Nottingham Building Society

Pillar 3 Disclosures

31 December 2021

Contents

1. Overview

1. Overview

1.1. Background

In January 2014, the Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRD), commonly known as the Capital Requirements Directive IV (CRD IV), introduced the definition of capital resources as well as capital and disclosure requirements. The rules are enforced in the UK by the Prudential Regulation Authority (PRA).

CRD V (Directive (EU) 2019/878) was implemented in the EU on 28 December 2020 introducing the remaining Basel III prudential reforms as agreed by the Basel Committee on Banking Supervision (BCBS). However, this is not fully enacted into UK legislation at 31 December 2021 and therefore this document continues to be reported under CRD IV.

The disclosure in this document meets the Nottingham Building Society's, obligation under Pillar 3 reporting, which applies to banks and building societies and complements the minimum capital requirements in Pillar 1 and the supervisory review process in Pillar 2. The Pillar 3 disclosures require firms to publish key information about their underlying risks, capital and risk management and are aimed at promoting market discipline.

1.2. Basis and frequency of disclosures

This document details The Nottingham's Pillar 3 disclosures as at 31 December 2021, with comparative figures for 31 December 2020 where relevant, and has been prepared to meet the disclosure requirements of CRD IV as presented in Part Eight of Regulation (EU) No 575/2013 as amended by CRR II and CRD V to the extent applicable to the Society at the reporting date. The Society has adopted the standardised approach for all exposures and risk areas and uses the capital risk weighting percentages set by the CRR.

The Pillar 3 report is based upon the Society's Annual Report and Accounts for the year ended 31 December 2021, unless otherwise stated. Pillar 3 disclosures are issued on an annual basis in conjunction with the publication of the Annual Report and Accounts in accordance with regulatory guidelines.

1.3. Location and verification

These disclosures and the Annual Report and Accounts are published on The Nottingham's website (www.thenottingham.com).

These disclosures have been reviewed by the Executive Committee and approved by the Board. The disclosures are not subject to external audit. However, some of the information within the disclosures also appears in the Society's audited 2021 Annual Report and Accounts.

The Society has a formal policy in place, which outlines how it complies with Pillar 3 disclosure requirements.

1. Overview

1.4. Developments

The Covid-19 pandemic continues to have an impact on the Society's principal risk categories. While the effects of the pandemic have reduced during 2021, a high level of uncertainty remains. The Society therefore continues to carefully manage its risk in relation to the ongoing pandemic along-side the economic risks of loan affordability, inflationary pressures and rising rate environment.

The Basel Committee on Banking Supervision released 'Basel III: Finalising post-crisis reforms to the Basel III framework' in December 2017, with these revised standards now planned to take effect post March 2023, following the PRA announcement to delay implementation in November 2021.

Alongside this reform the EU published Capital Requirement Regulation II (CRR II) [EU Regulation 2019/876] in June 2019 to refine the implemented Basel framework and amend areas such as leverage ratio, net stable funding ratio and counterparty credit risk.

Following the UK's exit from the EU, the elements of CRR II and CRD V which became applicable in the EU during 2021, required onboarding into UK law. In October 2021, the PRA issued policy statement PS22/21 publishing the final rules for the implementation of Basel standards in the UK which is set out in the PRA Rulebook for relevant banks, building societies and collective firms. The implementation of CRR II into UK legislation was delayed by the PRA to January 2022.

1.5 Scope of application

The disclosure requirements in this document apply to Nottingham Building Society ("the Society"). For prudential purposes the Society is shown on an unconsolidated basis.

PRA number: 200785

The principal office of the Society is Nottingham House, 3 Fulforth Street, Nottingham NG1 3DL.

The consolidated financial statements of the group include the results of the following subsidiary entities:

- Harrison Murray Ltd
- Nottingham Property Services
- HM lettings Ltd
- Nottingham Mortgage Services (until July 2021)

In July 2021, the Society disposed of its 100% owned mortgage broking subsidiary, Nottingham Mortgage Services Ltd.

During the prior year, the Group exited the delivery of estate agency services, resulting in the closure to new business. As a result, the three estate agency entities, Harrison Murray Ltd, Nottingham Property Services Ltd and HM Lettings Ltd are in the process of final wind down at 31 December 2021.

There are no current or foreseen material, practical or legal impediment to prompt transfer of capital resources or repayment of liabilities among Nottingham Building Society and its subsidiaries.

1. Overview

1.5 Scope of Application (continued)

The following company is a special purpose vehicle (SPV) established in connection with the Society's securitisation programme. Although The Nottingham has no direct or indirect ownership interest in this company, it is accounted for as a subsidiary of Nottingham Building Society. This is because the SPV is principally engaged in providing a source of funding to the Society, which in substance means the Society is exposed to rights of variable returns from its involvement in the SPV and has the ability to affect those returns through its power over the entity.

Name of SPV	Nature of business
Arrow Mortgage Finance No. 1 Limited	Secured Funding Vehicle

There is no significant risk transfer associated with the securitisation, so far as the purposes of regulatory capital and Pillar 3, the SPV is consolidated within the Society disclosures.

1.6 Directors

A summary of the relevant experience of each of the Executive and Non-Executive Directors is given on pages 26 and 27 of the 2021 Annual Report and Accounts.

Confirmation of directorships held is disclosed in the Annual Business Statement, which is available on page 117 of the 2021 Annual Report and Accounts.

The policy regarding recruitment and diversity for selection of Directors is outlined on page 37 of the 2021 Annual Report and Accounts.

A copy of the 2021 Annual Report and Accounts is available at www.thenottingham.com.

2. Risk management objectives & policies

2.1. Introduction

The Nottingham recognises risk as a natural consequence of its business activities and environment. It endeavours through positive risk strategies, to manage these in a manner that ensures delivery of its strategic objectives and business plan, whilst protecting members' interests, its financial resources and reputation.

2.2. Risk management framework

The Board is responsible for ensuring that an effective framework is in place to promote and embed an effective risk-aware culture that identifies, appropriately mitigates and manages the risks which the Group and Society face in the course of delivering its strategic objectives.

This includes both current risks and those associated with the implementation of future strategy. The Board annually reviews and approves a risk appetite statement. In pursuing its strategy, the Board ensures there are appropriate capabilities and resources available, along with sufficient capital strength to succeed. This includes focusing on risk and reward to ensure it is at an acceptable level.

The Nottingham operates a 'three lines of defence' approach to the allocation of responsibilities for risk identification and management, as illustrated below:

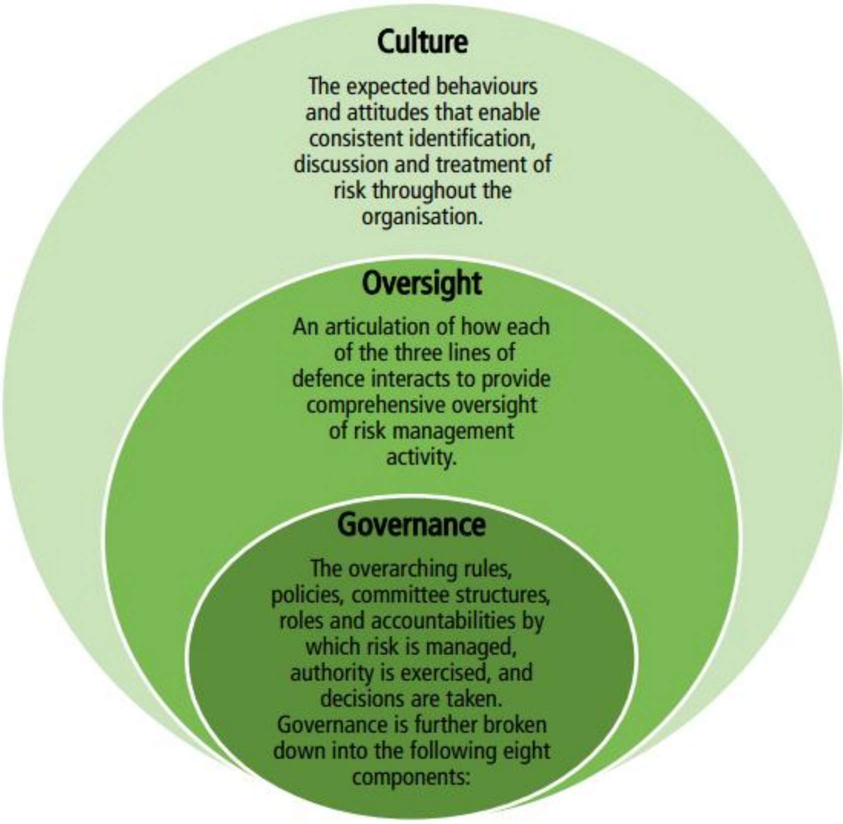
Three Lines of Defence	Focus	Summary of core responsibilities
1st line of defence: Front Line Function	Control	Day to day management and control of risk
2nd line of defence: Risk Management	Oversight	Oversight and challenge of first line of defence
3rd line of defence: Internal Audit	Assurance	Independent assurance of the first two lines of defence.

2. Risk management objectives & policies

2.2 Risk management framework (continued)

The Nottingham's risk management framework is based on the three lines of defence model covering all aspects of risk management as outlined below and is focused on the following:

No	Focus	Summary of risk management
1	Roles and Responsibilities	Defined roles and responsibilities which clearly articulates how stakeholders interact to provide robust governance.
2	Accountability	Articulation of the delegated authority levels of specific roles, individual accountability and the committee structure put in place to manage risk management.
3	Categorisation	The principal categories of risk in which The Nottingham has the greatest actual or potential exposure.
4	Committee Structure	The implementation of relevant management committees (who actively manage risk within the Society) and oversight committees (whose role is to ensure that management committees are adequately assessing the management risks).
5	Policy and Standards	Documented principles, minimum requirements, roles and accountabilities, including how exceptions are handled.
6	Rick Appetite	The setting, articulation, review, monitoring and approval of thresholds for each category of risk.
7	Methodology	Processes, procedures and tools enabling a consistent approach to identifying, evaluating, treatment and monitoring of risk.
8	Management and Monitoring	Supporting dashboards, reporting and other information that expresses the overall current and future business exposure to risk, including items for management attention.

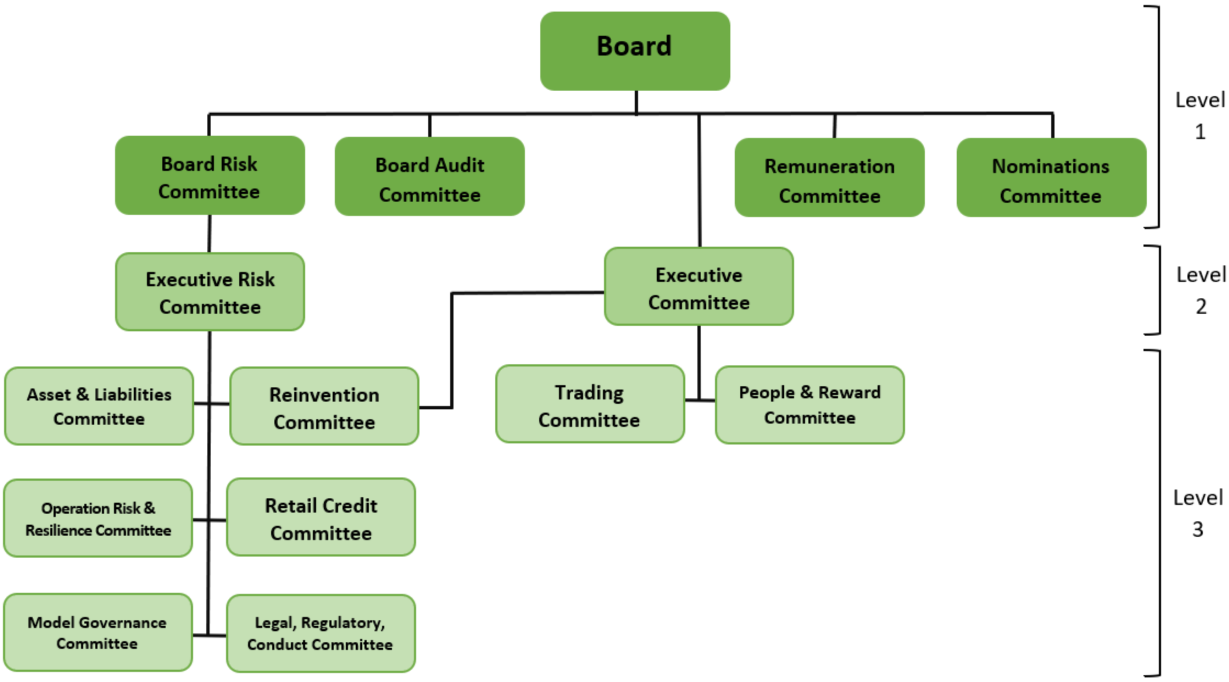


The Board considers that the risk management arrangements and systems are adequate in relation to the strategy, size and complexity of the Society

2. Risk management objectives & policies

2.3. Organisation and structure of risk management

The Nottingham's risk committee structure has been designed to support a wide-ranging approach to the identification and management of risk. In so doing each of the six principal 'management level' risk committees reports to the Board Risk Committee, through the Executive Risk Committee. It is the responsibility of the Board Risk Committee to take a society wide view of The Nottingham's overall exposure to risk.



2. Risk management objectives & policies

Detailed below are the board and management level risk committees along with a summary of their respective remits:

Board Risk Committee (BRC)	
Committee members	All Non-Executive Directors
Summary terms of reference	The BRC is responsible for: • ensuring key risks are identified and appropriate steps taken by management to mitigate them; • ensuring due consideration is given to all significant matters relating to governance, control, regulatory and compliance issues; • monitoring the Group's key risks and controls; • ensuring adequate capital and liquidity are maintained to address the Group's key risk exposures, both to ensure regulatory compliance and the achievement of strategic goals; and • ensuring all conduct risks together with the operational resilience of the Group are properly considered, again to ensure regulatory compliance and the achievement of fair and proper outcomes for all our members. It also oversees, at a high level, the operation of the Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP). In addition, the BRC monitors The Nottingham's overall capital and liquidity adequacy and exposure to risk.
Frequency	Quarterly

Board Audit Committee (BAC)	
Committee members	Four Non-Executive Directors
Summary terms of reference	The principal role of the Board Audit Committee is providing support to the Board in its oversight of financial reporting and the control environment across the Society. The BAC monitors and assesses the effectiveness of the Society's internal audit function, agree and review progress of the annual Internal Audit Plan. The BAC considers the scope and planning of external audit activities and recommends to the Board any decisions on the engagement of external auditors for non-audit services.
Frequency	Quarterly with additional meetings to deal with the interim financial statements and Annual Report and Accounts.

Executive Committee (ExCo)	
Committee members	All Executive Directors and senior managers
Summary terms of reference	The Executive Committee is responsible for acting on behalf of the Board in formulating strategy, the business plan and for organising the Society's assets and resources to deliver value to members in a fair and appropriate manner. The Committee oversees the management of risk in relation to strategic risk and changes in the external environment, which have the potential to affect the Group's business model. The ExCo is supported by three sub-committees: • People and Reward Committee; • Reinvention Committee; and • Trading Committee.
Frequency	At least monthly

2. Risk management objectives & policies

Executive Risk Committee (ERC)	
Committee members	All Executive Directors and senior managers
Summary terms of reference	The Executive Risk Committee is responsible for acting on behalf of the Board and Board Risk Committee in the management and oversight of The Nottingham's principal risks. It reviews relevant policies to ensure that the Society acts in such a way as to organise, manage and protect the Society's assets to deliver value to members through the provision of savings and mortgages, whilst remaining within law, regulation and agreed Board risk appetites. The Committee is responsible for ensuring that the risk management framework is effectively implemented throughout The Nottingham. The ERC is supported by six sub-committees, which are further detailed below: • Retail Credit Committee (RCC); • Assets and Liabilities Committee (ALCO); • Legal, Regulatory & Conduct Risk Committee (LRC); • Operational Risk & Resilience Committee (ORRC); • Model Governance Committee (MGC); and • Reinvention Committee (RC).
Frequency	Minimum eight meetings per annum

Retail Credit (RCC)	
Committee members	Chief Financial Officer and relevant senior managers
Summary terms of reference	The Retail Credit Committee assists the Executive Risk Committee (ERC) and Board Risk Committee (BRC) in the prudent management of The Nottingham's overall retail credit risk with oversight of the mortgage lending portfolio through active monitoring and analysis of the external environment, supporting and reviewing the impact of new lending initiatives and considerations of credit risk implications of lending policy changes. The Retail Credit Committee ensures that the management of retail credit risk is consistent with the retail credit risk policy approved by the BRC.
Frequency	Monthly

Assets and Liabilities Committee (ALCO)	
Committee members	Chief Financial Officer and relevant senior managers.
Summary terms of reference	The Assets and Liabilities Committee (ALCO) is responsible for overseeing The Nottingham's liquidity risk, market and interest rate risk, wholesale credit risk and its capital sustainability risk. ALCO monitors and reviews the current and forecast balance sheet positions, including the balance sheet risks through the control limits and triggers.
Frequency	Monthly

2. Risk management objectives & policies

Operational Risk & Resilience Committee (ORRC)	
Committee members	Chief Customer Officer and relevant senior managers.
Summary terms of reference	The ORRC is responsible for actively overseeing the management of operational risk across The Nottingham. It is also responsible for ensuring that the Society maintains sufficient operational resilience to ensure the ongoing delivery of key services to customers. Operational risk is defined as the risk of loss resulting from human factors, inadequate or failed internal processes and systems or from external events. Operational risk exists in every aspect of the Society's business activities.
Frequency	Monthly

Legal, Regulatory & Conduct Risk Committee (LRC)	
Committee members	Head of Compliance & DPO and relevant senior managers.
Summary terms of reference	The LRC is responsible for overseeing how the Society conducts its business, ensuring that all customer impacting activities are conducted in a clear, transparent and fair manner, delivering fair outcomes for customers.
Frequency	Minimum eight meetings per annum

Model Governance Committee (MGC)	
Committee members	Chief Risk Officer & General Counsel and relevant senior managers
Summary terms of reference	The MGC is responsible for assisting the Executive Risk Committee in the oversight of computer-based models and End User Computing (EUC) applications that are used throughout The Nottingham's strategic and operational activities. The Committee oversees the management of risks related to models to ensure that models are included within the Society's governance framework, and are robustly designed, developed, documented and reviewed.
Frequency	Minimum four meetings per annum

Reinvention Committee (RC)	
Committee members	Head of Change and relevant senior managers
Summary terms of reference	The Reinvention Committee is responsible for the oversight and management of the Transformation and Change risk category; within which role it reports to Executive Risk Committee. It is also responsible for ensuring that transformation and change activity supports the effective delivery of the Society's strategy. In this second role, the Committee reports to the Executive Committee. The Reinvention Committee acts on behalf of the Executive Committee and Executive Risk Committee in the oversight, delivery execution and operational tolerance impact of transformational, large and small business change for the Society through the effective control of a portfolio of change activity.
Frequency	Minimum eight meetings per annum

2. Risk management objectives & policies

2.4. Risk strategy

The Nottingham's overall risk appetite is defined by the Board and documented within the risk appetite section of the Board Risk Policy. This is supported by detailed risk appetite statements for The Nottingham's main risk categories. The Nottingham's risk appetite reflects the changing economic environment, new business opportunities, and evolving strategic objectives.

Secondary, more granular risk policies are approved by the relevant management level risk committees. These risk policies set out the key risks, how they are managed and incorporate further limits and triggers, which are monitored by the individual management level risk committees.

The second line risk function is responsible for overseeing and monitoring the effectiveness of first line risk management processes including the effective implementation of the risk management framework.

In addition, the third line of defence reviews the operation of controls during their assessments to provide assurance to the Board that controls are operating as expected or where weaknesses are identified to assist the strengthening of the risk management framework.

The Nottingham manages and monitors risk using dashboards, reports and other information that expresses the current and future business exposure to risk and highlights items for management attention and action.

Management committees review risk for the specific categories of risk for which they are responsible, escalating to the Executive Risk Committee and the Board Risk Committee where risk indicators fall outside of acceptable tolerances, together with plans to bring risk back within appetite, if appropriate.

The Executive Risk Committee reviews The Nottingham's overall risk profile, escalating to the Board Risk Committee and Board where risk indicators fall outside of acceptable tolerances.

During 2021, the information received and considered by the risk committees provided reasonable assurance that during the year there were no material breaches of control or regulatory standards and that The Nottingham maintained an adequate system of internal control.

Where weaknesses in controls are identified by the three lines of defence, the Board monitors the steps taken to remedy the issues and ensures that the Society responds to changing external threats and economic circumstances and to the changing regulatory environment.

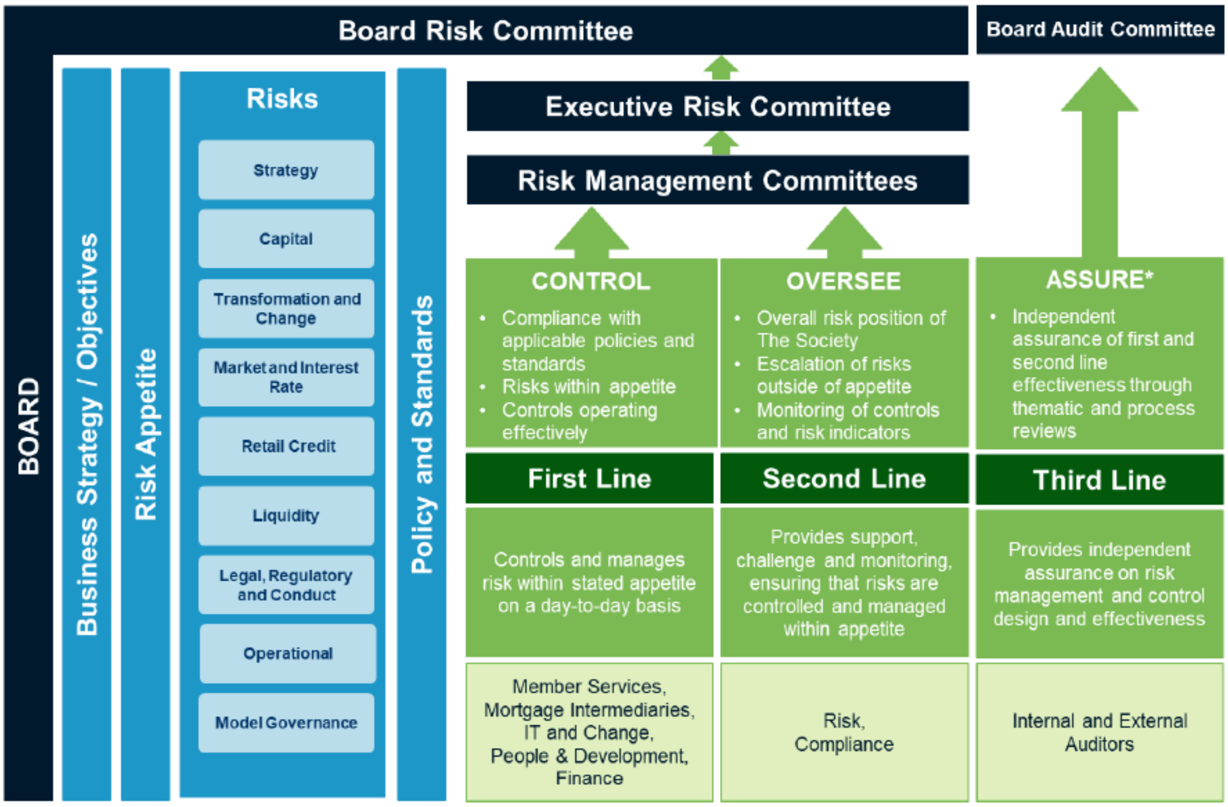
2. Risk management objectives & policies

2.5. Risk appetite

The Nottingham defines its overall appetite for risk in two ways:

1. Quantitatively, by outlining, in numerical and or financial terms, objective limits for risk taking (as described below); and
2. Qualitatively, by outlining in non-numerical terms the basic principles that are adopted by The Nottingham when managing its exposure to risk.

The Nottingham's strategic objectives and business plan, as approved by the Board, are aligned with its risk appetite. In doing so the risk appetite is consistent with the outcomes of these processes and has been designed to support both the maintenance of The Nottingham's financial position and the achievement of its strategic objectives. This is illustrated in the following diagram:



*while the reporting and oversight of audit actions is the responsibility of Board Audit Committee, the management and closures of audit actions is undertaken by the Executive Committee.

The risks associated with climate change are considered within the strategy risk category.

2. Risk management objectives & policies

2.5 Risk appetite (continued)

The Nottingham's overall risk appetite is used to determine the appetites for the nine risk categories that are defined in the risk management framework:

- Strategy (including climate-related risk);
- Capital;
- Transformation & Change;
- Market & Interest Rate;
- Retail Credit;
- Liquidity;
- Model Governance;
- Legal, Regulatory & Conduct; and
- Operational.

These risks, alongside how the Board manage them, are considered in detail within the risk management report included in the 2021 Annual Report and Accounts.

2.6. Stress testing and planning

The Nottingham uses stress testing and scenario planning to help inform management of the impact from high impact stress events. Stress testing forms an integral part of the corporate planning process to ensure The Nottingham remains within risk appetite and has sufficient capital and liquid resources to carry out its strategic objectives.

3. Capital resources

The Basel III regulations, more commonly known as CRD IV, came into force in 2014. One of the objectives of the regulations is to improve the banking sector's ability to absorb shocks arising from financial and/or economic stress. This is to be achieved through increasing both the quality and quantity of regulatory capital firms are required to hold.

The following table shows The Nottingham's capital resources as at 31 December 2021 based on both the transitional and final CRD IV rules basis.

Common Equity Tier 1 (CET1) Capital	2021 CRD IV Transitional £m	2021 CRD IV Final £m	2020 CRD IV Transitional £m	2020 CRD IV Final £m
General Reserves	219.2	219.2	205.5	205.5
Fair value reserves	(0.1)	(0.1)	-	-
CET 1 Capital before regulatory adjustments	**219.1**	**219.1**	**205.5**	**205.5**
Intangible assets	(16.7)	(16.7)	(11.9)	(11.9)
IFRS 9 transitional relief	1.6	-	2.3	-
Deferred tax assets that rely on future profitability	(0.2)	(0.2)	(1.6)	(1.6)
Additional value adjustments	(0.3)	(0.3)	(0.2)	(0.2)
Total regulatory adjustments to CET 1	**(15.6)**	**(17.2)**	**(11.4)**	**(13.7)**
Common Equity Tier 1 capital	**203.5**	**201.9**	**194.1**	**191.8**
Additional Tier 1 Capital				
Capital instruments classified as liabilities - Permanent interest-bearing shares (PIBS)	2.4	-	4.7	-
Additional Tier 1 Capital	**2.4**	**-**	**4.7**	**-**
Total Tier 1 Capital	**205.9**	**201.9**	**198.8**	**191.8**
Tier 2 Capital				
Capital instruments classified as liabilities - Permanent interest-bearing shares (PIBS)	21.4	23.8	19.1	23.8
Total Tier 2 Capital	**21.4**	**23.8**	**19.1**	**23.8**
Total Capital	**227.3**	**225.7**	**217.9**	**215.6**
Total risk weighted assets (RWA)	**1,233.5**	**1,233.5**	**1,291.7**	**1,291.7**
Capital ratios and buffers				
Common Equity Tier 1 ratio *(as a % of RWA)*	16.5%	16.4%	15.0%	14.8%
Tier 1 ratio *(as a % of RWA)*	16.7%	16.3%	15.4%	14.8%
Total capital *(as a % of RWA)*	18.4%	18.3%	16.9%	16.7%
Institution specific buffer requirement (CET 1 requirement plus CCB + CYB)	7.0%	7.0%	7.0%	7.0%
- Of which capital conservation buffer requirement	2.5%	2.5%	2.5%	2.5%
- Of which countercyclical buffer requirement	-	-	-	-

3. Capital resources

3. Capital resources (continued)

Common Equity Tier 1 capital
The fair value reserve is included in regulatory capital under CRD IV.

Intangible assets continue to be fully deducted from CET 1 capital. There is also a further valuation deduction required for prudent valuation on fair valued assets and liabilities.

The classification & measurement and impairment modules of IFRS 9 ‘Financial Instruments’ were adopted by the Society from 1 January 2018. The hedge accounting module of IFRS 9 has not been adopted and therefore the Society continues to apply the requirements of IAS 39 to derivative financial instruments. Since 31 December 2020, the Society has recognised transitional provisions in relation to IFRS 9 movements post 1 January 2020 to its CET 1 position following the regulatory amendments made in response to the Covid-19 pandemic.

Deferred tax assets arising from prior year statutory losses and dependent on future profitability have been deducted from CET1 in accordance with Article 36 and 38 of CRR.

Additional Tier 1 capital
Under the CRD IV rules, PIBS no longer contribute towards Tier 1 capital due to their lack of loss absorbency features. They are subject to the transitional rules of CRD IV which allow the instrument to be grandfathered until December 2021.

Tier 2 capital
The Society’s PIBS instruments are classified as Tier 2 instruments as they transition out of Additional Tier 1 capital.

3. Capital resources (continued)

IFRS9 transitional arrangement
As per guidance in EBA Article 473a, regarding transitional relief arrangements for the implementation of IFRS 9 ((EU) No 2020/873 (CRR Quick fix)), the following table discloses the capital, capital ratios and the leverage ratio that The Nottingham would have in the case it was not to apply this Article.

The Society has recognised IFRS 9 transitional relief adjustments from 2020 following the additional guidance issued during the year in light of the Covid-19 pandemic.

Available capital (£m)	2021 £m	2020 £m
Common Equity Tier 1 (CET1) capital	203.5	194.1
CET1 capital as if IFRS 9 transitional arrangements had not been applied	201.9	191.8
Tier 1 capital	205.9	198.8
Tier 1 capital as if IFRS 9 transitional arrangements had not been applied	204.3	196.5
Total capital	227.3	217.9
Total capital as if IFRS 9 transitional arrangements had not been applied	225.7	215.6
Risk-weighted assets (£m)		
Total risk-weighted assets	1,233.5	1,291.7
Total risk-weighted assets as if IFRS 9 transitional arrangements had not been applied	1,233.5	1,291.7
Capital ratios (%)		
Common Equity Tier 1 ratio	16.5%	15.0%
Common Equity Tier 1 ratio as if IFRS 9 transitional arrangements had not been applied	16.4%	14.8%
Tier 1 ratio	16.7%	15.4%
Tier 1 as if IFRS 9 transitional arrangements had not been applied	16.6%	15.2%
Total capital ratio	18.4%	16.9%
Total capital ratio as if IFRS 9 transitional arrangements had not been applied	18.3%	16.7%
Leverage ratio		
Leverage ratio total exposure measure (£m)	3,670.5	3,737.1
Leverage ratio exposure measure as if IFRS 9 transitional arrangements had not been applied (£m)	3,668.9	3,734.8
Leverage ratio[1] (%)	5.6%	5.3%
Leverage ratio[1] as if IFRS 9 transitional arrangements had not been applied (%)	5.6%	5.3%

[1] As defined within CRD IV

3. Capital resources

3.1. Reconciliation of regulatory capital

A reconciliation of balance sheet capital to regulatory capital is presented below:

	2021 CRD IV Transitional £m	2021 CRD IV Final £m
Total equity attributable to members per the Statement of Financial Position	**219.1**	**219.1**
Adjustments for items not eligible for inclusion in CET 1 capital:		
- Intangible fixed assets	(16.7)	(16.7)
- Additional value adjustments	(0.3)	(0.3)
- IFRS 9 transitional relief	1.6	-
- Deferred tax assets that rely on future profitability	(0.2)	(0.2)
Total adjustments to CET 1 Capital	**(15.6)**	**(17.2)**
Adjustments to Additional Tier 1 capital:		
- Amortisation of PIBS under transitional rules	2.4	-
Adjustments to Tier 2 capital:		
- Permanent interest-bearing shares (PIBS)	21.4	23.8
Regulatory Capital	**227.3**	**225.7**

4. Capital adequacy

4. Capital adequacy

4.1. Capital management

The Nottingham's policy is to maintain a strong capital base to maintain member, creditor and market confidence and to sustain the future development of the business. The Board manages The Nottingham's capital and risk exposures to maintain capital in line with regulatory requirements. This is subject to regular stress tests to ensure The Nottingham maintains sufficient capital for possible future events.

As a mutual, The Nottingham has no outside shareholders to whom it needs to pay dividends. As such The Nottingham does not have to maximise profitability so long as it maintains an adequate capital position.

The Nottingham's capital requirements are also monitored by the Prudential Regulation Authority (PRA).

4.2. Internal Capital Adequacy Assessment Process and Pillar 2

The Board monitors The Nottingham's capital position with the aid of its Internal Capital Adequacy Assessment Process (ICAAP) on an annual basis. This requires The Nottingham to assess its capital adequacy over the planning horizon and determine the level of capital it requires to support both current and future potential risks.

The Nottingham uses the Standardised Approach to calculate its credit risk weightings. Internally, The Nottingham operates a similar standard to the Internal Ratings Based (IRB) approach for its retail mortgages, the benefit of which is an enhanced risk management capability.

Under the Standardised Approach the level of capital required against a given level of exposure to credit risk is calculated as:

Credit risk capital requirement = Exposure value x Risk weighting* x 8%.

* The risk weighting applied will vary depending on whether the asset is retail or wholesale. For retail assets, variables such as loan to value and security will impact the risk weighting. Wholesale assets are dependent on counterparty, duration and credit rating.

The primary source for obtaining information on counterparties' creditworthiness is External Credit Assessment Institutions (ECAIs). There have been no changes to the ECAIs during the year and the Society continues to use two ECAIs to assign credit quality steps for short and long term investments; namely Moody's Investors Service (Moody's) and Fitch Group (Fitch). Unrated counterparties may be approved by the Board Risk Committee.

Credit ratings are reviewed regularly, and a list of relevant changes provided to the monthly ALCO. Where ratings fall below the standard minimum criteria for a counterparty limit, management will propose action for managing the exposure, which will be escalated through the ALCO and ERC to BRC. In addition to credit ratings, The Nottingham may also consider other factors when determining credit worthiness, such as capital adequacy, financial performance, non-performing loans and key market metrics.

4. Capital adequacy

4.2 Internal Capital Adequacy Assessment Process and Pillar 2 (continued)

The table below presents the constituent elements of the CRD IV capital requirements.

Pillar 1		Firm specific calculation based on individual firms' risk weighted assets – a minimum of 8%.
Pillar 2A		Firm specific calculation for risks not fully captured under Pillar 1.
Pillar 2B	**Capital Conservation Buffer (CCB)**	Used to absorb losses in periods of economic and financial stress. Set at 2.5%
	Countercyclical Capital Buffer (CCyB)	Set by the Bank of England's (BoE) Financial Policy Committee (FPC) within a range of 0.0% and 2.5%. To ensure financial institutions build up capital in favourable economic conditions, which can be utilised in economic downturns. Set at 0.0% at 31 December 2021 (2020: 0.0%)

4.2.1. Countercyclical capital buffers

Regulation (EU) 2015/1555 requires disclosure information relevant for the calculation of the countercyclical capital buffer as at 31 December 2021, which is presented below.

All credit exposures relevant to the calculation of the countercyclical buffer are geographically distributed within the UK.

As the CCyB rate has been set at 0.0% there is no institutional specific countercyclical buffer rate requirement as 31 December 2021 (31 December 2020: £nil).

The BoE Financial Policy Committee announced in 13 December 2021, that the CCyB for UK financial institutions will increase to 1.0% with binding effect from 13 December 2022.

4. Capital adequacy

4.3. Capital requirements summary

The Society's minimum capital requirement under Pillar 1 is the sum of the credit risk capital requirement and the operational risk capital requirement.

The following table shows the Society's overall minimum capital requirement as at 31 December 2021:

Pillar 1: Capital requirements	31 December 2021 £m	31 December 2020 £m
Credit Risk Standardised Approach (excluding counterparty credit risk)		
- Loans and advances to customers	87.9	90.8
- Wholesale lending	1.5	1.1
- Other Items	1.6	4.1
- Mortgage commitments	0.7	0.6
Counterparty credit risk (CCR)		
- CVA	0.5	0.4
Operational Risk	6.5	6.3
Minimum capital requirement	**98.7**	**103.3**
Capital resources (section 3)	227.3	217.9
Excess of own funds over minimum Pillar 1 capital requirement	**128.6**	**114.6**

4.4. Leverage ratio

The CRD IV framework requires firms to calculate a simple, transparent, non-risk-based leverage ratio that is a supplementary measure to the risk-based capital requirements.

The leverage ratio measures the relationship between the capital resources of the Society and its total assets as well as certain off-balance sheet exposures. The ratio is defined as the Capital Measure divided by the Exposure Measure, with this ratio expressed as a percentage on an end point basis.

The capital measure for the leverage ratio is Tier 1 capital from the risk-based capital framework as defined in paragraphs 49 to 96 of the Basel III framework (see table in Section 4.2), taking account of the transitional arrangements.

4. Capital adequacy

4.4 Leverage Ratio (continued)

The Exposure Measure is the total on and off-balance sheet exposures (subject to credit conversion factors) as defined in the Delegated Act amending CRR Article 429, which includes deductibles applied to Tier 1.

Leverage ratio	Transitional 2021 £m	Final 2021 £m	Transitional 2020 £m	Final 2020 £m
Total Tier 1 capital	**205.9**	**201.9**	**198.8**	**191.8**
Exposure:				
- Total regulatory balance sheet exposure	3,634.8	3,634.8	3,756.8	3,756.8
- Netted derivative and other adjustments	28.4	28.4	(29.9)	(29.9)
- Mortgage pipeline	25.2	25.2	21.6	21.6
- Tier 1 deductions	(17.9)	(19.5)	(11.4)	(13.7)
Leverage ratio exposure	**3,670.5**	**3,668.9**	**3,737.1**	**3,734.8**
Leverage ratio	**5.6%**	**5.5%**	**5.3%**	**5.1%**
Leverage ratio excluding central bank deposits	**6.1%**	**6.0%**	**6.0%**	**5.7%**

At the 31 December 2021, The Nottingham had a leverage ratio of 5.6%, well above the 3% regulatory minimum based on the transitional rules. Under the final CRD IV rules basis, leverage ratio of 5.5% remains well above the 3% regulatory minimum.

The UK leverage ratio framework (PS21/21 – The UK leverage ratio framework) has been released during 2021. This introduces the exclusion of certain central bank reserves from the leverage exposure measure and requires a minimum leverage requirement of 3.25% taking effect from 1 January 2022. Whilst not yet in force, the Society is in excess of this regulatory minimum.

The Nottingham will continue to operate at a level in excess of the regulatory minimum.

4.5. Total Capital Requirement

The Society is required to hold a certain amount of capital against the assets it holds, which is referred to as its Total Capital Requirement (TCR). As at 31 December 2021, the Society's Total Capital Requirement was set at 8.81% (31 December 2020: 8.77%) of risk weighted assets or £108.7m (31 December 2020: £113.3m).

5. Credit risk

5. Credit risk

Credit risk is the risk that a financial loss arises from the failure of a customer or counterparty to meet their contractual obligations. The Nottingham manages the level of credit risk it undertakes by applying various control disciplines, the objectives of which are to maintain asset quality in line with the stated risk appetite.

As a building society, this is most likely to arise through the inability of borrowers to repay their mortgage commitments (retail credit risk) or through the failure of a treasury counterparty (wholesale credit risk).

Lending and business decisions

The Nottingham uses application scorecards to help it assess whether mortgage applications fit within its appetite for credit risk. Once loan funds have been advanced, behavioural scorecards are used to review the ongoing risk profile of both the portfolios and individual customers. In addition, residential and buy-to-let (BTL) mortgages property values are updated on a monthly basis.

Through the use of scorecards, The Nottingham is able to estimate the likely level of default, mortgage arrears, impairment charges and capital allocation.

If the scorecard decision is to accept, and the customer and property to be mortgaged meet The Nottingham's policy criteria, the mortgage application will be processed. Where applications are declined, applicants are given as much information as possible regarding the reason for the decision.

Pricing

Pricing models are utilised for all mortgage product launches. The models include expected loss estimates and capital utilisation enabling the calculation of a risk adjusted return on capital.

Concentration risk

The design of retail products takes into account the overall mix of products to ensure that The Nottingham's exposure to market risk remains within permitted parameters.

5.1. Loans and advances to customers

Retail credit risk

Exposure to retail credit risk is limited to the provision of loans secured on property within the UK. All mortgage loan applications are reviewed by an individual underwriter supported by the use of application scorecards and are assessed with reference to The Nottingham's retail credit risk lending policies. The lending policy is set with reference to The Nottingham's Retail Credit Risk Appetite, which is ultimately approved by the Board Risk Committee. Exposure to retail credit risk is carefully monitored by the Retail Credit Committee, which reports to the Board Risk Committee through the Executive Risk Committee.

5. Credit risk

5.1 Loans and advances to customers (continued)

Secured Business Lending Credit Risk

The Nottingham's secured business lending policy is used to manage the level of credit risk emanating from secured business lending. Primarily, secured business lending loans are made available to Small and Medium sized Enterprises (SMEs) for either owner occupied or investment property purposes. Loans are only granted against the 'bricks and mortar' value (i.e. loans are only provided for the purchase/ re-mortgaging of a property and not for working capital or machinery, etc.).

Secured business lending credit risk is monitored by the Retail Credit Committee.

The table below details the minimum credit risk capital requirement by standardised exposure class as at 31 December 2021, broken down by exposure value.

Standardised exposure classes	31 December 2021		31 December 2020	
	Exposure Value £m	Capital Requirement £m	Exposure Value £m	Capital Requirement £m
Retail	7.3	0.4	20.7	1.2
Secured by Mortgages on Residential Property	2,912.5	80.8	2,973.6	82.8
Secured Business Lending	105.0	6.4	104.0	6.3
Past Due Items	4.3	0.3	4.8	0.4
Total Loans and advances to customers	**3,029.1**	**87.9**	**3,103.1**	**90.7**

The following table shows the residual maturities of all loans and advances exposures as at 31 December 2021.

31 December 2021	<3 months £m	>3 months < 1 year £m	>1 year < 5 years £m	>5 years £m	Total £m
Retail	-	-	-	7.3	**7.3**
Secured by Mortgages on Residential Property	2.8	8.0	101.3	2,800.4	**2,912.5**
Secured Business Lending	0.3	0.6	7.7	96.4	**105.0**
Past Due Items	-	0.1	0.5	3.7	**4.3**
Total Loans and advances to customers	**3.1**	**8.7**	**109.5**	**2,907.8**	**3,029.1**

31 December 2020	<3 months £m	>3 months < 1 year £m	>1 year < 5 years £m	>5 years £m	Total £m
Retail	-	-	-	20.7	**20.7**
Secured by Mortgages on Residential Property	3.7	6.6	100.8	2,862.5	**2,973.6**
Secured Business Lending	0.8	1.0	6.0	96.2	**104.0**
Past Due Items	-	-	0.1	4.7	**4.8**
Total Loans and advances to customers	**4.5**	**7.6**	**106.9**	**2,984.1**	**3,103.1**

5. Credit risk

5.1 Loans and advances to customers (continued)

Credit risk exposures can be further sub-divided. The table below shows the geographical analysis of these exposures at 31 December:

31 December 2021 Region (United Kingdom)	Retail £m	Secured by Mortgages on Residential Property £m	Secured Business Lending £m	Past Due Items £m	Total £m
Eastern	0.5	282.5	5.7	-	**288.7**
East Midlands	1.1	483.5	22.0	0.7	**507.3**
London	0.5	249.4	10.9	0.9	**261.7**
North East	0.7	152.8	1.1	0.1	**154.7**
North West	1.0	337.3	18.6	0.2	**357.1**
South East	0.7	410.0	9.0	0.6	**420.3**
South West	0.3	245.3	17.7	0.1	**263.4**
Wales	0.2	98.2	6.0	0.1	**104.5**
West Midlands	1.2	287.7	8.0	0.5	**297.4**
Yorkshire & Humberside	0.8	359.8	5.8	1.1	**367.5**
Other	0.3	6.0	0.2	-	**6.5**
Total	**7.3**	**2,912.5**	**105.0**	**4.3**	**3,029.1**

31 December 2020 Region (United Kingdom)	Retail £m	Secured by Mortgages on Residential Property £m	Secured Business Lending £m	Past Due Items £m	Total £m
Eastern	3.2	297.0	6.3	0.3	**306.8**
East Midlands	3.3	528.1	22.0	0.7	**554.1**
London	0.6	234.5	11.1	1.3	**247.5**
North East	1.4	152.1	1.3	0.2	**155.0**
North West	1.6	333.8	18.4	0.5	**354.3**
South East	2.9	419.0	9.1	0.4	**431.4**
South West	1.4	255.2	15.8	-	**272.4**
Wales	0.6	96.6	4.4	0.1	**101.7**
West Midlands	3.3	286.0	8.3	0.3	**297.9**
Yorkshire & Humberside	2.3	367.8	5.9	1.0	**377.0**
Other	0.1	3.5	1.4	-	**5.0**
Total	**20.7**	**2,973.6**	**104.0**	**4.8**	**3,103.1**

5. Credit risk

5.2. Wholesale lending

A Board approved policy statement restricts the level of risk by placing limits on the amount of exposure that can be taken in relation to one counterparty or group of counterparties, and to industry sectors. Each counterparty must meet the minimum investment criteria with a number of factors considered when determining credit worthiness. Wholesale credit risk is reported by ALCO through to the Executive Risk Committee and Board Risk Committee.

The Nottingham's Liquidity Risk policy determines the amounts, products and counterparties under which wholesale lending can be undertaken, with only sterling denominated lending permitted. Alongside lending to the UK Government and Central Bank, limits are in place with a number of UK building societies and specific UK and overseas banks as well as Multilateral Development Banks. Each counterparty must meet the minimum investment criteria as set out in the Liquidity Risk policy or be specifically approved by the Board Risk Committee. In addition, investments in Residential Mortgage Backed Securities (RMBS) and Covered Bonds are permitted in instances where they meet the Board approved minimum investment criteria.

The table below details the exposure value and minimum credit risk capital requirement by standardised exposure class as at 31 December.

Standardised exposure class	31 December 2021		31 December 2020	
	Exposure Value £m	Capital Requirement £m	Exposure Value £m	Capital Requirement £m
Central Government or Central Banks	324.2	-	383.4	-
Multilateral Development Banks	104.7	-	78.7	-
Institutions	64.8	0.7	30.1	0.4
Securitisation positions	61.5	0.5	46.7	0.4
Derivative financial instruments	37.0	0.3	17.4	0.3
Total Wholesale lending	**592.2**	**1.5**	**556.3**	**1.1**

The following table shows the residual maturities of all wholesale credit exposures as at 31 December.

31 December 2021	<3 months £m	>3 months < 1 year £m	>1 year < 5 years £m	>5 years £m	Total £m
Central Government or Central Banks	284.6	-	39.6	-	**324.2**
Multilateral Development Banks	14.0	-	90.7	-	**104.7**
Institutions	5.9	-	58.9	-	**64.8**
Securitisation positions	-	-	61.5	-	**61.5**
Derivative financial instruments	0.1	10.3	26.4	0.2	**37.0**
Total Wholesale lending	**304.6**	**10.3**	**277.1**	**0.2**	**592.2**

31 December 2020	<3 months £m	>3 months < 1 year £m	>1 year < 5 years £m	>5 years £m	Total £m
Central Government or Central Banks	383.4	-	-	-	**383.4**
Multilateral Development Banks	8.1	-	70.6	-	**78.7**
Institutions	8.3	-	21.8	-	**30.1**
Securitisation positions	-	8.5	38.2	-	**46.7**
Derivative financial instruments	0.5	1.4	15.1	0.4	**17.4**
Total Wholesale lending	**400.3**	**9.9**	**145.7**	**0.4**	**556.3**

5. Credit risk

5.2 Wholesale lending (continued)

The geographical split and credit rating of The Nottingham's treasury exposures at 31 December are detailed in the table below.

31 December 2021 Credit Rating Credit Quality Step	UK £m	Supranational Institutions £m	North America £m	Total £m
1	438.5	94.9	-	**533.4**
2	48.8	-	-	**48.8**
3	-	-	-	**-**
Unrated	-	10.0	-	**10.0**
Total	**487.3**	**104.9**	**-**	**592.2**

31 December 2020 Credit Rating Credit Quality Step	UK £m	Supranational Institutions £m	North America £m	Total £m
1	446.2	78.6	0.2	**524.9**
2	31.3	-	-	**31.3**
3	-	-	-	**-**
Unrated	-	-	-	**-**
Total	**477.5**	**78.6**	**0.2**	**556.3**

The credit ratings of the external credit assessment institutions correspond to the following credit quality steps:

Credit Quality Step	Moody's	Fitch
1	Aaa to Aa3	AAA to AA-
2	A1 to A3	A+ to A-
3	Baa1 to Baa3	BBB+ to BBB-
4	Ba1 to Ba3	BB+ to BB-
5	B1 to B3	B+ to B-
6	Caa1 and below	CCC+ and below

5. Credit risk

5.3. Impairment provisions

5.3.1. Impairment of loans and advances to customers

The Society applies IFRS 9 'Financial instruments' to calculate loss provisions on its mortgage assets.

Under IFRS 9, the Society assesses on a forward-looking basis the Expected Credit Losses (ECL) associated with its mortgage assets carried at amortised cost and FVOCI and with the exposure arising from loan commitments. The allowance is based on the ECLs associated with the probability of default in the next 12 months unless there has been a significant increase in credit risk since origination and the measurement of ECL reflects:

- An unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

IFRS 9 outlines a 'three-stage' model for impairment based on changes in credit quality since initial recognition as summarised below:

- **Stage 1:** A financial instrument that is not credit-impaired on initial recognition and its credit risk has not significantly increased since origination. ECL is measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months.
- **Stage 2:** If a significant increase in credit risk (SICR) since initial recognition is identified, the financial asset is moved to 'Stage 2' but is not yet deemed to be credit impaired. The definition of a significant increase in credit risk is detailed below. ECL for stage 2 assets are measured based on expected credit losses on a lifetime basis.
- **Stage 3:** If the financial asset is credit-impaired, it is moved to 'Stage 3'. The definition of credit-impaired and default is outlined below. ECL for stage 3 assets is also measured on expected credit losses on a lifetime basis.

Forward-looking information is taken into account in the measurement of ECL with its use of economic assumptions such as unemployment rates, house price indices and Bank of England interest rates.

The Society has no purchased or originated credit impaired assets and has not applied any simplified approaches.

5. Credit risk

5.3 Impairment provisions (continued)

5.3.1 Impairment of loans and advances to customers (continued)

The Society defines a financial asset as in default, which is fully aligned with the definition of credit-impaired, when it is more than 90 days past due on contractual repayments.
It is the Society's policy to consider a financial instrument as 'cured' and therefore reclassified out of Stage 3 when none of the default criteria have been present for at least twelve consecutive months for forbearance defaults and nine months for any other defaults. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated position, at the time of the cure, and whether there has been a significant increase in credit risk compared to initial recognition.

The Society considers a financial instrument to have experienced a significant increase in credit risk when one or more of the following criteria has been met:

Financial instrument	Definition of significant increase in credit risk
2021 Loans and advances to customers – Retail (residential and BTL)	• Over 30 days past due on contractual repayments; • Change in PD exceeds relative threshold of 100% AND absolute threshold of 0.5%; or • In forbearance;
2020 Loans and advances to customers – Retail (residential and BTL)	• Over 30 days past due on contractual repayments; • In forbearance • Lifetime probability of default doubled since origination: and • Lifetime probability of default greater than 1%.
2021 Loans and advances to customers - SBL	• Over 30 days past due on contractual repayments; • Change in PD exceeds relative threshold of 100% AND absolute threshold of 0.5%; or • In forbearance.
2020 Loans and advances to customers - SBL	• Over 30 days past due on contractual repayments; • On management watchlist; • Lifetime probability of default doubled since origination; or • In forbearance.

During the year, the Society has updated its SICR criteria. This has been treated as a change in accounting estimate and further disclosed in note 15 and page 62 of the 2021 Annual Reports and Accounts which are published on The Nottingham's website (www.thenottingham.com).

5. Credit risk

5.3 Impairment provisions (continued)

5.3.1 Impairment of loans and advances to customers (continued)

The Society adopted the transitional arrangements for IFRS 9 adjustments under Article 473a of CRR, on implementation of IFRS 9 in 2018. However, due to a net release of impairment provision being recognised on day one, there was no transitional adjustment to CET1 capital recognised in previous years. Following regulatory amendments to the calculation methodology to take into account the impact of Covid-19 events on the expected credit loss outputs, the Society has recognised an IFRS 9 transitional adjustment of £1.6m at 31 December 2021 (2020: £2.3m).

The resultant impairment charge is deducted from the appropriate asset values in the balance sheet. Details of past due loans and expected credit loss by stage split by Days Past Due (DPD) at 31 December 2021 are shown in the table below.

31 December 2021	Loans fully secured on residential property £m	Loans fully secured on land £m	Total £m
Stage 1: 12 month expected credit losses			
< 30 days past due	2,666.7	215.1	2,881.8
Stage 2: Lifetime expected credit losses			
< 30 days past due	111.5	15.5	127.0
> 30 days past due	5.8	1.0	6.8
Stage 3: Lifetime expected credit losses			
< 90 days past due	12.1	0.7	12.8
> 90 days past due	4.1	0.3	4.4
Total Exposure	**2,800.2**	**232.6**	**3,032.8**
ECL allowance	1.7	1.4	**3.1**
Release for the year	(0.1)	(1.3)	**(1.4)**

The values shown in the table relate to the full value of the loan, not just the amount past due. All loans are UK based.

The table below details the position of impairment provisions, on an IFRS 9 basis.

	31 Dec 2021 Loans fully secured on residential property £m	31 Dec 2021 Loans fully secured on land £m	31 Dec 2021 Total £m	31 Dec 2020 Loans fully secured on residential property £m	31 Dec 2020 Loans fully secured on land £m	31 Dec 2020 Total £m
Expected Credit Loss allowance						
Stage 1	1.4	0.8	**2.2**	0.5	1.5	**2.0**
Stage 2	0.2	0.5	**0.7**	1.1	0.7	**1.8**
Stage 3	0.1	0.1	**0.2**	0.2	0.5	**0.7**
Total	**1.7**	**1.4**	**3.1**	**1.8**	**2.7**	**4.5**

5. Credit risk

5.3 Impairment provisions (continued)

5.3.1 Impairment of loans and advances to customers (continued)

The tables below reconcile the movement in both gross balances and expected credit losses in the period.

Gross Balances	Non-credit impaired		Credit impaired	Total
	Subject to 12 month ECL	Subject to lifetime ECL	Subject to lifetime ECL	
	Stage 1 £m	Stage 2 £m	Stage 3 £m	£m
At 1 January 2021	1,913.4	1,183.9	8.9	3,106.2
Stage transfers:				
Transfers from stage 1 to stage 2	(44.7)	44.7	-	-
Transfers to stage 3	(3.9)	(8.1)	12.0	-
Transfers from stage 2 to stage 1[1]	923.1	(923.1)	-	-
Transfers from stage 3	2.1	0.8	(2.9)	-
Net movement arising from transfer of stage	876.6	(885.7)	9.1	-
New assets originated[2]	494.6	34.0	1.1	529.7
Net further lending/repayments and redemptions	(402.8)	(198.4)	(1.9)	(603.1)
At 31 December 2021	**2,881.8**	**133.8**	**17.2**	**3,032.8**

Expected Credit Loss allowance	Non-credit impaired		Credit impaired	Total
	Subject to 12 month ECL	Subject to lifetime ECL	Subject to lifetime ECL	
	Stage 1 £m	Stage 2 £m	Stage 3 £m	£m
At 1 January 2021	2.0	1.8	0.7	4.5
Stage transfers:				
Transfers from stage 1 to stage 2	-	-	-	-
Transfers to stage 3	-	-	-	-
Transfers from stage 2 to stage 1	1.1	(1.1)	-	-
Transfers from stage 3	0.1	0.1	(0.2)	-
Net movement arising from transfer of stage	1.2	(1.0)	(0.2)	-
New assets originated[1]	0.5	0.1	-	0.6
Further lending/repayments and redemptions	(0.8)	(0.1)	-	(0.9)
Changes in risk parameters in relation to credit quality	(0.7)	(0.1)	(0.3)	(1.1)
At 31 December 2021	**2.2**	**0.7**	**0.2**	**3.1**

[1] Transfers from stage 2 to stage 1 in the period is impacted by a refinement of SICR criteria as outlined in note 1 of the Annual Report and Accounts.
[2] New assets originated enter at stage 1. The balances presented are the final position as at 31 December 2021.

5. Credit risk

5.3 Impairment provisions (continued)

5.3.1 Impairment of loans and advances to customers (continued)

Gross Balances	Non-credit impaired		Credit impaired	Total
	Subject to 12 month ECL Stage 1 £m	Subject to lifetime ECL Stage 2 £m	Subject to lifetime ECL Stage 3 £m	£m
At 1 January 2020	2,471.0	676.8	5.8	3,153.6
Stage transfers:				
Transfers from stage 1 to stage 2[1]	(737.1)	737.1	-	-
Transfers to stage 3	(1.6)	(4.5)	6.1	-
Transfers from stage 2 to stage 1	115.2	(115.2)	-	-
Transfers from stage 3	0.3	1.5	(1.8)	-
Net movement arising from transfer of stage	(623.2)	618.9	4.3	-
New assets originated[2]	447.1	24.1	0.7	471.9
Net further lending/repayments and redemptions	(381.5)	(135.9)	(1.9)	(519.3)
At 31 December 2020	**1,913.4**	**1,183.9**	**8.9**	**3,106.2**

Expected Credit Loss allowance	Non-credit impaired		Credit impaired	Total
	Subject to 12 month ECL Stage 1 £m	Subject to lifetime ECL Stage 2 £m	Subject to lifetime ECL Stage 3 £m	£m
At 1 January 2020	0.1	0.7	0.8	1.6
Stage transfers:				
Transfers from stage 1 to stage 2	-	-	-	-
Transfers to stage 3	-	-	-	-
Transfers from stage 2 to stage 1	0.1	(0.1)	-	-
Transfers from stage 3	-	0.1	(0.1)	-
Net movement arising from transfer of stage	0.1	-	(0.1)	-
New assets originated[1]	0.3	-	-	0.3
Further lending/repayments and redemptions	-	-	(0.1)	(0.1)
Changes in risk parameters in relation to credit quality	1.5	1.1	0.1	2.7
At 31 December 2020	**2.0**	**1.8**	**0.7**	**4.5**

[1] The level of gross loan transfers from stage 1 to stage 2 in the period is impacted by the highly sensitive models and 1% floor within its SICR criteria.
[2] New assets originated enter at stage 1. The balances presented are the final position as at 31 December 2020.

Further information on ECL allowances under IFRS 9 can be found in note 15 of the 2021 Annual Report and Accounts, which are published on The Nottingham's website (www.thenottingham.com).

5. Credit risk

5.3 Impairment provisions (continued)

5.3.2. Impairment of treasury assets

Under IFRS 9, the Society assesses on a forward-looking basis the ECL associated with its financial assets carried at amortised cost and FVOCI. This includes the Society's treasury assets.

The Society reviews the external credit ratings of its liquid assets at each reporting date. Those assets, which are of investment grade or higher, are considered to have low credit risk and therefore are assumed to have not had a significant increase in credit risk since initial recognition. This includes the Society's debt security portfolio. The Society's policy to allow only high quality, senior secured exposures to Residential Mortgage Backed Securities (RMBS) and Covered Bonds ensures continued Society receipt of contractual cash flows in stressed scenarios. For all other wholesale liquidity balances, a simple model calculates the ECL allowance, based on externally provided 12-month Probability of Default (PD) rates for individual counterparties.

All of the Society's treasury assets are classified as stage 1 for ECL calculation purposes under IFRS 9. The Society does not have any expected credit loss allowance held against its liquidity portfolio as at 31 December 2021(2020: £nil) as the stage 1 ECL calculated is immaterial to the financial statements.

5.4. Credit risk mitigation

The Nottingham employs a range of techniques and strategies to reduce the credit risks of its retail and wholesale lending.

5.4.1. Loans and advances to customers

All mortgage loan applications are assessed with reference to The Nottingham's retail credit lending policies, which includes assessing applicants for potential fraud risk, and which is approved by the Board.

For new customers the first element of the retail credit control framework is achieved via credit scoring and affordability assessment, which assesses the credit quality of potential customers prior to making loan offers. Customers' credit scores combine demographic and financial information. A second element is lending policy rules, which are applied to new applications to ensure that they meet the risk appetite of The Nottingham. All mortgage applications are reviewed to ensure that any additional lending criteria are applied and that all information submitted within the application is validated.

For existing customers who have been added to the lending portfolio, management use behavioural scorecards to review the ongoing creditworthiness of customers by determining the likelihood of them defaulting over a rolling 12-month period together with the amount of loss if they do default.

5. Credit risk

5.4 Credit risk mitigation (continued)

5.4.1 Loans and advances to customers (continued)

The Society has remained committed to providing support to those of our members who have experienced difficulties in meeting their mortgage payments due to the impacts of the Covid-19 pandemic. The Society fully complied with all regulatory guidance offering affected customers payment deferrals or other tailored support during 2020 and 2021. The government-led payment deferral scheme came to an end during 2021, with the significant majority of customers returning to fully paying status, and only a small number of customers requiring further forbearance support.

In the event of a default, the ultimate source of collateral remains the borrower's property. The Nottingham takes a first charge on all mortgage lending. The collateral is supported by an appropriate form of valuation using either an independent firm of valuers or an Automated Valuation Model (AVM).

The Nottingham insures its residential mortgage book against losses using Mortgage Indemnity Guarantee (MIG) insurance. MIG insurance is taken on all purchases where the loan to value (LTV) exceeds 80%. However, for prudence, no credit risk mitigation benefits have been taken from this insurance when assessing its Pillar 1 capital requirements.

The Nottingham does not have any exposure to the sub-prime market.

5.4.2. Treasury assets & counterparty credit risk

In addition to retail credit risks, The Nottingham is also exposed through its treasury function. This arises from counterparties who may be unable to repay loans and other financial instruments that the treasury team holds as part of its liquidity portfolio. A regular assessment of investment quality is undertaken by the Treasury Risk team which is reported monthly to the ALCO.

Instruments used for risk management purposes include derivative financial instruments (derivatives), which are contracts whose value is derived from one or more underlying price, rate or index inherent in the contract or agreement, such as interest rates, exchange rates or stock market indices.

The objective of The Nottingham in using derivatives is in accordance with the Building Societies Act 1986 and is to limit the extent to which The Nottingham will be affected by changes in interest rates. Derivatives are not used in trading activity or for speculative purposes.

The derivative instruments used by The Nottingham in managing its statement of financial position risk exposures are interest rate swaps. These are used to protect The Nottingham from exposures arising principally from fixed rate mortgage lending, fixed rate savings products and fixed rate wholesale funding. An interest rate swap is a contract to exchange one set of interest rate cash flows for another. Such swaps result in the economic exchange of interest rates. No exchange of principal takes place. Instead, interest payments are based on notional principal amounts agreed at inception of the swap. The duration of the interest rate swap is generally short to medium term and their maturity profile reflects the nature of the exposures arising from the underlying business activities.

5. Credit risk

5.4 Credit risk mitigation (continued)

5.4.2 Treasury assets & counterparty credit risk (continued)

The Nottingham applies fair value hedging techniques to reduce its exposure to interest rate risk as follows:

Activity	Risk	Fair value interest rate hedge
Fixed rate mortgage	Increase in interest rates	Society pays fixed, receives variable
Fixed rate savings bond	Decrease in interest rates	Society receives fixed, pays variable
Fixed rate funding	Decrease in interest rates	Society receives fixed, pays variable

Under the European Securities & Market Authority (ESMA) regulations it has become mandatory for all eligible derivate instrument transactions to be centrally cleared once an institution's exposure exceed a prescribed threshold. The Nottingham centrally clears all eligible derivatives. As such the vast majority of The Nottingham's derivatives are fully collateralised with a central clearing member, and therefore mitigating counterparty credit risk.

The table below shows the derivative contracts held using the Mark to Market (MTM) method:

	Replacement Cost £m	Credit Exposure £m	Total Exposure £m
31 December 2021	22.5	14.5	37.0
31 December 2020	2.3	15.1	17.4

6. Market Risk

6. Market risk

Market risk is the risk of changes to The Nottingham's financial condition caused by market variables, in particular interest rates. Differing interest rate characteristics between assets and liabilities, and in particular fixed rate products, expose The Nottingham to the risk of either a reduction in interest income or an increase in interest expense relative to variable rate interest flows.

The instruments that are used for market risk management purposes include derivative financial instruments (derivatives). The objective of The Nottingham in using derivatives is in accordance with the Building Societies Act 1986 and is to limit the extent to which The Nottingham will be affected by changes in interest rates.

The treasury risk team is responsible for the day-to-day oversight of market risks. The balance sheet is subjected to a range of stress tests, including a 2% shift in interest rates on a weekly basis and standardised regulatory stress test performed quarterly. The results are measured against risk appetite for market risk. In addition, management review interest rate basis risk and its potential impact on earnings. Risk positions are reviewed monthly by ALCO and reported through to the Executive Risk and Board Risk Committees.

The Nottingham's sensitivity to this measurement (in terms of economic value) was:

	31 December 2021 £m	31 December 2020 £m
2% shift in interest rates	0.1	0.9

A Board approved policy statement defines the maximum acceptable level of interest rate risk as well as the steps that may be taken to reduce it.

7. Operational risk

7. Operational risk

The Nottingham defines operational risk as the risk of loss resulting from human factors, inadequate or failed internal processes and systems, or from external events. Operational risk exists in every aspect of The Nottingham's business activities. Proactive management of operational risk is essential in helping the Society achieve both short-term operational objectives and longer-term strategic goals.

To ensure the effective monitoring and reporting of risk, The Nottingham maintains a number of risk registers. These risk registers help management assess the probability and impact of the risks identified, and the effectiveness of mitigating controls.

Furthermore, as part of the risk management framework all business areas are required to maintain functional risk registers. These documents include an assessment of the key risks faced by each functional area and an evaluation of the controls in place to ensure that risks are managed within risk appetite. The functional risk registers are used by management to document the effective management of both risks and controls within their business areas.

The Operational Risk & Resilience Committee, which comprises various senior managers, oversees the management of operational risk. In so doing it monitors a range of management information and other reports on The Nottingham's operational risk exposures. It also reviews the results of the operational risk scenario analysis that is performed for the purposes of The Nottingham's Internal Capital Adequacy Assessment Process.

The Operational Risk & Resilience Committee reports regularly to the Executive Risk Committee and then to the Board Risk Committee that in turn reports to the Board.

7.1. Minimum capital requirements for operational risk

The Nottingham calculates its operational risk capital requirement using the Basic Indicator Approach. This is determined in relation to the Society's net income averaged over the previous 3 years.

The Nottingham's minimum (Pillar 1) capital requirement for operational risk at 31 December is:

	2021 Operational risk capital requirement £m	2020 Operational risk capital requirement £m
Basic Indicator Approach	6.5	6.3

8. Liquidity risk

Liquidity risk is the risk that The Nottingham will not have sufficient financial resources available to meet its obligations as they fall due, under either normal business conditions or a stressed environment.

It is The Nottingham's policy that an appropriate amount and mix of liquidity is held in order to:

- Meet obligations as they fall due (including any unexpected adverse cash flow or stressed environment);
- Smooth out the effect of maturity mismatches; and
- Maintain public confidence in a stressed environment.

The monitoring of the liquidity policy is performed regularly as set out in the Board approved risk appetite and policy statements. Compliance with these policies is reported to the Assets and Liability Committee monthly, and also to the Executive Risk Committee and Board Risk Committee.

The Nottingham maintains a diverse funding base and ensures compliance with applicable regulatory requirements. Defined control limits determine the overall level of liquidity to be maintained. The base level and composition of The Nottingham's liquidity is subject to PRA guidance. The Nottingham's Internal Liquidity Adequacy Assessment Process (ILAAP) is reviewed annually and approved by the Board Risk Committee. The ILAAP forms a central part of The Nottingham's risk management and includes stress testing which analyses a range of severe scenarios to confirm that The Nottingham holds an adequate amount of available liquidity.

Furthermore, The Nottingham has documented within its Recovery and Resolution Plan metrics that would indicate an emerging market-wide or Nottingham-specific stress event. The Plan includes a range of options available to The Nottingham in the event of such a stress to ensure an adequate level of liquidity is maintained.

The Nottingham is required to be compliant with the Liquidity Coverage Ratio (LCR), which measures the amount of high-quality liquid assets relative to estimated net stressed cash outflows within a 30-day period.

The table below shows the major components of the LCR on an average basis at each quarter end, based on the previous twelve months of data.

	Total weighted value			
	Quarter ending 31 March 2021 £m	Quarter ending 30 June 2021 £m	Quarter ending 30 September 2021 £m	Quarter ending 31 December 2021 £m
Liquidity buffer	533	519	513	512
Total net cash outflows	240	247	248	250
Liquidity coverage ratio (%)	222	211	208	206

12 data points are used in the calculation of the averages for each period of reporting. The LCR at 31 December 2021 was 216% (31 December 2020: 215%). This is well in excess of the minimum regulatory requirements of 100%.

9. Other risks

9. Other risks

9.1. Business conduct risk

Business conduct risk is the risk that The Nottingham does not conduct its business activities in a clear, transparent and fair manner. The Nottingham must ensure it complies with the FCA's Principles of Business (PRIN).

Each business area is responsible for ensuring compliance with all regulatory and legal obligations with regard to conduct of business that affect its area of operations.

The Legal, Regulatory & Conduct Risk Committee, supports the Board Risk Committee through the Executive Risk Committee by overseeing the manner in which The Nottingham conducts business with its members and customers.

It achieves this by ensuring effective governance and control frameworks are in place, maintained and monitored. In addition, the Committee will identify and drive actions to address priorities for improvement that will enable The Nottingham to deliver and sustain self-imposed targets in customer satisfaction and ensuring good customer outcomes.

9.2. Business risk

Business risk is the risk of unexpected changes in the external environment that have the potential to affect The Nottingham's business model either through the level of demand for The Nottingham's products and services and/or its ability to meet it.

The Nottingham looks to mitigate its exposure to business risk by having a diverse range of products and services so that its income source is not reliant on one product or one area of its business.

The Board monitors The Nottingham's exposure to business risk. In so doing it receives a range of management information on a monthly basis from the Executive Risk Committee.

9.3. Strategy risk

Strategy risk is the risk that The Nottingham pursues an inappropriate strategy or that risks associated with its implementation are not fully recognised. When discussing strategy, the Board takes care to ensure that risks such as system changes, long term funding approach and acquisitions are evaluated and that management has plans to mitigate them.

The Executive Risk Committee and Board Risk Committee oversee the detailed evaluation of these risks.

9. Other risks

9.4. Regulatory and compliance risk

These risks are the risk of loss from failure to comply with statutory and regulatory requirements. The Nottingham, being a retailer of mortgage, savings and insurance products, is regulated by the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) and as such must comply with relevant policies.

The Nottingham must also comply with the relevant sections of the Building Societies Act 1986 and other legal requirements.

Each business area is responsible for ensuring compliance with all regulatory and legal requirements that affect its area of operations. Oversight of the business is undertaken by the Compliance function.

9.5. Concentration risk

As a regional building society, The Nottingham is exposed to concentration risk. This includes the potential for geographical and product concentrations in terms of both its mortgage book and wholesale activities.

Retail credit risk

The Nottingham has geographic concentration risk as it is regionally based in the East Midlands and domiciled in the UK, acquiring all of its current business from England and Wales.

Geographic concentration risk is monitored by observing the spread of The Nottingham's exposure by region and the impact of house price changes during various economic scenarios. The risk is monitored on an ongoing basis by Retail Credit Committee.

Wholesale credit risk

The Nottingham’s prudent approach to wholesale lending creates a potential source of concentration risk if, for example, there is a general tightening of credit conditions.

Minimum acceptable credit ratings are approved by the Board Risk Committee with ALCO reviewing details of changes to counterparty ratings on a monthly basis.

The Liquidity Risk policy sets out the amounts, products and counterparties under which liquid assets can be held with a control framework set to monitor these.

Funding concentration risk is reduced by maintaining a range of controls to ensure there is sufficient diversification across both wholesale and retail, including on a combined basis. Treasury monitors large exposures on a daily basis and reports any exceptions to policy to ALCO. Limits are monitored on an ongoing basis and are formally reviewed at least once a year as part of the overall review of the Liquidity Risk policy.

9. Other risks

9.6. Pension scheme obligation risk

Pension liability risk is the risk that there may be a shortfall with respect to meeting the benefits that are due within a defined benefit pension scheme.

The Nottingham operates a contributory defined benefit pension scheme. The scheme closed to new members in 1997 and closed to future service accrual from 31 January 2009. The membership consists of pensioners, those with deferred benefits and current members.

The Nottingham is exposed to the risk that it will need to make further unexpected future contributions to the scheme. The risk may arise from a number of factors including:

- A fall in the discount rate increasing the present value of scheme liabilities;
- An increase in life expectancy increasing the present value of scheme liabilities; and
- A fall in equity prices reducing the fair value of scheme assets.

The Nottingham uses independent actuarial advice to advise on the risks that may lead to an increase in the deficit. This is reviewed by ALCO and the Board.

9.7. Model risk

Model governance risk is defined as the potential loss an institution may incur, as a consequence of decisions that could be principally based on the output of models, due to errors in the development, implementation or use of such models.

The Nottingham has a low appetite for model governance risk and makes resources available to mitigate Model Governance Risks to an acceptable level primarily within the constraints of impact to The Nottingham, its customers and cost.

9.8. Climate change risk

The Nottingham's Board is ultimately accountable for all climate change related matters. The Executive Committee is responsible for determining the Society's strategic response to climate change. The Board Risk Committee and the Executive Risk Committee are responsible for oversight of climate-related risks which are considered within the strategy risk category. All committees are supported by the Climate Change Working Group which provides a central point of collation and focus for all climate-related activities at the Society, including inputs from The Nottingham's Responsible Society strategic initiative.

The Climate Change Working Group is chaired by the Chief Executive Officer, who leads the Society's response to climate change. The working group is attended by Executive team and Leadership team members from across the business. It meets regularly to co-ordinate activities and assesses climate change risk across two main categories. Physical risk considers the impact of physical effects of climate change or weather-related events such as flooding. Transitional risk assesses the transition to a low-carbon and climate resilient future such as changes in policy and regulation.

9. Other risks

9.8 Climate change risk (continued)

The Nottingham recognises that climate change impacts all areas of the business and in order to capture all of the material touchpoints, climate change is embedded within the Society's enterprise-wide risk management framework. Climate-related risks are being considered as part of corporate planning scenarios, including the impact on our business and members of how any intended government action plans to become net zero by 2050.

The risk management report on pages 31 to 35 and sustainability report on pages 22 to 25 of the Annual report and Accounts include further disclosures in relation to the Society's response to managing climate-related risks.

10. Securitisation

10.1. Overview

The Society has securitised a number of mortgage loans by pooling them together and transferring the beneficial interest of the loans to a Special Purpose Vehicle (SPV), Arrow Mortgage Finance No.1 Limited (Arrow 1).

The Society has a bilateral securitisation facility to raise wholesale funding and provide funding diversification. Securitisation funding forms a balanced portion of the Society's wholesale funding, which helps generate liquidity from illiquid asset types, i.e. residential mortgage loans.

10.2. Originated securitisation

Originated securitisation transactions involve the sale of a portfolio of mortgage assets to another entity, the SPV. An SPV is a purposely created company where the ultimate holding company is unrelated to the originator of the loans, and is usually held by a trust, meaning Nottingham Building Society does not legally own the SPV.

The Society has securitised certain residential mortgage loans by the transfer of the beneficial interest in such loans to a SPV. The legal title to the mortgages remains with the Society and would only transfer to the SPV in limited circumstances, including the insolvency of the Society.

The table below sets out the roles that Society takes in relation to a securitisation transaction. The Society retains the first loss element.

	Society's role in the securitisation process	
Securitisation Company	Originator, Seller, Administrator, Cash Manager	Subordinated Loan Provider
Arrow 1	✔	✔

To raise funds for the purchase (being initially equal to the face value of the assets), a senior bilateral loan was provided to the SPV by the investor. Interest and principal received from the underlying assets is used to fund the payment of senior loan interest and principal. Any residual income after paying the interest and principal and any fees and other operating costs is distributed to the originating entity.

As there has been no transfer of significant credit risk, the Society does not calculate specific risk weighted exposure amounts for any positions it holds in the securitisation, or assets awaiting securitisation, and these continue to be calculated in line with the capital requirements consistent with other mortgage assets.

10. Securitisation

10.2 Originated securitisation (continued)

The position on originated securitisations at 31 December is detailed below.

31 December 2021 Securitisation company	Issue date	Gross assets securitised £m	Senior Loan £m	Subordinated Loan £m	Underlying assets past due and impaired £m
Arrow 1	July 2016	147.6	127.1	26.6	-

31 December 2020 Securitisation company	Issue date	Gross assets securitised £m	Senior Loan £m	Subordinated Loan £m	Underlying assets past due and impaired £m
Arrow 1	July 2016	207.1	191.2	26.6	-

10.3. Treatment of originated securitisations

Residential mortgages have been pledged by the Society in order to raise wholesale funding. The pledged mortgages remain on the balance sheet of the Society, as it has retained substantially all the risks and rewards of ownership. These assets are held at amortised cost. Arrow 1 is fully consolidated into the Group accounts in accordance with IFRS 10. The transfer of mortgage loans to the securitisation company is not treated as a sale by the Society (as originator), and therefore no gains are recognised.

At 31 December 2021, there are no assets awaiting securitisation (2020: none).

10.4. Purchased securitisation positions

The Society invests in mortgage backed securities as part of its overall investment strategy to maintain a diverse and liquid portfolio.

Purchases and retention of residential mortgage backed securities are undertaken within a clearly defined liquidity risk policy. All residential mortgage backed securities are monitored on a regular basis and if the credit rating deteriorates below AAA level the position is reviewed. The Society holds no re-securitisations.

The valuation process of our investments in securitisation exposures primarily focuses on quotations from third parties and observed trade levels. The process has been consistent through 2021.

The Society's exposure to purchased securitisation positions amounted to £61.5m at 31 December 2021 (2020: £46.7m).

At 31 December 2021, no purchased securitisation positions were past due or impaired.

11. Asset encumbrance

Article 100 of the CRR requires the institutions to report to the competent authorities the level of their repurchase agreements, securities lending and all forms of asset encumbrance. From a legal perspective, asset encumbrance is a claim against a property by another party. From a financial perspective, such claims have traditionally taken the form of security interests, such as pledges, given on assets by a borrower to a lender. In other words, giving collateral encumbers assets.

The majority of The Nottingham's encumbrance is driven by secured financing activities, which include transactions in repo and collateral swaps as well as securitisation. The remaining encumbrance is driven by hedging derivatives. The Society maintains a level of asset encumbrance in line with the scale and scope of its operations.

A proportion of wholesale funding is provided on a secured basis where, generally, the collateral provided is in the form of mortgage pools. This means that both the credit quality and amount of mortgages have a direct impact on the amount of funding available to The Nottingham.

The majority of this secured funding is in the form of TFSME drawings with the Bank of England.

Having unencumbered mortgage pools also provides The Nottingham with access to the operations that fall within the Bank of England's Sterling Monetary Framework (e.g. ILTR); therefore these unencumbered pools are a source of liquidity. As well as providing collateral to the Bank of England, mortgage pools are also used to collateralise secured funding obtained from market counterparties.

The levels of asset encumbrance are monitored via control limits and triggers, which are forecast as part of the Financial Plan.

11.1. Encumbered and unencumbered assets

The tables below show components of our encumbered and unencumbered assets for the year ended 31 December 2021, calculated as the median of the end-of-period values for each of the four quarters in the year.

31 December 2021	Carrying amount of encumbered assets £m	Fair value of encumbered assets £m	Carrying amount of unencumbered assets £m	Fair value of unencumbered assets £m
Assets of the reporting institution	**652.2**	-	**3,016.8**	-
Debt securities	5.0	5.0	230.3	230.3
- of which: issued by general governments	5.0	5.0	37.7	37.7
- of which: issued by financial institutions	-	-	192.6	192.6
Other assets	644.7	-	2,723.6	-

Other assets include loans and advances (including mortgages) and other balance sheet items not listed above.

11. Asset encumbrance

11.2. Collateral received

	31 December 2021	
	Fair value of encumbered collateral received or own debt securities issued £m	Unencumbered: fair value of collateral received or own debt securities issued available for encumbrance £m
Collateral received by the reporting institution	**-**	**-**
Debt securities	-	-
- of which: issued by general governments	-	-
Total assets, collateral received and own debt securities issued	**652.2**	-

11.3. Sources of encumbrance

	31 December 2021	
	Matching liabilities, contingent liabilities or securities lent £m	Assets, collateral received and own debt securities issued other than covered bonds and ABS encumbered £m
Carrying amount of selected financial liabilities	511.7	652.2

12. Remuneration Committee and policy

The primary objective of the Committee is to make recommendations to the Board on the general remuneration policy of The Nottingham and specifically on the remuneration of Executive Directors. The Committee also has oversight of the remuneration of both the Society's senior management team and Remuneration Code staff.

The Society is within the scope of the Regulator's Remuneration Code. As a result, those individuals who comprise Remuneration Code staff also fall within the remit of the Remuneration Committee.

The Committee comprises a minimum of three non-executive directors (one of which acts as Chairman of the Committee) and the Chief Executive, Head of People & Development, Senior Legal Counsel & Company Secretary attend.

Further details regarding the remuneration policy and the role of Remuneration Committee are set out in the Directors Remuneration Report in the 2021 Annual Report and Accounts which are published on The Nottingham's website (www.thenottingham.com).

Appointments to the Board are made on merit and against objective criteria balancing skills, experience, independence and knowledge on the Board. The Society gives consideration to diversity in respect of gender and other measures, both at Board level and in recruitment throughout the business.

12.1. Material risk takers

Material risk takers are defined by the Regulator as 'staff whose activities have a material impact on the firm's risk profile, this includes staff that perform significant influence functions, senior managers and risk takers'. This includes executive and non-executive directors.

The table below sets out the aggregate quantitative remuneration for code staff in relation to their services for The Nottingham for the year ended 31 December 2021.

31 December 2021		Senior Management	Other Code Staff	Non-Executive Directors	Total
Number of staff	No	12	1	7	**20**
Fixed pay	£000	1,886	50	400	**2,336**
Variable pay	£000	247	2	-	**249**
Total	**£000**	**2,133**	**52**	**400**	**2,585**
Proportion of variable to total pay	%	11.6%	4.4%	-	**9.6%**
Deferred variable pay	£000	200	-	-	**200**
Severance payments	£000	-	-	-	**-**

No severance payment and no signing on payments were made to individual material risk takers during the year.

No one individual has received remuneration of EUR1 million or more in 2021.

12. Remuneration Committee and policy

12.2. Remuneration policy

The main components of remuneration are outlined on page 44 of the 2021 Annual Report and Accounts but are summarised below. As a building society, with no share instruments, there are no non-cash forms of remuneration.

Fixed pay	
Basic salary	Grade, market benchmarking and performance driven. Grade is determined using the Willis Towers Watson global grading framework and salaries for roles are determined by using functional external market benchmark data.
Pensions	The Society contributes up to a maximum of 16% of salary or paid as cash allowance (dependent upon age of joining and period of time in the scheme) for members of the Group Personal Pension Plan. The pension benefits relating to the Executive Directors are outlined in the 2021 Annual Report and Accounts.
Benefits	Include the provision of a car allowance, private medical insurance and death in service benefits.
Variable pay	
Variable pay	Material risk takers participate in one discretionary bonus scheme, the Annual Bonus Plan. The bonus scheme is based upon a modular scorecard approach derived from the Society's strategic goals, which include effective risk management. As a mutual, the Society does not issue shares on the Stock Exchange. For this reason, the annual performance pay cannot be based upon Share Option Schemes or Share Incentive plans. The Society is a level three firm (as assets are less than £15bn) and is therefore not subject to the rules on retained shares and other instruments and deferral of variable pay.

13. Contacts

13. Contacts

Should you have any queries regarding this document, please contact:

The Company Secretary
Nottingham Building Society,
Nottingham House,
3 Fulforth Street,
Nottingham,
NG1 3DL

14. Glossary

Additional Tier 1 capital (AT1)	Capital that meets certain rules under CRD IV and which comprises the Society's PIBS but only under the transitional provisions.
Arrears	A customer is in arrears when they are behind in meeting their contractual obligations with the result that an outstanding loan payment is overdue. The value of the arrears is the value of any payments that have been missed.
Basel III	Basel III became effective in the UK on 1 January 2014 through CRD IV and sets out the details of strengthened global regulatory standards on bank capital adequacy and liquidity.
Buy-to-let loans (BTL)	Buy-to-let loans are those loans which are offered to customers buying residential property specifically to let out and generate a rental income.
Capital Requirements Directive (CRD IV)	CRD IV is the European legislation which came into force from 1 January 2014 to implement Basel III. It is made up of the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD), outlining the capital requirements framework and introduced liquidity requirements, which regulators use when supervising firms.
Common Equity Tier 1 capital (CET1)	CET1 capital consists of internally generated capital generated from retained profits, other reserves less intangible assets and other regulatory deductions. CET1 capital is fully loss absorbing.
Common Equity Tier 1 ratio	Common Equity Tier 1 capital as a percentage of risk weighted assets.
Capital Conservation Buffer (CCB)	A buffer to be held by all financial institutions, set at 2.5% of RWA, which can be drawn down in times of stress.
Countercyclical buffer (CYB)	An option available to European Authorities to implement an additional capital buffer to prevent excessive growth in domestic economies.
Counterparty credit risk	Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows.
Credit Quality Steps	A credit quality assessment scale as set out in CRR Articles 111 - 141 (Risk weights under the Standardised Approach to credit risk).
Credit risk	This is the risk that a customer or counterparty fails to meet their contractual obligations.
Debt securities	Assets representing certificates of indebtedness of credit institutions, public bodies or other undertakings excluding those issued by central banks.
Derivative financial instruments	A derivative financial instrument is a contract between two parties whose value is based on an underlying price or index rate it is linked to, such as interest rates, exchange rates or stock market indices. The Society uses derivative financial instruments to hedge its exposure to interest rate risk.

14. Glossary

Expected Credit Loss (ECL)	The present value of all cash shortfalls over the expected life of the financial instrument. The term is used for accounting for impairment provisions under the new IFRS 9 standard.
Exposure	The maximum loss a financial institution might suffer if a borrower, counterparty or group fails to meet their obligations.
External Credit Assessment Institution (ECAI)	An ECAI (e.g. Moody's, Standard and Poor's, Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.
Fair value	Fair value is the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arm's length transaction.
Fair value through other comprehensive income (FVOCI)	Financial assets held at fair value on the balance sheet with changes in fair value being recognised through other comprehensive income.
Financial Conduct Authority (FCA)	The statutory body responsible for conduct of business regulation and supervision of UK authorised firms.
General Reserves	The accumulation of the Society's historic and current year profits which is the main component of Common Equity Tier 1 capital.
IFRS 9	IFRS 9 'Financial Instruments' is the accounting standard applicable from 1 Jan 2018, which includes requirements for the classification and measurement of financial instruments, impairment of financial assets and hedge accounting.
Impairment	The term impairment is usually associated with a long-lived asset that has a fair market value less than the historical cost (or book value) of the asset.
Impaired loans	Loans where there is objective evidence that an impairment event has occurred, meaning that the Society does not expect to collect all the contractual cash flows or expect to collect them later than they are contractually due.
Interest rate risk	The risk of loss due to a change in market interest rates. Interest rate risk can have an impact on Society's mortgages and savings products.
Internal Capital Adequacy Assessment Process (ICAAP)	The Society's own assessment, as part of Basel III requirements, of the levels of capital that it needs to hold in respect of its regulatory capital requirements for risks it faces under a business as usual scenario including stress events.
Internal Liquidity Adequacy Assessment Process (ILAAP)	The Society's own assessment of the liquidity resources it requires in order to remain within the risk tolerances it has set. This will include an evaluation of potential stresses based on multiple market environments.
Leverage Ratio	The ratio of Tier 1 capital divided by the total exposures, which includes on and off-balance sheet items.
Liquid Assets	Total of cash in hand, loans and advances to credit institutions, and debt securities.

14. Glossary

Liquidity Resources	Assets held in order to manage liquidity risk. Liquidity resources comprise cash and balances with the Bank of England, UK Government securities and multilateral development banks, other securities and bank deposits and Bank of England approved mortgage portfolios.
Loan to value ratio (LTV)	LTV expresses the amount of a mortgage as a percentage of the value of the property.
Market risk	The risk that movements in market risk factors, including foreign exchange rates, interest rates, credit spreads and customer-driven factors will create potential losses or decrease the value of the Society balance sheet.
Member	A person who has a share investment or a mortgage loan with the Society.
Minimum capital requirement	The minimum amount of regulatory capital that a financial institution must hold to meet the Basel III Pillar 1 requirements for credit, market and operational risk.
Multilateral Development Banks	A multilateral development bank is an international financial institution chartered by two or more countries for the purpose of encouraging economic development.
Operational risk	The risk of loss arising from inadequate or failed internal processes, people and systems, or from external events.
Other items	Other assets not included in other definitions.
Past due items	Loans which are 90 days or more in arrears.
Permanent Interest Bearing Shares (PIBS)/ Subscribed Capital	Unsecured, deferred shares of the Society that are a form of Additional Tier 1 capital under the transitional rules of CRD IV. PIBS rank behind the claims of all depositors, payables and investing members of the Society. PIBS are also known as subscribed capital.
Pillar 1	The parts of CRD IV which set out the minimum capital requirements for credit, market and operational risk.
Pillar 2	Those aspects of CRD IV which set out the process by which the Society should review its overall capital adequacy, and the processes under which the regulators / supervisors evaluate how well financial institutions are assessing their risks and take appropriate actions in response to the institutions' assessments.
Pillar 3	The part of CRD IV governing the production of this document. It sets out information disclosures relating to risks, the amount of capital required to cover these risks, and the approach to risk management.
Probability of default (PD)	A component of the IFRS 9 expected credit loss calculation. An estimate of the probability that a borrower will default on their credit obligation over a fixed time period. A 12-month ECL uses a 12 month PD, whilst a lifetime ECL uses the estimated PD over the remaining contractual life of the loan.
Prudential Regulation Authority (PRA)	The statutory body responsible for the prudential supervision of banks, building societies, insurers and small number of significant investment firms in the UK. The PRA is a subsidiary of the Bank of England.
Residential Loans	Loans that are loaned to individuals rather than institutions and are secured against residential property.
Retail	The portion of any residential mortgage exposure above 80% LTV, as per CRR Article 125.
Risk appetite	The articulation of the level of risk that the Society is willing to accept (or not accept) in order to safeguard the interests of the Society's members whilst also achieving business objectives.

14. Glossary

Risk weighted assets (RWA)	The value of assets, after adjustment, under the relevant Basel III capital rules to reflect the degree of risk they represent.
Secured Business Lending (SBL)	Loans secured on commercial property which is only made available to Small and Medium sized Enterprises and includes limited company buy-to-let lending.
Secured by Mortgages on Residential Property	Residential mortgages where LTV is less than or equal to 80%, as per CRR Article 125.
Securitisation	The process by which a group of assets (usually mortgage loans) is aggregated into a pool which is used to back the issuance of new securities. A company transfers assets to a special purpose vehicle which secures funding backed by those assets. The Society has established a securitisation structure (using residential mortgages as assets) as part of its funding activities.
Shares	Funds deposited by a person in a retail savings account with the Society. Such funds are recorded as liabilities for the Society.
Significant increase in credit risk (SICR)	A significant increase in credit risk on a financial asset is judged to have occurred when an assessment, using quantitative and qualitative factors, identifies at a reporting date that the credit risk has moved significantly since the last asset was originally recognised.
Special Purpose Vehicle (SPV)	A legal entity (usually a limited company) created to fulfil narrow, specific or temporary objectives. In the context of the Society, the SPV is used in relation to securitisation activities.
Stage 1	A component of the IFRS 9 expected credit loss calculation. Stage 1 assets are assets which have not experienced a significant increase in credit risk since the asset was originally recognised on the balance sheet. 12 month ECL are recognised as the impairment provision for all financial assets on initial recognition. Interest revenue is the EIR on the gross carrying amount.
Stage 2	A component of the IFRS 9 expected credit loss calculation. Stage 2 assets have experienced a significant increase in credit risk since initial recognition. Lifetime ECL is recognised as an impairment provision. Interest revenue is the EIR on the gross carrying amount.
Stage 3	A component of the IFRS 9 expected credit loss calculation. Stage 3 assets are identified as in default and considered credit impaired. Lifetime ECL is also recognised as an impairment provision. Interest revenue is the EIR on the net carrying amount.
Standardised Approach	The basic method used to calculate capital requirements for credit risk. In this approach the risk weighting used in the capital calculation are determined by specified percentages.
Term Funding Scheme (TFS) Term Funding with additional incentives for SMEs (TFSME)	Schemes launched by the Bank of England and HM Treasury, which provides funding to participating banks and building societies with the aim of stimulating lending within the economy.
Tier 1 capital	A component of regulatory capital, it comprises CET1 and AT1.
Tier 1 ratio	Tier 1 capital as a percentage of risk weighted assets.
Tier 2 capital	Comprises the collective impairment allowance (for exposures treated on a Standardised basis), less certain regulatory deductions.
Total Capital Requirement (TCR)	The total amount of capital the regulator requires the Society to hold, which is made up of Pillar 1 and Pillar 2A capital.
Wholesale funding	Amounts owed to credit institutions, amounts owed to other customers and debt securities in issue.