Secure Trust Bank Plc

Pillar 3 disclosures for the year ended 31 December 2017

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1. Overview

1.1 Background

The European Union ('EU') implemented the Basel III proposals published in December 2010 through the Capital Requirements Regulation ('CRR') and Capital Requirements Directive (together referred to as 'CRD IV') which came into force on 1 January 2014. This provides consistent capital adequacy standards governing the level of capital that banks must hold to protect their depositors and shareholders and an associated supervisory framework.

The Prudential Regulation Authority ('PRA') is responsible for the implementation of rules and guidance and enforcement within the UK. The rules include disclosure requirements known as 'Pillar 3' which apply to banks and other financial institutions. These are designed to promote market discipline through the disclosure of key information about risk exposures and risk management processes. CRD IV also made changes to rules on corporate governance, including remuneration, and introduced standardised regulatory reporting within the EU.

The Basel framework consists of three pillars:

- **Pillar 1**: Defines the minimum capital requirements that institutions are required to hold for credit, market and operational risks.
- **Pillar 2**: This builds on Pillar 1 and incorporates the Group's own assessment of additional capital resources needed in order to cover specific risks that are not covered by the minimum regulatory capital resources requirement set out under Pillar 1. The amount of any additional capital requirement is also assessed by the PRA during its Supervisory Review and Evaluation Process ('SREP') and is used to determine the overall capital resources required by the Group.
- **Pillar 3**: Aims to improve market discipline by requiring banks to publish information on their principal risks, capital structure and risk management.

1.2 Basis of disclosures

This document sets out the Pillar 3 disclosures for Secure Trust Bank Plc and its subsidiaries (the Group) as at 31 December 2017. These disclosures provide information on the capital requirements and on the management of key risks faced by the Group.

The disclosures have been prepared for Secure Trust Bank Plc. These disclosures cover the Pillar 3 qualitative and quantitative disclosure requirements. Further details on risks are included in the 'Principal Risks and Uncertainties' section within the 2017 Annual Report and Accounts, which can be found in the investor section of the Secure Trust Bank's website (www.securetrustbank.com/investor-information).

The Pillar 3 disclosure requirements have subsequently been enhanced by the Basel Committee on Banking Supervision with revised guidance issued in January 2015 and March 2017. This document reflects the disclosure requirements applicable at 31 December 2017.

1.3 Content of Report

The Pillar 3 report is issued annually in conjunction with the 2017 Annual Report and Accounts. Pillar 3 disclosures are also required to be issued at the half year and at the March and September quarter ends, although these require a reduced level of information.

1.4 Media and location

Pillar 3 disclosures are published on the Secure Trust Bank PLC corporate website (www.securetrustbank.com/investor-information).

1.5 Verification

The Pillar 3 disclosure report is prepared in accordance with a policy describing internal controls and processes around preparation of this document.

These Pillar 3 disclosures have been prepared to explain the basis upon which the Group has prepared and disclosed certain capital requirements and information about the management of certain risks and for no other purpose. They do not constitute any form of financial statement and must not be relied upon in making any judgement on the Group.

1.6 Changes in disclosure requirements

Extensive changes were made to Pillar 3 disclosure at 2016 year end, when the Basel Committee January 2015 guidance was implemented. Further significant changes have been implemented in this report through the implementation of the Basel Committee March 2017 guidance. These include a restructuring of the report, such that the location of certain content has changed, and the introduction of new requirements as follows:

- Overview of risk management key prudential metrics & RWA (section 2), amended requirements
- Composition of capital and TLAC (section 4), amended requirements
- Disclosure of the leverage ratio (section 6), this is a new requirement
- Liquidity management (section 7), this is a new requirement. In addition, disclosure of the Net Stable Funding Ratio (NSFR) is required from June 2018
- Interest Rate Risk in the Banking Book (IRRBB), amended requirements
- Remuneration (section 13), significantly enhanced disclosure.

2. Overview of Risk Management Key Prudential Metrics and RWA

2.1 Risk Overview

The Board has assessed that the principal risks that are inherent in the Group's business, and could impact on its business model, financial performance and future prospects, are as follows:

Risk	Description
Credit Risk	The risk that a counterparty will be unable to pay amounts in full when due. Counterparties include customers who are lent to on both a secured and unsecured basis as well as the market counterparties with whom the Group deals.
Liquidity Risk	The risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset at a particular time.
Operational Risk	The risk that the Group may be exposed to direct or indirect loss arising from a wide variety of causes associated with the Group's processes, personnel, technology and infrastructure, and from external factors other than the risks identified above. The scope of Operational Risk is broad and includes Business Process, Business Continuity, Financial Crime, Change, Human Resources, Information Security and Risk in addition to the risks from third parties.
Capital Risk	The risk that the Group will have insufficient capital resources to meet the minimum regulatory requirements and to support the business.
Market Risk	The risk that the value of, or revenue generated from, the Group's assets and liabilities is impacted as a result of adverse market movements, predominately interest rates. When interest rates change the present value and timing of future cash flows change. This in turn affects the underlying value of the Groups assets, liabilities and off balance sheet instruments as well as altering interest sensitive elements of income and expenditure.
Conduct Risk	The Group defines Conduct Risk as the risk that the Group's products and services, and the way that they are delivered, result in poor outcomes for customers or harm to the Group. This could be as a result of poor or inappropriate execution of the Group's business activities or staff behaviour.

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

Please see the 'principal risks and uncertainties' section of the 2017 Annual Report and Accounts for further information regarding key risks.

2.2 Key Metrics (at consolidated group level)

		a	b	c	d	e
		31-Dec-17	30-Sep-17	30-Jun-17	31-Mar-17	31-Dec-16
		£'m	£'m	£'m	£'m	£'m
	Available capital (amounts)					
1	Common Equity Tier 1 (CET1)	238.9	214.9	218.5	226.7	227.4
1a	Fully loaded ECL accounting model CET1	-	-	-	-	-
2	Tier 1 capital	238.9	214.9	218.5	226.7	227.4
2a	Fully loaded ECL accounting model Tier 1	-	-	-	-	-
3	Total capital	243.3	220.2	223.8	232.0	232.7
3a	Fully loaded ECL accounting model total capital	-	-	-	-	-
	Risk weighted assets (amount)					
4	Total risk weighted assets (RWA)	1,446.1	1,423.5	1,426.6	1,306.4	1,264.0
	Risk based capital ratios as a percentage of RWA					
5	Common Equity Tier 1 (CET1) ratio (%)	16.5%	15.1%	15.3%	17.4%	18.0%
5a	Fully loaded ECL accounting model CET1 (%)	-	-	-	-	-
6	Tier 1 ratio (%)	16.5%	15.1%	15.3%	17.4%	18.0%
6a	Fully loaded ECL accounting model Tier 1 ratio (%)	-	-	-	-	-
7	Total capital ratio (%)	16.8%	15.5%	15.7%	17.8%	18.4%
7a	Fully loaded ECL accounting model total capital ratio (%)	-	-	-	-	-
	Additional CET1 buffer requirements as a percentage of RWA					
8	Capital conservation buffer requirement (2.5% from 2019) (%)	1.3%	1.3%	1.3%	1.3%	0.6%
9	Countercyclical buffer requirement (%)	0.0%	0.0%	0.0%	0.0%	0.0%
10	Bank G-SIB and/or D-SIB additional requirements (%)	0.0%	0.0%	0.0%	0.0%	0.0%
11	Total of bank CET1 specific buffer requirements (rows 8-10) (%)	1.3%	1.3%	1.3%	1.3%	0.6%
12	CET1 available after meeting the bank's specific buffer requirements (%)	15.3%	13.8%	14.1%	16.1%	17.4%
	Basel III leverage ratio					
13	Total Basel III leverage ratio exposure measure	1,942.7	1,911.8	1,724.9	1,624.7	1,563.9
14	Basel III leverage ratio (%) (row 2/row 13)	12.3%	11.2%	12.7%	14.0%	14.5%
14a	Fully loaded ECL accounting model Basel III leverage ratio (%) (row 2a/row 13)	-	-	-	-	-
	Liquidity Coverage Ratio					
15	Total HQLA	218.7	225.6	114.0	132.7	131.9
16	Total net cash outflow	29.7	26.7	25.4	26.3	17.6
17	LCR ratio (%)	736.4%	845.1%	448.7%	504.3%	751.8%

Total Risk Exposure (TRE) has been reported in row 4 rather than Risk Weighted Assets (RWA). TRE represents RWA plus the Operational Risk component. Disclosure of capital ratios based on TRE is consistent with the basis used in the 2017 Annual Report and Accounts and other regulatory returns and is thus considered more meaningful.

The significant increase in High Quality Liquid Assets (HQLA) and the Liquidity Coverage Ratio from Q3 2017 principally relates to new borrowing from the Bank of England under the Term Funding Scheme. Initially these additional funds have been held in the Group's Bank of England reserve account, which forms the principal component of HQLA.

The 'fully loaded ECL accounting model' lines are intended to disclose the impact of following the transitional rules available in respect of IFRS 9. The Group has notified the PRA that it wishes to adopt these transitional rules from 2018. For 2017 and prior these lines have not been populated as the transitional rules do not apply to these periods.

2.3 Risk Appetite

The Group's sets a high level risk appetite statement to confirm the risk parameters within which the strategic aims and vision of the Group are to be achieved. The Board has identified risk themes, risk drivers and major risk categories relevant to the business to enable it to produce the following risk appetite statements which underpin the strategy of the Group:

Key theme	Risk appetite statement	Risk categories
Profitability	The Group is profit and growth orientated whilst seeking to maintain a conservative and controlled risk profile. The Group manages credit risk through a pricing for risk model, which drives a potential post tax return on equity in excess of 20% in aggregate.	Market risk Credit risk
Financial strength	The Group's financial strength is safeguarded by a strong capital base and a prudent approach to liquidity management. The Group's governance and capital planning processes and procedures are designed to ensure that capital levels will not fall below the Group's individual capital guidance requirements. Liquidity is maintained at a level above the overall liquidity adequacy rule with the majority of loans funded typically by retail deposits.	Credit risk Liquidity risk Capital risk
Conduct with customers and reputation	The Group conducts its business in a way that seeks to avoid negative outcomes for customers by consistently treating them fairly. The Group is straightforward and fair with its customers and seeks to achieve excellent customer service standards. The Group's aim is to be seen as a sound and professional business in the marketplace. It has no appetite for reputational risk arising from the way in which it or its partners behave. It seeks to remain fully compliant with all relevant regulatory requirements.	Conduct risk
Business processes and people	The appetite of the Group for operational risk is to have well defined, scalable and controlled processes, running on robust and resilient systems, effective delivery of change and business continuity management. STB has a low tolerance for Operational losses but understands that losses may occur in the pursuit of its Business objectives.	Operational risk Regulatory risk

The Group's risk appetite statements are subject to regular monitoring and review. Please see the risk appetite statement within the 'risk management' section of the 2017 Annual Report and Accounts for further information.

The Board has set a requirement that the Group is able to withstand a severe but plausible stress scenario without breaching minimum capital requirements.

2.4 The Risk Management Framework

The Group's risk management framework supports decision-making across the Group and is designed to ensure that each risk is managed, monitored and overseen through a dedicated risk-specific committee. The Group operates a "Three Lines of Defence" model for the management of its risks in which each risk has a defined risk appetite which is controlled and managed through documented policies and frequent reporting, and is overseen by one or more committees as part of the Group's governance process.

The Group's risk management framework is summarised in the table below, which sets out for each risk the relevant policy governing the risk, the method of reporting and the responsible committee(s).

Risk	Credit	Market	Liquidity	Operational	Capital	Conduct	Regulatory
Key control documents	Consumer Credit Risk Policy Business and Commercial Credit Risk Policy	Treasury Policy and ILAAP	Treasury Policy and ILAAP	Operational Risk Policy and Framework	ICAAP	Conduct Risk Policy	Compliance Manual
Reporting	Credit Risk Reports	ALCO and Treasury Reports	ALCO and Treasury Reports	Operational Risk MI and Reporting	ICAAP and Other Capital Reports	Conduct Risk MI and Reporting	Compliance Reports
Monitoring committee	Consumer Credit Risk Committee SME Credit Committee	ALCO	ALCO	Group and Business Level Operational Risk Committees	ALCO	Customer Focus Committee	Group Compliance and Regulatory Risk Committee
Oversight committee	Risk Committee	Risk Committee	Risk Committee	Risk Committee	Risk Committee	Risk Committee	Risk Committee

Further details of these risks will be found in the ‘risk management’ section of the 2017 annual report and accounts.

Risk Governance

The Group operates a three lines of defence model for risk management:

- The first line of defence is through business line managers and risk owners, who manage risks by maintaining appropriate systems and controls in order to identify, assess, control and mitigate operational risks as encountered.
- The second line of defence comprises the risk management functions, which provide business support, governance, reporting and oversight for all significant categories of risk. It enables the Group to adopt a common strategy and approach to operational risk management and set Group-wide policies and designs an operational risk management framework that helps businesses to control risks and that provides consistent insight into the risk profile.
- Internal Audit forms the third line of defence and provides the Audit Committee and senior management with comprehensive, independent and objective assurance on the effectiveness of risk governance, risk management and internal controls in the first and second lines of defence, and reports significant risk exposures and control issues to the Audit Committee.

2.5 Risk Oversight, Monitoring and Reporting

The Group has a Chief Risk Officer (CRO) who is responsible for ensuring that each risk is identified, monitored and mitigated. Through the Risk function, the CRO is responsible for providing assurance to the Board and the Directors that the principal risks are appropriately managed and that the Group is operating within defined risk appetites.

The monitoring and control of risk is a fundamental part of the management process within the Group, involving the Board, Risk Committee and Audit Committee. The following committees also form a key part of the Group’s risk management governance structure:

Assets and Liabilities Committee (ALCO)
The Assets and Liabilities Committee is a sub-committee of the Risk Committee and is responsible for implementing and controlling the liquidity funding and asset and liability management risk appetite of the Group, ensuring the high level control over the Group's balance sheet and associated risks. The committee meets monthly to set and control capital deployment, treasury strategy guidelines and limits focusing on the effects of the future plans and strategy on the Group's assets and liabilities.

Consumer Credit Risk Committee
This committee meets monthly to ensure that there is control of credit and lending decisions and related risks. Consumer Mortgages, Retail, Motor and Personal Lending loans are reviewed in alternate months to ensure a detailed analysis is undertaken of the entire portfolio. This committee determines whether the credit strategies and risk polices are working and will make recommendations on any changes required.

SME Credit Committees
The Group operates a Credit Committee structure for its Business Finance division with lending authorities approved at the Board Risk Committee. There is no local sales authority with all deals going via the respective Credit Risk functions for manual underwriting and where required under the mandate approval at the STB Credit Committee level.

Group Operational Risk Committee
The committee meets quarterly to review and monitor the adequacy, implementation and the level of embeddedness of the operational risk management framework across the Group. It recommends and undertakes improvements where required. The committee assesses the operational risks across the Group and recommends, initiates and monitors any further mitigating action required.

Group Compliance and Regulatory Risk Committee
This committee meets quarterly to review and monitor regulatory change with which the Group is required to comply and it provides oversight that appropriate co-ordinated and controlled action is taken to deliver the required changes to an acceptable standard, which achieves compliance in a timely manner. This committee also reviews and approves the compliance risk management framework, the compliance universe and annual monitoring plan, anti-money laundering and financial crime systems of governance and control. It ensures that the Compliance function offers close and continual support to the first line of defence in understanding regulatory requirements and delivery of required outcomes.

Customer Focus Committee
This committee reviews and challenges the customer experience delivered by the Group, ensuring that treating customers fairly principles, conduct risk and customer service excellence requirements are met and good customer outcomes are achieved.

Information Security Management Committee
The committee meets quarterly to oversee the Group's management of information, including safeguarding the personal information of its customers. The committee is also responsible for monitoring cyber security risk.

2.6 Qualitative Information on Stress Testing

The Group performs stress testing as a key tool to understand and manage the impact of risks crystallising. As well as providing an understanding of resistance to internal and external shocks, stress testing forms a key component of the Group's capital and liquidity assessments.

The stress testing performed is designed to:

- Provide sufficiently severe and forward looking scenarios
- Confirm that the Group has sufficient capital and liquidity resources
- Ensure that the Group remains within its risk appetite
- To ensure alignment between the risk management framework and decision making

ICAAP
The Internal Capital Adequacy Assessment Process (ICAAP) is the Group's evaluation of its capital position and requirements, assessed under the Capital Requirements Regulation and Capital Requirements Directive (CRD IV) framework. The ICAAP provides details of the current approaches used to manage risk across the Group. As part of that assessment, the ICAAP has to assess capital requirements both against the Group's current position and during severe but plausible stresses over the planning horizon.

The Group assesses its capital requirements both on a stressed scenario specified by the regulator and a second scenario overlaid with a range of more severe stresses. The stresses used reflect both low and high Bank of England Base Rate scenarios.

ILAAP
The Internal Liquidity Adequacy Assessment Process (ILAAP) is the Group's documentation of its liquidity position and funding requirements, assessed against regulatory requirements and the Group's internal risk tolerance. An integral component of the approach to liquidity risk management is stress testing, some of which is prescriptive using very detailed rules and guidance issued within prudential regulations and reported within regulatory returns.

Reverse stress testing
Reverse stress testing is integrated into existing stress testing within the ICAAP and ILAAP processes, but goes beyond standard tests by considering any extreme event that has the capacity to 'break' the Group. As such it helps to identify risks and possible controls which might ordinarily be missed when using standardised risk assessments.

A key outcome from the process is to consider whether any of the scenarios are sufficiently plausible to necessitate a change to the Group's strategy or underlying controls.

Recovery plan

The Recovery Plan aims to improve the financial resilience of the Group by describing and evaluating the recovery options available to recover from a significant financial event. The PRA expects the Recovery Plan to be consistent with the ICAAP and ILAAP. The stress scenarios are employed to test the Recovery Plan should be aligned with the stress testing utilised in the ICAAP and ILAAP processes.

2.7 Overview of Risk Weighted Assets

		a	b	c	d
		Risk Weighted Assets		Minimum Capital Requirement	
		31/12/17 £'m	31/12/16 £'m	**31/12/17 £'m**	31/12/16 £'m
1	Credit Risk (excluding counterparty credit risk) CCR	**1,278.6**	1,137.0	**102.3**	91.0
2	Of which standardised approach (SA)	**1,278.6**	1,137.0	**102.3**	91.0
3	Of which internal rating-based approach (IRB)	**-**	-	**-**	-
4	Counterparty credit risk	**-**	-	**-**	-
5	Of which standardised approach for counterparty credit risk (SA-CCR)			**-**	-
6	Of which internal model method (IMM)	**-**	-	**-**	-
7	Equity positions in banking book under market based approach	**-**	-	**-**	-
8	Equity investments in funds - look through approach	**-**	-	**-**	-
9	Equity investments in funds - mandate-based approach	**-**	-	**-**	-
10	Equity investments in funds - fall-back approach	**-**	-	**-**	-
11	Settlement risk	**-**	-	**-**	-
12	Securitisation exposures in banking book	**-**	-	**-**	-
13	Of which IRB ratings-based approach (RBA)	**-**	-	**-**	-
14	Of which IRB supervisory formula approach (SFA)	**-**	-	**-**	-
15	Of which SA/simplified supervisory formula approach (SSFA)	**-**	-	**-**	-
16	Market risk	**-**	-	**-**	-
17	Of which standardised approach (SA)	**-**	-	**-**	-
18	Of which internal model approaches (IMM)	**-**	-	**-**	-
19	Operational risk	**167.5**	127.0	**13.4**	10.2
20	Of which Basic Indicator Approach	**167.5**	127.0	**13.4**	10.2
21	Of which Standardised Approach	**-**	-	**-**	-
22	Of which Advanced Measurement Approach	**-**	-	**-**	-
23	Amounts below the threshold for deduction (subject to 250% risk weight)	**-**	-	**-**	-
24	Floor adjustment	**-**	-	**-**	-
25	Total (1+4+7+8+9+10+11+12+16+19+23+24)	**1,446.1**	1,264.0	**115.7**	101.1

The minimum capital requirement above represents the Group's Pillar 1 capital requirement and excludes any additional Pillar 2A capital add-ons.

The credit risk RWA has increased by 12%, in comparison to the 25% increase in total assets in the year, from £1,510m to £1,892m. 8% of the overall increase in total assets is attributable to higher levels of sovereign assets which are risk weighted at 0% with the remainder accounted for by a change in business mix towards lower weighted exposures.

The operational risk capital requirement has increased by 31% in the period, from £10.2m to £13.4m, due to the annual recalculation under the basic indicator approach, following approval of the annual accounts for the previous year. The 2017 calculation is based on a weighted average of eligible income in the years 2014 to 2016 inclusive, whereas the 2016 calculation was based on 2013 to 2015 inclusive. The increase in capital requirement is therefore indicative of the rate of growth of the business in recent years.

3 Linkages between financial statements and regulatory exposures

3.1 Differences between accounting and regulatory scopes of consolidation and mapping of financial statement risk categories with regulatory risk categories

	a	b	c	d	e	f	g
	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	Carrying values of items:				
			Subject to credit risk framework	Subject to counterparty credit risk framework	Subject to the securitisation framework	Subject to the market risk framework	Not subject to capital requirements or subject to deduction from capital
	£'m	£'m	£'m	£'m	£'m	£'m	£'m
Assets							
Cash and balances at central banks	226.1	226.1	226.1	-	-	-	-
Loans and advances to banks	34.3	34.3	-	34.3	-	-	-
Loans and advances to customers	1,598.3	1,598.3	1,598.3	-	-	-	-
Debt securities held to maturity	5.0	5.0	5.0	-	-	-	-
Equity instruments available for sale	-	-	-	-		-	-
Property, plant and equipment	11.5	11.5	11.5	-	-	-	-
Intangible assets	10.4	10.4	-	-	-	-	10.4
Deferred tax assets	0.6	0.6	0.6	-	-	-	-
Other assets	5.4	5.4	5.4	-	-	-	-
Total assets	**1,891.6**	**1,891.6**	**1,846.9**	**34.3**	**-**	**-**	**10.4**
Liabilities							
Due to banks	113.0	113.0	113.0	-	-	-	-
Deposits from customers	1,483.2	1,483.2	1,483.2	-	-	-	-
Current tax liabilities	3.0	3.0	3.0	-	-	-	-
Deferred tax liabilities	-	-	-				-
Other liabilities	41.9	41.9	41.9	-	-	-	-
Provisions for liabilities and charges	1.4	1.4	1.4	-	-	-	-
Total liabilities	**1,642.5**	**1,642.5**	**1,642.5**	**-**	**-**	**-**	**-**

3.2 Main sources of differences between regulatory exposure amounts and carrying values in financial statements

		a	b	c	d	e
			Items subject to:			
		Total	Credit risk framework	Counterparty credit risk framework	Securitisation framework	Market risk framework
		£'m	£'m	£'m	£'m	£'m
1	**Asset carrying value under scope of regulatory consolidation (as per template LI1)**	**1,891.6**	**1,846.9**	**34.3**	**-**	**-**
2	Liabilities carying amount under regulatory scope of consolidation (as per template LI1)	1,642.5	1,642.5	-	-	-
3	Total net amount under regulatory scope of consolidation	249.1	204.4	34.3	-	-
4	Off balance sheet amounts	177.9	177.9	-	-	-
5	Differences in valuations	-	-	-	-	-
6	Differences due to different netting rules, other than those already included in row 2	-	-	-	-	-
7	Differences due to consideration of provisions	-	-	-	-	-
8	Differences due to prudential filters	-	-	-	-	-
9						
10	**Exposure amounts considered for regulatory reporting purposes**	**2,069.5**	**2,024.8**	**34.3**	**-**	**-**

Explanation of differences between accounting and regulatory exposure amounts

There are no differences between the reported carrying values within the financial statements and the regulatory balances as reported in the Group's financial regulatory returns (section 3.1).

The difference between the Group's net carrying value per table LI1 of £1,891.6m and the regulatory reporting exposure amount of £2,069.5m (section 3.2) is represented by off balance sheet commitments of £177.9m. These off balance sheet commitments represent agreed loan facilities which remain undrawn at the balance sheet date.

Where financial assets are individually evaluated for impairment, management uses their best estimates in calculating the net present value of future cash flows. Management has to make judgements on the financial position of the counterparty and the net realisable value of collateral (where held), in determining the expected future cash flows.

4 Composition of Capital and Total Loss Absorbing Capital

4.1 Composition of regulatory capital

The table below summarises the composition of The Group's regulatory capital as at 31 December 2017:

	31/12/17 £'m	31/12/16 £'m
Tier 1		
Share capital	7.4	7.4
Share premium	81.2	81.2
Retained earnings	159.2	149.0
Other reserves and adjustments	(8.9)	(10.2)
Common Equity Tier 1 capital	**238.9**	**227.4**
Tier 2		
Collective allowance for impairment of loans and advances	4.4	5.3
Total Tier 2 capital	**4.4**	**5.3**
Total Tier 1 & Tier 2 capital	**243.3**	**232.7**

The Group's Total Loss Absorbing Capacity (TLAC) at 31 December 2017 is equal to its minimum capital requirement (Pillar 1+2A capital). The Group is not required by the PRA to hold a MREL recapitalisation reserve.

4.2 Management of Capital

In order to protect the capital adequacy of the Group, internal capital is held to provide a cushion for unexpected losses. In assessing the adequacy of its capital, the Group considers its risk appetite, the material risks to which the Group is exposed and the appropriate management strategies for each of the Group's material risks, including whether or not capital provides an appropriate mitigant.

The Internal Capital Adequacy Assessment Process (ICAAP) is a key element of the Group's implementation of the EU Capital Requirements Directive (CRD). It is a process that brings together the risk management framework of the Group and the financial discipline of budgeting and business planning.

The ICAAP is reviewed and updated each year in conjunction with the annual budget process, unless there are any changes in the control environment or other events that warrant a more immediate update. When performing the annual update the Board will review the continued appropriateness of the stated risk appetite and compare it against actual performance. It will also request the performance of stress testing, to assess the Group's capital adequacy in a range of scenarios.

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

The Board has adopted the PRA Pillar 2A capital guidance methodology to determine the level of capital that needs to be held. This method takes the Pillar 1 capital formula calculations (for credit, market and operational risk) as a starting point and then considers whether each of these calculations delivers an adequate capital sum to cover all anticipated risks. Where the PRA and Board consider that the Pillar 1 calculations do not adequately reflect the risks, additional Pillar 2A capital is held.

4.3 Capital Requirement

The following table shows the Group's Pillar 1 capital requirements by asset class (credit risk requirements represent gross exposures and exposures after credit risk mitigation):

Pillar 1 Requirement	2017	2016
Credit Risk requirements arising from exposures to:	£'m	£'m
Institutions	0.6	0.3
Corporates	14.0	12.2
Retail	44.8	38.9
Secured on immoveable property	39.5	35.9
Exposures in default	1.9	1.2
Other	1.5	2.5
Market risk capital requirement	-	-
Operational risk capital requirement	13.4	10.1
Total Pillar 1 Capital Requirement	**115.7**	**101.1**

The retail capital requirement has increased by 15% in the year due to strong growth in the motor (+16%) and retail finance channels (+40%). However this is partially offset by the sale of the Personal Lending portfolio during the year, which was valued at £65m at the end of 2016.

The capital requirement for property lending increased by 10% despite overall real estate finance lending increasing by 28%, from £451m to £581m. Within this there was a reduction in the proportion of development lending, which attracts a 150% risk weighting, and greater levels of residential investment lending, which is weighted at 35%. In addition the consumer mortgage business launched in late 2017 with lending of £16m by year end, which was generally risk weighted at 35%.

Operational risk is the risk to achieving the Group's strategy or objectives as a result of inadequate or failed internal processes, people and systems or from external factors. These can relate to breaches of law and regulations, error or omission, unauthorised activities and fraud, system failure or external events.

CRD IV requires that the Group holds Pillar 1 capital against operational risk. The amount of capital the Group is required to hold is determined by the Basic Indicator Approach. This is calculated as 15% of the average of the last three years' eligible income.

The table below sets out the Group's operational risk capital BIA indicator calculation for the 2017 year:

Eligible Income for Year Ending			**BIA Indicator £'000**
2014 £'000	2015 £'000	2016 £'000	
60,106	90,968	116,987	***167,538***

The capital requirement is then set at 8% of the BIA indicator, equating to £13.4m (2016: £10.1m). The reason for the year on year increase is explained in section 2.7 above.

5 Macro-prudential Supervisory Measures

5.1 Geographical distribution of the credit exposures used in the countercyclical capital buffer

The countercyclical capital buffer (CCyB) rate applicable in the United Kingdom at 31 December 2017 was 0%. As a result disclosure of the geographic distribution of credit exposures is not required.

A CCyB buffer is required from June 2018; the underlying credit exposures are expected to arise solely in the UK.

6 Leverage Ratio

CRD IV introduces a non-risk based leverage ratio that is supplementary to the risk based capital requirements. The calculation determines a ratio based on the relationship between Tier 1 capital and total exposures, including off- balance sheet items. The leverage ratio does not distinguish between unsecured and secured loans, nor recognise the ratio of loan to value of secured lending.

The PRA has implemented the Financial Policy Committee's (FPC) direction to introduce a UK leverage ratio framework. This currently only applies to banks and building societies with retail deposits of £50 billion or more and on this basis the Group is not captured by this requirement.

The UK leverage ratio framework sets a minimum ratio of 3.25% from December 2017, previously 3%. Although not subject to the framework, the Group follows the requirements as best practice and has maintained its ratio well in excess of the minimum requirement.

6.1 Summary comparison of accounting assets vs leverage ratio exposures

		2017 £m
1	Total consolidated assets per published financial statements	1,891.6
2	Adjustments for investments in banking, financial, insurance or commercial entities that are conslidated for accounting purposes but outside the scope of regulatory consolidation	-
3	Adjustment for fiduciary assets recognised on the balance sheet pursuant to the operative accounting framework but excluded from the leverage ratio exposure measure	-
4	Adjustments for derivative financial instruments	-
5	Adjustments for securities financing transactions (repos and similar secured lending)	-
6	Adjustments for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	51.1
7	Other adjustments	-
8	**Leverage ratio exposure measure**	**1,942.7**

6.2 Leverage ratio common disclosure template

		31 Dec 2017 £m	30 Sept 2017 £m
	On balance sheet exposures		
1	On balance sheet exposures (excluding derivatives and securities financing transactions (SFTs), but including collateral)	1,891.6	1,850.5
2	(Asset amounts deducted in determining Basel III Tier 1 capital)		-
3	**Total on balance sheet exposures** (excluding derivatives and SFTs) , (sum of rows 1 & 2)	**1,891.6**	**1,850.5**
	Derivative exposures		
4	Replacement cost associated with all derivatives transactions (where applicable net of eligible cash variation margin and/or with bilateral netting)	-	-
5	Add on amounts for PFE associated with all derivatives transactions	-	-
6	Gross up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the operative accounting framework	-	-
7	(Deductions of receivables asset for cash variation margin provided in derivatives transactions)	-	-
8	(Exempted CCP leg of client-cleared trade exposures)	-	-
9	Adjusted effective notional amount of written credit derivatives	-	-
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)	-	-
11	**Total derivative exposures** (sum of rows 4 to 10)	**-**	**-**
	Securities financing transaction exposures		
12	Gross SFT assets (with no recognition of netting), after adjusting for sale accounting transactions	-	-
13	(Netted amounts of cash payable and cash receivables of gross SFT assets)	-	-
14	CCR exposure for SFT assets	-	-
15	Agent transaction exposures	-	-
16	**Total securities financing transaction exposures** (sum of rows 12 to 15)	-	-
	Other off-balance sheet exposures		
17	Off-balance sheet exposure at gross notional amount	177.9	192.3
18	(Adjustments for conversion to credit equivalent amounts)	- 126.8	- 131.0
19	**Off-balance sheet items (sum of rows 17 and 18)**	**51.1**	**61.3**
	Capital and total exposure		
20	**Tier 1 capital**	**238.9**	**214.9**
21	**Total exposures (sum of rows 3, 11, 16 and 19)**	**1,942.7**	**1,911.8**
	Leverage Ratio		
22	**Basel III leverage ratio**	**12.3%**	**11.2%**

The principal reason for the increase in leverage ratio between September and December 2017 is attributable to the certification of 2017 profits into CET1 Capital at December.

7 Liquidity

The table below describes our governance in respect of key liquidity risks and describes the mitigation in place:

7.1 Liquidity Risk Management

a) Governance of liquidity risk management	Description	Mitigation
i) Risk tolerance	The Group's Board has agreed a liquidity risk appetite to ensure that adequate liquidity resources are held to meet its Overall Liquidity Adequacy Requirement (OLAR) and to meet the minimum Liquidity Coverage Ratio (LCR). The Group assesses and formally demonstrates the adequacy of its liquidity through the Internal Liquidity Adequacy Assessment Process (ILAAP). As part of the ILAAP, the Group conducts regular and comprehensive liquidity stress testing to ensure compliance with OLAR.	The liquidity requirements of the Group are mainly met by maintaining funds in its Bank of England reserve account to cover any short-term net outflow requirements. Longer term funding is also in place for structural liquidity and funding requirements. The Group is required to meet daily cash flow requirements arising from maturing deposits and loan draw-downs, and maintains significant cash resources to meet all of these needs as they fall due.
ii) Structure and responsibilities for liquidity risk management	The Group has a formal governance structure in place to manage and mitigate liquidity risk on a day to day basis. The Board sets and approves the Group's liquidity risk management strategy. The ALCO, comprising senior management and executives of the Group, meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and ILAAP metrics that is managed on a day-to-day basis by the Group's treasury function.	The Group's Chief Risk Officer is responsible for leading the Group's Risk Function, which is independent from the Group's operational and commercial functions. The Risk Function is responsible for ensuring that appropriate risk management processes and controls are in place, and that they are sufficiently robust, so as to ensure that key risks are identified, assessed, monitored and mitigated. The Chief Risk Officer is responsible for providing assurance to the Board that the Group's principal risks are appropriately managed and that it is operating within its risk appetite.

iii) Internal liquidity reporting	Liquidity metrics are monitored daily through daily liquidity reporting and monthly through ALCO. Metrics are also included in the Monthly Information pack tabled at the Group's Executive Committee (Exco) and the Board.	The primary measure used by management to assess the adequacy of liquidity is the Overall Liquidity Adequacy Requirement (OLAR), which is the Board's own view of the Group's liquidity needs as set out in the Board approved ILAAP. The Group maintained liquidity in excess of its required OLAR through the year.
iv) Communication of liquidity risk strategy, policies and practices across business lines and with the board of directors	The Group's ALCO is responsible for implementing and controlling the liquidity risk appetite established by the Board. ALCO monitors compliance with the Group's policies and oversees the overall strategy, guidelines and limits so that the Group's future plans and strategy can be achieved within risk appetite.	The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, and can fund its assets at reasonable cost and without incurring unacceptable losses or risking damage to the Group's reputation through a failure to meet its obligations.
b) Funding strategy, including policies on diversification in the sources and tenor of funding, and whether the funding strategy is centralised or decentralised	The Group 's funding risk appetite is to ensure that the Group has access to stable funding markets and is not reliant on any single source of funding. The Group is mainly funded by capital and customer deposits. The Group also has limited borrowings under Bank of England funding schemes but does not have other direct exposures to wholesale markets. The Group's funding strategy is managed centrally.	The Group maintains at all times liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. The Group maintains a buffer of unencumbered High Quality Liquid Assets (HQLA) that is available to meet its liquidity requirements.
c) Liquidity risk mitigation techniques	The Group seeks to mitigate liquidity risk through a number of strategies and processes: • The diversification of its deposit and loan products; • Offering depositors competitive interest rates to reduce churn and volatility; • Contractual repayment term matching of a monitored proportion of its loan and deposit book; • Acquiring funding through lower value, higher volume deposits; • Monthly ALCO meetings reviewing early warning indicators and tolerances of all relevant balance sheet items;	The Group's liquidity risk appetite is to ensure that adequate liquidity resources are held to withstand all known reasonable combinations of idiosyncratic and market risks for up to 60 days. The aim is not to measure liquidity with a single metric but rather a range of principles and metrics which, when taken together, helps ensure that the Company's liquidity risk is maintained at an acceptable level.

	• Access to Bank of England liquidity schemes; • Holding adequate levels of high quality liquid assets with a high proportion of cash in the Group's Bank of England Reserve Account.	
d) An explanation how stress testing is used	The key risk drivers identified in the Group's Individual Liquidity Adequacy Process as being applicable to the Group are Retail Funding, Intraday Liquidity Risk and Pipeline Risk. The Group uses various short and medium term forecasts to monitor future liquidity requirements and these include stress testing assumptions to identify the required levels of liquidity. Stress testing is typically performed on a daily basis and forecasted levels of liquidity under stress are forecast regularly and monitored by ALCO.	An integral component of the approach to liquidity risk management is stress testing, some of which is prescriptive using very detailed rules and guidance issued within prudential regulations and reported within regulatory returns. In addition to the regulatory prescribed stress testing, the Group undertakes its own stress tests. The Board sets limits against both regulatory and internal stress testing requirements.
e) An outline of the Group's contingency funding plans	If for reasons which may be beyond the business' control, the Group was to encounter a significant and sustained outflow of deposits or other stress on the Group's liquidity resource, a Liquidity Contingency Plan (LCP) is maintained to ensure the Group is able to maintain sufficiently liquid to remain a viable independent financial institution following a severe liquidity stress event. The integration of the LCP to the RRP, ILAAP and ICAAP is achieved through the use of consistent EWI's and invocation trigger points (ITP) that are regularly monitored and reported against.	The Liquidity Contingency Plan (LCP) forms part of the Group's risk management framework, linking the Group's Internal Liquidity Adequacy Assessment Process (ILAAP) to the Recovery and Resolution Plan (RRP) on a consistent basis.

The Overall Liquidity Adequacy Requirement (OLAR) ratio is the key metric used to monitor future cash flow and liquidity forecasts. This relates the projected 60 day liquidity position to holdings of High Quality Liquid Assets (HQLA). This is reported to the Assets and Liability Committee monthly. The OLAR ratio is calculated as the HQLA / 60 day liquidity surplus and is maintained in excess of 110%. At 31 December 2017 the OLAR was well in excess of the required minimum at 147.6% (2016: 191.7%).

The measures in place to manage liquidity risk on sources of funding are described in note 31 of the 2017 Annual Report and Accounts. The loan to deposit ratio and total funding ratio are calculated and monitored as described in section (iv) of the appendix to the 2017 Annual Report and Accounts,

Details of the maturity profiles and liquidity gaps of balance sheet amounts are disclosed in note 31 of the 2017 Annual Report and Accounts.

7.2 Liquidity Coverage Ratio (LCR)

		a	b
		Total unweighted value (average)	**Total weighted value** (average)
		£'m	£'m
High quality liquid assets			
1	Total HQLA		218.7
Cash outflows			
2	**Retail deposits and deposits from small business customers, of which:**	**40.5**	**24.6**
3	Stable deposits	-	-
4	Less stable deposits	40.5	24.6
5	**Unsecured wholesale funding, of which:**	**60.0**	**23.6**
6	Operational deposits (all counterparties) and deposits in networks of cooperative banks	-	-
7	Non-operational deposits (all counterparties)	60.0	23.6
8	Unsecured debt	-	-
9	**Secured wholesale funding**		-
10	**Additional requirements, of which:**	**5.8**	-
11	Outflows related to derivative exposures and other collateral requirements	-	-
12	Outflows related to loss of funding on debt products	-	-
13	Credit and liquidity facilities	-	-
14	**Other contractual funding obligations**	**261.8**	**26.2**
15	**Other contingent funding obligations**	**47.4**	**44.5**
16	**TOTAL CASH OUTFLOWS**	**415.5**	**118.9**
Cash inflows			
17	**Secured lending (e.g. reverse repos)**	**-**	**-**
18	**Inflows from fully performing exposures**	**209.9**	**127.0**
19	Other cash inflows	-	-
20	**TOTAL CASH INFLOWS**	**209.9**	**127.0**
			Total Adjusted Value
21	**Total HQLA**		**218.7**
22	**Total net cash outflows**		**29.7**
23	**Liquidity Coverage Ratio (%)**		**736.4%**

High quality liquid assets principally represent the Group's Bank of England reserve account and treasury bills. The Key Metrics table in section 2.2 shows the movement of the LCR ratio over the last 5 quarters.

The data points used in creating the average figures for the table are the Group's monthly liquidity returns. In calculating the net cash outflow figure (row 22), the cap limiting the allowable cash inflow to 75% of the cash outflow has been applied.

8 Credit Risk

Credit risk is the risk that customers or other counterparties are unable to meet their financial obligations to the Group as they fall due.

General qualitative information about credit risk

8.1 How the business model translates into the components of the Group's credit risk profile

The Group's business model is predominately targeted at loans and advances to customers. The loan books are split into three distinct segments which are Business Finance, Consumer Finance and Consumer Mortgages. Each of these segments is split further into their respective product areas.

Business Finance
For Real Estate Finance and Commercial Finance, lending decisions are made on an individual transaction basis, using expert judgement and assessment against criteria set out in the lending policies. Asset Finance lending is outsourced to Haydock, who operate in line with the Group's credit policies and risk appetite. The Group's employees based in Haydock's premises assess this lending for compliance with policy.

Lending to this segment has continued to grow, with continued application of robust risk governance, credit appetite and lending policies, alongside the significant experience within the lending teams. This has served the Group well to date as it continues to manage the impacts of the 2016 referendum result, particularly in the Central London Real Estate Market, where risk appetite has been substantially reduced.

A programme to develop probability of default modelling for each of the Business Finance portfolios has been completed in conjunction with the IFRS 9 project.

Consumer Finance
For the Retail Finance and Motor Finance products, the Group's Credit Risk appetite is managed by the employment of a bespoke scorecard. All applications are assessed against the scorecard and, in addition to being utilised to determine accepted and declined proposals; it is also the key determinant in the rate for risk model used in the Group. The scorecard is utilised in association with a suite of policy rules that reject applicants that may marginally pass the scorecard, yet the Group has no appetite to write. For example customers who are insolvent, over-indebted, fraudulent or unable to manage their current repayments.

The Group has confidence in the decisions made using the scorecard and policy rules and therefore has a low threshold for exceptions, with overrides not permitted to exceed 0.05% by value each month; for 2017 the actual exception rate was 0.029%. Exposures are managed by maximum individual loan exposures of £20,000 for motor finance and £25,000 for retail finance (with the exception of Artworks lending which has a £38,000 limit).

In 2017, due to concerns about excessively aggressive competitive activities and the potential for risk to be mispriced, STB has initiated a strategic repositioning of its lending portfolio away from higher risk consumer lending. In the last nine months the bank has ceased originating new medium term unsecured personal loans and sub-prime motor finance. It has proportionately increased its new business volumes in secured lending. As capital and other resources are repositioned, this has resulted in slower growth in the consumer segment.

Consumer Mortgages

The Group entered the mortgage sector in Q2 2017 having recruited a senior management team with experience specific to that sector. The Group aims to identify segments of UK consumers who have difficulties securing mortgage lending from the existing market players, or whose options are limited. This includes those who are fundamentally credit worthy but have more complex needs maybe owing to their income / employment profile or to historic minor credit events that have been demonstrably overcome.

Mortgage applications are manually underwritten once they have been passed through a comprehensive suite of credit policy rules and scored using a generic bureau score, Risk Navigator. The Group has a very good understanding of this score, having used it to good effect for other products. It is this complementary blend of credit scoring techniques, rules and manual review that provides the Group with confidence around its mortgage lending. Volumes have been low in 2017, as the Group has taken a conservative and measured approach upon entering the market.

8.2 Criteria and approach used for defining credit risk management policy and for setting credit risk limits

The Secure Trust Bank strategy is to have a balanced lending portfolio that constitutes a mix of consumer finance, residential mortgage lending and commercial finance, comprising asset finance, real estate finance and invoice finance. The composition of the business mix is agreed by the Board. The Board also agrees maximum lending limits in terms of individual loan to customers and concentration risk to any one particular introducer.

8.3 Structure and organisation of the credit risk management and control function

The Group operates a three lines of defence model to credit risk:

Underwriting and Quality Assurance - First Line of Defence Consumer Lending

The Underwriting and Operational Quality Assurance teams are the first line of defence, headed up by the Group Head of Motor Operations, with the V12 Operations Director having first line responsibility for the Retail Finance business. For STB Leasing the first line of defence activities are undertaken by Rentsmart under the outsourcing agreement.

Credit Committee Process - First Line of Defence Business Lending

Responsibility and accountability lies with the line management in the individual SME businesses. Line management are responsible for credit risk strategy and credit risk mitigation for the Group's products, from new acquisition to write off, through portfolio analysis. The Head of Operational Risk facilitates the risk assessment process and regular review of risk registers, which encompass the Credit Risk Department and credit risk within the first line areas of the business. A reporting process is in place to highlight key risk to the Group's senior management and risk committees.

Operational/ Credit Risk - Second Line of Defence

The Operational Risk, Compliance and Credit Risk functions are the second line of defence. Credit Risk is headed up by the Group Heads of Credit Risk (Consumer and Business). Reporting to the Chief Risk Officer, the Group Heads of Credit Risk are responsible for credit strategy and credit risk mitigation for all the Group's lending products from new acquisition to write-off, through portfolio analysis.

The Head of Operational Risk facilitates the risk assessment process and the quarterly review of risk registers, which encompasses the Credit Risk department and credit risks within first line areas of operation. A reporting process exists to highlight key risks to the Group's Senior Management and Risk Committees.

The Compliance department, headed by the Chief Compliance Officer, determines the annual compliance monitoring plan, which is approved by the Group Risk Committee. Key issues identified by compliance monitoring activities are escalated to the Group Exco, the minutes of which are received by the Group Board.

An incident reporting process is also in operation which seeks to proactively identify weaknesses in controls, including credit risk controls, and to ensure that root causes are identified and addressed.

Internal Audit – Third Line of Defence

The Group has an independent internal audit function managed by a Chief Internal Auditor who has right of attendance at the Group ExCo meeting. Credit Risk is audited annually with different elements of Credit Risk reviewed at the specific request of the Group Board Risk Committee.

Relationships between the credit risk management, risk control, compliance and internal audit functions

All Group processes, business units and support functions are in scope for internal audit review. The internal audit plan, which is risk based, covers all significant business processes and enabling functions over a four year period and the plan is updated each year and approved by the Board Audit Committee. Credit risk features in the internal audit plan every year, in both business process reviews (reviewing credit risk management as operated by the underwriting teams and supported by QA at application stage and in-life) and in audits of the effectiveness of the second line of defence functions. Although not every business unit or second line function is covered every year, all are covered over a four year period and the processes or functions that are regarded as highest risk are subject to review more frequently.

8.4 Scope and main content of the reporting on credit risk exposure and on the credit risk management function to the executive management and to the board of directors

A Portfolio review pack is created on a monthly basis to monitor trends in applicant quality and portfolio performance. Metrics are generated to review the effectiveness of the scorecard and designed to identify any deterioration of its discriminatory strength.

Data is scrutinised at application level but furthermore by introducers. Introducer statistics include application volumes, and quality, written rates/ quality and post acceptance the performance of the written loans.

8.5 Credit quality of assets

		a	b	c	d
		Gross carrying values of:		Allowances/ Impairments £'m	Net values (a+b+c) £'m
		Defaulted exposures £'m	Non-defaulted exposures £'m		
1	Loans	44.4	1,593.1	(39.2)	1,598.3
2	Debt Securities	-	-	-	-
3	Off-balance sheet exposures	-	177.9	-	177.9
4	**Total**	**44.4**	**1,771.0**	**(39.2)**	**1,776.2**

8.6 Changes in stock of defaulted loans and debt securities

		2017 £m
1	**Defaulted loans and debt securities at end of the previous period (restated)**	**30.5**
2	Loans and debt securities which have defaulted since the last reporting period	26.9
3	Returned to non-defaulted status	(1.9)
4	Amounts written off	(7.3)
5	Other changes	(3.8)
6	**Defaulted loans and debt securities at end of the reporting period (1+2+3+4+5)**	**44.4**

The Group has changed its policy on the charge-off of debt sold by Secure Trust Bank PLC to Debt Managers (Services) Limited, a wholly owned subsidiary undertaking. A description of this change in accounting policy is set out in note 1.3 of the Group's 2017 Annual Report and Accounts. The table above reflects the restated opening balance with the impact of the change reflected in row 5 'other changes'. Defaulted exposures are defined as loans which are greater than 90 days past due and impaired.

8.7 Additional disclosure related to the credit quality of assets

The Group follows the regulatory definition for past due and impaired exposures for accounting purposes. All exposures greater than 90 days overdue are considered as impaired.

Impairments are calculated based on criteria including the number of months overdue and the likelihood of recovery.

The Group does not restructure accounts.

All lending takes place within the United Kingdom.

8.8 Residual Maturity of Assets

	Within 3 months £'m	3-6 months £'m	6-12 months £'m	After 12 months £'m	**Total £'m**
Cash and balances at central banks	226.1	-	-	-	**226.1**
Loans and advances to banks	34.3	-	-	-	**34.3**
Loans and advances to customers	280.8	131.0	246.4	940.1	**1,598.3**
Debt securities held to maturity	5.0		-	-	**5.0**
Other assets	5.4	-	0.6	21.9	**27.9**
Total	**551.6**	**131.0**	**247.0**	**962.0**	**1,891.6**

Cash and balances at central banks represents balances at the Bank of England. Loans and advances to banks represents loans to other banking institutions. Loans and advances to customers represents: the Business Finance portfolio comprising secured lending to businesses for Real Estate, Asset Finance and Invoice Finance; the Consumer Finance portfolio including unsecured Retail Finance lending in addition to secured lending for Motor Finance; and Consumer Mortgages.

8.9 Ageing analysis of past due exposures by industry sector

	Past due but not impaired (£'m)						Carrying Amount of the impaired assets £'m	Specific allowances for individually assessed financial assets £'m	Specific allowances for collectively assessed financial assets £'m	Accumulated write offs £'m
	Up to 30 days	31 - 60 days	61 - 90 days	91-180 days	181 days - 1 Year	More than 1 Year				
Central banks	-	-	-	-	-	-	-	-	-	-
General governments	-	-	-	-	-	-	-	-	-	-
Credit institutions	-	-	-	-	-	-	-	-	-	-
Other financial corporations	-	-	-	-	-	-	-	-	-	-
Non-financial corporations	2.4	0.3	0.1	-	-	-	0.3	(1.4)	(0.7)	-
Households	22.4	8.4	4.3	-	-	-	18.8	(33.4)	(3.7)	(32.4)
Total	**24.8**	**8.7**	**4.4**	**-**	**-**	**-**	**19.1**	**(34.8)**	**(4.4)**	**(32.4)**

8.10 Qualitative disclosure required related to credit risk mitigation techniques

a. Credit risk mitigation for the unsecured retail business is principally facilitated through use of the bespoke scorecard described in section 8.1 above. This is considered a robust approach as overrides are only allowed by exception and the proportion and absolute value of such exceptions are capped.

b. All commercial business lending is secured at prudent loan to value ratios and therefore is considered adequately mitigated.

8.11 Credit risk mitigation techniques -overview

		a	b	c	d	e	f	g
		Exposures unsecured: carrying amount	Exposures secured by collateral	Exposures secured by collateral, of which: secured amount	Exposures secured by financial guarantees	Exposures secured by financial guarantees, of which: secured amount	Exposures secured by credit derivatives	Exposures secured by credit derivatives, of which: secured amount
		£'m	£'m	£'m	£'m	£'m	£'m	£'m
1	Loans	811.5	1,047.2	886.5	19.1	19.1	-	-
2	Debt Securities	-	-	-	-	-	-	-
3	**Total**	**811.5**	**1,047.2**	**886.5**	**19.1**	**19.1**	**-**	**-**
4	Of which defaulted	12.3	32.1	28.4	-	-	-	-

Unsecured exposures represent exposures to the Retail Finance business and those to the Bank of England and banking institutions. Secured exposures represent the Motor Finance business, Consumer Mortgages and Business Finance portfolios.

8.12 Qualitative disclosure on the banks use of external credit ratings under the standardised approach for credit risk

The Group does not currently make use of external credit ratings in the assessment of credit risk.

8.13 Standardised approach- credit risk exposure and CRM effects

		a	b	c	d	e	f
		Exposures before CCF and CRM		**Exposures post CCF and CRM**		**RWA and RWA density**	
		On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	RWA	RWA density
		£'m	£'m	£'m	£'m	£'m	£'m
	Asset Classes:						
1	Sovereigns and their central banks	231.1	-	231.1	-	-	0%
2	Non central government public sector entities	-	-	-	-	-	-
3	Multilateral development banks	-	-	-	-	-	-
4	Banks	34.3	-	34.3	-	6.9	20%
5	Securities firms	-	-	-	-	-	-
6	Corporates	220.4	15.5	220.4	-	195.7	89%
7	Regulatory retail portfolios	765.1	56.0	747.0	4.1	563.3	75%
8	Secured by residential property	16.9	7.7	16.9	7.7	7.4	30%
9	Secured by commercial real estate	577.2	98.7	577.2	45.5	486.7	78%
10	Equity	-	-	-	-	-	-
11	Past due loans	23.8	-	23.8	-	23.8	100%
12	Higher risk categories	-	-	-	-	-	-
13	Other Assets	18.1	-	18.1	-	19.3	107%
14	**Total**	**1,886.9**	**177.9**	**1,868.8**	**57.3**	**1,303.1**	**68%**

8.14 Standardised approach- exposures by asset class and risk weights

		a	b	c	d	e	f	g	h	i	j
	Asset Classes / Risk Weight	0%	10%	20%	35%	50%	75%	100%	150%	Other	Total credit exposures amount post CCF and post CRM
		£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m	£'m
1	Sovereigns and their central banks	231.1	-	-	-	-	-	-	-	-	231.1
2	Non central government public sector entities	-	-	-	-	-	-	-	-	-	-
3	Multilateral development banks	-	-	-	-	-	-	-	-	-	-
4	Banks	-	-	34.3	-	-	-	-	-	-	34.3
5	Securities firms	-	-	-	-	-	-	-	-	-	-
6	Corporates	-	-	-	-	-	98.8	121.6	-	-	220.4
7	Regulatory retail portfolios	-	-	-	-	-	751.2	-	-	-	751.2
8	Secured by residential property	-	-	-	24.6	-	-	-	-	-	24.6
9	Secured by commercial real estate	-	-	-	378.1	-	-	27.4	217.1	-	622.6
10	Equity	-	-	-	-	-	-	-	-	-	-
11	Past due loans	-	-	-	-	-	-	23.8	-	-	23.8
12	Higher risk categories	-	-	-	-	-	-	-	-	-	-
13	Other Assets	-	-	-	-	-	-	17.3	-	0.8	18.1
14	**Total**	**231.1**	**-**	**34.3**	**402.7**	**-**	**850.0**	**190.1**	**217.1**	**0.8**	**1,926.1**

9 Counterparty Credit Risk

9.1 Qualitative disclosure related to counterparty credit risk

The Group is exposed to counterparty risk through placing their excess funds with banking institutions. Failure of one of these counterparties has been considered, but is thought unlikely, as the Group's policy is to place funds with institutions considered systemically important in the UK. Exposure to these banking institutions has substantially reduced as the majority of available funds are invested in the Group's Bank of England reserve account.

The Group has transactional accounts with Barclays and the Royal Bank of Scotland group. The balances are within counterparty limits approved by the Board, which are set out in the Wholesale Counterparty and Credit Risk Policy (approved by the Group's Assets & Liabilities Committee).

The Group does not have any derivative or security financing transaction (SFT) exposures at 31 December 2017 nor have there been any during the 2017 year.

Therefore the Board considers that the Group is not significantly exposed to counterparty risk and accordingly no capital add-on is required.

9.2 Analysis of counterparty credit risk (CCR) exposure by approach

The Group has not entered into any derivatives or securities financing transactions (SFTs) during the year. Accordingly table CCR1 has not been provided.

9.3 Credit valuation adjustment (CVA) capital charge

The Group has not entered into any derivatives or securities financing transactions (SFTs) during the year. Accordingly no CVA capital charge is required and therefore table CCR2 has not been provided.

9.4 Standardised approach – CCR by regulatory portfolio and risk weights

	a	b	c	d	e	f	g	h	i	j
Risk Weight / Regulatory Portfolio	0% £'m	10% £'m	20% £'m	35% £'m	50% £'m	75% £'m	100% £'m	150% £'m	Others £'m	Total credit exposures £'m
Sovereigns and their central banks	231.1	-	-	-	-	-	-	-	-	231.1
Non central government public sector entities (PSEs)	-	-	-	-	-	-	-	-	-	-
Multilateral development banks (MDBs)	-	-	-	-	-	-	-	-	-	-
Banks	-	-	34.3	-	-	-	-	-	-	34.3
Securities firms	-	-	-	-	-	-	-	-	-	-
Corporates	-	-	-	408.2	-	98.8	164.6	264.6	-	936.2
Regulatory retail portfolios	0.3	-	-	0.3	-	767.2	59.3		-	827.1
Other assets	-	-	-	-	-	-	17.3	-	0.8	18.1
Total	**231.4**	**-**	**34.3**	**408.5**	**-**	**866.0**	**241.2**	**264.6**	**0.8**	**2,046.8**

9.5 Composition of collateral for CCR exposure

The Group has not entered into any derivatives or securities financing transactions (SFTs) during the year. Accordingly table CCR5 has not been provided.

9.6 Credit derivatives exposure

The Group has not entered into any derivatives or swaps during the year. Accordingly table CCR6 has not been provided.

9.7 Exposure to central counterparties

The Group has not entered into any derivatives or SFTs during the year. Accordingly table CCR8 has not been provided.

10 Securitisation

The Group has not entered into any securitisation transactions during the year, nor does it have any securitisation exposure at 31 December 2017. Accordingly table SEC1 has not been provided.

11 Market Risk

The Group does not hold any capital in respect of market risk at 31st December 2017, apart from that related to Interest Rate Risk in the Banking Book (IRRBB) which is described in part 12 below.

No entity within the STB Group trades in securities, there is no appetite for foreign exchange risk and all treasury transaction are undertaken on a matched basis, thereby eliminating settlement risk.

12 Interest Rate Risk in the Banking Book (IRRBB)

Interest rate risk is the risk of potential loss through unhedged or mismatched asset and liability positions, which are sensitive to changes in interest rates. When interest rates change, the present value and timing of future cash flows change. This in turn changes the underlying value of the Group's assets, liabilities and off-balance sheet instruments and hence its economic value. Changes in interest rates also affect the Group's earnings by altering interest-sensitive income and expenses, affecting its net interest income.

The Group seeks to 'match' interest rate risk on either side of the Statement of Financial Position. However, this is not a perfect match and interest rate risk is present on money market deposits of a fixed rate nature, fixed rate loans and fixed rate savings products.

The Group monitors the interest rate mismatch on a monthly basis. The main test employed is a 200bps interest rate shock across all interest indices on a parallel basis. The Group maintained such exposures within the Risk Appetite set by the Board throughout the year.

The Group measures Earnings at Risk (EaR) and Value at Risk (VaR), predominantly by monitoring the Interest Rate Sensitivity Gap. Interest rate risks inherent in new products or through changes to the terms and conditions of existing products were assessed over the course of the year.

This potential exposure is managed by the Group treasury function and overseen by the Assets and Liabilities Committee (ALCO). The policy is not to take significant unmatched own account positions in any market.

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

13 Remuneration

13.1 Role of the remuneration committee

Remuneration policy is overseen by the Remuneration Committee. The Remuneration Committee is composed of four members. Victoria Stewart was appointed as the Chairman of the Remuneration Committee on 21 July 2017. There were no changes to the membership of the Committee in 2017.

The Remuneration Committee meets at least twice a year and additionally when required to address non-routine matters. The Company Secretary or the Deputy Company Secretary acts as Secretary to the Remuneration Committee. Other individuals attend at the request of the Remuneration Committee Chairman and during the year the Chief Executive Officer, HR Director and other senior managers attended meetings to report to the Committee.

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

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

The key matters considered by the Committee from 1 January 2017 to the date of this report were:

Item	Comment
Directors Remuneration Report (DRR) and other disclosures in the Annual Report & Accounts.	The Committee considered the disclosures required in the Annual Report & Accounts for the first time as a company listed on the Main Market. The Committee received advice from the Company Secretary, HR Director and Deloitte when compiling the DRR and the additional disclosures in the Notes.
Remuneration Policy (“Policy”) proposed at AGM	The Committee reviewed and approved for recommendation to the Board the Remuneration Policy, having consulted with major shareholders and received advice on the Policy from Deloitte, the HR Director and the Company Secretary. The Policy was proposed to shareholders at the AGM held on 3 May 2017 and was approved as set out on the Company website, www.securetrustbank.com
Share Schemes presented at AGM.	In connection with the Policy, the Committee considered proposals regarding three share plans, being a Long Term Incentive Plan, a Deferred Bonus Plan and an HMRC approved eligible employee Save As You Earn (Sharesave) Plan. Further details on each plan and their operation can be found in the Policy on the Company website. The plans were presented to shareholders at the 2017 AGM and approved. The plans were then implemented in June and September 2017.
Executive Directors bonus arrangements	The Remuneration Committee considered the bonus arrangements in relation to the Executive Directors for 2016 under the arrangements that applied before the adoption of the Remuneration Policy. These arrangements had operated on a discretionary basis but the Remuneration Committee took into account the financial performance of the Group and personal

	performance in a year of record profits, strong return on equity and operational and regulatory performance. The Remuneration Committee considered the bonus arrangements in relation to the Executive Directors for 2017 in accordance with the Remuneration Policy and the targets set as part of a balanced business scorecard. In doing so the Remuneration Committee took into account the financial performance of the Group and personal performance.
Forward calendar and items for 2018	The Committee agreed a standing agenda and calendar of meetings for 2018. Four meetings are planned to be held in 2018 to address routine matters.
Annual review of terms of reference	The Committee reviewed its term of reference and approved these for recommendation to the Board.

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

13.2 Key features of the remuneration policy

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

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

In developing and implementing the policy the Group has also had regard to regulatory requirements and the responsibilities of senior managers under the senior manager regime.

The Group is currently a level 3 firm within the classifications applied by the regulators for their remuneration codes for regulated entities. That means that the Group is not required to satisfy in full all elements of the remuneration codes. Notwithstanding this, in formulating and applying the Remuneration Policy the Committee has had regard to the remuneration codes.

The application of the remuneration policy is described in the Remuneration Report within the 2017 Annual Report and Accounts. In determining appropriate rewards for executive management the Remuneration Committee has had regard to the achievements of 2017, the balanced business scorecard agreed by the Committee and the parameters of the Remuneration Policy. The Remuneration Committee, in determining appropriate awards for Executive Directors, also has had regard to the risk culture of the Group and regulatory matters, as well culture and employee engagement.

Remuneration arrangements for other employees are determined throughout the Group based on the same principle that reward should be achieved for delivery of the business strategy and should be sufficient to attract and retain high calibre talent.

The Committee considers the general basic salary increase, remuneration arrangements and employment conditions for the broader employee population when determining remuneration policy for the Executive Directors. There is no consultation with employees on Director remuneration.

The Committee may make minor changes to this policy, which does not have a material advantage to Directors, to aid in its operation or implementation, taking into account the interests of shareholders but without the need to seek shareholder approval.

13.3 Shareholder views

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

The Board recognises the importance of maintaining good relationships with shareholders. The Chief Executive Officer and the Chief Financial Officer would normally expect to meet with institutional shareholders on a regular basis, including following the publication of financial information or updates by the Group. The Chairman has joined them in some meetings throughout 2017. The Group's brokers also facilitate communication between the Group and its institutional shareholders.

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

13.4 Existing contractual arrangements

The Committee retains discretion to make any remuneration payment or payment for loss of office outside the policy in this report:

- where the terms of the payment were agreed before the policy came into effect;
- where the terms of the payment were agreed at a time when the relevant individual was not a Director of the Company, and in the opinion of the Committee, the payment was not in consideration of the individual becoming a Director of the Company; and
- to satisfy contractual arrangements under legacy remuneration arrangements, including any arrangements in place prior to Admission.

For these purposes, 'payment' includes the satisfaction of awards of variable remuneration, and in relation to an award involving shares the terms of the payment are agreed at the time the award is granted.

The Committee may satisfy any Phantom Share Option granted under the Group's Phantom Share Option Scheme and may adjust the terms of any such Phantom Share Option to take account of any variation of share capital, demerger, delisting, special dividend or other event which may affect the Company's share price.

13.5 Service agreements and letters of appointment

Executive Directors' service agreements are on a rolling basis and may be terminated on 12 months' notice by the Company or the Executive Director. Service agreements for new Executive Directors will generally be limited to 12 months' notice by the Company.

All Non-Executive Directors' letters of appointment are on a rolling basis and may be terminated on six months' notice by the Company or the Non-Executive Directors. All Non-Executive Directors are subject to re-election at intervals of not more than three years.

For further information regarding the operation of the Remuneration Policy please refer to the Remuneration Committee section of the 2017 Annual Report and Accounts.

13.6 Bonus arrangements

Bonuses for the Executive Directors for the financial year ended 31 December 2017 were subject to stretching performance metrics based on a balanced business scorecard of financial, customer, operational and staff metrics. Up to 70% of the bonus was subject to financial performance metrics and 30% of the bonus was subject to a mixture of customer, operational and staff performance metrics. A high level description of the performance metrics and objectives for both Executive Directors is set out in the Remuneration Committee section of the 2017 Annual Report and Accounts.

13.7 Awards granted during the financial year

a) 2017 Long term incentive plan (LTIP)

Following shareholder approval at the 2017 AGM, share options were granted to senior employees in accordance with the rules of the Secure Trust Bank PLC 2017 LTIP. Each of the options granted was subject to the performance conditions and performance period as detailed in the 2017 Annual Report and Accounts. A holding period applies to the awards granted to the Executive Directors. The award will, ordinarily, be released so that the Executive Directors are entitled to acquire the shares following the end of a holding period which ends on the second anniversary of the vesting date

The Company granted awards under the LTIP to the Executive Directors subject to EPS, Relative TSR and risk management performance metrics. Performance will be assessed over a three year performance period.

The EPS and relative TSR performance targets are set out in the table below:

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

The Awards made on 1 June 2017 used the following group of selected peers for assessing TSR performance: Aldermore Group, Arbuthnot Banking Group, Close Brothers, One Savings Bank, Metro Bank, Paragon Group of Companies, Provident Financial, S&U, Shawbrook Group and Virgin Money.

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

b) 2017 Share save plan

Following shareholder approval at the 2017 AGM, share options over ordinary shares were offered to all eligible employees in accordance with the rules of the Secure Trust Bank PLC 2017 Share save Plan (SAYE). Options were granted on 20 September 2017 to the successful applicants. Each option has an exercise price per Ordinary Share of 1318.8p. Subject to the rules of the Scheme, the options will ordinarily vest on 1 November 2020 and be exercisable for a period of six months.

229 employees have been granted options under the Scheme in respect of a total of 125,987 Ordinary Shares. Both executive directors qualified as eligible employees and participated in the scheme. Both were granted options over 1,364 shares.

c) 2011 Share option scheme

No awards under the 2011 Share Option Scheme were granted during the financial year ended 31 December 2017.

13.8 Statement of Directors' shareholding and share interests

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

The interests of the Directors and their connected persons in the Company's ordinary shares as at 31 December 2017 are set out in the 2017 Annual Report and Accounts.

13.9 Remuneration awarded during the financial year

			a	b
	Remuneration amount		Senior Managers	Other material risk takers
1	Fixed Remuneration	Number of Employees	8	13
2		Total Fixed Remuneration (3+5+7)	£2,305,161	£2,552,967
3		Cash based	£2,305,161	£2,552,967
4		of which: deferred	-	-
5		Shares or share linked instruments	-	-
6		of which: deferred	-	-
7		Other forms	-	-
8		of which: deferred	-	-
9	Variable Remuneration	Number of Employees	8	13
10		Total Variable Remuneration (11+13+15)	£1,498,477	£1,841,161
11		Cash based	£700,000	£1,040,100
12		of which: deferred	£175,000	-
13		Shares or share linked instruments	£798,477	£801,061
14		of which: deferred	£798,477	£801,061
15		Other forms	-	-
16		of which: deferred	-	-
17	**Total Remuneration (2 + 10)**		**£3,803,638**	**£4,394,128**

Senior managers represent the executive and non-executive directors of the Group. Other material risk takers have been determined in accordance with the EBA ‘Material Risk Takers Regulatory Technical Standards’ definition as staff ‘whose professional activities have a material impact on the Group’s risk profile’.

13.10 Special payments made during the financial year

Special payments	Guaranteed Bonuses		Sign-on awards		Severance payments	
	Number of employees	Total amount	Number of employees	Total amount	Number of employees	Total amount
Senior management	-	-	-	-	-	-
Other material risk takers	-	-	1	£52,600	-	-

13.11 Deferred remuneration at 31 December 2017

		a	b	c	d	e
Deferred and Retained Remuneration		Total amount of outstanding deferred remuneration	Of which: Total amount of outstanding deferred and retained remuneration exposed to ex-post explicit/implicit adjustment	Total amount of amendment during the year due to ex-post explicit adjustments	Total amount of amendment during the year due to ex-post implicit adjustments	Total amount of deferred compensation paid out in the financial year
Senior Managers	Cash	£175,000	-	-	-	-
	Shares	£798,477	£798,477	-	£798,477	-
	Cash-linked Instruments	-	-	-	-	-
	Other	-	-	-	-	-
Other material risk takers	Cash	-	-	-	-	-
	Shares	£801,061	£801,061	-	£801,061	-
	Cash-linked Instruments	-	-	-	-	-
	Other	-	-	-	-	-
	Total	**£1,774,538**	**£1,599,538**	**-**	**£1,599,538**	**-**

None of the deferred remuneration awarded during 2017 or in prior years is subject to direct adjustment clauses. The valuation of share based awards will fluctuate with the market value of the Secure Trust Bank Plc (STB plc) share price.

The total value of share remuneration disclosed relates to those awarded in 2017 as noted in section 13.9 above. Similar share awards remain outstanding from previous years however no value has been attributed to them as the market value of STB plc shares at 31 December 2017 is below the option prices of these awards. No share options relating to deferred awards from prior years were exercised during the year.