



Always with your interest at heart

Pillar 3 Disclosure

31 December 2021

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1. Overview

1.1 Background

This document presents the consolidated Pillar 3 disclosures of Furness Building Society, as at 31 December 2021.

The Society is regulated for prudential capital purposes under the Basel 3 regulation which was implemented in the EU via the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD), together known as Capital Requirements Directive IV (CRD IV). CRD IV consists of three main 'Pillars':

Pillar 1	This covers the minimum capital requirements of Basel 3. The calculation is based on a risk based approach. It focuses on credit, operational and market risk in determining the Society's Minimum Capital Requirement.
Pillar 2	Assessment of capital adequacy – the Internal Capital Adequacy Assessment Process (ICAAP), undertaken by the Society, and the Supervisory Review and Evaluation Process (SREP), undertaken by the PRA in the UK, assess additional capital requirements not captured by Pillar 1. This is known as the Total Capital Requirement.
Pillar 3	Pillar 3 complements Pillars 1 and 2 and aims to encourage market discipline by setting out disclosure requirements which should allow market participants to assess key pieces of information on a firm's capital, risk exposures, risk management processes and remuneration. These requirements are set out in Part 8 of the CRR ('Part 8'). These requirements are updated with additional guidance issued by appropriate bodies such as Basel Committee, European Banking Authority.

The document has been prepared to meet the Pillar 3 disclosure requirements of CRD IV as presented in Part 8 (Articles 431 to 455) of Regulation (EU) no 575/2013. A Basel Committee on Banking Supervision (BCBS) March 2017 review led to a consolidation of all existing BCBS disclosure requirements into the Pillar 3 framework. These guidelines apply only to Globally and Other Systematically Important Institutions.

The Society is not a Globally or Other Systemically Important Institution and taking account of its relatively simple business model and low risk profile, has chosen not to reflect in full the BCBS framework. However, the Society has had regard to these guidelines in preparation of this document.

1.2 Basis and Frequency of Disclosures, Scope of Application

These Pillar 3 disclosures are based on the Society's Annual Report & Accounts for the year ended 31 December 2021. All figures are stated as at 31 December 2021 with comparatives as at 31 December 2020 where applicable, unless otherwise stated.

The disclosures are updated on at least an annual basis and are issued in conjunction with the publication of the Annual Report & Accounts. The content of Pillar 3 reporting will continue to be reviewed on an ongoing basis to ensure that it is appropriate and informative in line with regulatory changes and best practices and remain proportionate (in terms of materiality) to a small to medium building society.

This document is published on Furness Building Society's website (www.furnessbs.co.uk).

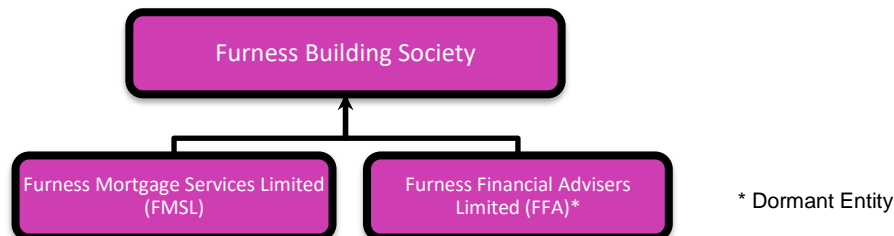
The disclosures are reviewed by the Board. They are not subject to External Audit, however, some of the information within the disclosures also appears in the Group's audited Annual Report & Accounts for the years ended 31 December 2021 or 31 December 2020, usually rounded to the nearest £0.1m.

The Society's Annual Report & Accounts have been prepared in accordance with FRS102 and 'IAS 39 Financial Instruments' accounting standards, whereas the Pillar 3 disclosures are prepared under

CRD IV rules. The main differences between accounting and regulatory reported exposures and capital are set out in sections 3 & 4 of this document.

The Society has adopted the Standardised Approach ('SA') for credit risk and the Basic Indicator Approach ('BIA') for operational risk.

Our Pillar 3 disclosures are based on the Society's consolidated Group position, which is also detailed in our Annual Report & Accounts. The Group consolidation includes the Furness Building Society and its two wholly owned subsidiaries, Furness Mortgage Services Limited (FMSL) and Furness Financial Advisers Limited (FFA).



References hereafter to the “**Group**” within these Pillar 3 disclosures comprise these three entities.

See below a brief overview of the above two subsidiaries.

Furness Mortgage Services Limited (FMSL) manages secondary mortgage portfolios and acquired five mortgages books from 2000 to 2004. FMSL's current mortgage portfolio is in 'run-off' and no longer issues mortgages. As at 31 December 2021 FMSL had £3.1m of mortgage balances outstanding.

Furness Financial Advisers Limited (FFA) is no longer trading and is operationally dormant, but as at 31 December 2021 still retains capital and intercompany balances with the Society.

1.2 Summary of Key Prudential Metrics

Key Metrics	Dec-21	Dec-20
Available Capital	£m	£m
Common Equity Tier1 (CET1)	77.0	70.4
Tier 1	77.0	70.4
Total Capital	77.8	72.2
Risk-weighted assets	£m	£m
Total risk-weighted assets (RWA)	401.6	375.5
Risk-based capital ratios as a percentage of RWA	%	%
Common Equity Tier 1 Ratio	19.18%	18.74%
Tier 1 ratio	19.18%	18.74%
Total capital ratio	19.37%	19.23%
Additional CET1 buffer requirements as a percentage of RWA	%	%
Capital conservation buffer requirement	2.50%	2.50%
Countercyclical buffer requirement	0.00%	0.00%
Total of bank CET1 specific buffer requirements	2.50%	2.50%
CET1 available after meeting the Society's minimum capital requirements *	9.25%	8.96%
Basel III Leverage Ratio		
Total Basel III leverage ratio exposure measure (£m)	1,183.6	1,138.7
Basel III leverage ratio (%)	6.51%	6.18%
Liquidity Coverage Ratio		
Total Liquid Assets (£m)	150.8	167.4
Total net cash outflow (£m)	76.4	61.1
LCR Ratio (%)	197.3%	273.8%
Net Stable Funding Ratio		
Total available stable funding (£m)	1,044.8	1005.1
Total required stable funding (£m)	702.1	682.4
NSFR ratio (%)	148.8%	147.3%

* reflects the amount of CET1 capital available after meeting our Pillar 1 and Pillar 2A requirements, see section 4.5 for further information regarding Total Capital Requirements (TCR).

Capital and Leverage Ratios

The Group's CET1 ratio at December 2021 is 19.18%, which is 44bp higher than December 2020 (18.74%). The main drivers behind the change over 2021 are as follows:

- CET1 capital increased by £6.6m in the year. The Society made a profit in the year of £4.0m after tax, plus a gain on Other Comprehensive Income of £3.0m, primarily driven by an actuarial gain recognised on the FRS102 pension scheme liability. The pension scheme assets experienced an increased level of returns, partially offset by an increase in inflation expectations, and has furthermore benefitted from a switch to a lower-risk investment portfolio (see Section 2.1.2 for further detail). Intangible assets have increased by £0.4m, which offsets the CET1 measure.
- RWAs increased by £26.1m in 2021 driven by a £50.7m increase in mortgage assets over the year, as well as increased off-balance sheet commitments.

As at December 2021 the Society holds a CET1 surplus to minimum capital requirements of 9.25%, which is 6.75% above specific buffer requirements of 2.50%. Over the year, the surplus to minimum requirements increased as a result of the capital growth outlined above, whilst requirement levels in percentage terms remained unchanged.

As at 31 December 2021, the Group's Leverage Ratio was 6.51%, (6.18%: 2020), which is above the current 3% regulatory minimum level. The increase was due to Tier 1 capital growth partly offset by a rise in the Leverage Ratio exposure measure as a result of overall balance sheet and mortgage commitment growth.

Liquidity and Funding Ratios

The Group held liquidity and funding levels above minimum regulatory requirements of 100% for both the Liquidity Coverage Ratio (197.3%) and Net Stable Funding Ratio (148.8%) as at 31 December 2021. There was a reduction of £16.6m in total liquid assets during 2021 due to utilisation of excess liquidity to fund mortgage lending.

2. Risk Management

2.1 Risk Management Framework

2.1.1 Overview

The Group is a retailer of financial instruments in the form of mortgages and savings. The Group also uses wholesale financial instruments to invest in liquid assets, raise wholesale funding and to manage the interest rate risks arising from its operations.

The Board has overall responsibility for maintaining a system of internal control to ensure that an effective risk management and oversight process operates across the Society. The risk management framework is designed to identify, understand and monitor the risks within the business, including risks to which the Society may become exposed, and manages rather than eliminates risks to meet the Society's business objectives.

The Society uses the industry standard three lines of defence model for the management of risk:

• LINE 1 – BUSINESS OPERATIONS

Business Areas – The first opportunity to identify risks and put in place steps to mitigate them as necessary. Management is delegated responsibility to identify and evaluate the risks within their business areas and ensure controls are operating effectively over those risks, such that the Society meets the aim of its internal control system and operates within the risk appetite agreed by the Board. The delegated management responsibility extends to activities undertaken by outsourced and third-party relationships

• LINE 2 – OVERSIGHT FUNCTIONS

Risk Management Committees and related functions (e.g. Compliance and Risk) – These areas provide oversight and support the business in identifying and managing risk and generally co-ordinate the risk management activity across the whole business. These areas provide a level of assurance as to the adequacy and operation of the risk and control environment across the Group. Where the Society does not have internal expertise or resource capacity, the Society will engage with third parties to provide second line assurance as necessary.

• LINE 3 – INDEPENDENT ASSURANCE

The Internal Audit function, which is outsourced, provide independent assurance which is reported to the Audit Committee. This is the 'backstop' line of defence and provides objective assurance that all risks have been identified and are being managed appropriately through the control framework in place, including the adequacy of the internal control system.

The Board has determined a clearly defined Statement of Risk Appetite, containing both quantitative and qualitative measures which are integrated into decision making processes.

The risk framework comprises a number of Committees, including the key committees of Board Risk and Audit. Through the Board Risk and Audit Committees, the Board receives comprehensive and timely reporting on the Society's identification, measurement and management of risk.

The Board's defined Statement of Risk Appetite is reviewed and adjusted at least annually and forms a key part of the corporate planning process. Adherence to the risk appetite is monitored by the Committees in the risk framework and reported to the Board each month against agreed measures.

The risk management framework is proportionate to the scale and complexity of the business and is commensurate with the degree of risk in the business to support decision making. It ensures the Society deploys a consistent approach to risk management in each of the principal risk areas.

2.1.2 Summary of Key Risk Areas

Business and Strategic Risk

The Society considers that Business and Strategic risks are inextricably linked.

Strategic risk is the risk resulting from our strategic decisions which have the potential to impact the Corporate Plan and forecast results or performance over the planning period. A crystallisation of strategic risk could affect the overall strength of the Society or impact the business model. The Board regularly discusses strategic issues and challenges the Corporate Plan proposed by Executives. It ensures strong levels of capital and liquidity are maintained to provide resilience against external factors which may cause stresses to the business.

Margin risk is the risk of erosion between the interest rates charged to our mortgage borrowers and the interest rates paid to our savings account holders. Whilst the interest rate environment remains relatively low but with the expectation of rising rates, in an exceptionally competitive market, margin decline is a significant risk which requires robust management.

The Board sets margin objectives within the Corporate Plan, and the Executive and Pricing Committee and Assets & Liabilities Committee (ALCO) monitor the position closely.

The Society's strategy is reviewed at least annually by the Board and Management to ensure it remains appropriate, deliverable and sustainable with external assistance sought when required to validate conclusions. The on-going management of strategic risk is supported by the business performance and risk reporting data provided to the Board and Risk Committees.

The current challenging economic environment and competitive low interest rate mortgage market continues to put pressure on the net interest margin and this has been addressed through our strategy development. Consideration has also been given to the potential ramifications of geopolitical uncertainty on our current and future obligations and the Society's prospects over the Corporate Plan period of three years to 2024.

In 2022 the Society will continue to invest in technology, capability and product propositions and distribution to ensure we are in the best position to meet customer expectations and secure a sustainable future for the Society.

Credit Risk

Credit risk is the risk that borrowers or counterparties to whom the Society has lent money may default on their obligation to repay the Society. The Society holds security on customer mortgages in the form of property and land. A reduction in the House Prices Index (HPI) impacts the value of these and may increase the loss in the event of default. Furthermore, property and land also becomes harder to sell during an economic downturn and therefore increases the discount on the sale price of the property (forced sale discount), further increasing the Society's credit risk.

The Society manages the risk associated with mortgage borrowers by means of a prudent Lending policy that includes both a thorough assessment of the creditworthiness of the borrower and the value of the proposed security. Mortgages are monitored closely and on an ongoing basis, with timely action being taken for those mortgages that fall into arrears.

The Society continues to manage the risk that our borrowers may default on repayments through prudent lending criteria comprising detailed credit history assessments as well as robust property valuations. Fluctuations in the house price index impact the credit risk inherent in the mortgage book, although in 2021 there was an average indexed increase of 10.00% on the previous year.*

*Land Registry Data - UK House Price Index, November 2021

The Credit Risk Committee meets regularly to consider the risks associated with this lending and reviews large and potential accounts in default. The Society has continued improving the analysis and management information to understand and manage its credit risk exposures effectively.

In the case of liquid asset investments, the credit risk associated with lending to financial institutions is addressed by the Society's Assets and Liabilities Committee (ALCO) which ensures that investments are restricted principally to cash held with the Bank of England, UK Government issued debt instruments, liquid regulatory compliant AAA rated debt securities and operational call accounts with large UK based clearing banks with investment-grade credit ratings.

The Society keeps abreast of developments affecting financial sector firms and takes appropriate action to safeguard the Society's investments.

The Society utilises manual underwriting procedures which enables individual risk assessment of complex cases. Underwriting procedures have been updated to allow for the impact of Covid-19.

See section 5.1 for further detail of the Society's approach to credit risk, including further analysis of past due and impaired assets by lending category and a credit analysis of Treasury Assets.

Concentration Risk

As a regional building society, the Society is exposed to concentration risk because its activities are highly concentrated in residential lending and/or associated products and services funded predominantly by retail deposits. Concentration risk is concerned mainly with the risk that in extreme scenarios, the lack of diversification may mean the losses resulting from such concentrations may be sufficient to threaten the solvency of the Group.

The following types of concentration risk are monitored to ensure that lending is not more than is appropriate for the Group in relation to its Position/Size; Geographic, Funding, Large Exposures and Product Type.

The Society's heartland is within the North West area where it also has a higher proportion of its mortgage balances. This regional geographic concentration risk is considered when undertaking stress testing and models the impact of falls in regional property prices. The Society's lending concentration in the North West has been steadily decreasing over recent years with the increased use of UK-wide intermediary origination channels. The Society regularly monitors its geographic concentration risk and adjusts its lending strategy where appropriate in line with Board limits.

The Society has a low proportion of its total lending in the form of commercial mortgages (£4.7m as at 31 December 2021) and monitors the amount of this type of lending on a regular basis to ensure that the quality and quantity remain within the Board's risk appetite.

See section 5.1 for further analysis of the Society's exposures by lending category and geography.

Interest Rate and Basis Risk

The Society is exposed to interest rate and basis risk arising within the banking book, which results from different interest rate features, re-pricing dates and maturities of assets (mortgages and treasury investments) and liabilities (retail savings, wholesale funding and subordinated debt).

The Society's ALCO monitors and manages this exposure. The following activities are affected by interest rate risk:

- fixed rate mortgage lending and fixed rate treasury investments
- fixed rate savings products and fixed rate wholesale treasury funding
- management of the investment of reserves and other net non-interest bearing liabilities.

To manage fixed rate risk, the Society uses a combination of natural hedging, matching on balance sheet assets and liabilities with similar maturity dates, and interest rate swaps.

Basis risk is the risk of divergence between several bases, such as SONIA and the Bank of England Base Rate. The Society manages its basis rate risk exposure mainly by setting limits against the relative exposures and carefully monitoring the positions.

The Society's interest rate related risk appetite is measured against:

- the economic impact of a parallel shift in interest rates of 2% over the life of the balance sheet
- the impact on annualised Net Interest Income (NII) of a 100bps interest rate shock on a static balance sheet

See section 5.2.1 for further details on the measurement and control of interest rate risk.

Liquidity Risk

Liquidity risk is the risk of the Society failing to meet its financial obligations as they fall due, resulting in the inability to support normal business functions and activity. There is also a risk of breaching regulatory requirements.

The nature of the Society's business involves 'maturity transformation' whereby the Society borrows for relatively short terms and lends on mortgages for much longer periods. This mismatch creates liquidity risk whereby the Society could be unable to meet its financial obligations as they fall due.

Funding risk is the inability to access funding markets or to do so at excessive cost. In order to minimise funding risk the Society ensures there is no over reliance on a single source of funds.

The purpose of the Society's Internal Liquidity Adequacy Assessment Process (ILAAP) is to ensure that these commitments can be met in a timely manner under both normal and stressed conditions and that the Group maintains the confidence of its existing and potential investors and suppliers.

On a day-to-day basis the Group's liquidity position is managed by the Treasury function which is responsible for the liquid asset portfolio and contingency arrangements. Liquidity and funding risk is monitored by the ALCO which meets on a frequent basis and receives a variety of management information reports which enable it to monitor the amount and composition of the liquid asset portfolio and ensure Group compliance with the regulations covering liquidity as well as the Board Statement of Risk Appetite of the Group.

The Society's liquidity policy has been developed to ensure that the Group is able to meet known, and also a reasonable level of possible unforeseen, financial obligations as they fall due under both normal conditions and defined stress scenarios. This is achieved by a combination of:

- undertaking an annual review of Liquidity and Funding via the ILAAP
- maintaining an appropriate level of high quality liquid assets (Liquidity Buffer)
- having access to additional sources of funds through the wholesale market as well as from retail customers
- access to Bank of England liquidity insurance facilities
- regular stress testing to ensure the Society can meet its liquidity adequacy requirements under a number of defined stress scenarios
- maintaining and testing a Liquidity Contingency Plan.

Sufficient liquidity is maintained at a level aimed at ensuring management, regulatory and member confidence in the solvency of the Group. A significant proportion of the Society's liquid assets are held in a Bank of England reserve account, UK Bank call accounts and short term deposits, to provide instant access to funds if and when required. In addition the Society holds a portfolio of treasury investments where there is an active secondary market enabling liquidation if required under a stress scenario. These treasury investments are all eligible for use as collateral in the Discount Window Facility with the Bank of England and inclusion in the Society's Liquid Asset Buffer.

See section 5.2.2 and 5.2.3 for further details on the measurement and control of liquidity risk.

Capital Risk

Capital risk refers to the potential for a scenario to occur that reduces the Society's capital to an unsustainable level or below the minimum regulatory requirements. The Society regularly tests various scenarios to ensure it retains sufficient capital to manage foreseeable and possible events.

The Society's Internal Capital Adequacy Assessment Process (ICAAP) is the Society's evaluation of its capital position and requirements and sets out the approaches to manage capital risk across the planning horizon including the evaluation and monitoring of risk appetite limits.

The Society maintains a sufficient level of regulatory capital in order to absorb losses, deliver the Corporate Plan and support the Society's risk profile in both normal and stressed conditions.

The Board has approved a set of risk appetite measures and operating limits to manage and monitor capital levels on an ongoing basis, including:

- maintaining a conservative capital surplus over and above minimum regulatory Pillar 1, Pillar 2 and regulatory buffer requirements over the corporate planning period
- monitoring profit and mortgage asset growth to ensure the Society's growth remains sustainable.
- monitoring Early Warning Indicators on a monthly basis for both CET1 and Leverage Ratios, ensuring a sufficient surplus to regulatory requirements.

See sections 3 and 4 for further detail on the Group's capital position as at December 2021 and the stress testing undertaken as part of the Internal Capital Adequacy Assessment Process (ICAAP).

Operational Risk

Operational risk is the risk of loss arising from inadequate or failed internal processes or systems, human error or external events, and can arise across the whole business, with higher likelihood in periods of transformational change or other large projects.

While the Society's response to the unprecedented events of 2020 and 2021 has included the adoption of remote working, enabling us to maintain critical services for our members, it has presented a significant operational risk including cyber risks, potential productivity impacts and those on an individual wellbeing level. We will continue to monitor these closely over the course of 2022.

We have robust systems and controls in place to mitigate operational risks and we have numerous software and other infrastructure protection in place to support operational resilience and mitigate against the risk of disruption from events such as cyber or data loss.

The Society continues to focus on improvements in operational resilience in 2022 and mitigate against the risk of disruption from events such as cyber-attacks or data loss. In addition, the Society has committed a significant level of investment into eSavings for our customers and will be delivering a new platform with a number of enhanced functions.

The Society is exposed to Legal and Regulatory risks, which is the risk of fines, public censure limitations on business or restitution costs arising from failure to understand or correctly interpret regulatory change. Regulatory changes are monitored and reported monthly to the Executive and Risk Committees.

The Society has a Management Risk Committee which is chaired by the Chief Risk Officer and comprises of representatives of the Society's Leadership Team and the Operational Risk Manager. This Committee provides oversight to all the Society's operational risks. Ultimately, the Board is responsible for deciding on whether it accepts the residual risk that exists after the application of these controls.

Conduct Risk

Conduct risk is the risk that the Society fails to design and implement operational arrangements, systems and controls which deliver fair outcomes for customers whilst maintaining regulatory and legal compliance.

The Group must ensure that it conducts dealings with its customers in a manner that is fair and is in their interests. The Board is ultimately responsible for the fair treatment of customers.

The Society has a Management Risk Committee which is chaired by the Chief Risk Officer with representatives of the Society's Leadership Team.

Conduct risk key performance indicators, which cover culture, marketing, product development, sales processes and post-sale service, are considered by the Board on a quarterly basis.

Although the Society seeks to control its own conduct risk, it also carries a potential liability to the Financial Services Compensation Scheme (FSCS) the size of the liability depends upon the failure of other members of the FSCS.

Pension Liability Risk

The Society operates a Defined Benefit Pension Scheme that provides benefits based upon final pensionable pay. This Scheme was closed to new entrants in September 2000 and closed to future accrual with effect from 1 January 2017.

At the end of the year, the Scheme deficit was £0.9m (£5.7m: 2020). We have agreed to increase our future contributions in order to maintain the previously agreed term of the payment plan.

During 2020, following a competitive tender process, we completed a transfer of the trusteeship and governance of the Defined Benefit Pension Scheme to Entrust Pension Limited. The new arrangements completed in March 2021 and provide the full time professional expertise required for the complex management of the scheme.

In H1 2021 the pension Trustees, in conjunction with the ISIO actuarial team and with agreement from the Society, carried out a review of the Scheme's investment strategy, taking into account expected returns, hedging ratios, Value at Risk, time to full funding, and management costs. The move to a new, lower-risk strategy was agreed and implemented in the second half of 2021.

The Society monitors possible future pension risk as part of the ICAAP process and ensures sufficient capital is held against this risk.

Climate change Risk

In line with much of the financial services industry we are aware of the potential long-term and structural risks that accompany the risks of climate change. In 2021 the Society introduced the Climate Risk Framework that is used to govern the Society's exposures to climate risk and establishes the process for understanding, managing and disclosing climate induced risks. As part of our standard underwriting process, we carefully consider the information we receive regarding the flood risk of properties. The Society will continue to closely monitor any emerging trends in information as well as the regulatory requirements relating to property.

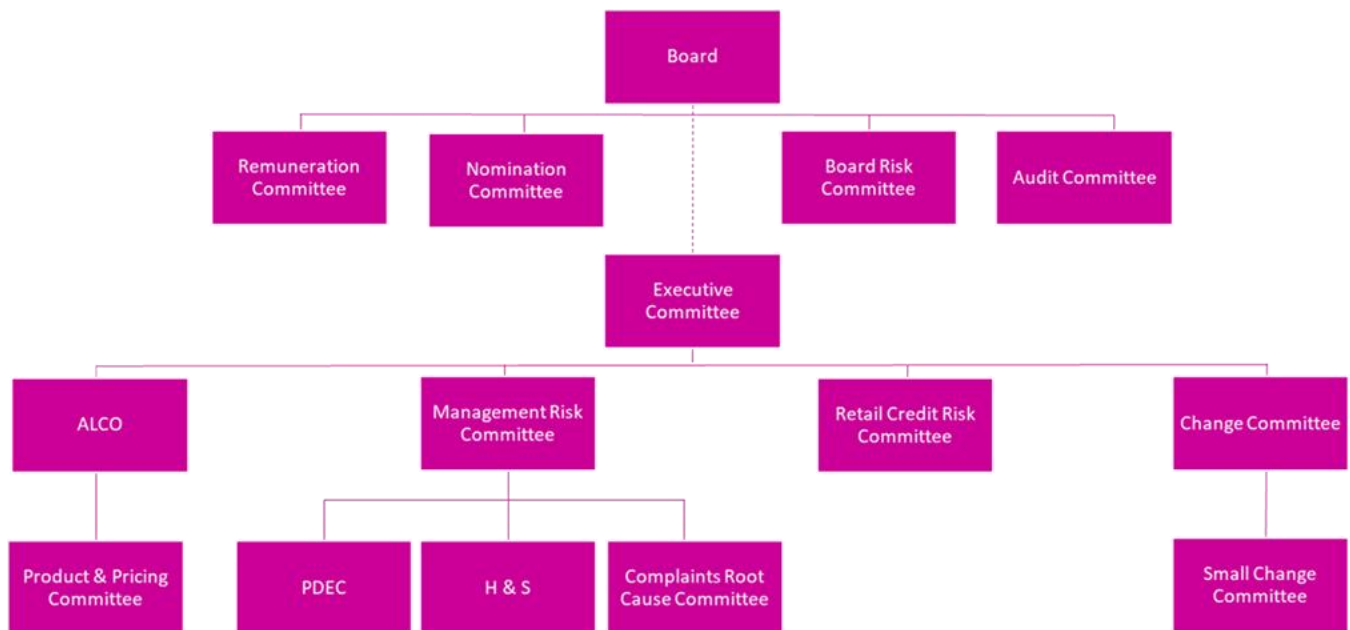
The Society also undertakes climate related stress testing as part of the ICAAP to assess the impact from selected transitional and physical risks to the Society's lending portfolio. This analysis highlighted that there were no significant material capital add-ons required from the scenarios in question. In 2022, the Society will continue to develop the Climate Risk Framework further and to identify further risks and mitigating strategies.

2.2 Main Board and Committee Structure

2.2.1 Board of Directors

The Society's Board of Directors comprises two Executive Directors and six Non-Executive Directors.

The Board governance and committee framework is as shown below:



From a risk management perspective there are two Board appointed committees which report directly to the Board; the Board Risk Committee and Audit Committee.

In addition the Group's Assets and Liabilities Committee (ALCO) chaired by the Finance Director, the Management Risk Committee and Retail Credit Risk Committee, both Chaired by the Chief Risk Officer, provide reports to the Board Risk Committee with all three comprised of Executives and members of the Senior Management team.

2.2.2 Audit Committee

Composition: Three Non-Executive Directors

The Audit Committee comprises only Non-Executive Directors in order to maintain independence which is crucial in assessing the work of Management and the assurance provided by the Internal and External Audit functions. The Committee invites Executive Directors together with representatives from the Internal and External Auditor to attend the meetings and also regularly meets with the Internal and External Auditor and the Society's Chief Risk and Compliance Officers independently.

Main Functions: The key roles and responsibilities delegated to the Committee by the Board are to:

- monitor the integrity of the Society's external financial reporting, including reviewing significant financial reporting judgements made by Management to ensure that they are appropriate
- providing advice to the Board on whether the Annual Report & Accounts, taken as a whole, is fair, balanced and understandable, and provides the information necessary for members to assess the Society's position and performance, business model and strategy
- review the effectiveness of the Society's internal controls and risk management systems
- ensure that there are satisfactory whistleblowing arrangements to enable employees to raise any concerns about possible improprieties and that there are effective arrangements for investigation of any such concerns

- monitor and review the activities and performance of both Internal and External Auditor's and the Society's Compliance function.

The Audit Committee meets on a quarterly basis, with additional meetings held as required to approve the Annual Report & Accounts.

2.2.3 Board Risk Committee

Composition: Non-Executive Directors, Finance Director and Chief Risk Officer

Main Functions: The Committee's main roles are:

- advise the Board on risk appetite, which is the amount of risk the Society is willing to take in pursuit of its strategic objectives
- regularly assess the principal risks facing the Society
- advise the Board on current risk exposure and future risk strategy
- monitor the risk profile and key limits against the prescribed risk appetite
- monitor and review the effectiveness of the risk framework to ensure that key risks are identified and appropriately managed
- ensure the Risk function is adequately resourced to perform effectively
- provide technical reviews of key policies and critical documents.

2.2.4 Nomination Committee

Composition: Non-Executive Directors, Chief Executive

Main Functions: The Committee's main roles are:

- review and recommend the structure, size and composition of Board
- advise Board on succession planning for senior roles
- review leadership requirements of the organisation and oversee recruitment and selection process of Board appointments including identification of suitable candidates
- recommend to Board on the appointments and removal of roles with SMF responsibilities
- oversee performance appraisal of Executives and evaluate Directors' performance evaluation process
- oversight and evaluation of SMF functions and prescribed responsibilities
- approval and re-election of Directors
- provide oversight of compliance with relevant regulatory requirements and reporting of any significant issues to Board
- approval of Diversity Policy
-

2.2.5 Remuneration Committee

Composition: Four Non-Executive Directors

Main Functions: The Committee's main roles are:

- review and recommend the Board Statement on Remuneration, including incentive schemes, and ensuring compliance with relevant regulatory requirements
- agree list of staff covered by the relevant codes
- monitor the Society's employment packages and ensure they comply with relevant codes
- oversee performance appraisal of Executives and evaluate Directors' performance evaluation process
- oversight and approval of Executive performance and remuneration
- review of Society workforce remuneration and alignment with culture

2.2.6 Assets and Liabilities Committee (ALCO)

Composition: Chief Executive, Finance Director (Chair), Chief Risk Officer, Marketing and Sales Director, Group Treasurer, Balance Sheet Lead, Head of Commercial Finance, Head of Mortgages, Head of Savings with one Non-Executive Director.

Main Functions: The Committee is an executive decision making committee whose decisions and recommendations are reported to the Board on a monthly basis. The principal objective of the Committee is:

- to ensure that the Society's overall objectives with regard to liquidity, funding and interest rate risk are appropriately managed, controlled and aligned with Corporate Plan objectives and risk appetites
- to review the Society's treasury activity and the current and proposed strategy and limits for liquidity, wholesale funding and hedging activities
- to ensure that the Group complies with Society and Regulatory limits
- to implement and control Board approved liquidity risk appetite and pricing policy across all business lines.

The Committee receives a variety of reports to enable it to discharge the above mentioned responsibilities and meets at a minimum on a monthly basis and more frequently when necessary.

2.2.7 Management Risk Committee

Composition: Chief Risk Officer (Chair), Chief Compliance Officer, Operations & Change Director, Marketing & Sales Director, Head of HR, Chief Information Officer, Head of Financial Change, Operational Risk Manager and Planning & Control Lead.

Main Functions: The Committee is a management committee that provides oversight over the Society's Operational, Conduct and Strategic Risk profile:

- to receive, review and challenge Operational and Conduct Risk MI to ensure that the risks are managed within the Board's Risk Appetite and the Society's risk limits
- to review and consider any proposed changes to the Society's controls and recommend any material changes to the Executive Committee
- to review the Operational Risk and Conduct Risk policies (and any supporting policies) and recommend any changes to the Board Risk Committee.

The Committee receives a variety of reports to enable it to discharge the above mentioned responsibilities and meets at a minimum six times a year and more frequently when necessary.

2.2.8 Retail Credit Risk Committee

Composition: Chief Risk Officer (Chair), Operations & Change Director, Credit Risk Manager, Head of Financial Change, Head of Corporate Finance, Broker Hub Lead, Head of Mortgage Strategy and Senior Underwriter.

Main Functions: The Committee is a management committee that provides oversight over the Society's Credit Risk profile:

- to receive and challenge credit risk MI to ensure that the credit risks are managed within the Board's Risk Appetite and the Society's risk limits
- to monitor the performance of the Society's underwriting controls and the management of arrears
- to review the Credit Risk Policy and any proposed changes to the key underwriting controls and/or new products and where appropriate recommend these to the Board Risk Committee and/or Board for approval.

The Committee receives a variety of reports to enable it to discharge the above mentioned responsibilities and meets at a minimum on a monthly basis and more frequently when necessary.

3. Capital Resources

3.1 Overview of RWAs and Minimum Pillar 1 Capital Requirements

	Risk Weighted Assets		Minimum Pillar 1 Capital Requirements	
	Dec 21	Dec 20	Dec 20	Dec 20
	£m	£m	£m	£m
Credit Risk (excluding counterparty credit risk)	369.2	341.9	29.5	27.2
of which standardised approach	369.2	341.9	29.5	27.2
Counterparty credit risk (CCR)	1.7	2.0	0.1	0.2
of which standardised approach for credit risk	1.7	2.0	0.1	0.2
Operational Risk	29.5	28.3	2.4	2.3
of which basic indicator approach	29.5	28.3	2.4	2.3
Amounts below the thresholds for deduction (250% risk weight)	1.2	3.3	0.1	0.3
Total Risk Weighted Assets and Minimum Pillar 1 Capital	401.6	375.5	32.1	30.0

Total Risk Weighted Assets (RWAs) increased by £26.1m in 2021 driven by a £50.7m increase in mortgage assets over the year, as well as increased off-balance sheet commitments.

The £26.1m RWA increase increased Pillar 1 minimum capital requirements by £2.1m.

3.2 Regulatory Capital

The Group's total capital resources as at 31 December 2021, calculated in accordance with CRD IV, are £77.8m (£72.2m: 2020) as set out in the table below:

Composition of Regulatory Capital	Dec-21	Dec-20
Common Equity Tier 1 Capital: Instruments and Reserves	£m	£m
Retained Earnings	78.0	71.0
Accumulated other comprehensive income (and other reserves)	0.0	0.0
Common Equity Tier 1 Capital before Regulatory Adjustments	78.0	71.0
Common Equity Tier 1 Capital: Regulatory Adjustments	£m	£m
Other intangibles other than mortgage servicing rights (net of related tax liability)	(1.0)	(0.6)
Total regulatory adjustments to Common Equity Tier 1	(1.0)	(0.6)
Total Common Equity Tier 1	77.0	70.4
Tier 2 Capital: Instruments and Provisions	£m	£m
Directly issued qualifying Tier 2 instruments	0.5	1.5
Provisions	0.3	0.3
Total Tier 2 Capital	0.8	1.8
Total Regulatory Capital	77.8	72.2
Total Risk Weighted Assets (RWA)	401.6	375.5

Common Equity Tier 1 (CET1) Capital £77.0m (+£6.6m in 2021)

The Group's main source of CET1 is from its General Reserves, which include the Society's retained profits accumulated since formation, plus any reported Available for Sale Reserves. The Group's Intangible Assets are deducted from its regulatory CET1.

CET1 is £77.0m as at 31 December 2021, with a £6.6m increase in the year. The Society made a profit in the year of £4.0m after tax, plus a gain on Other Comprehensive Income of £3.0m, primarily driven by an actuarial gain recognised on the FRS102 pension scheme liability. The pension scheme assets experienced an increased level of returns, partially offset by an increase in inflation expectations, and has furthermore benefitted from a switch to a lower-risk investment portfolio (see Section 2.1.2 for further detail). Intangible assets have increased by £0.4m, which offsets the CET1 measure.

There are currently no known impediments that would prevent the transfer of capital resources to Furness Building Society from its subsidiaries should the need arise.

Tier 2 Capital £0.8m (-£1.0m in 2020)

Reported Tier 2 capital includes a Subordinated Debt of £0.5m plus a £0.3m regulatory adjustment relating to Collective Impairment Provisions.

Total outstanding Subordinated Debt is £5.0m as at 31 December 2021 but is subject to £4.5m of amortisation deductions as the debt is now within five years of final maturity. The £1.0m reduction in Tier 2 in 2021 results from an additional Subordinated Debt deduction of £1.0m in the year as the instrument moves closer to final maturity.

The subordinated loan has a final maturity on 25 June 2022. The interest payment on the loan is currently calculated as the average of the largest four building societies' headline mortgage rates plus a margin of 2.25%.

	Dec-21	Dec-20
Capital Ratios and Buffers	%	%
Common Equity Tier 1 (as a % of RWAs)	19.18%	18.74%
Tier 1 (as a % of RWAs)	19.18%	18.74%
Total Capital (as a % of RWAs)	19.37%	19.23%
Institution-specific buffer requirement (as a % of RWAs)	2.50%	2.50%
Of which capital conservation buffer requirement (as a % of RWAs)	2.50%	2.50%
Of which society-specific countercyclical buffer requirement (as a % of RWAs)	0.00%	0.00%
Common Equity Tier 1 available after meeting the Society's minimum capital requirements (as a % of RWAs)	9.25%	8.96%

The Society's CET1 ratio at December 2021 is 19.18%, which is 44bp higher than December 2020 (18.74%). The main drivers behind the change over 2021 are as follows:

- RWAs increased by £26.1m in the year, driven by a £50.7m increase in mortgage assets over the year, as well as increased off-balance sheet commitments.
- CET1 capital reduced by £0.8m in the year due to a increase in retained earnings (£4.0m), Other Comprehensive Income of £3.0m and an increase in intangible assets (£0.4m).

As at 31 December 2021, the Group's Leverage Ratio was 6.51% (6.18%: 2020), which is above the current 3% regulatory minimum level.

3.3 Reconciliation of Regulatory Capital to the Annual Report

	Dec 21 (£m)
General Reserves	78.0
Available for Sale Reserve	0.0
Total Reserves in Statement of Financial Position	78.0
Intangible Assets	(1.0)
Subordinated Debt	0.5
Collective Impairment Provisions	0.3
Regulatory Capital	77.8

4. Capital Requirements

4.1 Approach to assessment of adequacy of capital

Under Pillar 1 the Group has followed the Standardised Approach permitted by CRD IV when calculating the minimum capital requirement for Credit Risk and the Basic Indicator Approach in relation to Operational Risk. This approach involves applying a regulator-defined risk based percentage requirement calculation to produce the Group's minimum Pillar 1 credit and operational risk capital requirements.

As required under Pillar 2, the Society's Board also performs a further assessment of the risks that the Group is exposed to and calculates the additional amount of capital that it considers necessary to cover these risks over and above Pillar 1 minimum requirements.

This is covered in the Society's annual Internal Capital Adequacy Assessment Process (ICAAP), which ensures that its capital resources are sufficient to support its business plan in both normal and stressed economic conditions. The ICAAP serves two key purposes:

- 1) an annual assessment of the Group's firm specific Pillar 2A risks plus a Pillar 2B forecast stress test scenario, based on its current and future risk profile as per the business plan
- 2) an assessment of the Group's ability to meet its current Total Capital requirements, provided by the Prudential Regulatory Authority (PRA), on a forecast basis.

Based on the ICAAP assessment, the Board closely monitors and controls the Society's regulatory capital levels to ensure all Pillar 1, 2 and buffer requirements set by the PRA are met. It is important that the Group maintains sufficient capital to support its ongoing activities and this requirement is an integral part of the Group's corporate planning process.

The credit risk related capital requirement for various types of mortgage lending and treasury related investments has a major influence on the Group's appetite for such exposures with limits being established and monitored on a regular basis for each type of credit exposure.

The Group undertakes regular stress testing of each major credit risk component with the results of this testing influencing business decisions on an ongoing basis.

4.2 Pillar 1 Capital Requirement - Credit Risk

The Group applies the 'Standardised Approach' to credit risk under CRD IV. The Pillar 1 credit risk capital requirement under this approach is calculated using the formula below:

- Exposure value x applicable risk weight (driven by asset type, counterparty, LTV and performing/past due status) x 8%.

The Group's minimum Pillar 1 credit risk capital requirement as at 31 December 2021 is £29.7m. The table below breaks down the capital requirement by exposure class, including a reconciliation of assets reported in the Group's Annual Report & Accounts to CRD IV reported exposures:

Exposure Class	Asset (£m)	Risk Weighted Assets (£m)	Capital (£m)
Central Government \ Central Bank	151.4	0.0	0.0
Institutions	10.3	1.7	0.1
Total Treasury Assets	161.7	1.7	0.1
Residential Retail Performing	955.3	336.9	27.0
Residential Retail Past Due	2.7	2.6	0.2
Commercial Real Estate Performing	3.8	3.7	0.3
Commercial Real Estate Past Due	0.0	0.0	0.0
Total Retail and Commercial Real Estate Assets	961.8	343.2	27.5
Other Assets	7.3	7.9	0.6
Total Assets as per Statement of Financial Position	1,130.8	352.8	28.2
Regulatory Adjustment Intangible Assets	(1.0)	(1.0)	(0.1)
Derivatives	3.7	1.8	0.1
Residential Retail - Pipeline Lending	50.1	18.5	1.5
Total Off Balance Sheet	52.8	19.3	1.5
Total Exposure Value	1,183.6	372.1	29.7

Below is a breakdown of credit risk exposures under the standardised approach by asset class and risk weight.

Asset Classes	Risk weight→										Total credit exposures amount (post ccf post crm)
	0%	10%	20%	35%	50%	75%	100%	150%	others	£m	
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Sovereigns and their central banks	151.4										151.4
Non-central government public sector entities											0.0
Multilateral development banks											0.0
Banks			8.5							1.1	9.6
Securities firms											0.0
Corporates											0.0
Regulatory retail portfolios											0.0
Secured by residential property				998.0		7.4					1005.4
Secured by commercial real estate							3.8				3.8
Equity											0.0
Past-due loans								2.7			2.7
Higher-risk categories											0.0
Other assets	0.7				3.7		5.8			0.5	10.7
Total	152.1	0.0	8.5	998.0	3.7	7.4	12.3	0.0	1.6		1183.6

4.3 Pillar 1 Capital Requirement - Operational Risk

The Group uses the Basic Indicator Approach (BIA) to calculate additional capital required to cover Operational Risk under Pillar 1. The Basic Indicator Approach requires the calculation of the Relevant Indicator as set out in Article 316 of the CRR.

The Society's Operational Risk Capital Requirement under the relevant indicator equals Net Interest and Net Non –Interest Income over the past three accounting years times 15% times 8%.

As at 31 December 2021, the Society's Pillar 1 capital requirement under the BIA for Operational Risk is £2.4m (2020 £2.3m).

4.4 Total Pillar 1 Minimum Capital Requirement

The Group's total minimum capital requirement including both credit and operational risk is £32.1m as at December 2021 (£30.0m: December 2020). The table below shows the Society's excess capital resources over the minimum Pillar 1 capital requirement at the year-end.

As at Dec 21	£m
Credit Risk	29.7
Operational Risk	2.4
Total Pillar 1 Minimum Capital Requirement	32.1
Total Capital Resources	77.8
Excess Capital over Pillar 1 Minimum Capital	45.7

The exposures in each asset class as at December 2021 and average exposures held in each class during the financial year are detailed below:

Exposure Class	Total Assets (£m)	Average Assets (£m)
Central Government \ Central Bank	151.4	159.4
Institutions	10.3	13.9
Total Treasury Assets	161.7	173.3
Residential Retail Performing	955.3	929.5
Residential Retail Past Due	2.7	2.8
Commercial Real Estate Performing	3.8	4.0
Commercial Real Estate Past Due	0.0	0.0
Total Retail and Commercial Real Estate Assets	961.8	936.4
Other Assets	7.3	6.2
Total Assets as per Statement of Financial Position	1,130.8	1,115.8
Regulatory Adjustment Intangible Assets	(1.0)	(0.8)
Derivatives	3.7	2.4
Residential Retail - Pipeline Lending	50.1	43.9
Total Off Balance Sheet	52.8	45.4
Total Exposure Value	1,183.6	1,161.2

4.5 Total Capital Requirement

The Prudential Regulatory Authority published its updated Total Capital Requirement under Pillar 2A in December 2017 which came into force from 1 January 2018. Pillar 2A Capital requirements are for risks not fully captured under the Capital Requirements Regulations.

At December 2021 the Society's Total Capital Requirement for Pillar 1 and Pillar 2A risks were £40.6m (2020 £38.5m): in-line with capital requirements set out in the 2020 SREP.

Total Capital Requirement	£m
Pillar 1	32.1
Pillar 2A	8.5
Total	40.6

Note the Group holds sufficient CET 1 Capital to meet all of its Total Capital Requirement and regulatory capital buffers – see section 3.2 for further details on capital ratio surplus to minimum capital and buffer requirements.

4.6 Countercyclical Capital buffer

The Society's Total Exposure Value of £1,183.6m is geographically concentrated as depicted in the table below. The Countercyclical buffer rate is 0% as at December 2021, following the action taken on 11 March 2020 as part of a package of financial measures introduced to support the economy though the effects of the Covid-19 pandemic. On 13 December 2021, the Financial Policy Committee announced that the Countercyclical buffer rate will increase to 1.0% on 13 December 2022.

The Countercyclical buffer requirement equates to nil as at December 2021.

Geographical Breakdown - Dec 19	Countercyclical capital buffer rate	Exposure Value (£m)	Risk weighted assets (£m)	Bank specific countercyclical buffer rate	Countercyclical buffer amount (£m)
U.K.	0.0%		401.6	0.0%	-
			-		
Total	0.0%	-	401.6	0.0%	-

4.7 Leverage Ratio

In addition to the risk based Pillar 1 capital requirements detailed above, CRD IV also requires firms to calculate a simple, non-risk based Leverage Ratio. The ratio is calculated as Tier 1 capital resources divided by total exposures, expressed as a percentage.

As at 31 December 2021, the Group's Leverage Ratio was 6.51%, (6.18%: 2020) above the current 3% regulatory minimum level. The Society's Leverage Ratio increased due to Tier 1 Reserves increasing by 9.4% (£6.6m) whilst asset exposures increased by 3.9% (£44.9m) due to Mortgage Asset growth of £50.7m and an increase in off-balance sheet mortgage commitments. The breakdown of leverage exposure values and ratio as at December 2021 are shown below:

	2021	2020
Summary comparison of accounting assets vs leverage ratio exposure	£m	£m
Total consolidated assets as per published financial statements	1,130.8	1,100.7
Adjustments for derivative financial instruments	3.7	1.0
Adjustments for off balance sheet items (converted to credit equivalents)	50.1	37.6
Other Adjustments	(1.0)	(0.6)
Leverage Ratio Exposure Measure	1,183.6	1,138.7
Leverage Ratio common disclosure template	£m	£m
On Balance Sheet Exposures	1,130.8	1,100.7
Asset amounts deducted in determining Basel III Tier 1 Capital	(1.0)	(0.6)
Total On Balance Sheet Exposures	1,129.8	1,100.1
Derivatives		
Replacement Cost of all derivative transactions	2.4	0.2
Add on amounts for potential future replacement costs of derivative contracts	1.3	0.8
Total derivative exposure	3.7	1.0
Other Off Balance Sheet Exposures		
Off Balance Sheet exposures at gross equivalent amounts	100.3	75.2
(Adjustments for conversion to credit equivalent amounts)	(50.2)	(37.6)
Off Balance Sheet items	50.1	37.6
Capital and Total exposure		
Tier 1 Capital	77.0	70.4
Total Exposures	1,183.6	1,138.7
Basel III Leverage Ratio	6.51%	6.18%

5. Credit and Other Financial Risks

5.1 Credit & Concentration Risk

The Group is exposed to the risk that arises from customers or counterparties failing to meet their obligations as they fall due, primarily from mortgage loans to retail and commercial customers and from liquid asset investments held by the Treasury function.

The Society's Retail Credit Risk Committee is responsible for reviewing the Group's Lending policy and recommends changes to the Society's Board Risk Committee and Board of Directors.

Risk Appetite and Credit Risk Management

The Society has a detailed Risk Appetite Statement which supports managers to translate the risk appetite into policies, limits and procedures. Credit risk is controlled through detailed policy limits and Lending policy criteria. This takes into account the different risks associated with the types of lending undertaken by the Society.

Credit risk management is embedded throughout the business and representatives from the relevant business areas attend monthly Retail Credit Risk Committee meetings. The Retail Credit Risk Committee operates under a Terms of Reference agreed by the Board Risk Committee and:

- monitors and manages the risk profile, quality and performance of new and residual mortgage assets within the Risk Appetite
- monitors and manages the Lending policy and the limits regarding the Society's internal controls and the 'Supervisory Statement'
- reviews such other credit risk related management information as considered appropriate.

The Board Risk Committee receives regular reports from the Retail Credit Risk Committee and the Board receives regular reports on the performance of the mortgage portfolio.

The Society operates a 'Three lines of Defence Model':

Primary responsibility for credit risk management and control rests with Line 1 management. Within the Operations department mortgage cases are reviewed, checked, underwritten and approved. Where the policy requires, mortgage cases will be authorised by the Executive Advances Committee. In all cases, Line 1 management is responsible for managing and controlling credit risk in line with the policies, procedures and controls.

As second line, the Risk and Compliance functions provide independent oversight of mortgage credit risk by undertaking structured sampling of a number of cases each month, plus periodic reviews of tranches of mortgage lending or of specific parts of the mortgage book. The Risk and Compliance functions also undertake compliance reviews of mortgage lending, which includes some sampling of cases.

The Risk and Compliance functions liaise on a regular basis with third line Internal Audit in order to ensure that there is adequate oversight and assurance around credit risk activities.

General Approach to Mortgage Lending

The Society's mortgage lending is principally through the intermediary channel through an on-line intermediary mortgage application system.

A centralised Underwriting team is based at the Society's Head Office. This Underwriting team is independent of the Mortgage Sales function which ensures segregation between sales and underwriting functions. Authority to approve mortgage applications is delegated by the Board.

The Society's underwriting approach is to make lending decisions which are sound, sustainable and take into account the borrower's willingness and ability to repay the amount borrowed:

- all cases are individually underwritten using credit reference data and a number of sources of evidence regarding the status of the borrower
- the Society does not use an automated application scorecard to determine lending decisions
- a detailed Lending policy sets out the Society's lending criteria for different types of lending along with the necessary evidence requirements and minimum level of approval required if a policy exception is sought
- policy criteria cover items such as income, security type, income and expenditure profile, credit history, acceptable security types, tenure and LTV.

There is monitoring within the business to ensure the loans are affordable and all lending is responsible. This is supported by Risk Management, Compliance and Internal Audit undertaking reviews of adherence to policies and regulation in accordance with the Board approved risk based plans.

The Retail Credit Risk Committee meets regularly to monitor management information and control the risks associated with the mortgage lending portfolio in order to ensure activity remains within policy and approved limits. On a monthly basis, the performance of the mortgage book against lending and risk appetite limits and mortgage arrears are considered by the Retail Credit Risk Committee and reported to the Board Risk Committee and Board.

5.1.1 Mortgage Credit & Concentration Risk

Geographic Concentration

A detailed analysis of the geographic distribution of residential and commercial mortgage lending by UK region as at 31 December 2021 is set out below. A loan is defined as past due when it is three months or more in arrears. Note the numbers below reflect notional value of loans and do not include accounting adjustments so will not fully reconcile to amounts shown in table 4.2.

Loans Secured on Residential Property Excluding Buy to Let

Geographic Area	Performing (£m)	Past Due (£m)	Total (£m)
North West	218.8	1.0	219.8
North & Midlands	176.4	0.9	177.3
London & South	274.0	0.7	274.7
Scotland	54.2	0.0	54.2
Northern Ireland	0.0	0.0	0.0
Total	723.4	2.6	726.0

Loans Secured on Residential Property Buy to Let

Geographic Area	Performing (£m)	Past Due (£m)	Total (£m)
North West	42.5	0.1	42.6
North & Midlands	50.2	0.0	50.2
London & South	126.9	0.0	126.9
Scotland	13.6	0.0	13.6
Northern Ireland	0.0	0.0	0.0
Total	233.2	0.1	233.3

Loans Secured on Commercial Real Estate

Geographic Area	Performing (£m)	Past Due (£m)	Total (£m)
North West	3.7	0.0	3.7
North & Midlands	0.1	0.0	0.1
London & South	0.0	0.0	0.0
Scotland	0.0	0.0	0.0
Northern Ireland	0.0	0.0	0.0
Total	3.8	0.0	3.8

Maturity Analysis

A residual maturity breakdown of combined total residential, buy to let and commercial mortgage loans as at 31 December 2021 is detailed below. Values shown in the table are amortised cost including adjustments for provisions, Effective Interest Rate (EIR) and hedging.

Maturity	£m
In not more than 3 months	0.7
In more than 3 months but not more than 1 year	4.5
In more than 1 year but not more than 5 years	77.1
In more than 5 years	879.5
Total	961.8

Provisions

Management determines the Group's impairment allowances following an appraisal of all outstanding mortgages, liquid asset investments and other assets:

- the Group measures the amount of impairment loss by applying estimated loss factors based on the Group's experience of default, loss emergence periods, the effect of changes in house prices, selling costs and any adjustment for the expected forced sales value
- individual assessments are made of all loans and advances against properties which are in possession, or in arrears by three months or more, or are subject to forbearance activities or other significant causes of concern. Individual impairment allowances are made against those loans and advances where there is objective evidence of impairment.

An analysis of total collective and individual impairment provisions by lending type over 2021 is shown below.

	Loans Secured on Residential Property (£m)	Other Loans (£m)	Total (£m)
Individual Impairment	0.53	0.19	0.72
Collective Impairment	0.32	0.00	0.32
Total Impairment at 1 Jan 2021	0.85	0.19	1.04
Written Off			
Individual Impairment	(0.05)	0.00	(0.05)
Collective Impairment	0.00	0.00	0.00
Total 2021 Written Off	(0.05)	0.00	(0.05)
Provision Movement			
Individual Impairment	(0.15)	(0.09)	(0.24)
Collective Impairment	(0.05)	0.00	(0.05)
Total 2021 Provision Movement	(0.20)	(0.09)	(0.29)
Individual Impairment	0.33	0.10	0.43
Collective Impairment	0.27	0.00	0.27
Total Impairment at 31 Dec 2021	0.60	0.10	0.70

Mortgage related provisions have been deducted from the associated asset values shown in the statement of financial position. Provisions for potential customer compensation are shown in the statement of financial position under the caption 'Provisions for Liabilities'. At 31 December 2021 the Group did not have any provisions relating to the Group's liquid asset investments.

The statement of financial position and the related provisions for liabilities can be found in the Group's 2021 Annual Report & Accounts.

5.1.2 Market Counterparty Credit & Concentration Risk

The Society is exposed to the risk that market counterparties will fail to meet their obligations as they fall due and subsequently default resulting in a loss. Treasury credit risk primarily arises from the Society investing in liquid assets.

Credit risk generated by entering into interest rate swaps is mitigated as all OTC derivatives entered into by the Society are centrally cleared through London Clearing House (LCH) via its clearing agent Société Générale Corporate & Investment Banking (SGCIB). Counterparty credit risk is transferred from the swap counterparty to LCH which is considered to be a much higher credit quality, being majority owned by the London Stock Exchange.

Prudential regulation requires the Society to hold eligible liquidity to meet the minimum requirements of the Liquidity Coverage Ratio (LCR) plus any Regulatory Pillar 2 liquidity add-on.

Assets eligible to be included in the buffer must be high quality in order to reduce risk exposure. The range of regulatory reforms seen during the last few years has significantly improved the health of the UK Banking sector however the risk of counterparty default remains. The Society mitigates and controls the risk of counterparty default by the following means:

- liquid assets are entirely denominated in sterling
- liquidity is invested in accordance with a Board approved policy and risk appetite
- the majority of the Society's liquid assets are held in a Reserve Account with the Bank of England, or other Central Bank exposure in the form of Treasury Bills or Gilts
- limited short term deposits are held in the form of call account balances with the Society's Clearing Bank. Any exposures to bank institutions are subject to minimum credit rating requirements and limits, which are monitored daily by Treasury and reported to ALCO and Board monthly
- a limited amount of liquidity is invested in bond issues which have a AAA credit rating with all three rating agencies. This AAA status must be maintained throughout the period which the Society holds the asset.

A summary of the Group's Treasury asset credit risk as at December 2021 by exposure class and External Credit Assessment Institution (ECAI) credit rating quality steps is shown below. Note that Fitch ratings are applied in the table below:

Credit Quality	Fitch rating	Central Govern	Banks and Institutions	Building Societies	Total (£m)
1	AAA to AA-	151.4	0.0	0.0	150.1
2	A+ to A-	0.0	8.5	0.0	8.5
3	BBB+ to BB-	0.0	0.0	0.0	0.0
4	BB+ to BB-	0.0	0.0	0.0	0.0
5	B+ to B-	0.0	0.0	0.0	0.0
6	CCC+ and below	0.0	0.0	0.0	0.0
Total		151.4	8.5	0.0	159.9

A further breakdown of the Group's Treasury assets by geography is shown below:

United Kingdom	159.9
European Union	0.0
Total (£m)	159.9

An analysis of exposures to Clearing Banks and Building Societies by residual maturity as at 31 December 2021 is shown below:

Repayable on Demand	8.5
In not more than 3 Months	0.0
In more than 3 Months not more than 1 year	0.0
More than 1 year not more than 5 years	0.0
Total (£m)	8.5

5.2 Other Financial Risks

5.2.1 Interest Rate Risk in the Banking Book (IRRBB)

IRRBB is the adverse impact on the Society's future cash flows arising from changes in interest rates including:

- Economic Value (NPV) – the risk to the capital value of the Society as a result of changes in interest rates
- Earnings Risk (NII) – the risk to the Society's profitability as a result of changes in interest rates
- Basis Risk – the risk to the Society's profitability arising from non-parallel movements in net mismatch exposures to different bases
- Optionality – the risk to the Society's profit arising from the provision of embedded optionality in products such as early prepayment or access with or without penalty.

The Society is exposed to interest rate risk as a retailer of financial instruments, principally in the form of mortgage and savings products, investment in liquid assets and wholesale borrowing.

Risk control and mitigation is exercised by the following:

- Interest Rate Risk is managed within a Board approved Treasury and Financial Risk Management policy
- the Society's Board has set out clear limits and risk appetite for each aspect of Interest Rate Risk
- Interest Rate Risk is managed by the Society on balance sheet or through interest rate swaps in a manner consistent with the Building Society Act 1986.

The Society ensures compliance with risk appetite and maintains interest rate risk exposure within defined limits through monthly monitoring by the Assets and Liabilities Committee (ALCO) of the following metrics:

- Economic Value +/- 200bps parallel instantaneous yield curve shock
- Earnings +/- 100bps static simulation of earnings at risk over a 12 month period.

Sensitivity of reported reserves to +200bps interest rate movement (economic value)	£000
At 31 December 2021	1,863
Average for the period	1,408
Maximum for the period	1,863
Minimum for the period	989

Sensitivity of projected net interest income to +100bps interest rate movement (earnings)	£000
At 31 December 2021	1,030
Average for the period	836
Maximum for the period	1,030
Minimum for the period	727

The Society models a range of variations in different interest rate bases, including SONIA and Bank Base Rate.

The composition of the balance sheet is modelled in line with the five-year Corporate Plan to determine the extent to which the Society maintains control over the impact of interest rate movements through administered rate mortgage and savings balances.

The Society's balance sheet is denominated solely in sterling and as such is not directly affected by currency risk.

5.2.2 Liquidity Risk

Liquidity risk is the risk that the Society cannot satisfy the Overall Liquidity Adequacy Rule (OLAR) by having insufficient liquidity resources to meet its obligations as they fall due. These obligations include repayment of share and deposit balances and mortgage lending commitments.

Risk control and mitigation is exercised by the following means:

- continuous forecasting of cash flow requirements and assessment of retail/wholesale funding and mortgage pipeline risk
- the required amount, quality and type of liquid assets required to meet OLAR in accordance with Liquidity Risk policy, Funding policy and Board Liquidity Risk Appetite
- the Society performs regular stress testing to ensure that the Society can meet OLAR both under BAU conditions and under a range of regulatory defined liquidity stress scenarios.

5.2.3 Liquidity Coverage Ratio and Net Stable Funding Ratio

The Liquidity Coverage Ratio is a measure designed to ensure a common reporting standard for banks and building societies under the European Capital Requirements Regulation (CRR) and a key component of liquidity regulation under CRD IV.

The measure is designed to ensure that banks and building societies have sufficient high quality unencumbered liquid assets to meet a stressed liabilities outflow over a 30 day time horizon.

High Quality Assets are stocks of liquid assets which can quickly be converted into cash within the market and have an appropriate reduction in value under the measure of liquid assets to recognise realisation. The measure must meet a minimum requirement of at least 100%.

The table below sets out the Society's quarterly Liquidity Coverage Ratio during 2021.

Liquidity Coverage Ratio					
Quarter Ending	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
	£m	£m	£m	£m	£m
Liquid Assets	167.4	171.5	135	131.2	150.8
Total Net Cash Outflows	61.1	72.6	77.4	75.6	76.4
Liquidity Coverage Ratio (%)	273.8%	236.3%	174.3%	173.4%	197.3%

There was a reduction in total liquid assets during 2021 due to utilisation of surplus liquidity to fund mortgage growth during the year.

The c.£37m overall increase in retail customer deposits in 2021 has increased the net cash outflow metric, as well as lending pipeline requirements which had increased by £7.7m from December 2020 to December 2021.

The Net Stable Funding Ratio (NSFR) was introduced to reduce funding risk over a longer time horizon by requiring banks to fund their activities with sufficiently stable sources of funding in order to mitigate the risk of future funding stress. A minimum requirement of at least 100% must be maintained to meet regulatory requirements.

The table below sets out the Society's quarterly Net Stable Funding Ratio during 2021:

Net Stable Funding Ratio					
Quarter Ending	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
	£m	£m	£m	£m	£m
Available Funding	1005.1	1020.6	1025.4	1028.5	1044.8
Required Funding	682.4	690.7	713.3	708.3	702.1
Net Stable Funding Ratio (%)	147.3%	147.8%	143.7%	145.2%	148.8%

5.2.4 Asset Encumbrance

CRD IV requires firms to disclose amounts of assets encumbered and unencumbered as part of the Pillar 3 disclosure. The tables below provides a breakdown the Society's encumbered and unencumbered assets as at December 2021 including matching liabilities where relevant.

Disclosure of asset encumbrance	Encumbered assets		Unencumbered Assets	
	Carrying Amount £m	Fair Value Amount £m	Carrying Amount £m	Fair Value Amount £m
Assets of the reporting institution: Of which:	155.6	155.6	975.2	975.8
Equity instruments				
Debt securities:	0.0	0.0	10.1	10.1
of which covered bonds				
of which asset backed securities				
of which issued by general governments	0.0	0.0	10.1	10.1
of which issued by financial corporations				
of which issued by non- financial corporations				
Other Assets including mortgage loans	155.6	155.6	965.1	965.3

Sources of Encumbrance	Matching liabilities ,contingent liabilities or securities lent (£m)	Assets , collateral received and own debt securities issued (other than covered bonds and ABS) encumbered (£m)
Carrying amount (£m)	91.1	155.6

As at December 2021, the Society has £155.6m of assets encumbered and comprises:

- £150.9m of mortgage assets pledged to the Bank of England to support both Term Funding Scheme borrowings and to support contingent liquidity drawdowns if required. Note the Society has £90m of Term Funding Scheme borrowing as at December 2021.
- £4.7m of cash collateral posted to LCH clearing house in support of interest rate swaps.

6. Remuneration

The Group's Senior Management remuneration policy is aligned with FCA regulations, to attract and retain suitably qualified and competent individuals who have the motivation and ability to ensure the Group's continuing success.

The Remuneration Committee determines the level of remuneration for Executive Directors and the Senior Management team which is reviewed annually taking into account rates and benefits paid by comparable organisations, together with individual responsibilities, experience, expertise and overall contribution.

The Remuneration Committee is made up of four Non-Executive Directors, including the Chair of the Risk Committee. The Chief Executive and Chief Compliance Officer also attend except when the Chair concludes that the matter under discussion is sensitive. The meeting is chaired by the Vice-Chairman. The Committee generally meets five times a year.

Executive Directors' remuneration comprises fixed and variable components, pension, benefits and other arrangements which are aligned with business strategy, its risk appetite, objectives, values and long term interests of the Society. Individual salary increases are based on the rating given to an individual's performance against their performance, behaviours and role profile at their annual review.

Executive Directors participate in an incentive scheme under which they may receive a non-pensionable bonus depending upon performance in relation to pre-determined objectives. These objectives are approved by the Remuneration Committee in line with the strategic objectives of the Group in order to incentivise them to perform at the highest levels in the interests of members and within the risk appetite of the Group.

The bonus amount varies between 0% and 40% depending on performance against a number of pre-agreed measures, approved by the Remuneration Committee. Payment of 50% of the award is deferred for three years.

The Remuneration Committee determined that, in addition to the three Executive Directors in post during all or part of 2021, six other Executives and Management are designated as being Material Risk Takers and subject to the Remuneration Code.

Fixed and variable remuneration for Material Risk Takers in relation to 2021 (including deferred elements) is set out below:

Remuneration - Dec 21	Executive Directors	Other Material Risk Takers
Total fixed remuneration (£000)	578	682
of which cash based - non deferred	525	625
of which other - non deferred	53	56
Number of Employees	3	6
Total variable remunerations (£000)	273	178
of which cash based	184	98
of which deferred	89	80
Number of Employees	3	6
Total Remuneration (£000)	851	860

Note that the Executive Directors' Remuneration information shown in page 43 of the Annual Report & Accounts includes only details relating to Executive Directors who held positions during the year. As such the Annual Report & Accounts remuneration disclosure differs to the numbers detailed in the table above due to the inclusion of individuals who held Senior Management responsibilities

during the year but were not Executive Directors (including the Chief Risk Officer and Chief Compliance Officer/Group Secretary) and other Material Risk Takers.

7. **Contacts**

In the event of queries around this document please contact one of the following:

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