Julian Hodge Bank Limited

Directors’ report and financial statements

31 October 2014

Registered number 743437

Officers and professional advisers

Directors	Keith James	O.B.E., M.A.	Chairman
	Jonathan Hodge		Deputy Chairman
	David Austin	LL.B., A.C.A.	Managing Director
	David Landen	B.Sc., F.C.C.A.	Finance Director
	Alun Bowen	M.A, F.C.A, F.R.S.A	
	Adrian Piper	B.A., M.Sc., M.C.I.P.D., M.C.I.M	

Company Secretary	Rhian Yates	B.Sc., F.C.C.A.

Registered Office
31 Windsor Place
Cardiff
CF10 3UR

Auditor
KPMG LLP
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Cardiff
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Principal bankers
Lloyds TSB Bank Plc
London

Barclays Bank Plc
Cardiff

Economic adviser
Professor Patrick Minford
Cardiff Business School

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Chairman's statement

I am pleased to present the Julian Hodge Bank Limited results for the year ended 31 October 2014.

The Bank made a pre-tax profit of £4.3 million (2013: £3.5 million), which represents a considerable improvement on the previous year and reflects our continuing investment in the business together with a more benign economic environment.

Highlights

- Pre-tax profit has increased by 23.6%.
- Tier 1 capital ratio of 25.5%.
- Increase in loans and advances of 15%
- Specific credit losses of only £54,000.
- Increase in deposits of 8.5%.

Economic Environment

The early part of the year was characterised by a tangible improvement in confidence bolstered by clear evidence that the UK was in recovery mode.

Whilst growth has been maintained throughout 2014, the second half of the year and in particular the final quarter has seen concerns being raised over its sustainability.

The eurozone continues to flirt with deflation and whilst the President of the European Central Bank utters fine words, meaningful action has been conspicuously absent.

The UK and USA remain in splendid isolation as regards economic growth amongst the major nations and the worry is that the eurozone, given its relative importance as a trading partner, more so than the USA, will drag down the UK.

This uncertainty and ebbing of confidence is manifested in the current prognosis for interest rates, with no expectation of a rise in Bank of England Base Rate before the second half of 2015. The fear factor is even more pronounced when one considers longer term rates, which have descended to levels not previously seen.

Nevertheless, if the UK is able to avoid eurozone contagion and the new government of whichever hue is elected in 2015 can get to grips with the deficit without stifling enterprise, then the future looks promising.

Financial Performance

The profit for the year has been driven by a good all-round performance from our primary business units, coupled with an improvement in commercial and residential property prices. Interest margins have increased as evidenced by a turnaround in net interest income, which became positive again having been negative for the previous two years.

I anticipate that this margin improvement will continue into 2015 if the demand for credit remains subdued. That, combined with an extension of the Bank of England's Funding for Lending Scheme for another year, will dampen the demand from banks for retail deposits.

The five-year summary highlights how the Bank has shown steady progress from the depths of the financial crisis, and, if the UK economy continues its upward trajectory, there is no reason why this trend should not continue.

Chairman's statement (*continued*)

Five Year Summary

	2014	2013	2012	2011	2010
	£m	£m	£m	£m	£m
Profit before tax	**4.3**	**3.5**	**3.1**	**2.6**	**2.1**
Total assets	**784.7**	**726.5**	**802.5**	**710.9**	**825.3**
Loans and advances to customers	**440.8**	**384.0**	**358.8**	**362.8**	**398.4**
Customer deposits	**633.2**	**583.6**	**658.9**	**579.6**	**696.2**
Shareholder's funds	**132.0**	**128.2**	**125.6**	**124.7**	**124.1**

Commercial Lending

Last year I highlighted the positive outlook for Commercial Lending and I am delighted to say that my optimism has been vindicated.

The division has produced a much improved performance as fee income has risen, driven by increased new business levels.

In common with other areas of the Bank's business, interest margins have improved as funding costs have reduced; credit losses have been minimal and commercial property prices have recovered some of their previous losses as confidence in the market has grown.

As the year progressed, we saw heightened levels of activity within our core markets with particular interest in our renewable energy funding proposition.

In order to meet demand, we have taken on more staff to ensure that we have the capacity to maintain our service levels to both new and existing clients.

At the year end we have a significant new business pipeline and a number of early stage opportunities, which augurs well for 2015.

Hodge Lifetime

Hodge Lifetime is the group's brand covering the retirement market. Our core products are pension annuities and equity release mortgages. We believe that this market offers significant growth potential, underpinned by strong demographic trends.

There is a growing trend for lending into retirement for a variety of reasons – not least because the 'Bank of Mum and Dad' continues to be called upon to help children onto, and up, the property ladder. It is also more common for people to enter retirement without having paid off their mortgage.

Late in 2013, we launched the Retirement Mortgage, aimed at a different market segment to our other equity release products. For those retirees that benefit from a reasonable level of pension income, a Retirement Mortgage offers a more flexible way of borrowing in retirement, with the interest on the loan being paid from pension income.

This product has been extremely well-received by the market and is starting to gain traction, particularly for older borrowers as there remains a lack of alternative mortgage products.

The Retirement Mortgage is funded by the Bank, and we hope that this product becomes a significant source of new business during 2015.

Residential property remains the principal form of saving for the majority of retirees and it is inevitable that a growing proportion will utilise their major asset to improve their retirement prospects through equity release, especially if their pension savings can be accessed in a flexible way.

Chairman's statement (*continued*)

Hodge Lifetime *(continued)*

Our lifetime mortgages, where interest is rolled up until death, are amongst the most flexible plans in the market, offering the ability to repay an element of the loan capital should the customer's circumstances change, and the freedom to downsize to a smaller property and repay the loan without incurring any early repayment charges. These products highlight our commitment to innovation and serving the needs of the customer.

As at 31 October 2014 the Bank also had £618 million of equity release mortgage assets under management including £397 million for other financial institutions.

We were pleased to be named the Best Equity Release Provider for the second year running at the 2014 Moneyfacts Investment, Life and Pensions awards. In addition, at the 2014 Equity Release Awards, we were named the Best Provider for Adviser Support, in recognition of our commitment to supporting the financial advice community in growing this market.

Hodge Life Assurance Company Limited, a wholly owned subsidiary of the Bank, specialises in matching pension annuity liabilities with the long-term fixed rate returns offered by traditional equity release loans. It had a successful year reporting a profit before tax of £6.9 million (2013: £14.5 million). While profit reduced year on year, the results for 2013 included elements of non-recurring profit, and after eliminating these effects, the Company has performed at a similar level to the previous year. This is despite the upheaval caused by the pension reforms announced by the Chancellor in his March 2014 Budget, which severely disrupted the pension annuity market for the remainder of the year.

Since that date, there has been much speculation as to how these reforms will take effect, coupled with further announcements from the Treasury as to proposed changes in the taxation of pensions and annuities. Whilst it remains to be seen how the UK public responds to the Budget changes, we still expect many UK retirees to want the security of a fixed income for their lifetime. The proposed changes to the taxation treatment of pension contracts offer the prospect of meaningful product innovation to better suit the needs of our customers.

Treasury and Funding

The Funding for Lending Scheme and balance sheet reduction being undertaken by some of the major banks has meant that the market for retail deposits has been reasonably soft which has allowed the Bank to improve its overall interest margin.

Whilst downward pressure on retail deposit rates is good for banks generally, it is obviously a concern for savers, whose returns have ebbed away, year after year.

In this respect, I am delighted that we have grown our deposit base by 8.5% this year having attracted many new customers to the Bank as well as retaining the loyalty of existing ones.

I would like to thank those savers, both new and old, who have supported the Bank during the year. We aim to provide all our customers with a bespoke service, specific to their requirements and plan to improve our services in 2015 to make it even easier to do business with us.

Our People

I must pay tribute to our employees, who make the Bank what it is.

We aim to provide our customers with a professional and personal service, which can only be achieved by staff who are committed to the highest standards of customer service.

In this respect I would like to thank them all for the way they have looked after our customers and contributed to the success of our business.

Chairman's statement (*continued*)

The Outlook

The fragility or otherwise of the UK's economic recovery can be debated ad infinitum. What is clear is that, across the board, confidence has returned. Employment is at record highs and whilst the productivity conundrum puzzles the economists, the man in the street is more positive.

Our business is heavily influenced by residential and commercial property prices. These have remained buoyant over the year and whilst similar improvement may be too much to ask in 2015, there is no reason to suggest that there will be any material setbacks. Indeed, the changes in stamp duty announced in the Chancellor's Autumn Statement should, if anything, bolster confidence in the residential market.

In summary, I believe that 2015 will provide the Bank with the opportunity to further enhance its reputation and performance in its key markets.

Keith James
Chairman
18 December 2014

Strategic Report

Principal activities

The Bank is principally engaged in the business of banking and equity release. Details of the principal subsidiary and its activities are set out in note 14 to the accounts.

The Bank is an Authorised Institution under the Financial Services and Markets Act 2000.

Corporate strategy

The Board has adopted a prudent strategic plan with the long term aim of achieving stable returns and modest capital growth in accordance with the requirements of its Shareholder. At the heart of the Bank's philosophy is a wish to protect its capital base for the benefit of its depositors and Shareholder by conducting business in those areas where it has the greatest expertise and experience and best understands the risks which it is taking.

A rolling five-year strategy is approved by the Board annually, complemented by a detailed business plan for the forthcoming financial year. The Board sets aside specific time during the year to review its strategy and to gauge progress towards its achievement. The current strategy is based on a continuing involvement in (a) commercial property, primarily through the Bank's commercial lending business and (b) residential property through its equity release activities, both of which it believes will enable it to achieve its strategic objectives.

Business review and future developments

A review of business and future developments is included in the Chairman's statement on pages 1 to 4.

Results and dividends

The profit for the year after taxation amounted to £4,090,000 *(2013: £3,543,000).* No dividend was paid during the year *(2013: £nil)* leaving a surplus for the year of £4,090,000 (*2013: £3,543,000)* to be taken to reserves.

Employees

The Bank has an equal opportunities employment policy, and it is the Board's policy to employ disabled persons whenever suitable vacancies arise and to provide for such employees the appropriate level of training and career progression within the Bank.

The directors recognise the importance of communication with employees and they make it their policy to be accessible to them.

Corporate governance

This statement explains the extent to which the Bank has applied the principles of good governance contained in The UK Corporate Governance Code for the year ended 31 October 2014.

The Board of the Bank comprises two executive and four non-executive directors. The roles of Chairman and chief executive are separate to ensure that neither can exercise unfettered powers of decision-making on matters of material importance to the Bank.

The Board has sought to ensure that directors are properly briefed on issues arising at Board meetings by:

- distributing papers sufficiently in advance of meetings;
- considering the adequacy of the information provided before making decisions; and
- deferring decisions when directors have concerns about the quality of information.

Strategic Report *(continued)*

Corporate governance *(continued)*

The Board is ultimately responsible for the Bank's system of internal control and for reviewing its effectiveness. The system of control is designed to manage rather than eliminate risks which are inherent in the Bank's business and can provide only reasonable and not absolute assurance against material misstatement or loss.

The Bank's system of internal financial control includes appropriate levels of authorisation, segregation of duties and limits for each aspect of the business. There are established procedures and information systems for regular budgeting and reporting of financial information. Financial reports are presented to the Board monthly detailing the results and other performance data.

There is a well-established internal audit function within the Bank that is provided by PwC on an outsourced basis. Its role is primarily to review the effectiveness of controls and procedures established to manage risk. An audit programme is agreed annually in advance with the audit committee and the head of internal audit attends each meeting of the committee to present a summary of audit reports completed during the period and to provide any explanations required by the committee.

The audit committee has reviewed the effectiveness of the Bank's system of internal financial control during the year.

Governance framework

The following is a summary of the framework for corporate governance adopted by the Bank.

The Board

The Board has ultimate responsibility for the proper stewardship of the Bank in all its undertakings. It meets regularly throughout the year to discharge its responsibilities for all important aspects of the Bank's affairs, including monitoring performance, considering major strategic issues, approving budgets and business plans and reporting to the shareholder.

A board control manual has been adopted which describes the high-level policy and decision-making arrangements within the Bank. The manual includes a schedule of matters reserved to the Board together with those items delegated to directors and Board and executive committees.

Board Committees

The Board has established the following standing committees:

- Audit committee: Adrian Piper (Chairman), Keith James, Jonathan Hodge and Alun Bowen

  All members of the audit committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chairman.

  The function of the audit committee is to review the work of the internal audit function, to consider the adequacy of internal control systems, to review the relationship with the external auditors, to review the statutory accounts and to consider compliance issues.

  The committee meets at least four times a year.

Strategic Report *(continued)*

Board Committees ***(continued)***

- Risk and conduct committee : Alun Bowen (Chairman), Keith James, Jonathan Hodge and Adrian Piper

  All members of the board risk and conduct committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chairman.

  The function of the board risk and conduct committee is to oversee the management of risk and the conduct of business on behalf of the Board to ensure that significant risks are identified, understood, assessed and managed and that good customer outcomes are achieved. It is responsible for the second line of defence of the business, ensuring that the level of assurance available to the Board is sufficient and appropriate.

  The committee meets at least four times a year.

- Remuneration and nomination committee: Jonathan Hodge (Chairman), Keith James, Alun Bowen and Adrian Piper.

  The role of this committee is twofold:

  1. To consider remuneration policy and specifically to determine the remuneration and other terms of service of executive directors and senior managers. The executive directors decide fees payable to non-executive directors.

  2. To recommend the appointment of directors to the Board and Board committees and to ensure that the Bank has an appropriate succession plan for executive and senior management positions.

  The committee meets as required.

Executive Committees

Executive management has primary responsibility for the operation of the Bank's internal financial control framework. It monitors credit risk, market risk, liquidity risk and operational risk by means of relevant committees as described below. The Bank's policy on risk management is set out on the following page.

- Group management board

  Chaired by the Managing Director the committee consists of executive management and is responsible for the formulation and execution of the Bank's strategy, and the day-to-day management of the Bank, subject to specific limitations and constraints imposed by the Board and is also responsible for formulating the IT strategy and policy and monitors and authorises IT activities throughout the Bank.

  The committee meets as required, but as a minimum will meet six times per year.

- Executive risk committee

  Chaired by the Managing Director, the committee meets quarterly and monitors the Bank's risk management framework. It also monitors and co-ordinates the activities of compliance, risk assurance and internal audit throughout the Bank.

Strategic Report *(continued)*

Executive Committees *(continued)*

- Assets and liabilities committee

  Chaired by the Managing Director, the committee implements the policies of the Board with respect to liquidity and interest rate risk management and provides recommendations to the Board on strategies for managing these risks. It also monitors and controls treasury counterparty risk arising from deposits with other banks and institutions which are usually unsecured together with debt securities acquired as investments. The committee meets weekly.

- Retail credit risk committee

  Chaired by the Managing Director, the committee's principal responsibility is to monitor and control retail credit risk throughout the Group and ensure risk underwriting is appropriate. The primary credit risk arises from loans to customers through the Hodge Lifetime division.

  The Committee meets as required, but as a minimum will meet four times a year.

- Commercial credit risk committee

  Chaired by the Managing Director, the committee's principal responsibility is the implementation and maintenance of the overall risk management framework relating to commercial credit risk. The Committee is also responsible for reviewing, challenging and if appropriate, approving credit proposals for new commercial lending deals that are within its remit as set by the Board.

  The Committee meets as required, but as a minimum will meet four times a year.

Risk Management

The Bank regards the monitoring and controlling of risk as a fundamental part of the management process and accordingly involves its most senior people in developing risk policy and in monitoring its application. The Board has agreed a risk management policy and developed a risk management framework.

The Bank operates a three lines of defence risk model for risk management and oversight. This structure clearly defines the roles and responsibilities of risk management, risk oversight and risk assurance separately from those of commercial and operational activities undertaken by the Bank. This model comprises the following elements:

First line of defence has responsibility for implementation of the Bank's strategy and for the management of risk across the organisation and comprises executive committees, management and staff.

Second line of defence relates to risk oversight and independent challenge of the first line of defence. The board has delegated oversight of risk management to the risk and conduct committee. An internal assurance team is responsible for undertaking a programme of assurance monitoring to enable the risk and conduct committee to assess whether the first line of defence is operating effectively.

The **third line of defence** provides objective assurance on the effectiveness of the Bank's governance and risk management processes and controls. This assurance is obtained via the use of internal audit services provided by PwC. The Board retains ultimate responsibility for risk management in the Bank.

Strategic Report *(continued)*

Risk Management *(continued)*

In the normal course of its business, the Bank is exposed to credit risk, liquidity risk, house price risk, interest rate risk, conduct risk and operational risk.

Credit risk is the risk that a counterparty will be unable or unwilling to meet a commitment that it has entered into with the Bank. The Bank manages its credit risk through the retail credit committee, commercial credit committee and the assets and liabilities committee. Regular credit exposure reports are produced which include information on credit and property underwriting, large exposures, asset concentrations, industry exposure and levels of bad debt provisioning.

Liquidity risk is the risk that the Bank will encounter difficulty in realising assets or otherwise raising funds to meet commitments when they fall due. The Bank manages its liquidity risk through its assets and liabilities committee, and monitors its liquidity position on a daily basis and has adopted a policy to ensure that it has adequate resources to enable it to conduct its normal business activities without interruption. The maturity analysis of assets and liabilities is disclosed in the notes to the Bank’s balance sheet.

The customer deposit base represents a stable source of funding due to the number and diversity of depositors. Liquidity is further managed through dealings in the money markets.

House price risk is the risk that arises when there is an adverse mismatch between actual house prices and those implicit in the costing of the Bank’s equity release products, such that the ultimate realisation of the property would not yield the expected return to the Bank and could, in certain circumstances, result in a capital loss.

Interest rate risk is the risk that arises when there is an imbalance between the maturity dates of rate sensitive assets, liabilities and off-balance sheet items. The Bank manages its interest rate risk through its assets and liabilities committee. The Bank’s policy is to maintain interest rate risk at a controlled level within limits set by the Board.

The table in note 24 shows an estimate of the interest rate sensitivity gap as at 31 October 2014. Assets and liabilities are included in the table at the earliest date at which the applicable interest rate can change.

The Bank enters into derivative transactions, normally interest rate swaps. The purpose of such transactions is to manage the interest rate and other risks arising from the Bank’s operations and other resultant positions. The Bank’s interest rate risk management policy defines the type of derivative transactions that can be undertaken. Further information is given in note 24 to the accounts.

Conduct risk is the risk that the Bank’s behaviour results in poor outcomes for customers. The Bank is exposed to this risk by virtue of the markets in which it chooses to operate.

Operational risk is the risk of economic loss from control failures or external events, which result in unexpected or indirect loss to the Bank.

The evaluation of the various risks and the setting of policy is carried out through the Bank’s executive risk committee which acts as the conduit through which adherence to the Bank’s risk management policy and framework is monitored.

Strategic Report *(continued)*

Going concern

The Bank's forecasts and projections include scenario testing undertaken in accordance with the Internal Capital Adequacy Process (ICAAP) and Individual Liquidity Adequacy Assessment (ILAA), which are required by the Prudential Regulation Authority to demonstrate appropriate levels of capital and liquidity respectively under stressed conditions. The directors consider that the overall level of capital, including Tier 1 capital, of £116.0m (25.5% as a percentage of risk weighted assets) and liquidity, including liquid assets (Gilts, central bank reserves and wholesale cash deposits), of £123m (19.4% of total deposits) are adequate. Accordingly the directors confirm that they are satisfied that the Bank has adequate resources to continue in business for the foreseeable future. For this reason they continue to adopt the going concern basis in the preparation of the financial statements.

Rhian Yates
Secretary

31 Windsor Place
Cardiff
CF10 3UR

18 December 2014

Directors' report

The directors present their report together with the audited financial statements for the year ended 31 October 2014.

Directors and their interests

The directors who held office during the year are listed below:

Keith James*	- Chairman
Jonathan Hodge*	- Deputy Chairman
David Austin	- Managing Director
David Landen	- Finance Director
Adrian Piper*	
Alun Bowen*	

* Non-executive

No contract was entered into by the Bank in which a director had a material interest.

Jonathan Hodge's interests in the shares of Group undertakings are shown in the Directors' Report of the ultimate UK parent undertaking, The Carlyle Trust Limited.

None of the other directors held any interest in the shares of Group undertakings.

Political contributions

The Bank made no political contributions during the year.

Disclosure of information to the auditor

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Bank's auditor is unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Bank's auditor is aware of that information.

Auditor

KPMG LLP was appointed as auditor during the year. A resolution for the re-appointment of KPMG LLP as auditor of the company and authorising audit committee to determine its remuneration is to be proposed at the forthcoming Annual General Meeting.

By order of the Board

Rhian Yates
Secretary

31 Windsor Place
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CF10 3UR

18 December 2014

Statement of directors’ responsibilities in respect of the Strategic report, the Directors’ report and the financial statements

The directors are responsible for preparing the Strategic Report, the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions, and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

KPMG LLP
3 Assembly Square
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CF10 4AX
United Kingdom

Independent auditor's report to the member of Julian Hodge Bank Limited

We have audited the financial statements of Julian Hodge Bank Limited for the year ended 31 October 2014 set out on pages 15 to 39. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the Company's member, in accordance with Chapter 3 of part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's member those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's member for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' responsibilities statement set out on page 12, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at http://www.frc.org.uk/auditscopeukprivate

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 October 2014 and of its profit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic report and the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Independent auditor’s report to the member of Julian Hodge Bank Limited
(continued)

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

• adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
• the financial statements are not in agreement with the accounting records and returns; or
• certain disclosures of directors' remuneration specified by law are not made; or
• we have not received all the information and explanations we require for our audit.

Simon Clark (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants
3 Assembly Square
Britannia Quay
Cardiff
CF10 4AX
United Kingdom

Profit and loss account
for the year ended 31 October 2014

	Note	**2014** **£000**	2013 £000 (Restated – see note 4)
Interest receivable			
Interest receivable and similar income arising from treasury bills and debt securities		**4,715**	4,493
Other interest receivable and similar income		**24,196**	23,021
		28,911	27,514
Interest payable	*5*	**(26,027)**	(29,424)
Net interest income/(expense)		**2,884**	(1,910)
Fees and commissions receivable		**2,220**	1,140
Fees and commissions payable		**(1,540)**	(330)
Other finance income	*6*	**800**	300
Other operating income:			
Rents receivable		**871**	888
Profit on sale of reversionary interests		**2,969**	2,134
Profit on sale of stock and work in progress		**705**	676
Profit on sale of treasury bills		**-**	286
Profit on sale of debt securities		**379**	488
Profit on sale of equities		**-**	4,542
Net operating income		**9,288**	8,214
Administrative expenses:			
Staff costs	*4*	**(3,509)**	(2,700)
Other administrative expenses		**(1,869)**	(1,810)
Depreciation and amortisation	*16*	**(42)**	(31)
Movement on provisions for bad and doubtful debts	*12*	**(748)**	(125)
Movement in valuation of stock and work in progress	*13*	**1,144**	(97)
Operating profit being profit on ordinary activities before taxation	*3*	**4,264**	3,451
Tax on profit on ordinary activities	*7*	**(174)**	92
Profit on ordinary activities after taxation being profit for the financial year	*22*	**4,090**	3,543

The results for the year ended 31 October 2014 relate entirely to continuing operations. There is no difference between the profit for the year and the profit on a historical cost basis.

The notes on pages 18 to 39 form part of these financial statements.

Statement of total recognised gains and losses
for the year ended 31 October 2014

	Note	2014	2013
		£000	£000
Profit for the financial year		**4,090**	3,543
Revaluation of investment properties		**305**	-
Actuarial loss recognised in the pension scheme	*26*	**(1,700)**	(1,200)
Deferred tax thereon		**340**	240
Recognition of pension scheme reimbursement asset		**900**	-
Deferred tax thereon		**(180)**	-
Total recognised gains and losses in the financial year		**3,755**	2,583

Balance sheet
at 31 October 2014

	Note	**2014**	2013
		£000	£000
Assets			
Cash and balances held at central banks	*8*	**18,503**	35,593
Treasury bills	*9*	**75,518**	78,148
Loans and advances to banks	*10*	**28,762**	25,640
Loans and advances to customers	*11 & 12*	**440,781**	384,021
		563,564	523,402
Stock and work in progress	*13*	**3,163**	4,519
Shares in group undertakings and participating interests	*14*	**15,972**	15,972
Debt securities	*15*	**85,128**	87,602
Tangible fixed assets	*16*	**645**	115
Investment properties	*17*	**9,175**	8,870
Reversionary interests in properties	*18*	**57,373**	59,360
Other assets	*20*	**47,126**	23,165
Corporation tax		**-**	803
Prepayments and accrued income		**2,525**	2,697
Total assets		**784,671**	726,505
Liabilities			
Amounts owed to credit institutions and central banks		**10,000**	5,000
Customer accounts	*19*	**633,232**	583,587
Other liabilities:			
Other		**1,409**	1,411
Accruals and deferred income		**5,176**	6,128
Pension deficit	*26*	**2,880**	2,160
Total liabilities		**652,697**	598,286
Share capital and reserves			
Called-up share capital	*21*	**100,000**	100,000
Profit and loss account	*22*	**33,118**	29,668
Revaluation reserve	*22*	**(1,144)**	(1,449)
Shareholder's funds	*22*	**131,974**	128,219
Total liabilities and shareholder's funds		**784,671**	726,505
Memorandum items			
Commitments	*23*	**150,610**	141,578

These financial statements were approved by the Board of directors on 18 December 2014 and were signed on its behalf by:

David Austin
Director

David Landen
Director

Notes

(forming part of the financial statements)

1 Accounting policies

Basis of preparation

Except as noted below, the financial statements have been prepared in accordance with the provisions of section 396 of the Companies Act 2006, including applying the requirements set out in Schedule 2 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 relating to banks. The financial statements have been prepared in accordance with applicable UK accounting standards and under the historical cost accounting rules as modified to include the revaluation of certain assets and investments and comply with the revised Statement of Recommended Practice (SORP) issued by the British Bankers' Association (BBA).

Under FRS1 the Bank is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the Bank in its own published consolidated financial statements.

The Bank is exempt by virtue of section 400 of the Companies Act 2006 from the requirement to prepare group financial statements. These financial statements present information about the Bank as an individual undertaking and not about its group.

Going Concern

The Bank's forecasts and projections include scenario testing as carried out in accordance with the Internal Capital Adequacy Process (ICAAP) and Individual Liquidity Adequacy Assessment (ILAA), which are processes required by the Prudential Regulatory Authority to demonstrate appropriate levels of capital and liquidity respectively under stressed conditions. The directors consider that the overall level of capital, including Tier 1 capital of £116.0m and liquid assets, (made up of Gilts, central bank reserves and wholesale cash deposits) of £123m are adequate. Accordingly the directors confirm that they are satisfied that the Bank has adequate resources to continue in business for the foreseeable future. For this reason they continue to adopt the going concern basis in the preparation of the financial statements.

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements, except as noted below.

Shares in group undertakings and participating interests

Investments in subsidiary undertakings and participating interests are stated at cost less provision for impairment in value.

Treasury bills

Treasury bills intended for use on a continuing basis in the Bank's activities are classified as treasury bills and are stated at cost adjusted for any amortisation of premiums and discounts arising on acquisition and less provision for any permanent impairment in value.

Where dated treasury bills have been purchased at a premium or discount, the premiums and discounts are amortised through the profit and loss account from the date of purchase to the date of maturity on a straight line basis.

Debt securities

Debt securities intended for use on a continuing basis in the Bank's activities are classified as debt securities and are stated at cost adjusted for any amortisation of premiums and discounts arising on acquisition and less provision for any permanent impairment in value.

Where dated debt securities have been purchased at a premium or discount, the premiums and discounts are amortised through the profit and loss account from the date of purchase to the date of maturity on a straight line basis.

Notes *(continued)*

1 Accounting policies *(continued)*

Loans and advances

Loans and advances are held at cost less provisions. Provisions against loans and advances to customers are based on the record of payments received and, where appropriate, the security held. Specific provisions have been made against amounts which are considered irrecoverable in respect of all identified impaired advances. General provisions have been made in respect of losses inherent in the portfolio at a fixed percentage of gross debtors excluding unearned interest. If the collection of interest is considered doubtful, it is suspended and excluded from interest income in the profit and loss account. Loans and advances are written off to the extent that there is no longer any realistic prospect of recovery.

Fees and commissions receivable

Fees and commissions receivable for services provided are recognised when earned. Fees and commissions which increase the yield on transactions are spread over the lives of the underlying transactions on a systematic basis.

Off balance sheet instruments

The Bank's policy is to hedge against mismatches when it is appropriate or prudent to do so by the use of interest rate swaps. The related costs are recognised in the profit and loss account within interest payable.

Tangible fixed assets and depreciation

Depreciation in respect of tangible fixed assets is provided to write off the cost less residual value on a straight line basis over estimated useful lives as follows:

Fixtures, fittings and equipment	-	5 years
Short leasehold improvements	-	term of lease

Investment properties

Design and construction management expenses together with interest incurred in respect of investment properties in the course of development are capitalised until the building is effectively completed and available for letting. Thereafter they are charged to the profit and loss account.

In accordance with SSAP 19:

- investment properties are revalued annually and surpluses or deficits are transferred to a revaluation reserve unless a deficit on an individual property is considered permanent. In this case the deficit is charged to the profit and loss account and any subsequent reversal is credited to the profit and loss account in the period in which it arises; and
- no depreciation is provided in respect of freehold investment properties.

This treatment, as regards certain of the Bank's investment properties, may be a departure from the requirements of the Companies Act concerning depreciation of fixed assets. However, these properties are not held for consumption but for investment and the directors consider that systematic annual depreciation would be inappropriate. The accounting policy adopted is therefore necessary for the financial statements to give a true and fair view. Depreciation is only one of the many factors reflected in the annual valuation and the amount which might otherwise have been shown cannot be separately identified or quantified.

The investment properties are formally valued approximately every 3 years by professional valuers, and desktop valuations are used in the intervening years.

Notes *(continued)*

1 Accounting policies *(continued)*

Reversionary interests in properties

Reversionary interests in properties are included in the financial statements at cost, being the amount of the cash advanced to the customer together with related acquisition costs. The cash advance reflects the then current market value of the property, as reduced by the impairment to market value arising from the existence of a lease for life for the customer.

The provision for impairment and the current market value of the properties are reviewed on an annual basis. Any deficit below the initial advance is provided for in the profit and loss account. The profit on sale of reversionary interests is calculated as the difference between the net sale proceeds and cost, less any impairment.

Stock

The Bank's stock comprises land and work in progress and is stated at the lower of cost and net realisable value.

Net realisable value means estimated selling price less all further costs to completion and all costs to be incurred in marketing, selling and distribution.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Related party disclosures

As the Bank is a wholly owned subsidiary of The Carlyle Trust Limited it has taken advantage of the exemption under FRS 8 from the requirement to disclose transactions and balances with other wholly owned subsidiaries in the same group or investees in that group.

Notes *(continued)*

1 Accounting policies *(continued)*

Pension scheme

The Bank and its subsidiary undertakings are participating employers in The Carlyle (1972) Pension and Life Assurance Scheme, a defined benefits scheme operated by The Carlyle Trust Limited. The assets of the scheme are held separately from those of the Bank.

In respect of the above scheme, the pension costs charged against profits are based on an actuarial method and actuarial assumptions designed to provide the anticipated pension costs over the service lives of the employees and directors in the scheme, in a way that seeks to ensure that the regular pension cost represents a substantially level percentage of the current and expected future pensionable payroll in the light of current actuarial assumptions. Variations from regular costs are spread over the remaining service lives of current employees in the scheme.

Pension scheme assets are measured using market values. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability.

The pension scheme surplus (to the extent that it is recoverable) or deficit is recognised in full. The movement in the scheme surplus/(deficit) is split between operating charges, finance items and, in the statement of total recognised gains and losses, actuarial gains and losses.

Reimbursement right on pension deficit

The Bank has recognised a reimbursement right in respect of its pension scheme deficit (see note 20). The obligation falls to the Bank's immediate parent, The Carlyle Trust Limited. The recognition of part of the change in value of the reimbursement right asset within the statement of total recognised gains and losses (the STRGL) is a departure from the requirement of FRS 3 Reporting financial performance, that gains and losses may be excluded from the profit and loss account and recognised instead in the STRGL only if they are specifically permitted or required to be taken directly to reserves. Since the change in value of the pension obligation to which the reimbursement right relates is required by FRS 17 to be recognised in part in the STRGL, in the opinion of the directors it would not give a true and fair view of the company's result for the year for the entire change in value of the reimbursement right asset to be recognised in the profit and loss account. As a result, an actuarial gain of £900,000 (2013: £nil) has been recognised in the STRGL rather than in the profit and loss account.

Funding for lending scheme (FLS)

In order for the Bank to access funding from the FLS, mortgages and covered bonds have been pledged as collateral. Where the risk and reward of ownership of the collateral remains with the Bank they are retained on balance sheet. The interest receivable on these assets continues to be accounted for as earned on an accruals basis. Treasury bills borrowed under the FLS are not recognised on the balance sheet when substantially all the risks and rewards of the ownership remain with the lender. The interest cost of borrowing the treasury bills is accrued on a straight line basis over the drawdown period.

Notes *(continued)*

2 Segmental information

All material activities are in respect of banking and are carried on within the United Kingdom.

3 Profit on ordinary activities before taxation

	2014	2013
	£000	£000
Profit on ordinary activities before taxation is stated after charging:		
Remuneration of the auditor and its associates		
Audit of these financial statements	**25**	21
Audit of financial statements of subsidiaries pursuant to legislation	**25**	21
Other services relating to taxation	**26**	27
Other advisory services	**11**	10
Pension scheme audit	**8**	8
Depreciation	**42**	31
Bad debt provision charge	**824**	1,179
Hire of vehicles under operating leases	**21**	32

Notes *(continued)*

4 Directors and employees

	2014	2013
	£000	£000
		(Restated)
Staff costs		
Wages and salaries	**2,919**	2,157
Social security	**268**	250
Pension costs (note 26)	**322**	293
	3,509	2,700

Certain intercompany recharges, amounting to £778,000, from the Bank to its principal subsidiary undertaking have been reclassified from staff costs to other administrative expenses in the prior year as, in the opinion of the directors, the new presentation better reflects the nature of the costs incurred.

The average number of employees of the Bank during the year was as follows:

	2014	2013
	No	No
Provision of finance and banking	**51**	49
Property, investment and other	**42**	27
	93	76

Staff costs include remuneration in respect of directors as follows:

	2014	2013
	£000	£000
Fees	**186**	174
Aggregate emoluments as executives	**332**	281
	518	455

The emoluments of the highest paid director, excluding pension contributions, were as follows:

Aggregate emoluments	**219**	188

The highest paid director is a member of a defined benefit scheme under which his accrued pension at the year end was £57,439 *(2013: £53,000).*

Retirement benefits are accruing to 2 *(2013: 2)* directors in a defined benefit scheme.

5 Interest payable

	2014	2013
	£000	£000
Swap interest payable	**13,668**	12,892
On customer accounts	**12,359**	16,528
On amounts owed to parent and fellow subsidiary undertakings	**-**	4
	26,027	29,424

Notes *(continued)*

6 Other finance income

	2014	2013
	£000	£000
Expected return on pension scheme assets (note 26)	**1,400**	1,300
Interest on pension scheme liabilities (note 26)	**(1,100)**	(1,000)
Past service benefit	**500**	-
Net finance income	**800**	300

7 Tax on profit on ordinary activities

Analysis of charge in year

	2014		2013	
	£000	**£000**	£000	£000
UK corporation tax				
Current tax on income for the year		**362**		(1,205)
Adjustments in respect of prior years		**(343)**		230
Total current tax		**19**		(975)
Deferred tax (see note 20)				
Origination/reversal of timing differences	**(19)**		1,035	
Deferred tax movement on pension scheme	**160**		100	
Adjustment in respect of prior years	**14**		(252)	
		155		883
Tax on profit on ordinary activities		**174**		(92)

The current tax charge for the year is lower (*2013: lower)* than the blended rate of corporation tax in the UK. The differences are explained below.

	2014	2013
	£000	£000
Current tax reconciliation		
Profit on ordinary activities before tax	**4,264**	3,451
Current tax at 21.83% *(2013: 23.42%)*	**931**	808
Effects of:		
Expenses not deductible for tax purposes	**3**	36
Capital allowances for the year in excess of depreciation	**(51)**	(47)
Release of provisions not deductible until paid	**129**	(867)
Adjustments in respect of prior years	**(343)**	230
Pension contributions	**(175)**	(71)
Non-taxable gain on sale of investments	**-**	(1,064)
Brought forward losses utilised	**(58)**	-
Movement in market value of treasury bills	**(417)**	-
Total current tax charge/(credit) (see above)	**19**	(975)

Notes *(continued)*

7 Tax on profit on ordinary activities (continued)

A reduction in the rate from 23% (effective 1 April 2013) to 21% (effective from 1 April 2014) and 20% (effective from 1 April 2015) were substantively enacted on 2 July 2013. This will reduce the company's future current tax charge accordingly.

The deferred tax at 31 October 2014 has been calculated based on the rate of 20% which was substantively enacted at the balance sheet date.

8 Cash and balances held at central banks

	2014	2013
	£000	£000
Repayable on demand	**18,503**	35,593

9 Treasury bills

	2014	2013
	£000	£000
Listed on a UK recognised investment exchange	**75,518**	78,148

Maturity analysis	**2014**	2013
	£000	£000
Between three months and one year	**1,000**	3,017
More than one year but less than five years	**10,786**	9,439
Five years and over	**63,732**	65,692
	75,518	78,148

Of this amount £49,641,000 has been provided as collateral for derivative financial instruments (see note 24)

	Nominal value	**Net premium/(discount)**	**Net book value**
	£000	**£000**	**£000**
Movement			
At beginning of year	77,634	514	78,148
Additions	-	-	-
Disposals	-	-	-
Redemptions	(2,500)	(81)	(2,581)
Amortisation of premium	-	(49)	(49)
At end of year	**75,134**	**384**	**75,518**

Market value	**2014**	2013
	£000	£000
Listed on a UK recognised investment exchange	**81,910**	81,591

Notes *(continued)*

10 Loans and advances to banks

	2014 £000	2013 £000
Repayable on demand	**28,762**	25,640

11 Loans and advances to customers

	2014 £000	2013 £000
Loans and advances	**425,278**	357,513
Amounts owed by immediate parent and fellow subsidiary undertakings	**15,503**	26,508
	440,781	384,021

Loans and advances to customers other than immediate parent and fellow subsidiary undertakings are repayable as follows:

	2014 £000	2013 £000
Within three months	**47,241**	51,422
Between three months and one year	**35,010**	48,414
Between one and five years	**56,006**	62,401
Over five years	**292,858**	202,901
General and specific bad debt provisions (note 12)	**(5,837)**	(7,625)
	425,278	357,513
Of which repayable on demand or at short notice	**25,889**	15,720

Of this amount £54,691,000 has been pledged as collateral under the Funding for Lending Scheme

Notes *(continued)*

12 Provisions for bad and doubtful debts

2014

	Total	Specific	General
	£000	**£000**	**£000**
At 1 November 2013	**7,625**	**5,569**	**2,056**
Charge against profits	**824**	**130**	**694**
Amounts written off	**(2,612)**	**(2,612)**	**-**
At 31 October 2014	**5,837**	**3,087**	**2,750**

The charge above excludes a recovery of £76,000 of an amount previously written off.

2013

	Total	Specific	General
	£000	£000	£000
At 1 November 2012	21,545	17,030	4,515
Charge/(release) against profits	1,179	3,638	(2,459)
Amounts written off	(15,099)	(15,099)	-
At 31 October 2013	7,625	5,569	2,056

The charge above excludes a recovery of £1,054,000 of an amount previously written off.

	2014	2013
	£000	£000
Loans and advances for which interest is suspended:		
Loans and advances before specific provisions	**12,317**	11,197
Loans and advances after specific provisions	**9,303**	5,569

Notes *(continued)*

13 Movement in valuation of stock and work in progress

2014	Total £000
At 1 November 2013	**4,519**
Additions	-
Disposals	(2,500)
Movement in valuation	1,144
At 31 October 2014	**3,163**

14 Shares in group undertakings and participating interests

	Investments in subsidiary undertakings £000
Cost and net book value	
At beginning of year	**15,972**
At end of year	**15,972**

The Bank's principal subsidiary undertaking is as follows:

	Country of Incorporation	Principal Activity	Class and Percentage of shares held
Subsidiary undertaking			
Hodge Life Assurance Company Limited	United Kingdom	Life Assurance	100%

Notes *(continued)*

15 Debt securities

Debt securities	**2014**	2013
	£000	£000
Debt securities – listed on a UK recognised investment exchange	**85,128**	87,602

Debt securities – maturity analysis	**2014**	2013
	£000	£000
Within three months	**6,951**	-
Between three months and one year	**7,184**	-
More than one year but less than five years	**37,533**	47,955
Five years and over	**33,460**	39,647
	85,128	87,602

	Nominal value	**Net premium/(discount)**	**Net book value**
	£000	**£000**	**£000**
Debt securities – movement			
At beginning of year	85,601	2,001	87,602
Additions	11,766	16	11,782
Disposals	(8,200)	352	(7,848)
Redemptions	(6,000)	114	(5,886)
Amortisation of premium	-	(522)	(522)
At end of year	**83,167**	**1,961**	**85,128**

Of this amount £21,100,000 has been pledged as collateral under the Funding for Lending Scheme

Debt securities – market value	**2014**	2013
	£000	£000
Debt securities – listed on a UK recognised investment exchange	**89,564**	92,433

Notes *(continued)*

16 Tangible fixed assets

	Total £000	Assets under construction £000	Short leasehold improvements £000	Fixtures, fittings and equipment £000
Cost				
At 1 November 2013	896	-	65	831
Additions	576	506	-	70
Disposals	(19)	-	-	(19)
At 31 October 2014	**1,453**	**506**	**65**	**882**
Depreciation				
At 1 November 2013	781	-	65	716
Provided in the year	42	-	-	42
Disposals	(15)	-	-	(15)
At 31 October 2014	**808**	**-**	**65**	**743**
Net book value				
At 31 October 2014	**645**	**506**	**-**	**139**
At 31 October 2013	115	-	-	115

17 Investment properties

Freehold	**£000**
At 1 November 2013	8,870
Revaluation	305
At 31 October 2014	**9,175**
The historical cost of investment properties was:	
At 31 October 2014	**10,319**
At 1 November 2013	10,319

A desktop market valuation was undertaken by Savills as at 31 October 2014.

18 Reversionary interests in properties

The estimated market value of the Bank's reversionary interests in properties is £83,818,000 (*2013: £79,934,000).* If these were realised at their market value on 31 October 2014 an additional tax charge of £5,553,000 *(2013: £4,740,000)* would have arisen.

Notes *(continued)*

19 Customer accounts

	2014	2013
	£000	£000
Repayable on demand	**12,168**	13,496
With agreed maturity dates or periods of notice and repayable:		
- within three months	**247,913**	196,265
- between three months and one year	**245,627**	231,306
- between one and five years	**126,570**	140,729
- over five years	**1**	1,202
Amounts owed to parent and fellow subsidiary undertakings	**6**	-
Amounts owed to subsidiary undertakings	**947**	589
	633,232	583,587

Amounts owed to parent and fellow subsidiary undertakings and amounts owed to subsidiary undertakings have no fixed terms for repayment.

20 Other assets

	2014	2013
	£000	£000
Collateral held by swap counterparties (see note 24)	**41,124**	17,015
Other debtors	**4,364**	5,237
Deferred tax assets (see below)	**738**	913
Reimbursement asset	**900**	-
	47,126	23,165

The deferred taxation asset is calculated at 20% *(2013: 20%)* as follows:

	2014	2013
	£000	£000
Tax losses	**13**	67
Accelerated capital allowances	**267**	327
Other timing differences	**458**	519
	738	913

The unprovided deferred tax asset is £nil (*2013: £nil*).

The deferred tax asset at 31 October 2014 has been calculated based on the rate of 20%, substantively enacted at the balance sheet date.

Notes *(continued)*

21 Called up share capital

	2014	2013
	£000	£000
Allotted, called-up and fully paid:		
100,000,000 *(2013: 100,000,000)* ordinary shares of £1 each	**100,000**	100,000

22 Capital and reserves – reconciliation of movements in shareholder's funds

	Called up share capital	**Profit and loss account**	**Revaluation reserve**	**Total**
	£000	**£000**	**£000**	**£000**
Year ended 31 October 2014				
At beginning of year	**100,000**	**29,668**	**(1,449)**	**128,219**
Profit for the financial year	**-**	**4,090**	**-**	**4,090**
Actuarial loss recognised	**-**	**(1,360)**	**-**	**(1,360)**
Surplus on revaluation of investment property	**-**	**-**	**305**	**305**
Recognition of reimbursement asset (net of deferred tax)	**-**	**720**	**-**	**720**
At end of year	**100,000**	**33,118**	**(1,144)**	**131,974**

	Called up share capital	Profit and loss account	Revaluation reserve	Total
	£000	£000	£000	£000
Year ended 31 October 2013				
At beginning of year	100,000	27,085	(1,449)	125,636
Profit for the financial year	-	3,543	-	3,543
Actuarial loss recognised	-	(960)	-	(960)
At end of year	100,000	29,668	(1,449)	128,219

23 Memorandum items and interest rate contracts

	2014	2013
	£000	£000
Commitments		
Undrawn credit lines, stand-by facilities, other lending commitments and capital commitments of which:		
expiring in less than one year	**86,184**	65,903
expiring in more than one year	**64,426**	75,675
	150,610	141,578
Interest rate contracts (principal amount)		
Hedging	**411,208**	431,750

Notes *(continued)*

24 Financial instruments

Objectives and policies

The Bank’s objectives and policies on the use of financial instruments, including derivatives, are set out in the Directors’ report.

Interest rate risk

2014	Not more than three months £000	More than three months but not more than six months £000	More than six months but not more than one year £000	More than one year but not more than five years £000	More than five years £000	Non-interest bearing £000	Total £000
Assets							
Cash and balances held at central banks	18,503	-	-	-	-	-	18,503
Treasury bills	1,669	-	47	11,597	62,206	-	75,518
Loans and advances to banks	28,762	-	-	-	-	-	28,762
Loans and advances to customers	174,756	449	6,446	23,111	241,856	(5,837)	440,781
Shares in group undertakings	-	-	-	-	-	15,972	15,972
Debt securities	23,738	-	3,434	28,001	29,954	-	85,128
Investment properties	-	-	-	-	-	9,175	9,175
Reversionary interests in properties	273	689	2,769	43,184	10,458	-	57,373
Stock and work in progress	-	-	-	-	-	3,163	3,163
Other assets	42,063	-	-	-	-	5,063	47,126
Non-financial assets	-	-	-	-	-	3,170	3,170
Total assets	**289,764**	**1,138**	**12,696**	**105,893**	**344,474**	**30,706**	**784,671**
Liabilities							
Deposits by banks	10,000	-	-	-	-	-	10,000
Customer accounts	259,390	63,149	182,476	126,567	13	1,637	633,232
Other liabilities	-	-	-	-	-	4,289	4,289
Non-financial liabilities	-	-	-	-	-	5,176	5,176
Shareholder’s funds	-	-	-	-	-	131,974	131,974
Total liabilities	**269,390**	**63,149**	**182,476**	**126,567**	**13**	**143,076**	**784,671**
Off balance sheet items	**156,126**	**223,341**	**15,412**	**(12,142)**	**(382,737)**	**-**	**-**
Interest rate sensitivity gap	**176,520**	**161,330**	**(154,368)**	**(32,816)**	**(38,276)**		
Cumulative gap	**176,520**	**337,850**	**183,482**	**150,666**	**112,390**		

Notes *(continued)*

24 Financial instruments *(continued)*

2013	Not more than three months £000	More than three months but not more than six months £000	More than six months but not more than one year £000	More than one year but not more than five years £000	More than five years £000	Non-interest bearing £000	Total £000
Assets							
Cash and balances held at central banks	35,593	-	-	-	-	-	35,593
Treasury bills	55,134	1,499	1,018	9,439	11,058	-	78,148
Loans and advances to banks	25,640	-	-	-	-	-	25,640
Loans and advances to customers	188,568	2,132	8,825	25,568	164,412	(5,484)	384,021
Shares in group undertakings	-	-	-	-	-	15,972	15,972
Debt securities	17,346	645	752	29,212	39,647	-	87,602
Investment properties	-	-	-	-	-	8,870	8,870
Reversionary interests in properties	666	144	187	4,612	53,751	-	59,360
Stock and work in progress	-	-	-	-	-	4,519	4,519
Other assets	17,015	-	-	-	-	6,150	23,165
Non-financial assets	-	-	-	-	-	3,615	3,615
Total assets	**339,962**	**4,420**	**10,782**	**68,831**	**268,688**	**33,642**	**726,505**
Liabilities							
Deposits by banks	5,000	-	-	-	-	-	5,000
Customer accounts	210,193	57,709	173,393	140,501	1,202	589	583,587
Other liabilities	-	-	-	-	-	3,571	3,571
Non-financial liabilities	-	-	-	-	-	6,128	6,128
Shareholder's funds	-	-	-	-	-	128,219	128,219
Total liabilities	**215,193**	**57,709**	**173,393**	**140,501**	**1,202**	**138,507**	**726,505**
Off balance sheet items	**175,350**	**155,400**	**(3,716)**	**(73,717)**	**(253,717)**	**-**	**-**
Interest rate sensitivity gap	**300,119**	**102,111**	**(166,327)**	**(145,387)**	**13,949**		
Cumulative gap	**300,119**	**402,230**	**235,903**	**90,513**	**104,465**		

The tables above summarise the re-pricing mismatches on the Bank's balance sheet as at 31 October 2014 and 31 October 2013. Items are allocated to time-bands by reference to the earlier of the next contractual interest rate re-pricing date and the maturity date.

A negative interest rate sensitivity gap exists when more liabilities than assets re-price during a given period. Although a negative gap position tends to benefit net interest income in a declining interest rate environment, the actual effect will depend on a number of factors including the extent to which repayments are made earlier or later than the contracted dates and variations in interest rate sensitivity within re-pricing periods.

Fair values

The following table provides a comparison by category of the carrying amount and the fair values of the Bank's financial assets. The fair value is the amount at which a financial instrument could be exchanged in an arm's length transaction between informed and willing parties, other than in a forced or liquidation sale.

Notes *(continued)*

24 Financial instruments *(continued)*

Fair values *(continued)*

	Book value		Fair value	
	2014	2013	**2014**	2013
	£000	£000	**£000**	£000
Financial assets				
Treasury bills	**75,518**	78,148	81,910	81,591
Debt securities	**85,128**	87,602	89,564	91,028
Interest rate swaps	**-**	-	(90,833)	(71,769)

The Bank holds no other financial asset or liability for which a liquid and active market exists, either for the instrument itself or for its component parts. None of the Bank's financial assets or liabilities are part of a trading book.

The methods and assumptions used for determining the fair value of each category of financial instrument are:

(i) Under the Bank's accounting policy, treasury bills and debt securities are included in the balance sheet at their original cost adjusted for any amortisation of premiums and discounts arising on acquisition and less provision for any permanent diminution in value. Consequently the fair value equates to the market value of these securities at the balance sheet date.

(ii) The fair value of derivative instruments is calculated by discounting all future cashflows based upon the Bank's cost of money rate.

Hedges

As stated in its accounting policy the Bank's policy is to hedge against mismatches when it is appropriate or prudent to do so. The table below shows the amount of interest that has been included in the profit and loss account for the current year.

	2014	2013
	£000	£000
Gains	**1,861**	1,536
Losses	**(15,528)**	(14,428)
Net losses to 31 October	**(13,667)**	(12,892)

As at 31 October 2014, the Bank had a number of outstanding interest rate swap contracts that were entered into for hedging purposes. The notional losses that would have arisen had these contracts matured on 31 October 2014 amounted to £90,833,000 *(2013: £71,769,000)*. These amounts have not been recognised in the financial statements as at 31 October 2014, nor do they reflect the actual losses (if any) that will be recognised in the financial statements as these contracts mature in the future.

The collateral pledged against the market value of derivative instruments comprises interest-bearing cash deposits, which are included in Other assets (note 20), and Treasury bills (note 9). Interest on this collateral is included in the profit and loss accounts within interest receivable.

Foreign currencies

The Group holds no financial assets or liabilities denominated in foreign currencies.

CRD IV

Article 89 of the Capital Requirements Directive IV (CRD IV) requires credit institutions and investment firms in the EU to disclose annually, specifying, by Member State and by third country in which it has an establishment, the particular information on a consolidated basis for the year ended 31 October 2014. See details as disclosed at http://www.julianhodgebank.com/group/financial.asp.

Notes *(continued)*

25 Capital commitments

The Bank had contracted capital commitments amounting to £nil at 31 October 2014 *(2013: £Nil).*

26 Pension schemes

The Carlyle Trust Group operates a defined benefits pension scheme for certain directors and employees, The Carlyle (1972) Pension and Life Assurance Scheme.

The assets of the scheme are administered by Trustees and are held in a fund that is separate and independent of other Bank funds. The scheme was established with effect from 1972, is fully approved under Chapter I Part XIV of the Income and Corporation Taxes Act 1988, and is contracted-out of the State Earnings Related Pension Scheme.

Pension costs are assessed in accordance with the advice of a qualified, independent actuary using the projected unit method. The assumptions which have the most significant effect on the calculation are the long term average investment return expected in future and the rate of future increases to benefits, both before and after retirement.

The benefit basis changed to a career average revalued earnings (“CARE”) basis, from a final salary basis, with effect from 1 April 2005.

The most recent actuarial report of the scheme, as at 1 April 2013, showed that the value of the assets was £22,200,000. This represented 85% of the CARE benefits that had accrued to members after allowing for expected future increases to benefits. Future investment returns of 5.20% per annum up to retirement and 4.2% in retirement and future benefit increases of 3.6% per annum were assumed.

The Bank’s total expense for the year, including its share of prior service savings, amounted to £322,000 *(2013: £293,000)*. The employer’s contribution rate increased to 15.3% *(2013: 14.5%)*.

The FRS 17 valuation as at 31 October 2014 has been produced by a qualified independent actuary, and is based on the results of the valuation as at 1 April 2013.

Scheme assets

The fair value of the scheme’s assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the scheme’s liabilities, which are derived from cash flow projections over long periods and thus inherently uncertain, were:

	2014	2013
	£m	£m
Fair value of plan assets	**23.5**	23.0
Present value of funded defined benefit obligations	**(27.1)**	(25.7)
Deficit	**(3.6)**	(2.7)
Related deferred tax asset	**0.7**	0.6
Net deficit	**(2.9)**	(2.1)

Notes *(continued)*

26 Pension schemes *(continued)*

Movements in present value of defined benefit obligation

	2014 **£m**	2013 £m
Present value of scheme liabilities at start of the period	**25.7**	22.8
Interest cost	**1.1**	1.0
Current service cost	**0.4**	0.3
Member contributions	**0.1**	0.1
Actuarial loss	**1.1**	2.0
Benefits paid	**(0.8)**	(0.5)
Past service cost	**(0.5)**	-
Present value of scheme liabilities at end of the period	**27.1**	25.7

Movements in fair value of plan assets

	2014 **£m**	2013 £m
Market value of assets at the beginning of the year	**23.0**	21.0
Expected return on scheme assets	**1.4**	1.3
Actuarial (loss)/gain	**(0.6)**	0.8
Member contributions	**0.1**	0.1
Employer contributions	**0.4**	0.3
Benefits paid	**(0.8)**	(0.5)
Market value of assets at the end of the year	**23.5**	23.0

Income/(expense) recognised in the profit and loss account

	2014 **£m**	2013 £m
Current service cost	**(0.4)**	(0.3)
Interest cost	**(1.1)**	(1.0)
Expected return on scheme assets	**1.4**	1.3
Past service benefit	**0.5**	-
Total	**0.4**	0.0

The expense is recognised in the following line items in the profit and loss account:

	2014 **£m**	2013 £m
Other finance income	**0.8**	0.3
Staff costs	**(0.4)**	(0.3)
Total	**0.4**	0.0

The total amount recognised in the statement of total recognised gains and losses in respect of actuarial gains and losses is a loss of £1.7m *(2013: loss of £1.2m)* before tax.

Notes *(continued)*

26 Pension schemes *(continued)*

Cumulative actuarial gains/(losses) reported in the statement of total recognised gains and losses for accounting periods ended on or after 22 June 2002 and subsequently included by prior year adjustment under paragraph 96 of FRS 17, are losses of £7.8m *(2013: losses of £6.1.m)* before tax.

The fair value of the plan assets and the return on those assets was as follows:

	Fair value 2014 £m	**Long term rate of return 2014**	Fair value 2013 £m	Long term rate of return 2013
Equities	14.4	6.5%	13.1	6.5%
Bonds	2.8	4.0%	4.6	4.0%
Property	0.6	5.5%	0.5	5.5%
Other – cash	5.7	3.5%	4.8	3.5%
Total market value of assets	23.5		23.0	

The actual return on assets was 3.5% (2013: 10%)

The major assumptions used in this valuation were:

	2014	2013
Rate of increase in salaries	**4.20%**	4.30%
Rate of increase in LPI pensions in payment and deferred pensions	**3.10%**	3.20%
Rate of CARE revaluation	**2.20%**	3.20%
Discount rate applied to scheme liabilities	**4.10%**	4.40%
RPI inflation assumption	**3.20%**	3.30%

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date are based on standard actuarial mortality tables and include an allowance for future improvements in longevity as follows:

Post retirement mortality (life expectancy)	**2014**	2013
Current pensioners age 65 - male	**87.3**	87.3
Current pensioners age 65 - female	**89.5**	89.5
Future pensioners age 65 (current age 45) - males	**88.6**	88.6
Future pensioners age 65 (current age 45) - females	**91.0**	91.0

History of plan balance sheets

	2014 £m	2013 £m	2012 £m	2011 £m	2010 £m
Fair value of plan assets	**23.5**	23.0	21.0	20.0	19.9
Present value of funded defined benefit obligations	**(27.1)**	(25.7)	(22.8)	(20.8)	(20.1)
(Deficit)	**(3.6)**	(2.7)	(1.8)	(0.8)	(0.2)
Related deferred tax asset	**0.7**	0.6	0.4	0.2	0.1
Net deficit	**(2.9)**	(2.1)	(1.4)	(0.6)	(0.1)

Notes *(continued)*

26 Pension schemes *(continued)*

History of experience gains and losses

	2014	2013	2012	2011	2010
Difference between the expected and actual return on scheme assets:					
Amount	**£(0.6)m**	£0.8m	£(0.4)m	£(0.9)m	£1.5 m
Percentage of year end scheme assets	**(2.5%)**	3.5%	1.9%	4.5%	7.5%
Experience gains and losses on scheme liabilities:					
Amount	**£0.0m**	£0.0m	£0.0m	£0.0m	£0.6m
Percentage of year end present value of scheme liabilities	**0.0%**	0.0%	0.0%	0.0%	3.0%
Total amount recognised in statement of total recognised gains and losses:					
Gains/(losses) before tax	**£(1.6)m**	£(1.2)m	£(1.4)m	£(0.5)m	£0.8m
Percentage of year end present value of scheme liabilities	**(6.3%)**	4.7%	6.1%	2.4%	4.0%

The Bank expects to contribute approximately £0.4m to its defined benefit plan in the next financial year.

27 Ultimate parent undertaking

The immediate parent undertaking of the Bank is The Carlyle Trust Limited, registered in England and Wales, which controls and co-ordinates the management of a group of companies. The ultimate parent undertaking and controller is The Carlyle Trust (Jersey) Limited (incorporated in Jersey). Within the meaning of the Companies Act 2006, The Carlyle Trust Limited is the parent undertaking of the largest and only group of undertakings for which group accounts are drawn up and of which the Bank is a member. The accounts of The Carlyle Trust Limited can be obtained from The Registrar of Companies, Companies House, Crown Way, Cardiff, CF14 3UZ.

28 FSCS Levy

The Bank is a member of the Financial Services Compensation Scheme (FSCS), and it has been advised by the Prudential Regulatory Authority that it will be asked to contribute additional levies for the foreseeable future following the failure of a number of banks during the credit crunch. The FSCS has advised of an expected shortfall in the region of £800 million; this will be levied in three equal instalments between 2013 and 2015. During the year the Bank paid the third of three instalments and this is included in the current year charge.

A provision of £295,000 for Julian Hodge Bank’s estimated share of the levy remains in force at the balance sheet date *(2013: £300,000)*.