 31 December 2019	11.1	1.5	4.7	39.9	57.2

Year ended 31 December 2018	Leasehold property £m	Fixtures, fittings and equipment £m	Assets on operating leases £m	Total £m
Cost				
As at 1 January 2018	0.8	11.2	63.7	75.7
Additions	–	3.6	8.2	11.8
Disposals	(0.1)	–	(9.8)	(9.9)
Transfer to finance leases	–	–	(3.8)	(3.8)
As at 31 December 2018	0.7	14.8	58.3	73.8
Accumulated depreciation				
As at 1 January 2018	0.5	8.0	27.6	36.1
Charge for the year	0.1	1.9	7.6	9.6
Disposals	–	–	(8.0)	(8.0)
Transfer to finance leases	–	–	(3.0)	(3.0)
As at 31 December 2018	0.6	9.9	24.2	34.7
Carrying amount				
As at 31 December 2018	0.1	4.9	34.1	39.1

Further details relating to assets on operating leases and right-of-use leasehold property are set out in Note 29.

[1] Adoption of IFRS 16 'Leases' on 1 January 2019 resulted in the recognition of right-of-use assets. A new asset category was created to present these assets. See Note 1.6(a) for details.

19. Intangible assets

See accounting policies in Note 1.7(m)

	2019 Goodwill £m	2019 Computer software £m	2019 Total £m	2018 Goodwill £m	2018 Computer software £m	2018 Total £m
Cost						
As at 1 January	44.8	36.3	81.1	44.8	29.1	73.9
Additions	–	8.0	8.0	–	9.8	9.8
Disposals	–	–	–	–	(2.6)	(2.6)
As at 31 December	44.8	44.3	89.1	44.8	36.3	81.1
Accumulated amortisation and impairment						
As at 1 January	1.1	13.6	14.7	–	8.2	8.2
Charge for the year	–	7.8	7.8	–	6.1	6.1
Impairment in the year	–	–	–	1.1	–	1.1
Disposals	–	–	–	–	(0.7)	(0.7)
As at 31 December	1.1	21.4	22.5	1.1	13.6	14.7
Carrying amount						
As at 31 December	43.7	22.9	66.6	43.7	22.7	66.4

Computer software additions include £7.6 million of internally generated assets (2018: £9.6 million).

Impairment testing of goodwill

For the purposes of impairment testing, goodwill is allocated to the Group's CGUs, which are also the Group's reportable lending divisions, as detailed in Note 2.

Details of impairment testing, including key assumptions and sensitivity analysis, are set out in Note 1.9(b).

No impairment losses have been recognised in the year ended 31 December 2019. In year ended 31 December 2018, an impairment loss of £1.1 million was recognised against the goodwill allocated to the Consumer Lending CGU. This reduced the carrying amount of goodwill in this CGU to £nil.

The following table sets out the carrying amount of goodwill by CGU as at 31 December (after the recognition of impairment losses):

	2019 £m	2018 £m
Property Finance	9.0	9.0
Business Finance	34.7	34.7
Total goodwill	43.7	43.7

Notes to the financial statements

For the year ended 31 December 2019

20. Deferred tax assets

See accounting policies in Note 1.7(f)

Deferred tax assets are attributable to the following items:

	2019 £m	2018 £m
Decelerated tax depreciation	11.2	12.1
IFRS 9 adjustment	2.8	4.9
General provisions	0.6	0.7
Other	0.3	0.3
Total deferred tax assets	**14.9**	18.0

Movements in deferred tax assets are attributable to the following items:

	2019 £m	2018 £m
As at 1 January	**18.0**	15.7
Impact of adopting IFRS 9	–	5.6
Restated balance as at 1 January	**18.0**	21.3
Current period movement – recognised in income	(0.8)	(3.5)
Adjustment in respect of prior years	(2.3)	0.2
As at 31 December	**14.9**	18.0

The Group's deferred tax assets result primarily from decelerated capital allowances. The business plan projects profits in future years sufficient to fully recognise the deferred tax assets. The tax assets will unwind over the remaining life of the underlying assets with which they are associated.

Reduction in the UK corporation tax rate from 19% to 17% (effective 1 April 2020) was substantively enacted on 16 March 2016. As detailed in Note 43, in March 2020, it was announced in Budget 2020 that the main rate of corporation tax will remain at 19%, rather than reducing it to 17% from 1 April 2020.

The deferred tax asset in both reported years has been calculated based on an aggregation rate of 25%. This is based on a rate of 17% substantively enacted at the reporting date and the additional 8% of tax suffered in relation to the banking surcharge that will unwind over the remaining life of the underlying assets with which they are associated.

21. Investment in associate

See accounting policies in Note 1.7(n)

The Group acquired 19.99% of the ordinary shares of The Mortgage Lender Limited on 26 March 2018. Although the Group holds less than 20% of the ordinary shares, the Group is deemed to have significant interest. As such, the investment in The Mortgage Lender Limited is accounted for using the equity method of accounting.

The Mortgage Lender Limited's principal activity is mortgage finance and its place of incorporation and principal place of business is the UK.

To align to the Group's reporting period, The Mortgage Lender Limited has changed its financial year end date from 31 August to 31 December. Consequently, The Mortgage Lender Limited reports a long 16-month reporting period from 1 September 2018 to 31 December 2019. In the year ended 31 December 2019, monthly unaudited management accounts have been used for the purposes of applying the equity method of accounting. In the year ended 31 December 2018, the financial statements for the year to 31 August 2018 and monthly unaudited management accounts for September to December 2018 were used.

Summarised financial information in respect of The Mortgage Lender Limited is set out below:

As at 31 December	2019 £m	2018 £m
Current assets	4.4	3.9
Non-current assets	0.5	0.5
Current liabilities	(1.5)	(0.5)
Non-current liabilities	(0.1)	(0.1)
Net assets	3.3	3.8

	12 months to 31 December 2019 £m	9 months from acquisition to 31 December 2018 £m
Revenue	14.5	4.3
Loss from continuing operations	(0.7)	(2.3)
Total comprehensive loss for the period	(0.7)	(2.3)
Dividends received from the associate during the period	–	–

A reconciliation of the above summarised financial information to the carrying amount of the investment in associate recognised in the statement of financial position as at 31 December is shown below:

	2019	2018
Net assets of the associate (£m)	3.3	3.8
Proportion of the Group's ownership interest in the associate	19.99%	19.99%
Group's share of net assets (£m)	0.7	0.8
Goodwill (£m)	4.7	4.7
Total investment in associate (£m)	5.4	5.5

The total investment in associate includes a £0.1 million share of the losses of the associate recognised in the statement of profit and loss for the year ended 31 December 2019 (2018: £0.5 million loss).

22. Other assets

	Group 2019 £m	Company 2019 £m	Group 2018 £m	Company 2018 £m
Other debtors	1.9	–	2.9	–
Prepayments	7.1	0.5	9.8	0.1
Amounts due from Group companies	–	0.9	–	1.7
Total other assets	9.0	1.4	12.7	1.8

Notes to the financial statements

For the year ended 31 December 2019

23. Assets held for sale

See accounting policies in Note 1.7(o)

As at 31 December 2019, a portfolio of unsecured personal loans from the Consumer Lending division met the criteria for classification as a disposal group held for sale.

Details of the loans classified as held for sale are as follows:

As at 31 December 2019	Gross carrying amount £m	Loss allowance £m	Carrying amount £m
Total loans held for sale	112.6	(8.5)	104.1

Further analysis of the Group's assets held for sale and the associated loss allowance can be found in the creditworthiness risk section of the Risk Management Report on page 106.

On 24 December 2019, a loan sale agreement was signed and a deposit of £48.9 million was received. In accordance with the terms of the loan sale agreement, the risks and rewards of ownership are not transferred until full payment is received on the completion date (31 January 2020). As such, in the year ended 31 December 2019, the sale of the loan portfolio is not recognised and the loan assets continue to be recognised at amortised cost in the statement of financial position as assets held for sale. The deposit received is recognised as deferred income and is included in other liabilities in the statement of financial position (see Note 30).

24. Investment in subsidiaries

Investment in subsidiaries in the Company statement of financial position is as follows:

	2019 £m	2018 £m
Equity shares in Shawbrook Bank Limited	267.8	267.8
Capital securities in Shawbrook Bank Limited	125.0	125.0
Share-based payments	17.2	16.4
Total investment in subsidiaries	410.0	409.2

Details of subsidiary companies are set out in Note 37. The principal terms of the capital securities in Shawbrook Bank Limited are detailed in Note 33.

Movements in the Company's investment in subsidiaries are as follows:

	2019 £m	2018 £m
As at 1 January	409.2	409.5
Share-based payments	0.8	(0.3)
As at 31 December	410.0	409.2

25. Amounts due to banks

See accounting policies in Note 1.7(p)

	2019 £m	2018 £m
Central bank facilities	758.5	876.6
Secured bank borrowings	123.1	152.0
Derivative collateral	–	0.8
Total amounts due to banks	881.6	1,029.4

Total amounts due to banks include:

- £757.0 million (2018: £875.0 million) drawn under the Bank of England's Term Funding Scheme which fall due for repayment between 2021 and 2022. These amounts are collateralised by loan assets of £974.2 million (2018: £1,402.7 million) and investment securities of £100.0 million (2018: £nil).
- £123.1 million (2018: £152.0 million) of secured bank borrowings which fall due for repayment in 2020. These amounts are secured on loan assets of £163.6 million (2018: £200.7 million).

26. Customer deposits

See accounting policies in Note 1.7(q)

	2019 £m	2018 £m
Instant access	2,020.2	1,365.6
Term deposits and notice accounts	4,088.7	3,612.2
Fair value adjustments for hedged risk	0.5	0.1
Total customer deposits	6,109.4	4,977.9

27. Provisions for liabilities and charges

See accounting policies in Note 1.7(r)

	2019			2018		
	Loss provisions £m	Other provisions £m	Total £m	Loss provision £m	Other provisions £m	Total £m
As at 1 January	1.0	10.6	11.6	–	2.8	2.8
Impact of adopting IFRS 9	–	–	–	0.5	–	0.5
Restated balance as at 1 January	1.0	10.6	11.6	0.5	2.8	3.3
Provisions utilised	–	(7.8)	(7.8)	–	(1.8)	(1.8)
Provisions made	–	4.5	4.5	0.5	9.6	10.1
As at 31 December	1.0	7.3	8.3	1.0	10.6	11.6

Notes to the financial statements

For the year ended 31 December 2019

27. Provisions for liabilities and charges continued

Loss provision

Loss provision represents the loss allowance on financial guarantee contracts and loan commitments. Further details are set out in Note 41.

Other provisions

Other provisions are as follows:

- £7.3 million (2018: £10.2 million) for customer remediation and conduct issues. See Note 1.9(c) for details.
- £nil (2018: £0.4 million) relating to the Financial Services Compensation Scheme.

28. Debt securities in issue

See accounting policies in Note 1.7(h

In June 2019, a Group company, Shawbrook Mortgage Funding 2019-1, issued £250.0 million of sterling mortgage backed floating rate Class A notes to external investors as part of the Group's securitisation programme detailed in Note 15. The notes are secured on a portfolio of variable and fixed rate mortgage loans.

The notes bear interest on their principal amount at an initial rate of Compounded Daily SONIA plus 1.12% per annum, until the optional redemption date of 16 September 2022. Interest is payable quarterly in arrears in March, June, September and December, commencing on 16 September 2019.

The final maturity date of the notes is 16 December 2050. The final maturity date of the notes is later than the final repayment date of any of the underlying loans.

The notes may be redeemed in part from time to time, but such redemptions are limited to the principal repayments received from borrowers in respect of the underlying loans. The notes may all be repurchased by the Group at any interest payment date on or after the optional redemption date, or at any interest payment date when the current balance of the loans outstanding is less than or equal to ten percent of the principal amount outstanding on the notes on the date they were issued.

The Group's obligations to the note holders are limited to the cash flows (principal and interest) generated from the underlying loans.

Movements in debt securities during the year are as follows:

	2019 £m
As at 1 January	–
Issue of notes	250.0
Redemptions	(8.2)
Capitalised costs	(1.7)
Accrued interest and amortisation of costs	0.6
As at 31 December	**240.7**

As part of the securitisation programme, further sterling mortgage backed floating rate notes (Class B, C and Z) amounting to £45.9 million were issued by Shawbrook Mortgage Funding 2019-1 plc and were retained by Shawbrook Bank Limited. These notes are eliminated in full on consolidation.

As at 31 December 2019, for liquidity purposes, certain of the internally held notes have been used in a security swap in exchange for UK gilts. No cash consideration was exchanged in this transaction. The notes sold are not derecognised and the UK gilts purchased are not recognised on the statement of financial position.

29. Leases

See accounting policies in Note 1.7(s)

As detailed in Note 1.6(a), on 1 January 2019 the Group adopted IFRS 16 'Leases', replacing IAS 17 'Leases'. The Group used the modified retrospective approach, meaning comparative information is not restated. As such, information for 2019 is presented on an IFRS 16 basis and information for 2018 is presented on an IAS 17 basis. The impact of this on the comparability of the below disclosures is set out in the respective sections.

Group as a lessor

Lessor accounting under IFRS 16 is largely unchanged from IAS 17. As such, the accounting policies applied by the Group are consistent in both reported years and comparison of the disclosed information can be made between the reported years.

Finance leases

Assets leased to customers under finance leases are predominantly plant and machinery. Details of the Group's finance lease receivables are set out in Note 14.

Operating leases

Assets leased to customers under operating leases are predominantly plant and machinery. The carrying amount of the Group's assets on operating leases and the movements during the year are set out in Note 18. Net income from operating leases is presented on the face of the statement of profit and loss.

Future minimum rentals receivable under non-cancellable operating leases as at 31 December are as follows:

	2019 £m	2018 £m
Less than 1 year	**9.7**	8.4
Between 1 and 5 years	**20.2**	16.2
More than 5 years	**1.2**	0.9
Total future minimum rentals receivable	**31.1**	25.5

Group as a lessee

On adoption of IFRS 16 on 1 January 2019, the Group only had operating leases. In 2018, under the requirements of IAS 17, these leases were held off-balance sheet. As such, comparative information is not shown in the following tables.

The Group has lease contracts for several buildings. These leases typically have lease terms of between 5 and 10 years. The Group does not sublease any of these leased assets. For these leases, a right-of-use asset is recognised to represent the right to use the underlying asset and a lease liability is recognised to represent the obligation to make lease payments.

The carrying amount of the right-of-use assets and the movements during the year are set out in Note 18.

Notes to the financial statements

For the year ended 31 December 2019

29. Leases continued

The carrying amount of the lease liabilities and the movements during the year are set out in the table below:

	2019 £m
As at 1 January	–
Impact of adopting IFRS 16	10.9
As at 1 January (adjusted)	10.9
Additions	2.5
Disposals	(0.2)
Interest expense	0.2
Payments	(1.0)
As at 31 December	12.4

The maturity analysis of these lease liabilities is presented in the liquidity risk section of the Risk Management Report on page 125.

The Group has certain leases of office equipment with low value. For these leases, the Group applies the recognition exemptions for leases of low value assets, whereby no right-of-use asset is recognised and lease payments are charged to administrative expenses in the statement of profit and loss. Total expense recognised is summarised in the table below.

The Group also has several leases for buildings which, at the date of initial application of IFRS 16, had a remaining lease term of less than 12 months. For these leases, the Group elected to apply the short-term lease recognition exemption, whereby no right-of-use asset was recognised and lease payments continue to be charged to administrative expenses in the statement of profit and loss. Total expense recognised is summarised in the table below.

The following table provides a summary of the amounts recognised in the statement of profit and loss during the year ended 31 December 2019:

	2019		
	Administrative expenses £m	Interest expense £m	Total £m
Depreciation expense of right-of-use assets	1.5	–	1.5
Interest expense on lease liabilities	–	0.2	0.2
Rental expense on short-term leases	0.3	–	0.3
Rental expense on low value assets	0.1	–	0.1
Total recognised in the statement of profit and loss	1.9	0.2	2.1

In the year ended 31 December 2018, the amount recognised in administrative expenses in the statement of profit and loss for operating leases under IAS 17 was £2.4 million.

In the year ended 31 December 2019, the Group had cash outflows for leases included in the statement of cash flows of £1.0 million. This comprises £0.2 million for payment of the interest portion of the lease liability and £0.8 million for payment of the principal portion of the lease liability.

As at 31 December 2019, the Group is not committed to any lease contracts that have not yet commenced.

30. Other liabilities

Other liabilities in the Group statement of financial position are as follows:

Group	2019 £m	2018 £m
Other creditors	64.2	19.5
Accruals[1]	28.9	20.2
Total other liabilities	**93.1**	39.7

Other creditors include amounts relating to sundry creditors and other taxes.

In the year ended 31 December 2019, other creditors includes a £48.9 million deposit received in relation to the sale of a portfolio of unsecured personal loans from the Consumer Lending division. Further details are provided in Note 23.

31. Subordinated debt

See accounting policies in Note 1.7(t)

Subordinated debt liability
The Company has the following Tier 2 securities in issue:

- £75.0 million fixed rate reset callable subordinated notes due 2025. The notes were issued in October 2015 and were listed on the London Stock Exchange on 28 October 2015. The notes bear interest on their principal amount at an initial rate of 8.5% per annum until the first reset date of 28 October 2020. Interest is payable semi-annually in arrears in April and October.
- £20.0 million fixed rate reset callable subordinated notes due 2029. The notes were issued in September 2019 and were listed on the Open Market of the Frankfurt Stock Exchange on 11 October 2019. The notes bear interest on their principal amount at an initial rate of 6.5% per annum until the first reset date of 27 September 2024. Interest is payable semi-annually in arrears in March and September commencing in March 2020.

The following table sets out movements in the subordinated debt liability during the year:

	2019 £m	2018 £m
As at 1 January	**75.5**	75.4
Issue of notes	20.0	–
Interest expense and similar charges	6.8	6.5
Repayment of interest	(6.4)	(6.4)
As at 31 December	**95.9**	75.5

Subordinated debt receivable
Following the Company's issues of Tier 2 securities to the market, as detailed above, subordinated debt issues were made from Shawbrook Bank Limited to the Company on terms consistent with the listed loan notes. The subordinated debt receivable in the Company statement of financial position is £96.4 million (2018: £76.1 million).

The subordinated debt ranks behind any claims against the Group from all depositors and creditors.

1 On adoption of IFRS 16 'Leases' on 1 January 2019, accruals totalling £0.6 million related to contracts previously classified as operating leases were derecognised. See Note 1.6(a) for details.

32. Share capital

Ordinary shares of £0.01 each: issued and fully paid, are as follows:

	2019		2018	
	Number of shares	£	Number of shares	£
As at 1 January and 31 December	253,086,879	2,530,869	253,086,879	2,530,869

Each ordinary share has full voting, dividend and capital distribution rights, including on a winding up, but does not have any rights of redemption. Par value is £0.01 per share.

33. Capital securities

See accounting policies in Note 1.7u)

	2019 £m	2018 £m
As at 1 January and 31 December	124.0	124.0

The Company issued £125.0 million fixed rate reset perpetual Additional Tier 1 write down capital securities in December 2017. Net proceeds after the deduction of issuance costs totalled £124.0 million. The capital securities were listed on the Irish Stock Exchange on 8 December 2017.

The capital securities bear interest on their principal amount at an initial rate of 7.875% per annum until the first rest date of 8 December 2022. Interest is payable semi-annually in arrears in June and December and is non-cumulative. Interest is fully discretionary and the Company may elect to cancel (in whole or in part) the interest otherwise scheduled to be paid. Any interest not paid when scheduled will be cancelled. During the year ended 31 December 2019, the Group paid interest as scheduled amounting to £9.8 million (2018: £9.8 million).

The capital securities are perpetual with no fixed redemption date. The Company may elect to redeem all, but not part, of the capital securities on the first reset date or any reset date thereafter, or for certain regulatory or tax reasons. Any optional redemption requires the prior consent of the Prudential Regulation Authority.

The capital securities constitute direct, unsecured and subordinated obligations and rank pari passu without any preference among themselves. On a winding up of the Company, they rank ahead of the holders of all other classes of issued shares but junior to the claims of senior unsubordinated and subordinated creditors other than those whose claims rank pari passu with or junior to them.

In the event of the Group's Common Equity Tier 1 capital ratio falling below 7.0%, an automatic and permanent write down shall occur on the next business day, resulting in the reduction of the full principal amount of capital securities to zero, the cancellation of all capital securities and the cancellation of any interest which is accrued and unpaid.

Following the listing of the capital securities to the market, capital securities were issued from Shawbrook Bank Limited to the Company on consistent terms as the listed capital securities.

34. Notes to the cash flow statement

See accounting policies in Note 1.7(v)

Adjustments for non-cash items and other adjustments included in the statement of profit and loss

	Group 2019 £m	Company 2019 £m	Group 2018 £m	Company 2018 £m
ECL charge for the year	2.6	–	15.1	–
Accrued interest on investment securities	(0.1)	–	(0.2)	–
Depreciation of property, plant and equipment	12.0	–	9.6	–
Loss on disposal of property, plant and equipment	–	–	0.1	–
Amortisation of intangible assets	7.8	–	6.1	–
Impairment of goodwill	–	–	1.1	–
Loss on disposal of intangible assets	–	–	1.9	–
Share of results of associate	0.1	–	0.5	–
Accrued interest on subordinated debt receivable	–	(0.3)	–	–
Accrued interest and amortisation of costs on debt securities	0.6	–	–	–
Accrued interest and amortisation of costs on subordinated debt liability	0.4	0.4	0.1	0.1
Share-based payments	0.8	–	(0.3)	–
Gain on disposal of subsidiary	(0.3)	–	–	–
Total non-cash items and other adjustments	23.9	0.1	34.0	0.1

Net change in operating assets

	Group 2019 £m	Company 2019 £m	Group 2018 £m	Company 2018 £m
Increase in mandatory deposits with central banks	(3.6)	–	(4.6)	–
Increase in loans and advances to customers	(822.2)	–	(1,037.8)	–
(Increase)/decrease in derivative financial assets	(2.8)	–	0.2	–
Increase in operating lease assets	(14.4)	–	(5.6)	–
Decrease/(increase) in other assets	3.7	0.4	(2.4)	(0.3)
Increase in assets held for sale	(104.1)	–	–	–
(Increase)/decrease in operating assets	(943.4)	0.4	(1,050.2)	(0.3)

Net change in operating liabilities

	Group 2019 £m	Company 2019 £m	Group 2018 £m	Company 2018 £m
Increase in customer deposits	1,131.5	–	601.7	–
(Decrease)/increase in provisions for liabilities and charges	(3.3)	–	8.3	–
Increase in derivative financial liabilities	9.2	–	2.3	–
Increase/(decrease) in other liabilities	54.0	(0.2)	(23.1)	(0.1)
Increase/(decrease) in operating liabilities	1,191.4	(0.2)	589.2	(0.1)

Notes to the financial statements

For the year ended 31 December 2019

34. Notes to the cash flow statement continued

Cash and cash equivalents

	Group 2019 £m	Company 2019 £m	Group 2018 £m	Company 2018 £m
Cash and balances at central banks	1,064.6	–	645.2	–
Loans and advances to banks	59.1	–	50.6	–
Less: mandatory deposits with central banks	(12.5)	–	(8.9)	–
Total cash and cash equivalents	1,111.2	–	686.9	–

35. Financial instruments

See accounting policies in Note 1.7(w)

Classification of financial instruments

The following table provides a reconciliation between the line items in the statement of financial position and categories of financial instruments. There were no reclassifications between categories during either of the reported years.

	2019			2018		
	Mandatorily at FVTPL £m	Amortised cost £m	Carrying amount £m	Mandatorily at FVTPL £m	Amortised cost £m	Carrying amount £m
Financial assets						
Cash and balances at central banks	–	1,064.6	1,064.6	–	645.2	645.2
Loans and advances to banks	–	59.1	59.1	–	50.6	50.6
Loans and advances to customers	–	6,637.7	6,637.7	–	5,845.9	5,845.9
Investment securities	–	200.0	200.0	–	139.9	139.9
Derivative financial assets	4.4	–	4.4	1.6	–	1.6
Assets held for sale	–	104.1	104.1	–	–	–
Total financial assets	4.4	8,065.5	8,069.9	1.6	6,681.6	6,683.2
Financial liabilities						
Amounts due to banks	–	881.6	881.6	–	1,029.4	1,029.4
Customer deposits	–	6,109.4	6,109.4	–	4,977.9	4,977.9
Derivative financial liabilities	14.9	–	14.9	5.7	–	5.7
Debt securities in issue	–	240.7	240.7	–	–	–
Lease liabilities	–	12.4	12.4	–	–	–
Subordinated debt liability	–	95.9	95.9	–	75.5	75.5
Total financial liabilities	14.9	7,340.0	7,354.9	5.7	6,082.8	6,088.5

Fair value of financial instruments
A summary of the Group's valuation methods used to calculate the fair values of its financial instruments is as follows:

- **Cash and balances at central banks and loans and advances to banks:** fair value approximates to carrying amount as balances have minimal credit losses and are either short-term in nature or re-price frequently.
- **Loans and advances to customers:** fair value is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date, and adjusted for future credit losses if considered material.
- **Investment securities, debt securities in issue and subordinated debt liability:** fair values are based on quoted prices where available or by discounting cash flows using market rates.
- **Derivative financial instruments:** fair values of derivatives are obtained from quoted market prices in active markets and, where these are not available, from valuation techniques including discounted cash flows.
- **Amounts due to banks and customer deposits:** fair value is estimated using discounted cash flows applying either market rates where practicable or rates offered with similar characteristics by other financial institutions. The fair value of floating rate placements, fixed rate placements with less than six months to maturity and overnight deposits is considered to approximate to their carrying amount.
- **Assets held for sale:** fair values are calculated using expected or known sales price. Where such data is not available, fair values are calculated in accordance with the type of asset held for sale using the valuation methods detailed above.

In accordance with IFRS 7 'Financial Instruments: Disclosures', fair value disclosures are not required for lease liabilities. Accordingly, lease liabilities are not included in the following tables.

The Group uses a fair value hierarchy which reflects the significance of the inputs used in making the measurements. There are three levels to the hierarchy as follows:

- **Level 1:** quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date;
- **Level 2:** inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). A Level 2 input must be observable for substantially the full term of the instrument. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves observable at commonly quoted intervals, implied volatilities and credit spreads. Assets and liabilities classified as Level 2 have been valued using models whose inputs are observable in an active market; and
- **Level 3:** inputs for the asset or liabilities that are not based on observable market data (unobservable inputs).

The consideration of factors such as the scale and frequency of trading activity, the availability of prices and the size of bid/offer spreads assist in the assessment of whether a market is active. If, in the opinion of Management, a significant proportion of an instrument's carrying amount is driven by unobservable inputs, the instrument in its entirety is classified as Level 3 of the fair value hierarchy. Level 3 in this context means that there is little or no current market data available from which to determine the level at which an arm's length transaction would be likely to occur. It generally does not mean that there is no market data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

35. Financial instruments continued

The table below analyses the Group's financial instruments measured at amortised cost (excluding lease liabilities) into the fair value hierarchy. There were no transfers between the levels of the fair value hierarchy during either of the reported years.

	2019			2018		
	Level 3 £m	**Level 2 £m**	**Level 1 £m**	Level 3 £m	Level 2 £m	Level 1 £m
Financial assets (at amortised cost)						
Cash and balances at central banks	**–**	**–**	**1,064.6**	–	–	645.2
Loans and advances to banks	**–**	**59.1**	**–**	–	50.6	–
Loans and advances to customers	**6,637.7**	**–**	**–**	5,845.9	–	–
Investment securities	**–**	**–**	**200.0**	–	–	139.9
Assets held for sale	**104.1**	**–**	**–**	–	–	–
Financial liabilities (at amortised cost)						
Amounts due to banks	**–**	**881.6**	**–**	–	1,029.4	–
Customer deposits	**–**	**6,109.4**	**–**	–	4,977.9	–
Debt securities in issue	**–**	**240.7**	**–**	–	–	–
Subordinated debt liability	**–**	**95.9**	**–**	–	75.5	–

The table below analyses the Group's financial instruments measured at fair value into the fair value hierarchy. There were no transfers between the levels of the fair value hierarchy during either of the reported years. The Level 3 financial instruments in the year ended 31 December 2019 represent the balance guaranteed swaps entered into during the year in relation to the Group's securitisation (see Note 15).

	2019			2018		
	Level 3 £m	**Level 2 £m**	**Level 1 £m**	Level 3 £m	Level 2 £m	Level 1 £m
Financial assets (at fair value)						
Derivative financial assets	**1.3**	**3.1**	**–**	–	1.6	–
Financial liabilities (at fair value)						
Derivative financial liabilities	**1.3**	**13.6**	**–**	–	5.7	–

The following table provides a comparison of the carrying amount per the statement of financial position and the calculated fair value for the Group's financial instruments measured at amortised cost. In accordance with IFRS 7, cash and balances at central banks, loans and advances to banks and assets held for sale are not included in the table, as the carrying amount is a reasonable approximation of fair value and fair value disclosures are therefore not required. Lease liabilities are also excluded from the table as fair value disclosures are not required.

	2019		2018	
	Carrying amount £m	**Fair value £m**	Carrying amount £m	Fair value £m
Financial assets (at amortised cost)				
Loans and advances to customers	**6,637.7**	**6,784.7**	5,845.9	6,105.8
Investment securities	**200.0**	**200.4**	139.9	139.0
Financial liabilities (at amortised cost)				
Amounts due to banks	**881.6**	**873.3**	1,029.4	1,014.8
Customer deposits	**6,109.4**	**6,121.1**	4,977.9	4,972.8
Debt securities in issue	**240.7**	**241.2**	–	–
Subordinated debt liability	**95.9**	**100.0**	75.5	78.0

Offsetting financial assets and financial liabilities

The disclosures set out in the following tables include financial assets and financial liabilities that:

- are offset in the Group's statement of financial position; or
- are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in the statement of financial position.

Financial instruments such as loans and deposits are not disclosed in the following tables unless they are offset in the statement of financial position.

As at 31 December 2019	**Gross amount £m**	**Amount offset £m**	**Net amount presented on statement of financial position £m**	**Related amounts not offset Cash collateral received/pledged £m**	**Net amount £m**
Financial assets					
Derivative financial assets	**4.4**	**–**	**4.4**	**(4.4)**	**–**
Total financial assets	**4.4**	**–**	**4.4**	**(4.4)**	**–**
Financial liabilities					
Derivative financial liabilities	**14.9**	**–**	**14.9**	**(14.9)**	**–**
Total financial liabilities	**14.9**	**–**	**14.9**	**(14.9)**	**–**

As at 31 December 2018	Gross amount £m	Amount offset £m	Net amount presented on statement of financial position £m	Related amounts not offset Cash collateral received/pledged £m	Net amount £m
Financial assets					
Derivative financial assets	1.6	–	1.6	(1.6)	–
Total financial assets	1.6	–	1.6	(1.6)	–
Financial liabilities					
Derivative financial liabilities	5.7	–	5.7	(5.7)	–
Total financial liabilities	5.7	–	5.7	(5.7)	–

Notes to the financial statements

For the year ended 31 December 2019

36. Ultimate parent company

The ultimate parent and controlling party of the Group is Marlin Bidco Limited. Marlin Bidco Limited is a company jointly owned by PSCM Pooling LP and Marlinbass Limited. Both companies are incorporated in Guernsey and are investment vehicles of Pollen Street Capital Limited and BC Partners LLP respectively.

The largest company in which the results of the Group are consolidated is that headed by Shawbrook Group plc (see Note 1.1). No other financial statements include the results of the Group.

37. Subsidiary companies

See accounting policies in Note 1.4

The Company has the following subsidiary companies as at 31 December 2019 whose results are included in the consolidated financial statements:

Name	Country of incorporation	Class of shares	Ownership %	Principal activity
Shawbrook Bank Limited and its subsidiaries, as follows:	England and Wales	Ordinary	100	Banking
Shawbrook Buildings and Protection Limited	England and Wales	Ordinary	100	Dormant
Singers Corporate Asset Finance Limited	England and Wales	Ordinary	100	Dormant
Singers Healthcare Finance Limited	England and Wales	Ordinary	100	Dormant
Coachlease Limited	England and Wales	Ordinary	100	Dormant
Hermes Group Limited	England and Wales	Ordinary	100	Dormant
Singer & Friedlander Commercial Finance Limited	Scotland	Ordinary	100	Dormant
Link Loans Limited	England and Wales	Ordinary	100	Non-trading
Centric SPV 1 Limited	England and Wales	Ordinary	100	Dormant
Resource Partners SPV Limited	England and Wales	Ordinary	100	Dormant
Centric Group Holdings Limited	England and Wales	Ordinary	100	Dissolved[1]

All subsidiaries have the same registered office as the Company, as detailed in Note 1.1, except for Singer & Friedlander Commercial Finance Limited for which the registered office is: 8 Nelson Mandela Place, Glasgow, Scotland, G2 1BT.

Changes to the Group's subsidiaries during the year ended 31 December 2019 are as follows:

- **Shawbrook International Limited:** Company number: 121556, incorporated in Jersey. Sold on 31 October 2019.
- **Centric Group Finance Limited:** Company number: 06405442. Dissolved on 12 February 2019.

Special purpose vehicles

As part of the Group's financing arrangements, in the year ended 31 December 2019, certain mortgage loans originated by the Group's principal subsidiary, Shawbrook Bank Limited, were transferred to a SPV (see Note 15). The shares of the SPV and its holding company are ultimately beneficially owned through an independent trust. However, these entities are considered to be controlled by the Group and are therefore treated as subsidiaries of the Group and are fully consolidated. Details of these entities are as follows:

Name	Country of incorporation	Principal activity
Shawbrook Mortgage Funding 2019-1 plc	England and Wales	Residential mortgages
Shawbrook Mortgage Funding 2019-1 Holdings Limited	England and Wales	Holding company

The registered office for the above entities is: 35 Great St. Helen's, London, EC3A 6AP.

[1] Centric Group Holdings Limited (company number: 06402868) was dissolved on 4 February 2020.

38. Related party transactions

Transactions with key management personnel
Key management personnel refer to the Executive Management team and Directors of the Group.

Compensation
Total compensation for employed key management personnel for the year is as follows:

	2019 £m	2018 £m
Short-term employee benefits	5.8	7.0
Other long-term benefits	0.2	0.2
Termination benefits	0.4	1.4
Total compensation for employed key management personnel	6.4	8.6

In addition to the above, in the year ended 31 December 2019, the Group incurred fees of £0.1 million (2018: £0.1 million) in relation to the Institutional Directors appointed to the Board by the ultimate parent company, as set out and agreed within the Framework Agreement. The institutional Directors are not employed by the Group and their fees are not included in the above table.

Further details of compensation paid to the Directors of the Group are provided in the Directors' Remuneration Report on page 66.

Transactions
The Group provides employee loans to certain key management personnel. These loans are subject to interest in accordance with the beneficial loan arrangements rate set by HMRC from time to time. The loans do not involve more than the normal risk of collectability or present other unfavourable features. As at 31 December 2019, the amount outstanding in respect of these loans is £0.4 million (2018: £nil). Interest income recognised in respect of these loans during the year ended 31 December 2019 is less than £0.1 million (2018: £nil). No provisions have been recognised in respect of these loans (2018: £nil) and no balances have been written off or forgiven during the year to 31 December 2019 (2018: £nil).

The Group also holds savings deposits from certain key management personnel and their close family members. Such deposits are held in the ordinary course of business on normal commercial terms. As at 31 December 2019, the amount held in respect of these deposits is £0.3 million (2018: £0.3 million). Interest expense recognised in respect of these deposits during both reported years was less than £0.1 million.

Transactions with the ultimate parent
The ultimate parent and controlling party of the Group is detailed in Note 36.

As at 31 December 2019, the balance owed to Marlin Bidco Limited is £0.8 million (2018: £nil).

During the year ended 31 December 2019, certain employees, including key management personnel, acquired non-voting 'B' Class ordinary shares in Marlin Bidco Limited as part of an employee share-based payment scheme. See Note 9 for further details.

Transactions with associate
Details of the Group's associate are provided in Note 21.

As at 31 December 2019, the balance owed to the Mortgage Lender Limited is £0.1 million (2018: £nil).

In the year ended 31 December 2019, the Group paid £4.0 million of commission and servicing fees to the Mortgage Lender Limited (2018: £0.8 million).

Notes to the financial statements

For the year ended 31 December 2019

38. Related party transactions continued

Transactions with subsidiaries

Subsidiaries of the Group are detailed in Note 37.

Transactions between the Company and its subsidiaries

As at 31 December 2019, the balance owed to the Company by its principal subsidiary, Shawbrook Bank Limited, is £0.9 million (2018: £1.7 million) (see Note 22). Movements in amounts owed by Shawbrook Bank Limited are as follows:

	Company 2019 £m	Company 2018 £m
As at 1 January	**1.7**	1.0
Subordinated debt receivable	**(20.0)**	–
Interest receivable on subordinated debt	**6.4**	6.4
Subordinated debt payable	**20.0**	–
Interest payable on subordinated debt	**(6.4)**	(6.4)
Coupon receivable on capital securities	**9.8**	9.8
Coupon payable on capital securities	**(9.8)**	(9.8)
Professional fees and other costs	**0.5**	1.5
Transfer of funds	**(1.3)**	(0.8)
As at 31 December	**0.9**	1.7

Shawbrook Bank Limited has issued £95.0 million (2018: £75.0 million) of subordinated debt to the Company. The terms and conditions are consistent with the subordinated notes listed by the Company (see Note 31).

Shawbrook Bank Limited has issued £125.0 million (2018: £125.0 million) of capital securities to the Company. The terms and conditions are consistent with the capital securities listed by the Company (see Note 33).

Transactions between the Group's subsidiaries

Prior to the sale of Shawbrook International Limited in October 2019, Shawbrook Bank Limited made payments of £0.8 million (2018: £31.4 million) to Shawbrook International Limited. In addition, seven loans with a carrying amount of £13.8 million were transferred from Shawbrook International Limited to Shawbrook Bank Limited.

All amounts owing from Shawbrook International Limited to Shawbrook Bank Limited were repaid upon the sale of Shawbrook International Limited. As at 31 December 2018, the balance owed by Shawbrook International Limited to Shawbrook Bank Limited was £42.6 million.

As part of the Group's securitisation programme, in the year ended 31 December 2019, loans originated by Shawbrook Bank Limited with a carrying amount of £286.2 million were transferred to a bankruptcy remote SPV, Shawbrook Mortgage Funding 2019-1 plc (see Note 15). The SPV issued sterling mortgage backed floating rate notes, of which £45.9 million were retained by Shawbrook Bank Limited (see Note 28).

39. Capital commitments

The Group's capital commitments as at 31 December 2019 are £nil (2018: £nil).

40. Contingent liabilities

See accounting policies in Note 1.7(y)

Part of the Group's business is regulated by the Consumer Credit Act (CCA), which contains very detailed and highly technical requirements. The Group continues to commission external reviews of its compliance with the CCA and other consumer regulations. The Group has identified some areas of potential non-compliance which are not considered to be material. While the Group considers that no material present obligation in relation to non-compliance with the CCA and other consumer regulations is likely, there is a risk that the eventual outcome may differ.

The Group's Consumer Lending division is exposed to risk under Section 75 of the CCA, in relation to any misrepresentations or breaches of contract by suppliers of goods and services to customers where the purchase of those goods and services is financed by the Group. While the Group would have recourse to the supplier in the event of such liability, if the supplier becomes insolvent that recourse would have limited value.

41. Financial guarantee contracts and loan commitments

See accounting policies in Note 1.7(z)

Financial guarantee contracts
In both reported years, the Group has had one financial guarantee contract amounting to £2.5 million. The contract is a continuous obligation which may be terminated by the Group on giving three months written notice.

The loss allowance for financial guarantee contract in both reported years is £nil, because the contract is fully collateralised through a first fixed charge over a blocked deposit account. As such, the amount the Group should have to pay should the guarantee be called upon is £nil.

Loan commitments

	2019 £m	2018 £m
Gross amount committed	**591.5**	549.3
Loss allowance recognised within provisions (see Note 27)	**(1.0)**	(1.0)
Total loan commitments	**590.5**	548.3

Further analysis of the Group's loan commitments and the associated loss allowance, including the movement in the loss allowance during the year, can be found in the creditworthiness risk section of the Risk Management Report on page 107.

Notes to the financial statements

For the year ended 31 December 2019

42. Country by country reporting

The Capital Requirements (Country by Country Reporting) Regulations 2013 came into effect on 1 January 2014 and place certain reporting obligations on financial institutions that are within the scope of the Capital Requirements Directive IV.

Shawbrook Group plc and its subsidiaries are all UK or Channel Island registered entities. The activities of the Group and its subsidiaries are detailed in the Strategic Report and Note 37.

Required disclosures are summarised below:

	2019	2018
Net operating income (£m)	**295.1**	274.1
Profit before tax (£m)	**122.4**	110.0
Tax charge (£m)[1]	**28.8**	25.9
Tax paid (£m)	**28.7**	26.3
Average number of employees on a full-time equivalent basis	**814**	731

The Group received no public subsidies during the year (2018: £nil).

43. Post balance sheet events

On 31 January 2020, the Group completed the sale of a portfolio of unsecured personal loans from the Consumer Lending division. The gain on disposal is circa ~£0.5 million. As at 31 December 2019, these loans are classified as held for sale and further details can be found in Note 23.

Since the close of the financial reporting period, the outbreak of coronavirus (Covid-19) has been labelled a global pandemic by the World Health Organization. As the outbreak continues to evolve, the Board has employed preventative measures to minimise potential risk to employees and provide ongoing services to customers. The Group has updated its existing business continuity plans and has implemented its Incident Management Plan. In the Risk Management Report, a new top risk theme, global pandemic risk, has been established and further assessment of the risk is provided (see page 90 and 96, respectively). The impacts for the Group and its customers are being continuously assessed, taking into consideration measures implemented by the Bank of England and the UK government designed to support businesses and protect the economy. Due to the level of uncertainty surrounding this unprecedented event, it is challenging to predict the full extent and duration of the implications and the financial effect cannot currently be evaluated with a high degree of certainty. The Group estimates that there could be negative impacts on areas including the Group's loan book (specifically asset quality and ECLs), net interest income, impairments and provisions. The Group considers this a non-adjusting event after the reporting period and no changes have been made to the financial statements.

On 11 March 2020, it was announced in Budget 2020 that the main rate of corporation tax will remain at 19%. The impact of this on the deferred tax asset is an increase of £0.2 million. This constitutes a non-adjusting event after the reporting period and no changes have been made to the financial statements.

There have been no other significant events between 31 December 2019 and the date of approval of the 2019 Annual Report and Accounts that require a change or additional disclosure in the financial statements.

[1] Comparatives for the year ended 31 December 2018 have been restated to reflect amendments to IAS 12 'Income Taxes'. See Note 1.6(b) for details.

Other information

Other information.

Abbreviations

ALCo	Asset and Liability Committee
AT1	Additional Tier 1
bps	Basis point
CCA	Consumer Credit Act
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CET1	Common Equity Tier 1
CGU(s)	Cash generating unit(s)
Code	UK Corporate Governance Code 2018
CRD IV	Capital Requirements Directive IV
D&I	Diversity and inclusion
EAD	Exposure at default
ECL	Expected credit loss
EIR	Effective interest rate
ERMC	Enterprise Risk Management Committee
EU	European Union
FCA	Financial Conduct Authority
FVOCI	Fair value through other comprehensive income
FVTPL	Fair value through profit or loss
GDPR	General Data Protection Regulation
GPC	Group Product Committee
IAS	International Accounting Standards
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
ILAAP	Internal Liquidity Adequacy Assessment Process
ISA	Individual Savings Accounts
Kwh	Kilowatts per hour
LCR	Liquidity coverage ratio
LGD	Loss given default
LIBOR	London Inter-Bank Offered Rate
LTIP	Long-Term Incentive Plan
MI	Management information
MIP	Management Incentive Plan
MREL	Minimum requirements for own funds and eligible liabilities
NSFR	Net stable funding ratio
OPCo	Operations Committee
OTC	Over-the-counter
PD	Probability of default
PRA	Prudential Regulation Authority
RMF	Risk Management Framework
RRP	Recovery Plan and Resolution Pack
SICR	Significant increase in credit risk since initial recognition
SMF	Senior Manager Function
SME(s)	Small and medium enterprise(s)
SONIA	Sterling Overnight Index Average rate
SPPI	Solely payments of principal and interest on the principal amount outstanding
SPV	Special purpose vehicle
TFS	Term Funding Scheme
VAT	Value added tax

'Company' refers to: Shawbrook Group plc
'Group' refers to: the Company and its subsidiaries
'Bank' refers to: Shawbrook Bank Limited
'Shareholder' refers to: Marlin Bidco Limited

Key performance indicators

Certain financial measures disclosed in the Annual Report and Accounts do not have a standardised meaning prescribed by IFRS and may not therefore be comparable to similar measures presented by other issuers. These measures are deemed to be 'alternative performance measures'. Definitions of the Group's key performance indicators are set out below:

Average principal employed	The average of monthly closing loans and advances to customers[1] (net of loss allowance and fair value adjustments for hedged risk) and assets on operating leases included in property, plant and equipment.
Common Equity Tier 1 (CET1) capital ratio	Common Equity Tier 1 capital, divided by, risk-weighted assets.
Cost of risk	Impairment losses on financial assets, divided by, average principal employed.
Cost to income ratio	The sum of administrative expenses and provisions for liabilities and charges, divided by, net operating income.
Gross asset yield	Net operating income less interest expense and similar charges, divided by, average principal employed.
Leverage ratio	Total Tier 1 capital, divided by, total leverage ratio exposure measure. Total leverage ratio exposure measure is total assets excluding derivatives and intangible assets, and adjusted for off-balance sheet items such as pipeline and undrawn collateral, exposure value for derivatives and transitional adjustments[2].
Liability yield	Interest expense and similar charges, divided by, average principal employed.
Liquidity coverage ratio	Liquidity buffer, divided by, total 30-day net cash outflows in a standardised stress scenario.
Loan book	The sum of loans and advances to customers[1] (net of loss allowance and fair value adjustments for hedged risk) and the carrying amount of assets on operating leases included in property, plant and equipment.
Management expenses ratio	The sum of administrative expenses and provisions for liabilities and charges, divided by, average principal employed.
Net interest margin	Net operating income, divided by, average principal employed.
Return on lending assets before tax	Profit before tax, divided by, average principal employed.
Return on tangible equity	Profit after tax (adjusted to deduct distributions made to holders of capital securities), divided by, average tangible equity. Average tangible equity is calculated as, total equity less capital securities and intangible assets at the beginning of the period, plus total equity less capital securities and intangible assets at the end of the period, divided by two.
Risk-weighted assets	A measure of a bank's assets adjusted for their associated risks. Risk weightings are established in accordance with Prudential Regulation Authority rules and are used to assess capital requirements and adequacy under Pillar 1.
Total capital ratio	Total regulatory capital, divided by, risk-weighted assets.
Total Tier 1 capital ratio	Total Tier 1 capital, divided by, risk-weighted assets.
Total capital ratio	Total regulatory capital, divided by, risk-weighted assets.
Total Tier 1 capital ratio	Total Tier 1 capital, divided by, risk-weighted assets.

[1] In the year ended 31 December 2019, for the purpose of this KPI calculation, loans and advances to customers includes loans transferred to assets held for sale, as they are still considered to be part of the Group's overall loan book until derecognised.

[2] Transitional adjustments refer to adjustments for phasing in the impact of IFRS 9 'Financial Instruments' adoption in accordance with EU regulatory transitional arrangements.

Shawbrook Bank

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