Pillar 3
Disclosure document

As at 31 December 2019

Darlington
Building Society

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Contents

Terms and Conditions

This Pillar 3 disclosure relates to Darlington Building Society (“the Society”) as a Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) regulated entity. The Society and its subsidiary companies (together “the Group”), does not include any other regulated entities..

All balances are presented in £’000 unless stated otherwise.

DARLINGTON BUILDING SOCIETY Pillar 3 Disclosures as at 31st December 2019

1. Introduction

Background

The Society is a mutual organisation run for the benefit of its members. The Society seeks to protect members' savings by holding sufficient capital at all times. The Society's core capital predominantly comprises of General Reserves as shown in the Balance Sheet.

The Society has one wholly-owned active subsidiary, Darlington Homes Limited (DHL), which owns and manages a number of commercial and residential properties. As described in Table 6 below, DHL is not in scope for regulatory consolidation and as such the following disclosures relate only to the Society as a regulated entity.

The Society operates under the Capital Requirements Directive (CRD) IV requirements "Basel III", a comprehensive set of reform measures developed by the Basel Committee on Banking Supervision to strengthen the regulation, supervision and risk management of the banking sector across the world. These measures aim to:

• Improve the banking sector's ability to absorb shocks arising from financial and economic stress, whatever the source • Improve risk management and governance • Strengthen banks' transparency and disclosures.

The Society adopts the 'Standardised Approach' for Credit risk and the 'Basic Indicator Approach' for Operational risk. These approaches are explained in more detail in Section 4 of this document.

Regulation

The PRA is the regulatory body responsible for implementing CRD within the UK. These rules include requirements for the Society to disclose key information about risk and are referred to as "Pillar 3" requirements.

The Society's Pillar 3 Disclosures at December 2019 comprise all information required under Pillar 3, both quantitative and qualitative. They are made in accordance with Part 8 of the Capital Requirements Regulation (CRR) within CRD IV and the European Banking Authority's ('EBA') final standards on revised Pillar 3 Disclosures issued in December 2016. These disclosures are supplemented by subsequent amendments to disclosure requirements, specific additional requirements of the PRA and discretionary disclosures made by the Society.

The Society has calculated capital for prudential regulatory reporting purposes throughout 2019 using the Basel III framework of the Basel Committee ('Basel') as implemented by the European Union ('EU') in the amended Capital Requirements Directive and Regulation ('CRD IV'), and in line with the PRA's Rulebook for the UK banking industry.

The Basel Committee's framework is structured around three 'pillars': the Pillar 1 minimum capital requirements and Pillar 2 supervisory review process are complemented by Pillar 3 market discipline. The aim of Pillar 3 is to produce disclosures that allow market participants to assess the scope of application by banks of the Basel Committee's framework and the rules in their jurisdiction, their capital condition, risk exposures and risk management processes, and hence their capital adequacy.

2. Risk Management

Governance and Oversight

The Board is responsible for determining a framework for risk management and control. It approves all policies and Committee terms of reference.

Throughout 2019 the Board had four sub-committees to deal with specific issues. The Board determines the responsibilities and composition of these committees, which are authorised to make decisions within agreed parameters and/or make recommendations to the full Board as appropriate.

> The Board Risk and Compliance Committee - This Committee ensures that the Society meets its regulatory and legal obligations with regard to all areas of the business relating to risk as specified in our Risk Appetite Statement. This includes areas of business conduct to ensure that at all times the Society's objectives are met by delivering business in a clear, transparent and fair manner, whether that is by the Society itself or by a third party acting on its behalf. Members of senior management appear in front of the Board Risk and Compliance Committee to be challenged on how they manage and mitigate risks in their business areas. In considering the risks, the Committee will understand the Group's strategies and tactics, along with the key success factors used to measure its performance. The committee met six times in 2019.
>
> The Board Risk and Compliance Committee reviews the risk culture of the Group, setting the tone in respect of risk management. The Committee is also responsible for ensuring the risk culture is fully embedded and supports at all times the Society's agreed risk appetite, covering the extent and categories of risk which the Board considers as acceptable. The Committee assumes responsibility for monitoring the Society's Risk Management Framework, which embraces risk principles, policies, methodologies, systems, processes, procedures and people.
>
> The Audit Committee - This Committee discharges its duties by considering matters relating to internal and external audit arrangements and financial reporting. The Committee met four times in 2019. The present committee members are all non-executive directors.
>
> The Nominations and Governance Committee - This Committee considers the structure, size and composition of the Board and makes recommendations to the Board regarding any proposed changes. The Committee is also responsible for reviewing succession planning for members of the Board and executive. The Committee will nominate candidates to fill Board vacancies and will consider nominations made by members. The Committee met seven times in 2019.
>
> The Remuneration Committee - This Committee considers the remuneration and contractual arrangements for the nonexecutive directors, executive directors and executive committee. The Committee met twice in 2019 and comprises all nonexecutive directors, with the Chief Executive in attendance.

Terms of Reference for the four sub-committees are published on our website at www.darlington.co.uk

The Executive are responsible for designing, operating and monitoring risk management and internal control processes. The key executive management committees are the Asset and Liabilities Committee, chaired by the Finance Director and the Risk Management Committee chaired by the Chief Risk Officer:

> The Assets and Liabilities Committee - This Committee controls the methods for managing credit risk of counterparties, basis risk, settlement risk, funding risk, interest rate risk and structural risk in the balance sheet. The Committee implements appropriate limits and monitors relevant exposures. A Financial Risk Management Policy is maintained which sets out the Society's risk appetite and approach to liquidity, funding and structural balance sheet management. The Committee meets at least once a month. This is an executive committee, however, non-executive directors attend at their discretion.

The Risk Management Committee - This Committee, which is an Executive Committee, is responsible for management oversight of the Society's operational risk and credit risk exposures. Credit risk arises from the Society's residential and commercial lending activities. Operational risks include the Society's conduct in treating customers fairly, properly and in accordance with our stated values and regulations. Risks to the Society are considered which are impacting now and in the future. The committee uses the Board agreed risk appetite to guide decisions.

Risk Management Framework

The Society has a formal mechanism for identifying and addressing risks throughout the business. This framework is based on the best practice 'three lines of defence' model, as follows:

The Society uses a risk assessment framework to assess the likelihood and impact of its key risks. This is regularly monitored and reviewed by the Executive. This process forms a base for the identification of risks for incorporation into the ICAAP under Pillar 2. Risks identified are cross referenced to the relevant section of the ICAAP to ensure all risks are supported by additional capital where appropriate.

The internal audit function which is outsourced to an external agent under specific terms of reference, provides independent and objective assurance that operational processes are appropriate and effectively applied.

Principal Business Risks

The principal business and financial risks to which the Group is exposed are credit, market, liquidity, operational, pension, conduct, strategic and regulatory these are detailed in the following table:

Risk Universe	Risk	Risk Mitigation
Credit Risk	The risk that a member, customer or counterparty may not be able to meet their obligations to the Society as they fall due.	• A Board approved Credit Risk appetite is in place and is managed through the Credit Risk and Responsible Lending Policy. • Underwriting assessments of applications. • Credit risk metrics are monitored regularly through Risk Management Committee.
Prudential Risk	Liquidity Risk The risk that the Group may not be able to meet its financial obligations as they become due, or may do so only at a disproportionate or excessive cost.	• A Board approved Liquidity Risk appetite is in place and is managed through the Financial Risk Management Policy. • The key assumptions, risks and controls around the management of liquidity risk are outlined in the ILAAP document which is approved annually by the Board. • The Group operates a range of internal stress tests to ensure that sufficient liquidity is available at all times to address stress and business as usual requirements.

		• The Asset and Liability Committee monitors the liquidity position on a monthly basis.
	Market Risk The risk that the income from, or value of the Group's assets and liabilities may change when affected by fluctuations in market rates such as house price index, inflation and interest rates.	• A Board approved Risk appetite for Market Risk is in place and is managed through the Financial Risk Management Policy. • The Group Monitors Market Risk through a series of defined metrics. • The Asset and Liabilities Committee oversee the Group's management of Market Risk. • A dedicated Treasury function exists to manage this risk with Second line oversight from Risk and Compliance. • The Group does not actively trade, market risk is in respect of banking book assets only.
Operational Risk	The risk that an exposure or loss may arise from inadequate, inappropriate, insufficient or otherwise failed or failing internal processes or systems, human error or external events.	• A Board approved Operational Risk appetite is in place and is managed through the Risk Management Framework. • The Risk Management Framework sets out how colleagues are expected to identify, assess, monitor, manage and report their risk exposures. • Operational Loss Events are identified through a dedicated system. • The Risk Management Committee provides oversight across the Group's operational risk exposures. • There is a three lines of defence review in place which challenges compliance with the framework.
Conduct and Compliance Risk	The risk that we fail to treat customers' fairly, meet expected customer outcomes or fail to comply with relevant conduct regulations.	• A Board approved Conduct Risk appetite is in place and is managed through the Risk Management Framework. • Key conduct risk metrics are in place through our conduct risk MI to manage and monitor the key conduct risks within the Society. • A dedicated second line Risk and Compliance function has been established to monitor compliance with regulations in the Society.
Strategic & Governance Risk	Pension Risk The risk of financial deficit in the defined benefit plan of the Society.	• The Independent Pension Trustees of the Society's Defined Benefit Plan are responsible for managing the scheme and determining and implementing an appropriate investment strategy. Society oversight is provided by the Pension Oversight Committee.
Risk Universe	**Risk**	**Risk Mitigation**

	Economic Uncertainty The risk that an economic downturn or prolonged uncertainty has a detrimental effect on the Society achieving its objectives.	• Continued monitoring of economic data and political events • Risk analysis provided to each Board meeting. • Risk Appetite monitoring and contingency planning when events manifest. • Stress testing undertaken on potential scenarios.

Full details regarding the financial risks and instruments used by the Group are given in the Annual Report and Accounts, Note 25, Financial Instruments.

3. Capital

Capital Resources

Total Society capital resources at 31st December 2019, amount to £44.4m. This is made up predominantly of Common Equity Tier 1 capital; General Reserves (the accumulated profits of the Society) net of regulatory adjustments. Tier 2 capital comprises the collective provision for impairment in relation to bad and doubtful debts.

Table 1 Components of Common Equity Tier 1, Tier 1 capital and Tier 2 capital as at 31st December 2019

£'000	At 31 December 2019
Common Equity Tier 1 (CET1)	
General reserve	45,743
Regulatory adjustments[1]:	
Pension scheme asset adjustment[2]	(1,887)
Total CET1 and Tier 1 capital[3]	**43,856**
Tier 2 Capital	
Collective provisions for impairment (general credit risk adjustments)	554
Total capital available	**44,410**

Capital Forecasting and Planning

The Group adopts an iterative five-year corporate planning framework which includes detailed consideration of the Society as a standalone entity. The Corporate Plan is reviewed and approved by the Board annually to take account of current and changing economic conditions and the Group's future strategic objectives, including the strategic objectives of the Society. The Society performs a comprehensive range of stresses to identify the potential impacts and risks to the business if economic conditions or business performance differ from the assumptions within the Corporate Plan.

The Society's Directors monitor performance against budget at monthly Board meetings. The Group and Society complete quarterly re-budgeting when internal business decisions and/or external economic conditions lead to a material change in the Group and Society's ability to meet the agreed Corporate Plan.

The Corporate Plan includes detailed consideration of the Society's activities and is integral to the Society's ICAAP in particular the Board's risk appetite for different business activities/risks and desired capital resource levels to support

[1] The Society does not adjust regulatory capital in respect of prudent value adjustments / additional value adjustments in accordance with Article 34 of CRR because they are trivial in size (£2,000).

[2] Pension scheme asset adjustment is quoted net of associated deferred tax liability

[3] The Society has no additional Tier 1 capital instruments hence CET1 and Tier 1 capital amounts are the same.

those activities. The ICAAP contains the capital plan for the next five years and the Board ensures that adequate capital resources are retained to support the corporate goals contained within the plan.

The capital plan details the capital resources requirement (effectively, the minimum capital required) in each year using the standardised approach for credit risk and the basic indicator approach for operational risk together with additional capital provision determined by the Board to be appropriate to cover additional risks not covered under the standard capital calculations.

Capital Risk Appetite

The Society annually reviews the risk appetite in relation to the capital it should hold and the levels of capital adequacy it will maintain. This assessment is based on the current and forecast capital requirements as well as building the Society's resilience to potential external capital shocks.

Capital Adequacy Assessment

The Society assesses whether the capital it holds is sufficient based on the risks within the Society's financial position (i.e. balance sheet). This exercise is completed through the methodology outlined in the Capital Requirements Directive (CRDIV).

The tables on the following pages outline:

- Capital available in excess of total capital requirements
- Differences between accounting and regulatory scopes of consolidation and mapping of financial statement categories with regulatory risk categories
- Main sources of differences between regulatory exposure amounts and carrying values in financial statements
- Differences in the scopes of consolidation – entity by entity
- Overview of Risk Weighted Assets
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- Geographical breakdown of exposures
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- Standardised approach – credit risk exposure and Credit Risk Mitigation (CRM) effects
- Standardised approach
- Analysis of Counterparty Credit Risk ("CCR") exposure by approach
- Credit Valuation Adjustment ("CVA") capital charge
- Exposures to Central Counterparties ("CCPs")
- CCR exposures by regulatory portfolio and risk
- Composition of collateral for exposures to CCR
- Market risk under the standardised approach
- Derivative exposures net of posted collateral and in line with Master Netting Agreements
- Asset encumbrance, assets and source of encumbrance

The Society's capital adequacy assessment is reviewed periodically by the Prudential Regulatory Authority (PRA). In line with all financial institutions they regulate, the PRA provide an independent assessment of the capital requirements of the Society. This is communicated to the Society as a Total Capital Requirement.

Table 2 – Capital available in excess of total and overall capital requirements

£'000	At 31 December 2019
Total capital available	**44,410**
Total Capital Requirement (TCR)	27,425
Excess capital over TCR	**16,985**

Leverage Ratio

The consolidated group leverage ratio has been calculated as at 31st December 2019 as 6.58%.

The leverage ratio is a measure of capital adequacy expressed as a percentage. The PRA published its final rules on the exclusion of claims on central banks from the UK leverage ratio framework and the recalibration of the minimum leverage ratio from 3% to
3.25% of tier 1 capital.

Capital flows

The table below outlines the flow of regulatory capital and movements in deductions to regulatory capital throughout 2019. Table 3 – 2019 Regulatory Capital Flows

£'000	At 31 December 2019
Common Equity Tier 1 (CET1)	
General reserve 1 Jan 2019	43,909
Total CET1 and Tier 1 capital 1 Jan 2019	43,909
Movements in relation to 2019:	
Total comprehensive income 2019	**1,834**
Change in pension scheme asset adjustment	(1,887)
Total CET1 and Tier 1 capital 31 Dec 2019	**43,856**
Tier 2 Capital	
Collective provisions for impairment 1 Jan 2019	510
Total Tier 2 Capital 1 Jan 2019	510
Movements in relation to 2019:	
Collective provision for impairment charge in the year	44

Total Tier 2 capital 31 Dec 2019	**554**
Total Capital Available	**44,410**

The Society is not part of a Group for the purposes of regulatory capital and as such there are no restrictions or impediments to the total available capital balance shown above.

Table 4: Differences between accounting and regulatory scopes of consolidation and mapping of financial statement categories with regulatory risk categories

£'000	Carrying values as reported in published Society financial statements	Carrying values under scope of regulatory consolidation	Carrying values of items			
			Subject to the credit risk framework	Subject to the CCR framework	Subject to the market risk framework	Not subject to capital requirements or subject to deduction to capital
Assets						
Cash and balances at central banks	85,596	85,596	85,596			
Loans and advances to credit institutions	10,418	10,418	10,418			
Debt securities	9,021	9,021	9,021			
Loans and advances to customers	551,284	551,818	551,818			
Derivative financial instruments	122	122		122	122	
Other assets	11,988	11,988	11,988			
Total assets	668,429	668,963	668,841	122	122	
Liabilities						
Shares	561,412	561,412				561,412
Amounts owed to credit institutions	30,419	30,419				30,419
Amounts owed to other customers	27,443	24,843				24,843
Derivative financial instruments	1,300	1,300				1,300
Other liabilities	2,112	4,712				4,712
Reserves	45,743	46,277				46,277

Total liabilities	668,429	668,963	-	-	-	668,963

The amounts shown in the column ‘Carrying values under scope of regulatory consolidation’ equal the sum of the amounts shown in the remaining columns of this table when adjustment is made to reflect that for the line items ‘Derivatives financial instruments’, the assets included are subject to regulatory capital charges for both CCR and market risk.

Table 5: Main sources of differences between regulatory exposure amounts and carrying values in financial statements.

	£'000	Total	Items subject to		
			Credit risk framework	CCR framework	Market risk framework
1	**Assets carrying value amount under the scope of regulatory consolidation (as per template EU LI1)**	**668,963**	**668,841**	**122**	**122**
4	Off-balance-sheet amounts and potential future exposure for counterparty risk	29,724	28,875	849	849
5	*Differences due to amounts not subject to regulatory capital requirements*	(7,695)	(7,695)		
10	**Exposure amounts considered for regulatory purposes**	**690,992**	**690,021**	**971**	**971**

The amounts shown in the column 'Carrying values under scope of regulatory consolidation' equal the sum of the amounts shown in the remaining columns of this table when adjustment is made to reflect that for the line items 'Derivatives financial instruments', the assets included are subject to regulatory capital charges for both CCR and market risk.

Table 6: Differences in the scopes of consolidation – entity by entity

Name of the entity	Method of accounting consolidation	Method of regulatory consolidation	Description of the entity
Darlington Building Society	Fully consolidated	Full consolidation	Credit institution
Darlington Homes Limited	Fully consolidated	Neither consolidated nor deducted	Property development and sales company
Dormant subsidiaries	Fully consolidated	Neither consolidated nor deducted	Dormant subsidiary

Table 7: Overview of Risk Weighted Assets

		R VAs		Minimum capital requirements[2]
	£'000	31 Dec 2019	31 Dec 2018	31 Dec 2019
1	**Credit risk (excluding CCR)**	**213,930**	**205,260**	**17,114**
2	Of which the standardised approach	213,930	205,260	17,114
19	**Market risk**	**377**	**623**	**30**
20	Of which the standardised approach	377	623	30
23	**Operational risk**	**19,466**	**18,656**	**1,557**
25	Of which basic indicator approach	19,466	18,656	1,557
29	**Total**	**233,773**	**224,539**	**18,701**

[2]"Minimujm Capital Requirements" here and in all tables where the term is used, represents the Pillar 1 capital charge at 8% of RWAs.

Under the standardised approach for credit risk, the Society applies a risk weighted asset to each of its exposure classes as set out in the PRA handbook BIPRU Section 3 and provides 8% of that risk weighted asset value as the minimum capital requirements for credit risk.

Under the basic indicator approach for operation risk, The Society calculates its average total income over the previous three years and provides 15% of that average total income as the minimum capital requirement for operation risk.

Table 8: Total and average net amount of exposures

£'000		Net value of exposures at the end of the period	Average net exposures over the period
16	Central governments or central banks	85,475	75,985
19	Multilateral development banks	0	487
21	Institutions	20,409	25,649
22	Corporates	731	713
24	Retail	7,895	6,703
26	Secured by mortgages on immovable property	570,793	554,377
28	Exposures in default	1,017	1,207
34	Other exposures	4,672	5,068
35	***Total standardised approach***	**690,992**	**670,189**
36	***Total***	***690,992***	***670,189***

Item 21; Other Credit Institutions, Items 21 & 24; Balances in excess of 80% Loan to Value, Item 26; Balances below 80% Loan to Value.

Table 9: Geographical Breakdown of Exposures

£'000		Europe	United Kingdom	Netherlands	Australia	North America	USA	Canada	Total
7	Central governments or central banks	85,475	85,475						**85,475**
10	Multilateral development banks	-							**-**
12	Institutions	16,391	13,385	3,006	2,007	2,011	5	2,006	**20,409**
13	Corporates	731	731						**731**
14	Retail	7,895	7,895						**7,895**

15	Secured by mortgages on immovable property	570,793	570,793						**570,793**
16	Exposures in default	1,017	1,017						**1,017**
22	Other exposures	4,672	4,672						**4,672**
23	**Total standardised approach**	**686,974**	**683,968**	**3,006**	**2,007**	**2,011**	**5**	**2,006**	**690,992**
24	**Total**	**686,974**	**683,968**	**3,006**	**2,007**	**2,011**	**5**	**2,006**	**690,992**

Item 12; Other Credit Institutions, Items 13 & 14; Balances in excess of 80% Loan to Value, Item 15; Balances below 8-% Loan to Value.

The Groups primary activity is mortgage lending exclusively within the UK. The Annual Report and Accounts include a breakdown of the geographical mortgage loan exposures within the UK. The Group's ICAAP includes an assessment of the geographic concentration risk within the UK and the Society holds additional capital where required in relation to this risk.

£'000		Agriculture, Forestry and Fishing	Wholesale and Retail Trad	Accommodation and Food Service Activities	Real Estate Activities	Professional Scientific and Technical Activities	Human Health Services and Social Work Activities	Arts, Entertainment and Recreation	Other Services	Fully secured on residential property	Other	Total
7	Central Governments or Central Banks										85,475	85,475
10	Multilateral Development Banks										0	0
12	Institutions										20,409	20,409
13	Corporates			73	604				54			731
14	Retail									7,895		7,895
15	Secured by mortgages on immovable property	150	286	2,371	5,730	221	-	395	1,994	559,645		570,793
16	Exposures in default			-						1,017		1,017
22	Other exposures										4,672	4,672
23	**Total standardised approach**	**150**	**286**	**2,444**	**6,422**	**241**	-	**395**	**2,048**	**568,449**	**110,556**	**690,992**
24	**Total**	**150**	**286**	**2,444**	**6,422**	**241**	-	**395**	**2,048**	**568,449**	**110,556**	**690,992**

Table 10: Concentration of Exposures by Industry or Counterparty Types

Item 12; Other Credit Institutions, Items 13 & 14; Balances in excess of 80% Loan to value, Item 15; Balances below 80% Loan to value

Table 11: Maturity of Exposures

		Net Exposure Value					
£'000		On Demand	< = 1 Year	> 1 Year < = 5 Years	> 5 Years	No Stated Maturity	Total
7	Central Governments or Central Banks	85,475					85,475
10	Multilateral Development Banks		0				0
12	Institutions	874	15,522	4,013			20,409
13	Corporates				731		731

14	Retail			12	7,883		7,895
15	Secured by mortgages on immovable property		1,920	27,195	541,678		570,793
16	Exposures in default		62	59	897		1,017
22	Other exposures					4,672	4,672
23	**Total standardised approach**	**86,349**	**17,503**	**31,279**	**551,188**	**4,672**	**690,992**
24	**Total**	**86,349**	**17,503**	**31,279**	**551,188**	**4,672**	**690,992**

Item 12; Other Credit Institutions, Items 13 & 14; Balances in excess of 80% Loan to value, Item 15; Balances below 80% Loan to value

When the amount is repaid in instalments, the exposure has been allocated in the maturity bucket corresponding to the last instalment. This is in accordance with the Final Report on the Guidelines On Disclosure Requirements Under Part Eight Of Regulation (EU) No 575/2013.

Table 12: Credit Quality of Exposures by Exposure Classes and Instruments

		Gross carrying value of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges of the period	Net values
£'000		Defaulted exposures[1]	Non-defaulted exposures					(a+b-c-d)
16	Central governments or central banks		85,475					**85,475**
19	Multilateral development banks		-					**-**
21	Institutions		20,409					**20,409**
22	Corporates		914	183		21	-29	**731**
24	Retail		7,895					**7,895**
26	Secured by mortgages on immovable property		570,850	56			11	**570,793**
28	Exposures in default		1,017	0			9	**1,017**
34	Other exposures		4,672					**4,672**
35	***Total standardised approach***	**-**	**691,231**	**239**	**-**	**21**	**-8**	**690,992**
36	***Total***	**-**	**691,231**	**239**	**-**	**21**	**-8**	**690,992**

37	Of which: Loans		580,675	239		21	-8	**580,436**
38	Of which: Debt securities		9,021					**9,021**
39	Of which: Off balance-sheet exposures		849					**849**

Item 21; Other Credit Institutions, Items 22 & 24; Balances in excess of 80% Loan to value, Item 26; Balances below 80% Loan to value

Table 13: Credit Quality of Exposures by Industry or Counterparty Types

£'000		Gross carrying value of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges of the period	Net values
		Defaulted exposures	Non-defaulted exposures					(a+b-c-d)
1	Agriculture, forestry and fishing		150					**150**
7	Wholesale and retail trade		286					**286**
9	Accommodation and food service activities		2,444					**2,444**
11	Real estate activities		6,577	155		21	(23)	**6,422**
12	Professional, scientific and technical activities		269	28			(5)	**241**
16	Human health services and social work activities		-					**-**
17	Arts, entertainment and recreation		395					**395**

18	Other services		2,048					**2,048**
19	Fully secured on residential property		568,505	57			20	**568,449**
20	Central banks and credit institutions		110,556					**110,556**
21	***Total***	**-**	**691,231**	**240**	**-**	**21**	**(8)**	**690,992**

Table 14: Credit Quality of Exposures by Geography

£'000		Gross carrying value of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges of the period	Net values
		Defaulted exposures	Non-defaulted exposures					(a+b-c-d)
1	Europe		**687,214**	**239**		**21**	**-8**	**686,975**
2	United Kingdom		684,207	239		21	-8	**683,968**
3	Netherlands		3,006					**3,006**
4	Australia		**2,007**					**2,007**
8	North America		**2,011**					**2,011**
9	USA		5					**5**
10	Canada		2,006					**2,006**
11	***Total***	**-**	**691,232**	**239**	**-**	**21**	**-8**	**690,992**

The Society's credit exposures relevant for the calculation of the countercyclical capital buffer (CCyB) are all in the UK and as such the institutions specific CCyB is 1%, consistent with the UK CCyB. It is noted that the UK CCyB and therefore the Society's CCyB will increase to 2% on 16 December 2020.

Table 15: Non-Performing and Forborne Exposures

	Gross carrying values of performing and non-performing exposures	Accumulated impairment and provisions and negative fair value adjustments due to credit risk	Collaterals and financial guarantees received

£'000			Of which performing but past due > 30 days and <= 90 days	Of which performing forborne	Of which non-performing				On performing exposures		On non-performing exposures		On nonperforming exposures	Of which forborne exposures
						Of which defaulted	Of which impaired	Of which forborne		Of which forborne		Of which forborne		
010	Debt securities	9,021												
020	Loans and advances	580,675	1,846	8,004	1,019			-	226		13	-		
030	Off-balance-sheet exposures	849												

Table 16: Changes in Stock of General and Specific Credit Risk Adjustments

£'000		Accumulated specific credit risk adjustment	Accumulated general risk adjustment
1	**Opening Balance**	253	
2	Decreases due to amounts set aside for estimated loan losses during the period	(14)	
4	Decreases due to amounts taken against accumulated credit risk adjustments	-	
9	**Closing balance**	239	
10	Recoveries on credit risk adjustments recorded directly to the statement of profit or loss	9	
11	Specific credit risk adjustments directly recorded to the statement of profit or loss	(14)	

Table 17: Changes in Stock of Defaulted and Impaired Loans and Debt Securities

£'000		Gross carrying value defaulted exposures
1	**Opening balance**	-
2	Loans and debt securities that have defaulted or impaired since the last reporting period	-
6	**Closing balance**	-

Table 18: Credit Risk Mitigation Techniques - Overview

£'000		Exposures unsecured - Carrying amount	Exposures secured - Carrying amount	Exposures secured by collateral	Exposures secured by financial guarantees	Exposures secured by credit derivatives
1	Total loans	11,528	568,908	568,908		
2	Total debt securities	9,021				
3	**Total exposures**	**20,549**	**568,908**	**568,908**		
4	Of which defaulted					

Table 19: Standardised Approach – Credit Risk Exposure and Credit Risk Mitigation (CRM) Effects

£'000 Exposure classes	**Exposures before CCF and CRM**		**Exposures post CCF and CRM**		**RWAs and RWA density**		
	On-balancesheet amount	Off-balancesheet amount	On-balancesheet amount	Off-balancesheet amount	RWAs	RWA density	RWA exposure (8% of RWA)

1	Central governments or central banks	85,475		85,475		-	0%	-
4	Multilateral development banks	-		-		-	0%	-
6	Institutions	20,409		20,409		4,317	21%	345
7	Corporates	731		731		731	100%	58
8	Retail	4,112	3,782	4,112	3,782	3,652	46%	292
9	Secured by mortgages on immovable property	545,700	25,093	545,700	25,093	201,954	35%	16,156
10	Exposures in default	1,017		1,017		1,017	100%	81
16	Other items	4,672	-	4,672	-	4,672	100%	374
17	**Total**	**662,117**	**28,875**	**662,117**	**28,875**	**216,343**	**33%**	**17,306**

Table 20: Standardised Approach

£'000	Exposure classes	Risk weight							Total	Of which unrated
		0%	20%	35%	50%	75%	100%	150%		
1	Central governments or central banks	85,475							**85,475**	
4	Multilateral development banks	-							**-**	
6	Institutions		19,624		784				**20,408**	**3,006**
7	Corporates						731		**731**	**731**
8	Retail					7,895			**7,895**	**7,895**
9	Secured by mortgages on immovable property			556,635			14,159		**570,794**	**570,793**

10	Exposures in default						1,017	-	**1,017**	**1,017**
16	Other items						4,672		**4,672**	**4,672**
17	**Total**	**85,475**	**19,624**	**556,635**	**784**	**7,895**	**20,579**	**-**	**690,992**	**588,114**

Table 21: Analysis of CCR Exposure by Approach

£'000		Notional	Replacement cost/current market value	Potential future credit exposure	Multiplier	EAD post CRM	RWAs
1	Mark to market		-5	-5		-11	810
2	Original exposure	2,500				122	122
3	Standardised approach		5		1	5	-405
11	**Total**					**117**	**527**

Table 22: CVA Capital Charge

£'000		Exposure value	RWAs
EU4	Based on the original exposure method	849	377
5	Total subject to the CVA capital charge	849	377

Table 23: Exposures to CCPs

£'000		EAD post CRM	RWAs
11	**Exposures to non-QCCPs (total)**		**377**
12	Exposures for trades at non-QCCPs (excluding initial margin and default fund contributions); of which	849	377

13	(i) OTC derivatives	849	377

Table 24: CCR Exposure by Regulatory Portfolio and Risk

£'000	Exposure classes	Risk weight		Total	Of which unrated
		20%	50%		
6	Institutions	65	784	849	
11	Total	65	784	849	

Table 25: Composition of Collateral for Exposures to CCR

	Collateral used in derivative transactions	
	Fair value of posted collateral	
£'000	Segregated	Unsegregated
Cash - GBP		2,101
Total		**2,101**

Table 26: Market Risk Under the Standardised Approach

£'000		RWAs	Capital requirements
	Outright products	377	30
1	Interest rate risk (general and specific)	377	30
9	**Total**	**377**	**30**

Table 27: Gross positive fair value of contracts, netting benefits, netted current credit exposure, collateral held and net derivatives credit exposure.

	Fair value presented in the Society's Balance Sheet	Collateral pledged not subject to offset for the purpose of financial reporting disclosure	Net collateralised position	Net position under Master Netting Agreements not subject to offset for the purposes of financial reporting disclosures
Financial assets				
Interest rate swaps	122	-	923	1,044
Financial liabilities				
Interest rate swaps	1,300	(2,101)	-	121

Table 28: Asset encumbrance - COREP Template F32.01, assets of the reporting institution

		Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
10	Assets of the reporting institution	55,743		595,580	
30	Equity instruments	-		-	
40	Debt securities	-	-	10,859	10,859
50	of which: covered bonds	-	-	-	-
60	of which: asset-backed securities	-	-	-	-

70	of which: issued by general governments	-	-	-	-
80	of which: issued by financial corporations	-	-	10,859	10,859
90	of which: issued by non-financial corporations	-	-	-	-
120	Other assets	55,743		584,721	

Figures above reflect the median values of the Society's previous four quarterly end of period positions.

Table 29: Sources of encumbrance - COREP Template F32.04

		Matching liabilities, contingent liabilities or securities lent	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered
10	Carrying amount of selected financial liabilities	23,146	55,343

Figures above reflect the median values of the Society's previous four quarterly end of period positions.

An asset is encumbered when it is pledged, or is subject to any form of agreement to secure or collateralise a transaction from which it cannot be freely withdrawn.
The Society's asset encumbrance typically arises from cash pledged as collateral against derivative transactions and from other assets pledged as collateral to facilitate the Society's participation in the Bank of England's Sterling Monetary Framework.
Secured funding provides the Society with a diversified funding capability but does not make up a large portion of the Society's total funding.

4. Credit Risk - Mortgages

The Society regards as 'impaired' any mortgage or loan account where more than three monthly repayments have not been made at the accounting date or where there is objective evidence that the loan account is impaired. An account is ‘past due’ where one or more monthly repayment has not been made. Arrears of mortgage repayments are monitored closely by the Society’s financial support team and the Risk Management Committee. The Society has performed satisfactorily when compared with national arrears and possession statistics.

A residual maturity analysis of Loans and Advances to Customers is provided in Note 11 of the Annual Report and Accounts 2019 which assumes that the loans and advances run for their full, contractual term.

5. Provisions

The Society accounting policy in relation to the provision for bad and doubtful debts is set out in full in the accounting policies (Note 1), to the Annual Report and Accounts 2019. Full details of the movement on provisions for bad and doubtful debts are provided in Note 12 to the Annual Report and Accounts 2019. For capital adequacy purposes, collective provisions are regarded as Tier 2 capital. Specific provisions have been utilised to adjust downwards the net exposure value of residential risk weighted assets for the purposes of capital adequacy calculations.

6. Credit Risk - Treasury

The purpose of the Liquidity credit risk appetite, as outlined in the Financial Risk Management Policy (FRMP), is to ensure that the Society balances the return achieved on assets against the risk of loss in respect of counterparty default within limits set out in that document for both the amount invested and the counterparty rating. Investments in banks and building societies are held purely for liquidity management purposes. The minimum acceptable mutually inclusive credit ratings are set out in the Society’s FRMP based on publically available external credit agency information from Fitch IBCA, treasury deposits are also made with unrated building societies.

Policy limits and counterparties are regularly reviewed by ALCO, with formal approval of these being made at Board. The Society receives counterparty rating amendments from its Treasury advisors and limits are suspended if downgrades to counterparty take the institution below the levels stated in the FRMP. In these circumstances ALCO will decide if present exposures held with the counterparty are to be realised or held to maturity. These decisions are reported to the Board. The Board may approve a counterparty with a rating below the minimum set where a market assessment is such that we believe the strength of the counterparty to be sufficiently robust to withstand the investment.

The Society deems that it is not exposed to wrong way risk, the risk that exposures to a counterparty are negatively correlated to the creditworthiness of that counterparty, as a result of any of its activities.

The Society does not hold an external credit rating and as such does not consider the impact of downgrade events.

Note 25 of the Annual Report and Accounts shows the breakdown of liquid assets by maturity and credit quality as at 31 December 2019, categorised into Credit Quality Steps as defined by the European Banking Authority (EBA) for the purposes of capital reporting .

7. Basis Risk

This is the risk that the interest receivable or payable on the Society’s assets and liabilities are linked to differing underlying repricing structures or bases of interest rate. The main activities undertaken by the Society that give rise to basis risk are as follows:

- Management of the investment of capital and other non-interest bearing liabilities;

- Fixed rate, including; o Fixed rate mortgages and other lending; o Fixed rate investments through Treasury operations; o Fixed rate retail savings products offered to members; o Fixed rate wholesale funding taken through Treasury operations
- Tracker mortgages and other lending and Tracker retail investments offered to members (against Bank of England Base Rate);

- Purchase of financial instruments linked to basis metrics such as LIBOR, SONIA and Bank Base rate as part of Treasury operations.
- Administered mortgages and other lending and administered retail investments offered to members, where the Society sets the interest rate receivable and payable.

Basis risk is managed on a continuous basis within limits set by Board and monitored by ALCO, using a combination of on and off balance sheet instruments, specifically interest rate SWAP's or matched products. Hedging action is taken as appropriate to maintain an exposure within the Board approved Gap and sensitivity limits.

The Society Balance Sheet is reviewed on a monthly basis against Board limits measured a range of Interest Rate Risk sensitivities.

The ALCO performs sensitivity analysis on a monthly basis to assess the interest rate risk faced by the Group over a 12 month period, if no management actions were undertaken. A range of risks measured by ALCO are shown in below:

Society	**12 Month Impact £'000**	**Comment**
Possible Scenarios		
Increase in Bank Base Rate by 0.25%	148	Improvement in profit before tax
Decrease in Bank Base Rate by 0.25%	(21)	Reduction in profit before tax
Severe but Plausible Scenarios		
Increase in Bank Base Rate by 2.0%	1,182	Improvement in profit before tax
Decrease in Bank Base Rate to Zero	(37)	Reduction in profit before tax

8. Remuneration Policy and Practices

The Society's objective in setting the remuneration policy is to ensure that remuneration is set at a level to retain and attract individuals of the calibre necessary to operate an organisation such as Darlington Building Society whilst being in line with effective risk management and business strategy practices.

The remuneration of the executive directors and other members of the executive are determined by the Remuneration Committee. The Terms of Reference of this Committee are set out on our website, www.darlington.co.uk .

In setting remuneration, the Committee takes account of the remuneration and benefits package payable to executive directors and other executives carrying similar responsibilities in organisations comparable to the Darlington Building Society.

It is determined that the executive committee which comprises of the executive directors being; the Chief Executive, the Finance Director and the Chief Risk Officer and five further executives are designated as subject to the Remuneration Code as set out in SYSC 19D.

Further information on the mandate of the Remuneration Committee and its decision making process in determining the remuneration policy for the executive directors and other members of the executive team is contained in the Report on Directors Remuneration within the Annual Report and Accounts for the year ended 31 December 2019.

For all of the Executives fixed remuneration includes pension contributions made by the Society on behalf of the employees and the value of taxable benefits. Variable remuneration relates to Bonus payments which are at the sole discretion of the remuneration committee and are not guaranteed, subject to malice and clawback.

Aggregate information on the remuneration of the three executive directors and other five executives for the period ended 31 December 2019 is shown in the table below. Staff involved in the Treasury function are not incentivised or awarded Bonuses based on the performance of the Treasury portfolio and no targets are set for return on assets to ensure the security of liquid assets is paramount at all times.

Category	Number	Salary	Bonus	Pension Contribution	Other Benefits	Total Remuneration
Key Management compensation	15	916	49	52	2	1,019
Other Staff in Certification Regime	14	442	18	35	0	495
Total		**1,358**	**67**	**87**	**2**	**1,514**