# Saffron Building Society

## Annual Report and Accounts 2010

Savings | Mortgages | Financial Advice | Insurance | Since 1849

www.saffronbs.co.uk

# Contents

# Financial Highlights

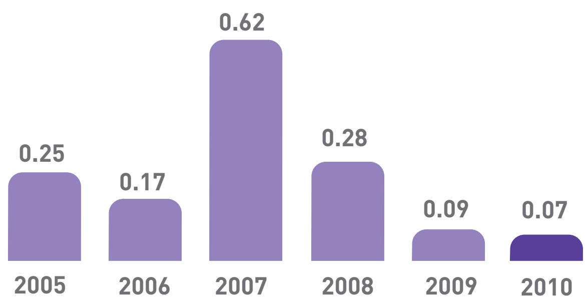
ASSETS (£m)


- Assets increased by 11.4% in the year.
- Retail balances increased by 15.2%.
- The increase in mortgage lending was fully financed through retail savings.

PROFIT BEFORE TAXATION (£m)

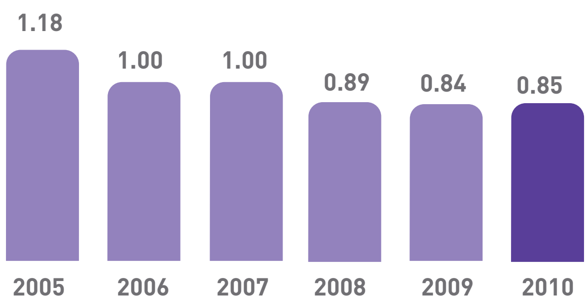

- Profit before tax of £1.1m compared to £2.0m in 2009.
- Profits reduced as a result of low interest rates which have impacted on the return on the Society's investments.
- Strong performance from the Group's other income sources.

SOCIETY ARREARS RATIO (%)




- This ratio expresses mortgage balances in arrears as a % of the total Society mortgage book. The amount at 0.07% is below the Building Societies average of 1.55%.
- The Group arrears performance (greater than 3 months in arrears by number) at 0.39% (2009: 0.57%) is below the Council of Mortgage Lenders published average at 2.15%. The amount by value has decreased from 0.57% to 0.43%.

MANAGEMENT EXPENSES RATIO (%)




- This ratio expresses management expenses of the group as a % of average assets.
- The Group ratio above shows continuing efficiencies within the Society along with a good contribution from Saffron Independent Financial Advisers Limited which was once again profitable. The Society ratio was 0.80% (2009: 0.82%).
- The level of expenses has increased in line with asset growth. The long term trend remains downward and increasing efficiency remains a core objective.

# Chairman's Report

**Peter Harrison**
Chairman

**I am pleased to be able to present the 2010 report and accounts for Saffron Building Society (the "Society"). These demonstrate the continued security and solidity of Saffron's commitment to remaining an independent and dynamic mutual Society. Since economic turmoil really came to a head in 2008, the tangible signs of improvement have been keenly anticipated and whilst it is technically true that the UK came out of recession in 2010, and that house price declines stabilised, the UK economy has remained a difficult and uncertain environment for individuals and businesses alike.**

Although 2010 was not nearly so sensational in terms of the demise of financial institutions, we have still seen a number for whom the challenges of such a fragile economic environment have proven unmanageable. However I am pleased to be able to report another strong set of results for Saffron, despite the difficult underlying market conditions. Andy Golding will comment further on economic factors, the Society's response to them and the resultant performance in his Chief Executive's report.

There are three key priorities that the Board of Saffron adheres to in setting the strategy and direction for the Society:

- Security of members' money
- Making mutuality relevant and of value to members and
- Demonstrating the very best governance and risk management.

We believe these factors are critical in running a safe, secure and yet dynamic building society. I will use these headings to frame my report.

### Security of Members' Money

This is at the very heart of the Board's priorities. We recognise the trust that members place in their Society and take the responsibility for that extremely seriously. This is why you have not seen Saffron entering complex markets such as commercial lending and why we are extremely challenging of other businesses we work with, particularly those with whom we deposit the Society's own liquid funds.

The Society has maintained excellent arrears performance across its entire mortgage portfolio and this enviable result places Saffron significantly better than the Building Societies Association and Council of Mortgage Lenders average.

Saffron remains very strong from a capital and liquidity perspective and our regular severe stress testing continues to demonstrate the Society's ability to withstand significant market stress. Despite investment during 2010 in improved IT systems, new branch premises and enhanced online savings offerings, we have continued to manage the cost base effectively against the assets of the Society.

Finally, whilst making excessive profits is not at the heart of our mutual ethos, it is important to us that we remain profitable, even in such a low interest rate climate. I am, therefore, pleased to report profits of £1.1 million after taking into account the investments we have made in improving the Society and the product range during the year.

### Making mutuality relevant and of value

It may be true that mutuals have been around for some time and Saffron of course is now 161 years old. That said we recognise the importance of taking all that is core to mutuality and continually seeking to improve its relevance in an evolving market place by getting closer to our members and looking for ways for them to have a greater say in the Society.

Andy will report in more depth on what the Society has been up to during 2010, but the communities we serve and the products we offer are all an important part of Saffron doing its bit as a regional community mutual.

The press has been full of reports of a lack of mortgages and a decline in the volume of savings, but despite this, Saffron's assets have grown by over 11% in 2010. We opened 30,000 savings accounts for both new and existing members, we have completed £144 million of new mortgage loans, our financial planning subsidiary Saffron Independent Financial Advisers has helped 256 new clients with their financial planning and Saffron Insure now looks after the home and car insurance needs of over 3,000 members.

These figures speak for themselves and when coupled with some of our innovative developments in online savings and accolades from the charity Fairbanking in the national press, it is clear to see that Saffron's commitment to relevance and value is being well received.

# Chairman's Report
(continued)

### Governance and risk management

As Chairman my duties include ensuring that the Board of Saffron Building Society demonstrates competence, challenge, knowledge of the wider issues affecting the financial services market place and most of all an understanding of the responsibilities and accountabilities required to run a member owned institution.

For these reasons Saffron is keen to retain the very best Executive Directors it can afford and the highest quality Non Executive Directors available in the market. That ethos will not change and the Board has remained strong during 2010. You may recall that at the 2010 Annual General Meeting (AGM) both Charles Wilson and John Goodfellow were elected to serve the Society and both proved to be excellent appointments in the year. However, unfortunately, after a period of serious illness John Goodfellow, resigned as a Non Executive Director. We were extremely disappointed to see John go and on behalf of the Board I wish him all the best for a full recovery and thank him for his contribution. As I write we are actively seeking a replacement who will stand for election at the 2012 AGM.

The Board operates a robust and effective committee structure to manage risk. Our Credit, Audit and Compliance, Asset and Liability and Risk Committees are attended by a selection of Non Executives and in turn report to the full Society Board to ensure that all directors are adequately informed to make strategic decisions with an understanding of the risks involved. This culture of risk management is central to our plans, again to ensure that the security of the Society and its members is paramount.

Finally from a governance perspective I stated last year that following the removal of the short term executive bonus scheme, its last payment was made in March 2010. This leaves in place the medium term incentive scheme which is deferred in payment for three years and payable subject to ongoing performance of the Society and individual. Your Board believes strongly in such a bonus scheme being available so that a proportion of overall income is at risk based on individual performance.

### Outlook

At the time of writing there is no clarity about when economic conditions may recover or indeed when interest rates may rise. However Saffron remains well able to trade its way through this challenging period and is well positioned for a rising rate environment when it eventually happens.

Everyone in the Society is committed to the mutual model and our staff have worked tirelessly during the year to deliver the very best service they can to members. I would like to thank the staff and Andy and his executive team for their unflinching commitment to keeping Saffron and its members safe and thriving in a challenging market place. I would also like to thank you, our members, for your continued loyalty to and engagement with your Society.

Peter Harrison

**Peter Harrison**
Chairman

# Chief Executive's Report

**Andy Golding**
Chief Executive

**Whilst 2008 and 2009 were historic years in financial terms for the entire global economy, for many 2010 has felt much more like a year of waiting. Waiting, for example, to see the full effects of the new Coalition Government's fiscal policies; waiting to see what would happen on house prices that increased a bit and then declined a bit; waiting on unemployment figures that have been up and down in the year. The Bank of England's Monetary Policy Committee have been waiting too, but their target of 2% core price inflation has continued to evade them whilst economists forecasts ranged from further significant down turn to a strong export led recovery. The question I have been asked more times in the year than any other is "when will interest rates go up?". The truth of the matter is no one really knows but if inflation is going to be kept under control, at some point, possibly in 2011 or at the latest early 2012, the consensus is that they will have to.**

In an uncertain environment the temptation is to do nothing. Many financial services companies have stayed under the radar, choosing to keep the hatches battened down and not embark on new strategies. But here at Saffron we reviewed our strategic plans and decided that our duty was to provide the services that members demanded of us and I would therefore describe Saffron in 2010 as very much "open for business."

I am pleased to present this year's results as a further demonstration of our clear strategy of security, community, proposition and sustainability. Peter Harrison commented in his report on our desire to remain profitable regardless of the trading conditions. This is important to us, but so is investing and shaping the business for the future, not only for today's membership but for generations of members to come.

The Board runs the Society to a balanced business scorecard, which sees us measure and manage key metrics and outputs across the four quadrants of Financial, Member and Customer, Internal Quality and Risk and Staff. I will use our balanced business scorecard headings as an agenda for providing you with more detail about how we have performed and just what the Society has been doing during 2010.

## Financial

A building society is a net saver and in normal conditions makes a significant proportion of its profit from the investment of its own liquid assets. When base rate is at 5% the actual amounts earned on over £230m of investments is a significant profit generator. Of course with base rate being at only 0.5% for the whole of 2010 the same cannot be said. Therefore running costs and profits must come from the margin on mortgage book over savings rates, coupled with other income generation. In this low rate period, we have actually sought to continually improve the offering to our savings members, whilst at the same time balancing the pricing of our mortgage offerings to attract quality mortgage borrowers.

Peter Harrison shared in his report the success that this strategy delivered in terms of new retail savings, mortgage growth and more members making use of our other services. This combined with careful cost management has enabled us to grow, invest in improving the Society and its offerings, whilst still delivering profitability in a stagnant external market place.

## Member and customer

During the year we have made a number of member focused changes to the Society. We have invested in our branch locations in both Brentwood and our new Branch Agency in Buntingford. We have improved our online functionality for users of our e-saver products. We have already received feedback that the customer experience is much better. We have completely upgraded our core IT systems and this will enable us to streamline other processes during 2011, aimed at improving the way we work for you. We have developed a number of new products for both borrowers and savers, including our innovative wedding and car savings plans, regular savings accounts, our self build mortgages, and our new style branch instant access accounts with bonuses for those who don't withdraw in a quarter. These have proved extremely popular.

We recognise that developing new products is important to ensure that we remain competitive and thanks to feedback from members we have introduced benefits for family linked products during the year and intend to enhance this further in 2011.

We seek regular feedback from members and you provide us with excellent information about where we get it right and, more importantly, where we don't. Internal ISA transfer processing was a good example of where you told

# Chief Executive's Report
(continued)

us we were just not good enough, so again we have improved our systems to make the process simpler and quicker.

As Peter Harrison alluded to, we have done a lot of new business in the year. Our savings balances grew by over £103 million and our mortgages by £144 million. We are proud to be a growing building society and keen to continually improve our product and service offerings to you.

Finally we introduced a set of promises to you during 2010:

- Membership is ownership, talk to us and we'll listen
- Safe and secure but definitely not boring
- No gimmicks, no jargon, no silly rules
- Doing good stuff in your community now and in the future
- Our staff are brilliant and we'll prove it

These promises are easy to write down, but much harder to live up to all the time, but the Board and every member of staff have signed up to them and we are all committed to continually striving to be the kind of mutual building society you want.

### Internal Quality and Risk

Risk management is central to our primary objective of protecting the security of members' money. The regulatory climate has intensified since the economic downturn began, but at Saffron we have sought to embrace and live up to the requirements as part of the culture of the business.

We have worked hard to ensure that our mortgages perform well and our arrears performance of 0.07% of Society (0.39% Group) mortgages being in arrears is a testament to that work and the quality of our underwriting and mortgage lending approach. Where borrowers have found themselves in difficulty we have worked with them and exercised as much appropriate forbearance as possible to help them stay in their home whilst they get their finances back on track.

We have received a very low level of complaints during 2010, but have treated each one extremely seriously, ensuring that we learn from mistakes and where possible make changes to our processes to prevent recurrence.

### Our staff

The Society has a good record of attracting and retaining high quality staff. Not just competent individuals, but people who understand and value mutuality and the importance of being a member owned institution.

As a mutual we have a corporate responsibility to focus on community, not just the communities in which we trade, but our community of members and stakeholders in the widest sense. During the year the staff and management have been involved in a huge number of community events to raise much needed funds for charities in and around our region. Activities ranged from bathing in mud baths to sponsored bike rides and our 118 full time equivalent staff raised in excess of £10,000 in 2010 for some wonderful causes. I should also say that many of you kindly donated or sponsored those activities, which I know is much appreciated by the staff.

You will see from our member promises mentioned earlier, that we think our staff are pretty amazing. Of course as human beings none of us can get it right all the time, but as the Chief Executive of this Society I can assure you that we are all committed to trying.

As well as physical communities, we have sought to embrace the growing communities that are evolving online. I am proud of our Facebook presence which shares information and pictures about all the good things we get up to in the community and that Saffron is the most followed building society on twitter. I also continue to write my regular blog, which seems to attract positive feedback from those that follow it.

### Final thoughts

As we enter 2011 with a continuing sense of economic uncertainty, the Board and I are clear about how we need to operate. We must continue to find ways to improve our service and product range, remember what a building society is here to do, provide savings and mortgages and associated quality products well and most of all do what the Society has done well for over 16 decades; look after your money and serve you well.

Finally I would like to thank my team and staff for making the Society what it is and you, our members for your custom and loyalty.

**Andy Golding**
Chief Executive

# Community Report

**The Society has always taken its social responsibility very seriously, but more than this, the fundamentals of mutuality are centred on a sense of community. This encapsulates our community of members, the communities we serve, the jobs we create and the partner businesses we work with. In addition the Board believes that the Society needs to strive for a positive impact on community in the widest possible sense.**

**In 2010 we introduced you to our promises. This report details how we feel we have performed against the corporate responsibility and community orientated promises in the year.**

### Membership is ownership – talk to us, and we'll listen

Members of a mutual organisation like a building society have the right to vote at the Annual General Meeting (AGM), electing directors, approving the remuneration policy and appointing auditors. At Saffron Building Society we try to involve you in other ways as well.

Our member survey last year asked for your views on whether the Society should participate in the Government Dormant Accounts Scheme which will allow building societies to re-invest the money from accounts where the owners cannot be traced and no activity has taken place for many years. You told us that you would like us to use this scheme to support regional charities.

We have listened to you and have set up Saffron Building Society Community Fund. This fund is being managed by Essex Community Foundation but decisions about which causes to support rest with the Society. We would like your help again. This time we would like you to tell us the type of charities you would like us to support. Please complete our survey and let us know what you think. This can be accessed at the end of the online voting process or by picking up a form in your local branch or agency.

Our annual member conference was replaced this year with a series of member lunches hosted by the Executive team. These were an opportunity to explore on a more

Haverhill Branch raise money for Macmillan Cancer Support.


Staff led by Jon Hall, Finance Director, take to their bikes to raise more money for Macmillan Cancer Support

personal level what is important to members and we learned a lot from the 53 members who attended.

Our thanks go to those who gave up their time and to other members who have worked alongside us on our Customer Complaints forum, and in other ways during the year. If you would like to play a more active role and be part of shaping our future please give us a call on 01799 582938 or email marketing@saffronbs.co.uk and add your name to our mailing list.

Last year we again ran an online survey, accessed at the end of the AGM voting process, and 22% of those who voted online took part. We are going to do the same this year as it helps us to understand if we are improving our service to you. We know that we have members who do not wish to use the internet so we also have survey documents available in our branches. We do hope that you will participate.

### Our staff are brilliant and we'll prove it

You frequently tell us our staff are a real asset – whether they are the faces you see as you come into our branches, the voices you talk to over the telephone or those who behind the scenes support their work. We agree with you and our promises encourage you to find out how brilliant they are.

# Community Report
(continued)


Eric Pickles MP opens our new Brentwood Branch premises.

We want to be a great employer and we regularly ask our staff what they want us to do differently.  They tell us we are very good at keeping them informed about the business and what we expect of them but they are also happy to say when we could do better and we continue to work on these areas.

We take pride in offering access to professional and comprehensive training and development activities and strongly encourage staff to study for qualifications through our study support programme. Take up on this is rising as the word is spreading on how valuable self learning is. This means we have staff confident in their own knowledge and their ability to provide a good service to members.

You know best who you value amongst our staff and so we have given you the chance in our survey to again nominate someone who really looks after you well so that we can recognise them through our internal award scheme.

**Doing good stuff in your community now and in the future**

In 2010 we decided to try something new. We introduced in branch voting to select charities for our staff to support. You chose 3 charities, Kisses 4 Kids, Macmillan Cancer Support and Little Haven's Hospice. Our staff set to work to raise as much money as possible and to promote these charities. After an amazing 6 months of fundraising activity the total donations reached just over £10,000. This was largely down to the ideas, willingness to get involved and commitment that our people showed and we are hugely proud of their efforts and the results. None of this would have been possible without the generosity of our members though so a big "thank you" to you as well. You will find pictures of some of the activities undertaken on these pages.

We kept our matched funding scheme going and this resulted in Society donations of £2,762 to charities close to the hearts of our staff. Further donations of £3,167 were made to other regions good causes.

To finish the year we made a £10,000 donation into our newly established Saffron Building Society Community Fund. This donation is supplemented by a £5,000 grant from the Grassroots scheme and gets our new charitable support plans off to a flying start.

Staff led by Andy Golding, Chief Executive, help with the gardening at St Elizabeth's Centre.

# Finance Director's Review

**In planning for the current level of interest rates the Society regards continued investment in a competitive retail savings range and being an active mortgage lender as being critical to our members. The significant drop in income on the Society's own liquidity investment portfolio has therefore been managed through a lower current level of profitability which grows capital, but at a slower pace whilst interest rates remain at historic lows.**

**Jon Hall**
Finance Director

Saffron results are likely to benchmark well against the Building Society sector given its straightforward model of retail savings funding residential mortgages, notably:

i) delivering profits and growing capital in the current economic conditions,

ii) increasing both member savings and mortgage balances,

iii) supplementing net interest with income generating advice based services such as insurance broking, financial advice and other investments,

iv) effective expenses management and

v) once again excellent arrears performance from the mortgage portfolio.

### Income statement and profitability

Group profit before tax represented 0.12% (2009: 0.24%) of average Assets. This measure will increase as interest rate rises will provide a greater return on funding costs from the Society's investments and those mortgages linked to base rate.

| | 2010 | 2009 | Change |
|---|---|---|---|
| **Profitability Measures** | | | |
| Group Operating Profit | £1.3m | £2.6m | (£1.3m) |
| Profit Before Tax | £1.1m | £2.0m | (£0.9m) |
| **Income Measures** | | | |
| Net Interest Margin | 0.79% | 1.02% | (0.23%) |
| Non Interest Income | £1.8m | £1.1m | £0.7m |
| **Expense Measures** | | | |
| Administration Expenses | £7.5m | £7.1m | £0.4m |
| Ratio to Average Assets | | | |
| – Group | 0.85% | 0.84% | 0.01% |
| – Society | 0.80% | 0.82% | (0.02%) |
| Group Cost Income Ratio | 85.4% | 73.5% | 11.9% |

- The return on the Society's investment portfolio fell to 1.15% in 2010 (2009: 2.76%). The spread between mortgage balances and retail savings increased slightly to 1.14% (2009: 1.07%).
- The rise in other income was attributable to higher fees associated with new mortgage lending and increased income of £0.3m from Saffron Independent Financial Advisers Ltd.
- Whilst the ratio of expenses to assets has remained in line with recent years the drop in net interest has caused an increase in the cost to income ratio.

### Balance sheet

Total Group assets, at £931m, increased by 11.4% in 2010. This reflected a return to asset growth after a slight decrease in assets of 2% in 2009.

| | 2010 | 2009 | Change |
|---|---|---|---|
| **Liquidity Measures** | | | |
| Liquidity Balances | £235m | £213m | £22m |
| % of funding liabilities | 27% | 27% | – |
| **Mortgage Measures** | | | |
| Mortgage Balances | £690m | £617m | £73m |
| Gross Mortgage Lending | £144m | £46m | £98m |
| Weighted Book LTV | 70% | 69% | 1% |
| Society Arrears | | | |
| – SBS By Value | 0.07% | 0.09% | 0.02% |
| – SBS By Number | 0.19% | 0.14% | 0.05% |
| – BSA Average | 1.55% | 1.16% | 0.39% |
| Group Arrears (3 months) | | | |
| – SBS By Number | 0.39% | 0.57% | (0.18%) |
| – CML Average | 2.15% | 2.40% | (0.25%) |
| – SBS By Value | 0.43% | 0.57% | (0.14%) |
| **Retail & Other Funding Measures** | | | |
| Retail Balances | £783m | £680m | £103m |
| Credit Institution Funding | 11% | 13% | (2%/£7m) |
| Retail Balances: Mortgages | 113% | 110% | 3%/£30m |

# Finance Director's Review

(continued)

- Saffron has demonstrated a strong capability to both retain retail balances and fund new residential mortgages with new retail deposits in often publicised difficult 2010 conditions.
- The addition of excellent online and branch based corporate deposit products to the offering has also been well received, as demonstrated by the balance growth.
- A growth in liquidity and increased surplus of retail funds to cover mortgage balances has further strengthened the balance sheet.
- This theme of a stronger and bigger Society is reflected in the continuing exceptional arrears management performance both within the Society and the Crocus subsidiary.

### Capital resources

Total capital stood at £50.4m at 31 December 2010. This reflects an increase in capital from retained profit after tax for the year of £0.8m in addition to an increase of £0.2m as a result of the annual revaluation of the defined benefit pension scheme.

| Capital Measures | 2010 | 2009 | Change |
|---|---|---|---|
| Total Capital resources | 16.3% | 17.1% | (0.8%) |
| Tier 1 Capital | 12.5% | 13.0% | (0.5%) |

- Whilst capital has increased in the year, the ratio to assets has reduced slightly due to current lower levels of profitability.
- Saffron's capital continues to perform positively when stress tested against potential significant worsening of economic conditions.

### Future financial development

Looking into 2011 and beyond the Society has established its plans which allow for:

- A continued period of low net interest income from prolonged low interest rates. This reflects the challenges to a retail funded organisation seeking to offer a valued product range to saving members. In addition this will result in a similar level of return on the Society's own free capital to that achieved in 2010.
- Continued strong performance from other advice based services as our current and future members seek to ensure maximum value from outlays on items such as insurance or to get quality advice in areas such as investments, pensions and other financial planning.
- Active residential mortgage lending within clearly defined risk management parameters funded through retail deposits. In addition, maintaining a strongly competitive product range available to our existing savings and mortgage members.
- It is recognised that the withdrawal of Government funding support to large banks and building societies in 2011 will further increase the competition for retail funds.
- Efficient management of administration expenses, targeting an improvement in the cost to income ratio, whilst increasing the quality of customer products and services.
- Sustainable increases in the current asset levels whilst protecting liquidity and capital resources.

These future plans have been developed to maintain a bigger, better and stronger independent regional building society.

Jon Hall

**Jon Hall**
Finance Director

# Directors' Report

**The Directors are pleased to present their Annual Report, together with the Annual Accounts and Annual Business Statement of the Society and its subsidiary undertakings ("the Group") for the year ended 31st December 2010.**

## Business objectives and activities

The principal purpose of the Group is to make loans that are secured on residential property and are funded primarily by members.

It is the overall aim of the Society to develop and maintain a close relationship with our members, providing products and services that meet your needs and demonstrate the benefits of mutuality.

## Business review

The Society's business activities, together with the factors likely to affect its future development, performance and position are reviewed in detail by the Chairman, Chief Executive and Finance Director on pages 3 to 10.

The Society has considerable financial resources, notably its liquidity position and capital as described in the Finance Director's review. As a result of an ongoing assessment the directors believe the Society is well placed to manage its business risks successfully and continue to maintain adequate resources despite the potential tentative nature of any medium term economic recovery. This is reflected in the basis of preparation of the annual Report and Accounts.

The Society looks forward to continuing to deliver for members; mortgages, savings and other services through the straightforward operating model that has sustained it through more than 160 years.

## Results for the year

### Profit

Group operating profit before provisions in 2010 was £1.3m (2009: £2.6m), the fall is as a result of lower net interest income (down £1.6m). There was an increase of £0.7m in income from fees for new mortgage lending, financial advice, investments and insurance broking. Administrative expenses were slighter higher by £0.4m at Group and £0.2m at Society level. Rather than pass reductions onto savers, the Society has absorbed the significant fall in income relating to its liquidity investment portfolio as shown by the lower levels of profitability.

In 2010 £0.2m has been charged as an increase in the provision for bad and doubtful debts (2009: £0.6m).

The Group pre-tax profit was £1.1m (2009: £2.0m) with £0.8m (2009: £1.7m) after tax transferred to reserves.

### Assets

At 31st December 2010 assets totalled £931m, an increase of £95m (11.4%). Mortgage balances were up by 11.8% and savings balances by 15%.

### Mortgage arrears

In the Group at 31st December 2010 there were 2 accounts (2009: 4) (Society: 1 in comparison to 2 in 2009) where payments were 12 months or more in arrears. The total amount of arrears outstanding on these 2 accounts was £21k and the aggregate capital balance was £261k.
At 31st December 2010 the Group held 11 properties (2009: 14) as a result of the court repossession process (Society: 10 compared to 13 in 2009).

### Capital

The Society at 31st December 2010 had total capital resources of £50.4m, 16.3% (2009: 17.1%) of risk weighted assets in accordance with the Capital Requirements Directive, commonly referred to as Basel 2. Core Tier 1 capital is 12.5% (2009:13.0%) of risk weighted assets.

## Principal Risks and Uncertainties

A summary of the principal risks and uncertainties facing the Society, and its subsidiary undertakings, and the procedures put in place to manage them is set out below and in more detail in note 25 to the accounts on pages 36 to 38.

The Board retains full responsibility for the operational activities of the Society. In order to ensure that the interests of all members are adequately protected at all times, it has established and embedded a robust governance structure and risk management framework that are designed to identify, manage, monitor and control the major risks exposed in the delivery of the Society's strategic objectives.

The principal risks that arise from the Society's operations are credit, treasury, operational, strategic and external risks. These key categories of risk are common to most financial services firms in the UK.

## Risk Management Framework

The oversight and direction of the Board is central to the Society's risk management framework. It ensures, through a series of Board sub-committees and management forums, that appropriate policies, procedures and processes are implemented across the business to control and monitor risk exposure.

The framework identifies operational roles and responsibilities (both individual and collective) in the risk management process and ensures that exposed risks are aligned to the Risk Appetite Statement of the Board, with any unacceptable risk exposures being managed and mitigated.

# Directors' Report
(continued)

Each of the Board sub-committees include at least two Non-Executives Directors, with other committee members drawn from the executive and appropriate members of senior management.

The key risk orientated committees, operating under the delegated authority of the Board, include the Risk Committee, Assets and Liabilities Committee, Credit Committee and Audit & Compliance Committee.

### Uncertainties

With reference to 2011, the principal uncertainties faced by the Group are associated with the outlook for financial markets and the UK economy as a whole. These include;

- whether the stalling in the housing market evidenced in the second half of 2010 continues throughout 2011;
- the potential for less availability of funding and increased retail savings pressure following the withdrawal of Government liquidity schemes for banks and large building societies;
- the impact of an uncertain economic growth outlook on unemployment levels combined with consumers being squeezed with higher living and mortgage costs;
- a change to the regulatory architecture, which is likely to have a significant impact on the financial services sector.

These developments are taking up a considerable amount of management's time, in ensuring that the Society remains compliant, effective, efficient and importantly focused on serving members' best interests.

### Supplier payment policy

The Group will discharge supplier's invoices within agreed terms when they fully conform to the terms and conditions of the purchase.

The number of creditor days was 26 days (2009: 26) at the end of the year.

### Our people

Once a year the Board reviews employment policies and ensures that they are designed to provide fair and effective employment conditions and equal opportunities.

The Society has accreditation as an 'Investor in People', recognising the commitment to the ongoing training and development of staff and the alignment of individual goals to the Society's strategic aims.

We would like to thank all of our staff for the hard work and support they have given the Society over the last 12 months.

### Charitable donations

During the year the Society made donations totalling £15,930 (2009: £5,845) in support of charities and organisations. No contributions were made for political purposes (2009: nil).

### Business associates

We would like to thank our solicitors, auditors, agents and professional advisors for their continued support during the year.

### Directors

The following served as directors of the Society during the year:

T J Bayley (Non Executive Director)

J P Eastgate (Sales & Marketing Director)

A J Golding (Chief Executive)

J G Goodfellow (Non Executive Director from 28th January 2010 to 30th November 2010)

A H Goodman (Non Executive Director to 22nd April 2010)

J E Hall (Finance Director)

P O Harrison (Chairman)

A Rushworth (Operations Director)

J E Smith (Vice Chairman)

C R L Wilson (Non Executive Director)

T J Bayley, A J Golding and A Rushworth retire by rotation at the Annual General Meeting (AGM) on 27th April 2011 and being eligible will stand for re-election.

Following the resignation of John Goodfellow in November 2010 the board has been seeking a replacement Non Executive Director and in accordance with the rules the successful applicant will be co-opted to the board in early 2011 before standing for election at the AGM in 2012.

Biographies of the Directors appear at page 20.

None of the Directors hold any shares in, or debentures of, any associated body of the Society.

### Auditors

Deloitte LLP has acted for the Society throughout 2010 and has audited the Group accounts for 2010, which are published here.

A resolution to re-appoint Deloitte LLP as auditors to the Group will be proposed at the Annual General Meeting.

Peter Harrison

**Peter Harrison (Chairman)**
On behalf of the Board
24th February 2011

# Directors' Remuneration Report

**In line with best practice in corporate governance the Board has established a Remuneration and Loans Committee which comprises all the Non Executive Directors. It reviews and approves remuneration policy, packages and service contracts for Executive Directors and fees for Non Executive Directors. It also considers and approves loans to Directors or connected persons. This report explains how the Society complies with the principles relating to remuneration in the UK Corporate Governance Code 2010 through the policies it adopts.**

### Executive directors' remuneration

The Board's policy is to set remuneration levels to attract and retain high quality Executive Directors and to encourage performance through rewards directly linked to Society and individual performance. The Committee reviews and takes into account benchmark data and seeks advice on remuneration in comparable financial services organisations as necessary.

The main components of the remuneration package for Executive Directors are:

### Basic salary

Basic salaries for Executive Directors take into account the following principal factors:

- Job content and responsibilities;
- Individual performance, assessed annually; and
- Salary levels for similar positions in comparable organisations.

In 2010 Directors basic salaries were increased and these changes are reflected in the remuneration table. Andy Golding (Chief Executive) chose to defer a pay review in light of the lower profit levels forecast for the Group.

There is an annual appraisal scheme for all Executive Directors which incorporates 360 degree feedback. The results of this exercise help to inform levels of salary award.

### Bonus

Bonuses paid in 2010 are shown in the table of remuneration on page 28. These are the last annual bonuses to be paid following the decision by the Board to remove the short term bonus scheme.

During 2010 the Society's Executive Directors were eligible to accrue a medium term non pensionable performance bonus. Medium term bonuses are capped at 30% of salary and only paid subject to achievement of core objectives on a 3 year deferred basis. Having met the objectives in respect of profit asset growth, capital adequacy and quality in 2010 an accrual has been made to make bonus payments in 2013.

Objectives for 2011 have been set around profit, cost/income ratio and asset growth, capital adequacy, quality and personal achievement.

In the event of non achievement of any area covered by objectives no payments would be made to directors in respect of that element of the scheme. All payments to individuals are performance related and are also subject to claw-back where the Remuneration and Loans Committee considers it appropriate. The bonus plan is non-contractual with the Remuneration and Loans Committee having the final decision on payments to be made and the right to withdraw the scheme if it is no longer considered fit for purpose.

### Pensions

The Executive Directors are included in the Society's Group Personal Pension Plan which offers benefits to staff irrespective of grade. The current employer contribution for directors is 13.5% of basic salary.

### Other benefits

Executive Directors are also eligible for a fully expensed Society car, permanent health insurance and private medical insurance. The Society has no share option scheme and none of the Directors have any beneficial interest in, or any rights to subscribe for shares in any subsidiary undertaking.

No Executive Directors are entitled to salaries or fees from subsidiary directorships.

### Service contracts

All Executive Directors are employed on a permanent service contract. Details are included in the annual business statement on page 40.

### Non Executive Directors' fees

The Remuneration and Loans Committee reviews the level of fees for Non Executive Directors each year, taking into account data on fees paid in the mutual financial services sector, levels of responsibility, time commitments and the recommendations of the Chief Executive and Chairman.

# Directors' Remuneration Report

(continued)

There are no bonus schemes or other benefits for Non Executive Directors and they are not entitled to any pension from the Group.

In 2010, for the second year running, Non Executive Director fees were held at previous levels.

### Analysis of Directors's remuneration

The remuneration of each Director is analysed in Note 7 of the report and accounts.

This report is published with the aim of giving members an insight into how decisions around Directors' remuneration are taken. A resolution will be put forward at the Annual General Meeting inviting members to vote on the report on Directors' remuneration. The vote is advisory and the Board will take into account members' views in determining future policy.

# Directors' Responsibilities

**The following statement, should be read in conjunction with the statement of the Auditors' responsibilities in relation to the preparation of the Annual Accounts, Annual Business Statement and Directors' report.**

The Directors are required by the Building Societies Act 1986 ("the Act") to prepare, for each financial year, annual accounts which give a true and fair view of the:

- State of the affairs of the Society and the Group at the end of the financial year.
- Income and expenditure of the Society and the Group for the financial year.

In preparing these accounts, the Directors are required to:

- Select appropriate accounting policies and apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether the applicable UK accounting standards have been followed, subject to any material departures discussed and explained in the accounts;

and

- Prepare the accounts on the going concern basis unless it is inappropriate to presume that the Group will continue in business. In addition to the accounts, the Act requires the Directors to prepare, for each financial year, an annual business statement and a Directors' report, each containing prescribed information relating to the business of the Society and its subsidiaries.

## DIRECTORS'S RESPONSIBILITIES FOR ACCOUNTING

### Records and internal controls

The Directors are responsible for:

- Ensuring the Society and subsidiary undertakings keep accounting records in accordance with the Act;
- Taking reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Financial Services Authority under the Financial Services and Markets Act 2000;

and

- Safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

As well as our branch and agency network the Society operates a comprehensive website www.saffronbs.co.uk. The maintenance and integrity of this site is the responsibility of the Directors.

### Going concern

The Directors are satisfied that having considered the current uncertain economic conditions, the Group has adequate resources to continue in business for the foreseeable future. For this reason, the accounts continue to be prepared on the going concern basis.

This assessment has been made by the Directors with reference to stress testing of the liquidity and capital position against significant worsening of economic conditions. The key elements assessed by the Directors in the stress testing include further material declines in house prices, rising arrears and default rates, availability and cost of funding sources and declining margins from interest rates at continuing low levels.

The Directors are assured in their assessment by the level of capital and liquidity at the end of 2010 and action taken to protect the business and develop additional member services.

# Corporate Governance Report

**The Board of Directors is responsible for providing leadership and setting the strategic direction of the Society within a framework of prudent and effective controls which enable risk to be assessed and managed. This report explains how the Society applies the UK Corporate Governance Code as a framework. Although the Code does not apply until the next financial year and the Society, as a mutual, is not required to comply, this approach reflects the commitment of the Board of Directors to adopting its principles. The Society continually monitors developments and its intention is to ensure that the highest level recommendations are adopted or non compliance explained.**

## LEADERSHIP:

### The Board

It is the Board's role to set the strategic aims, ensure that the necessary financial and human resources are in place to meet the objectives and review the performance of the Executive team. The Board also puts in place a framework to enable risk to be assessed and managed. The Board consists of four Executive Directors and five Non Executive Directors whose role is to provide independent challenge. At the end of 2010 there were only 4 serving Non Executive Directors as a vacancy existed which it is intended will be filled in 2011. The Board meets at least 11 times a year and adheres to a formal calendar of items for review. The Board retains certain powers for decision making but also delegates certain responsibilities and powers to committees which are listed below.

The Chairman holds meetings twice a year with the Non Executive Directors without the Executive Directors being present. The Chairman is responsible for the leadership of the board and its effectiveness.

The Society maintains liability insurance cover for Directors and Officers.

The Board has established committees to consider certain specialist areas in more detail than would be possible at a Board meeting. Each committee operates within defined terms of reference. Minutes of meetings are formally recorded and reported to the full Board by the respective committee chairman. The committees and their summary terms of reference are set out below. The full terms of reference are available on the Society website or on request from the Society Secretary.

### Remuneration and loans committee (Board committee):

This committee comprises all the Non Executive Directors and is currently chaired by Peter Harrison (Society Chairman). In line with Corporate Governance guidance, a new Chairman will be appointed when the committee first meets in 2011. It sets remuneration policy for Directors, reviews and approves remuneration arrangements and service contracts for Executive Directors as well as Directors' fees. It also considers and approves loans to Directors or connected persons. The committee meets at least once a year to review remuneration and as necessary to approve applications for Directors' loans.

### Nominations committee (Board committee):

This committee consists of the Chairman, Vice Chairman and Chief Executive and is chaired by Peter Harrison (Society Chairman). The committee reviews the balance of Board skills and experience, its structure and composition, any new appointments and the performance of Directors. It decides on the membership of committees. The committee also ensures that the Society meets its statutory responsibilities in respect of compliance with the Building Societies Act and follows good practice in corporate governance, including reviewing compliance with the UK Corporate Governance Code.

### Audit and compliance committee (Board committee)

The committee comprises nominated Non Executive Directors, excluding the Chairman, with various members of the Executive invited to attend as appropriate. Trevor Bayley (Non Executive Director) chairs this committee. It reviews the effectiveness of the Group's systems of internal control and monitors compliance with regulatory requirements and with the relevant codes of practice. The committee approves the annual external audit, internal audit and risk management plans and reviews the compliance plan. These are based on a thorough risk assessment of the full scope of the Group's business activities. The committee meets on a quarterly basis and monitors progress. All Non Executive Directors on this committee have experience that is relevant to the role and at least one member present has recent financial experience.

### Assets and liabilities committee (Management committee):

The committee comprises Executive Directors supported by the Head of Finance and the Society's Treasurer. Named Non Executive Directors also attend meetings. It recommends treasury and balance sheet risk management strategies, capital requirements in the context of the Society's policy statement concerning liquidity, wholesale funding and structural risk

# Corporate Governance Report

(continued)

management policies. The committee meets monthly and is chaired by Andy Golding (Chief Executive).

### Credit committee (Management committee):

The Committee comprises Executive Directors supported by the Head of Underwriting and Risk and Lending Analysis Manager. Named Non Executive Directors are also scheduled to attend meetings. It reviews lending propositions and loan performance as well as benchmark and trend data. It reviews and recommends to the Board changes to lending policy or limits. The committee meets monthly and is chaired by Jonathan Hall (Finance Director).

### Risk committee (Management committee)

The Risk committee is a newly established committee under the chairmanship of Andy Golding (Chief Executive) and consists of the Executive directors and named members of the management team. It assists the Board through the review of information obtained both externally and internally, formulating views about the impact and likelihood of risks crystallizing and recommending measures to control and mitigate these risks.

Current membership of the committees and attendance for all current Directors is shown on page 18.

### Roles of the Chairman, Non Executive Directors and Executive Directors:

The Society maintains clear division of responsibility between the Non Executive Directors and Executive Directors and these are outlined in job descriptions and a table of delegated powers.

Under the Rules, the Chairman and Vice Chairman are elected by the Board on an annual basis.

The Chairman sets standards and expectations for board directors and ensures constructive challenge and openness between Non Executive and Executive Directors.

## EFFECTIVENESS:

### Board balance and independence

The Board is ordinarily composed of five Non Executive Directors and four Executive Directors. In the event of the absence of a Non Executive Director, the Chairman has a casting vote, maintaining an appropriate balance. At the end of 2010 there were only four serving Non Executive Directors as a vacancy existed which it is intended will be filled in 2011.

The Board considers that all Non Executive Directors are independent in character and judgement. With the exception of the Chairman all current Non Executive Board members have served terms of less than six years. The Board has considered the appointment of a Senior Independent Director but has concluded that the responsibilities associated with such an appointment are being undertaken by all Non Executive Directors. A direct email link to a Non Executive Director is available on the Society website for any member who wishes to make contact other than through the Chairman or Chief Executive.

Were business relationships to exist between the Society and a company associated with a Non Executive Director all dealings would be undertaken at arms length.

### Appointments to the board:

The Board advertises externally for candidates for Board appointments. Members can nominate their own candidates for appointment subject to Society rules. The appointment of Directors is based on objective criteria including the ability to meet the requirements of the FSA's approved person's regime. Board succession planning ensures that the correct mix of skills is represented on the Board and committees. The recruitment of new Non Executive Directors is delegated to the Nominations Committee who ensure that directors are able to commit the time required to effectively fulfil the role, at the time of appointment and on an ongoing basis.

### Information and professional development:

Board reporting is of a high standard with an annual review of the scope and appropriateness of the information being undertaken each year. More detailed reporting is provided to Board committees and this is also copied to all Board members for information.

Non Executive Directors attend internal training sessions, Building Societies Association seminars and conferences and receive copies of industry circulars and FSA publications to further their knowledge. Training is tracked and records are held centrally. An induction programme is in place for all new Non Executive Directors to ensure that they can provide effective challenge as soon as possible after appointment. Training and development needs are identified as part of the annual review process undertaken by the Chairman.

### Performance evaluation:

The Board operates an annual appraisal scheme in which all Directors appraise the performance of each of their colleagues, including the Chairman, with the consolidated results also being used to evaluate any overall

# Corporate Governance Report

(continued)

weaknesses. The results of the exercise inform the decision to recommend a director for re-election.

The Board calendar includes a yearly review of Board and committee effectiveness. Again all Board members contribute to an assessment process and the results are evaluated and then discussed at a board meeting. In 2011 the formal assessment will be extended to all board committees. There is currently no plan to undertake externally facilitated formal evaluation although in 2010 a review of Corporate Governance arrangements was undertaken by KPMG LLP (the Group Internal Auditor) at the Board's request.

### Re-election policy:

The Directors are subject to election at the first AGM after their appointment and at three yearly intervals thereafter. A Non Executive Director will normally serve for two terms of three years (with a maximum of three terms). If, in exceptional circumstances, it is deemed that a Non Executive Director should remain on the Board for longer, annual re-election by the membership will be sought. There are currently no Non Executive Directors who have served in excess of nine years. The Nominations Committee reviews the performance of Directors before allowing them to stand for re-election.

## ACCOUNTABILITY:

### Financial and business reporting:

The Director's responsibilities for financial reporting are described in the Report of Director's Responsibilities on page 15.

### Internal control and risk:

Senior management are responsible for designing systems to identify and control risk and ensure that the Board are sighted on risk management through a quarterly review programme which is open to challenge. The introduction of a management risk committee will further enhance reporting.

Internal audit provides an independent confirmation to the Audit and Compliance Committee that appropriate procedures are in place and are being followed.

The Board receives a formal annual report of the effectiveness of systems and controls from the Audit and Compliance Committee.

The Board has satisfied itself that a strong culture of compliance operates and that the systems are effective and appropriate given the nature of the business activity undertaken.

### Audit committee

The Board has established an Audit & Compliance Committee. The work of this committee is described on page 16.

## REMUNERATION:

The Directors' Remuneration Report details the Board position on the Code principle related to remuneration issues.

## RELATIONS WITH MEMBERS:

As a mutual the Society does not have shareholders but is responsible to its members.

In 2010 informal member group lunches were hosted by the Executive Directors to meet with and gauge the views of members on issues that affect them.

Considerable work has been done to extend communication with members with the introduction of an annual members' survey and the establishment of a members' panel. Non-Executive Directors spend time in the branches on an annual basis to help them understand the member perspective.

### Constructive use of the Annual General Meeting (AGM):

Details of the AGM are mailed to all members who are encouraged to attend or to vote on resolutions. Prepaid envelopes are included to enable members to appoint a proxy to vote on their behalf if they are unable to attend. The proxy form provides the opportunity to formally abstain from resolutions should the member so wish. The number of votes in favour of resolutions is published on the Society website after the AGM.

As a further encouragement to vote the Society will be donating 20p to charity for every vote cast. Voting is made easier with an on-line voting option.

In 2011 members' views on various topics will be sought through a web based survey highlighted by the AGM mailing and through a questionnaire available in branches.

# Corporate Governance Report

(continued)

**Director's attendance at meetings:**

| Name | Board | Audit & Compliance | Remuneration & Loans | *Assets & Liabilities | *Credit | Nominations |
|---|---|---|---|---|---|---|
| Number of meetings held | 11 | 4 | 3 | 11 | 11 | 3 |
| T J Bayley | 11 | 4 | 3 | 11 | 0 | 0 |
| J P Eastgate | 11 | 0 | 0 | 11 | 11 | 0 |
| A J Golding | 11 | 4 | 0 | 11 | 11 | 3 |
| J G Goodfellow (resigned November 2010) | 7 | 1 | 2 | 7 | 7 | 0 |
| A H Goodman (retired April 2010) | 2 | 0 | 2 | 1 | 2 | 0 |
| J E Hall | 10 | 4 | 0 | 10 | 10 | 0 |
| P O Harrison | 11 | 0 | 3 | 4** | 2** | 3 |
| A Rushworth | 11 | 0 | 0 | 10 | 10 | 0 |
| J E Smith | 11 | 4 | 3 | 0 | 10 | 3 |
| CRL Wilson | 11 | 4 | 3 | 0 | 11 | 0 |

*These committees are management committees which are attended by Non Executive Directors by invitation.
**Attendance on a voluntary basis.

# Directors' Biographies

**The Board of the Saffron Building Society is made up of Executive and Non Executive Directors. The role of the Executive Directors is to deal with the day-to-day running of the Society, while Non Executive Directors, who are from a range of different specialist areas, bring an outside perspective to the management of the Society and also represent the views of the membership.**

### Non Executive Director – TREVOR BAYLEY

Trevor is a Chartered Accountant and has 30 years' experience in Financial Services having been with Britannia Building Society for 21 years, 12 of which were as a Main Board Director. More recently he was with National Savings and Investments where he was Finance Director and Deputy Chief Executive before retiring in December 2006. Trevor was awarded an OBE in the 2007 New Years Honours List. Trevor joined the board in May 2007.

### Sales & Marketing Director– JOHN EASTGATE

John has over twenty years experience in financial services, initially spending over ten years with Barclays, where he progressed to senior management positions. He joined the Society in April 2008 after five years with Experian, where he headed the banking team in the Decision Analytics division. John joined the board as Sales & Marketing Director in October 2008.

### Chief Executive – ANDY GOLDING

Andy has over twenty-five years' experience in financial services, with a strong background in the banking and mortgage markets. He has held senior management positions with NatWest, John Charcol the UK's leading independent mortgage broker and Bradford and Bingley. Andy joined the Society Board in 2004 as Sales & Marketing Director and took over as Chief Executive in 2006. In addition to his formal directorships he sits on the Building Societies Association Council and the Council of Mortgage Lenders Executive Board.

Andy is a strong advocate of mutuality and is regularly sought to speak at industry events on all matters related to the maintenance of a dynamic and independent mutual sector. He is also recognised within the industry for the innovative use of social media in financial services.

### Finance Director – JONATHAN HALL

Jonathan qualified as a chartered accountant with PricewaterhouseCoopers and has a strong background in the financial services market, having been part of the senior management team at Norwich Union. Jonathan joined the Society in August 2004 from Central Trust plc where he was Group Financial Controller. Jonathan was appointed to the board of Safe Home Income Plans (SHIP) in 2008. Jonathan has represented building societies on working groups for regulatory and commercial developments in the sector.

### Chairman – PETER HARRISON

Peter Harrison is a chartered accountant with over 30 years' experience in the profession specialising in financial services. He worked at KPMG for over 20 years where he became a Senior Partner and the Head of the Financial Services practice in the UK. He joined the Board in 2004. Peter now undertakes varied assignments in the area of financial services including as a Non Executive Director for a quoted Investment Trust and a Senior Advisor and consultant with KPMG.

### Operations Director – ANDREW RUSHWORTH

Andrew joined the Society from AMP Banking, where he was responsible for the design and build of the operational customer service and technology infrastructure as part of the company's UK launch. Andrew stepped up to the Board in December 2004 from his previous position within the Society as General Manager of IT.

### Non Executive Director & Vice Chairman – JAN SMITH

Jan Smith has over 20 years financial services experience with particular emphasis on strategy development, marketing, sales and customer service. She has held Board Director positions at TSB Bank plc, First Direct, Mazda Cars and RAC. She now operates as an independent strategy and marketing specialist working with companies such as Whitbread, Open University, and BACS. She is also a Non Executive Director of the Government Actuary's Department and Mid Essex Services Hospital NHS Trust. Jan joined the Board in 2005.

### Non Executive Director – CHARLES WILSON

Charles Wilson is a solicitor with broad experience of the financial services sector, having worked at Abbey and Nationwide. He served on several industry bodies including the board of Financial Ombudsman Service and the working group that established the LINK cash machine network. Charles took early retirement in 2005 and served as a Non Executive director of Hazell Carr plc.
He joined the Board in July 2009.

# Independent auditor's report to the members of Saffron Building Society

We have audited the Group and Society financial statements of Saffron Building Society for the year ended 31st December 2010 which comprise Group and Society Income and Expenditure Accounts, the Group Statement of Total Recognised Gains and Losses, Group and Society Balance Sheets, the Group Cash Flow Statement and the related notes 1 to 25. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the Society's members, as a body, in accordance with section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society or the Society's members as a body, 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, the directors are responsible for the preparation of financial statements which 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

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and Society's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements.

### Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Group's and the Society's affairs as at 31st December 2010 and of the Group's and the Society's income and expenditure for the year then ended; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986.

### Opinion on other matters prescribed by the Building Societies Act 1986

In our opinion:

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

### Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Building Societies Act 1986 requires us to report to you if, in our opinion:

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

Matthew Perkins (Senior statutory auditor)
for and on behalf of
**DELOITTE LLP**
Chartered Accountants and Statutory Auditors
Birmingham, United Kingdom

24th February 2011

# Income and expenditure account

for the year ended 31st December 2010

| | Notes | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|---|
| Interest receivable and similar income | 2 | 21,598 | 20,778 | 22,190 | 21,415 |
| Interest payable and similar charges | 3 | (14,620) | (14,620) | (13,600) | (13,600) |
| Net interest receivable | | 6,978 | 6,158 | 8,590 | 7,815 |
| Pension finance income | 8 | 81 | 81 | 122 | 122 |
| Income from investments | | – | 300 | – | – |
| Fees and commissions receivable | | 2,376 | 1,867 | 1,691 | 1,454 |
| Fees and commissions payable | | (747) | (743) | (808) | (738) |
| Other operating income | | 245 | 173 | 214 | 214 |
| Total income | | 8,933 | 7,836 | 9,809 | 8,867 |
| Administrative expenses | 5 | (7,111) | (6,658) | (6,777) | (6,560) |
| Depreciation | | (401) | (401) | (327) | (327) |
| Other operating charges | 4 | (140) | (1) | (145) | 52 |
| Operating profit before provisions | | 1,281 | 776 | 2,560 | 2,032 |
| Provisions for bad and doubtful debts | 9 | (191) | (115) | (558) | (489) |
| Provisions for contingent liabilities and commitments - FSCS Levy | 24 | – | – | – | – |
| Profit on ordinary activities before taxation | | 1,090 | 661 | 2,002 | 1,543 |
| Tax on profit on ordinary activities | 10 | (258) | (256) | (320) | (191) |
| Profit for the financial year | 22 | 832 | 405 | 1,682 | 1,352 |

All results were derived from continuing operations.

# Statement of total recognised gains and losses

for the year ended 31st December 2010

| | Notes | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|---|
| Profit for the financial year | | 832 | 405 | 1,682 | 1,352 |
| Actuarial gain / (loss) recognised in the pension scheme | 8 | 373 | 373 | (1,556) | (1,556) |
| Movement in deferred tax relating to the pension scheme | 8 | (197) | (197) | 199 | 199 |
| Total gains and losses recognised since last Annual Accounts | | 1,008 | 581 | 325 | (5) |

The notes on pages 25 to 38 form part of these accounts

# Balance sheet

as at 31st December 2010

| | Notes | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Liquid assets | | | | | |
| Cash in hand and balances with the Bank of England | | 623 | 623 | 577 | 577 |
| Loans and advances to credit institutions | 11 | 91,119 | 90,766 | 76,241 | 76,004 |
| Debt securities | 11 | 143,291 | 143,291 | 135,759 | 135,759 |
| | | 235,033 | 234,680 | 212,577 | 212,340 |
| Loans and advances to customers | | | | | |
| Loans fully secured on residential property | 12 | 682,330 | 630,256 | 609,789 | 556,767 |
| Other loans | 12 | 4,588 | 4,588 | 4,670 | 4,670 |
| | | 686,918 | 634,844 | 614,459 | 561,437 |
| Investments in subsidiary undertakings | 13 | – | 51,621 | – | 52,869 |
| Tangible fixed assets | 14 | 7,491 | 7,491 | 7,168 | 7,168 |
| Other assets | 15 | 635 | 348 | 1,036 | 609 |
| Prepayments & accrued income | | 420 | 454 | 437 | 469 |
| Net pension asset | 8 | 685 | 685 | 178 | 178 |
| **Total assets** | | 931,182 | 930,123 | 835,855 | 835,070 |
| **Liabilities** | | | | | |
| Shares | 16 | 742,185 | 742,185 | 673,992 | 673,992 |
| Amounts owed to credit institutions | 17 | 94,704 | 94,704 | 102,072 | 102,072 |
| Amounts owed to other customers | 18 | 41,006 | 41,006 | 5,999 | 5,999 |
| | | 877,895 | 877,895 | 782,063 | 782,063 |
| Other liabilities | 19 | 1,803 | 1,741 | 3,177 | 2,962 |
| Accruals and deferred income | 20 | 1,112 | 1,112 | 1,251 | 1,251 |
| Subordinated liabilities | 21 | 10,000 | 10,000 | 10,000 | 10,000 |
| | | 890,810 | 890,748 | 796,491 | 796,276 |
| General reserves | 22 | 39,441 | 38,444 | 38,433 | 37,863 |
| Revaluation reserve | 23 | 931 | 931 | 931 | 931 |
| **Total liabilities** | | 931,182 | 930,123 | 835,855 | 835,070 |

The notes on pages 25 to 38 form part of these accounts.

These accounts were approved by the Board of Directors on 24th February 2011, and were signed on its behalf by:

P Harrison  Chairman

J E Smith  Vice Chairman

A Golding  Chief Executive

# Group cashflow statement

for the year ended 31st December 2010

| | Group 2010 £000 | Group 2009 £000 |
|---|---|---|
| **Net cash inflow from operating activities (see below)** | **27,684** | 23,672 |
| Tax paid | **(265)** | (284) |
| | | |
| **Capital expenditure and financial investment** | | |
| (Purchase) / Repayment of debt securities | **(8,443)** | (3,837) |
| Purchase of tangible fixed assets | **(729)** | (268) |
| Net cash inflow from sales of fixed assets | **5** | 11 |
| | | |
| **Increase in Cash** | **18,252** | 19,294 |
| | | |
| **Reconciliation of operating profit to net cash inflow / (outflow) from operating activities** | | |
| Operating profit | **1,090** | 2,002 |
| Decrease in prepayments and accrued income | **1,180** | 1,173 |
| Increase / (Decrease) in accruals and deferred income | **158** | (7,844) |
| Increase / (Decrease) in provisions for bad and doubtful debts | **61** | (231) |
| Depreciation and amortisation | **540** | 525 |
| Pension contributions | **(250)** | (290) |
| Pension income | **(81)** | (122) |
| **Net cash inflow / (outflow) from trading activities** | **2,698** | (4,787) |
| | | |
| (Increase) / Decrease in loans and advances to customers | **(72,520)** | 23,063 |
| Increase / (Decrease) in shares | **67,846** | (3,791) |
| (Decrease) in amounts owed to credit institutions | **(7,235)** | (3,077) |
| Increase / (Decrease) in amounts owed to other customers | **34,925** | (1,570) |
| Decrease in loans/advances to credit institutions | **3,337** | 14,830 |
| (Decrease) in other liabilities | **(1,367)** | (996) |
| **Net cash inflow from operating activities** | **27,684** | 23,672 |

| **Analysis of increase in cash** | 2009 Cash Balances | Net Increase | **2010 Cash Balances** |
|---|---|---|---|
| | £000 | £000 | **£000** |
| Cash in hand | 577 | 46 | **623** |
| Loans and advances to credit institutions repayable on demand (note 11) | 33,985 | 18,206 | **52,191** |
| | 34,562 | 18,252 | **52,814** |

# Notes to the accounts

## 1 Accounting policies

### a) Basis of preparation:

The accounts have been prepared under the historical cost convention, modified to include revaluations of certain fixed assets, and in accordance with applicable United Kingdom accounting standards, the Building Societies (Accounts and Related Provisions) Regulations 1998 and the relevant aspects of the Statements of Recommended Practice issued by the British Bankers' Association and regarded as best practice for the industry.

The Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future. For this reason, the accounts continue to be prepared on the going concern basis.

### b) Basis of consolidation:

The Group accounts consolidate the accounts of the Society and its subsidiary undertakings. In the Society accounts, investments in the subsidiary undertakings are stated at the lower of cost or net book value.

### c) Liquid assets:

Debt securities intended for use on a continuing basis in the Society's activities are classified as financial fixed assets and are stated at cost. Premiums and discounts arising on the purchase of financial fixed assets are amortised over the period to maturity of the security. Any amounts so amortised are charged/credited to the income and expenditure account for the relevant financial years. Other liquid assets are stated at the lower of cost or net realisable value.

### d) Taxation:

Corporation tax is charged on profits adjusted for tax purposes. Deferred tax is provided for without discounting on timing differences arising from the allocation of certain income and expenditure to different periods for tax and accounts purposes, except as otherwise required by FRS 19.

### e) Fixed assets and depreciation:

Freehold properties comprise branches and office buildings and are stated at revalued amounts, being the fair value being determined by the market based evidence, at the date of the valuation less any subsequent impairment. Valuations are completed annually. Increases in valuations of freehold buildings are credited to the revaluation reserve except where they reverse decreases for the same asset previously recognised in the income statement, in which case the increase in the valuation is recognised in the income statement. Decreases in valuations are recognised in the income statement except where they reverse amounts previously credited to the revaluation reserve for the same asset, in which case the decrease in valuation is recognised in the revaluation reserve.

Assets are depreciated over their estimated useful lives as follows:

- Freehold premises – 50 years
- Short leasehold premises – over the remainder of the lease
- Computer equipment – 4 years
- Motor vehicles – 6 years
- Other equipment, fixtures and fittings – 10 years

### f) Premiums on the acquisition of mortgages:

Premiums arising on the acquisition of mortgage portfolios are amortised over five years, or the economic life of the portfolio if shorter, the amount amortised being included within other charges. Unamortised premiums are included within other assets in the balance sheet.

### G) Retirement benefits:

The Society operates a final salary pension scheme administered by trustees, the funds of which are separate from those of the Society. The defined benefit scheme is funded by contributions partly from the employees and partly from the Society at rates assessed by independent actuaries.

The scheme assets are measured at market value at each Balance Sheet date and liabilities are measured using the projected unit valuation method, discounted using a corporate bond rate. The resulting pension scheme surplus or deficit is recognised immediately on the Balance Sheet, net of deferred tax, and any resulting actuarial gains and losses are recognised immediately in the Statement of Total Recognised Gains and Losses.

The Society also operates a stakeholder pension scheme and the Society contributions for this scheme are charged to the income and expenditure account.

### h) Provision for bad and doubtful debts:

Provisions are made to reduce the value of loans and advances to the amount which the directors consider is likely to be recoverable.

# Notes to the accounts

(continued)

Specific provisions are made against loans and advances when, in the opinion of the directors, it is considered likely that losses may ultimately be realised. Currently this is considered to be where arrears are more than 2.5% of the outstanding loan balance. Anticipated losses on these accounts are calculated as the difference between the achievable market value of the security, calculated by applying an industry recognised house price index less forced sale deduction to valuations, and the outstanding loan balance, after making appropriate allowance for costs of repossession and sale. A factor is then applied to the provision based on the loans recent performance. Allowance is made for loss insurance cover where appropriate.

A general provision is made to cover latent losses which, although not specifically identified, are known from experience to exist in the Group's loan portfolios. Such provisions are calculated using a combination of past loss experience, lending quality and consistency with industry levels. These provisions are regularly reviewed against actual experience.

### i) Mortgage discounts and other incentives:

Cash incentives and other expense related incentives to borrowers are included in 'Other operating charges' when paid. Interest discounts reduce interest receivable over the period of the discount.

### j) Hedging rate and instruments:

All interest rate hedges are valued on an equivalent basis to the underlying asset. Cashflows arising in relation to such instruments are accounted for on an accruals basis. If the hedge contract is terminated early, the realised gain or loss is amortised over the residual life of the underlying instrument.

If the underlying instrument is redeemed, the remaining unamortised amount is immediately charged/credited to the income and expenditure account. Amounts accrued on hedging contracts and instruments are included within 'Other assets' or 'Other liabilities'.

### k) Operating leases:

Rentals under operating leases are charged to administrative expenses in the income and expenditure account on a straight line basis over the life of the lease.

# Notes to the accounts

(continued)

## 2. Interest receivable and similar income

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| On loans fully secured on residential property | 22,141 | 19,563 | 18,831 | 16,049 |
| On loans to subsidiaries | – | 1,758 | – | 2,007 |
| On other loans | 265 | 265 | 288 | 288 |
| On debt securities | | | | |
| Interest from fixed income securities | 611 | 611 | 3,003 | 3,003 |
| On other liquid assets | | | | |
| Interest and other income | 1,973 | 1,973 | 2,772 | 2,772 |
| Net expense on financial instruments | (3,392) | (3,392) | (2,704) | (2,704) |
| | 21,598 | 20,778 | 22,190 | 21,415 |

## 3. Interest payable and similar charges

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| On shares held by individuals | 12,630 | 12,630 | 10,546 | 10,546 |
| Subordinated liabilities | 632 | 632 | 632 | 632 |
| Other | 1,358 | 1,358 | 2,422 | 2,422 |
| | 14,620 | 14,620 | 13,600 | 13,600 |

## 4. Other Operating Charges

Other operating charges comprise cash incentives, legal fees and amortisation of the premium arising from the purchase of mortgage books by Crocus Home Loans Limited.

## 5. Administrative expenses

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Staff costs (Note 6) | 4,208 | 4,077 | 4,057 | 3,926 |
| Remuneration of auditors: | | | | |
| statutory audit services | 50 | 50 | 54 | 54 |
| other services | 7 | 7 | – | – |
| Operating lease rentals | 179 | 149 | 221 | 206 |
| Other administrative expenses | 2,667 | 2,375 | 2,445 | 2,374 |
| | 7,111 | 6,658 | 6,777 | 6,560 |

# Notes to the accounts

(continued)

## 6. Staff numbers and costs

The average number of persons employed by the Society (including the Executive Directors) during the year was as follows:

| | Group 2010 | Society 2010 | Group 2009 | Society 2009 |
|---|---|---|---|---|
| Principal office | 78 | 72 | 77 | 73 |
| Branch offices | 62 | 62 | 62 | 62 |
| | 140 | 134 | 139 | 135 |

| The aggregate costs of these persons were as follows: | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Wages and salaries | 3,612 | 3,494 | 3,508 | 3,390 |
| Social security costs | 373 | 360 | 321 | 308 |
| Other pension costs (Note 8) | 223 | 223 | 228 | 228 |
| | 4,208 | 4,077 | 4,057 | 3,926 |

## 7. Remuneration of and transactions with directors

Analysis of Directors' emoluments:

| Executive | Salary/ fees £000 | Annual bonus paid £000 | Medium term bonus paid £000 | Other non-cash benefits £000 | Pension contributions £000 | 2010 Total £000 | 2009 Total £000 |
|---|---|---|---|---|---|---|---|
| A J Golding | 148 | 25 | 28 | 16 | 20 | 237 | 226 |
| J E Hall | 125 | 19 | 22 | 15 | 17 | 198 | 176 |
| A Rushworth | 88 | 13 | 16 | 11 | 11 | 139 | 131 |
| J P Eastgate | 88 | 13 | – | 12 | 12 | 125 | 122 |
| | 449 | 70 | 66 | 54 | 60 | 699 | 655 |
| Non-Executive | | | | | | | |
| T Bayley | 23 | – | – | – | – | 23 | 22 |
| J Goodfellow (28.1.10 to 30.11.10) | 17 | – | – | – | – | 17 | – |
| A H Goodman | 7 | – | – | – | – | 7 | 20 |
| P O Harrison | 33 | – | – | – | – | 33 | 30 |
| J E Smith | 23 | – | – | – | – | 23 | 22 |
| C R L Wilson (from 23.7.09) | 20 | – | – | – | – | 20 | 9 |
| R J Herbert (to 21.4.09) | – | – | – | – | – | – | 10 |
| | 123 | – | – | – | – | 123 | 113 |
| Total 2010 | 572 | 70 | 66 | 54 | 60 | 822 | – |
| Total 2009 | 546 | 74 | 61 | 50 | 37 | – | 768 |

Annual bonus is the balance of bonus earned in respect of 2009 paid in March 2010.
The Board took the decision in 2010 to cease annual bonus arrangements so the payment in 2010 was the last to be settled under this scheme.
Medium term bonus was earned and accrued in 2007 with payment deferred until 2010.
The bonus arrangements are explained in full in the Director's Remuneration Report.

Mortgage loans with directors and connected persons:
At 31 December 2010, there were outstanding mortgage loans granted in the ordinary course of business to three directors and their connected persons, amounting in aggregate to £913,966 (2009: £782,033).
Details of the above transactions are included in the Society's register of directors' loans, extracted details of which are available for inspection by members during normal office hours at the Society's principal office for a period of 15 days prior to and including the Annual General Meeting.

# Notes to the accounts
(continued)

## 8. Pensions

**Defined contribution scheme**
The amounts charged to the Income and Expenditure Account in respect of contributions to the Group's defined contribution stakeholder pension scheme represents the contribution payable in the year. The amounts paid into the scheme amounted to £223,000 (2009: £228,000).

**Defined benefit scheme**
The Society operates a combined contributory and non-contributory defined benefit pension scheme covering its longer serving employees. The scheme closed to staff who joined the Society after 4th August 2003. The assets of the scheme are held in a managed fund independent of the Society's finances.

The funding of the scheme is based upon regular triennial actuarial valuations, the most recent being 1st May 2008. The principal assumptions relate to the rate of return on investments, then assumed to be 5.5% (2005: 6.8%) per annum for the pre-retirement period and 5.5% (2005: 5.1%) for the post-retirement period. The rate of increase in salaries and pensions, was assumed to be 4.0% (2005: 3.9%) per annum.

At the date of the latest actuarial valuation, the market value was £5,818,000 (2005: £3,055,000) which was sufficient to cover 83% (2005: 72.5%) of the benefits that had accrued to members at that date. From 1st January 2008 the scheme was closed to future accrual.

The scheme is shown in the Balance Sheet as a net pension asset, and is made up of the scheme's surplus of £951,000 (2009: £247,00), less the related deferred tax liability of £266,000 (2009: £69,000).

Based on an actuarial valuation, consistent with the methods prescribed in the standard, a net surplus on the Society' scheme has been identified as follows:

| Date of Fund Valuation | 31st December 2010 | 31st December 2009 | 31st December 2008 |
|---|---|---|---|
| **Main assumptions** | | | |
| Rate of increase in salaries | 3.5% | 3.5% | 3.1% |
| Rate of increase in pensions in payment | 3.4% | 3.4% | 3.0% |
| Rate of increase in pensions in payment after 5.04.05 | 2.5% | 2.5% | 3.1% |
| Discount Rate | 5.5% | 5.7% | 6.4% |
| RPI Inflation assumptions | 3.5% | 3.5% | 3.1% |
| CPI Inflation assumptions | 2.8% | – | – |

These assumptions used by the actuary are the best estimates, chosen from a range of possible assumptions which may not be borne out in practice.

The assets in the Scheme and the expected rates of return were:

| | Long term rate of return expected at 31st December 2010 | Value 31st December 2010 £000 | Long term rate of return expected at 31st December 2009 | Value 31st December 2009 £000 | Long term rate of return expected at 31st December 2008 | Value 31st December 2008 £000 | Long term rate of return expected at 31st December 2007 | Value 31st December 2007 £00 |
|---|---|---|---|---|---|---|---|---|
| Equities | 7.5% | 2,514 | 7.8% | 2,331 | 7.0% | 1,395 | 7.8% | 2,101 |
| Bonds | 5.5% | 4,705 | 5.7% | 4,099 | 6.7% | 4,348 | 5.8% | 3,099 |
| Property | 7.0% | 757 | 7.8% | 669 | 7.0% | 652 | 7.8% | 820 |
| Cash | 0.5% | 7 | 0.5% | 9 | – | – | – | – |
| Total market value of assets | | 7,983 | | 7,108 | | 6,395 | | 6,020 |
| Present value of scheme liabilities | | (7.032) | | (6,861) | | (5,004) | | (5,735) |
| Surplus in scheme | | 951 | | 247 | | 1,391 | | 285 |

The scheme liabilities were valued in accordance with the guidelines set out in FRS 17 using a discount rate of 5.7% per annum. This is the long dated corporate bond yield for AA rated bonds used by the fund manager Legal & General.

| **Demographic Assumptions** | 31st December 20010 | 31st December 2009 | 31st December 2008 |
|---|---|---|---|
| Mortality (Pre retirement) | AMC00/AFC00 | AMC00/AFC00 | PA(90)-6 years |
| Mortality (Post retirement) | S1PAmc | S1PAmc | A90-10(m)-8(F) |

# Notes to the accounts
(continued)

## 8. Pensions *(continued)*

Movement in surplus during the year

| | 2010 £000 | 2009 £000 | 2008 £000 |
|---|---|---|---|
| Surplus at the beginning of year | **247** | 1,391 | 285 |
| Contributions | **250** | 290 | 40 |
| Pension finance income | **81** | 122 | 73 |
| Actuarial gain / (loss) | **373** | (1,556) | 993 |
| Surplus at the end of the year | **951** | 247 | 1,391 |
| Related deferred tax liability | **(266)** | (69) | (268) |
| Net pension asset | **685** | 178 | 1,123 |

Analysis of other pension costs charged in arriving at operating profit:

Analysis of amounts included in pension finance income

| | 2010 | 2009 |
|---|---|---|
| Expected return on pension scheme assets | **471** | 443 |
| Interest on pension scheme liabilities | **(390)** | (321) |
| | **81** | 122 |

Analysis of amount recognised in the statement of total recognised gains & losses

| | 2010 | 2009 |
|---|---|---|
| Actual return less expected return on scheme assets | **261** | 12 |
| Experience gains and losses arising on scheme liabilities | **–** | (373) |
| Changes in assumptions underlying the present value of scheme liabilities | **112** | (1,195) |
| Total actuarial gain / (loss) recognised in the statement of total recognised gains & losses | **373** | (1,556) |

History of experience gains and losses

| | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| Difference between the actual and expected return on assets | | | | | |
| £000 | **261** | 12 | 200 | (167) | 179 |
| percentage of scheme assets | **3.26%** | 0.17% | 3.13% | 2.80% | 4.10% |
| Experience gains and losses | | | | | |
| £000 | **–** | (373) | (61) | 9 | (13) |
| percentage of scheme liabilities | **0.00%** | 5.44% | 1.22% | 0.20% | 0.20% |
| Total actuarial gain or loss | | | | | |
| £000 | **373** | (1,556) | 993 | 751 | 396 |
| percentage of scheme liabilities | **5.30%** | 22.68% | 19.84% | 13.10% | 6.50% |

# Notes to the accounts

continued

## 9. Provision for bad and doubtful debts

Provisions against loans to customers have been made as follows:

| | Loans fully secured on residential property | | Other loans fully secured on land | | Total provisions for bad and doubtful debts | | |
|---|---|---|---|---|---|---|---|
| | Specific £000 | General £000 | Specific £000 | General £000 | Specific £000 | General £000 | Provision £000 |
| Group | | | | | | | |
| At 1 January 2010 | 1,034 | 1,613 | – | 1 | 1,034 | 1,614 | 2,648 |
| Charge / (credit) for the year | 184 | 4 | – | 3 | 184 | 7 | 191 |
| Amounts written off previously provided | (130) | – | – | – | (130) | – | (130) |
| At 31 December 2010 | 1,088 | 1,617 | – | 4 | 1,088 | 1,621 | 2,709 |
| Society | | | | | | | |
| At 1 January 2010 | 911 | 1,316 | – | 1 | 911 | 1,317 | 2,228 |
| Charge / (credit) for the year | 144 | (32) | – | 3 | 144 | (29) | 115 |
| Amounts written off previously provided | (44) | – | – | – | (44) | – | (44) |
| At 31 December 2010 | 1,011 | 1,284 | – | 4 | 1,011 | 1,288 | 2,299 |

## 10. Taxation on profit on ordinary activities

| | **Group 2010 £000** | **Society 2010 £000** | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| The taxation charge for year comprises: | | | | |
| Current tax charge | **–** | **–** | 526 | 360 |
| Deferred tax – origination and reversal of timing differences | **258** | **256** | (168) | (131) |
| (Overpayment) / underpayment in respect of previous years | **–** | **–** | (38) | (38) |
| Total tax charge | **258** | **256** | 320 | 191 |
| Factors affecting the tax charge for the year are: | | | | |
| Profit on ordinary activities before taxation | **1,090** | **661** | 2,002 | 1,543 |
| Profit on ordinary activities multiplied by 28% | **305** | **185** | 561 | 432 |
| Effects of: | | | | |
| Difference between capital allowances and depreciation | **(28)** | **(28)** | (11) | (11) |
| Movement in non-taxable provisions | **(214)** | **(216)** | 175 | 138 |
| Depreciation on non-qualifying assets | **23** | **23** | 22 | 22 |
| Income not taxable for tax purposes | **(23)** | **(106)** | (34) | (34) |
| Disallowable expenses | **7** | **7** | 5 | 5 |
| Group relief | **–** | **205** | – | – |
| Contribution into defined benefit pension scheme | **(70)** | **(70)** | (192) | (192) |
| Current tax charge for the year | **–** | **–** | 526 | 360 |

In June 2010 the UK government announced that they would introduce legislation to reduce the corporation tax rate from 28% to 24% over the next four years, reducing the rate by 1% per annum. The legislation to reduce the corporation tax rate for the year commencing 1 April 2011 down to 27% was substantively enacted on 27 July 2010. As such, deferred tax balances as at 31 December 2010 have been calculated at the reduced rate of 27%.

The impact of this tax rate change on the deferred tax balance at 31 December 2010 is not thought to be significant and therefore has not been separately quantified above.

# Notes to the accounts
(continued)

## 11. Liquid assets

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Loans and advances to credit institutions repayable from the balance sheet date in the ordinary course of business are as follows: | | | | |
| Accrued interest | 89 | 89 | 80 | 80 |
| On demand | 52,191 | 51,838 | 33,985 | 33,748 |
| In not more than three months | 32,500 | 32,500 | 38,010 | 38,010 |
| In more than three months but not more than one year | 6,339 | 6,339 | 4,166 | 4,166 |
| | 91,119 | 90,766 | 76,241 | 76,004 |
| Debt securities (unlisted) | | | | |
| Issued by public bodies | 42,582 | 42,582 | 9,641 | 9,641 |
| Issued by other borrowers | 100,709 | 100,709 | 126,118 | 126,118 |
| | 143,291 | 143,291 | 135,759 | 135,759 |
| Debt securities have remaining maturities as follows: | | | | |
| Accrued interest | 466 | 466 | 1,376 | 1,376 |
| In not more than one year | 101,533 | 101,533 | 104,173 | 104,173 |
| In more than one year | 41,292 | 41,292 | 30,210 | 30,210 |
| | 143,291 | 143,291 | 135,759 | 135,759 |

The unamortised premium on debt securities included above was £481,358 (2009: £465,993).

The Directors of the Society consider that the primary purpose of holding securities is prudential. Securities held as liquid assets are held with the intention of use on a continuing basis in the Society's activities and are classed as financial fixed assets.

Movements during the year of debt securities held as financial fixed assets, excluding accrued interest of £466,000 (2009: £1,376,000), are analysed as follows:

| | Group 2010 £000 |
|---|---|
| Cost and Net book value | |
| At 1 January 2010 | 134,383 |
| Additions | 393,176 |
| Disposals | (384,734) |
| At 31 December 2010 | 142,825 |

## 12. Loans and advances to customers

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

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| On call and at short notice | 119 | 21 | 47 | 47 |
| In not more than three months | 128 | 128 | 107 | 74 |
| In more than three months but not more than one year | 1,981 | 1,494 | 1,539 | 1,337 |
| In more than one year but not more than five years | 30,718 | 28,963 | 26,134 | 24,156 |
| In more than five years | 656,681 | 606,537 | 589,280 | 538,051 |
| | 689,627 | 637,143 | 617,107 | 563,665 |
| Less provision (Note 9) | (2,709) | (2,299) | (2,648) | (2,228) |
| | 686,918 | 634,844 | 614,459 | 561,437 |
| The maturity analysis comprises: | | | | |
| Loans fully secured on residential property | 682,330 | 630,256 | 609,789 | 556,767 |
| Other loans fully secured on land | 4,588 | 4,588 | 4,670 | 4,670 |
| | 686,918 | 634,844 | 614,459 | 561,437 |

# Notes to the accounts

(continued)

## 13. Investments in subsidiary undertakings

| | Society 2010 £000 | Society 2009 £000 |
|---|---|---|
| Shares in subsidiary undertaking | **86** | 86 |
| Loans to subsidiary undertaking | **51,535** | 52,783 |
| | **51,621** | 52,869 |

| Movement during the year of loans to subsidiary undertaking: | 2010 £000 | 2009 £000 |
|---|---|---|
| Cost | | |
| At 1st January | **52,783** | 55,146 |
| Repayments received | **(1,248)** | (2,363) |
| At 31 December | **51,535** | 52,783 |

The Society holds 100% of the ordinary share capital of Crocus Home Loans Limited, for the purpose of secured lending on residential property. The share capital authorised and issued is £1,000.

The Society holds 100% of Saffron Independent Financial Advisers Limited, for the purposes of providing independent financial advice. The share capital authorised and issued is £85,000.

The following 100% owned subsidiaries were not carrying on business at the end of the financial year:

Saffron Walden Investment Services Limited
Saffron Walden Property Developments Limited
Saffron Walden Property Sales Limited
The issued share capital of each Company is £2.

All subsidiary undertakings are registered in England and Wales and operate within the United Kingdom.

## 14. Tangible fixed assets

| | Group & Society | | | |
|---|---|---|---|---|
| | Land & buildings | | Equipment, fixtures | |
| | Freehold £000 | Short leashold £000 | fittings & vehicles £000 | Total £000 |
| Cost | | | | |
| At 1 January 2010 | 7,129 | 26 | 2,988 | 10,143 |
| Additions | – | 3 | 726 | 729 |
| Disposals | – | – | (15) | (15) |
| Revaluations | – | – | – | – |
| At 31 December 2010 | 7,129 | 29 | 3,699 | 10,857 |
| Depreciation | | | | |
| At 1 January 2010 | 703 | 26 | 2,246 | 2.975 |
| Charged in year | 84 | 3 | 314 | 401 |
| Disposals | – | – | (10) | (10) |
| At 31 December 2010 | 787 | 29 | 2,550 | 3,366 |
| Net Book Value | | | | |
| At 31 December 2010 | 6,342 | – | 1,149 | 7,491 |
| At 31 December 2009 | 6,426 | – | 742 | 7,168 |

Freehold land and buildings are held at valuation and were professionally valued by Cheffins Commercial, Chartered Surveyors, on an existing use basis for branches and open market value for investment properties as at 31 December 2008. The valuation was £6.5m compared to a net book value of £5.6m. The Directors are of the opinion that this valuation remains appropriate at 31st December 2010.

The net book value of land and buildings occupied by the Society for its own activities is as follows:

| | Group & Society | |
|---|---|---|
| | **2010 £000** | 2009 £000 |
| Freehold | **4,113** | 3,854 |

# Notes to the accounts

(continued)

## 15. Other assets

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Other assets | 11 | – | 14 | 4 |
| Premium on the acquisition of mortgage portfolios | 186 | – | 325 | – |
| Deferred tax | 438 | 348 | 697 | 605 |
| | 635 | 348 | 1,036 | 609 |
| The elements of deferred taxation are as follows: | | | | |
| Difference between accumulated depreciation and capital allowances | (32) | (32) | (5) | (5) |
| General provision for bad and doubtful debts | 438 | 348 | 452 | 369 |
| Other timing differences | 32 | 32 | 250 | 241 |
| Deferred taxation asset | 438 | 348 | 697 | 605 |

The amounts provided are the full potential liabilities.

| | Group £000 | Society £000 |
|---|---|---|
| At 1 January 2010 | 697 | 605 |
| Deferred tax movement for the year | (259) | (257) |
| At 31 December 2010 | 438 | 348 |

## 16. Shares

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Held by individuals | 742,185 | 742,185 | 673,992 | 673,992 |

Repayable from the date of the balance sheet in the ordinary course of business as follows:

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Accrued interest | 3,696 | 3,696 | 3,349 | 3,349 |
| On demand | 566,915 | 566,915 | 506,780 | 506,780 |
| In more than three months but not more than one year | 130,889 | 130,889 | 120,573 | 120,573 |
| In greater than one year | 40,685 | 40,685 | 43,290 | 43,290 |
| | 742,185 | 742,185 | 673,992 | 673,992 |

## 17. Amounts owed to credit institutions

Repayable from the balance sheet date in the ordinary course of business as follows:

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Accrued interest | 154 | 154 | 287 | 287 |
| In not more than three months | 71,050 | 71,050 | 86,030 | 86,030 |
| In more than three months but not more than 1 year | 23,500 | 23,500 | 15,755 | 15,755 |
| | 94,704 | 94,704 | 102,072 | 102,072 |

# Notes to the accounts
(continued)

## 18. Amounts owed to other customers

Repayable from the balance sheet date in the ordinary course of business as follows:

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Accrued interest | 84 | 84 | 2 | 2 |
| Repayable on demand | 40,922 | 40,922 | 5,997 | 5,997 |
| | 41,006 | 41,006 | 5,999 | 5,999 |

## 19. Other liabilities

| Falling due within one year | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Income tax | 571 | 571 | 348 | 348 |
| Corporation tax | – | – | 219 | 99 |
| Other creditors | 1,232 | 1,170 | 2,610 | 2,515 |
| | 1,803 | 1,741 | 3,177 | 2,962 |

## 20. Accruals & deferred income

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Interest accrued on subordinated liabilities | 270 | 270 | 270 | 270 |
| Other accruals | 842 | 842 | 981 | 981 |
| | 1,112 | 1,112 | 1,251 | 1,251 |

## 21. Subordinated liabilities

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Fixed Rate 6.32% Subordinated Debt 2028 | 10,000 | 10,000 | 10,000 | 10,000 |

The Society entered into a subordinated liabilities issue during 2003. The issue is for £10,000,000, denominated in sterling, and the loan is repayable at maturity. The Society has an early repayment option in 2020 following prior consent of the Financial Services Authority.

The rights of repayment of the holders of this issue are subordinated to the claims of all depositors, all creditors and members holding shares in the Society, as regards the principal of their shares and interest due to them.

## 22. General reserves

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| General reserve at start of the year | 38,433 | 37,863 | 38,108 | 37,868 |
| Actuarial gains net of deferred tax | 176 | 176 | (1,357) | (1,357) |
| Profit for financial year | 832 | 405 | 1,682 | 1,352 |
| **General reserve at end of the year** | 39,441 | 38,444 | 38,433 | 37,863 |

| | Group 2010 £000 | Group 2009 £000 |
|---|---|---|
| General reserve excluding pension reserve | 40,876 | 40,044 |
| Pension reserve | (1,435) | (1,611) |
| **General reserve including pension reserve** | 39,441 | 38,433 |

# Notes to the accounts
(continued)

## 23. Revaluation reserve

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Revaluation reserve at start of the year | 931 | 931 | 931 | 931 |
| Revaluation reserve at end of year | 931 | 931 | 931 | 931 |

## 24. Guarantees and other financial commitments

a) Financial Services Compensation Scheme
Based on its share of protected deposits, the Society pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. In September 2008 a claim was triggered against the FSCS by the transfer of Bradford and Bingley's retail deposits to Abbey. In October 2008 further claims were triggered against the FSCS by the transfer of the internet deposit business of Kaupthing Singer and Freidlander (Kaupthing Edge) and the deposit business of Heritable Bank (a subsidiary of Landsbanki hf) to ING Direct. The FSCS is also paying claims in relation to other deposits of these banks which have not been transferred to ING Direct but are covered by the FSCS including the UK depositors of the internet banking subsidiary of Landsbanki hf (Icesave). In November 2008 a further claim was triggered against the FSCS by the administration of London Scottish Bank.

The FSCS has met, or will meet, the claims by way of loans received from the Bank of England which have or will be replaced by loans from HM Treasury. The FSCS has, in turn, acquired rights in the realisation of assets of the banks. The FSCS is liable to pay interest on these loans and may have a further liability if there are insufficient funds from the realisation of the assets of the banks to fully repay these loans.

While the Society has not been directly notified of the levies payable as a result of the above claims, the FSCS has announced that, for three years, it expects to make levies on deposit takers to cover the interest on the loans referred to above and other management expenses capped, in the first year at no more than £1 billion. The brought forward provision from 2009 was £834,606 and the levy for 2009/10 of £261,181 was paid during 2010. The Society has made an estimation for 2010/11 and 2011/12 for which there is a liability as at 31st December 2010 of £573,424.

The Society has a contingent liability which cannot be quantified in respect of contributions to the Financial Services Compensation Scheme required under the Financial Services and Markets Act 2000. An assessment of the Society's exposure to such contributions is set out above.

b) There were no capital commitments for the Group contracted but not provided for as at 31st December 2010.

c) Annual commitments under non-cancellable operating leases are as follows:

| | Group 2010 £000 | Society 2010 £000 | Group 2009 £000 | Society 2009 £000 |
|---|---|---|---|---|
| Land and buildings | | | | |
| Operating leases which expire in 5 years or less | 107 | 107 | 68 | 68 |
| Total operating Leases | 107 | 107 | 68 | 68 |
| Other | | | | |
| Operating leases which expire in 5 years or less | 128 | 99 | 100 | 100 |

## 25. Financial Instruments

The off-balance sheet instruments currently utilised by the Group in managing its balance sheet risk exposures are interest rate swaps. These are used to protect the Group from exposures arising from fixed rate mortgage lending. The Group is not authorised to undertake transactions for trading or speculative purposes. As such all off-balance sheet financial instruments are classified as hedging contracts. The duration and maturity profile of the interest rate swap reflects the nature of the exposures arising from underlying business activities.

Under an interest rate swap, the Group agrees with a third party to exchange at specific intervals the difference between fixed rate and floating rate interest amounts calculated by reference to an agreed notional principal amount. The notional principal of these instruments reflects the extent of the Group's involvement in the instruments, but does not represent its exposure to credit risk which is assessed by reference to the replacement cost.

**Risk Management**
The main financial risks arising from the Group activities are liquidity risk, interest rate risk, credit risk and operational risk. The Board reviews and agrees policies for managing each of these risks as summarised below:

**Liquidity Risk**
The Group's policy is to maintain sufficient liquid funds to ensure liabilities can be met as they fall due so as to retain full public confidence in the solvency of the Group. This is achieved by maintaining a prudent level of liquid assets. The Group has maintained its minimum level of liquidity above our normal range in response to the recent market conditions.

# Notes to the accounts

(continued)

## 25. Financial Instruments *(continued)*

**Credit Risk**

Credit risk is the risk of default by counterparties to transactions. Appropriate credit limits have been set by the Board for individual counterparties, sectors and countries and the Asset and Liability Committee ("ALCO") ensures these limits are adhered to. The Group is not aware of any impairment to its treasury portfolio in terms of receiving value from its holdings on maturity.

**Operational Risk**

Operational risk, which is inherent in all business activities, is the direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. It can occur in any of the Group's businesses and includes errors, omissions, natural disasters and deliberate acts of fraud. The Group manages risk with an overall governance and control strategy. Within this structure, potential risk exposures are assessed to determine the appropriate types of controls to be applied. It is recognised that such risks can never be entirely eliminated and that the cost of controls in minimising these risks may outweigh the potential benefits. However, where required, the Group continues to invest in risk management and mitigation such as business continuity management and incident management. Independent assessment of the effectiveness of the management of operational risk is undertaken by the Internal Audit function.

**Interest Rate Risk**

The Group is exposed to movements in interest rates, in relation to fixed rate mortgage lending. This risk is managed within limits set by the Board, using interest rate swap contracts. After taking into account the interest rate swap contracts entered into by the Group, the interest rate sensitivity exposure of the Group at 31st December 2010 was as follows:

| As at 31st December 2010 | 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** | | | | | | | |
| Liquid assets | 198,278 | 22,495 | 1,007 | 2,075 | 9,993 | 1,185 | 235,033 |
| Loans and advances to customers | 550,261 | – | 25,344 | 65,110 | 48,912 | (2,709) | 686,918 |
| Tangible fixed assets | – | – | – | – | – | 7,491 | 7,491 |
| Other assets | – | – | – | – | – | 1,740 | 1,740 |
| Total assets | 748,539 | 22,495 | 26,351 | 67,185 | 58,905 | 7,707 | 931,182 |
| **Liabilities** | | | | | | | |
| Shares | 566,584 | 66,384 | 64,505 | 40,685 | – | 4,027 | 742,185 |
| Amounts owed to credit institutions and other customers | 112,056 | 13,500 | 10,000 | – | – | 154 | 135,710 |
| Other liabilities | – | – | – | – | 10,000 | 2,915 | 12,915 |
| Reserves | – | – | – | – | – | 40,372 | 40,372 |
| Total liabilities | 678,640 | 79,884 | 74,505 | 40,685 | 10,000 | 47,468 | 931,182 |
| Interest rate swaps – asset hedge | (90,698) | – | – | – | – | | |
| Interest rate swaps – liability hedge | 10,000 | – | – | 33,000 | 47,698 | | |
| Interest rate swaps | (80,698) | – | – | 33,000 | 47,698 | – | – |
| Interest rate sensitivity gap | 150,597 | (57,389) | (48,154) | (6,500) | 1,207 | (39,761) | – |
| Cumulative interest rate sensitivity gap | 150,597 | 93,208 | 45,054 | 38,554 | 39,761 | | |

# Notes to the accounts

(continued)

## 25. Financial Instruments (continued)

As at 31st December 2009

| | 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 |
|---|---|---|---|---|---|---|---|
| Total assets | 686,179 | 11,516 | 16,405 | 58,785 | 54,765 | 8,205 | 835,855 |
| Total liabilities | 598,698 | 54,126 | 82,202 | 63,290 | 14,000 | 23,539 | 835,855 |
| Interest rate swaps – asset hedge | (100,796) | 9,000 | 10,000 | 35,000 | 46,796 | – | – |
| Interest rate swaps – liability hedge | – | – | – | – | – | – | – |
| Interest rate swaps | (100,796) | 9,000 | 10,000 | 35,000 | 46,796 | – | – |
| Interest rate sensitivity gap | 188,277 | (51,610) | (75,797) | (39,505) | (6,031) | (15,334) | – |
| Cumulative interest rate sensitivity gap | 188,277 | 136,667 | 60,870 | 21,365 | 15,334 | – | |

The table below shows the notional principal amounts, credit risk weighted amounts and replacement costs of derivatives. Notional principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The credit risk weighted amount, which is calculated according to rules specified by the Financial Services Authority, is based on the replacement cost but also takes into account measures of the extent of potential future exposure and nature of the counterparty. The replacement costs represents the costs of replacing contracts with a positive value, calculated at market rates current at the balance sheet date reflecting the Groups' maximum exposure should all counterparties default.

| | **2010 Notional principal amount £000** | **2010 Risk weighted amount £000** | **2010 Replacement cost £000** | 2009 Notional principal amount £000 | 2009 Risk weighted amount £000 | 2009 Replacement cost £000 |
|---|---|---|---|---|---|---|
| Interest rate contracts | **90,698** | **198** | **33** | 106,796 | 190 | 71 |
| Under one year | **10,000** | **–** | **–** | 25,000 | – | – |
| Between one and five years | **33,000** | **55** | **–** | 35,000 | 35 | – |
| Greater than five years | **47,698** | **143** | **33** | 46,796 | 155 | 71 |
| | **90,698** | **198** | **33** | 106,796 | 190 | 71 |

Set out below is the comparison of book values of some of the Group's financial assets as at 31st December 2010. The Group does not undertake transactions for trading or speculative purposes. The table excludes certain financial assets and financial liabilities which are not listed or publicly traded, or for which a liquid and active market does not exist.

| | **2010 Group Book value £000** | **Society Fair value £000** | 2009 Group Book value £000 | Society Fair value £000 |
|---|---|---|---|---|
| Debt securities | **143,291** | **143,291** | 135,759 | 135,573 |
| Subordinated liabilities | **(10,000)** | **(10,000)** | (10,000) | (10,000) |
| | **133,291** | **133,291** | 125,759 | 125,573 |
| Interest rate swaps | **–** | **33** | – | 71 |

**Hedges**

Gains and losses on instruments used for hedging purposes are not recognised until the exposure being hedged is itself recognised. Unrecognised gains and losses on hedges at the balance sheet date were £33,000 and £7,424,000 respectively (2009: £71,000 and £4,941,000 respectively). The amount of unrecognised losses at the balance sheet date which are expected to be recognised in the next year is £nil and £nil.

# Annual business statement

for the year ended 31st December 2010

## 1. Statutory percentages

| | Ratio at 31 Dec 2010 % | Statutory limit % |
|---|---|---|
| Lending limit | **0.9** | 25 |
| Funding limit | **15.5** | 50 |

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986.

The lending limit measures the proportion of business assets other than in the form of loans fully secured on residential property. Business assets are the total assets of the Group plus provisions for bad and doubtful debts less liquid assets and tangible fixed assets.

The funding limit measures the proportion of shares, deposits and debt securities not in the form of shares held by individuals.

The statutory limits are prescribed in Building Society legislation and ensure that the principle purpose of a Building Society is that of making loans which are secured on residential property and are funded substantially by its members.

## 2. Other percentages

| | Ratio at 31 Dec 2010 % | Ratio at 31 Dec 2009 % |
|---|---|---|
| As a percentage of shares and borrowings | | |
| Gross capital | **5.7** | 6.3 |
| Free capital | **5.1** | 5.6 |
| Liquid assets | **26.8** | 27.2 |
| As a percentage of mean total assets: | | |
| Profit after taxation | **0.09** | 0.20 |
| Management expenses | **0.85** | 0.84 |

The above percentages have been prepared from the Group accounts:

'Shares and borrowings' represent the total of shares, amounts owed to credit institutions and amounts owed to other customers, in each case including accrued interest.

'Gross capital' represents the aggregate of reserves and subordinated liabilities.

'Free capital' represents the aggregate of gross capital and general provisions for bad and doubtful debts less tangible fixed assets.

'Liquid assets' represent the total of cash in hand and balances with the Bank of England and loans and advances to credit institutions.

'Mean total assets' represent the average of total assets at the beginning and the end of the financial year

'Management expenses' represent the aggregate of administrative expenses and depreciation shown in the Group Income and Expenditure Account

# Annual business statement

for the year ended 31st December 2010

(continued)

## 3. Information relating to the Directors and other Officers as at 31st December 2010

| NAME | DATE OF BIRTH | DATE OF APPOINTMENT | OCCUPATION | OTHER DIRECTORSHIPS |
|---|---|---|---|---|
| **Directors** | | | | |
| T J Bayley OBE, FCA | 22.09.51 | 25.5.07 | Chartered Accountant | Crocus Home Loans Ltd<br>AB Publishing Ltd<br>Waterloo Mills Ltd |
| J P Eastgate | 19.06.68 | 17.10.08 | Sales & Marketing Director | Crocus Home Loans Ltd<br>Saffron Independent Financial Advisers Ltd |
| A J Golding | 03.01.69 | 21.04.04 | Chief Executive | Crocus Home Loans Ltd<br>Saffron Independent Financial Advisers Ltd<br>NHS Northamptonshire Primary Care Trust<br>Building Societies Trust<br>Saffron Education Trust |
| J E Hall FCA | 24.01.69 | 23.09.04 | Finance Director | Crocus Home Loans Ltd<br>Saffron Independent Financial Advisers Ltd<br>Safe Home Income Plans ("SHIP") |
| P O Harrison FCA | 17.03.52 | 27.11.03 | Chartered Accountant | Crocus Home Loans Ltd<br>Templeton Emerging Markets Investment Trust plc |
| A Rushworth | 22.08.63 | 16.12.04 | Operations Director | Crocus Home Loans Ltd |
| J E Smith | 05.04.47 | 28.04.05 | Strategy, Marketing & Sales Specialist | Crocus Home Loans Ltd<br>The Virtual Company Ltd<br>Government Actuary's Department<br>Mid Essex Hospital Services NHS Trust<br>Council for Licensed Conveyancers<br>Saffron Independent Financial Advisers Ltd |
| C R L Wilson | 21.11.49 | 23.07.09 | Solicitor | Crocus Home Loans Ltd |
| Other Officers | | | | |
| S E Andrews | 01.11.56 | 01.09.01 | Society Secretary<br>General Manager<br>(People & Development) | |
| R J Barrett | 25.05.63 | 4.10.04 | Head of Regulated Sales and Managing Director Saffron Independent Financial Advisers Ltd | Saffron Independent Financial Advisers Ltd |

Documents may be served on the above-named Directors and officers at the following address:
Deloitte LLP, Four Brindleyplace, Birmingham, B1 2HZ

## 4. Directors service contracts

As at 31st December 2010 J P Eastgate, A J Golding, J E Hall and A Rushworth had service contracts with the Society which could be terminated by either party giving six months notice. These service contracts were entered into from the dates of appointment as shown above.

## Our services and facilities for disabled customers

We treat all our members as individuals and understand that our standard printed brochures do not suit all.
If you would like this document to be supplied in large print, audio or Braille please contact us on 0800 072 1100.

## Head Office

Saffron House, 1A Market Street, Saffron Walden, Essex CB10 1HX

Tel: 01799 522211 Fax: 01799 581901

**www.saffronbs.co.uk 0800 072 1100**

MIX
Paper from responsible sources
FSC® C004309
www.fsc.org