Newcastle Building Society
Annual Report and Accounts 2014

Building trust...
Building people...
Building communities...
Building Society since 1863.

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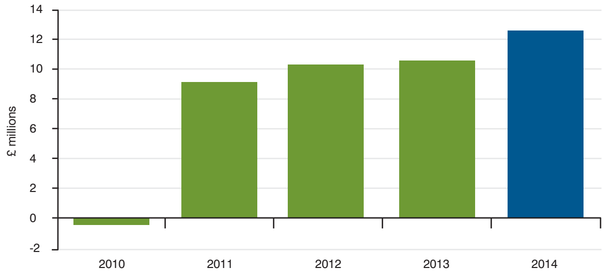
Local knowledge. Mutual understanding.

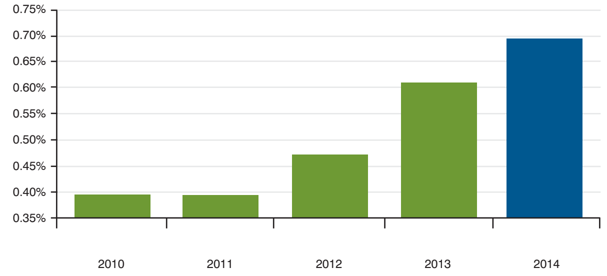
Newcastle
Building Society

2014 key highlights

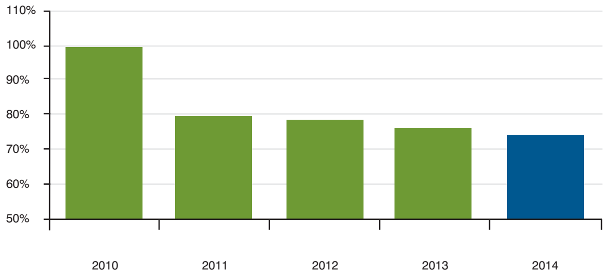
Operating Profit / (loss) before Impairments, Provisions, FSCS levy and Exceptional Items



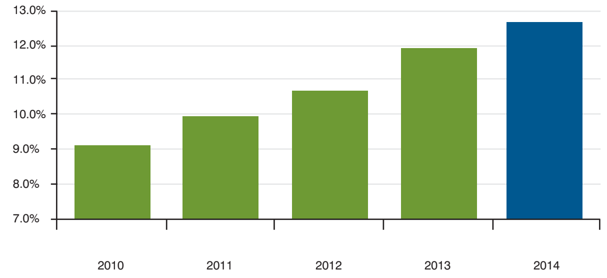
Interest Margin as a Percentage of Mean Total Assets



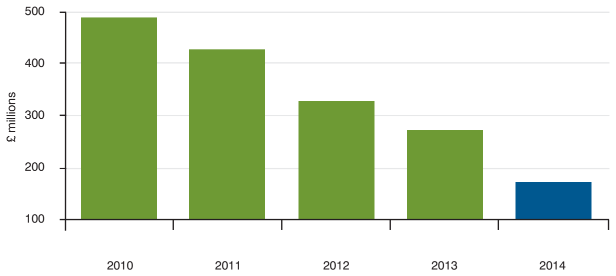
Cost to Income Ratio



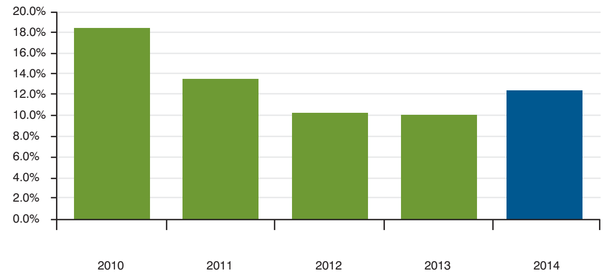
Core Equity Tier 1 Capital Ratio



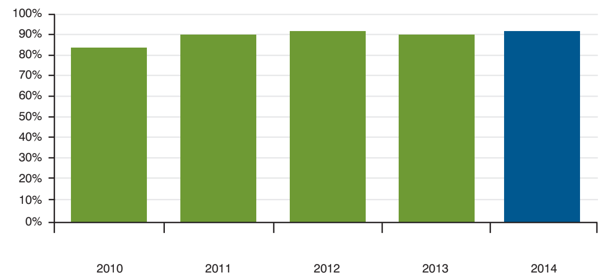
Commercial Investment Loan Exposure (net of provisions)



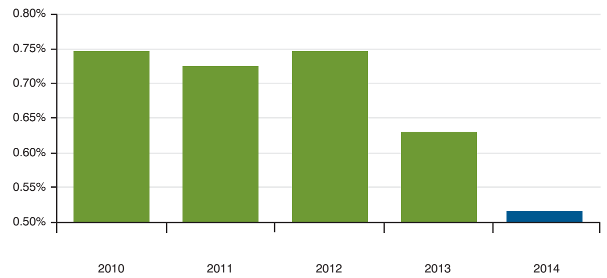
Percentage Staff Turnover



Overall Customer Satisfaction Percentage



Percentage of Loans in Arrears of 3 months or more (number of loans)



Contents

Our Vision

We aim to deliver excellent service to our Members and customers; long term, secure and rewarding employment to our staff; and recognisable support to local communities. We also aim to provide best in class service for our Solutions business customers.

Our Objectives

Our Members, customers, employees and the communities we serve all have an important part to play in the future of the Society. We believe we can best serve the interests of all stakeholders by remaining a strong, dynamic and independent mutual building society.

Our objectives for each are:

Our Members and Customers

- To provide a good range of savings, investment, mortgage and insurance products that provide value for money;
- To be a friendly customer-focused organisation, which understands its customers, listens to and acts on what they say;
- To offer expert and trusted advice across a range of services;
- To deliver exceptional service in a prompt, courteous, professional, respectful and efficient manner;
- To be straightforward in what we do;
- To take personal ownership and care about what we deliver;
- To treat customers fairly and in a way that is consistent with mutuality; and
- To provide a diversified income stream through our Solutions business by sharing our technology and processing capability, built on our core building society competencies, with business partners.

Our Employees

- To provide secure and rewarding long term employment;
- To provide further development of our staff;
- To provide our staff with a thorough understanding of our corporate strategy to enable them to pursue it with commitment and passion;
- To be open and honest and do what we say we will do;
- To respect our employees and operate within an environment of mutual trust and understanding; and
- To provide competitive and fair remuneration packages.

Our Communities

- To be seen to be a major contributor to the economic wellbeing of the areas in which we operate; and
- To support the communities in which we operate, by way of both personal and financial involvement.

Our Values

'F.O.R.T.S.' – The Building Blocks of our Society

Friendly. Ownership. Respect. Trust. Straightforward.

Our staff have developed strong and realistic values that reflect the way the Society likes to do business with customers and how our staff want to work together, these are embedded in everything that we do.

Our values were developed through feedback from the entire organisation, via a staff survey, meetings and workshops. The ongoing focus on values is supported by a team of 'Values Champions' that promote and share the ways in which our staff demonstrate our values.

Our Values are what we call the 'building blocks' of the Society and cascade down from the Society's Board through to the whole organisation. They have been formed from a solid foundation upon which we can build an even more engaged and committed workforce. They have been delivered in a way that is informal and simply forms part of our day-to-day business. However, they aren't just empty words; more than that they reflect a culture within the business which is supportive and delivers year on year increased value for our Members and customers.

Chairman's Statement

Phil Moorhouse - Chairman

As I reported in my first statement as Chairman last year, we were seeing signs of being back to 'business as usual' for the Society with a simpler business model and reduced risk on our balance sheet. I am pleased to report in the last year we have continued that progress and are seeing further steady development of the business as a leading traditional regional mutual building society. This year-on-year progress has been made in a challenging and competitive marketplace, which makes the results even more pleasing.

In financial terms, our operating profit and capital ratios show an improved position and we have maintained a strong liquidity position throughout the year. As a result of our stronger capital position, we have been able to reduce the cost of some of our capital under the terms of those agreements, which will be of benefit to the Society going forward.

Our residential lending has continued at a healthy level with new loans of some £350m in the year. The Solutions business, which provides savings administration services to third parties, continues to show good levels of profitability with a strong new business pipeline. Finally, we continue to make progress in managing our legacy asset wind down strategy. The Chief Executive's review on page 6 covers our performance in detail.

In summary, this resulted in continued improvement in the Society's performance and progress in our strategic aims.

Background

In 2014, the economy continued its recovery as evidenced by improving growth, falling unemployment and increases in consumer spending. There have been lower levels of inflation, which was influenced latterly by decreases in fuel, energy and food prices. This has resulted in part in the Consumer Prices Index being at its lowest level in 12 years.

Despite regular speculation about interest rates, the bank base rate remained at its historically low level of 0.5% and the housing market reported an increase in house prices, with the South of the country leading the way. The Society's mortgage products, in particular the First Time Buyer portfolio, remained very popular having consistently offered 90-95% LTV products for a number of years.

We described last year the introduction of the Twin Peaks regulatory structure which is now operating; we continue to work with our regulators in a positive and open way and in an increasingly regulated environment it is important that we maintain these relationships.

The Mortgage Market Review (MMR) was introduced to the industry in the earlier part of the year aimed at making it more sustainable in the longer-term, while supporting borrowers to a greater extent. Although a significant change in the market, the Society had already made great progress in its mortgage processes so that the impact in the business post implementation was minimal.

Members

We continued to offer financial advice for all on the high street via our subsidiary Newcastle Financial Services Limited and gained our highest customer satisfaction scores for that division. We believe this personal 'face-to-face' advice is a key part of our service and is important to consumers.

In 2014, our competitive product range and excellent customer service (see customer satisfaction score in the Chief Executive's Review on page 7) has helped us acquire more than 33,000 new accounts.

This is against a backdrop of regular member engagement in 2014, including financial seminars, a wide range of community events, a member business update seminar, a variety of customer panels, all of which enabled us to have two-way communication with this key stakeholder group. As a mutual, engagement with our members is crucial to us; it gives us valuable feedback that can shape how we train our staff and the products and services we provide.

Member engagement contributed to the development of our distribution strategy so, in 2015, we will commence further investment into our branch network. We will focus on developing the services we offer in key branches within our heartland.

Our Board

We aim as a Society, to have a Board with a wide skill-set that reflects the breadth of the services we provide. This year, we strengthened the board further with two Non Executive Director appointments. Karen Ingham, based in our region, currently works at a senior level in the consumer sector having many years of experience in customer service. Richard Bottomley, OBE, FCA, was managing partner at KPMG's Newcastle office for a number of years with a broad financial background and strong ties to the region.

Retiring from our Board in February 2015 is Richard Mayland who has served as a Non Executive Director for over nine years. He has provided excellent support and guidance during this time; we thank him for this and wish him well.

Our People

2014 saw the start of a project to develop our 'Employer Brand', which is focussed on ensuring the Newcastle is a great place to work with the best people possible. The rollout of this will come in 2015 and it is something that will support the culture of the organisation very well.

It is this culture that has created a very supportive network within the organisation, which can be seen in the amount of participation in community activities. This has helped us raise thousands of pounds for local good causes as well as offer physical support to many regional charities.

It is this attitude and determination that has helped the business achieve very pleasing customer satisfaction scores which in turn creates a great energy in the business. The results of our 2014 staff survey have been equally encouraging.

Outlook

The Board are pleased to report steady and consistent progress toward our strategy of being a leading traditional regional building society. The economic background has improved but we are mindful of challenges that may arise in the run up to the general election and the uncertainty in the European economy, so we will continue to plan on a prudent basis. We are in a stronger position to deal with the challenges that arise and we can look forward with confidence.

Finally, and importantly I would like to thank, on behalf of the Board, all members of staff for their very positive commitment to the organisation. What we already have as a business and aim to achieve going forward is and will be hugely influenced by the efforts of every person in the organisation.

Phil Moorhouse
Chairman
24 February 2015

Chief Executive's Review

Jim Willens - Chief Executive

I am pleased to report that 2014 has been another year of continued and steady progress during which the Society has achieved the objectives set out for the year as measured by our corporate key performance indicators. We have continued to successfully implement the strategy that was set at the start of 2010 to return the Society to a traditional building society model with a diversified income stream via our Solutions business built on core building society competencies. The improvement in our year on year performance is evidence that our strategy is working and after following it for 5 years we can see the significant transformation to the business that has taken place and that we are well positioned to weather the more volatile markets and economic backdrop which have again been evident in 2014.

The UK has now had a bank base rate of 0.5% for almost six years and treasury markets and economists are expecting rates to stay at this level for longer than was expected a year ago. This is good news for borrowers who are benefitting from some of the most competitive mortgage rates ever seen in the UK but it is not so good for savers who are seeing reduced returns. Lower levels of unemployment, more modest house price growth, and rising disposable incomes (as wage growth outstrips inflation) suggest that 2015 will continue to be a good year for borrowers looking to buy a home in the UK.

Against the more competitive market backdrop and the changes brought about by the implementation of the Mortgage Market Review, I am pleased we have been able to support lending to our members, exceeding our budgeted gross and net lending targets for 2014. Equally pleasing is our range of competitive savings products, including the very popular Sir Bobby Robson Foundation account, where cumulative donations to the charity have now reached £1m.

From a financial perspective, profitability and capital ratios continued to strengthen further in 2014, and the quality and level of our liquidity was robust. Our key non-financial measures, the satisfaction of both our members and employees, continued above target and we were delighted to receive the Silver Investor in People award. We exceeded our targets for wind down of legacy assets and delivered on schedule on key IT infrastructure and regulatory projects.

Financial Performance

Profit before tax improved from £1.3m (restated) to £4.0m reflecting a higher net interest margin that benefitted from mortgage lending activity and reduced funding costs. Our operating profit (before provisions and Financial Services Compensation Scheme levy) increased to £12.4m from £10.6m. Our cost to income ratio improved to 74% from 76% with administrative expenses benefitting from strong cost control and the positive impact of a pension liability management exercise undertaken in 2014.

Profitability of our Solutions business remained stable and was in line with expectations. During the year the Society launched one major new contract, with a further three contracts near completion that are expected to go live in the first half of 2015. In addition, there are a number of other contracts at project stage.

The Society's capital ratios continued to improve year on year with the Solvency Ratio improving from 17.8% to 18.6% and Core Equity Tier 1 ratio improving from 11.9% to 12.7%. Tier 1 ratio improved from 14.1% to 14.6% and the leverage ratio remained over 5%. As announced in August 2014 the Society exceeded the 12% Ceiling Trigger set out in the Capital Agreement that was finalised in May 2010 which meant that with effect from 1st September 2014, the conversion option attaching to the securities ceased to apply and the prevailing coupon was reduced. We were delighted to achieve this trigger, several years ahead of plan, further demonstrating the Society's improved financial strength since 2010.

In 2014 the Society continued to unwind legacy portfolios with higher risk or lower margin that do not fit a traditional building society model. A reduction of £181m (2013: £160m) was achieved including £74m on commercial investment loans and £64m on loans to housing associations. Since the start of 2010 we have reduced legacy portfolios by £770m with the largest element of this reduction relating to commercial investment loans, falling by £344m or 63%. Provisions for impairment charges reduced from £6.7m to £5.9m. The Society also completed the disposal of the remaining properties in the residential investment property portfolio (Kings Manor Properties Limited) in 2014.

The percentage of mortgage loans in arrears of 3 months or more, across the whole mortgage portfolio based on the number of loans, reduced from 0.64% to 0.53%; around half of the industry average and at a record low since we have been tracking 3 months arrears. Our liquidity at the end of the year was strong at 23.6% compared to over 26% at the start of 2014. This fall was in line with our expectations and holdings continue to be mainly in AAA/AA rated assets.

Members

It has been another challenging year for savers with rates offered in the wider savings market continuing to fall. Against this background the Society opened over 30,000 new savings accounts and has continued to offer a range of good value savings products including easy access, regular savings and fixed rate bonds, providing competitive rates wherever possible, balancing the needs of savers and borrowers with our funding requirements. Our Big Home Saver remained a popular product for those wanting to save regularly in preparation for buying a home and our Big Little Saver was also popular with parents and grandparents alike to help promote the savings habit in young children. Our Sir Bobby Robson Foundation accounts remain a key part of our product offering, reaching a key milestone of £1m cumulative donations to the charity in 2014. The Society is very proud of this partnership.

We continued to support first time buyers with a range of competitive 90-95% loan to value products, which were very popular with homebuyers and represented around 20% of 2014 mortgage lending. We have operated in the first time buyer space since 2011 and the Society has its own mortgage indemnity insurance arrangements in place, which has meant we have not had to rely on government schemes to support first time buyer lending. Our overall gross lending was maintained at £350m which was slightly ahead of budget as was our net residential lending to homeowners at £134m; this was against a more competitive market backdrop. The implementation of the new regulations arising from the Mortgage Market Review in April 2014 had little impact for the Society as we have completed an affordability assessment for borrowers for several years and all of our mortgage advisors are fully qualified to provide advice.

In addition to having a consistent range of good value mortgage products, we are investing significant resource into our online mortgage application system with online decision in principle and broker registration systems going live in 2014 and online mortgage applications set to go live in the first half of 2015. We continue to offer all of our mortgage products to both new and existing customers and this is reflected in our high customer retention rates with over three quarters of borrowers choosing to stay with us on product maturity.

Throughout the year we regularly engaged with our members, who provided feedback to help us develop our business, provide challenge and make what we do relevant. In 2014 we developed video advice for our website to encourage good savings habits and guidance in support of the first time buyer borrowing process. Also, following feedback, we further enhanced our online savings to be available on mobile phones and tablets. We will develop the rest of our website in line with this. Our Customer Panel provided us with feedback on a range of topics such as electronic payments, use of passbooks, as well as helping the Society develop further its unique ISA proposition.

We also hosted a 'Meet the Chief Executive' session for members to receive a business update and ask our Board members about the general marketplace, our products and services. This was in addition to the financial planning seminars we held throughout the year to existing and potential customers that focussed on providing information on a range of financial subjects, such as saving and investments, insurance, mortgages, and wider financial planning. We also arranged local community history walks and branch events. These and other member engagement events will continue throughout 2015 and are an important part of the support we aim to provide to our customers.

We have seen a further fall in complaint volumes in 2014; total complaints fell by 20% with MPPI complaints falling by 33% and non-MPPI complaints falling by 3.5%. We found in favour of our customers in 42% of non-MPPI complaints and 2% of MPPI complaints with only 6% of non-MPPI complaints subsequently referred to the Financial Ombudsman Service (FOS). The majority of cases referred to FOS are found in the Society's favour.

Another very pleasing achievement came in the form of our annual customer survey. This showed overall satisfaction at 92% an increase from 91% the previous year. NFSL continued to support our aim of delivering financial advice that's accessible for all and the customer satisfaction results for this part of our business reached 97%, which is a significant increase on the 92% for 2013. This is an achievement that is particularly noteworthy given it was only in 2013 that new regulations were brought into force in the form of the Retail Distribution Review, which resulted in many institutions withdrawing from the advice marketplace.

Employees

We continue to engage with our staff so we understand their views of the Society and what it's like to work here. This has formed part of our Employer Brand development, which focuses on building trust, building our people and building our communities. Ultimately we want to be employer of choice in the North East. In 2014 staff from all levels across the business took part in "Who We Are" workshops and the feedback from this has helped us shape our people agenda and help drive forward developments we want to make to the business. This work ties in perfectly to the Values that we launched in 2013. Developing our Employer Brand alongside the rollout of our Values will continue to have a positive impact on improving service to our customers. By engaging with our staff and understanding their needs, supporting their development and keeping them motivated, we will ensure we continue to deliver excellent customer service.

We have again held our annual staff survey and I'm pleased to say we have achieved an outstanding result. Around three quarters of staff participate in the survey and the satisfaction rate reached a new high of 90% in 2014.

This year, we introduced the Talent Management programme, which is designed to support development of potential future leaders of our business. For this, we work in partnership with the University of Sunderland Business School to progress our staff through a Leadership Programme. The purpose of this is to encourage personal transformation and understanding of leadership styles. This supplements other programmes that the Society already has in place.

Our staff turnover rate across the whole business increased from a record low in 2013 of 10.2% to 12.6% in 2014, reflecting a more competitive employment market and reducing rates of unemployment.

In April we gave an annual pay award that was ahead of UK wage inflation. In December the Remuneration Committee approved a Society-wide Corporate Bonus, based on achievement of the Corporate Key Performance Indicators, which will be paid to staff after the approval of the Annual Report and Accounts.

Communities

Our 'Cornerstone of the Community' initiative entered its fifth year. Two activities are at the heart of this and they continued in earnest. Our financial education curriculum-based learning programme has now helped more than 1,400 school pupils learn about being financially independent later in life and is something we are looking to extend even further in 2015.

In addition, we held our biggest ever awards ceremony for local heroes during which a range of local community groups and individuals were rewarded for their hard work within the North East. Our hope is that this will continue to gain momentum and we aim to hold four events during the next 12 months in our heartland area.

We also updated our Charity of the Year programme that has run for six years. Instead of supporting one local charity over 12 months, we will extend our support for a minimum of two years. This means we can deliver even more value to a local good cause, Percy Hedley Foundation, a very well deserving charity that helps children and adults in our region with learning disabilities.

The Society also developed a new Volunteer Policy, which has granted our staff time during their working week to support a range of charities. We hope, through this Policy, to help even more organisations in our area that wouldn't ordinarily be able to receive such support without significant financial investment.

Our fund within the Community Foundation celebrated its 25th birthday and we marked the occasion with more donations to worthy causes in the area for specific projects, such as a local school to help build a sensory room for children with disabilities, a food bank, a family support group and an organisation that pays for days out for disadvantaged children within our region.

Summary

I am pleased with the Society's continued and steady progress in 2014 and that we are in good shape going into 2015 and beyond.

Our success is dependent on the outstanding team of people we have working at the Society. Their exceptional loyalty and commitment has enabled the Society to deliver the year on year improvement in our results and I would like to thank them for their contribution in 2014 and over the last 5 years.

Jim Willens
Chief Executive
24 February 2015

The Directors present their Strategic Report on the Group for the year ended 31 December 2014.

Overview of Business and Strategy

As a mutual organisation our owners are our customers and the Society's business model is based on providing Members with a secure home for savings and mortgages to buy homes. Our members have for over 150 years trusted us to look after their money in return for interest on the amount saved, allowing us to use these balances to extend mortgages to customers looking to buy a home.

Our borrowers pay us a rate of interest which is generally higher than we pay out to savers and this generates a "margin" which is then used to cover the administrative costs of running the Society's business and to generate a profit. From a financial perspective the Society needs to make profits in order to grow and protect our business but we do not seek to maximise profits. We look to optimise our profit position to maintain capital strength and allow us to continually improve our services to Members.

As well as providing mortgage and savings accounts to our Members we also provide a number of other related services, including regulated financial advice for investments through our partner Openwork LLP, insurance products including home and contents insurance through our partner Legal & General Group PLC, as well as other services we believe our Members will benefit from. The Society also provides IT and savings administration services to third party financial institutions, based on the core competencies within the Society's business.

The Solutions business operates on a commercial basis, to make a profit, and the profits from this business generate capital enabling the Society to invest and do more mortgage lending than it otherwise would have been able to do.

In 2010 the Society reviewed its strategy and identified a number of areas where improvement was required in order to enhance the financial strength of the Society and refocus attention on key stakeholders i.e. Members, Staff, Communities, Regulators and Solutions customers. The key objectives of the strategy, which remain unchanged from 2010, are as follows:-

- To put our Members at the heart of our business providing good value products, excellent customer service and high satisfaction levels;
- To engage fully with employees and improve satisfaction year on year;
- To simplify the Society's business and return to a straightforward building society model with a diversified Solutions business built on core competencies;
- To unwind legacy mortgage portfolios that have a high risk or low return and that do not fit with the building society model of prime residential lending to individuals; and
- To reduce the cost base and improve profitability and key capital ratios to further strengthen the Society's financial base.

Key Performance Indicators

The Society uses a suite of financial and non-financial Corporate Key Performance Indicators (KPIs) to monitor ongoing performance against the strategic plan objectives and 2014 has continued the steady progress made since 2010.

Our KPIs are important to us, particularly the year on year trends and how they compare to our peer group, as they show the continuing progress the Society is making.

PROFITABILITY	2014	2013	KPI met
Group operating profit before provisions and exceptional items	£12.4m	£10.6m	✓
Profit before tax	£4.0m	£1.3m	✓
Net interest margin	0.70%	0.61%	✓
Cost to income ratio	74%	76%	✓
Solutions operating profit	£6.9m	£6.9m	✓
CAPITAL			
Total Capital (Solvency) ratio	18.6%	17.8%	✓
Tier 1 ratio	14.6%	14.1%	✓
Core Tier 1 ratio	12.7%	11.9%	✓
CREDIT QUALITY			
Properties in possession	7	12	✓
3 months or more arrears for total mortgage portfolio, by number	0.53%	0.64%	✓
3 months or more arrears for total mortgage portfolio, by balance	0.75%	1.00%	✓
Legacy portfolio wind-down	£181m	£160m	✓
LIQUIDITY			
Liquidity as a percentage of shares, deposits and liabilities	23.6%	26.3%	✓
NON FINANCIAL			
Staff turnover	12.6%	10.2%	✓
Staff satisfaction	90%	81%	✓
Gross lending	£350m	£350m	✓
Net residential lending	£134m	£130m	✓
Telephone - % achievement of all service levels	91%	78%	✓
Servicing - % achievement of all service levels	99%	97%	✓
Complaints handling % - achievement within service level	99%	97%	✓
Customer satisfaction	92%	91%	✓
Investment in infrastructure and delivery of key regulatory projects	100%	100%	✓

A Corporate Bonus of 3% of basic salary is payable to all staff based on achievement of the Corporate KPIs for 2014, as determined on a discretionary basis, by the Remuneration Committee.

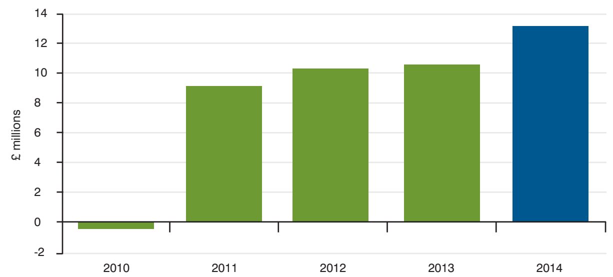
Further details are provided in the Chief Executive's report on page 6 the Directors' Report on page 18 and also within the detailed commentary provided below. The principal risks and uncertainties facing the Society in delivering this ongoing strategy are set out in the Risk Management Report on pages 30 to 33.

Overview of Financial Performance

Although remaining relatively modest, profit before tax continued an improving trend, increasing to £4.0m in 2014 from £1.3m (as restated, see Note 1) in 2013. This improvement once again comes as a result of improved operating profit and lower overall provisions for liabilities and charges.

Operating profit before impairments, provisions and exceptional items is considered by the Board to be a primary financial KPI; it has improved to £12.4m in 2014 from £10.6m in 2013. The improvement has been achieved through a higher net interest margin due mainly to lower retail funding costs and lower costs achieved due to ongoing efficiency projects including a pension liability management exercise. This progress continues to be supported by a diversified income stream generated by the Solutions business where profits remained stable.

Operating Profit / (loss) before Impairments, Provisions, FSCS levy and Exceptional Items



The financial strength of the Society continued its year on year improvement with the Core Equity Tier I ratio increasing to 12.7% from 11.9% in 2013, reflecting further de-risking of the Group's balance sheet in 2014. Core Equity Tier I capital is the strongest form of capital and represents accumulated profits built up over time compared to group assets, weighted according to how much risk they carry. The increase above 12% is particularly significant as it triggered the cessation of the capital conversion feature and removal of the coupon uplift from instruments to which the Capital Agreement had been applied in 2010, at a time when the Society's Core Tier 1 ratio was only 8.7% and this provided a much needed form of contingent capital. We achieved this trigger several years ahead of plan, further demonstrating the Society's improved financial strength since 2010.

Gross residential lending remained steady in 2014 at £350m (2013: £350m) in the face of increased competition and new regulations introduced in the form of the Mortgage Market Review in April 2014. The Society's strategy to de-risk its balance sheet saw a further £181m of legacy mortgages with either low margins or higher risk profile redeem from the balance sheet in 2014 (2013: £160m). However, the Society retains its cautious approach to remaining legacy exposures mindful of underlying trading conditions and sensitivities in the commercial property sector. As such the Society has provided a further £5.9m against impaired loans where a trigger event has identified there may be a problem in the servicing of the loan.

The Society fully exited the residential letting business in 2014 by completing the sale at market value of the final properties held by the subsidiary, Kings Manor Properties Limited, bringing to a close another legacy business area.

Income statement review

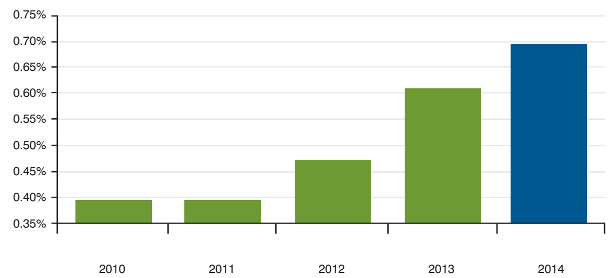
GROUP INCOME STATEMENT	2014	2013 Restated
	£m	£m
Net interest income	25.1	23.4
Other income and charges	22.3	24.1
Total income	**47.4**	**47.5**
Administrative expenses	(33.2)	(34.6)
Depreciation	(1.8)	(2.3)
Operating profit before impairments, provisions, FSCS levy & exceptional items	**12.4**	**10.6**
Impairment losses - banks and debt securities	-	0.8
Impairment losses - loans	(5.9)	(6.7)
Provisions for liabilities and charges	(2.5)	(4.0)
Gain on disposal of Prepaid Cards	-	0.6
Profit for the year before taxation	**4.0**	**1.3**

Net interest income

Net interest margin has increased from 0.61% in 2013 to 0.70% in 2014 driven mainly by lower funding costs as market-wide retail savings rates fell further in response to a fall in the longer term rate view and ongoing funding initiatives provided by the Bank of England. The Society's margin also benefitted from holding reduced levels of liquidity across the year; liquidity has a negative impact as the returns generated are generally lower than the cost of funding. Mortgage lending volumes were maintained in 2014 although the market was more competitive and this fed through to narrower margins on new business. Residential lending growth was margin enhancing overall however this was partially offset by the negative impact on margin of legacy wind down, particularly on commercial loans.

Net interest income is expected to continue to improve and we will maintain our strategy of managing the margin with a view to the long term future; this includes balancing the risks and rewards from residential lending while offering consistent value to savers.

Interest Margin as a Percentage of Mean Total Assets



Other income and charges

Net other income across the Group decreased in line with expectation by 11% to £23.3m in 2014 from £25.2m in 2013. Reduced mortgage administration fees was a key driver for this reduction as the Society offered more fees free mortgage products to compete in a more challenging UK market.

Income from the Solutions' business fell slightly from £15.9m to £15.2m as savings balances under management were affected by the ongoing availability of cheaper funding via Bank of England initiatives, resulting in reduced demand for retail funding. However, further efficiencies and processing improvements saw the operating profit for the Solutions business remain unchanged at £6.9m. This was despite both the fall in income and recognition of costs associated with new contracts where income streams will not be seen in full until 2015.

Diversification through the Solutions business is a key element of the Society's strategy, the pipeline of savings management contracts is strong and further growth of the business is expected in 2015 and beyond.

Administrative expenses and depreciation

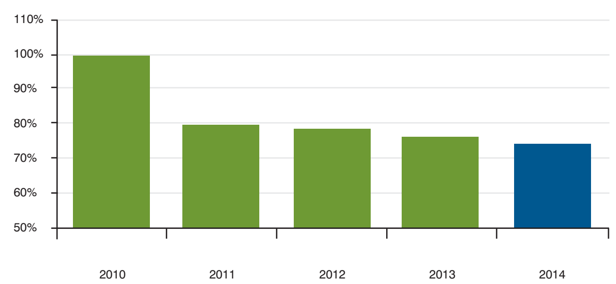
Administrative expenses and depreciation (together "management expenses") fell from £36.9m in 2013 to £35.0m in 2014; this is despite upward pressure on costs in relation to wage inflation and increased costs of regulation.

Administrative expenses have reduced mainly due to the £2.3m (net of associated costs) benefit of a liability management exercise for the Group's (now closed) defined benefit pension scheme. A pension increase exchange has allowed retirees and members still of working age to receive larger sums in the early years of their retirement in exchange for the foregoing of increases in later years. Further details are disclosed in Note 7 of the Annual Report and Accounts.

The ratio of management expenses to mean total assets was 0.93% in 2014 compared to 0.94% (restated) in 2013; the 1bp movement is wholly due to an increase in mean total assets, in turn a result of increased fair value adjustments. The management expense ratio is less reflective of the Group's business model in that the Solutions business income stream requires minimal assets to support it. The Board feels that a more relevant measure, and a KPI it monitors on a monthly basis, is the ratio of cost incurred to income generated. This metric improved to 74% in 2014 from 76% in 2013 and further long term improvement is expected as income grows and strong cost control is maintained. Underlying costs grew by less than 3% in 2014 reflecting an annual pay review of 2% in April 2014 and a slightly higher Corporate Bonus payment of 3% in respect of 2014 (2.5% in 2013). Depreciation expense fell to £1.8m in 2014 from £2.3m in 2013, however depreciation is expected to increase going forward reflecting a greater annual investment in the branch refurbishment programme and also the full year impact on depreciation of capital expenditure of £3.5m in 2014.

Further investment in IT and infrastructure is expected over the coming years to ensure we continue to offer the best service to customers, provide a quality environment for our staff to work in and to maintain our technology platforms at a leading level.

Cost to Income Ratio



Impairment losses

The impairment charge for loans and advances to customers has fallen overall to £5.9m in 2014 from £6.7m in 2013, excluding provision charges for suspended interest. Although the Society has experienced reducing provision charges overall in each of the last three years the charge remains above historic, pre-credit crunch, levels. The continued high level of provisioning reflects the ongoing demands and economic uncertainty which particularly impact on legacy commercial investment loans, borrowers and property values. A summary of loan impairment charges, which demonstrates the significance of commercial provisions to the overall charge, is included below with full details of provisions included in Note 14 on page 54 of the Annual Accounts.

IMPAIRMENT CHARGES BY AREA	2014 £m	2013 £m
Commercial	7.7	6.1
Residential (1)/ Other	(1.8)	0.6
Provisions charge for the year	5.9	6.7
Interest added to provisions (2)	(0.2)	2.2
Total charge recognised	**5.7**	**8.9**

(1) Residential includes provisions in relation to owner occupier and Buy to Let properties
(2) Interest provisions flow through net interest margin and relate primarily to commercial loans

Commercial

The total commercial impairment charge for the year including interest added to provisions amounted to £7.5m for 2014 (2013: £8.3m). The Society has been successful in its strategy to de-risk the commercial portfolio by winding down the loan book with a £344m, or two thirds, reduction in exposures since the beginning of 2010. The difficult trading conditions prevalent at the depth of the financial crisis have over the last few years abated to a degree but the requirement to provide for impairments that are considered 'incurred' continues. Impairment calculations are carried out by considering future discounted cash-flows as per rules laid out in international accounting standard, IAS39. In considering future cashflows the Society estimates the future valuation of the security less anticipated disposal costs, any interest rate hedge unwind required as well as interest rates, operational expenses and charges. The Society considers several factors when deciding if a commercial exposure is impaired including any missed payments, tenant failure, tenant voids and likelihood of re-letting and any other potential loan servicing issues arising from assessments or professional advice particularly where this provides evidence that a loan is or is unlikely to be fully serviced. In addition a full review has been carried out of loans where forbearance has been granted during 2014 including; capitalising arrears, extending the loan term, or where there has been a renegotiation of the original loan terms and conditions. The Society has a provisioning committee, chaired by the Society's Strategy Planning and Risk Director, with terms of reference for ensuring full and consistent application of the Society's impairment methodology to commercial loans, with the best internal and external information available.

Residential

In 2014 the impairment provision for residential lending is a credit of £1.8m (2013: charge of £0.6m) which relates to historic lending to Buy to Let (BTL) portfolio investors, where the Society has been successful in legal action to recover losses written off in previous years. Portfolio BTL is another legacy loan portfolio being wound down (although the Society may return to the BTL market for individuals requiring smaller loan balances in the future) and the provision release follows successful management to redemption of previously problematic loan exposures. Credit losses on the Society's residential lending assets continue to be small compared to the size of the portfolio which amounts to over 91% of the Group's total mortgage assets. The credit quality of these loans is excellent and they continue to perform, with 3 month arrears being around half industry averages. Impairment of the residential book is considered collectively for loans with 3 months or more arrears based on an estimation of loss given default and probability of default based on individual loan circumstances. All properties entering possession are provided specifically based on loan to value and anticipated disposal costs. A small collective provision arises from the Society's roll-rate to possession modelling for loans with low arrears, previous arrears or where forbearance has previously been granted.

Provisions for liabilities and charges

The 2014 charge recognised in the Income Statement of £2.5m relates to the Financial Services Compensation Scheme (FSCS) levy (2013: £2.7m restated). The levy charge covers estimated liabilities under the rules of the scheme in compliance with applicable International Financial Reporting Standards and guidance, IAS37 and IFRIC6. The Society has adopted the clarification set out in IFRIC 21 for the 2014 reporting period and, as adoption results in a change to accounting policy, affected figures in previous periods have been restated. The restatement is not however considered sufficiently material to restate previous year in additional columns in the primary statements. Further details of the restatement can be found in Note 1 on page 47, and in Note 26 on page 62.

Taxation

The Group shows an effective corporation tax rate of 28% in 2014 or £1.1m. The tax charge relates to the reduction in the deferred tax asset carried on the balance sheet. This reduction arises as taxable losses from previous years are used to extinguish the current year corporation tax charge (£0.9m). Corporation tax rate changes in 2014-5 were enacted in 2013 and therefore the impact of these tax rate reductions on the deferred tax asset were written off in 2013. The Society and Group have not paid any corporation tax since 2007 due to the taxable losses available.

Other Taxes paid by the Society in 2014 are summarised in the table below:

	£m
Employer's national insurance	1.8
Value added tax	1.5
Total	**3.3**

Further details of the Group's activities and the tax jurisdictions in which it operates can be found in the Country by Country Reporting on page 81.

Balance sheet review

Liquid assets

The Society has continued to maintain a high level of quality liquid assets throughout 2014, operating at all times at levels in excess of the minimum regulatory liquidity standards. The majority of the Society's liquidity is held in a regulatory liquid assets buffer which comprises cash balances with the Bank of England, UK Government gilts and Supranational bonds. The Society also holds Residential Mortgage Backed Securities and Covered Bonds that can be used to raise funding through the repo markets or via the various Bank of England liquidity schemes. The Society also holds eligible mortgage collateral that can be used to draw down funding from the Bank of England liquidity schemes. A lower liquidity percentage of 23.6% at 31 December 2014 (2013: 26.3%) reflects a more optimal position for the Society with careful management by the treasury team reflecting the need to balance levels of liquidity against the negative margin impact of low yielding liquidity.

The Society has a robust and careful approach to its liquid asset investments with thorough credit risk assessment policies and practices. As can be seen in the tables below, the majority of liquidity is held with UK institutions and held mainly in assets rated AA- or above.

RATING	2014 %	2013 %
AAA	33.0	40.4
AA+ to AA-	48.8	50.9
A+ to A-	12.5	5.7
BAA+ or lower	0.2	0.9
Unrated societies	5.5	2.1
Total	**100.0**	**100.0**

COUNTRY EXPOSURE	2014 %	2013 %
Australia	-	1.6
Iceland	0.2	0.5
UK	94.5	93.4
Supranational	5.3	4.5
	100.0	**100.0**

The Society has no exposures to counterparties based in the Eurozone. The Icelandic exposure relates to legacy holdings dating back to 2008 and prior years.

The table below shows the Society's liquid assets profile by asset class at fair value.

ASSET CLASS	2014 %	2013 %
Cash in hand and balances with the Bank of England	40.5	33.4
Cash with banks and building societies	26.5	12.8
Gilts	-	11.1
Fixed rate bonds	-	0.6
Floating rate notes	3.9	3.4
Residential mortgage backed securities	22.0	27.3
Covered bonds	7.1	11.4
	100.0	**100.0**

All of the Society's liquid assets are denominated in UK sterling; the Society does not invest in instruments denominated in other currencies.

Loans and advances to customers

Loans and advances to customers fell by £47m overall in 2014 as shown in the table below, which also illustrates the Society's strategy to wind down legacy portfolios and concentrate on prime owner-occupied residential lending. The net £47m balance reduction includes £181m fall in legacy books and a £134m increase in prime residential balances (NB there are also some legacy books in wind down within the prime residential portfolio e.g. the small loan book in Jersey). The prevailing low interest rate environment has meant the Society is still experiencing higher than average capital and lump sum repayments on residential loans; also all new lending has been on a repayment basis only since 2012. It is therefore pleasing to see prime residential lending continue to grow in 2014. The Society will continue to pursue interlinked strategies of legacy wind down, and residential lending growth where the balance between credit risk and net return are within risk appetite.

LOAN PORTFOLIOS	2014 £m	2014 LTV%	2013 £m	2013 LTV%
Prime Residential	1,678	54.9	1,552	56.1
Specialist Residential	101	70.2	132	73.4
Housing Associations	670	70.6	734	71.8
Commercial	192	86.8	267	96.4
Other	43	79.7	46	63.4
	2,684		2,731	
Provisions	(24)		(30)	
	2,660	**62.1**	**2,701**	**65.5**

Since the start of 2010 the Society has reduced legacy portfolios by £0.8bn with the largest element of this reduction relating to commercial investment loans, falling by £344m or 63%. The loan to value ratios are down on all books except the Other category that contains the Society's lending secured on endowment policies and retail lending on serviced apartments. The Group's lending is all secured with a first charge registered against the collateral property. Residential loans are shown at indexed loan to value using the quarterly regional Halifax House Price Index, remaining loans are shown without indexing although all commercial loans have been revalued since 2011. Further information on security loan to value is provided in Note 33.

Overall Arrears

The Society measures mortgage arrears of 3 months or more (excluding possessions) by both number of loans and balance as a percentage of total number of loans and total balance, respectively. The levels of arrears experienced continue to be below Council of Mortgage Lenders reported averages. Overall by number of loans arrears are down by 11bp to 0.53% from 0.64% in 2013, influenced by a similar sized fall in the Society's largest loan category, residential lending. Overall by balance the arrears ratio has decreased by 25bp to 0.75% from 1.00% in 2013.

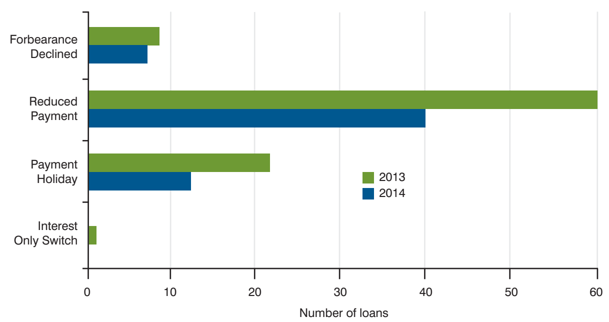
ARREARS PERFORMANCE
3 months or more arrears

	By number of loans		By balance	
	2014	2013	2014	2013
	%	%	%	%
Residential	0.52	0.63	0.39	0.61
Commercial Investment	1.24	1.50	6.03	5.78
Housing Association	-	-	-	-
Other	0.76	0.72	0.36	0.31
All mortgages	0.53	0.64	0.75	1.00

Residential Arrears, Forbearance and Possessions

Residential arrears have fallen by 11bp to 0.52% by number, and by 22bp to 0.39% by balance, the lowest since the 3 months or more metric has been measured. The decrease is due mainly to the managed reduction of the higher risk and higher value BTL mortgage book loans, and also due to the increasing size of the residential mortgage book. These specialist residential loans fall into the Society's legacy group of assets and management of problem cases within this category has again been successful in 2014. The low arrears rates reflect the strong credit quality of lending and benefits of having a long serving experienced underwriting team. Forbearance data is monitored closely on a monthly basis by the Society's Retail Credit Committee with the levels of concessions granted not considered to be material for the size of the overall book.

Residential Forbearance



Residential possessions - owner occupier, number of loans	31-Dec-13	Taken in	Sold	31-Dec-14
Equity release managed sale	3	1	4	-
Court action by the Society	1	5	5	1
Abandoned/surrendered	-	3	1	2
Total owner occupier possessions	4	9	10	3
BTL possessions	8	-	4	4
Total residential possessions	**12**	**9**	**14**	**7**

The Society continued to experience a low level of possessions on residential loans in 2014 with only three possession properties at the end of 2014 in relation to owner occupied loans, representing a reduction of one from the end of 2013. The Society took in 9 properties on owner occupied loans in 2014 with the majority of these a result of Society court action following exhaustion of options to assist the borrower involved. Further details are given in the table above. Possessions on BTL properties also reduced from 8 to 4 as no new possessions were taken in and 4 were divested. There was one new BTL case subject to LPA receiver appointment giving a total of four loans of this type being managed by an LPA receiver.

Commercial Investment Arrears, Forbearance and Possessions

At 31 December 2014 the Society had three commercial investment loans in arrears of 3 months or more with balances of £13.1m, this compared to four at the end of 2013 with balances of £16.8m. Two of these loans have offers accepted on them and are proceeding to sale subsequent to the year-end. Total specific provisions against these three loans amounted to £6.5m (2013: £3.7m). The Society had no commercial loans in possession at the end of 2014 (2013: none). At the end of 2014 the Society had no exposures subject to LPA receivership (2013: one exposure with balance of £16.3m).

The Society generally goes down the route of LPA receiver appointment where the relationship has broken down with the borrower and the Society needs to ensure the security property is properly managed in order to secure the best outcome for the Society in terms of eventual repayment of the loan. This approach has produced acceptable outcomes in the past few years and the Society expects to continue to adopt this approach should any further similar situations arise. The Society grants forbearance to commercial borrowers in the form of extending the loan term on maturity, capitalising arrears as part of a wider exercise to get a borrower back on track with a revised debt repayment plan, and adjusting the interest rate to aid serviceability particularly where a fixed rate has expired. Generally the Society expects commercial investment loans to be repaid on maturity given the stated strategy of winding down the portfolio but will grant forbearance when this is also in the best interests of the Society e.g. providing the borrower with a little more time to sell the security property following a tenant renewal. In Note 33 on page 77, details are given of forbearance granted to commercial borrowers in 2014; in summary the Society granted loan extensions on four loans (on original commercial terms or better), one of which would be considered impaired. There were no arrears capitalised on any loans.

Funding

The Society manages its funding levels, mix and duration carefully to ensure it has the required resources in place to meet its liquidity and lending targets. In recent years, because of the success in winding down legacy mortgage books this has had the effect of reducing overall funding requirements. Retail savings balances fell by £264m in 2014 with wholesale exposures increased across the year by £138m. This movement in funding mix resulted in the percentage of wholesale balances to total share and deposit liabilities increasing from 4.19% in 2013 to 8.59% in 2014. The Group's mortgage loans remain wholly funded by retail savings balances.

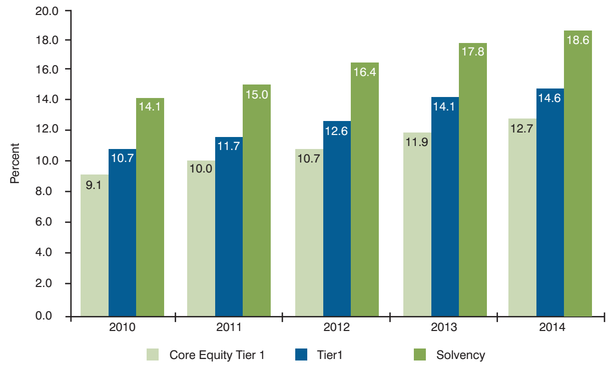
Capital

The table below shows the composition of the Group's capital and the capital ratios at the end of the year.

CAPITAL	2014 £m	2013 £m
Tier 1 Capital		
Core Tier 1 capital	159.7	167.1
Permanent interest bearing shares	24.0	29.7
	183.7	196.8
Tier 2 Capital		
Subordinated Debt	45.4	46.2
Collective impairment allowance	4.2	6.1
	49.6	52.3
Total Capital	**233.3**	249.1
Risk Weighted Assets		
Liquid Assets	56.5	71.2
Loans and Advances to customers	1,079.3	1,198.1
Other Assets	33.0	44.1
Off Balance Sheet	15.9	15.1
Operational Risk	72.2	71.4
	1,256.9	1,399.9
Capital Ratios	%	%
Core Tier 1 ratio	12.7	11.9
Tier 1 ratio	14.6	14.1
Solvency ratio	18.6	17.8

The Group complied with Individual Capital Guidance as notified by the Prudential Regulation Authority throughout 2014. All of the capital ratios show improvement in 2014 and follow a trend of a strengthening capital base with the total solvency ratio improving to 18.6% (2013: 17.8%) and Core Equity Tier I improving to 12.7% from 11.9%.

Capital Ratios



Basel III introduced several new capital requirements in 2014 and the Society has complied with all of these limits throughout the year. Also introduced by Basel III is the leverage ratio, which is a simplified capital strength ratio measuring qualifying tier 1 capital against on and off balance sheet assets. The Board monitors the leverage ratio on a monthly basis with the 31st December 2014 metric on a transitional basis being 5.2% (2013: 5.0%) and the final end point measure 4.5% (2013:4.4%). This is, and has remained throughout 2014, well in excess of the proposed target.

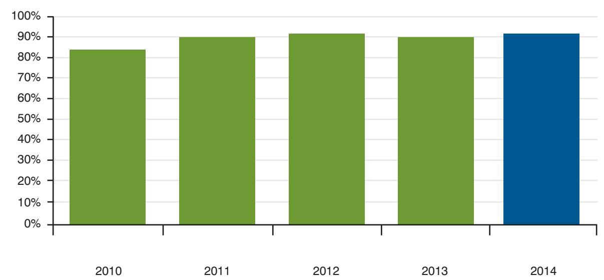
Further details on the Group's capital position including the transitional impact of Basel III is given in the Pillar III disclosures to be published on the Society's website in April.

Customers

In addition to financial indicators the Board monitors a range of KPIs designed to reflect how well the Group is meeting Members' and customers' needs. The Group's key customer metric is the customer satisfaction survey which shows the proportion of our customers who say that they are pleased with the service they received. The customer satisfaction survey showed overall satisfaction of 92% in 2014, above our target of 90% and an improvement on the 91% returned in 2013. In addition the overall satisfaction within the financial advice subsidiary, Newcastle Financial Services Limited, was 97% (2013: 92%), a fantastic result and testament to the quality and value Members receive from the financial planning service offered. Other customer KPI metrics including customer service levels in our call centres, measures of how easy it is to do business with the Society and the likelihood of Members to recommend our services, also surpassed targets.

The Society is keen to understand customers' needs and their thoughts on the organisation now and moving forward. The Society has in 2014 started to roll out its Distribution Strategy which has used customer feedback to influence for example new customer-facing technologies and how our branches look and work from a customer point of view. There is a delivery KPI for this important strategic project which shows that good progress is being made.

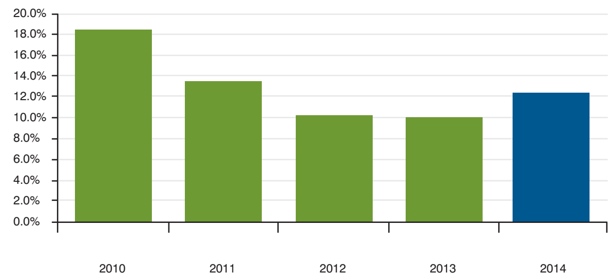
Overall Customer Satisfaction Percentage



Staff

The Society is committed to providing secure and long term employment for staff, the people agenda forming a key part of our strategy. The Society continues to invest in a number of programmes to develop and engage with staff and further details are given in the Directors' Report on page 19. Our staff turnover rate across the business was 12.6% in 2014 and although improving economic conditions have influenced the jobs market thereby influencing an increase on the record low of 10% in 2013, it remains well below the KPI target measure.

Percentage Staff Turnover



Outlook

There are still global headwinds blowing against the UK economic recovery and it is likely that the low interest rate environment will continue for longer than anticipated earlier in the year. Lower than target inflation and unemployment would appear to offer the opportunity for household budgets to improve but fresh turmoil in the Eurozone and the impending General Election will temper this somewhat in the short term at least.

The Society is in a much stronger position to deal with economic uncertainty having improved its capital base while retaining robust, high quality liquidity and improving year on year financial performance.

The Group's strategic objectives are clear and achievable, driving the business forward for the benefit of its Members, customers, staff and local communities. The financial strength of the Group means that we are going forward into 2015 well positioned to continue to deliver on our strategic objectives.

On behalf of the Board
Angela Russell
Deputy Chief Executive & Finance Director
24 February 2015

After reshaping our community and charity activities several years ago, we are very proud of the impact this is now having and how the scope of our activities is supporting the communities and people within our region.

As a mutual organisation, supporting the communities in which we operate is in our DNA. We aim to create a mutual support mechanism that adds real value to the local communities and lives of those within them. Below are some highlights of our biggest achievements this year.

Breaking the Million Pound Fundraising Barrier

In 2014 our donations broke through the million pound fundraising barrier for one of the region's best-loved charities.

The Society set up a unique partnership with The Sir Bobby Robson Foundation in spring 2012 by launching Foundation-branded ISA and Saver accounts, with an additional 0.1% of the total balances held in all such accounts being paid by the Society to the Foundation.

The Society is the largest corporate donor to the Foundation.

Lady Elsie Robson commenting on the milestone said: "When the Newcastle first approached us with this offer to help we had no idea where it would take us.

"To have raised more than £1 million is simply incredible. We hoped, and believed, it would work well but had no idea this partnership would become so successful.

"The Newcastle is very much part of this team effort. They understand what we're trying to achieve and its importance. I know they are very proud to be helping us find better ways to detect and treat cancer."

Watch a video we made with the Foundation via our YouTube channel www.youtube.com/NewcastleBSoc. or it can be viewed at: www.newcastle.co.uk/your-newcastle.

Jim Willens with Lady Elsie Robson at the launch of the Sir Bobby Robson Foundation Account.

Berta Leads at the Cornerstone Awards

An octogenarian community campaigner led a roll-call of everyday heroes from across the North East at a gala presentation evening held in their honour in front of around 200 people at the Great North Museum in Newcastle city centre.

The Society's annual Cornerstone of the Community Awards – with 2014's being the biggest ever event - recognises the positive impact individuals and groups have on the places they live in through their energy, enthusiasm and dedication.

Launched in 2011, the Awards cover four different categories, with nominations sought for each one right across the Society's branch network. Leading the way this year was Berta Walker, who picked up The People's Choice Award, which recognises an individual who is a great ambassador for their local area.

Now in her late 80s, Berta continues to work tirelessly for the Whickham community in which she lives, helping to run the St. Mary's Day Care Centre that she's been involved with for the past 30 years and she regularly raises money for local charities.

The Young Person's Award was given to 17 year-old Reece Dungey, who has been a member of the Children in Care Council in North Tyneside for five years, and has been involved with a wide range of projects aimed at improving and explaining the situations faced by looked after children.

Seventy-nine year-old Frances Cleminson of Gateshead was named as the Parent/Guardian of the Year, having looked after her six children, five of her sister's children, her mum in her final years and a number of foster children.

Described locally as a pillar of strength and a good angel, she has done all this on her own for the last 30 years after losing her husband.

Finally, The Sir Bobby Robson Foundation Team Award went to the Cornerstone Cafe in Whitley Bay, which hosts and is involved with a local group who support the rights of people with special needs.

There is a video of the evening, which can be viewed at www.youtube.com/NewcastleBSoc

Jim Willens with the 'Peoples' Choice' Winner, Berta Walker.

School Children Succeed

The seeds of an idea dreamt up by children from a Gateshead primary school has come into full bloom to win them the top prize in the Society's third annual Boardroom Challenge.

The team from Brighton Avenue beat rivals from 13 other North East schools to come out on top in the competition, which challenged the nine and ten year-old participants to develop business ideas that focus on benefiting their local community while also making a profit.

Eight teams made it through to the final of the competition and got the chance to present their creative fundraising ideas to a panel of senior business figures in the Society's boardroom.

And after an intense day of competition, the Brighton Avenue team came out on top due to the far-reaching impact their business idea would have on their local community.

The Brighton Avenue pupils, who nicknamed themselves The Veg Veterans, developed an idea around growing a community garden, with the produce grown not only being sold but also used to make other things to sell, and they're now set to use the competition's £1,000 prize to put their plans into action to raise money for the local People's Kitchen.

Both the Cornerstone Awards and Financial Education programme are part of the Society's ongoing Cornerstone of the Community campaign, which enables individual branches to provide support to good causes in their local areas in a variety of ways. Again, a video was made to showcase the talented youngsters, this can be viewed at www.youtube.com/NewcastleBSoc.

Boardroom Charity Challenge Winners, Brighton Avenue Primary, Gateshead.

Society Cyclists Raise Over £4,000

Society staff raised more than £4,000 for a range of good causes after successfully pedaling their way to the end of a long distance cycling challenge.

Dozens of staff from 19 of the Society's branches and two head offices came together to try to cover the full 3,656km distance of the Tour De France on exercise bikes located in their respective offices around the Society's heartland area.

At the end of a week-long series of events, the cyclists had smashed their target for the 'Tour De Branch' event by riding a combined distance of 4,119km.

Some of our staff prepare for the 'Tour de Branch' Challenge.

Staff Conquer 'Everest' Challenge

Staff took their fundraising work to new heights. They attempted to climb the 8,848m to the summit of Mount Everest – all on a stepper! The team of colleagues took turns on a step machine in order to do their respective bits towards the height of the world's biggest mountain being reached collectively across all the participating groups.

Staff taking part in our 'Everest' Charity Challenge.

The Society's Everest Challenge was set up as part of its ongoing 'Cornerstone of the Community' campaign, through which individual branches provide support to organisations and good causes in their local areas, which include a range of community charities, hospices, schools and voluntary organisations.

More than 300,000 steps were eventually achieved and around £1,500 raised for local charities.

Community Foundation

We have held an endowment fund with the Community Foundation for 25 years. Through this fund, each year we donate to a number of community groups.

In 2014, we decided to give over £8,000 to four local groups as nominated by our own staff.

Branch Manager Stephen Andrews (centre) with representatives from a local food bank.

Our Society-Wide Corporate Charity

For several years now, the Society has supported one charity for a 12-month period. This has helped raise over £150,000 for local charities. However, we wanted to extend our help further, so we decided to increase the length of time we support the chosen charity to a minimum of two years. This means we can add even more value supporting longer term projects.

The charity we're currently supporting is the Percy Hedley Foundation; a charity based in the North East which helps disabled adults and children, by providing services including school, college and disability employment.

Our Directors

Jim Willens
Chief Executive

Jim's expertise in, and commitment to, the building society sector spans more than 30 years. During this time, he has held significant senior posts including Retail Operations Director and Group Services Director at Nationwide. His roles over the years have included strategic responsibility for Branches, Telephony, Internet Services, Technology, Product Development and Central Support Services, which have involved leading teams in excess of 9,000 people. His career started out in the 'field' as a branch manager and he also held a range of retail and sales management positions. Jim has a strong track record of delivery and a passion for developing the people he works with to provide excellent customer service through the mutual business model both of which are key elements to the Society's strategy. He is a Non Executive Director of Brown Shipley & Co. Limited. Jim joined the Society in December 2009.

Angela Russell
Deputy Chief Executive and Finance Director

Angela is a highly experienced Chartered Accountant and Certified Public Accountant with 26 years' experience in finance in the UK and abroad. She has worked in a variety of positions covering finance, risk, audit, project and corporate planning roles. In particular, she has many years' experience in finance roles within the building society sector including her current role as Finance Director for the Newcastle, which she has held since 2010. She also held the post of Finance Director at the Universal Building Society. Prior to joining the building society sector Angela spent 12 years at PricewaterhouseCoopers LLP. She was a Non Executive Director at St Cuthbert's Care Limited in 2014 and in 2015 she has taken up a new appointment as member of the Audit Committee of Percy Hedley Foundation.

Andrew Haigh
Chief Operating Officer

Andrew has a track record in transforming and developing businesses. With 30 years' business experience and over 20 years in the mutual sector, he has held leadership roles as both an Executive and a Non Executive Director. As the former Chief Executive of Engage Mutual Assurance, he led the organisation for over 10 years, through a period of sustained growth and innovation. Andrew gained his strong customer focus through his early career in marketing and customer service roles with British Airways, Barclays and National & Provincial Building Society. An advocate of mutuality, he was previously Chairman of Mutuo, an independent organisation which promotes the development of new and existing mutuals to Government. Andrew joined the Society in 2014.

Patrick Ferguson
Strategy, Planning and Risk Director

Patrick was appointed to the Board in February 2014. Before this he was the Society's Group Risk Executive for almost four years after joining the Society in 2010. He has extensive experience in risk management, including conduct risk and regulatory compliance, in addition to financial reporting, planning, and budgeting. He has 15 years' experience in the Building Society sector and has held the posts of Finance Director, General Manager, Finance and Head of Strategy and Planning. He qualified as a chartered accountant with PricewaterhouseCoopers LLP.

David Buffham
Non Executive Director

David has spent most of his career at the Bank of England. He held a wide variety of banking and other roles, including the post of Bank of England Agent for the North East. There he was responsible for reporting to the Bank's Monetary Policy Committee on the region's economy and explaining policy to key stakeholders in the North East. He brings this knowledge and experience to the fore as Chairman of the Group Risk Committee and also as a member of the Nominations and Remuneration Committees. Additionally, he is a Director of Newton Facilities Management Limited. He is an experienced Non Executive Director and is a Director of Zytronic PLC, William Leech (Investments) Limited and The William Leech Foundation. David joined the Board in 2010.

John Morris
Non Executive Director

John is a Fellow of the Institute of Chartered Accountants and brings to the Society a significant amount of experience of both the banking and building society sectors. He worked for several years as Director of Finance for the Retail Banking Division at HBOS. Prior to that, he held senior posts at Halifax (Halifax Building Society and then Halifax PLC) as General Manager and Leeds Permanent Building Society where he held the post of General Manager Finance. He also worked at KPMG where he started his accountancy career. He is a member of the Audit, Nominations and Remuneration Committees. From the beginning of 2015 he joined Group Risk Committee having been a Board member since 2011.

Phil Moorhouse
Chairman

Phil has been the Society's Chairman since April 2013, having joined the Board as a Non Executive Director in 2011. He is a highly experienced accountant and is a Fellow of the Chartered Association of Certified Accountants. Phil has held a number of senior Board positions including that of Managing Director (UK) of Northgate PLC, which he held for more than seven years. This followed six years as Finance Director. He is a Director of Molins PLC where he is Chair of Audit and a Senior Independent Director. Additionally, he is Vice Chairman on the Board of Cumbria NHS Partnership Trust and was appointed a director of Transflex Vehicle Rental Limited on 20 January 2014. Phil brings his 36 years' industry expertise to the Newcastle's Board. Phil also chairs Newton Facilities Management Limited and Nominations Committee.

Ron McCormick
Deputy Chairman

Ron has established a successful career in the building society sector as an experienced accountant. He is both a Fellow of the Institute of Chartered Accountants and a Fellow of the Chartered Institute of Internal Auditors. He has previously worked as Group Finance Director then Group Commercial Director at Skipton Building Society, posts which he held for a total of 14 years. In addition, he has more than seven years' experience with Guardian Royal Exchange, as well as seven with KPMG, both in the UK and abroad. Following several years on the Society's Board, which he joined in 2007, in January 2011 he was appointed Deputy Chairman and Senior Independent Director. He is a member of the Society's Audit and Group Risk Committees. He also works as a senior adviser to businesses within a range of sectors. He is Chairman of Grassington Hub Ltd and a Director of Threshfield Quarry Development Trust Limited.

Catherine Vine-Lott
Non Executive Director

Catherine has a total of 36 years' experience in the financial services sector having spent her entire working life in the industry. This includes 18 years at Barclays where her positions included Chief Executive of Barclays Stock Brokers, as well as Barclays Personal Investment Management. In addition, she has significant experience with Legal and General both at group Board level and in running the wealth management division. This brings an abundance of expertise to the Society's Board, which she joined in January 2010, and to the Society's Audit and Remuneration Committees, which she Chairs. She is also an experienced Non Executive Director and currently sits on Just Retirement Limited's Board.

Ian Ward
Non Executive Director

Ian has spent over 40 years in financial services including Chief Executive of Leeds Building Society for 16 years until his retirement in August 2011. Ian is a Non Executive Director of Harrogate and District NHS Foundation Trust and a member of its Audit Committee. Ian was a director and vice-president of Leeds, York and North Yorkshire Chamber of Commerce and Chairman of its Property Forum. He was a member of the National Council of the Building Societies Association and a Director and Chairman of the Audit Committee of Leeds Training and Enterprise Council. He has been a Non Executive Director of Newcastle Building Society since July 2013 and is a member of the Group Risk Committee, and Director of Newton Facilities Management Limited. For information about other directorships taken up from January 2015 please see page 80.

Richard Bottomley OBE
Non Executive Director

Richard joined the Board in 2014 as a Non Executive Director. He is a fellow of the Institute of Chartered Accountants and in 2010 was awarded an OBE in the New Years Honours List for services to the Accountancy Profession and Business in the North East. He was Managing Partner at KPMG for 12 years prior to his retirement in 2008 and is a past President of the North East Chamber of Commerce. In his professional career spanning over 30 years he gained experience in Corporate Finance, Strategic Planning and was the Lead Audit Partner on some of the region's largest companies. More recently, Richard is Chairman of Greggs PLC Retirement Benefits Scheme, TL Dallas Group, Skillsbridge and a director at Durham CCC.

Karen Ingham
Non Executive Director

Karen has an extensive customer services background within the consumer sector and is extremely people and customer focused. She is currently the Customer Services Director at Virgin Media Limited. Her previous roles have included Head of Service and Customer Experience Director. She also spent 18 months as HR Director in the construction industry and started her career with 18 years in Financial Services at the Co-operative bank. Karen is a trustee of the Virgin Media Pension Scheme and also a member of the Chief Customer Officer Forum.

The Directors present their Annual Report and Accounts and Annual Business Statement for the year ended 31 December 2014, which they consider to be fair, balanced and understandable, providing Members with the information necessary to assess the Group’s performance, business model and strategy.

Objectives and Activities
It is the intention of the Directors that the Society will continue to remain an independent building society. We believe this status enables us to deliver excellent service to both our saving and borrowing Members; long term, secure and rewarding employment to our staff; and recognisable support to local communities. We also aim to provide best in class service for our Solutions business customers.

Business Review
The Chief Executive’s Review and Strategic Report on pages 6 to 13 set out the business activities and business performance in the year against our strategic objectives and key performance indicators, as well as likely future developments. The Directors have carried out a robust assessment of the Group’s capital, liquidity and profit forecasts and considered the risks faced by the Group, including under stressed scenarios. The Directors have considered the Group’s risk management and material controls as detailed in the Risk Management Report. The Directors are satisfied there are no material uncertainties that cast significant doubt about the Group’s ability to continue as a Going Concern and have, therefore, continued to adopt the Going Concern basis in preparing the Annual Report and Accounts. (See Note 1 on page 44).

Risk Management Objectives and Policies
The Board seeks to manage the key risks faced by the Group in order to minimise any potential adverse impact on performance. The key financial risks faced by the Group include credit risk, liquidity risk, operational risk and market risk which are managed through the Group’s documented risk management framework. Further details on material risks and how they are managed can be found below and in the Risk Management Report on pages 30 to 33.

Principal Risks and Uncertainties
The principal risks and uncertainties faced by the Group are summarised below.

Credit Risk - Commercial
The Society’s commercial mortgage portfolio has reduced in size by 63% over the last 5 years with total balances now standing at £192.9m representing 7.2% of total mortgage assets. The loan to value (LTV) on the commercial portfolio is higher than more traditional residential lending due mainly to downward movements in commercial property values since 2007. The Society ceased all commercial lending in 2008 and continues to successfully wind down the portfolio; however the potential for credit losses continues to be a material risk given commercial property prices could fall further. The Society mitigates the risk of significant credit losses by assessing each loan exposure individually and making provision for any exposure which demonstrates potential serviceability issues.

An additional £7.7m of provisions have been charged in the 2014 Annual Report and Accounts. The 3 month arrears rate on the Society’s commercial lending portfolio based on balances, was 6.03% at 31 December 2014 (2013: 5.78%) representing three loans with a value of £6.6m after provisions. This represented 1.24% of commercial real estate exposures based on number of loans (2013: 1.50%). Further details on commercial credit risk and provisioning are given in the Strategic Report on page 12, with further details on the risk governance structure given in the Risk Management Report on page 30.

The Society will, for the foreseeable future, maintain its robust approach of winding down the portfolio whilst at the same time reviewing provisions against the commercial property market backdrop and the existence of any trigger events suggesting a loss has been incurred. The Society does not assume any upside in its provisioning models.

Credit Risk – Residential
The Group’s residential lending portfolio comprises mostly well seasoned, performing, low LTV owner-occupier lending, which throughout the year continued to experience low levels of arrears and possessions. Average UK house prices have risen overall in 2014 across all regions, although the pace of growth has slowed somewhat toward the end of the year, including in the Society’s heartland region of North East England (which represents just under 20% of the residential mortgage book). This growth in house prices has lowered the Group’s average LTV ratio for residential lending thereby reducing the risk of significant losses should default occur. The Group maintains a diversified geographical distribution of residential lending, achieved through multi-channel mortgage delivery, mitigating exposure to concentrations of geographical credit risk.

Unemployment in the UK is falling at a higher rate than expected and, although no major effect on the Society’s arrears had been discernable over the recent period of higher unemployment, it remains a key factor in the credit risk associated with this type of lending. Overall, the number of 3 month residential arrears cases fell from 0.63% to 0.52% in 2014 with the value of 3 month arrears also falling from 0.61% to 0.39%. The number of residential properties in possession reduced from 12 to 7 of which 3 related to home owners. The number of residential loans subject to LPA receiver increased from 3 to 4, all relating to BTL portfolio investors and reflective of the Group’s strategy to manage this type of exposure to secure the best outcome. Further details are given in the Strategic Report. The Society expects risk within the residential mortgage portfolio to remain relatively benign and does not assume any upside in its provisioning models.

Liquidity Risk
The Society monitors on a daily basis the risk it will have insufficient cash to meet its liabilities as they fall due, including under stressed scenarios. The Society has throughout the year mitigated liquidity risk by maintaining high quality liquid assets and maintains low-level reliance on treasury markets, with the wholesale funding ratio remaining below 10% throughout the year. The Society undertakes lending only where funding is in place and operates a range of retail savings products to attract and retain customers. At the end of 2014 the liquidity ratio stood at 23.6% compared to 26.3% at the end of 2013.

Operational Risk
Further details on operational risk are given in the Risk Management Report on page 33.

Market Risk
The Society’s market risk relates only to interest rate risk in the banking book and the way interest margin is impacted by a changing rate environment. This includes basis risk as well as understanding the impact of upward and downward movements in interest rates. Sensitivity to, and effect of, interest rate changes is monitored by the Asset and Liability Committee. The Society actively measures the effect of rate movements in accordance with best practice, and manages the interest rate risk to which it is exposed using interest rate hedges or natural offsetting of asset and liability rate-characteristics. Further details are given in the Risk Management Report on page 32.

Group Results for the Year
Key developments and the future outlook are reviewed in the Chief Executive’s Review on pages 6 to 7 and in the Strategic Report on pages 8 to 13. The Strategic Report also includes the Group’s Key Performance Indicators (KPIs) and sets out how the Group has performed against its KPIs in 2014.

Staff
The Society operates an Equal Opportunities Policy. It is the intention of the Society that no applicant or employee receives less favourable treatment on the grounds of disability, sex, transgender status, sexual orientation, marital status, civil partnership status, race, ethnic origin, colour, age, nationality, national origins, political beliefs or trade union membership, or is disadvantaged by conditions or requirements that cannot be shown to be justifiable. The Board also has an approved diversity policy. The gender diversity for the Society’s staff at 31 December 2014 is as follows:

	Female		Male	
	2014	2013	2014	2013
Directors	23%	18%	77%	82%
Senior Managers	22%	20%	78%	80%
Employees	63%	64%	37%	36%
Overall	**62%**	**62%**	**38%**	**38%**

A pay review for staff takes place on an annual basis on 1 April. In addition a Corporate Bonus scheme operates for all staff which is based on the achievement of Corporate KPIs linked to the Society’s strategy. The 2014 Corporate Bonus payment, equal to 3.0% of salary, will be paid to all eligible staff following the approval of the Society’s year-end accounts. Unite has negotiating rights on behalf of all staff up to and including senior management level.

The Society takes its responsibilities for staff development very seriously and was the first building society to achieve Investors in People (IIP) status in 1992. The purpose of IIP is to improve an organisation’s performance through its people and in 2014 the Society was for the first time awarded ‘Silver Level’ status. The achievement of enhanced IIP status is a great endorsement of the recognition and importance that the Society places on investing in the learning and development of its staff.

The Society has an active staff engagement programme that aims to make continuous improvements thereby ensuring our organisation is a great place to work. In 2014 this engagement included not only the annual staff survey but also “Who We Are” workshops and the development of our Employer Brand strategy. The results and feedback received from staff will be used to shape aspects of people strategy going forward so we are an employer of choice in the North East. This work reinforces and extends the Values developed by staff to define both how we work with each other as well as how we operate as a business.

These Values are now firmly embedded into all aspects of day-to-day business, further details are given on page 4 under Our Vision and Our Values. Following on from the successful undergraduate placement and graduate training schemes adopted in previous years the Society introduced the Talent Management programme in 2014. In partnership with the University of Sunderland Business School the programme is designed to enhance and develop potential future leaders in the business.

Directors
As at 31 December 2014, the members of the Board, who had served throughout the year and continue to act as Directors were as follows:

David Buffham, Ron McCormick, Phil Moorhouse, John Morris, Angela Russell*, Catherine Vine-Lott, Ian Ward, and Jim Willens*.

Changes to the Directors in 2014 included the appointment of Karen Ingham and Richard Bottomley as Non Executive Directors on 4 September 2014 and 22 September 2014, respectively. Andrew Haigh* was appointed as Chief Operating Officer on 27 January 2014 and Patrick Ferguson* was appointed as Strategy, Planning and Risk Director on 19 February 2014. At the Annual General Meeting (AGM) to be held on 22 April 2015, all Directors will offer themselves up for either election or re-election, other than Richard Mayland who retired as a Director on 24 February 2015. Directors and Officers insurance has been put in place by the Society.

*Executive Directors

Independent Auditors
A resolution to re-appoint PricewaterhouseCoopers LLP will be proposed at the Annual General Meeting.

Statement of Disclosure to Auditors
So far as each Director is aware, there is no relevant audit information of which the Society’s auditors are unaware. Each of the Directors, whose names and functions are listed in the Our Directors section on pages 16 and 17 has taken all steps that he or she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Society’s auditors are aware of that information.

Statement of Directors' Responsibilities

The following statement, which should be read in conjunction with the statement of auditors' responsibilities on page 34, is made by the Directors to explain their responsibilities in relation to the preparation of the Annual Report and Accounts, Annual Business Statement and Directors' Report.

The Directors are responsible for preparing the Annual Report and Accounts, Annual Business Statement and Directors' Report in accordance with the appropriate law and regulations. The Building Societies Act 1986 (the Act) requires the Directors to prepare Group and Society Annual Accounts for each financial year. Under the Act they are required to prepare the Group and Society Annual Accounts in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU), and applicable law.

The Group and Society Annual Accounts are required by law and IFRS, as adopted by the EU, to give a true and fair view of the state of affairs of the Group and Society as at the end of the financial year and of the income and expenditure of the Group and Society for the financial year, and which provide details of Directors' emoluments in accordance with part VIII of the Act and the regulations made under it.

In preparing the Group and Society Annual Accounts, the Directors are required to:

- Select appropriate accounting policies and apply them consistently;
- Make judgements and accounting estimates that are reasonable and prudent;
- State whether applicable accounting standards have been followed subject to any material departures disclosed and explained in the Annual Accounts; and
- Prepare the Annual Accounts on the Going Concern basis unless it is inappropriate to presume the Group will continue in business.

In addition to the Accounts, the Act requires the Directors to prepare, for each financial year, an Annual Business Statement and a Directors' Report, each containing prescribed information relating to the business of the Group.

The Directors are responsible for ensuring that the Group:

- Keeps adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Society in accordance with the Act; and
- Takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its businesses in accordance with the rules made by the Financial Services Authority and Markets Act 2000.

They are also responsible for safeguarding the assets of the Society and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the financial information included on the Group's website. Legislation in the UK governing the preparation and dissemination of Annual Accounts may differ from legislation in other jurisdictions.

On behalf of the Board
Phil Moorhouse
Chairman
24 February 2015

Report of the Directors on Corporate Governance

Introduction

In discharging its responsibilities to be accountable to the Society's Members for the operation of the Society, the Board regards good corporate governance as extremely important. A revised UK Corporate Governance Code (the Code), issued by the Financial Reporting Council (FRC) in September 2012 is addressed to publicly quoted companies, however, the Society's Board considers it to be best practice to have regard to the Code when establishing and reviewing corporate governance arrangements. The Code applies to accounting periods beginning on or after 1st October 2012, and therefore, the Society has regard to the Code within the 2014 Annual Report and Accounts.

A working party continues to operate to ensure that the corporate governance procedures and processes within the Society are in line with the Code on an ongoing basis, including when updates or revised guidance are published. Although the FRC issued a revised version of the UK Corporate Governance Code on 17th September 2014, this is effective for reporting years commencing on or after 1st October 2014, and so will be first applicable to the Society's 2015 Annual Report and Accounts.

This report outlines the approach taken by the Society and how the Board considers it has demonstrated application of the principles of the Code.

The Board

The Society recognises that it must be headed by an effective Board which is responsible for the long term success of the Society. The composition of the Board is detailed on pages 16 and 17. The Board's Terms of Reference are reviewed on a regular basis and were last agreed by the Board in June 2014. Key responsibilities, included within the Terms of Reference, are set out below.

- The Board is responsible for agreeing the overall strategy for the Society, with the responsibility for implementing it being delegated to the Executive team. The Board is responsible for monitoring operational and financial performance in pursuit of the strategy;
- At a dedicated Board "Strategy Day" the Board agrees the strategic plan for the Society ensuring that the necessary financial and operational resources are in place so that the Society can meet its objectives and also that appropriate targets are set against which to review management performance;
- The Board is responsible for risk management, for governance, and for ensuring adequate internal controls. The Board delegates oversight of risk management to the Group Risk Committee, and oversight of internal controls to the Audit Committee;
- The Board completes a formal review of the effectiveness of risk management and internal controls on an annual basis with the latest review completed in January 2015;
- The Board is responsible for overseeing and approving the Society's Recovery and Resolution Plans and monitoring any recovery plan should it be invoked;
- The Board is responsible for approving the budgets and forecasts, the adequacy of capital and liquidity plans, the adequacy of the systems of internal control and major capital expenditure. In addition, the Board is responsible for final approval of the interim and annual accounts on a going concern basis;
- In order to oversee the business, the Board receives and reviews various reports and management information from Board Committees and the Executive team;
- The Board formally reviews its effectiveness, on an annual basis. The Board also has responsibility for overseeing the evaluation process for all Committees of the Board; and
- The Executive team have been delegated the task of ensuring that the business operates in a compliant way, with regard to all legislative requirements and guidance, and is focussed on delivery of the Strategic Plan and Budget, Internal Capital Adequacy Assessment Process (ICAAP), Individual Liquidity Adequacy Assessment (ILAA), and also progressing action points arising from the Board meetings, as appropriate.

There is a clear division of responsibilities between the running of the Board, and the Executive responsibility for the running of the Society's business. No one individual has unfettered powers of decision and the roles of Chairman and Chief Executive are exercised by different people within the Society. There is a need for all Non Executive Directors to be deemed to be independent, and the review of independence is carried out by the Nominations Committee (NomCo) as set out on page 22.

An effective Board should not necessarily be a comfortable place, with challenge, as well as teamwork, being an essential feature. Challenge by Non Executive Directors is something which is encouraged by the Chairman and, where appropriate, training is provided to support the challenge process. A culture of openness exists within the Society and Non Executive Directors are encouraged to meet with members of the Executive team.

Phil Moorhouse was appointed Chairman of the Society on 24th April 2013, and at the time of appointment was considered to be independent by the Board. The Board appointed Ron McCormick as Deputy Chairman and Senior Independent Director on 1st January 2011; he provides a sounding board for the Chairman and serves as an intermediary for the other Directors where necessary.

Board balance and independence is important and the Board should include an appropriate combination of Executive and Non Executive Directors (and in particular independent Non Executive Directors) such that no individual or small group of individuals can dominate the Board's decision making. The composition of the Board, through NomCo, reflects an appropriate balance of skills and at the end of 2014 the Board comprised of nine Non Executive Directors and four Executive Directors.

Details of the various Board Committees in existence are set out later in this report.

Board Changes and Elections/Re-elections

It is recognised that changes need to be made to the Board from time to time, and changes during 2014 are set out in the Directors' Report on page 19.

Copies of the Terms of Engagement for all of the Society's Directors are available on request, and at the Annual General Meeting (AGM).

One aspect of the Code provides that all directors of FTSE 350 companies should be subject to annual election by shareholders, and the Building Societies Association considers that this requirement would apply to the twelve largest building societies. Therefore, in line with good corporate governance, all Directors will continue to offer themselves up for either election or re-election at the Society's AGM. The biographies of all of the Directors are detailed on pages 16 and 17.

Management Information

The Chairman is responsible for ensuring that the Directors receive accurate, timely and clear information. Members of the Board receive monthly Board and Management Information packs except in August when there is no Board meeting, although a Management Information pack is still issued. A rolling Board agenda is tabled at each meeting to ensure all key areas are covered appropriately during the year. Sufficient time is set aside to ensure that constructive discussion and challenge can take place. Once a year, the Board considers whether the regular Management Information which Directors receive is adequate, and this was deemed to be so at the meeting held on 23rd April 2014.

All Directors have access to independent professional advice, if required, and also access to the services of the Group Secretary. Directors and Officers insurance has been put in place by the Society.

Board Effectiveness

The Board conducts a review of its effectiveness on an annual basis with the last review undertaken in December 2014. This review was carried out using a three pronged approach:-

- All Directors were asked to complete a questionnaire;
- An assessment was made against the first two principles of Leadership and Effectiveness set out within the revised UK Corporate Governance Code issued in September 2012, together with the FRC's guidance on board effectiveness published in March 2011; and
- Action points were followed up from the previous review reported at the January 2014 Board meeting, which was supported by an independent review completed by the Society's Internal Audit function which received consulting advice on the review from Deloitte LLP (Deloitte LLP provides other consultancy services to the Society mainly in relation to taxation and treasury).

The Board agreed that the review demonstrated it was conducting its business in an effective manner, had the depth of experience, and reacted to the changing needs of the business, as appropriate. Notwithstanding this conclusion, the review suggested some improvements, which will be followed up, as appropriate.

Board Committees

The Board has a number of Committees, all of which have their own Terms of Reference which are reviewed on an annual basis, further details being set down below. The Chairman of each Committee reports to the subsequent Board meeting on the matters discussed at each Committee meeting.

Similar to the Board, each Committee has carried out a review of its own effectiveness, and where improvement opportunities have been identified, the individual Committees are responsible for tracking action points. These reviews are carried out on an annual basis and the effectiveness review for each Committee is summarised and presented to the Board for review.

Information concerning attendances at the meetings is detailed on page 24. Terms of Reference for the Audit Committee, Group Risk Committee, Remuneration Committee and NomCo are included on the Society's website under governance (http://www.company-newcastle.co.uk/governance/)

Audit Committee

Details of the Audit Committee are contained in the Audit Committee Report on page 25.

Remuneration Committee

Details of the Remuneration Committee are contained in the Remuneration Committee Report on page 27.

Group Risk Committee

Details of the Group Risk Committee are contained in the Risk Management Report on page 30.

Nominations Committee (NomCo)

The Society has a separate NomCo comprising only of Non Executive Directors, and which operates within the Terms of Reference agreed by the Board. The Terms of Reference and the effectiveness of NomCo are reviewed on an annual basis and each of these tasks was carried out in December 2014.

The main objectives of NomCo are summarised as follows:-

- To oversee the structure of the Board and Board Committees;
- To identify suitable candidates to fill Board vacancies;
- To ensure that the Board has the appropriate balance of skills, diversity and experience; and
- To oversee the Board's succession plan.

All key decisions of NomCo, for example, Board appointments, must also be ratified by the full Board.

Members of NomCo are Phil Moorhouse (Committee Chairman), David Buffham, John Morris and Richard Mayland.

NomCo operates to a rolling agenda to ensure it discharges its full responsibilities. It normally meets a minimum of twice a year and in 2014 it met on two occasions.

NomCo is supported by the Chief Executive and the Human Resources Executive who attend meetings in an advisory capacity only.

Appointments to the Board

NomCo follows a stringent recruitment process when making appointments to the Board. This process is tailored to meet the requirements of each particular vacancy and the method of attracting candidates is adapted depending on the nature of the skills required for the vacancy. External consultants and advisors are normally utilised to ensure there is a robust list of suitable candidates with which to fill a vacancy. During the year the Society utilised the services of independent recruitment specialists NRG in the appointment of two new Non Executive Directors.

Whenever a new Director is appointed, the Financial Conduct Authority and Prudential Regulation Authority have the right to carry out formal "Significant Influence Function" (SIF) interviews in order that the director becomes an "Approved Person".

All Directors have been issued with Role Descriptions, and Terms of Engagement for Non Executive Directors, to ensure that all Directors fully understand and comply with their role and the responsibilities of being a Director of the Society.

During 2014, four new Directors joined the Board. Andrew Haigh was appointed Chief Operating Officer in January 2014 and Patrick Ferguson was appointed as Director of Strategy Planning and Risk in February 2014. In September 2014, Richard Bottomley and Karen Ingham were both appointed as Non Executive Directors.

Diversity of the Board

The Board recognises and embraces the benefits of having a diverse Board which utilises a range of factors including skills, industry experience, background, race, gender and the other qualities of its Directors. Giving specific regard to gender ratios, female representation on the Board has ranged from 33% in 2010 to 23% in 2014. It is important to note that all Board appointments are made on the basis of individual competence, skills and expertise measured against identified objective criteria.

Appointment is therefore based on merit and the Board has not set any measurable objectives for diversity although the position will be kept under review.

Re-election to the Board

It has been agreed previously by the Board that all Directors, as appropriate, should be required to seek annual re-election, which will take place at the forthcoming AGM, to be held on 22nd April 2015.

Non Executive Directors are usually expected to serve two full three year terms, subject to satisfactory performance evaluations and re-election by Members. They may also be proposed for a further third term but only in exceptional circumstances will Non Executive Directors be able to seek re-election when they have served nine years on the Board. NomCo has in place a risk based succession plan which is reviewed at each meeting as part of the standing agenda.

Independence of Directors

The Terms of Engagement for Non Executive Directors require that they declare to the Society any other external interests.

NomCo carries out an annual review of the independence of Non Executive Directors, and the last review was carried out on 16th January 2015. In the opinion of NomCo, and subsequently agreed by the Board, each of its Non Executive Directors is independent in both character and judgement. In January 2015, one of the Non Executive Directors, Ian Ward, was appointed as a director of a number of companies within the Charter Court Group, including Charter Court Financial Services Limited. He had previously advised the Board of the existence of this relationship, and under the Conflicts of Interest Policy had undertaken to advise the Board if any actual conflict arose.

The Society recognises that it is good corporate governance to have a Senior Independent Director. This role has been held by the Society's Deputy Chairman, Ron McCormick since 1st January 2011 and it is intended that, subject to re-election, he continues in this role.

During 2014, the Chairman met separately with the Non Executive Directors from time to time, without the Executive Directors present, in addition to regular telephone contact with the Non Executive Directors throughout the year.

Assessment of Directors

All Directors are subject to a formal appraisal of their performance on an annual basis. The Chairman conducts the appraisals of the Chief Executive and Non Executive Directors, the Chief Executive conducts the appraisals of the Executive Directors, whilst the Deputy Chairman/Senior Independent Director leads the appraisal of the Chairman.

Skills and Continuous Development

All Directors are required, as part of their terms of engagement, to follow a process of continuous development to ensure that their skills and experience meet the needs of the Society and the regulatory environment in which it operates. The training and development plans of Non Executive Directors are reviewed at least annually during their performance appraisal.

The Committee oversees the on-going training and development of Non Executive Directors including a formal induction programme for newly appointed Directors. The Chief Executive oversees the programmes for Executive Directors.

In order to ensure that the Committee discharges its duties in this area effectively, a Board skills matrix and a training menu for Non Executive Directors are in place.

Newcastle Strategic Solutions Limited (NSSL)

NSSL Board Members are:

Ron McCormick (NSSL Chairman), Phil Moorhouse, Nigel Wright (Non Executive Director only of NSSL) and Phil Grand (MD Savings and Mortgage Solutions).

The main responsibilities of NSSL, as delegated by the Society's main Board, are as follows:-

- To oversee the strategic direction of NSSL ensuring this is consistent with the Society's agreed strategy;
- To evaluate and monitor the financial and operational performance of NSSL against pre-determined objectives, which includes assessing performance in terms of sales performance, profitability, efficiencies, risk and compliance;
- Approval of new contracts where required under the Society's risk appetite and delegation of authorities;
- To ensure that NSSL complies with all relevant legislation and the appropriate regulations relating to its activities;
- To review NSSL's risk appetite statement on a regular basis;
- To ensure that an annual review of service resilience is conducted;
- To approve the NSSL budget on an annual basis (prior to inclusion in the Group budget which is approved by the main Board);
- To approve the NSSL statutory accounts;
- To consider and act upon the findings of internal and external audit reviews; and
- To ensure that a formal evaluation of the effectiveness of the NSSL Board is undertaken on an annual basis.

Relations with Members

Member engagement is at the heart of our strategy and the Society develops relationships with Members on a number of different levels. The first and most obvious is through the AGM voting process where we encourage Members, as owners of the business, to use their vote and we try to make this process as easy as possible.

Understanding what members think about our products and service is also extremely important. Members are encouraged to join our customer panel and we regularly consult with this group on a range of topics. We also use customer satisfaction surveys extensively and obtain feedback from different types of product holders and from customers who choose to deal with us through our main channels i.e. our branches, over the telephone, by post and via the internet. The information which is collected is used from these sources to help to develop and improve our offering.

Special Members' seminars are held on a regular basis and are designed to provide our customers with useful information to help them understand and make sense of what is becoming an increasingly uncertain financial world. These seminars provide an excellent opportunity not only to speak to our Members but also to interact and listen to their views. Periodically we also hold 'Meet the Chief Executive' events for members which provides an opportunity for Senior Management, including members of the Board, to engage with and listen to customer feedback.

Through our Corporate Social Responsibility (CSR) activities we are able to engage with both our Members and the communities we serve. Whether it is helping to raise money for local, worthy causes, or helping to develop financial education in local schools, we try hard to make a difference and improve the well being of people who live within our heartland. Further details of Member and Community Engagement are given in the Corporate Social Responsibility Report on page 14. We also keep in touch with Members via our Priority Register Service and on-line newsletter.

Board and Board Committee Membership Attendance Record

The table below sets out the number of meetings attended by Directors during 2014 with the number in brackets representing the maximum number of meetings the Director was eligible to attend.

Director	Board	Audit Committee	Group Risk Committee	Remuneration Committee	Nominations Committee	NSSL
Phil Moorhouse	**11** (11)	-	**9** (9)	-	**2** (2)	**6** (6)
Ron McCormick	**11** (11)	**4** (4)	**8** (9)	-	-	**5** (6)
Jim Willens	**11** (11)	-	-	-	-	-
Richard Bottomley	**4** (4)	**1** (1)	-	-	-	-
David Buffham	**11** (11)	-	**9** (9)	**3** (3)	**2** (2)	-
Patrick Ferguson	**10** (10)	-	-	-	-	-
Andrew Haigh	**11** (11)	-	-	-	-	-
Karen Ingham	**4** (4)	-	-	-	-	-
Richard Mayland	**9** (11)	**3** (4)	-	**3** (3)	**1** (2)	-
John Morris	**11** (11)	**4** (4)	-	**3** (3)	**2** (2)	-
Angela Russell	**11** (11)	-	-	-	-	-
Catherine Vine-Lott	**9** (11)	**3** (4)	-	**2** (3)	-	-
Ian Ward	**11** (11)	-	**9** (9)	-	-	-

Annual General Meeting (AGM)

The AGM provides an opportunity for members to question the Chairman, Chief Executive, Committee Chairmen and fellow Directors on the resolutions to be proposed at the meeting, the Annual Report and Accounts, and on any other aspect of the Society's business.

All members who are eligible to vote at the Annual General Meeting are encouraged to participate, either in person or by using their proxy voting form. The use of the online voting system is encouraged and for each vote placed online, the Society will be donating 30p to its Corporate Charity, which is Percy Hedley Foundation.

All votes are counted by independent scrutineers. As soon as practicable after the AGM, full details of the results of the voting are placed on the Society's website.

On behalf of the Board
Phil Moorhouse
24 February 2015

Audit Committee Report

Audit Committee

Members of Audit Committee at 31 December 2014 were:
Catherine Vine-Lott (Committee Chair), Richard Mayland, Ron McCormick, John Morris and Richard Bottomley. Subsequent to the year end Richard Mayland has retired from the Committee.

The Audit Committee's extensive experience and qualifications are detailed on pages 16 and 17 of the Annual Report and Accounts. Composition of the Committee meets the requirements of the UK corporate governance code for at least one member to have significant recent and relevant financial experience. The Committee members were selected for appointment by recommendation of the Nomination Committee in consultation with the Audit Committee Chairman.

Committee meetings:
The Committee meets at least four times each year coinciding with key dates in the Group's financial reporting calendar. A rolling schedule of items for discussion is agreed. Meetings are attended by Audit Committee members with attendance by invitation extended to the Internal Audit Executive, External Auditors, Chief Executive, Finance Director, Strategy Planning and Risk Director, Other Directors, and the Chairman of the Board. Other members of senior management are invited to attend at the request of the Audit Committee to update and report on relevant matters. For details of Committee meeting attendance see page 24 of the Annual Report and Accounts.

At least once a year the Audit Committee invites the Internal Audit Executive to meet the committee without senior management present. In addition, as well as a formal annual meeting, the Audit Committee has an opportunity to meet with the External Auditors, PricewaterhouseCoopers LLP (PwC), at each Audit Committee meeting, without senior management present. These meetings cover matters relating to its remit and any issues arising from audits, including matters required to be discussed by relevant law or regulation.

Key roles and responsibilities as delegated by the Board:
The main function of the Audit Committee is to assist the Board in fulfilling its oversight responsibilities, specifically the ongoing review, monitoring and assessment of:

- financial reporting;
- effectiveness of the internal control and risk management systems, including internal financial control
- internal audit; and
- external audit including re-appointment.

Further details are given below.

Financial reporting:
The Audit Committee's primary role regarding financial reporting is to monitor the integrity of the financial statements of the Group including the interim and annual reports, and any other formal announcements relating to the Group's financial performance. This responsibility is discharged though:

- review of interim announcements and Annual Report and Accounts, their clarity, completeness and compliance with relevant accounting standards and other regulatory and legal requirements;
- reporting to the board on the consistency and appropriateness of critical accounting policies and any changes thereto, taking into account the views of the external auditor;
- review and challenge of significant financial reporting judgements, estimates and the actions and judgements of management;
- advice to the board on whether the annual report and accounts, taken as a whole are fair, balanced and understandable and provides the information necessary for members to assess the performance, strategy and business model of the Group;
- review of any correspondence from regulators in relation to financial reporting; and
- review of the six monthly going concern assessment produced by the Finance Director.

The main areas of financial reporting significance considered by the Audit Committee in 2014 were as follows:

- Commercial and residential loan impairment provisions: This is inherently an area of accounting estimate and judgement. The Society's commercial loan impairment provisions are agreed by the Society's Provisioning Committee and then reported to the Audit Committee. The Audit Committee reviews the level of provisioning through detailed discussion with management on the key judgements and estimates made including triggers for and methodology behind impairment calculations. The Committee also considers the models used for production of residential provisions although the resulting provisions are small relative to commercial provisions. The impact of forbearance in the mortgage portfolios has been considered and appropriate disclosures made in the financial statements. The Committee is satisfied with the assumptions adopted and models used to calculate provisions over the residential and commercial mortgage books.
- Going Concern: Preparing the Annual Reports and Accounts under the Going Concern assumption requires the Board and Audit Committee to be satisfied about the long term viability of the Group's business operations, business planning, business management and risk management. Long term liquidity, capital and funding budgets and forecasts alongside capital, cash flow and business viability considerations are assessed formally at the half year and year-end to coincide with the approval of the interim and annual accounts. A balanced consideration of positive and negative plan aspects is considered with supporting narrative provided by the Group Finance Director. Based on this, the adoption of the Going Concern assumption to prepare the accounts is appropriate.
- FSCS levy provision and provisions for other liabilities and charges: The Audit Committee reviews and challenges the estimates and assumptions made by management when calculating provisions at the end of the reporting period. The Committee was satisfied with provisions in relation to legacy business areas and for potential consumer redress. In relation to the FSCS levy the committee also considered the impact of the final version of International Financial Reporting Interpretations Committee 21 on levies (IFRIC21) and the impact of its retrospective adoption on 1 January 2014, as detailed in Note 1 to the accounts on page 47.
- Hedge accounting: A complex area of accounting with a greater risk of error in application. The Audit Committee is appraised of the Group's derivative and hedge accounting position and strategy and also agrees the accounting policy for hedging, including disclosures in the Annual Report and Accounts. The Committee has concluded satisfactorily in this area.
- Taxation: Recovery of deferred tax assets is the main area of focus of the Committee and this is considered in conjunction with the review and approval of the Going Concern Review. The Committee was satisfied with the recovery of deferred tax assets. The Audit Committee review the Group Tax Risk Policy which sets out compliance with relevant jurisdictional legislation, identifying areas of tax risk for appropriate focus and managing the overall Group tax risk.
- Pension: Consideration of the assumptions and disclosures relating to the defined benefit pension scheme including the accounting treatment and calculation of the impact of any liability management exercises.
- The Committee considers matters raised by the External Auditors and the Committee concluded there were no adjustments required that were material to the Annual Report and Accounts.

Audit Committee Report (continued)

Having undertaken the above responsibilities and considerations throughout the Group's 2014 financial year the Audit Committee recommended to the Board that approval be given to the audited Annual Report and Accounts as at 31 December 2014.

Effectiveness of internal financial control

The Audit Committee works closely with the Group Risk Committee to ensure that management and staff take appropriate responsibility for departmental, business unit and subsidiary risk mitigation and internal control. The Audit Committee also reviews management and Internal Audit reports on the effectiveness of systems for internal control and risk management across the Group. Further details of risk management activities are given in the Risk Management report on pages 30 to 33 of the Annual Report and Accounts.

The Audit Committee is responsible for:

- review of the scope and effectiveness of the Group's internal controls and risk management systems including those for ensuring compliance with the regulatory environment in which the Group operates;
- review of the Society's procedures for detecting fraud and irregularities alongside review of the annual Money Laundering Reporting Officer's report;
- ensuring arrangements are in place by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting, control or other matters and to ensure independent investigation and appropriate follow up of such matters is undertaken; and
- reporting to the Board on significant findings concerning risk management, internal control, financial reporting and other aspects of relevance.

The Group's Internal Audit department forms a core component of the Group's risk management and internal control process. The Audit Committee is responsible for monitoring the effectiveness of the Group's Internal Audit function, its independence, objectivity and adherence with applicable professional standards. A formal review of the effectiveness of Internal Audit is undertaken by the Committee annually and an external review was completed in 2014 which concluded satisfactorily.

The Internal Audit department reflects the Audit Committee's primary available resource however the Committee retain the authority to obtain outside legal or independent professional advice as it sees fit. Reports from the Strategy Planning and Risk Director, Internal Audit, External Auditors and senior management provide input on key risks, uncertainties and controls direct to the Audit Committee.

The Committee also approves and reviews the Internal Audit work programme and results and ensures the Internal Audit department maintains sufficient access to the Board, management and the books and records of the Society. This oversight allows the Audit Committee to monitor and assess the role and effectiveness of the Internal Audit function in the overall context of the Group's Internal control framework and ensure appropriate management responsiveness to audit findings and recommendations given.

During the year the Audit Committee, through the Internal Audit department, completed a rolling review of the scope and effectiveness of the Group's internal controls. Specific areas of focus in 2014 included reviewing the controls in operation around residential lending, payroll, financial advice, cyber security, treasury, management information, complaints, governance, finance, fraud prevention, NSSL contracts and key projects. The Internal Audit department utilised KPMG LLP and Deloitte LLP for co-sourced internal audits to provide specialist expert input and promote knowledge transfer to the department.

External audit:

The Audit Committee is responsible for overseeing the Group's relationship with the External Auditors; PricewaterhouseCoopers LLP (PwC). This role extends to:

- appointment, reappointment, removal and assessment of independence, objectivity, effectiveness and remuneration of the External Auditors
- annual approval of the Society policy on the use of the External Auditors for non-audit work
- consideration of audit quality including reports by the Audit Quality Review Team

The Audit Committee assesses annually the qualification, expertise and resources of the External Auditors seeking reassurance that the auditors and their staff have no family, financial, employment, investment or business relationship with the Society that is considered to impact their independence. The External Auditors communicate their formal independence annually and appraise the Audit Committee of policies, processes and monitoring in place for maintaining their independence.

Prior to an External Audit engagement the Audit Committee discuss the nature and scope of the audit. They review findings of the auditors' work and assess the effectiveness of the audit process. This assessment reviews whether the auditor has met the agreed audit plan, considers the robustness and perceptiveness of the auditors in responding to questions from the Audit Committees and obtaining feedback about the conduct of the audit from key people involved.

The Audit Committee ensures that non-audit services provided by the External Auditors will not adversely impact the independence and objectivity of the audit firm in performing their duties. A formal Society policy on use of the External Auditors for non-audit work is reviewed annually encompassing pre-approved, low risk non-audit services alongside permitted and prohibited services requiring Audit Committee approval. During 2014 the External Auditors were engaged to provide advice in relation to corporate pensions, rates rebates, review of the effectiveness of Internal Audit, reporting on the Ceiling Trigger Notice and due diligence on loan collateral, by virtue of their expertise across these areas. With the exception of the latter two engagements which were carried out by the external audit team, the remaining work was carried out by PwC partners and staff that had no connection to the external audit team. The fees paid to the External Audit firm for audit and non-audit services are set out in Note 6 to the accounts.

PwC have been external auditors to the Group since 1994. A formal external audit tender process was undertaken in 2013 which followed a rigorous assessment process including the appointment of an audit selection panel comprising the Chairman of Audit Committee, The Society's Chairman, The Group Finance Director, The Group Financial Controller, the Chief Executive and one other member of the Audit Committee. Following submission of detailed proposals and a series of presentations a recommendation was made to Audit Committee and the Board to retain PwC as external auditors. The recommendation was made in light of a challenging and robust external audit and satisfaction with previous audits undertaken.

Directors' remuneration, including the members of the Audit Committee, is detailed within the Remuneration Committee Report on page 27 of the financial statements. The Report on Corporate Governance on pages 21 to 24 also sets out the process for review of effectiveness of Board sub-committees including the Audit Committee.

A full copy of the Terms of Reference for both the Audit Committee and Internal Audit can be viewed on the Society's website (www.newcastle.co.uk) under the Governance section.

On behalf of the Board
Catherine Vine-Lott
Chair of the Audit Committee
24 February 2015

Remuneration Committee Report

This report details the Society's approach to pay for the period 1st January to 31st December 2014. It sets out the remuneration policy and remuneration details for the Executive and Non-Executive Directors of the Society and how it applies the principles of the UK Corporate Governance Code relating to remuneration, the FCA Remuneration Code and the disclosure requirements arising under the EU Capital Requirements Directive IV (CRD IV).

The report is split into three main areas; the Statement by the Chair of the Remuneration Committee, the Report on Remuneration and the Directors' Remuneration Policy. All members eligible to vote at this year's Annual General Meeting will have the opportunity to approve the Directors' Remuneration Policy and the Directors' Remuneration Report through ordinary resolutions.

i) Statement by the Chair of the Remuneration Committee

The Remuneration Committee operates within the Terms of Reference (TOR) agreed by the Board. The TOR are reviewed annually and were last reviewed on 24th November 2014. The effectiveness of the committee is also reviewed on an annual basis and was last reviewed on 24th November 2014.

The main objectives of the committee are summarised as follows:

- To ensure compliance with the Regulators' Remuneration Code;
- To consider and make recommendations to the Board on executive remuneration and conditions of employment;
- Approval of the Society's Remuneration Policy Statement;
- Approval of Pillar 3 Remuneration disclosures; and
- To consider and make recommendations to the Board on the general framework of staff bonus schemes.

The Board believes remuneration should be sufficient to attract, retain and motivate senior managers to continue to run the Society successfully, whilst avoiding paying more than is necessary for this purpose.

The Remuneration Policy, therefore, focuses on rewarding our most senior executives in line with the achievement of our goals set out in the annual strategic plan whilst continuing to provide value for money for our members.

Composition of the Committee

The committee comprises solely of Non-Executive Directors who have no personal financial interest in the recommendations. The Chair of the Committee is Catherine Vine-Lott and the other members are Richard Mayland, David Buffham and John Morris. The Chairman and Chief Executive (except for items relating to his own remuneration) also attend meetings but are not members of the committee. The HR Executive acts as Secretary to the Committee.

During the year the Committee met three times and activities included:

- Reviewing the compliance of the Remuneration Policy against the requirements of the Regulators' Remuneration Code;
- Considering and agreeing pay and benefits for Executive Directors, senior managers and the Chairman, as well as overseeing remuneration matters across the Society and its subsidiaries;
- Reviewing the performance for the financial year and approving the resulting level of Corporate Bonus to be paid based on achievement of the Corporate Key Performance Indicators; and
- Consideration of the disclosure requirements for the Remuneration Report including Pillar 3 disclosures.

ii) Report on Remuneration

The total remuneration received by Directors is shown below. The information has been audited and shows remuneration for the years ended 31 December 2013 and 31 December 2014 as required under the Building Society (Accounts and Related Provisions) Regulations 1998.

Directors' Emoluments (Audited)

Emoluments of the Society's Directors from the Society and its subsidiaries are detailed below:

	Salary or fees	Annual bonus	Pension contributions to defined contribution scheme (Notes 1 & 2)	Other benefits	Total 2014 contractual benefits	2013 total
	£000	£000	£000	£000	£000	£000
Executive Directors						
JH Willens - notes 1, 3 and 5	300	9	-	40	349	297
AM Russell - notes 4 and 5	179	5	16	10	210	168
AS Haigh (appointed 27 January 2014) - note 2	140	5	-	22	167	-
P Ferguson (appointed 19 February 2014)	113	4	10	9	136	-
G Tiplady (made redundant 11 April 2013)	-	-	-	-	-	43
Total for Executive Directors	732	23	26	81	862	508
Non Executive Directors						
PJ Moorhouse	63	-	-	-	63	56
RJ Bottomley OBE (appointed 22 September 2014)	9	-	-	-	9	-
DJ Buffham	46	-	-	-	46	42
K Ingham (appointed 4 September 2014)	9	-	-	-	9	-
RD Mayland (retired 24 February 2015)	37	-	-	-	37	37
RJ McCormick	51	-	-	-	51	51
J Morris	37	-	-	-	37	37
CRR Vine-Lott	44	-	-	-	44	45
IW Ward (appointed 9 July 2013)	41	-	-	-	41	18
FD Holborn (retired 24 April 2013)	-	-	-	-	-	21
Total for Non Executive Directors	337	-	-	-	337	307
Total for all Directors	1,069	23	26	81	1,199	815

Notes:

1. Mr JH Willens has elected to take his pension contribution amounting to £27,000 as a cash payment, this is included in other benefits in the table above. He is liable for his own tax and national insurance contributions on this payment.
2. Mr AS Haigh has elected to take his pension contribution amounting to £12,635 as a cash payment, this is included in other benefits in the table above. He is liable for his own tax and national insurance contributions on this payment.
3. Mr JH Willens' salary was increased to £300,000 on 1 April 2013 and he declined to take the increase until 1 January 2014.
4. Mrs AM Russell's salary was increased to £170,000 on 1 April 2013 and she declined to take the increase until 1 January 2014. On 27 January 2014 her salary was increased to £180,000 following appointment to the additional role of Deputy CEO.
5. Mr JH Willens and Mrs AM Russell declined their bonus entitlement of 2.5% of salary due under the Corporate Bonus scheme in 2013.

The Chief Executive is the Society's most highly paid employee and no employee earns more than any Executive Director. The Chief Executive's salary was increased to £300,000 on 1 April 2013 and he declined to take this increase until 1 January 2014, having not taken a pay increase during his tenure as Chief Executive. The percentage increase in his total remuneration was 17.5% in 2014. The Chief Executive is also a Non-Executive Director of Brown Shipley & Co Limited and he retains the remuneration for this directorship as agreed by the Board.

iii) Directors' Remuneration Policy

The Society's Remuneration Policy is designed to provide competitive remuneration packages that attract, retain and reward our senior team, to deliver business objectives in support of the Society's strategy whilst providing value for members.

In implementing the Policy, the following key principles are observed:

- The Policy is clearly linked to our business strategy, objectives and values;
- Policy, process and practice are consistent with and promote effective risk management, whilst creating an acceptable relationship between risk and reward;
- Basic pay and total remuneration is set at a competitive level to attract and retain the appropriate calibre of people;
- Our approach to pay meets regulatory compliance and good corporate governance practice;
- Remuneration arrangements are transparent, consistent and fair, reflecting individual responsibilities and performance; and
- Remuneration arrangements are straightforward to understand, communicate and administer.

Remuneration for Executive Directors

The table below shows the elements of remuneration for Executive Directors and the way they operate.

How elements support our strategy	Operation	Maximum potential value	Performance conditions and assessment
Basic Salary Supports the recruitment and retention of Executive Directors, reflecting their individual roles, skills and contribution	Basic salary reflects the size of the role and responsibilities, individual performance (assessed annually) and the skills and experience of the individual. In setting appropriate salary levels, the Committee takes into account data for similar roles in comparable organisations. The Society aims to position Executive Directors competitively within the reference group.	Increases to base salary are determined annually by the Committee taking into account: • Individual performance • The scope of the role • Pay levels of comparable organisations • Pay increases elsewhere in the group	None applicable however individual performance is taken into account when considering base increases
Pension Supports recruitment and retention of Executive Directors at a cost that can be controlled by the Society.	Generally the Society contributes to a defined contribution pension scheme for the Executive Directors. The contribution can instead be paid in cash (which is excluded from bonus calculations) if the Executive Director is likely to be affected by the limits for tax approved pension saving.	9% of basic salary	None applicable
Benefits • To attract and retain Executive Directors • Provides a competitive level of benefits to assist Executive Directors to carry out their roles effectively	A number of benefits are provided to Executive Directors, including car or car allowance, private medical insurance, life insurance and permanent health insurance. The Committee reviews benefits and from time to time may make changes, for example to reflect market practice or the needs of the business.	The Society bears the cost of providing benefits which may vary from year to year.	None applicable
Short Term Incentive Scheme • Supports, attracts and retention of Executive Directors • Supports the development of a high performance culture • Rewards performance within the context of achieving corporate goals and objectives as set out in the corporate strategy	Performance measures and targets are set on an annual basis and are measured over the financial year. Payment is made in cash, after performance has been assessed. Payment is made at the discretion of the Committee.	The Committee determines the maximum incentive. A corporate bonus payment has been awarded of 3.0% of base salary in relation to 2014 performance.	The performance measures attached to the Corporate scheme are delivery of the Corporate KPIs which include: • Group profit, capital and liquidity targets • Quality measures around service, complaints and satisfaction • Targets for savings and mortgage business • Other KPIs covering people, Solutions business and delivery of major projects The measures are assessed by the Committee.

Notes to the table

As noted above, the Committee has complete discretion to make payment under the Corporate Bonus scheme and also has discretion to amend or remove the scheme where necessary to ensure the arrangements continue to meet the Committee's overriding remuneration principles.

Remuneration of Non-Executive Directors

The table below set outs the elements of Non-Executive Directors' remuneration and the policy on how each element is determined.

Element	Approach
Basic Fees	Reviewed annually based on time commitment and responsibility required by Board and Board committee meetings. Review takes into account fees paid by comparable financial services organisations. Fees set by the Remuneration Committee.
Additional Fees	Additional fees are payable for additional responsibilities such as committee chairmanship or membership.
Other items	Non-Executive Directors are not eligible to participate in any form of performance pay plans and do not receive pensions or other benefits.

The Remuneration Committee also determines the Chairman's fee.

Directors' service agreements and notice periods

Executive Directors are employed on service agreements which can be terminated by either the Society or the Director giving 6 months notice. Non-Executive Directors do not have service agreements. Non-Executive Directors are appointed for an initial three year term. They will generally be expected to serve more than one three year term.

Policy on termination pay

The Committee aims to treat departing Executive Directors fairly, taking into account the circumstances of their departure, but always careful to ensure that the interests of members are considered and that there are no rewards for failure.

Executive Directors are entitled to be paid their basic salary and contractual benefits (including pension contributions) during their notice period. The Society has the discretion to pay these as a lump sum in lieu of notice.

The rules of the Corporate Bonus scheme sets out treatment of award for individuals who cease to be an employee or Director of the Society.

Consideration of remuneration for individuals elsewhere in the Society

The Committee is responsible for setting the remuneration of the Executive Directors and approves the policy for senior managers who have material impact on the Society's risk profile (Code Staff).

In addition, the Committee reviews recommendations from the Chief Executive for approval of the remuneration of other executives.

When setting salary increases for Executive Directors, the Committee considers the level of salary increases across the Society.

All employees of the Society receive a basic salary and benefits consistent with market practice, and are eligible to participate in the Society's Corporate Bonus scheme and pension arrangements.

Consideration of member views

The Committee does not consult with the Society's members on its executive remuneration policy but takes into account feedback given by members. The Committee, has for a number of years, invited members to vote on the annual remuneration report, and members have always voted in favour. The Society has voluntarily elected to adopt some of the changes to remuneration reporting that apply to UK listed companies and one of the factors that the Committee took into consideration was the opportunity to give members a chance to vote on the Society's Remuneration Policy. The Committee believes this will give members an opportunity to indicate their support for the policy and the outcome of the vote will influence future policy development.

Summary of the Remuneration of Code Staff

A summary of the remuneration of Code Staff during 2014 and the business areas in which they operate is shown below.

Category	Typical Functions	Number in Category During the Year	Fixed Remuneration £000	Variable Remuneration £000	Total Remuneration 2014 £000	Total Remuneration 2013 £000
Executive Directors	CEO, Deputy CEO & Finance Director, Chief Operating Officer, Strategy Planning & Risk Director	4	839	23	862	508
Other Executives	Sales & Marketing, Treasury, Information Technology, Operations Human Resources, Commercial Services, Business Assurance	8	754	20	774	584
Control Functions	Compliance, Underwriting	2	114	2	116	308
Total		**14**	**1,707**	**45**	**1,752**	**1,400**

Catherine Vine-Lott
Chair of the Remuneration Committee
24 February 2015

Overview
The Society's risk management framework is designed to enable the Society to proactively identify and manage risks to support the achievement of the Society's objectives.

It includes monitoring and controlling the significant risks to which the Society is exposed to ensure the security and resilience of the Society. The Society's ability to identify, measure, monitor, report and control risks is key to delivering sustainable and resilient business performance, including fair outcomes for members and customers.

Risk Governance
The Board is ultimately responsible for ensuring that adequate systems of risk management are in place, and that the Society's strategy, risk appetite, and risk management are consistent. To assist the Board a Group Risk Committee (GRC) oversees the management of risk across the Group (see below).

The GRC is supported by an independent Group Risk department that is responsible for ensuring that appropriate risk management is used. This includes the provision of reports on risks, and risk management for the GRC and its sub-committees. The Society's Strategy Planning and Risk Director provides formal updates on risk management to the Board at least quarterly.

Risk Framework
The Society and Group risk management framework operates under the "three lines of defence" principle. The first line of defence is within departments, business units and subsidiaries where Executives, Managers and staff have responsibility for risk management and ensuring adequate controls are in place to mitigate risk. The second line of defence is provided by the GRC and supporting sub-committees together with oversight by the Group Risk department. The third line of defence is provided by Business Assurance and the Audit Committee, which are responsible for reviewing the effectiveness of the first and second lines of defence.

The risk framework includes the use of Board approved risk appetite statements covering profitability in a stressed scenario, capital, liquidity, operational risk, credit risk, interest rate risk, the fair treatment of customers and conduct risk, and IT risk. They set out key limits and escalation triggers. The risk appetite statements, together with the risk position, are reported to the Board quarterly, and formally approved annually.

The risk framework makes use of stress testing and scenario testing. Stress tests consider the potential outcomes for portfolios and for the Society in the event of stressed scenarios incorporating, for example, falling house prices and rising unemployment. Scenario tests consider the outcome in the event of a particular risk or event occurring, and are used to help evaluate the controls, and assess the adequacy of the Society's incident management and business continuity plans.

Group Risk Committee
The GRC oversees the Society's risk management and governance framework, and oversees the Society's overall risk profile. The Committee meets at least six times a year, and more frequently when required.

Members of the GRC throughout the year, all of whom were non-executive directors, were David Buffham (Committee Chairman), Ron McCormick, Phil Moorhouse, and Ian Ward.

The duties of GRC include:
- Oversight of overall risk appetite, risk management strategy and framework, including oversight of both prudential and conduct risk appetites;
- Oversight of compliance with risk policy;
- Oversight of the risk sub-committees (see below);
- Review and assessment of the adequacy of risk management information to monitor and control risks;
- Approval of new initiatives and projects, including the risks those initiatives and projects expose the Group to;
- Consideration and approval of the top risks for the Society and Group including low likelihood, high impact risks; and
- Approval of stress testing and scenario testing.

During 2014 the committee met nine times and in particular considered the following matters:
- Review of the risk appetites for prudential, and conduct risk;
- Oversight of the Internal Capital Adequacy Assessment Process, Individual Liquidity Adequacy Assessment, and annual stress testing report;
- Review and ratification of key risk policies covering lending, treasury, and operational risk;
- The application of the Prudential Regulation Authority's concurrent stress testing parameters and guidelines to the Group, and the results of that stress test; and
- Reviewed and agreed a statement of risk appetite covering customer outcomes and the fair treatment of customers and monitoring thereof, including the plan for compliance oversight.

The GRC is supported by four Executive committees that meet on a monthly basis, as follows:

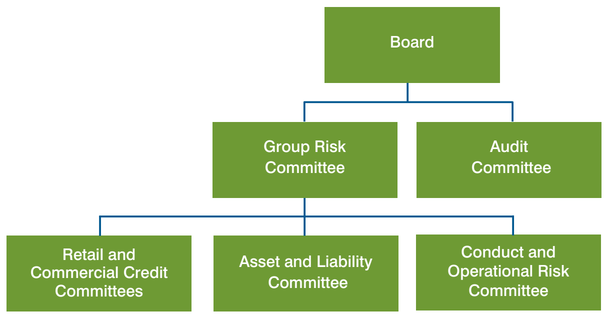
The Retail Credit Committee (RCC) is responsible for credit risk across the Group arising from the retail mortgage portfolio including lending policy, underwriting, limit setting and monitoring, forbearance, possessions, affordability, scorecard effectiveness and efficiency, and residential stress testing;

The Commercial Credit Committee (CCC) is responsible for credit and conduct risk across the Group's non-retail mortgage portfolio including loan strategy, limit monitoring, risk indicators and factors, annual reviews and breach reports, loan renegotiations and restructures, monitoring trends, and stress testing.

The Conduct and Operational Risk Committee (CORC) is responsible for operational and conduct risks arising across the Group, including operational risk policy, compliance policy, monitoring compliance with policies, risk event trends, actions on significant risk events, project risks, conduct risk indicators, business continuity policy, and scenario testing.

The Asset and Liability Committee (ALCO) is responsible for all aspects of treasury risk management including liquidity risk, interest rate risk, counterparty credit risk, and balance sheet management.

Risk Governance Structure



Risk and Impact	Mitigation	Change	Commentary
Credit Risk The primary credit risks are commercial, residential, and investment (see below).			
Commercial Commercial borrowers do not repay the Society and the Society's collateral is insufficient to meet the debt obligations. The risk is sensitive to economic conditions that can impact the viability of tenants and commercial real estate values.	The commercial loan book is being actively managed down. Commercial loans over £500k are subject to annual reviews reporting to the Commercial Credit Committee (CCC) or Risk and Recovery Committee (R&R) (depending on the size of the balance). Higher risk loans are subject to quarterly review. Concentration risk to single names and to sectors is monitored, In the event of a breach a report is provided to the CCC or R&R. Borrower and tenant watchlists are maintained by the Commercial credit risk team, and are reviewed monthly. Watchlists for borrowers and tenants are updated on a real time basis. Sector reviews are completed regularly. Where appropriate the Society uses property experts to provide it with options analyses. Stress testing is used to determine the risk associated with the portfolio and with individual loans within it.		The Society has withdrawn from new Commercial lending. Balances Fully Secured On Land have fallen by £74m (34.5%) in 2014, and now represent 7.2% of the mortgage book. The Society's exposure to single name risk has also materially reduced. Loans to registered social landlords (RSL) are subject to the same controls as commercial loans. However, the risk of default in relation to an RSL loan is extremely low. The assessment of risks has fallen significantly based on stress test losses.
Residential Retail borrowers do not repay the Society and the Society's collateral is insufficient to meet the debt obligations. The risk is sensitive to unemployment rates, house prices, and interest rates.	Loans are underwritten individually based on affordability, credit score and history, acceptable collateral (including loan to value), and the Society's lending criteria. The Society does not undertake sub-prime or self certification lending. The Society's lending policy is subject to review at least annually. The residential book is subject to monthly reporting in relation to its credit risk characteristics (including loan to value, loan to income, arrears, early delinquencies, and arrears arising from cohorts of lending). The Society's risk appetite is expressed in terms of losses arising in a stressed scenario, and stress testing is used to ensure that the portfolio is within the Society's risk appetite.		The Society has increased its lending to retail borrowers in 2014, and has a strategy to continue to do so. The Society's risk to residential lending has increased as the overall book has increased. Indexed LTV has reduced due to house price rises. Loans 3 months or more in arrears have fallen to their lowest reported level. The retail book remains within the Society's risk appetite.
Investment/Liquidity Credit The counterparties the Society invests liquid funds in default, or the value of the investment falls and the Society is obliged to crystallise that fall in value. The risk is sensitive to market volatility and credit spreads (both general credit spreads and name specific credit spreads).	Investments are subject to a GRC approved policy, which sets out what instruments, countries, and counterparties investments can be made in, and sets limits on exposures to instruments, countries, and counterparties. Investments are monitored and reported to management daily, and reported to the Assets and Liabilities Committee (ALCO) on a monthly basis, including compliance with the policy. The credit default swap rates for the Society's counterparties are monitored, and alerts raised if certain criteria are met in relation to those spreads. The mark to market value of the Society's investments in gilts, residential mortgage backed securities, and covered bonds are monitored daily and reported to ALCO monthly.		The Society's overall risk exposure has fallen as total liquidity has fallen, and the proportion of liquid assets held with highly rated counterparties has been maintained.

Risk and Impact	Mitigation	Change	Commentary
Conduct Risk Conduct risk is the risk of customer detriment arising from the Society's activities. Examples include products that do not perform as customers expected them to, or products being sold to customers for whom they are not suitable. Conduct risk and operational risk (see below) are closely aligned where the operational risk results in customer detriment (e.g. A failure to protect customer data is an operational risk which may result in customer detriment).	Conduct risk is wide-ranging, and the key mitigants are; The Society maintains a risk appetite statement relating to customer outcomes and measures performance relative to that statement monthly, reporting to the Conduct and Operational Risk Committee (CORC) with oversight from the GRC. All new products are approved by a Product Approval Committee, which includes consideration of an assessment of risks to customer outcomes. The Society maintains a Treating Customer Fairly dashboard, which looks at evidence supporting good customer outcomes (or suggesting poor outcomes) and this is reviewed quarterly and reported to the Board. The Society maintains an annual Compliance Plan, which is risk based, reporting to CORC with oversight from the GRC. (See also Operational Risk).	←	The Society has a simple product range covering mortgages, savings, insurance, and financial advice via Newcastle Financial Services Limited (an appointed representative of Openwork). The Society does not offer structured products, personal loans, protection payment products, or credit cards.
Liquidity Risk Liquidity risk is the risk of loss or failure caused by the Group being unable to meet its liabilities or commitments as they fall due, or to be able to do so only at excessive cost.	Liquidity is subject to a GRC approved Policy, which sets out limits in relation to liquidity. Liquidity is monitored and reported to management daily, and reported to the Assets and Liabilities Committee (ALCO) on a monthly basis, including compliance with the policy. Cashflow forecasts are used to forecast liquidity, and ensure compliance with the limits in the future. Stress tests are used to ensure that liquidity risk is within the risk appetite.	←	Whilst liquidity has reduced, the need for liquidity has reduced based on an assessment of the Society's funding maturity, and its access to funding, therefore overall liquidity risk is unchanged.
Interest Rate Risk Interest rate risk is the risk that the value of the Society's net assets or net interest income falls as a result of a change in interest rates. Basis risk is the risk that net interest income falls because of a change in the relationship between two market rates. For example, the Society has assets which earn interest based on the LIBOR rate, and liabilities where the rate is set by the Society .	Interest rate risk is subject to a GRC approved policy. Interest rate risk and basis risk are subject to policy limits, They are monitored and reported to ALCO monthly, including compliance with policy. The Society's uses interest rate swaps to manage interest rate risk. Derivatives are only used, in accordance with the Building Societies Act 1986, to mitigate risks arising from interest rates or indices. Forecasts are used to assess future compliance with limits and determine the need for management action. Stress tests are used to assess the Society's exposure to interest rate and basis risk.	←	The Society's policy in relation to interest rate risk has not been changed in the year nor has the overall interest rate risk to which the Society is exposed. Note 33 gives details of the derivative financial instruments held at 31 December 2014, together with the impact of a rate shock of 1% and 2%.

Risk and Impact	Mitigation	Change	Commentary
Pension Fund Obligation Risk The Group has funding obligations for a defined benefit scheme, which is closed to new entrants. It was closed to future benefit accrual with effect from 30 November 2010. Pension fund obligation risk is the risk that the value of the Scheme's assets, together with any agreed employer contributions, will be insufficient to cover the projected obligations of the Scheme over time. The return on assets, which includes equities and bonds, will vary with movements in equity prices and interest rates.	The pension fund is overseen by the Trustees of the Scheme, within an agreed Investment Strategy. Reports prepared by the Scheme's independent actuary are reviewed by the Trustees quarterly and, if appropriate, management action is taken. The Group performs stress testing on the pension scheme liabilities and assets at least annually. The Board received quarterly updates on the Society's Pension Scheme.	←	The Society undertook a Pension Increase Exchange (PIE) exercise in 2014, which reduced the risk associated with the pension scheme. However the savings generated by this exercise have been offset by adverse movements in markets arising mainly from a fall in long term gilt rates which has increased the value of the Scheme's liabilities.
Operational Risk Operational risk is the risk of loss, resulting from inadequate or failed internal processes, people and systems, or from external events. For the Group this definition includes legal risk, strategic risk and reputational risk.	Operational risk is subject to a GRC approved policy, which covers the framework for operational risk, including the measurement and management of risk, operational risk appetite, use of scenario testing for operational risk, tracking of risk events and operational losses, timescales for implementation of action plans and escalation procedures for more serious risk events that require immediate action to mitigate loss. Key risks and controls are identified for all areas of the business. Risk assessments remain the responsibility of the relevant departmental managers and Executives, and are updated regularly for new risks, the results of risk events and following internal audit reviews. Corporate Insurance policies are negotiated with regard to the key risks within the Group requiring greater mitigation.	←	As the Society's business model includes diversification via the Solutions Business, this increases exposure to operational risk particularly in relation to IT systems capability and human error. The Society implemented various projects in 2014 to enhance resilience. The overall size of the Solutions business was relatively static as set out in the segmental analysis in Note 9.
Capital Risk Capital risk is the risk that the Society is or becomes inadequately capitalised to address the risks to which it is exposed.	The Society updates its ICAAP on an annual basis. Capital adequacy is monitored on a monthly basis by the Board and the 3 year capital plan has been updated on a regular basis between ICAAP reviews against the background of changing economic circumstances. The Group maintains its capital at a level in excess of its Individual Capital Guidance. The Group publishes further information about risk exposures in its Pillar 3 disclosures, available on the Society's website (www.newcastle.co.uk) shortly after the publication of these accounts.	↓	The Society's Core Equity Tier 1 ratio has improved to 12.7% from 11.9%. As the Society attained the level of capital strength set out in the 2010 Capital Agreement in 2014 (12% Core Equity Tier 1 trigger), the convertible feature attached to certain of its PIBS and subordinated debt fell away. Further details are given in Note 27.

David Buffham
Chair - Group Risk Committee
24 February 2015

Report on the financial statements

Our opinion

In our opinion, Newcastle Building Society's Group Annual Accounts and Society Annual Accounts (the 'Annual Accounts'):

- give a true and fair view of the state of the Group's and of the Society's affairs as at 31 December 2014 and of the Group's and the Society's income and expenditure and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and, as regards the Group Annual Accounts, Article 4 of the IAS Regulation.

What we have audited

Newcastle Building Society's Annual Accounts comprise:

- the Group and Society Balance Sheets as at 31 December 2014;
- the Group and Society Income Statements and Statements of Comprehensive Income for the year then ended;
- the Group and Society Cash Flow Statements for the year then ended;
- the Group and Society Statements of Movement in Members' Interests for the year then ended; and
- the Notes to the Annual Accounts, which include a Summary of Significant Accounting Policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report and Accounts 2014 (the 'Annual Report'), rather than in the Notes to the Annual Accounts. These are cross-referenced from the Annual Accounts and are identified as audited. The financial reporting framework that has been applied in the preparation of the Annual Accounts is applicable law and IFRSs as adopted by the European Union.

Our audit approach

Overview

Materiality

- Overall Group materiality: £1,270,000 which represents 0.5% of net assets.

Audit scope

- We conducted all of our audit work from Newcastle upon Tyne using one team.
- Audit procedures were performed over all material account balances and financial information in the Society due to its significance to the Group's financial performance and position.
- Audit procedures were performed over specific account balances and financial information in 2 other Group undertakings that materially contributed to Group's financial performance and/or position.

Areas of focus

- Allowances for losses on loans and advances secured on commercial property.
- Accounting for the pension increase exchange.
- Valuation of derivative financial instruments and application of hedge accounting.
- The going concern assessment adopted in the preparation of the Annual Accounts.

The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)").

We designed our audit by determining materiality and assessing the risks of material misstatement in the Annual Accounts. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as "areas of focus" in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the Annual Accounts as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

Area of focus

Allowances for losses on loans and advances secured on commercial property/land

See Note 1 to the Annual Accounts for the Directors' disclosures of the related accounting policies, judgements and estimates and Notes 14 and 33 for detailed disclosures.

The Society has recognised an impairment charge on loans and advances to customers secured on commercial property/land of £7.7m in the year, leaving a balance of £170.8m on the balance sheet. This balance includes a specific provision of £18.5m and a collective provision of £3.6m for cases in the portfolio where an impairment event has occurred but has not been specifically identified. Whilst the Society has had success in its strategy of winding down this loan book over recent years, the portfolio remains significant both in the context of both the overall balance sheet and the results of the Group in the current and previous years.

Significant judgement needs to be applied by the Directors to estimate the potential loss on loans where an impairment event has occurred. Judgement is required in respect of identifying an impairment trigger event on loans and, once identified as impaired, the estimate of loss on a loan is calculated by use of models to discount the future cash flows expected to be received on the loan. This calculation is impacted by a number of assumptions which we focussed on, including, but not limited to:

- The value of the underlying security;
- Likelihood of re-letting where part/all of property remains vacant or tenancy agreements contain break clauses which pre-date the loan's maturity; and
- The exit strategy of the Society and, where this pre-dates the contractual maturity of the loan, the feasibility of delivering this strategy.

We also paid particular attention to the Director's assumptions in assessing the timing and value of future cash flows, as this is subject to significant estimation uncertainty and as a result there is an increased risk that impairment allowances may be materially understated.

How our audit addressed the area of focus

Specific provisions

We evaluated and challenged the Directors' future cash flow forecasts for loans where specific impairment allowances had been recognised, and the process by which they were drawn up. We tested the significant inputs in the models to underlying evidence, for example agreeing property values to valuations provided by external third parties and other details to tenancy agreements.

Where the Directors had obtained and relied upon third party property valuations, we obtained and read copies of these reports to check that the valuations were consistent with those applied in the Directors' cash flow models, and found no exceptions. We also independently assessed the competency of the external organisations contracted by the group to undertake these valuations, by confirming they held appropriate RICS qualifications as well as their objectivity. We did not identify any issues with the valuation assumptions used by these external organisations and considered them to be reasonable in light of our own independent assessment of applicable assumptions.

Our work on the cash flow forecasts also involved assessing the reasonableness of the assumptions used (as described) to derive the expected future cash flows. We also undertook sensitivity analyses to assess the changes required in those assumptions that would be required to result in material misstatement of the allowances, and the likelihood of such changes arising individually and in aggregate. We identified a small number of loans (which were already identified by management as impaired), which in our view required an increased provision allowance. Whilst these were not material they were discussed with management and increased allowances were recorded in the Annual Accounts.

We evaluated the outcome of commercial loans redeemed in the year by comparing these to management's previously expected outcome to ascertain whether losses realised were consistent with previously recorded provision allowances. Where additional losses arose, we noted that these were the result of the accelerated wind-down of specific accounts by the Directors during the year, and not the result of events or matters which existed and that should have been factored into provision allowances at the date of the previous accounts.

Completeness of provision allowances and the collective provision

The appropriateness of the collective provision of £3.6m was assessed through reading management's related accounting paper and utilising the evidence we had obtained from the procedures outlined above against the impairment criteria defined in accounting standards. We did not identify any material error in the collective provision based on the evidence obtained from those procedures.

In evaluating the completeness of specific impairment provision allowances on commercial loans and the appropriateness of the collective provision, we:

- Re-performed controls relied upon by the Directors to address accurate capture of arrears information, including testing over the allocation of cash receipts from borrowers to the correct loan accounts and recalculation of arrears for a sample of borrowers;
- Obtained "watch lists" representing borrowers being closely monitored by the Commercial Credit Committee and minutes of the committee's meetings to identify any loans of higher risk and we investigated the past performance of these loans to assess if an impairment event had occurred and the likelihood of loss in the event of default;
- Identified specific commercial loans which had not been assessed by the Directors as impaired but in our view represented a heightened risk of potential impairment, including loans with significant balances outstanding at the balance sheet date, with high Loan to Values (LTVs) and loans in arrears or where forbearance had been granted and again investigated the past performance of these loans to assess whether an impairment event had occurred and the likelihood of loss in the event of default;

Following completion of the above procedures, we did not identify any errors in the capturing and recording of arrears information and we did not identify any loans recorded on the watch lists or identified as higher risk through use of our own selection criteria for which we considered there to be evidence of a need for a specific provision.

Area of focus

Valuation of defined benefit pension scheme liabilities - accounting for the Pension Increase Exchange undertaken in the year

See Note 1 to the Annual Accounts for the Directors' disclosures of the related accounting policies and Note 31 for detailed disclosures.

During the year the Society undertook a liability management exercise in respect of its defined benefit pension scheme obligations. Under the exercise existing pensioners in the defined benefit plan were offered the option of receiving higher immediate pensions in exchange for forgoing future increases. This exercise is referred to throughout these Annual Accounts as the Pension increase exchange (PIE).

Following the conclusion of the PIE, income of £2.6m has been recognised in the Group and Society income statements to reflect the reduction in discounted total value of the pension scheme obligations payable by the Society.

Within this income figure is the estimated reduction in the value of scheme obligations arising from existing pensioners who have taken up the PIE offer and the estimated take-up from deferred scheme members yet to retire, who will be offered the same option when they are eligible to retire.

We focused the estimation of the reduction in scheme obligations arising from the PIE, which requires significant judgement, particularly in estimation of the future take up rate by deferred scheme members. The calculations required are performed by an external firm of actuaries, are complex, not routine and the impact on the income statements is material.

As a non-recurring exercise, we also focused on the disclosures of the impact of this transaction in the accounts as the risk that this may be inappropriately presented.

How our audit addressed the area of focus

We obtained the detailed breakdown of members in the scheme who took up the PIE during the year and, through testing on a sample basis, noted that this breakdown matched that which was provided to the external actuaries engaged by the Society to calculate the financial impact in the income statement.

We independently re-performed the calculation of the reduction in scheme liabilities for these members using our own internally developed benchmarks for the significant actuarial assumptions (including an appropriate discount rate) in addition to agreeing the increase in pension payments in this calculation to the increase stipulated in the offer accepted by these members. We did not identify a reportable difference between our recalculated figure and that recorded in the Annual Accounts by the Directors.

In calculating the total financial impact in the accounts, the Directors were required to estimate the assumed take-up rate for deferred members who will be eligible to accept the terms of the PIE upon retirement. In challenging this assumption, we noted that the Directors had applied an assumed take-up rate which was comparable with the known take-up rate from existing pensioners in the scheme and this in our view was a reasonable basis for this estimate for the accounts.

We evaluated, with reference to accounting standards, the presentation of the reduction in the fair value of scheme liabilities attributable to the PIE being taken entirely through the income statement and notes to the accounts as a past service cost. We found the treatment and presentation adopted in these accounts to be consistent with the accounting requirements.

Area of focus

Valuation of derivative financial instruments and application of hedge accounting

See Note 1 to the Annual Accounts for the Directors' disclosures of the related accounting policies and Note 33 for detailed disclosures.

The Society's operations expose the Group to significant interest rate risk, as a result of a mismatch between fixed and floating cash inflows and outflows to and from members, from investments or to providers of funds.

The Directors have sought to mitigate the risk of future movements in market interest rates affecting the Group's profitability through the use of a number of derivative financial instruments, mainly in the form of interest rate swaps. The Group has designated a number of these derivatives as accounting hedges, in accordance with accounting standards to reduce the volatility of future movements in interest rates on the amounts recorded in the income statement.

The Group has a significant number of derivative instruments and uses valuation systems and, in some instances, valuations provided by counterparties to the contracts to determine the fair value of each instrument at the balance sheet date. The Group also uses systems and in some cases bespoke cash flow models to assess hedge effectiveness for the accounting hedges as required by accounting standards.

We focused on this area as there are a larger number of instruments that require valuations, and these require judgement. The process of recording the valuations in the accounting records requires manual input and the criteria for achieving hedge accounting are onerous and complex, both of which increase the risk of error in application. In particular we focused on:

- the interest yield curves and discount rates applied in the Society's valuation systems and/or counterparty valuations; and
- the Society's hedge documentation and calculation spreadsheets used to calculate ineffectiveness in hedge relationships.

How our audit addressed the area of focus

We agreed fair values derived for each derivative financial instrument by management to the values recorded in the financial statements.

We obtained a sample of derivative contracts and undertook independent valuations for these instruments at the balance sheet date using our own models. Within our models we used externally available sources for interest yield curves and discount rates for the Group, in arriving at our own independent estimates of fair value.

We compared our independently determined fair values to those calculated by management for the same instruments, (whether through the use of valuation systems or those provided by counterparties) to evaluate any differences arising. In performing this comparison we calculated tolerable thresholds for valuation differences which took into account the complexity of the instrument being valued. We noted no differences outside of those tolerable thresholds.

We obtained and read the Group's hedging documentation to evaluate whether this documentation was compliant with the accounting requirements for applying hedge accounting and found no issues.

We also obtained and re-performed the hedge effectiveness calculations undertaken by management in assessing the effectiveness of the Group's hedge relationships. In performing this work we also recalculated the ineffectiveness recorded in the income statement within the 'Gains less losses on financial instruments and hedge accounting" line. In performance of these procedures we noted no differences to the effectiveness as calculated by the Directors and recorded in the accounts.

Area of focus

The going concern assessment adopted in the preparation of the Annual Accounts

See Note 1 to the Annual Accounts for the Directors' disclosures of the rationale for preparing the accounts on a going concern basis and the Strategic Report for detailed Capital disclosures.

We identified that the most significant assumption to assessing the Group and Society's ability to continue as a going concern was the expected future profitability of the Society, as the key determinant of the forecast capital position.

The capital position of the Group and the Society has continued to improve in recent years, with the Society's Core Equity Tier 1 capital at 12.7% at the balance sheet date compared to 11.9% at 31 December 2013 and 10.7% at 31 December 2012. In addition, the forecasts prepared by the Directors, and approved by the Board and the Audit Committee, contain an expectation that the Group and Society will maintain capital and liquidity levels with significant headroom over minimum levels prescribed by the Prudential Regulation Authority (PRA), which provides for a 'buffer' above the minimum levels prescribed by European regulations.

However, the calculations require adjustment to accounting figures to reflect regulatory requirements stipulated by the Basel Committee frameworks, are based on estimates of future performance and are fundamental to assessing the suitability of the basis adopted for the preparation of the accounts. We have therefore spent significant audit effort, including the time of senior members of our audit team in assessing the suitability of this assumption being applied.

How our audit addressed the area of focus

We obtained the board approved forecasts for the Group and Society and confirmed, prior to undertaking detailed audit procedures, that:

- they did not show an expectation of the Group and/or Society breaching minimum regulatory capital and liquidity levels prescribed by the PRA over the forecast period; and
- the period covered by the forecasts were sufficient in duration, in our view, for the Directors to be able to form an adequate view of the going concern position of the Group and Society.

We noted that the forecasts used by the Directors extend significantly beyond a 12 month period from the date of the financial statements and demonstrates that the Director's expect that the Group and Society would operate above the individually assessed regulatory minimums throughout the duration of this period.

We assessed the reasonableness of the forecasted profits for the Society through a number of procedures including:

- Comparison of future expected growth rates in interest and other income with previously observed growth rates and comparison of net interest margins to past performance and noting that for 2015 these were consistent with past performance;
- Obtaining and reading of contracts which underlie expected income growth in future years within the Solutions business to independently assess assumptions about how robust and predictable this growth is likely to be; and
- Assessing estimates for significant forecast expenditures against past performance, for example FSCS levies and impairment charges on loans and advances to customers.

We also assessed whether the forecasts accounted for known and predictable cash flows that would affect the future funding position of the Group and Society, for example contractually due repayments of subordinated notes. We noted no omissions of this nature in the forecasts, based on our knowledge from other audit procedures and understanding of the Group.

In undertaking the above, we performed sensitivity analyses using our own independently derived assumptions to assess the change required to eliminate the headroom in the forecasts above the minimum capital requirements. We then assessed the likelihood of these alternative scenarios, noting no reasonable likely scenario that would cast doubt on the ability of the Society to maintain its capital position over the forecast period.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the Annual Accounts as a whole, taking into account the geographic structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

Substantially all of the Group's activities are in the United Kingdom and it reports its operating results along two business lines, being the 'Member business' and the 'Solutions business' (refer to Note 9 of the Annual Accounts).

The Group is also comprised of a number of legal entities, but the majority of the Member business and Solutions business is undertaken by, and recorded within, the accounting records of the Society. Significant activity in these business lines recorded in other Group entities include:

- The provision of financial advice to customers, reported as a Member business activity, undertaken by a subsidiary undertaking of the Society, Newcastle Financial Services Limited (NFSL); and
- The provision of managed IT services, a Solutions business activity, undertaken by another subsidiary undertaking of the Society, Newton Facilities Management Limited (NFML).

Certain Group assets reside in other entities, including material leasehold land and buildings held within a subsidiary undertaking, Newcastle Portland House Limited (NPHL).

Accordingly, due to majority of the 'Member business' and the 'Solutions business' being conducted by the Society, and the financial significance of this to the Group Annual Accounts, we performed an audit of all material account balances and other financial information for the Society, together with the assessment of management's going concern assumption.

We also determined it necessary to perform specific audit procedures over account balances and other financial information in certain subsidiary undertakings where such entities significantly contributed to the amount recorded in the Group Annual Accounts. As a result, we performed audit procedures on Fee and commission income recorded in NFSL and Leasehold land and buildings recorded in NPHL. No specific audit procedures were deemed necessary on the account balances and other financial information in NFML, as the entity did not contribute materially to the Group's financial performance or position.

The accounting records and functions for the Society and its subsidiary undertakings are all located at the Society's principal office in Newcastle upon Tyne, with the consolidation of the Group Annual Accounts performed centrally from this location. All audit work was undertaken by a single audit team at this location.

Taken together, our audit procedures on the Society and its subsidiary undertakings provided us with sufficient audit evidence as a basis for our opinion on the Group Annual Accounts as a whole.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the Annual Accounts as a whole.

Based on our professional judgement, we determined materiality for the Annual Accounts as a whole as follows:

Overall group materiality	£1,270,000 (2013: £1,274,000)
How we determined it	0.5% of Net assets
Rationale for benchmark applied	We have applied this benchmark, a generally accepted auditing practice for building society audits, in the absence of indicators that an alternative benchmark would be appropriate and because we believe this provides an appropriate and consistent year on year basis for determining materiality for our audit.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £63,500 (2013: £63,700) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Opinion on other matters prescribed by the Buildings Societies Act 1986

In our opinion:

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

Other matters on which we are required to report by exception

Propriety of accounting records and information and explanations received

Under the Building Societies Act 1986 we are required to report to you if, in our opinion:

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

We have no exceptions to report arising from this responsibility.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the Directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 20, the Directors are responsible for the preparation of the Annual Accounts and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the Annual Accounts in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Society's members as a body in accordance with Section 78 of the Building Societies Act 1986 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of Annual Accounts involves

An audit involves obtaining evidence about the amounts and disclosures in the Annual Accounts sufficient to give reasonable assurance that the Annual Accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the Group's and the Society's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the Annual Accounts.

We primarily focus our work in these areas by assessing the Directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the Annual Accounts.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report and Accounts 2014 to identify material inconsistencies with the audited Annual Accounts and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Karyn Lamont (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Newcastle upon Tyne
24 February 2015

Income Statements for the year ended 31 December 2014

	Note	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Interest receivable and similar income	2	85.3	95.0	85.3	95.2
Interest payable and similar charges	3	(60.2)	(71.6)	(60.2)	(71.6)
Net interest income		25.1	23.4	25.1	23.6
Other income	4	24.0	26.1	20.8	22.9
Other charges	4	(1.7)	(1.4)	(1.7)	(1.4)
Gains less losses on financial instruments and hedge accounting		-	0.5	-	0.5
Loss recognised on revaluation of investment properties held for sale	18	-	(1.1)	-	-
Income from shares in subsidiary undertakings	5	-	-	-	3.1
Total operating income		47.4	47.5	44.2	48.7
Administrative expenses	6	(33.2)	(34.6)	(31.3)	(32.7)
Depreciation	17	(1.8)	(2.3)	(1.6)	(2.0)
Operating profit before impairments, provisions, FSCS levy and exceptional items		12.4	10.6	11.3	14.0
Impairment credit on loans and advances to banks	11	-	0.8	-	0.8
Impairment charges on loans and advances to customers	14	(5.9)	(6.7)	(5.9)	(6.7)
Impairment of loans to subsidiary undertakings	16	-	-	-	(3.2)
Provision for liabilities and charges	26	(2.5)	(4.0)	(2.5)	(4.0)
Gain on disposal of Prepaid Cards Business	10	-	0.6	-	0.6
Profit for the year before taxation		4.0	1.3	2.9	1.5
Taxation expense	8	(1.1)	(1.8)	(1.5)	(1.6)
Profit / (loss) after taxation for the financial year		2.9	(0.5)	1.4	(0.1)

The notes on pages 44 to 78 form part of these Accounts.

Statements of Comprehensive Income for the year ended 31 December 2014

	Note	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Profit / (loss) for the financial year		2.9	(0.5)	1.4	(0.1)
Other comprehensive (expense) / income:					
Items that may be reclassified to income statement					
Movement on available for sale reserve		(1.3)	(7.0)	(1.3)	(7.0)
Income tax on items that may be reclassified to income statement		0.3	1.3	0.3	1.3
Total items that may be reclassified to income statement		(1.0)	(5.7)	(1.0)	(5.7)
Items that may not be reclassified to income statement					
Actuarial remeasurements on retirement benefit obligations	31	(6.0)	2.1	(6.0)	2.1
Income tax on items that will not be reclassified to income statement	19	1.2	(0.6)	1.2	(0.6)
Total items that will not be reclassified to income statement		(4.8)	1.5	(4.8)	1.5
Total other comprehensive expense		(5.8)	(4.2)	(5.8)	(4.2)
Total comprehensive expense for the financial year		(2.9)	(4.7)	(4.4)	(4.3)

The notes on pages 44 to 78 form part of these Accounts.

Balance Sheets at 31 December 2014

	Note	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
ASSETS					
Cash and balances with the Bank of England		**310.6**	297.0	**310.6**	297.0
Loans and advances to banks	11	**203.9**	113.2	**203.8**	112.9
Debt securities	12	**253.6**	477.3	**253.6**	477.3
Derivative financial instruments	33	**16.4**	32.0	**16.4**	32.0
Loans and advances to customers	14	**2,660.1**	2,700.7	**2,649.2**	2,687.2
Fair value adjustments for hedged risk	15	**201.8**	120.9	**201.8**	120.9
Assets pledged as collateral	13	**48.5**	-	**48.5**	-
Investment in subsidiary undertakings	16	**-**	-	**16.0**	23.2
Property, plant and equipment	17	**23.0**	21.4	**15.0**	13.2
Investment properties held for sale	18	**-**	4.3	**-**	-
Deferred tax assets	19	**9.8**	9.4	**10.3**	9.7
Other assets	20	**8.5**	11.0	**15.6**	20.8
TOTAL ASSETS		**3,736.2**	3,787.2	**3,740.8**	3,794.2

The notes on pages 44 to 78 form part of these Accounts.

Balance Sheets at 31 December 2014

	Note	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
LIABILITIES					
Due to Members	21	**2,973.7**	3,235.2	**2,973.7**	3,235.2
Fair value adjustments for hedged risk	15	**8.4**	15.6	**8.4**	15.6
Due to other customers	22	**164.9**	122.7	**165.0**	122.8
Deposits from banks	23	**113.6**	11.4	**113.6**	11.4
Debt securities in issue	24	**1.0**	7.5	**1.0**	7.5
Derivative financial instruments	33	**201.6**	120.9	**201.6**	120.9
Other liabilities	25	**10.6**	10.6	**15.0**	15.9
Provisions for liabilities and charges	26	**3.1**	3.5	**3.1**	3.5
Retirement benefit obligations	31	**3.7**	2.0	**3.7**	2.0
Subordinated liabilities	27	**59.5**	59.0	**59.5**	59.0
Subscribed capital	28	**29.9**	29.7	**29.9**	29.7
Reserves		**166.2**	169.1	**166.3**	170.7
TOTAL LIABILITIES		**3,736.2**	3,787.2	**3,740.8**	3,794.2

These Accounts were approved by the Board of Directors on 24 February 2015 and signed on its behalf by:

Phil Moorhouse, Chairman
Catherine Vine-Lott, Chairman of Audit Committee
Jim Willens, Chief Executive

The notes on pages 44 to 78 form part of these Accounts.

Statements of Movement in Members' Interests for the year ended 31 December 2014

GROUP	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2014	168.5	0.6	169.1
Movement in the year	(1.9)	(1.0)	(2.9)
At 31 December 2014	**166.6**	**(0.4)**	**166.2**

Restated	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2013	167.5	6.3	173.8
Movement in the year	1.0	(5.7)	(4.7)
At 31 December 2013	**168.5**	**0.6**	**169.1**

SOCIETY	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2014	170.1	0.6	170.7
Movement in the year	(3.4)	(1.0)	(4.4)
At 31 December 2014	**166.7**	**(0.4)**	**166.3**

Restated	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2013	168.7	6.3	175.0
Movement in the year	1.4	(5.7)	(4.3)
At 31 December 2013	**170.1**	**0.6**	**170.7**

Movement in the year reflects changes disclosed in the Statements of Comprehensive Income, net of tax.

Opening reserves at 1 January 2013 have been restated as a result of the Group's adoption of IFRIC 21 Government Levies. Note 1 includes more detail on the restatement.

The notes on pages 44 to 78 form part of these Accounts.

Cash Flow Statements for the year ended 31 December 2014

	Note	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Cash outflows from operating activities	29	**(57.7)**	(257.1)	**(60.4)**	(267.1)
Payment into defined benefit pension scheme		**(2.0)**	(2.2)	**(2.0)**	(2.2)
Net cash outflows from operating activities		**(59.7)**	(259.3)	**(62.4)**	(269.3)
Cash (outflows) / inflows from investing activities					
Purchase of property, plant and equipment		**(3.5)**	(0.6)	**(3.5)**	(0.6)
Sale of investment properties		**4.3**	8.6	**-**	-
Sale of property, plant and equipment		**-**	0.1	**-**	-
Decrease in loans to subsidiary undertakings		**-**	-	**7.2**	18.5
Purchase of investment securities		**(234.4)**	(625.5)	**(234.4)**	(625.5)
Sale and maturity of investment securities		**405.0**	766.0	**405.0**	766.0
Net cash inflows from investing activities		**171.4**	148.6	**174.3**	158.4
Net cash outflows from financing activities					
Interest paid on subordinated liabilities		**(3.6)**	(3.4)	**(3.6)**	(3.4)
Interest paid on subscribed capital		**(3.8)**	(3.6)	**(3.8)**	(3.6)
Repayments under finance lease agreements		**(0.1)**	(0.1)	**(0.1)**	(0.1)
Net cash outflows from financing activities		**(7.5)**	(7.1)	**(7.5)**	(7.1)
Net increase / (decrease) in cash		**104.2**	(117.8)	**104.4**	(118.0)
Cash and cash equivalents at start of year		**410.2**	528.0	**409.9**	527.9
Cash and cash equivalents at end of year	29	**514.4**	410.2	**514.3**	409.9

The notes on pages 44 to 78 form part of these Accounts.

1 Significant Accounting Policies

Basis of Preparation
The Annual Accounts have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC); as adopted for use in the EU; and with those parts of the Building Societies (Accounts and Related Provisions) 1998 applicable to building societies reporting under IFRS.

The Board has reviewed medium and long term plans with particular emphasis on examining forecast liquidity, capital and profitability of the Group and the risks to those forecasts through a variety of stress testing scenarios. The outcome of this review is that the Directors are satisfied that the Society and the Group have adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements of the Society and the Group have been prepared on a going concern basis.

The Annual Accounts have been prepared under the historical cost convention except for those financial assets and hedging instruments which are required by IAS 39 to be carried at fair value. A summary of the Group's principal accounting policies is set out below:

Basis of Consolidation
The Group Accounts include the results of the Society and its subsidiary undertakings, all of which have accounting periods ending 31 December. Subsidiaries are entities over which the Society has the power to control the financial and operating policies so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that control ceases. Upon consolidation, inter-company transactions, balances and unrealised gains on transactions are eliminated. The accounting policies of subsidiaries are consistent with Group accounting policies.

Income Recognition
Interest Income and Expense
Interest receivable and interest payable for all interest-bearing financial instruments are recognised within 'Interest receivable and similar income' and 'Interest payable and similar charges' in the consolidated income statements, using the effective interest rate method (EIRM).

EIRM is used to calculate the amortised cost of financial instruments and to recognise interest receivable or payable over the relevant period. The effective interest rate is the rate that exactly discounts estimated cash flows (excluding credit losses) to zero, through the expected life of the instrument. In calculating the effective interest rate all contractual terms of the financial instrument (for example, early redemption charges) are taken into account.

Fees and Commissions
Fees and commissions relating to creating loans and advances to customers are deferred and spread as 'interest receivable', using the EIRM. Other fees and commissions are recognised as 'Other income' on the accruals basis as services are provided.

Dividend Income
Dividends receivable are recognised in the Income statements in 'Dividend income' when the right to receive payment is established.

Financial Assets
In accordance with IAS 39, Financial Instruments: Recognition and Measurement, the Group classifies its financial assets into the following categories:

Loans and Receivables
The Group's mortgage assets and similar loans are classified as loans and receivables and measured at amortised cost using EIRM. In accordance with EIRM, incremental up-front costs and fees receivable which are directly related to the loans (including administration and completion fees, arrangement fees, procuration fees and commissions paid to agents) are deferred and released to income over the effective life of the mortgage assets. Historical and forecast mortgage redemption data and management judgement are used to estimate the expected lives of mortgage assets.

The Group holds equity release mortgage assets on the Balance Sheet for which a limited portion contains no-negative-equity guarantees. The guarantees meet the IFRS 4 criteria for classification as insurance contracts. Income on the equity release mortgage assets is recognised in line with the Group's disclosed loans and receivables accounting policy. The Group performs liability adequacy testing on its insurance liabilities to ensure that the carrying amount of liabilities is sufficient to cover current estimates of future cash flows. At 31 December 2014 the insurance component of the Group Equity Release assets is wholly immaterial.

At Fair Value through Profit and Loss
The Group enters into derivative financial instruments to hedge its exposures relating to interest rates, index risk relating to savings products (equities, house prices and inflation) and longevity risk on equity release mortgages. At the balance sheet date the Group has entered into contracts which lead to derivatives designated as either fair value hedges or cash flow hedges in accordance with the risks that the hedges have been set up to mitigate. In accordance with the Treasury Policy Statement and the Building Societies Act 1986 the Group does not hold or issue derivative financial instruments for trading purposes.

In accordance with IAS 39, all derivative financial instruments (both assets and liabilities) are initially and on an ongoing basis, assessed to determine whether they are highly effective in offsetting the changes in fair value of hedged items. Derivatives are recognised at fair value on the date the derivative contract is entered into, and subsequently re-measured at their fair value with changes going through the Income Statements along with changes in fair value attributable to the hedged risk of the hedged items.

The carrying value of the hedged item is included on the balance sheet under the heading "Fair value adjustments for hedged risk". Any gain or loss arising from an ineffective portion is recognised immediately in the Income Statements under the heading "Gains less losses on financial instruments and hedge accounting".

When a hedging instrument expires, is sold, or no longer meets the criteria for hedge accounting, then hedge accounting is discontinued and any cumulative gain or loss is recognised in the Income Statements.

Available for Sale
These assets are non-derivative financial instruments where the intention is to hold for an indefinite period of time. They are initially measured at fair value, with subsequent fair value movements recognised directly in Members' Interests, until the asset is derecognised or impaired, at which point the cumulative gain or loss previously recognised in Members' Interests is recognised in the Income Statements. Interest received on the asset is recognised immediately in the Income Statements.

Significant Accounting Policies Continued

Held to Maturity
These are non-derivative financial assets with fixed maturities that the Group has a positive intention and ability to hold until maturity. Held to maturity investments are initially recognised at fair value and are subsequently measured at amortised cost using the effective interest rate method. Interest on held to maturity investments is included in the Income Statements and reported as interest receivable and similar income. At 31 December 2014 the Group held no financial assets designated as held to maturity.

Cash and Cash Equivalents
For the purpose of the Cash Flow Statements, 'Cash and cash equivalents' comprises cash in hand, balances with the Bank of England, loans and advances to banks available on demand or with original maturities of three months or less and investment securities with a maturity period of three months or less i.e. highly liquid assets readily convertible into cash.

Impairment of Financial Assets
Individual assessments are made against all those known loans and advances in arrears, in possession, where an event of default has occurred, where fraud has been identified or where any other potential loan servicing issues arising from assessments or professional advice are known. The value of those loans and advances that are considered to be impaired is reduced on an individual basis. Impairment calculations are carried out by considering future discounted cash flows as per rules laid out in international accounting standard, IAS39. In considering future cash flows the Society estimates the future valuation of the security less anticipated disposal costs, any irrecoverable hedging costs, and other payments and charges, which are then discounted using the original effective interest rate based on the Groups approved strategy for the loan at the balance sheet date. Collective impairment allowances are also made to reduce the value of those loans and advances where there has been an event which may give rise to impairment but of which the Society is not yet aware at the balance sheet date, with the result that the amount advanced may not be recovered in full. For the purposes of the collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Any impairment loss or allowance is recognised in the Income Statements.

Loans are classed as renegotiated when their terms have changed during the year. The Group applies a policy of capitalising arrears on residential loans with the customer's agreement, once the customer has made six contractual monthly mortgage repayments following the instance of non-payments. Capitalisation is only applied where there is no realistic alternative and this is expected to be of long-term benefit to the borrower.

Financial Liabilities
All financial liabilities are initially measured at fair value, being the issue proceeds, net of premia, discounts and transaction costs incurred. Derivative financial liabilities remain accounted for at fair value on the balance sheet date. Hedged risk and capital protection bond fair value adjustments are also held on the balance sheet at fair value. The remaining Group financial liabilities including shares, deposits, debt securities, subordinated liabilities and Permanent Interest Bearing Shares are subsequently measured at amortised cost, using the EIRM.

Investment Properties
At the balance sheet date the Group holds no investment properties having sold its portfolio during 2014. Comparative balance sheet disclosures detail investment properties owned by the Group's Kings Manor Properties Limited subsidiary. These were classified as Held for Sale, having met the conditions laid out in IFRS5. They were held at a fair value representing the agreed sales price of the property portfolio net of sales fees.

Property, Plant, Equipment and Depreciation
On transition to IFRS, the Group elected to adopt the exemption in IFRS 1 which permits an entity to use, on transition to IFRS, a value, which is not depreciated cost, as the 'deemed cost' of the asset. Property, plant and equipment is stated at cost (or 'deemed cost') less accumulated depreciation and any provisions for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Depreciation on assets commences when they are ready for their intended use and is provided at rates calculated to write down the assets to their estimated residual values over the course of their anticipated useful lives, on the following bases:

Freehold buildings and leasehold buildings:

With a residual lease term of greater than fifty years	- 2% per annum straight line
Other leasehold buildings	- over the term of the lease

Equipment, fixtures, fittings and motor vehicles:

Refurbishment expenditure	- 6.67% to 10% per annum, straight line
Equipment, fixtures and fittings	- 10% per annum, straight line
Computer equipment	- 20% per annum, straight line
Motor vehicles	- over the term of the lease

Gains and losses on disposals are determined by comparing the net disposal proceeds with the carrying amount of the asset and are included in the income statement in the period in which they arise.

Lease Purchase and Leasing
The Group enters into lease purchase contracts and finance and operating leases. Assets held under lease purchase contracts and finance leases are capitalised in property, plant and equipment at the fair value of the asset at the inception of the lease, with an equivalent liability categorised under other liabilities. Assets are depreciated in accordance with the relevant Group policy, over the lower of the useful life of the asset and the term of the lease. Finance charges are allocated to accounting periods over the life of each lease on a straight line basis or using the sum of digits method, depending on the cash flows attached to the agreement. Rentals under operating leases are charged on a straight line basis over the lease term. Both finance charges and rentals are recognised in administrative expenses in the Income Statements.

Taxation
Corporation tax is charged on profits adjusted for tax purposes. Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements of the individual entities. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Pension Scheme Costs
The Society operates a defined contribution scheme on behalf of directors and staff. For the defined contribution scheme, contributions are charged to the Income Statements, as they become payable, in accordance with the rules of the Scheme.

Significant Accounting Policies Continued

The Society previously operated a defined benefit scheme; this was closed to future accrual from 30 November 2010, and was funded by contributions partly from employees and partly from the Society at rates determined by an independent actuary. These contributions are invested separately from the Group's assets.

Under the revised IAS 19, the Scheme assets are measured at bid value at each Balance Sheet date and the obligations are measured by an independent actuary using the projected unit valuation method, discounted using a high quality corporate bond rate. The resulting pension scheme surplus or deficit is recognised immediately on the Balance Sheet and any resulting actuarial remeasurements are recognised immediately in the Statements of Comprehensive income with service cost and net interest recognised in the Income Statements.

Provisions

A provision is recognised when there is a present obligation as a result of a past event, it is probable that the obligation will be settled and it can be reliably estimated. Contingent liabilities have not been recognised.

Segment Information

The operating segments disclosed (Member business and Solutions business) are those used in the Group's management and internal reporting structures (for the Chief Operating Decision Maker) in accordance with IFRS 8. No segment information is presented on geographical lines, because substantially all of the Group's activities are in the United Kingdom.

Accounting Estimates and Judgements in applying Accounting Policies

The Group has to make judgements in applying its accounting policies which affect the amounts recognised in the Annual Accounts. These judgements are based on management's best knowledge but the eventual outcome may differ from them. In addition, estimates and assumptions are made that could affect the reported amounts of assets and liabilities within the following year. The most significant areas where judgements and assumptions are made are as follows:

Pensions

Significant judgements are required in relation to the assumptions for the valuation of the pension scheme surplus or deficit including discount, interest and mortality rates, inflation, take up of the Pension Increase Exchange offer and future salary increases. The Board receives independent external advice from actuarial consultants in arriving at the scheme assumptions which are outlined together with sensitivity analysis in Note 31 to the Annual Accounts.

Effective Interest Rate (EIR)

To calculate the appropriate EIR, certain assumptions are made in respect of the expected lives of specific asset portfolios which take into account such factors as the terms of the particular product, historic repayment data and prevailing economic conditions. These estimates are reviewed on a regular basis to ensure they reflect the portfolio's actual performance.

Impairment of Financial Assets

On loans fully secured on residential property the key assumptions in assessing the underlying value of the assets held as security for the loans is based on historic data and prudent expectations around future conditions. An estimate of forced sale adjustments (covering house price falls and disposal costs) has an impact on the level of provisioning for possession and arrears exposures.

A forced sale adjustment that was higher by 5% would increase residential provisions by £0.1m.

Loans secured on commercial property or land are more individually significant. Provision is made against loans in arrears, possession or Law of Property Act 1925 (LPA) receivership, or where a trigger event raises the likelihood of future problems servicing the loan. The key assumptions used in the discounted future value calculations used to determine the level of impairment required in respect of individual financial assets include:

- Predictions of the future value of underlying assets held as security for loans advanced, based on historic data, professional advice and expectations around future conditions including tenancy levels;
- Any sale adjustments, disposal costs, fees or other cash flows applicable;
- Any applicable adjustments arising on hedging instruments relating to the loan as employed by the Society; and
- Timing of cash flows.

Impairment of Treasury Assets

Treasury investments are regularly reviewed for objective evidence of impairment. In determining whether objective evidence exists, the Group considers, amongst other factors, financial difficulties of the counterparty, missed payments in breach of contractual arrangements, appointment of an administrator and current market conditions. Provision is made against treasury assets with reference to information provided by administrators on recoverability and also against traded market values. A 1% increase in the average recovery and market value assumption would decrease the current provision by £0.3m (and vice-versa).

Fair Value of Derivatives and Financial Assets

Fair values are determined by the three tier valuation hierarchy as defined within IFRS 7, Financial Instruments.

Where available, quoted market prices are used to facilitate valuations made. Financial valuation models using observable input data are used to value derivative financial instruments for which no active market exists. Further details are given in Note 33 to the Accounts.

Financial Services Compensation Scheme Provision

As explained in Note 26, the Society is committed to paying a levy to the Financial Services Compensation Scheme (FSCS). The provision for FSCS interest costs in this year's accounts is dependent on the interest charge levied which will not be invoiced until July 2015. The Society has estimated its obligation to the Scheme with reference to currently available external information on interest due on the loan.

Taxation

The Group is subject to tax in three jurisdictions and, consequently, estimates are required in determining the provision for corporation tax. As shown in Note 19 to the Annual Accounts the Group has deferred tax assets which are considered recoverable given the Society and Group plans over the planning horizon.

Accounting Developments

At the date of approval of these financial statements the following new and amended International Financial Reporting Standards are mandatory for the first time for the financial year beginning 1 January 2014.

- Amendments to IAS 32 on Financial instruments asset and liability offsetting. Clarifies some of the requirements for offsetting financial assets and financial liabilities on the balance sheet.
- Amendment to IAS 36, 'Impairment of assets' on recoverable amount disclosures. These narrow-scope amendments address the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal.

Significant Accounting Policies Continued

- Amendments to IAS 39 'Financial instruments: Recognition and measurement', on novation of derivatives and hedge accounting. Narrow scope amendments allowing hedge accounting to continue in a situation where a derivative which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws or regulation, if specific conditions are met.
- Amendment to IAS 19, 'Employee benefits' on defined benefit plans. Clarifies the requirements relating to how employee or third party contributions that are linked to service should be attributed to periods of service.
- Annual improvements 2012. Amendments made to IFRS 2, 'Share-based payment', IFRS 3, 'Business combinations', IAS 16, 'Property, plant and equipment', and IAS 38, 'Intangible assets', IFRS 8, 'Operating segments', IAS 24, 'Related party disclosures', and IFRS 13, 'Fair value measurement'.
- Annual improvements 2013. Amendments made to IFRS 1, 'First-time adoption of International Financial Reporting Standards', IFRS 3, 'Business combinations', IFRS 13, 'Fair value measurement', and IAS 40, 'Investment property',
- Amendments to IAS 10, 12 and IAS 27 on consolidation for investment entities. Allows many funds and similar entities exemption from consolidating most of their subsidiaries, instead, measuring them at fair value through profit or loss.

Developments not effective at 31 December 2014

There are a number of new or amended standards which become effective in 2015, and beyond, which allow for early adoption but the Society is not taking up any of those standards before their mandatory date.

- IFRS 9 Financial instruments will supersede IAS 39 giving classification and measurement, impairment and hedge accounting requirements for financial instruments. The Society is monitoring the development of IFRS 9 closely. In 2013 the implementation date for the standard was revised from 2015 to an undefined future period.

Restatements

The IFRS Interpretations Committee (IFRIC) have issued a new interpretation; IFRIC 21 'Levies' which became effective on 1 January 2014 and has been adopted retrospectively by the Group in the period.

IFRIC 21 clarifies the trigger point for recognising a provision based on a government imposed levy as being the 'obligating event that triggers payment'. IFRIC 21 affects the way the Society accounts for its proportion of the FSCS levy, which has a scheme year beginning 1 April, by clarifying that the FSCS levy for the year is to be provided for in full on 1 April each year, which will be based on what will be invoiced in July of that year. Previously an earlier trigger point for recognition had been adopted.

Under IAS 8, the Group has retrospectively adopted IFRIC 21 and restated its 2013 financial position and result. The restatement has resulted in an increase in the Group's net assets, as the FSCS provision is being booked in a later reporting period.

The restatement has had an impact on the profit figures for the period to 31 December 2013. The full year charge for 2013 has increased from £2.0m to £2.7m, recognised in full on 1 April 2013, with the tax charge restated accordingly.

The restatement has also impacted the opening and closing 2013 general reserves. Opening 2013 general reserves have been restated to remove excess historic provisions made in expectation of future FSCS levy charges. This has reduced the opening 2013 position by £1.7m.

Clarifying amendments to IAS 32 have had an impact on the balance sheet figures presented at 31 December 2013. Cash collateral pledged and received against exposures to and with financial derivative counterparties is now presented gross on the balance sheet. The Society's corresponding derivative financial instrument assets and liabilities have been similarly restated to their gross position. Further quantified detail is presented in Note 33 to the accounts on page 72.

Affected financial statement line items:

	Group Reported in 2013	2013 Restated	Society Reported in 2013	2013 Restated
	£m	£m	£m	£m
Income Statements				
Provisions for liabilities other charges	**(3.3)**	(4.0)	**(3.3)**	(4.0)
Profit for the year before taxation	**2.0**	1.3	**2.2**	1.5
Taxation Expense	**(1.9)**	(1.8)	**(1.7)**	(1.6)
Result after taxation for the financial year	**0.1**	(0.5)	**0.5**	(0.1)
Statements of Comprehensive Income				
Total comprehensive expense for the financial year	**(4.1)**	(4.7)	**(3.7)**	(4.3)
Balance Sheets				
Assets				
Derivative financial instruments	**21.4**	32.0	**21.4**	32.0
Fair value adjustments for hedged risk	**13.6**	120.9	**13.6**	120.9
Deferred tax assets	**9.8**	9.4	**10.1**	9.7
Liabilities				
Due to members	**3,236.1**	3,235.2	**3,236.1**	3,235.2
Derivative financial instruments	**13.1**	120.9	**13.1**	120.9
Fair value adjustments for hedged risk	**4.5**	15.6	**4.5**	15.6
Provisions for liabilities and charges	**5.1**	3.5	**5.1**	3.5
Reserves	**168.0**	169.1	**169.6**	170.7
Note 26 Provisions for liabilities and Charges				
Opening provision at 1 January 2013	**3.8**	1.6	**3.8**	1.6
New provisions during the year	**2.0**	2.7	**2.0**	2.7
Amounts utilised released the year	**(2.7)**	(2.8)	**(2.7)**	(2.8)
Closing provision at 31 December 2013	**3.1**	1.5	**3.1**	1.5

2 Interest receivable and similar income

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
On loans and advances to customers	**102.8**	105.5	**102.8**	105.7
On debt securities				
- interest and other income	**6.8**	11.8	**6.8**	11.8
- profits net of losses on realisation	**3.0**	7.9	**3.0**	7.9
On other liquid assets				
- interest and other income	**1.9**	2.0	**1.9**	2.0
Net expense on derivatives hedging assets	**(29.2)**	(32.2)	**(29.2)**	(32.2)
	85.3	95.0	**85.3**	95.2

3 Interest payable and similar charges

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
On shares held by individuals	**69.4**	86.5	**69.4**	86.5
On subscribed capital	**3.8**	3.6	**3.8**	3.6
On deposits and other borrowings				
- subordinated liabilities	**3.6**	3.4	**3.6**	3.4
- to other depositors and borrowers	**1.6**	2.2	**1.6**	2.2
Net income on derivatives hedging liabilities	**(18.2)**	(24.1)	**(18.2)**	(24.1)
	60.2	71.6	**60.2**	71.6

4 Other income and charges

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Other income				
Fee and commission income	**8.6**	8.4	**5.4**	5.5
Other operating income	**15.4**	17.7	**15.4**	17.4
	24.0	26.1	**20.8**	22.9

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Other charges				
Fee and commission expense	**1.7**	1.4	**1.7**	1.4

5 Income from shares in subsidiary undertakings

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Received from subsidiary undertakings	**-**	-	-	3.1

6 Administrative expenses

	Note	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Staff costs	7	**21.2**	23.1	**19.4**	21.5
Rentals under operating leases for land and buildings					
- payable to third parties		**1.4**	1.4	**1.4**	1.4
- payable to subsidiary undertaking		**-**	-	**0.1**	0.1
Other administrative expenses		**10.6**	10.1	**10.4**	9.7
		33.2	34.6	**31.3**	32.7

During the year the Group and Society obtained the following services from the Society's auditors and these are included in other administrative expenses.

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Fees payable to the Society's auditors for audit of Society and consolidated financial statements	**0.2**	0.2	**0.2**	0.2
Fees payable to the Society's auditors for other services	**0.2**	0.1	**0.2**	0.1
	0.4	0.3	**0.4**	0.3

Fees payable to the Society's auditor for the audit of consolidated financial statements includes **£22k** (2013: £24k) attributable to subsidiary companies. Fees payable to the Society's auditor for other services includes **£nil** (2013: £1.5k) for tax services, and **£180k** (2013: £140k) for other non-audit services.

7 Staff costs

	Note	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Wages and salaries		**19.5**	19.2	**18.0**	17.9
Social security costs		**1.8**	1.7	**1.6**	1.5
Pension costs for:					
- defined benefit scheme		**(2.3)**	-	**(2.3)**	-
- defined contribution scheme		**2.2**	2.2	**2.1**	2.1
	6	**21.2**	23.1	**19.4**	21.5

Included within pension costs for 2014 is a credit of £2.6m in relation to the reduction in pension liabilities in the defined pension scheme following the successful implementation of a pension increase exchange exercise. Associated costs amounted to £0.3m giving a net credit of £2.3m.

Directors' emoluments are disclosed in the Remuneration Committee report on page 27.

The monthly average number of persons employed, including Executive Directors, during the year was:

	GROUP 2014	GROUP 2013	SOCIETY 2014	SOCIETY 2013
Full time	**641**	673	**613**	642
Part time	**212**	203	**211**	202
	853	876	**824**	844
Principal Office	**643**	662	**636**	653
Branches	**210**	214	**188**	191
	853	876	**824**	844

8 Taxation expense

	Note	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Current tax					
UK corporation tax on profit at 21.49% (2013: 23.25%) for the year		-	-	-	-
Group relief for the year		-	-	-	(0.3)
Under provision in respect of previous years		-	-	0.3	-
Total current tax		-	-	0.3	(0.3)
Deferred tax					
Current year	19	1.1	1.8	1.1	2.1
Under / (over) provision in respect of previous years		-	-	0.1	(0.2)
Total deferred tax		1.1	1.8	1.2	1.9
Total taxation expense in the Income Statements		1.1	1.8	1.5	1.6

Analysis of taxation expense for the year

The tax on the Group and Society profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits as follows:

	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Profit before taxation	4.0	1.3	2.9	1.5
Profit before taxation at the standard rate of corporation tax in the UK of 21.49% (2013: 23.25%)	0.9	0.3	0.6	0.4
Expense / (income) not taxable / deductible for tax purposes:				
Expenses	0.2	0.2	0.6	0.8
Non-taxable dividend income received	-	-	-	(0.7)
Non-taxable expenses credit	(0.5)	-	(0.5)	-
Tax losses in respect of capital losses	0.5	-	0.5	-
Rate change	-	1.3	-	1.3
Under / (over) provision in respect of previous years	-	-	0.3	(0.2)
Total taxation expense	1.1	1.8	1.5	1.6

Factors affecting future tax charges

The Society has unrelieved trading losses which are expected to affect future taxable profits.

Notes to the Accounts for the year ended 31 December 2014

9 Segment information

The Chief Operating Decision Maker has been identified as the Board of Directors. The Board reviews the Group's internal reporting in order to assess performance and allocate resources. Management has determined the operating segments based on these reports.

Following the management approach of IFRS 8, operating segments are reported in accordance with the internal reporting provided to the Board of Directors. The operating segments used by the Group meet the definition of a reportable segment under IFRS 8.

The 'Member business' segment provides mortgage, savings, investment and insurance products to Members and customers. The 'Solutions business' segment (also referred to as NSSL) provides business to business services through people, processes and technology. The Board assesses performance based on profit before tax after the allocation of all central costs. Operating profit before impairments, provisions, FSCS levy and exceptional items is also assessed as this provides information on underlying business performance excluding legacy portfolio impairment charges, levies outside of management's direct control and non-recurring items.

No segment information is presented on geographical lines, because substantially all of the Group's activities are in the United Kingdom.

Income and directly attributable costs are allocated to each segment and support costs are apportioned, based on direct salary costs and detailed allocations by budget holders.

Year to 31 December 2014	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	25.1	-	25.1
Other income and charges	7.1	15.2	22.3
Administrative expenses	(25.3)	(7.9)	(33.2)
Depreciation	(1.4)	(0.4)	(1.8)
Operating profit before impairments, charges and FSCS levy	5.5	6.9	12.4
Impairment charges on loans and advances to customers	(5.9)	-	(5.9)
Provisions for liabilities and charges	(2.5)	-	(2.5)
(Loss) / profit for the year before taxation	(2.9)	6.9	4.0
Taxation expense			(1.1)
Profit after taxation for the financial year			2.9
Total assets	3,732.3	3.9	3,736.2

Restated year to 31 December 2013	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	23.4	-	23.4
Other income and charges	8.8	15.9	24.7
Losses recognised on revaluation of investment properties	(1.1)	-	(1.1)
Gains less losses from financial instruments and hedge ineffectiveness	0.5	-	0.5
Administrative expenses	(26.2)	(8.4)	(34.6)
Depreciation	(1.7)	(0.6)	(2.3)
Operating profit before impairments, provisions, FSCS levy and exceptional items	3.7	6.9	10.6
Impairment credit on loans and advances to banks	0.8	-	0.8
Impairment charges on loans and advances to customers	(6.9)	0.2	(6.7)
Provision for liabilities and charges	(4.0)	-	(4.0)
Gain on disposal of Prepaid Cards business	-	0.6	0.6
(Loss) / profit for the year before taxation	(6.4)	7.7	1.3
Taxation expense			(1.8)
Profit after taxation for the financial year			(0.5)
Total assets	3,783.2	4.0	3,787.2

10 Gain on Disposal of Prepaid Cards Division

On 21st December 2011 the Society sold its Prepaid Cards division (PPC) to Wirecard AG.

The total purchase price was payable as cash on the date of legal completion plus deferred consideration based on the financial performance of PPC in 2012 and 2013. Final settlement for this sale was recognised at 31st December 2013.

The Gain on disposal comprises the following elements:

	2014 £m	2013 £m
Deferred consideration receiveable	-	0.6

11 Loans and advances to banks

Repayable from the date of the Balance Sheets in the ordinary course of business as follows:

	GROUP		SOCIETY	
	2014 £m	2013 £m	2014 £m	2013 £m
Accrued interest	0.1	-	0.1	-
On demand	3.1	1.0	3.0	0.7
In not more than three months	212.5	131.1	212.5	131.1
Gross loans and advances to banks	215.7	132.1	215.6	131.8
Less: allowance for losses on loans and advances to banks	(11.8)	(18.9)	(11.8)	(18.9)
	203.9	113.2	203.8	112.9

Allowance for losses on loans and advances to banks

	GROUP and SOCIETY 2014 £m	2013 £m
Balance at 1 January	18.9	19.7
New provisions during the year	-	-
Amounts utilised during the year	(7.1)	(0.8)
At 31 December	11.8	18.9

At 31 December 2014 the Society had loans and advances to Icelandic banks totalling **£13.3m** (2013: £23.4m), against which allowance for losses of **£11.8m** (2013: £18.9m) has been made. The Society sold its exposure to Glitnir in October 2013 and received the funds in January 2014. Book value reflected the final agreed sales price less disposal costs.

12 Debt securities

Transferable debt securities	GROUP and SOCIETY 2014 £m	2013 £m
Issued by public bodies - listed	-	98.7
Issued by other borrowers - unlisted	253.6	378.6
	253.6	477.3
These have remaining maturities as follows:		
Accrued interest	1.6	2.9
In not more than one year	10.0	37.6
In more than one year but not more than five years	242.0	359.6
In more than five years	-	77.2
	253.6	477.3

The Directors consider that the primary purpose of holding securities is to comply with prudential requirements. All transferable debt securities are held with the intention of use on a continuing basis in the Group's activities. They are designated by management on initial recognition as being available for sale and are recognised, both initially and subsequently, at fair value with changes recognised directly in other comprehensive income.

Unlisted debt securities are primarily AAA related holdings of Residential Mortgage Backed Securities and covered bonds.

Under IAS 39 as amended, certain financial instruments were reclassified with effect from 1 July 2008. The table below sets out the financial instruments reclassified and their carrying and fair values:

	31 December 2014		31 December 2013	
	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m
Fair value through profit or loss financial instruments reclassified to held to maturity financial instruments	-	-	6.4	5.8

13 Assets pledged as collateral

Assets are pledged as collateral under repurchase agreements with banks. Securities pledged with banks are debt securities with a market value of £48.5m (2013: £nil). All collateral agreements mature within 1 year.

The nature and carrying amounts of the assets pledged as collateral are as follows:

	Group and Society Asset		Group and Society Related liability	
	2014 £m	2013 £m	2014 £m	2013 £m
Debt securities pledged	48.5	-	30.0	-

14 Loans and advances to customers

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
Loans fully secured on residential property	2,448.7	2,418.5	2,437.8	2,405.0
Loans fully secured on land	215.6	290.0	215.6	290.0
Other loans	19.6	22.7	19.6	22.7
Gross loans and advances	2,683.9	2,731.2	2,673.0	2,717.7
Less: allowance for losses on loans and advances	(23.8)	(30.5)	(23.8)	(30.5)
	2,660.1	2,700.7	2,649.2	2,687.2

Loans and advances to customers have remaining contractual maturities as follows:

	GROUP 2014 £m	GROUP 2013 £m	SOCIETY 2014 £m	SOCIETY 2013 £m
On demand	7.7	10.5	7.7	10.5
In not more than three months	92.0	109.1	92.0	109.1
In more than three months but not more than one year	98.4	91.8	98.3	91.7
In more than one year but not more than five years	290.5	338.5	289.6	337.6
In more than five years	2,195.3	2,181.3	2,185.4	2,168.8
Gross loans and advances	2,683.9	2,731.2	2,673.0	2,717.7
Less: allowance for losses on loans and advances	(23.8)	(30.5)	(23.8)	(30.5)
	2,660.1	2,700.7	2,649.2	2,687.2

Where a loan is repayable by instalment, each such instalment has been treated as a separate repayment in the maturity analysis set out above. The Group's experience is that in many cases mortgages are redeemed before their scheduled maturity date. As a consequence, the maturity analysis illustrated above may not reflect actual experience.

Allowance for losses on loans and advances

GROUP and SOCIETY

	Loans fully secured on residential property		Loans fully secured on land		Other loans		Total		
	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
Balance at 1 January 2014	1.7	0.4	22.6	5.5	0.3	-	24.6	5.9	30.5
(Credit) / charge for the year	(1.9)	0.1	10.6	(2.9)	-	-	8.7	(2.8)	5.9
Written back / (written off) during the year	1.1	-	(13.5)	-	-	-	(12.4)	-	(12.4)
Interest suspended	-	-	(1.2)	1.0	-	-	(1.2)	1.0	(0.2)
At 31 December 2014	**0.9**	**0.5**	**18.5**	**3.6**	**0.3**	**-**	**19.7**	**4.1**	**23.8**

GROUP and SOCIETY

	Loans fully secured on residential property		Loans fully secured on land		Other loans		Total		
	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
Balance at 1 January 2013	2.3	0.6	18.7	5.5	0.3	0.1	21.3	6.2	27.5
Charge / (credit) for the year	0.8	(0.2)	6.1	-	-	-	6.9	(0.2)	6.7
Written off during the year	(1.6)	-	(4.2)	-	-	(0.1)	(5.8)	(0.1)	(5.9)
Interest suspended	0.2	-	2.0	-	-	-	2.2	-	2.2
At 31 December 2013	**1.7**	**0.4**	**22.6**	**5.5**	**0.3**	**-**	**24.6**	**5.9**	**30.5**

15 Fair value adjustment for hedged risk

As disclosed in the statement of accounting policies, when specific criteria are met, the Group applies fair value hedge accounting and the adjustments to assets and liabilities are included on the balance sheet under the heading 'Fair value adjustment for hedged risk'.

The fair value adjustment for hedged risk for assets for the Group and Society was **£201.8m**, (2013: £120.9m as restated). The fair value adjustment for hedged risk for liabilities for the Group and Society was **£8.4m**, (2013: £15.6m as restated).

16 Investments in subsidiary undertakings

SOCIETY

Investments in subsidiary undertakings	Shares £m	Loans £m	Total £m
Cost			
At 1 January 2014	6.0	20.9	26.9
Additions	-	0.5	0.5
Repayments received	-	(7.7)	(7.7)
At 31 December 2014	**6.0**	**13.7**	**19.7**
Provisions			
At 1 January and 31 December 2014	0.6	3.1	3.7
Net book amount at 31 December 2014	**5.4**	**10.6**	**16.0**

Investments in subsidiary undertakings	Shares £m	Loans £m	Total £m
Cost			
At 1 January 2013	6.0	36.3	42.3
Additions	-	1.1	1.1
Repayments received	-	(16.5)	(16.5)
At 31 December 2013	**6.0**	**20.9**	**26.9**
Provisions			
At 1 January 2013	0.6	-	0.6
Write Offs	-	3.1	3.1
At 31 December 2013	**0.6**	**3.1**	**3.7**
Net book amount at 31 December 2013	**5.4**	**17.8**	**23.2**

The Society directly holds 100% of the issued ordinary share capital of all its subsidiary undertakings.

The Directors believe that the carrying value of the investments in subsidiary undertakings is supported by their underlying net assets. In 2013 the Society's loan to Kings Manor Properties Limited was written down to the value of the subsidiary's net assets, an adjustment of £3.1m. This is no longer a principal subsidiary undertaking.

Name of principal subsidiary undertakings	**Principal activity**
Newcastle Financial Services Limited	Provision of financial services
Newcastle Mortgage Loans (Jersey) Limited	Mortgage lending
Newcastle Portland House Limited	Commercial property rental
Newcastle Strategic Solutions Limited	Provision of specialised products and services
Newton Facilities Management Limited	Provision of managed IT services

All the above subsidiary undertakings, except for Newcastle Mortgage Loans (Jersey) Limited, which is incorporated and operates in Jersey, are incorporated in England and Wales and operate in the United Kingdom.

17 Property, plant and equipment

GROUP

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2014	6.7	12.2	29.0	47.9
Additions	-	-	3.5	3.5
Disposals	-	-	(1.0)	(1.0)
At 31 December 2014	**6.7**	**12.2**	**31.5**	**50.4**
Accumulated depreciation				
At 1 January 2014	0.9	3.2	22.4	26.5
Charge for the year	0.1	0.2	1.5	1.8
Disposals	-	-	(0.9)	(0.9)
At 31 December 2014	**1.0**	**3.4**	**23.0**	**27.4**
Net book amount at 31 December 2014	**5.7**	**8.8**	**8.5**	**23.0**

GROUP

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2013	6.7	12.2	28.5	47.4
Additions	-	-	0.6	0.6
Disposals	-	-	(0.1)	(0.1)
At 31 December 2013	**6.7**	**12.2**	**29.0**	**47.9**
Accumulated depreciation				
At 1 January 2013	0.8	3.0	20.6	24.4
Charge for the year	0.1	0.2	2.0	2.3
Disposals	-	-	(0.2)	(0.2)
At 31 December 2013	**0.9**	**3.2**	**22.4**	**26.5**
Net book amount at 31 December 2013	**5.8**	**9.0**	**6.6**	**21.4**

Notes to the Accounts for the year ended 31 December 2014

17 Property, plant and equipment Continued

SOCIETY

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2014	6.7	0.9	26.9	34.5
Additions	-	-	3.5	3.5
Disposals	-	-	(1.0)	(1.0)
At 31 December 2014	**6.7**	**0.9**	**29.4**	**37.0**
Accumulated depreciation				
At 1 January 2014	0.9	0.1	20.3	21.3
Charge for the year	0.1	-	1.5	1.6
Disposals	-	-	(0.9)	(0.9)
At 31 December 2014	**1.0**	**0.1**	**20.9**	**22.0**
Net book amount at 31 December 2014	**5.7**	**0.8**	**8.5**	**15.0**

SOCIETY

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2013	6.7	0.9	26.4	34.0
Additions	-	-	0.6	0.6
Disposals	-	-	(0.1)	(0.1)
At 31 December 2013	**6.7**	**0.9**	**26.9**	**34.5**
Accumulated depreciation				
At 1 January 2013	0.8	0.1	18.5	19.4
Charge for the year	0.1	-	1.9	2.0
Disposals	-	-	(0.1)	(0.1)
At 31 December 2013	**0.9**	**0.1**	**20.3**	**21.3**
Net book amount at 31 December 2013	**5.8**	**0.8**	**6.6**	**13.2**

Included within Equipment, fixtures, fittings and motor vehicles are assets under finance leases, which comprise motor vehicles and a long lease hold property that have the following net book amounts.

	GROUP and SOCIETY 2014 £m	2013 £m
Cost		
At 1 January	**0.8**	0.9
Accumulated depreciation	**(0.1)**	(0.1)
Net book amount at 31 December	**0.7**	0.8

18 Investment properties held for sale

	GROUP 2014 £m	GROUP 2013 £m
Fair value		
At 1 January	**4.3**	14.0
Net losses from fair value adjustments	**-**	(1.1)
Disposals	**(4.3)**	(8.6)
At 31 December	**-**	4.3

The residential investment property business does not fall into the Group's simplified building society model and the decision was taken to dispose of this portfolio of assets in 2012. At 31 December 2013 all assets remaining on balance sheet were sold subject to contract with the asset carrying amount adjusted to fair value being the agreed sale price of the remaining units. The final sale proceeds were received in the early part of 2014 and the subsidiary is now in the process of being wound up.

There was no material investment property rental income or direct operating expenses for the subsidiary in 2014.

	GROUP 2014 £m	GROUP 2013 £m
Income from rental properties	**-**	0.3
Operating expenses relating to rental properties	**-**	(0.3)
Net rental income from rented properties	**-**	-

19 Deferred tax

Deferred tax is calculated on all temporary differences under the liability method using a tax rate of **20%** (2013: 20%).
The movement on the deferred tax account is shown below.

	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
At 1 January	**9.4**	10.5	**9.7**	10.5
Income Statements expense	**(1.1)**	(1.8)	**(1.1)**	(2.1)
(Under) / over provision in respect of prior years	**-**	-	**(0.1)**	0.2
Credited on items taken directly through reserves	**1.5**	0.7	**1.5**	0.7
Transfer of capital losses from subsidiary undertaking	**-**	-	**0.3**	0.4
At 31 December	**9.8**	9.4	**10.3**	9.7

Deferred tax assets and liabilities are attributable to the following items.

	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Deferred tax assets				
Short term timing differences	**0.1**	0.6	**0.1**	0.3
Other items	**1.4**	0.8	**1.4**	0.8
Trading losses	**6.9**	6.9	**6.9**	6.9
Depreciation in excess of capital allowances	**1.4**	1.1	**1.9**	1.7
	9.8	9.4	**10.3**	9.7

	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Deferred tax assets				
Deferred tax asset to be recovered in less than 12 months	**1.2**	0.8	**1.2**	0.6
Deferred tax asset to be recovered in more than 12 months	**8.6**	8.6	**9.1**	9.1
	9.8	9.4	**10.3**	9.7

The deferred tax expense in the Income Statements comprises the following temporary differences:

	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Short term timing differences	**(0.1)**	(0.7)	**(0.1)**	(0.4)
Other items	**(0.8)**	(0.4)	**(0.6)**	(0.9)
Trading losses	**(0.5)**	(0.8)	**(0.7)**	(0.7)
Depreciation in excess of capital allowances	**0.3**	0.1	**0.2**	0.1
	(1.1)	(1.8)	**(1.2)**	(1.9)

Deferred tax assets are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable. The Chancellor announced in the 2014 Autumn Statement that a proposal was likely to be enacted whereby banks and building societies could only extinguish half of their tax liability on profits chargeable to corporation tax by utilising brought forward trading losses. At the balance sheet date this proposal had not been enacted, and the Society understands, that the impact on building societies is still being considered by the Treasury. Should this proposal be enacted it would take the Society longer to recover its deferred tax assets.

20 Other assets

	GROUP		SOCIETY	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Receivable from subsidiary undertakings	**-**	-	**0.6**	3.2
Interest receivable on financial instruments	**0.2**	2.0	**0.2**	2.0
Prepayments and accrued income	**6.3**	7.0	**12.8**	13.5
Other	**2.0**	2.0	**2.0**	2.1
	8.5	11.0	**15.6**	20.8

21 Due to Members

	GROUP and SOCIETY	
	2014	2013 Restated
	£m	£m
Held by individuals	**2,973.4**	3,235.1
Other shares	**0.3**	0.1
	2,973.7	3,235.2

Repayable from the date of the Balance Sheets in the ordinary course of business as follows:

Accrued interest	**29.3**	39.1
On demand	**1,550.6**	1,646.9
In not more than three months	**697.3**	927.1
In more than three months but not more than one year	**485.2**	436.7
In more than one year but not more than five years	**197.5**	182.7
In more than five years	**13.8**	2.7
	2,973.7	3,235.2

Included in share balances is a contractual balance of **£74.2m** (2013: £98.5m) relating to Capital Protection Bonds. The fair value includes adjustments of **£7.6m** (2013: £15.9m restated) which are attributable to changes in benchmark equity and interest rate indices. The Society is contractually required to pay only the par value of the shares on maturity, plus the relative performance of the index.

22 Due to other customers

	GROUP		SOCIETY	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Amounts owed to subsidiary undertakings	**-**	-	**0.1**	0.1
Other	**164.9**	122.7	**164.9**	122.7
	164.9	122.7	**165.0**	122.8

Repayable from the date of the Balance Sheet in the ordinary course of business as follows:

Accrued interest	**0.7**	0.6	**0.7**	0.6
On demand	**2.8**	3.5	**2.8**	3.5
In not more than three months	**99.7**	48.1	**99.8**	48.2
In more than three months but not more than one year	**57.2**	43.5	**57.2**	43.5
In more than one year but not more than five years	**4.5**	27.0	**4.5**	27.0
	164.9	122.7	**165.0**	122.8

Notes to the Accounts for the year ended 31 December 2014

23 Deposits from banks

Repayable from the date of the Balance Sheets in the ordinary course of business as follows:

	GROUP and SOCIETY	
	2014	2013
	£m	£m
Accrued interest	**0.2**	-
In not more than three months	**40.4**	4.4
In more than three months but not more than one year	**73.0**	1.0
In more than one year but not more than five years	**-**	6.0
	113.6	11.4

24 Debt securities in issue

	GROUP and SOCIETY	
	2014	2013
	£m	£m
Certificates of deposits	**1.0**	7.5

Debt securities have remaining maturities as follows:

In not more than three months	**-**	1.0
In more than three months but not more than one year	**1.0**	6.5
	1.0	7.5

25 Other liabilities

	GROUP		SOCIETY	
	2014	2013	**2014**	2013
	£m	£m	**£m**	£m
Amounts payable to subsidiary undertakings	**-**	-	**5.1**	6.2
Third party income tax withheld	**0.5**	0.8	**0.5**	0.8
Current tax liabilities	**0.2**	0.2	**-**	-
Obligations under finance leases	**1.1**	1.1	**1.1**	1.1
Other creditors	**0.9**	1.2	**0.9**	0.9
Accruals and deferred income	**7.9**	7.3	**7.4**	6.9
	10.6	10.6	**15.0**	15.9

Obligations under finance leases fall due as follows:

Within one year	**-**	0.1	**-**	0.1
In one to two years	**0.1**	0.1	**0.1**	0.1
In two to five years	**0.2**	0.1	**0.2**	0.1
In more than five years	**0.8**	0.8	**0.8**	0.8
	1.1	1.1	**1.1**	1.1

These liabilities are secured by charges over the assets to which they relate.

There is not a material difference between the minimum lease payment at the balance sheet date and their present value.

26 Provisions for liabilities and charges

GROUP and SOCIETY

	Repositioning Programme £m	FSCS Levy £m	Other Provisions £m	Total £m
Opening Provision at 1 January 2014	**0.6**	**1.5**	**1.4**	**3.5**
New Provisions during the year	**-**	**2.5**	**-**	**2.5**
Amounts utilised during the year	**(0.2)**	**(2.7)**	**-**	**(2.9)**
Closing Provision at 31 December 2014	**0.4**	**1.3**	**1.4**	**3.1**

GROUP and SOCIETY
Restated

	Repositioning Programme £m	FSCS Levy £m	Other Provisions £m	Total £m
Opening Provision at 1 January 2013	0.8	1.6	0.4	2.8
New Provisions during the year	-	2.7	1.3	4.0
Amounts utilised during the year	(0.2)	(2.8)	(0.3)	(3.3)
Closing Provision at 31 December 2013	0.6	1.5	1.4	3.5

Provision for Financial Services Compensation Scheme Levy
In common with all regulated UK deposit takers, the Society pays a levy to the Financial Services Compensation Scheme (FSCS) which covers a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes, using the rights that have been assigned to it. During the latter part of 2008 claims against the FSCS were triggered by the transfer of Bradford and Bingley's retail deposit business to Abbey National (now Santander) and the defaults of Kaupthing Singer and Friedlander, Heritable Bank and Landsbanki (Icesave).

Further defaults arose in relation to London Scottish Bank and Dunfermline Building Society. The FSCS has met these claims by way of loans received from HM Treasury.

The FSCS is liable to pay interest on the loans from HM Treasury and has a further liability where there are insufficient funds available from the realisation of the assets of the relevant institutions to repay fully the respective HM Treasury loans.

In 2014 the Society changed its accounting policy for the recognition of its liability for the FSCS levy in line with a new interpretation issued by the IFRS Interpretations Committee. Further details of the impact of IFRIC 21 "Government Levies" are given in Note 1 on pages 46 and 47. At 31 December 2014 the Society had a liability of £1.3m (2013: £1.5m as restated) in relation to interest payable in respect of the 2014/15 Scheme year as interest is paid in arrears, being billed in July 2015 and paid by September 2015. Interest payable has been calculated using the latest FSCS published data available.

Provision for Repositioning costs
The Society established a £4m provision in 2010 to cover costs and fees associated with its programme of cost reduction, business simplification and property rationalisation. At 31 December 2014 £0.4m (2013: £0.4m) of the provision remained, relating to the remaining vacant properties that the Society is currently marketing with property agents.

Other provisions
Other provisions include an estimate of the costs of potential consumer redress and a small provision for residual prepaid card exposures.

27 Subordinated liabilities

	GROUP and SOCIETY 2014 £m	2013 £m
6.375% fixed rate subordinated notes 2015 (2013: 7.375%)	**9.6**	9.6
7.190% fixed rate subordinated notes 2017 (2013: 8.190%)	**25.0**	25.0
3.853% fixed rate subordinated notes 2019	**25.0**	25.0
Less: unamortised issue costs	**(0.1)**	(0.1)
Less: unamortised capital exchange costs	**-**	(0.5)
	59.5	59.0

On a winding up, the subordinated notes rank behind the claims against the Society of all depositors, creditors and investing Members (other than holders of deferred shares i.e. permanent interest bearing shares) of the Society.

The notes are repayable, at the Society's option, with the prior consent of the Regulators, only on the payment of a penalty, on any interest date within five years of the maturity date.

On 10 May 2010 the Society announced that a Capital Agreement (the Agreement) had been approved by holders of certain classes of the Society's existing subordinated debt and permanent interest bearing shares. The Agreement involved adding a conversion feature such that the relevant instruments would convert into profit participating deferred shares (PPDS) should the Society's core tier 1 capital ratio fall below 5%. In return for this feature an increase in coupon was agreed for each instrument. The Agreement further contained an upper trigger point for core tier I ratio whereby relevant instruments would cease to be convertible and the coupon uplift would fall away if the Society's ratio exceeded 12%. In August 2014 the Society announced that it had exceeded the 12% Ceiling Trigger set out in the Capital Agreement. In accordance with the Agreement the instruments are no longer convertible and the coupon uplift has been removed, in addition the remaining unamortised capital exchange costs totalling £0.5m have been written off.

28 Subscribed capital

	GROUP and SOCIETY 2014 £m	2013 £m
12.625% permanent interest bearing shares	**10.0**	10.0
10.750% permanent interest bearing shares	**10.0**	10.0
12.000% permanent interest bearing shares (2013: 12.250%)	**10.0**	10.0
	30.0	30.0
Less: unamortised issue costs	**(0.1)**	(0.1)
Less: unamortised capital exchange costs	**-**	(0.2)
	29.9	29.7

The 12.625% and 10.750% subscribed capital issues were issued for an indeterminate period and are only repayable in the event of the winding up of the Society. The £10m 12.0% PIBS can be called by the Society on 18 December 2018 by giving 30 to 60 days notice to the PIBS holders, subject to having gained regulatory consent in advance of sending the notices.

29 Note to the Cash Flow Statements

Reconciliation of profit before taxation to net cash outflow from operating activities	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Profit before taxation	**4.0**	1.3	**2.9**	1.5
Depreciation and amortisation	**1.8**	2.3	**1.6**	2.0
Interest on subordinated liabilities	**3.6**	3.4	**3.6**	3.4
Interest on subscribed capital	**3.8**	3.6	**3.8**	3.6
Increase / (decrease) in derivative financial instruments	**96.3**	(10.2)	**96.3**	(10.2)
(Decrease) / increase in other financial liabilities at fair value through profit or loss	**(88.1)**	13.4	**(88.1)**	13.4
Changes in retirement benefit obligations	**3.7**	(2.0)	**3.7**	(2.0)
Other non-cash movements	**(9.0)**	22.8	**(9.6)**	21.8
Net cash inflow before changes in operating assets and liabilities	**16.1**	34.6	**14.2**	33.5
Decrease in loans and advances to customers	**47.3**	23.9	**44.7**	17.0
Decrease in shares	**(261.5)**	(209.3)	**(261.5)**	(209.3)
Increase / (decrease) in amounts due to other customers and deposits from banks	**144.4**	(103.9)	**144.4**	(106.9)
Decrease in debt securities in issue	**(6.5)**	(0.5)	**(6.5)**	(0.5)
Increase in other assets, prepayments and accrued income	**2.5**	6.7	**5.2**	10.5
Decrease in other liabilities	**-**	(8.6)	**(0.9)**	(11.4)
Net cash outflow from operating activities	**(57.7)**	(257.1)	**(60.4)**	(267.1)

Cash and cash equivalents	GROUP 2014 £m	GROUP 2013 Restated £m	SOCIETY 2014 £m	SOCIETY 2013 Restated £m
Cash and balances with the Bank of England	**310.6**	297.0	**310.6**	297.0
Loans and advances to banks repayable on demand	**3.1**	1.0	**3.0**	0.7
Investment securities	**200.7**	112.2	**200.7**	112.2
At 31 December	**514.4**	410.2	**514.3**	409.9

Cash and cash equivalents comprise cash in hand, balances with the Bank of England, loans and advances to banks available on demand or with original maturities of three months or less and investment securities with a maturity period of three months or less i.e. highly liquid assets readily convertible into cash.

30 Guarantees, contingent liabilities and commitments

(i) Until 11 June 1996, under Section 22 of the Building Societies Act 1986, the Society had an obligation to discharge the liabilities of its subsidiary undertakings insofar as they were unable to discharge the liabilities out of their own assets. Subsequently, the Society has voluntarily agreed to provide continued support to all of its subsidiary undertakings, insofar as any liabilities are not covered by legislation.

(ii) In common with other financial institutions, the Society has a contingent liability in respect of contributions to the Financial Services Compensation Scheme established under the Financial Services and Markets Act 2000. Details are given in Note 26.

(iii) Commitments

The Society has no capital commitments for the acquisition of property, plant and equipment at 31 December.

	GROUP and SOCIETY 2014 £m	GROUP and SOCIETY 2013 £m
Irrevocable undrawn committed loan facilities	**82.9**	78.3

Payments under non-cancellable operating lease agreements

Total minimum lease payments:

	GROUP and SOCIETY 2014 £m	GROUP and SOCIETY 2013 £m
Within one year	**1.5**	1.5
In one to five years	**4.4**	4.9
Over five years	**2.9**	3.8
	8.8	10.2

31 Retirement benefit obligations

Group and Society Pension schemes
The Society operates a UK registered trust based pension scheme that provides defined benefits. The scheme was closed to new entrants in 2000 and closed to future accrual of benefits in 2010. Pension benefits are linked to the members' final pensionable salaries and service at their retirement date (or date of leaving if earlier). The Trustees are responsible for running the Scheme in accordance with the Scheme's Trust Deed and Rules, which sets out their powers. The Trustees of the Scheme are required to act in the best interests of the beneficiaries of the Scheme. There is a requirement that one-third of the Trustees are nominated by the members of the Scheme.

There are two categories of pension scheme members:
- Deferred members: members with deferred benefits in the Scheme who are not yet receiving their pension.
- Pensioner members: in receipt of pension.

The defined benefit obligation is valued by projecting the best estimate of future benefit obligations (allowing for revaluation to retirement for deferred members and annual pension increases for all members) and then discounting to the balance sheet date. The majority of benefits receive increases linked at least partly to inflation (subject to a cap of no more than 5% pa). The valuation method used is known as the Projected Unit Method. The approximate overall average duration of the Scheme's defined benefit obligation as at 31 December 2014 was 18 years.

Future funding obligation
The Trustees are required to carry out an actuarial valuation every 3 years. The last actuarial valuation of the Scheme was performed by the Scheme Actuary for the Trustees as at 30 June 2013. In respect of the deficit in the Scheme as at 30 June 2013, the Society agreed to pay £1.7m per annum for 6 years. In addition, the Society will pay £0.3m per annum to meet the costs of running the Scheme. The Society therefore expects to pay £2.0m to the Scheme during the accounting year beginning 1 January 2015.

Assumptions
The results of the actuarial valuation as at 30 June 2013 have been updated to 31 December 2014 by a qualified independent actuary. The assumptions used were as follows:

Significant actuarial assumptions	2014	2013
Discount rate	3.60%	4.60%
RPI inflation	3.00%	3.40%
CPI inflation	2.00%	2.40%
Mortality assumption		
Mortality (post-retirement)	S1PA CMI_2014_M/F [1.00%] (yob)	S1PA CMI_2013_M/F [1.00%] (yob)
Other actuarial assumptions		
RPI pension increases	2.90%	3.30%
Revaluation of deferred pensions in excess of GMP	2.00%	3.30%
Life expectancies (in years)		
For an individual aged 62		
Male	24.6 years	24.5 years
Female	26.9 years	26.9 years
At age 62 for an individual aged 42 in 2014		
Male	26.1 years	26.0 years
Female	28.5 years	28.5 years

Risks
Through the Scheme, the Society is exposed to a number of risks:

Asset volatility: the Scheme's defined benefit obligation is calculated using a discount rate set with reference to corporate bond yields, however the Scheme invests significantly in equities and other growth funds. These assets are expected to outperform corporate bonds in the long term, but provide volatility and risk in the short term.

Changes in bond yields: a decrease in corporate bond yields would increase the Scheme's obligations, however this would be partially offset by an increase in the value of the Scheme's bond holdings.

Inflation risk: a significant proportion of the Scheme's defined benefit obligation is linked to inflation, therefore higher inflation will result in a higher defined benefit obligation (subject to the appropriate caps in place). The majority of the Scheme's assets are either unaffected by inflation, or only loosely correlated with inflation, therefore an increase in inflation would also increase the deficit. However, due to the caps in place the risk of high inflation is limited.

Life expectancy: if Scheme members live longer than expected, the Scheme's benefits will need to be paid for longer, increasing the Scheme's obligations.

The Trustees and Society manage risks in the Scheme through the following strategies:

Diversification: investments are well diversified, such that the failure of any single investment would have no material impact on the overall level of assets.

Investment strategy: the Trustees are required to review their investment strategy on a regular basis.

Pension increase exchange: an option has been introduced to allow members to exchange their pension increases for a higher immediate pension this has had the impact of reducing pension scheme liabilities in relation to retired members that have already taken up the option and based on the assumption of future take up by deferred members that retire in the future.

31 Retirement benefit obligations Continued

Sensitivity analysis Assumption	Change in assumption	Change in defined benefit obligation
Discount rate	+0.5% / -0.5%	+8% / –9%
RPI and CPI inflation	+0.5% / -0.5%	+4% / –4%
Assumed life expectancy	+ 1 year	+3%

Limitations of the sensitivity analysis
These calculations provide an approximate guide to the sensitivity of results and may not be as accurate as a full valuation carried out on these assumptions. Each assumption change is considered in isolation, which in practice is unlikely to occur, as changes in some of the assumptions are correlated.

Assets
The assets of the Scheme were invested as follows:

Asset class at market value	2014 %	2013 %
Equities and growth	43.8	50.1
Bonds	19.5	18.7
Gilts	34.3	28.4
Cash	2.4	2.8
Total	100.0	100.0
Actual return on assets over year	10.0	6.7

All assets listed above have a quoted market price in an active market.

Reconciliation to the Balance Sheets

	2014 £m	2013 £m
Market value of assets	91.8	82.6
Present value of defined benefit obligation	95.5	84.6
Funded status	(3.7)	(2.0)
Pension liability recognised in the Balance Sheets before allowance for deferred tax	(3.7)	(2.0)

Analysis of changes in the value of the defined benefit obligation over the year

	2014 £m	2013 £m
Value of defined benefit obligation at start of year	84.6	82.4
Interest cost	3.7	3.7
Past service credit	(2.6)	-
Benefits paid	(2.5)	(2.7)
Actuarial losses: experience differing from that assumed	-	1.2
Actuarial losses: changes in demographic assumptions	-	0.1
Actuarial losses / (gains): changes in financial assumptions	12.3	(0.1)
Value of defined benefit obligation at end of year	95.5	84.6

Analysis of changes in the value of the Scheme assets over the year

	2014 £m	2013 £m
Market value of assets at start of period	82.6	76.7
Interest income	3.7	3.4
Actual return on assets less interest	6.3	3.3
Employer contributions	2.0	2.2
Benefits paid	(2.5)	(2.7)
Administration costs	(0.3)	(0.3)
Market value of assets at end of year	91.8	82.6

31 Retirement benefit obligations Continued

Amount recognised in Income Statements

	2014 £m	2013 £m
Administration costs	0.3	0.3
Past service credit, less associated costs	(2.3)	-
Net interest	-	0.3
Amount (credited) / charged to Income Statements	(2.0)	0.6

Amounts recognised in Statements of Comprehensive Income

	2014 £m	2013 £m
Actuarial losses on defined benefit obligations	(12.3)	(1.2)
Actual return on assets less interest	6.3	3.3
Amounts recognised in Statements of Comprehensive Income	(6.0)	2.1

32 Related parties

The Group is controlled by Newcastle Building Society which is registered in England and Wales and operates in the United Kingdom. Further details of subsidiary undertakings are disclosed in Note 16 to these Accounts. The Directors are considered to be the only key management personnel as defined by IAS 24.

Transactions with directors and their close family members

Directors and their close family members have entered into the following transactions with Newcastle Building Society in the normal course of business.

Loans outstanding to directors and their close family members

	2014 £000	2013 £000
At 31 December	343	-

These loans were made on normal commercial terms and a register of them is available for inspection at the Principal Office for a period of 15 days up to and including the Annual General Meeting.

Deposits and investments held by directors and their close family members

	2014 £000	2013 £000
At 31 December	467	470

Amounts deposited by Directors and members of their close families earn interest on the same terms and conditions applicable to other customers.

Notes to the Accounts for the year ended 31 December 2014

32 Related parties Continued

Year ended 31 December 2014

	Interest paid to Society £000	Interest received from Society £000	Rent received from Society £000	Other amounts paid to Society £000	Other amounts received from Society £000
Kings Manor Properties Limited	-	-	-	4,253	-
Newcastle Financial Services Limited	-	-	-	-	-
Newcastle Mortgage Loans (Jersey) Limited	778	-	-	3,400	-
Newcastle Portland House Limited	-	-	66	-	-
Newton Facilities Management Limited	-	-	-	-	-

Year ended 31 December 2013

	Interest paid to Society £000	Interest received from Society £000	Rent received from Society £000	Other amounts paid to Society £000	Other amounts received from Society £000
Kings Manor Properties Limited	245	-	-	8,673	-
Newcastle Financial Services Limited	-	-	-	3,100	-
Newcastle Mortgage Loans (Jersey) Limited	1,019	-	-	7,890	-
Newcastle Portland House Limited	-	7	97	-	-
Newton Facilities Management Limited	-	-	-	-	-

At the year end the following unsecured balances were outstanding:

	Amounts owed by Society 2014 £000	Amounts owed to Society 2014 £000	Amounts owed by Society 2013 £000	Amounts owed to Society 2013 £000
Kings Manor Properties Limited	-	13	499	5,021
Newcastle Financial Services Limited	1,648	-	2,803	2,750
Newcastle Mortgage Loans (Jersey) Limited	-	10,614	-	13,225
Newcastle Portland House Limited	2,933	14	2,933	14
Newton Facilities Management Limited	73	37	73	10
Newcastle Strategic Solutions Limited	505	487	505	487

33 Financial instruments

These disclosures are given on a Group basis, as the risks of the organisation are managed on a Group basis. The Society basis is not materially different from the Group basis for any of the disclosures in this note.

Categories of financial instruments
The accounting policies note (Note 1 on page 44) describes how the classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the financial assets and liabilities in the balance sheet by the class of financial instrument to which they are assigned and by the measurement basis.

Group as at 31 December 2014	Note	Amortised cost £m	Available for sale £m	Fair value through income statements £m	Total £m
Financial assets					
Cash in hand and balances with Bank of England		310.6	-	-	310.6
Loans and advances to banks	11	203.9	-	-	203.9
Debt securities	12	-	253.6	-	253.6
Derivative financial instruments	33	-	-	16.4	16.4
Fair value adjustments for hedged risk	15	-	-	201.8	201.8
Loans and advances to customers	14	2,660.1	-	-	2,660.1
Assets pledged as collateral	13	48.5	-	-	48.5
Total financial assets		**3,223.1**	**253.6**	**218.2**	**3,694.9**
Financial liabilities					
Due to Members - shares	21	2,966.1	-	7.6	2,973.7
Fair value adjustments for hedged risk	15	-	-	8.4	8.4
Due to other customers	22	164.9	-	-	164.9
Deposits from banks	23	113.6	-	-	113.6
Debt securities in issue	24	1.0	-	-	1.0
Derivative financial instruments	33	-	-	201.6	201.6
Subordinated liabilities	27	59.5	-	-	59.5
Subscribed capital	28	29.9	-	-	29.9
Total financial liabilities		**3,335.0**	**-**	**217.6**	**3,552.6**

Cash in hand and balances with the Bank of England: Cash held for liquidity and operational purposes earning interest income.

Loans and advances to banks: Cash lent to financial institutions to generate an interest income return.

Debt securities: Assets comprising mainly covered bonds and residential mortgaged backed securities. Investments made to utilise liquid cash reserves to generate interest income.

Derivative financial instruments: financial instruments whose value is derived from an underlying asset, index or reference rate it is linked to. The Group does not operate a derivative financial instruments trading book. Exposures in the treasury portfolio are held for liquidity purposes or in the case of fair value exposures on derivatives, for hedging purposes.

Fair value adjustments for hedged risk: adjustments to reflect the fair value of financial instruments that are designated as hedged items as part of the Group's interest rate risk hedging activities.

Loans and advances to customers: cash lent to individual members of the Society, corporates and housing associations.

Assets pledged as collateral: assets still owned by the Group but transferred to the secure safekeeping of the Group's counterparties under a repurchase agreement.

33 Financial instruments Continued

Group as at 31 December 2013 Restated	Note	Amortised cost £m	Available for sale £m	Held to maturity £m	Fair value through income statements £m	Total £m
Financial assets						
Cash in hand and balances with Bank of England		297.0	-	-	-	297.0
Loans and advances to banks	11	113.2	-	-	-	113.2
Debt securities	12	-	470.9	6.4	-	477.3
Derivative financial instruments	33	-	-	-	32.0	32.0
Fair value adjustments for hedged risk	15	-	-	-	120.9	120.9
Loans and advances to customers	14	2,700.7	-	-	-	2,700.7
Assets pledged as collateral	13	-	-	-	-	-
Total financial assets		**3,110.9**	**470.9**	**6.4**	**152.9**	**3,741.1**
Financial liabilities						
Due to Members - shares	21	3,219.3	-	-	15.9	3,236.2
Fair value adjustments for hedged risk	15	-	-	-	15.6	15.6
Due to other customers	22	122.7	-	-	-	122.7
Deposits from banks	23	11.4	-	-	-	11.4
Debt securities in issue	24	7.5	-	-	-	7.5
Derivative financial instruments	33	-	-	-	120.9	120.9
Subordinated liabilities	27	59.0	-	-	-	59.0
Subscribed capital	28	29.7	-	-	-	29.7
Total financial liabilities		**3,449.6**	**-**	**-**	**152.4**	**3,602.0**

Due to members – shares: cash deposits made by customers held by the Society.

Due to other customers: cash deposits made by non-members of the Society.

Deposits from banks: deposits made by financial institutions with the Society.

Debt securities in issue: debt securities issued by the Society.

Subordinated liabilities: loan notes issued by the Society incurring fixed annual interest expense.

Subscribed capital: Permanent Interest Baring Shares issued by the Society, with further details given in Note 28.

Note: The Society has issued a number of structured customer share products whose interest depends on movements in equity indices. In line with IAS39, the derivative equity component of the liability is split out and measured at a fair value reflecting observable market prices.

33 Financial instruments Continued

Fair values of financial assets and liabilities

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.

The Group has financial assets and liabilities for which there is a practical right to set off the recognised amounts, and which are settled net in practise. However, the netting arrangements do not result in an offset of balance sheet assets and liabilities for accounting purposes as the right to set off is not unconditional in all circumstances.

Under IAS 32: Financial Instruments: Presentation, there are no financial assets or liabilities which are offset with the gross amount presented on the balance sheet.

Under IFRS 7, the Group must disclose the effect of its netting arrangements, including the effects of potential rights of set off associated with its recognised financial assets and liabilities.

Group as at 31 December 2014

	Gross fair value presented in the Balance Sheet	Offsetting financial collateral (received*)/ pledged not meeting the offsetting criteria of IAS 32	Net collateralised position	Net position under Master Netting Agreements not meeting the offsetting requirements of IAS 32 (pre-collateral)
Financial assets	**£m**	**£m**	**£m**	**£m**
Interest rate swaps	16.4	(8.1)	8.3	7.9
Financial liabilities				
Interest rate swaps	(201.6)	199.2	(2.4)	(193.8)

Restated Group as at 31 December 2013

	Gross fair value presented in the Balance Sheet	Offsetting financial collateral (received*)/ pledged not meeting the offsetting criteria of IAS 32	Net collateralised position	Net position under Master Netting Agreements not meeting the offsetting requirements of IAS 32 (pre-collateral)
Financial assets	£m	£m	£m	£m
Interest rate swaps	32.0	(11.1)	20.9	11.0
Financial liabilities				
Interest rate swaps	(120.9)	107.8	(13.1)	(98.3)

*Offsetting collateral is pledged and received in line with underlying Credit Support Annexes (CSA) with the Group's financial counterparties. The Group posts and receives cash collateral on a daily basis to minimise its own and counterparty exposures to mark-to-market positions. Collateral posted is measured against counterparty mark-to-market values and may not reflect the Society's internal valuation of its financial instruments.

The Society has entered into International Swaps and Derivatives Association (ISDA) Master agreements with financial counterparties in line with standard industry practise. Netting agreements contained within are not considered sufficient alone to satisfy the offsetting criteria of IAS 32. The netting agreements are intended to protect the Society against fair value loss in the unlikely future event of counterparty default.

Where the Society holds multiple financial assets and liabilities with a single counterparty, and a Master netting agreement is in effect, the net fair value exposure for each counterparty is calculated. Net exposures placed with counterparties are consolidated into the financial assets disclosure above, net exposures received from counterparties similarly consolidated into the financial liabilities.

Collateral

In the ordinary course of business, the Group may from time to time access market-wide facilities provided by central banks secured against non-cash collateral.

Cash collateral has been posted and received in line with Credit Support Annexes with the Group's financial counterparties, as detailed above. Cash collateral received is the legal property of the Group with no obligation to return. Similarly, cash collateral pledged is no longer under the legal ownership or control of the Group.

The fair value of collateral pledged and received is as set out below:

	GROUP and SOCIETY 2014 £m	2013 £m
Cash collateral received under CSA agreements	**8.1**	11.1
Other financial assets collateral pledged under repurchase agreements	**118.5**	-
Cash collateral paid under CSA agreements	**199.2**	107.8

Cash collateral is held to mitigate exposures to counterparties with postings updated daily to reflect mark-to-market exposures across the Society's derivative transactions.

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the Group's or Society's balance sheets at their fair value. These assets and liabilities are held at values reflecting their intended use. This is deemed to also reflect their highest and best use. If the Society's intended use of an asset or liability changes the accounting adopted for the item is revisited for reclassification. The carrying values below reflect the Group's maximum exposure to counterparty credit risk at 31 December 2014.

33 Financial instruments Continued

GROUP

	Note	Level*	Carrying value 2014 £m	Carrying value 2013 Restated £m	Fair value 2014 £m	Fair value 2013 Restated £m
Financial assets						
Cash and balances with the Bank of England		1	**310.6**	297.0	**310.6**	297.0
Loans and advances to banks	11	1	**203.9**	113.2	**203.9**	113.2
Debt securities held to maturity	12	1	**-**	6.4	**-**	4.2
Loans and advances to customers	14	3	**2,660.1**	2,700.7	**2,813.3**	2,839.2
Assets pledged as collateral	13	1	**48.5**	-	**48.5**	-
Financial liabilities						
Due to Members - shares	21	2	**2,973.7**	3,235.2	**3,004.1**	3,266.4
Due to other customers	22	2	**164.9**	122.7	**164.9**	122.7
Deposits due to other banks	23	2	**113.6**	11.4	**113.6**	11.4
Debt securities in issue	24	2	**1.0**	7.5	**0.9**	7.8
Subordinated liabilities	27	2	**59.5**	59.0	**65.1**	71.2
Subscribed capital	28	2	**29.9**	29.7	**47.6**	41.6

*Level defined below. The Group does not trade in financial instruments. Sale of financial assets to demonstrate their liquidity and divestment of financial assets that are not felt to meet the Group's risk profile and appetite have had an impact on the Group's financial result during 2014.

Loans and advances to banks

The fair value of floating rate and overnight deposits is their carrying amount. The fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and remaining maturity.

Loans and advances to customers

Loans and advances to customers are net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

Due to Members - shares

The fair value of shares represents the discounted amount of estimated future cashflows paid to shareholders.

Deposits due to other banks

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits and other borrowings without market price is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

Debt securities in issue

The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, a discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

Subordinated liabilities

The fair value of subordinated liabilities is calculated based on discounted cash flows reflecting the contractual liabilities.

Subscribed capital

The fair value of subscribed capital is calculated based on discounted cash flows reflecting the contractual liabilities.

Fair value measurement

The following table summarises the fair value measurement basis used for assets and liabilities held on the Balance Sheet at fair value:

	2014 Level 1 £m	2014 Level 2 £m	2014 Level 3 £m	2014 Total £m	2013 Level 1 £m	2013 Level 2 £m	2013 Level 3 £m	2013 Total £m
Financial assets								
Debt securities - available for sale	**235.6**	**-**	**-**	**253.6**	470.9	-	-	470.9
Derivative financial instruments	**-**	**16.4**	**-**	**16.4**	-	32.0	-	32.0
Fair value adjustments for hedged risk on underlying instruments	**-**	**201.8**	**-**	**201.8**	4.3	-	-	4.3
Financial liabilities								
Derivative financial instruments	**-**	**201.6**	**-**	**201.6**	-	13.1	-	13.1
Fair value adjustments for hedged risk on underlying instruments	**-**	**16.0**	**-**	**16.0**	-	-	-	-

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly (i.e. as price) or indirectly (i.e. Derived from prices).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

These definitions have been taken from March 2009 amendment to IFRS 13 'Improving Disclosures: Financial Instruments'.

The Society uses modelling software to measure fair value movements on its hedging instruments and hedged items on a portfolio (macro) basis. Industry anticipated interest rate movements are factored into the calculations to give an expected fair value of the derivative portfolio.

33 Financial instruments Continued

Derivatives held for hedging

Derivative financial instruments used by the Group have been described previously in the Risk Management Report and footnotes to the table on page 70 of Note 33. The derivative financial instruments are held primarily to mitigate interest rate risk across the Group's balance sheet. The Group actively monitors and manages interest rate risk using hedging as part of that strategy in line with IAS 39. Both fair value and cash flow hedge transactions have been undertaken with the fair values of the derivative instruments held at the Balance Sheet date set out below:

	2014 Notional Amount £m	2014 Fair Value Assets £m	2014 Fair Value Liabilities £m	2013 Notional Amount £m	2013 Fair Value Assets £m	2013 Fair Value Liabilities £m
At 31 December						
Interest rate swaps designated as fair value hedges	1,285.8	16.3	(201.6)	1,760.7	31.9	(120.9)
Interest rate swaps designated as cash flow hedges	200.0	0.1	-	200.0	0.1	-
Interest rate swaps	1.3	-	-	6.4	-	-
		16.4	(201.6)		32.0	(120.9)

The fair values disclosed above give the Group's exposure to derivative instrument credit risk at 31 December 2014 prior to any collateral adjustments as shown on page 72.

Hedge Ineffectiveness

	2014 £m	2013 Restated £m
(Losses) / gains on hedging instruments	(96.1)	53.2
Gains / (losses) on hedged items attributable to the hedged risk	96.1	(52.7)
Net gains representing ineffective portions of the fair value hedges	-	0.5

Liquidity risk

Liquidity risk is the risk that the Society does not hold sufficient liquid resources (resources readily transferable to cash or cash equivalents) to meet its obligations as they fall due.

For each material category of financial liability a maturity analysis is provided in Notes 21 to 24, which represents the contractual maturities. The table below analyses the Group's Financial Liabilities, which will be settled on a net basis, into relevant maturity groupings based on the remaining period at the Balance Sheet date to the contractual maturity date. The amounts disclosed in the table are contractual undiscounted cash flows.

Maturity has been defined by the earliest contractual date of repayment with reference to product terms and conditions. However, management information, both internally generated and through experience, indicates deposits are likely to be repaid later than the earliest date on which repayment is contractually required. The amounts disclosed in the table are contractual undiscounted cash flows and reflect a worst case repayment scenario.

The Group's liquidity risk is managed by The Asset and Liability Committee (ALCO). ALCO review and approve the results of liquidity stress testing scenarios monitoring cashflow forecasts for the next 3 years under base case and stressed scenarios. Lead by the Group Balance Sheet Management and Product Development departments ALCO appraise long term funding plans and scenarios to ensure adequate liquid assets are in place to meet both regulatory and operational requirements. For further detail see the Risk Management Report on page 32.

GROUP

At 31 December 2014	Repayable on demand	Up to 3 months	Between 3 and 12 months	Between 1 and 5 years	Over 5 years	Total
Due to Members - shares	1,579.9	697.3	485.2	197.5	13.8	2,973.7
Due to other customers	3.5	99.7	57.2	4.5	-	164.9
Deposits from banks	0.2	40.4	73.0	-	-	113.6
Debt securities in issue	-	-	1.0	-	-	1.0
Derivative financial instruments	-	-	1.0	10.3	190.3	201.6
Fair value adjustments for hedged risk	-	-	0.5	7.4	0.5	8.4

At 31 December 2013 Restated	Repayable on demand	Up to 3 months	Between 3 and 12 months	Between 1 and 5 years	Over 5 years	Total
Due to Members - shares	1,686.0	927.1	436.7	182.7	2.7	3,235.2
Due to other customers	4.1	48.1	43.5	27.0	-	122.7
Deposits from banks	-	4.4	1.0	6.0	-	11.4
Debt securities in issue	-	1.0	6.5	-	-	7.5
Derivative financial instruments	-	-	0.4	14.7	105.8	120.9
Fair value adjustments for hedged risk	0.4	0.9	6.1	8.2	-	15.6

33 Financial instruments Continued

Credit risk

Credit risk is the risk that a customer or counterparty is unable to honour their repayment of obligations as they fall due. The Group Risk Committee, as detailed on page 30 of these Annual Accounts, maintain oversight of the Retail and Commercial Credit Committees. The Committees are involved in the monitoring of the credit risk within the Group's assets.

Note 14 of the Accounts on page 54 contains details of total mortgage assets.

Once a mortgage has been written down as a result of an impairment loss, interest income is recognised in line with adjusted expected future cash flows on the mortgage.

The Group's lending is all secured with a first charge registered against the collateral property. The average loan to value of the Group's loan portfolios at 31 December 2014 is 62.1% (2013 65.5%) as detailed in the Strategic Report on page 11. Quarterly regional Halifax House Price Index data is used to monitor the value of residential collateral. Provisions are held against loan assets where the recovery of the asset is uncertain. Provisions of £23.8m (2013 £30.5m) are held against the Group's loans and advances to customers at 31 December 2014, as detailed in Note 14 to the accounts on page 54. The Group's Commercial Credit and Provisioning Committees consider a range of factors in identifying a loan's impaired status. These include where a property has been taken into possession, where a loan is no longer being serviced or difficulty in future servicing is expected, and review of watch lists.

The credit quality of the Group's residential loans is considered to be excellent with the loans continuing to perform and arrears being below industry averages. The Group's non-impaired commercial loan assets are also considered to be of a good credit quality.

Prime residential mortgage book

The Prime residential mortgage book consists of traditional residential loans. No sub-prime or self-certification lending has been undertaken.

Loan to value (indexed)	2014 £m	2014 %	2013 £m	2013 %
<70%	1,117.6	66.7	1,018.1	65.7
70% - <80%	262.9	15.7	227.2	14.6
80% - <90%	209.8	12.5	160.5	10.3
>90%	85.6	5.1	145.6	9.4
	1,675.9	100.0	1,551.4	100.0

The table below provides further information by payment due status:

	2014 £m	2014 %	2013 £m	2013 %
Neither past due nor impaired	1,656.8	98.8	1,529.0	98.5
Past due up to 3 months but not impaired	12.2	0.7	13.6	0.9
Impaired and past due 3 to 6 months	3.5	0.2	5.0	0.3
Impaired and past due over 6 months	3.2	0.2	3.7	0.2
In possession	0.2	0.1	0.1	0.1
	1,675.9	100.0	1,551.4	100.0

Against past due and possession cases, **£57.4m** (2013: £60.2m) of collateral is held.

No loans that would be past due or impaired have had terms renegotiated.

The average LTV of the prime residential mortgage book is **54.9%** at 31 December 2014 (2013: 56.1%).

33 Financial instruments Continued

Specialist residential mortgage book

The Specialist residential mortgage book consists of buy-to-let and residential investment loans.

Loan to value (indexed)	2014 £m	2014 %	2013 £m	2013 %
<70%	48.2	47.6	46.9	35.7
70% - <80%	38.4	38.0	29.4	22.3
80% - <90%	2.0	2.0	37.9	28.8
>90%	12.5	12.4	17.3	13.2
	101.1	100.0	131.5	100.0

The table below provides further information by payment due status:

	2014 £m	2014 %	2013 £m	2013 %
Neither past due nor impaired	87.8	86.8	100.5	76.4
Past due up to 3 months but not impaired	8.6	8.5	20.9	15.9
Not past due but impaired	-	-	2.5	1.9
Impaired and past due over 6 months	0.2	0.2	1.6	1.2
LPA receivership	3.7	3.7	3.1	2.4
In possession	0.8	0.8	2.9	2.2
	101.1	100.0	131.5	100.0

Against past due, LPA receivership and possession cases, **£15.9m** (2013 £48.1m) collateral is held.
No loans that would be past due or impaired have had terms renegotiated.
The average LTV of the specialist residential mortgage book is **70.2%** at 31 December 2014 (2013: 73.4%).

Commercial lending book

The commercial lending book comprises:

GROUP	2014 £m	2014 %	2013 £m	2013 %
Loans secured on commercial property	192.9	21.5	267.1	25.8
Loans secured on serviced apartments to retail customers	23.7	2.6	24.0	2.3
Loans to Housing Associations	679.5	75.9	744.3	71.9
	896.1	100.0	1,035.4	100.0

Notes to the Accounts for the year ended 31 December 2014

33 Financial instruments Continued

Loans secured on commercial property

Loan to value	2014 £m	2014 %	2013 £m	2013 %
<70%	39.2	20.3	45.0	16.8
70% - <80%	93.6	48.6	102.9	38.5
80% - <90%	14.9	7.7	34.9	13.1
>90%	45.2	23.4	84.3	31.6
	192.9	100.0	267.1	100.0

The table below provides further information by payment due status:

	2014 £m	2014 %	2013 £m	2013 %
Neither past due nor impaired	141.1	73.1	191.0	71.5
Not past due but impaired	36.4	18.9	38.1	14.3
Impaired and past due up to 3 months	2.3	1.2	4.9	1.8
Impaired and past due over 6 months	13.1	6.8	16.8	6.3
LPA receivership	-	-	16.3	6.1
	192.9	100.0	267.1	100.0

During 2014 there were no loans that had payment arrears capitalised, (which would have been considered to be forbearance). The Society extended the loan term on two loans maturing in 2014 with total balances of £2m, on original commercial terms and conditions. One of these loans, with a balance of £1.4m was subsequently fully repaid in 2014; the second of these loans has a balance of £0.6m secured against £0.9m of property.

A further one loan maturing in 2014 with a total balance of £2.6m was also extended, but prior to 2014 had previously been transferred onto the latest commercial terms and conditions, which are more favourable to the Society in terms of the rights afforded by the documentation. Collateral of £2.5m is held against this loan. Such extensions are granted to give the borrower more time to sell the security property or to aid amortisation of the debt prior to sale of the security property.

There are no specific provisions against any of these loans but they are covered by the collective provision.

In addition, the Society extended one impaired loan term that matured in 2014, totalling £3.3m with collateral valued at £1.5m. This loan was also transferred onto the latest commercial terms and conditions. The loan is not currently in arrears and the rent received is allowing amortisation of the debt. If the property was sold at the revised maturity date in September 2015, a loss potentially may arise given uncertainty over lease renewal and the related impact on property value. On this basis, a provision of £1.7m was in place at the 2014 year end with regard to this loan.

33 Financial instruments Continued

Loans secured on commercial property are diversified by industry type and an analysis is shown below:

	2014 £m	2014 %	2013 £m	2013 %
Retail	119.1	61.7	146.2	54.7
Office	27.3	14.2	37.7	14.1
Industrial	29.0	15.0	50.7	19.0
Hotel / Leisure	17.3	9.0	19.1	7.2
Student Accommodation	-	-	12.8	4.8
Other	0.2	0.1	0.6	0.2
	192.9	100.0	267.1	100.0

Loans to Housing Associations	2014	2014	2013	2013
Loan to value (unindexed)	£m	%	£m	%
<70%	307.5	45.3	336.1	45.2
70% - <80%	126.4	18.6	146.9	19.7
80% - <90%	229.1	33.7	261.3	35.1
>90%	16.5	2.4	-	-
	679.5	100.0	744.3	100.0

Loans to Housing Associations are secured on residential property
No Housing Association loans are past due or impaired

Interest Rate Risk
Interest rate risk is the exposure of the Group's net interest income to movement in interest rates. This is managed using a combination of limits set by the Board and by use of derivative instruments. The sensitivity to interest rate movements is measured using dynamic stress tests for a series of parallel rate shifts over various time periods.

The table below shows the impact of various interest rate scenarios on Group profit before tax, against the Society's current interest rate view.

A positive item is an increase in margin and a negative item is a reduction.

	+1% £m	+2% £m	-1% £m	-2% £m
At 31 December 2014				
Next 12 months	1.9	3.9	-	-
Next 2 years	2.6	5.2	-	-
Next 3 years	4.4	8.8	-	-
At 31 December 2013				
Next 12 months	1.7	3.3	-	-
Next 2 years	1.6	2.9	-	-
Next 3 years	1.3	2.7	-	-

The main risk measure used by ALCO is an immediate 200 basis points parallel shift in rates.

Due to the sustained 2014 low interest rate environment, the rate shocks for interest rate reductions communicated to ALCO have remained at -0.10% and -0.20% throughout 2014. An immediate 2% upward movement in interest rates would increase members' interests by **£8.2m** (2013: £5.7m increase). The derivative gains less losses for the year in respect of fair value hedges comprise losses on derivatives of **£96.1m** (2013: £53.2m gain) and associated gains on hedged items of **£96.1m** (2013: £52.7m loss).

Interest rate risk in the pension schemes
A reduction of 0.1% in the discount rate would increase the pension deficit by approximately £1.7m. Sensitivity is disclosed in the pensions note.

Currency risk
The Group has no exposure to currency risk.

Equity risk
The Group has no material direct exposure to equity risk. The Group has a number of structured products which have an embedded derivative attached to them i.e. the return payable is derived from the performance of an underlying index. Under IAS 39 both the underlying product and the derivative are fair value accounted through the Income Statements. The fair value amounts are approximately equal and offsetting so there is no material charge or credit in the accounts.

1 Statutory percentages

	2014 %	Statutory %
Lending limit	9.41	25.00
Funding limit	8.59	50.00

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986 as amended by the Building Societies Act 1997. Lending limit is calculated excluding all IAS 39 adjustments for derivatives and fair values.

The lending limit measures the proportion of business assets not in the form of loans secured on residential property. Business assets are the total assets of the Group plus allowances for losses on loans and advances less liquid assets, investment properties and property, plant and equipment as shown in the Group balance sheet.

The funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals.

The statutory limits are as laid down under the Building Societies Act 1986, as amended by the Building Societies Act 1997, and ensure that the principal purpose of a building society is that of making loans which are fully secured on residential property and are funded substantially by its Members.

2 Other percentages

As a percentage of shares and borrowings:	2014 %	2013 Restated %
Gross capital	7.86	7.63
Free capital	7.15	7.02
Liquid assets	23.61	26.28
Result for the year as a percentage of mean total assets	0.08	(0.01)
Management expenses as a percentage of mean total assets	0.93	0.94

The above percentages have been prepared from the Annual Accounts.

Gross capital represents the aggregate of the general reserve, available for sale reserve, subordinated liabilities and subscribed capital.

Free capital represents gross capital less property, plant and equipment, investment property and non-current assets held for sale.

Liquid assets are as shown in the Group Balance Sheets but exclude liquid assets pledged under repo agreements.

Shares and borrowings represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue.

Management expenses represent the aggregate of administrative expenses and depreciation.

Mean total assets is the average of the 2014 and 2013 total assets.

Annual Business Statement for the year ended 31 December 2014

Directors at 31 December 2014

	Date of Birth	Date of Appointment	Business Occupation
RJ Bottomley OBE, FCA	**22.05.53**	**22.09.14**	**Company Director**
	Other Directorships: Marsden Packaging Holdings Limited; MSL Energy Limited; MSL Property Care Services Limited; TL Dallas Group Limited; Skillsbridge Limited; Durham County Cricket Club Holdings Limited; Greggs 1978 Pension Scheme Trustee Limited.		
DJ Buffham	**13.08.59**	**24.05.10**	**Company Director**
	Other Directorships: Newton Facilities Management Limited; Northern Homes and Estates Limited; William Leech (Investments) Limited; The William Leech Foundation Limited; Zytronic PLC.		
P Ferguson BSc, CA	**06.03.69**	**19.02.14**	**Building Society Strategy, Planning and Risk Director**
	Other Directorships: None.		
AS Haigh BSc	**26.01.63**	**27.01.14**	**Building Society Chief Operating Officer**
	Other Directorships: None.		
K Ingham	**20.02.65**	**04.09.14**	**Company Director**
	Other Directorships: Virgin Media Limited; Virgin Media Pension Scheme (Trustee).		
RJ McCormick FCA, FCIIA	**09.05.49**	**16.08.07**	**Business Consultant**
	Other Directorships: Newcastle Strategic Solutions Limited; Grassington Hub Limited; Threshfield Quarry Development Trust Limited.		
RD Mayland FCA	**22.05.53**	**27.06.05**	**Company Director**
	Other Directorships: Tynehealth Limited; Community Services North East Limited; At Home in the Community Limited; St John's College, Durham.		
PJ Moorhouse FCCA	**18.01.53**	**31.10.11**	**Company Director**
	Other Directorships: Newton Facilities Management Limited; Newcastle Strategic Solutions Limited; Cumbria NHS Partnership Foundation Trust; Molins Public Limited Company; Transflex Vehicle Rental Limited.		
J Morris BA, FCA	**13.09.56**	**31.10.11**	**Chartered Accountant**
	Other Directorships: None.		
AM Russell BA, FCA, CPA	**18.03.67**	**01.07.10**	**Building Society Deputy Chief Executive & Finance Director**
	Other Directorships: Newcastle Financial Services Limited; Newcastle Mortgage Loans (Jersey) Limited; Newcastle Portland House Limited; St. Cuthberts Care Limited.		
CRR Vine-Lott MBA, FCISI, FCIM, ACIB	**30.01.60**	**01.01.10**	**Director in Financial Services**
	Other Directorships: Just Retirement Group PLC; Just Retirement Limited; Just Retirement Solutions Limited.		
IW Ward FCIB	**04.05.49**	**09.07.13**	**Company Director**
	Other Directorships: Charter Court Financial Services Group Limited (appointed 6 January 2015); Charter Court Financial Services Limited (appointed 6 January 2015); Charter Mortgages Limited (appointed 6 January 2015); Newton Facilities Management Limited; Exact Mortgage Experts Limited (appointed 6 January 2015); Broadlands Finance Limited (appointed 6 January 2015); Harrogate and District NHS Foundation Trust.		
JH Willens MBA, ACIB	**07.06.56**	**04.01.10**	**Building Society Chief Executive**
	Other Directorships: Kings Manor Properties Limited; Brown Shipley & Co. Limited.		

Documents may be served on any of the above named Directors: "Newcastle Building Society" c/o Addleshaw Goddard LLP (Ref. GAB), at the following address: Sovereign House,PO Box 8, Sovereign Street, Leeds LS1 1HQ. The Executive Directors have service contracts which can be terminated at any time by the Society on six months notice. There are no contracts for Non Executive Directors and no compensatory terms for loss of office.

Country-by-Country Reporting

The reporting obligations set out in Article 89 of the European Union's Capital Requirements Directive IV (CRD IV) have been implemented in the UK by the Capital Requirements (Country-by-Country Reporting) Regulations.

Newcastle Building Society is the biggest building society in the North East and the eighth largest in the UK with assets in excess of £3.7 billion.

As a mutual organisation, the Society's primary focus is its members and it aims to provide mortgage, savings and insurance products supported by excellent customer service. Additionally, the Society offers financial advice through Newcastle Financial Services Limited and provides outsourcing of financial services through the Newcastle Strategic Solutions division.

The consolidated financial statements of the Newcastle Building Society Group include the audited results of the Society and its subsidiary undertakings. The consolidated entities, their principal activities and countries of incorporation, are detailed in Note 16 to the Annual Report and Accounts. All of the consolidated entities were incorporated in the United Kingdom, with the exception of Newcastle Mortgage Loans (Jersey) Limited, which is incorporated and operates with no employees in Jersey. The Society also operates a branch in Gibraltar.

For the year ended 31 December 2014:

- Group total operating income was **£47.4m** (2013: £47.5m), profit before tax was **£4.0m** (2013: £1.3m as restated), the proportion not arising from UK-based activity is not considered material for the purposes of this disclosure.
- The average number of Group full time equivalent employees was **767.6**, (2013: 790.4) of which **761.0** (2013: 783.6) were employed in the UK and **6.6** (2013: 6.8) in Gibraltar.
- The Society and the Group paid no corporation tax in the year due to the taxable losses available.

Auditors' Report on Country-by-Country Reporting

Independent auditors' report to the Directors of Newcastle Building Society

We have audited the accompanying schedule of Newcastle Building Society for the year ended 31 December 2014 (the schedule). The schedule has been prepared by the directors based on the requirements of the Capital Requirements (Country-by-Country Reporting) Regulations 2013.

Directors' Responsibility for the schedule

The directors are responsible for the preparation of the schedule in accordance with the Capital Requirements (Country-by-Country Reporting) Regulations 2013, for the appropriateness of the basis of preparation and the interpretation of the Regulations as they affect the preparation of the schedule, and for such internal control as the directors determine is necessary to enable the preparation of the schedule that is free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on the schedule based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the schedule is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the schedule. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the schedule, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the schedule in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the schedule.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the Country-by-Country information in the schedule as at 31 December 2014 is prepared, in all material respects, in accordance with the requirements of the Capital Requirements (Country-by-Country Reporting) Regulations 2013.

Basis of Preparation and Restriction on Distribution

Without modifying our opinion, we draw attention to the schedule, which describes the basis of preparation. The schedule is prepared to assist the Directors to meet the requirements of the Capital Requirements (Country-by-Country Reporting) Regulations 2013. As a result, the schedule may not be suitable for another purpose.

Our report is intended solely for the benefit of the Directors of Newcastle Building Society. We do not accept or assume any responsibility or liability to any other party save where terms are agreed between us in writing.

PricewaterhouseCoopers LLP
Chartered Accountants
Newcastle upon Tyne
24 February 2015

Glossary

Set out below are the definitions of the terms used within the Annual Report and Accounts to assist the reader and to facilitate comparison with other financial institutions:

Arrears - A customer is in arrears when they are behind in their mortgage payments. A customer is 3 months in arrears when they have missed the equivalent of 3 mortgage payments.

Administrative expenses - Expenses incurred in running the day to day activities of the Society including staff, property, marketing and technology costs.

Basel II - The second of the Basel Accords, issued by the Basel Committee on Banking supervision, which defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. Basel II became law in the EU Capital Requirements Directive, and was implemented in the UK via the PRA Handbook.

Basel III - The third of the Basel Accords, issued by the Basel Committee on Banking supervision, which are a long-term package of changes that will strengthen regulatory requirements for capital and liquidity.

Buy to Let (BTL) - A mortgage designed to support customers purchasing an investment property to let out.

Capital Requirements Directive (CRD IV) - The EU legislative package covering prudential rules for banks, building societies and investment firms. CRD IV is made up of the Capital Requirements Directive and Capital Requirements Regulation, it is designed to implement the Basel III agreement across the EU.

Commercial lending / mortgage - Loans secured on commercial property.

Contractual maturity - The final payment date of a loan or other financial instrument, at which point all the remaining outstanding principal and interest is due to be paid.

Core Equity Tier 1 capital - Defined by the PRA as general reserves or qualifying capital instruments which for the Society is the accumulation of retained profits.

Covered bonds - Debt securities backed by a portfolio of mortgages that is segregated from the issuer's other on-balance sheet assets solely for the benefit of the holders of the covered bonds.

Credit risk - The risk that a customer or counterparty is unable to honour their repayment obligations as they fall due.

Debt securities - Assets representing certificates of indebtedness of credit institutions, public bodies or other undertakings excluding central banks.

Derivative financial instruments - A derivative financial instrument is a type of financial instrument (or an agreement between two parties) that has a value based on the underlying asset, index or reference rate it is linked to. The Group uses derivative financial instruments to hedge its exposures to interest rate risk.

Effective interest rate method (EIR) - The method used to measure the carrying value of a financial asset or a liability and to allocate associated interest income or expense over the relevant period.

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.

Financial Conduct Authority (FCA) - FCA regulates the conduct of financial firms providing services to consumers and maintains the integrity of the UK's financial markets.

Financial Services Compensation Scheme (FSCS) - The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the PRA is obliged to pay an annual levy, which goes towards running costs and compensation payments.

Forbearance - A term generally applied to arrangements which are provided to support mortgage customers experiencing financial difficulties. An example of this would be a temporary reduction in mortgage payments.

Free capital - Represents gross capital less property, plant and equipment and investment property.

Funding for Lending Scheme (FLS) - The Scheme to boost the incentive for banks and building societies to lend to UK households and non-financial companies. The Scheme is designed to reduce lending rates and increase availability by making available cheaper Bank of England funding.

Funding limit - Measures the proportion of shares and borrowings not in the form of shares held by individuals.

Gilts - These are bonds issued by certain national governments. The Group only classifies debt securities issued by the Bank of England as Gilts.

Gross capital - The aggregate of general reserve, available-for-sale reserve, subscribed capital and subordinated liabilities.

Icelandic treasury investments - Treasury investments in Icelandic banks purchased prior to the collapse of the Icelandic banking system in October 2008 where holdings are now negligible.

Impaired loans - Loans where an event has occurred which indicates the Group does not expect to collect all the contractual cash flows due, or expects to collect them later than they are contractually due.

Individual Capital Guidance (ICG): - Guidance from the PRA on the minimum level of capital that must be held.

Individual Liquidity Adequacy Assessment (ILAA): - The Group's internal assessment of the liquidity levels needed to meet its regulatory liquidity requirements.

Individual Liquidity Guidance (ILG): - Guidance from the PRA on the minimum quantity of a firm's liquidity resources and the firm's funding profile.

Individually / collectively assessed - Individual assessments are made of all mortgage loans where objective evidence indicates losses are likely or the property is in possession. A collective impairment provision is made against the remaining group of loans and advances where objective evidence indicates that it is likely that losses may be incurred.

Internal Capital Adequacy Assessment Process (ICAAP) - The Group's own assessment of the levels of capital that it needs to hold in respect of the risks it faces under a business as usual scenario and a variety of stress scenarios.

Legacy mortgage portfolios - Mortgage loan books where the Group has ceased new lending and is winding down exposures.

Lending limit - Measures the proportion of business assets not in the form of loans fully secured on residential property.

Leverage ratio - A Basel III ratio which measures Tier 1 capital against total on and off balance sheet assets.

Liquid assets - The total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.

Liquidity Coverage Ratio (LCR) - A Basel III measure of the amount of highly-liquid assets against cash outflows over a 30 day period.

Liquidity risk - The risk that the Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash inflows and outflows.

Loan-to-value ratio (LTV) - A ratio which expresses the amount of a mortgage as a percentage of the value of the property. The Group calculates UK residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis) to reflect changes in house prices.

Loans and advances to banks - Treasury investments purchased with banking institutions.

Management expenses - Management expenses represent administrative expense and depreciation. The management expense ratio is management expenses expressed as a percentage of mean total assets.

Market risk - The risk that movements in market risk factors, including re-pricing of assets and liabilities and the imperfect matching of interest rates between different asset and liability types, may adversely impact the Society.

Mean total assets - Represents the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.

Member - A person who has a qualifying share investment or a mortgage loan with the Society.

Mortgage Market Review (MMR) - A PRA issued policy statement on reform of the lending market designed to deliver a better market for consumers that is sustainable for all participants.

Net interest income - The difference between interest received on assets and interest paid on liabilities.

Non Executive Director - A member of the Society's Board who does not form part of the executive management team. He or she is not an employee of the Society.

Operational risk - The risk of loss arising from inadequate or failed internal processes, people and systems or from external events.

Other lending - loans and advances secured on traded endowment policies.

Past due - Loans on which payments are overdue including those on which partial payments are being made.

Permanent Interest Bearing Shares (PIBS) - Unsecured, deferred shares that are a form of capital. PIBS rank behind the claims of all subordinated debt holders, depositors, payables and investing Members of Newcastle Building Society.

Prepaid Cards business - The division of the Society licensed to issue cards loaded with electronic money which was sold in December 2011.

Prime - Prime mortgages are those granted to the most credit worthy category of residential borrowers.

Prudential Regulation Authority (PRA) - Part of the Bank of England and responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms.

Recovery and Resolution Plan (RRP) - In response to the latest financial crisis, the PRA now requires all financial institutions to prepare recovery and resolution plans, or living wills. The purpose of these plans is to mitigate the likelihood and impact of a future failure.

Renegotiated loans - Loans are classed as renegotiated with the customer's consent, when their terms have changed during the year. Loans and advances are generally renegotiated either as part of an on-going customer relationship or in response to an adverse change in the circumstances of the borrower.

Repo - Short to medium-term funding agreements which allow a borrower to sell a financial asset, such as Government bonds, as security for cash. As part of the agreement the borrower agrees to repurchase the security at a later date. For the party selling the security (and agreeing to repurchase it in the future) it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future), it is a reverse repurchase agreement or reverse repo.

Residential mortgage backed securities (RMBS) - Asset backed securities that represent interests in residential mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and principal).

Residential loans - Residential loans are secured against residential property.

Retail Distribution Review (RDR) - A process carried out by the PRA to change the way recommendations about investment products and pensions are made to investors. This also includes changing the way fees are charged for these services.

Risk appetite - The articulation of the level of risk that the Group is willing to take (or not take) in order to safeguard the interests of the Society's Members whilst achieving business objectives.

Risk-weighted assets (RWA) - The value of assets, after adjustment under Basel II rules, to reflect the degree of risk they represent. The Society measures RWA using the standardised approach.

Shares - Funds deposited by a person in a retail savings account with the Society. Such funds are recorded as liabilities for the Society.

Shares and borrowings - The total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue, including accrued interest.

Solutions - a division of the Society that offers business to business services through people, process and innovative application of technology. Services include complete systems for smaller societies and white-labelled savings management for a range of banks and building societies.

Solvency ratio - the ratio of total capital to total risk weighted assets.

Specialist lending - Aggregate of the Group's residential investment and buy to let mortgage portfolios. No lending has taken place on this book since 2008 and the exposure to portfolio Investors is being reduced.

Subordinated debt / liabilities - A form of Tier 2 capital that is unsecured and ranks behind the claims of all depositors, creditors, and investing Members (other than holders of PIBS).

Tier 1 capital - Tier 1 capital is divided into Core Equity Tier 1 and other Tier 1 capital. Core Equity Tier 1 capital comprises general reserves from retained profits. Other regulatory adjustments may be made for the purposes of capital adequacy. Under the grandfathering rules of Basel III qualifying capital instruments such as PIBS can be included in other Tier 1 capital (i.e. not Core Equity Tier 1) transferring to Tier 2 over the grandfathering period.

Tier 2 capital - Comprises the Group's qualifying subordinated debt and collective impairment allowance (for exposures treated on a Basel II standardised basis).

Wholesale funding - The total of amounts owed to credit institutions, amounts owed to other customers and debt securities in issue less.