

Company Registration Number 6105087

DECO 12 – UK 4 P.L.C
ANNUAL REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2014

TUESDAY



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DECO 12 – UK 4 P.L.C

ANNUAL REPORT AND ANNUAL FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2014

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DECO 12 – UK 4 P.L.C

COMPANY INFORMATION

The board of directors

Mr Graham Cox
Mr Graham Hodgkin

Company secretary

Sunil Masson

Registered office

c/o Deutsche Bank AG, London Branch,
Winchester House
Mailstop 428
1 Great Winchester Street
London
EC2N 2DB
United Kingdom

Auditor

Deloitte LLP
London
United Kingdom

DECO 12 – UK 4 P.L.C

STRATEGIC REPORT

FOR THE YEAR ENDED 31 DECEMBER 2014

The directors present their strategic report together with the audited financial statements of Deco 12 – UK 4 Plc (the “Company”) for the year ended 31 December 2014.

REVIEW OF THE BUSINESS

The Company was incorporated as a public company with limited liability on 14 February 2007 under the laws of England and Wales. The Company was established as a special purpose Company for the purposes of issuing loan notes (the “loan notes”) due January 2020. The loan notes comprise Class A1 notes, Class A2 notes, Class B notes, Class C notes, Class D notes, Class E notes and Class F notes with Class A1 notes bearing the highest ranking in priority. On 13 March 2007, the Company issued £672,883,707 loan notes in accordance with the Offering Circular dated 9 March 2007.

The Company used the proceeds from the issue of these loan notes to acquire the beneficial interest in a commercial mortgage portfolio from Deutsche Bank AG, London Branch, (the “mortgage loans”), to open accounts, to create security and receive interest in respect thereof, and to enter into certain related transactions as described in the Offering Circular.

The Notes are listed on the Irish Stock Exchange.

The directors do not anticipate any other changes to the present level of activity, or the nature of, the Company’s business in the near future.

RESULTS AND PERFORMANCE

The results of the Company for the year, as set out on page 10, show a loss on ordinary activities before tax of £603,242 (2013: profit of £22,034,156). The profit was primarily due to unrealised fair value gain on the derivative financial instruments of £9,069,040 (2013: £22,135,710). The Company had a shareholders’ deficit of £53,458,901 (2013: £52,855,259) as at 31 December 2014. The deficit was primarily due to the cumulative impairment on the mortgage loans of £15,228,303 (2013: £5,554,022) and the fair value liability on the derivative financial instruments totalling £32,743,274 (2013: £41,812,314).

STRATEGY

The principal activity of the Company is the issue of loan notes. The Company has issued loan notes to fund the acquisition of beneficial interest in a mortgage loan portfolio. These financial assets and liabilities provide the majority of the assets and liabilities of the Company along with associated interest income and expense.

The strategies used by the Company in achieving its objectives regarding the use of their financial instruments were set when the Company issued the loan notes. The principal risks arising from the Company’s financial instruments (both assets and liabilities) are credit risk, interest rate risk, refinancing risk and liquidity risk.

The Company has also entered into swap agreements. This is to mitigate the interest rate risk associated with the mismatch between the fixed and floating rate interest generated by the mortgage loans and the floating rate interest paid on the loan notes.

KEY PERFORMANCE INDICATORS (‘KPIs’)

The key performance indicator of the business is considered to be the net interest margin. During the year, the Company achieved a net interest margin (net interest income divided by interest income) of 4.09% (2013: 4.17%), which has slightly decreased since the prior year due to the decrease in the gross amount of the mortgage loans.

STRATEGIC REPORT (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES

The Company's financial instruments, other than derivatives, comprise mortgage loans, cash and cash equivalents, loan notes and various receivables and payables that arise directly from its operations. The main purpose of the interest bearing loan notes is to finance a mortgage portfolio acquired from Deutsche Bank AG, London Branch.

The Company also enters into derivative transactions. The purpose of such transactions is to manage the interest rate risk arising from the Company's operations and its sources of finance.

The Board reviews and agrees policies for managing risks arising on the Company's financial instruments and they are summarised below.

Currency risk

All of the Company's assets and liabilities are denominated in Pound Sterling and therefore there is no foreign currency risk.

Interest rate risk

Interest rate risk exists where assets and liabilities have interest rates set under a different basis or which are reset at different times. The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of its assets and liabilities are similar; where this is not possible the Company uses interest rate swaps to mitigate any residual interest rate risk.

Credit risk

The principal credit risk to the Company is that the borrowers will not be able to meet their obligations as they fall due. The mortgage loans are secured on a number of UK commercial properties which are geographically diverse and include a diverse tenant portfolio.

The most significant concentration of credit risk is considered to be a mortgage loan to Tesco Red Partnership totalling £347,400,000 (2013: Tesco Red Partnership: £347,400,000). At 31 December 2014, the total gross amount outstanding on the mortgage loans was £369,677,836 (2013: £374,404,930). The mortgage loan portfolio consists of three loans secured over 19 properties (2013: 3 loans secured over 22 properties). The three loans are referred to in these financial statements as the Tesco Red Partnership loan, the Borehamwood loan and the 2006/2007 Regent Capital Spectrum IV & V loan.

All 16 of the Tesco Red Partnership loan underlying properties are let to one tenant, Tesco Stores Limited, and the obligations of the latter under related leases are guaranteed by Tesco Plc which is rated BBB- (2013: A-), Ba1- (2013: Baa1), BBB (2013:A-) by Fitch, Moody's and S&P respectively. The downgrade reflected the opinion that Tesco Plc's profitability is expected to continue to weaken because of market competition in the United Kingdom which will remain persistently high over the next 12 months. Nonetheless, the Tesco Red Partnership loan is performing as per the respective terms set out in the loan agreement and the estimated market value of the underlying properties is still higher than the carrying value of the loan. Therefore, the Tesco Red Partnership loan has not been impaired as at year end.

Impairment

The Company assesses at each reporting date whether there is any objective evidence that a financial asset is impaired. A financial asset or portfolio of financial assets is impaired and an impairment loss incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset. The impairment represents the estimated difference between the market valuation of the collateral and the loan outstanding. As at 31 December 2014 the total impairment provision recognised was £15,228,303 (2013: £5,554,022) and the impairment charge recognised during the year amounted to £9,674,281 (£2013: £103,690).

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STRATEGIC REPORT (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES (Continued)

Impairment (continued)

Borehamwood loan: The loan was placed into special servicing following its default in October 2011 when it breached the interest payment date covenant test. The loan subsequently defaulted on its 21 April 2014 maturity date. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 24 April 2012 by the special servicer and the impairment provision recognised at 31 December 2013 was GBP 5,554,022. The special servicer sold the underlying property in January 2015 and a final amount of GBP 6,235,208 was recovered. These proceeds were used as the estimated market value as at 31 December 2014. An impairment reversal of GBP 599,394 was recognised during the year, based on the final recovery amount and a loan principal of GBP 11,189,836, resulting in an impairment provision recognised at 31 December 2014 of GBP 4,954,628.

2006/2007 Regent Capital Spectrum IV & V loan: The loan was placed into special servicing in March 2015 after the borrower breached an obligation in July 2014. This obligation required the borrower to have secured a tenant contributing a minimum of GBP 830,000 per annum rental income through an occupational lease. As such, an impairment assessment was carried out on the loan for the first time this yearend because no impairment provision had been recognised at 31 December 2013. The property was last valued on 19 December 2006. A charge of GBP 10,273,675 was recognised during the year, based on the estimated market value of the collateral at 31 December 2014 of GBP 814,325 and a loan principal of GBP 11,088,000, resulting in an impairment provision recognised at 31 December 2014 of GBP 10,273,675. The estimated market value of the collateral was derived from comparable recent property sales in the area.

Tesco Red Partnership loan: The loan is performing as per the terms of the loan agreement and financial covenants and there has been no history of impairment on the loan; therefore, no impairment assessment has been carried out and no impairment is held against the loan at 31 December 2014.

Refinancing risk

The ability of a borrower to make timely payment of principal due on any loan on the relevant loan maturity date may be dependent upon that borrower's ability to refinance the loan. In the event a borrower cannot refinance before or at the loan maturity date, repayment may be delayed, and in some circumstances the collateral, which could be enforced and sold, may be sold at a value below the then outstanding principal of the loan. As a result, repayment of the loan may be made at below par and the Company would be unable to repay certain classes of the loan notes in full.

Liquidity risk

A facility provided by Danske Bank A/S (London Branch) has been established which will be available, subject to certain criteria and circumstances, in the event of the Company being unable, on a temporary basis, to meet its financial commitments. The liquidity facility for £32,331,838 (adjusted for appraisal reduction) was renewed on 5 March 2015 up to 2 March 2016. The directors expect this facility to be renewed annually.

An amount of £32,331,838 (2013: £32,285,727) of the liquidity facility was drawn as at 31 December 2014. In 2013, Danske Bank A/S (London Branch) was downgraded below the Requisite Rating and, as per the Liquidity Facility Agreement, a Stand-by-Drawing amounting to the full amount of the available facility was drawn down. During the year ended 31 December 2014, an amount of £46,111 was drawn down (2013: repayment of £1,054,321). Further discussion of the Company's approach to financial instruments is set out in note 1 (significant accounting policies) and in note 12.

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STRATEGIC REPORT (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES (Continued)

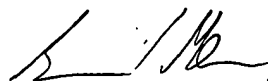
Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out above. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are set out in the financial statements. In addition, notes 1 and 12 to the financial statements include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; and its exposures to credit risk and liquidity risk.

The Company has net liabilities of £53,458,901 (2013: £52,855,259) as a result of impairments of £15,228,303 (2013: £5,554,022) on the loan assets and derivative liabilities of £32,743,274 (2013: £41,812,314) held at fair value. However, the terms of the loan notes are limited recourse and therefore the Company is only obliged to repay the notes to the extent that the Company receives cash from the loan assets. The note holders will therefore ultimately bear the Company's deficits on maturity of the notes.

Due to the limited recourse nature of the loan notes, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Signed by order of the Board



Sunil Masson

.....for and on behalf of

Company Secretary
.....24/06.....2015

DECO 12 – UK 4 P.L.C

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 2014

The directors present their report and the financial statements of Deco 12 – UK 4 Plc (the “Company”) for the year ended 31 December 2014.

PRINCIPAL ACTIVITIES

The Company is a special purpose company established in order to issue loan notes due January 2020 (the “loan notes”), to acquire the beneficial interest in a mortgage portfolio from Deutsche Bank AG, London Branch, (“the mortgage loans”), to open accounts, to create security and receive interest in respect thereof, and to enter into certain related transactions as described in the Offering Circular dated 9 March 2007. On 13 March 2007, the Company issued £672,883,707 loan notes in accordance with the Offering Circular.

RESULTS AND DIVIDENDS

The trading results for the year and the Company’s financial position at the end of the year are shown in the attached financial statements.

The loss of the Company for the year after tax amounted to £603,642 (2013: Profit of £22,033,729) after the gain on the financial derivative instrument of £9,069,040 (2013: £22,135,710) and an impairment charge of the loans of £9,674,281 (2013: Impairment charge of £103,690). The directors have not recommended a dividend (2013: £nil) for the year ended 31 December 2014.

CREDITOR PAYMENT POLICY

The Company’s policy concerning payment of its trade creditors is to pay in accordance with its contractual and other legal obligations. Due to the nature of the business, the main creditors are the noteholders. Principal and interest is repaid quarterly in accordance with the agreements in place. The Company does not follow any other code or standard on payment practice.

THE DIRECTORS

The directors who served the Company during the year were as follows:

Mr Graham Cox
Mr Graham Hodgkin

AUDITOR

Deloitte LLP have expressed their willingness to continue in office as auditor and a resolution to re-appoint them as auditor for the ensuing year will be proposed at the next annual general meeting.

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DIRECTORS' REPORT (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014


STATEMENT AS TO DISCLOSURE OF INFORMATION TO THE AUDITOR

The directors confirm that:

- so far as the directors are aware, there is no relevant audit information of which the Company's auditor is unaware; and
- each of the directors have taken all steps that they ought to have as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

Signed by order of the directors


.....for and on behalf of
Graham Hodgkin
Director
24/06 2015

DIRECTORS' RESPONSIBILITIES STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2014

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that year. In preparing these financial statements, International Accounting Standard 1 requires that directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DECO 12 – UK 4 P.L.C

We have audited the financial statements of Deco 12 – UK 4 P.L.c for the year ended 31 December 2014 which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows and the related notes 1 to 16. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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

Respective responsibilities of directors and auditor

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

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements 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.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2014 and of its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

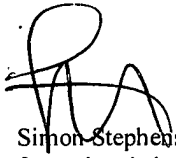
Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

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


Simon Stephens, FCA (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants and Statutory Auditors
London, United Kingdom

24/6/2015

DECO 12 – UK 4 P.L.C

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2014

Continuing operations	Notes	2014 £	2013 £
Interest income	2	20,105,802	21,584,825
Interest expense	3	<u>(19,284,161)</u>	<u>(20,685,217)</u>
Net interest income		821,641	899,608
Fair value movement on derivative financial instruments	13	9,069,040	22,135,710
Impairment reversal/(charge) against mortgage loans	6	<u>(9,674,281)</u>	<u>(103,690)</u>
Other operating expenses	4	<u>(819,642)</u>	<u>(897,472)</u>
(Loss)/Profit before tax for the year		(603,242)	22,034,156
Income tax charge	5	<u>(400)</u>	<u>(427)</u>
(Loss)/Profit after tax for the year attributable to equity holders		(603,642)	22,033,729
Other comprehensive income		-	-
Total comprehensive income for the year		<u>(603,642)</u>	<u>22,033,729</u>

The notes on pages 14 to 29 form part of these financial statements.

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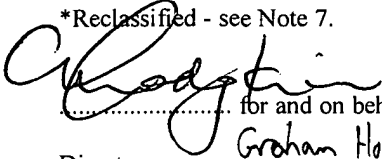
STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2014

	Notes	2014 £	2013 £
Assets			
Non-current assets			
Mortgage loans	6	<u>348,139,328</u>	<u>358,489,002</u>
Current assets			
Mortgage loans	6	6,310,208	10,361,908
Trade and other receivables	7	35,930,513	36,048,116*
Cash and cash equivalents	8	<u>497,145</u>	<u>428,577*</u>
		<u>42,737,866</u>	<u>46,838,601</u>
Total assets		<u>390,877,194</u>	<u>405,327,603</u>
Equity			
Share capital	9	12,502	12,502
Retained loss	9	<u>(53,471,403)</u>	<u>(52,867,761)</u>
Total shareholders' deficit	9	<u>(53,458,901)</u>	<u>(52,855,259)</u>
Non-current liabilities			
Loan notes	10	<u>369,461,027</u>	<u>370,002,324</u>
Total non-current liabilities		<u>369,461,027</u>	<u>370,002,324</u>
Current liabilities			
Loan notes	10	6,310,208	10,361,908
Accrued interest	10	512,480	577,623
Trade and other payables	11	35,307,471	35,426,917
Current tax liability		1,635	1,776
Derivative financial instruments	13	<u>32,743,274</u>	<u>41,812,314</u>
Total current liabilities		<u>74,875,068</u>	<u>88,180,538</u>
Total liabilities		<u>444,336,095</u>	<u>458,182,862</u>
Total equity and liabilities		<u>390,877,194</u>	<u>405,327,603</u>

These financial statements of Deco 12 – UK 4 P.L.c, Company Registration 6105087, on pages 10 to 29 were approved and authorised for issue by the directors on 24/06/2015 and are signed on their behalf by:

*Reclassified - see Note 7.


 for and on behalf of
 Director **Graham Hodgkin**

The notes on pages 14 to 29 form part of these financial statements.

DECO 12 – UK 4 P.L.C

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2014

	Share capital £	Retained loss £	Total equity £
Balance as at 1 January 2014	12,502	(52,867,761)	(52,855,259)
Profit for the year 31 December 2014	-	(603,642)	(603,642)
Other comprehensive income for the year	-	-	-
Balance at 31 December 2014	<u>12,502</u>	<u>(53,471,403)</u>	<u>(53,458,901)</u>

	Share capital £	Retained loss £	Total equity £
Balance as at 1 January 2013	12,502	(74,901,490)	(74,888,988)
Profit for the year 31 December 2013	-	22,033,729	22,033,729
Other comprehensive income for the year	-	-	-
Balance at 31 December 2013	<u>12,502</u>	<u>(52,867,761)</u>	<u>(52,855,259)</u>

The notes on pages 14 to 29 form part of these financial statements.

DECO 12 – UK 4 P.L.C

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2014

	Notes	2014 £	2013 £
Operating activities			
Profit before tax for the year		(603,242)	22,034,156
<i>Adjustments for:</i>			
Fair value movement on derivative financial instrument	13	(9,069,040)	(22,135,710)
Impairment (reversal)/charge against mortgage loans	6	9,674,281	103,690
Bank interest receivable	2	(89,333)	(102,861)
Other income		(38,155)	(125,809)
Interest payable on loan notes		(65,143)	15,028
Increase in trade and other receivables		330,748	(187,878)
(Decrease)/increase in trade and other payables		<u>(165,557)</u>	<u>231,966</u>
Net cash from/(used in) operating activities		(25,441)	(167,418)
 Tax paid		 <u>(541)</u>	 <u>(158)</u>
		<u>(25,982)</u>	<u>(167,576)</u>
 Investing activities			
Repayments of mortgage loans	6	4,727,094	11,999,514
Movements on funds place on deposit		(201,661)*	(32,230,140)*
Other income on mortgage loans		38,155	125,809
Bank interest received		<u>77,848</u>	<u>102,861</u>
Net cash from investing activities		<u>4,641,436</u>	<u>(20,001,956)</u>
 Financing activities			
Repayments of loan notes	10	(4,592,997)	(12,010,085)
Liquidity facility movement		<u>46,111</u>	<u>(1,054,321)</u>
Net cash used in financing activities		<u>(4,546,886)</u>	<u>(13,064,406)</u>
 Net increase/(decrease) in cash and cash equivalents		<u>68,568</u>	<u>(33,233,938)</u>
 Cash and cash equivalents at beginning of year		 <u>428,577*</u>	 <u>33,662,515*</u>
 Cash and cash equivalents at 31 December	8	 <u>497,145</u>	 <u>428,577</u>

Actual cash received and paid as interest income on the mortgage loans and interest expense on the loan notes during the year was £20,309,062 (2013: £21,159,277) and £2,879,198 (2013: £2,782,522) respectively.

*Reclassified - see Note 7.

As explained in the accounting policies on page 15, the cash is not freely available to be used.

The notes on pages 14 to 29 form part of these financial statements.

DECO 12 – UK 4 P.L.C

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2014

1. SIGNIFICANT ACCOUNTING POLICIES

Deco 12 – UK 4 P.L.c is a Company incorporated in the United Kingdom under the Companies Act 2006 and domiciled in England.

Statement of compliance

The Company's financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRSs") as they apply to the financial statements of the Company for the year ended 31 December 2014.

The accounting policies set out below have been applied in respect of the financial year ended 31 December 2014.

Basis of preparation

The financial statements have been prepared on the historical cost basis as modified for the revaluation of certain financial instruments under IAS 39 Financial Instruments: Recognition and Measurement.

The financial statements are presented in Pounds Sterling.

Due to the fact that the nature of the business is to provide finance, the directors are of the opinion that it is more appropriate to use interest income and interest expense rather than turnover and cost of sales in preparing the Statement of Comprehensive Income.

Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out above. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are set out in the financial statements. In addition, notes 1 and 12 to the financial statements include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; and its exposures to credit risk and liquidity risk.

The Company has net liabilities of £53,458,901 (2013: £52,855,259) as a result of impairments of £15,228,303 (2013: £5,554,022) on the loan assets and derivative liabilities of £32,743,274 (2013: £41,812,314) held at fair value. However, the terms of the loan notes are limited recourse and therefore the Company is only obliged to repay the notes to the extent that the Company receives cash from the loan assets. The note holders will therefore ultimately bear the Company's deficits on maturity of the notes.

Due to the limited recourse nature of the loan notes, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

Critical accounting judgements and key sources of estimation uncertainty

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. In particular, for the fair value of derivatives (note 13) and the recoverability of assets (note 6), the estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements and carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates used in the financial statements.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year or in the year of the revision and future years if the revision affects both the current and future years.

DECO 12 – UK 4 P.L.C

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments

The Company's financial instruments comprise mortgage loans, cash and liquid resources, derivatives, loan notes and various receivables and payables that arise directly from its operations. The main purpose of the loan notes is to finance the beneficial interest in a mortgage portfolio. These financial instruments are classified in accordance with the principles of IAS 39 Financial Instruments: Recognition and Measurement as described below.

Mortgage loans

The mortgage loans are classified as loans and receivables and are initially measured at fair value with subsequent measurement being at amortised cost using the effective interest method.

Impairment

Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. The allowance is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate computed at initial recognition.

Derecognition of financial assets

The Company derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Company neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Company recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Company retains substantially all the risks and rewards of ownership of a transferred financial asset, the Company continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Deferred consideration

A deferred consideration charge is included in interest expense. Deferred consideration is payable to the Class X certificate holders, dependent on the extent to which the surplus income, in excess of the agreed margin, generated by the mortgage loans in which the Company has purchased an interest, exceeds the administration costs of the mortgage loans.

Cash and cash equivalents

Cash and cash equivalents in the Statement of Financial Position comprise cash at banks and in hand and short-term deposits with an original maturity of three months or less. All withdrawals from the Company's bank accounts are restricted by the detailed priority of payments set out in the securitisation agreements and as such the cash and cash equivalents are not freely available to be used for other purposes.

Derivative financial instruments and hedging activities

The Company uses derivative financial instruments to hedge its exposure to interest rate risk arising from operational, financing and investment activities. In accordance with its treasury policy, the Company does not hold or issue derivative financial instruments for trading purposes. Derivatives are accounted for as held for trading.

IAS 39 requires all financial assets and liabilities to be recognised initially at fair value on the Statement of Financial Position. Subsequent to initial recognition, any changes in fair value of the derivatives held are recognised in the Statement of Comprehensive Income.

The fair value of interest rate swaps and basis swaps is the estimated amount that the Company would receive or pay to terminate the swap at the reporting date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Derivative financial instruments and hedging activities (continued)

Interest income receivable or interest expense on the interest rate swap is accounted for on an effective interest rate basis within interest income or interest expense in the Statement of Comprehensive Income.

Loan notes

Loan notes are classified as other financial liabilities and recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, loan notes are stated at amortised cost with any difference between cost and redemption value being recognised in the Statement of Comprehensive Income over the period of the borrowings on an effective interest basis.

Embedded derivatives

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host instrument, and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivatives recognised in the Statement of Comprehensive Income. Depending on the classification of the host instrument, the host is then measured in accordance with IAS 39.

Interest income and expense

Interest income and expense is accounted for on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial asset or liability to that asset's or liability's net carrying amount.

Value added tax

Value added tax is not recoverable by the Company and is included with its related cost.

Income tax expense

Income tax in the Statement of Comprehensive Income for the year comprises current and deferred tax. Income tax is recognised as expense or gain except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

Standards issued and adopted during the year

All new and amended accounting standards which have become effective for the current year have been adopted but have had no material effect on the reported performance, financial position or disclosures of the Company, therefore these standards have not been listed separately.

Standards issued, not yet effective and not early adopted

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective (and in some cases had not yet been adopted by the EU):

IFRS 9 Financial Instruments
IFRS 14 Regulatory Deferral Accounts
IFRS 15 Revenue from Contracts with Customers
Annual Improvements to IFRSs: 2012-14 Cycle
Annual Improvements to IFRSs: 2011-13 Cycle
Annual Improvements to IFRSs: 2010-12 Cycle

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

1. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Standards issued, not yet effective and not early adopted

The directors do not expect that the adoption of the Standards and Interpretations listed above will have a material impact on the financial statements of the Company in future periods, except that IFRS 9 will impact both the measurement and disclosures of financial instruments.

Beyond the information above, it is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

Segmental reporting

The principal asset of the Company is the beneficial interest in the mortgage portfolio originated in the United Kingdom which is funded by loan notes issued in the United Kingdom. The directors do not consider it necessary to provide a further analysis of the results of the Company from those already disclosed in these financial statements.

2. INTEREST INCOME

	2014	2013
	£	£
Income from mortgage loans	19,978,314	21,356,155
Bank interest received	89,333	102,861
Other income	38,155	125,809
	<u>20,105,802</u>	<u>21,584,825</u>

3. INTEREST EXPENSE

	2014	2013
	£	£
Net swap interest payable	15,806,257	16,651,396
Interest on loan notes	2,814,055	2,797,550
Bank charges	442	-
Deferred consideration	663,407	1,236,271
	<u>19,284,161</u>	<u>20,685,217</u>

4. OTHER OPERATING EXPENSES

	2014	2013
	£	£
Administration and cash management fees	679,980	758,385
Audit fees for audit of the Company's accounts	25,476	24,000
Fees paid for tax services	9,270	9,270
Corporate services fees	104,916	105,817
	<u>819,642</u>	<u>897,472</u>

Directors' emoluments amounted to £2,400 (2013: £2,400), being £1,200 (2013: £1,200) each, for their services as directors to the Company during the year with £nil (2013: £600) unpaid at year end. The directors had no material interest in any contract of significance in relation to the business of the Company (2013: none). The Company did not have any employees in the current year (2013: none).

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

5. INCOME TAX CHARGE

The Company has elected to be taxed under the Taxation of Securitisation Companies 2006 (Regulations) i.e. the “permanent regime”. Corporation tax is therefore calculated by reference to the profit of the Company required to be retained in accordance with the pre-enforcement priority of payments as defined in the terms and conditions of the loan notes.

The directors are satisfied that this Company meets the definition of a ‘securitisation company’ as defined by both The Finance Act 2005 and the subsequent secondary legislation and that no incremental unfunded tax liabilities will arise.

	2014	2013
	£	£
Current tax:		
Corporation tax charge for the year at a rate of 20% (2013: 20%)	400	427
(Over)/under provision of the prior year charge	-	-
Total income tax charge in Statement of Comprehensive Income	<u>400</u>	<u>427</u>
Reconciliation of total tax charge		
	2014	2013
	£	£
The tax assessed for the year is at the standard rate of corporation tax in the UK of 20% (2013: 20%)		
(Loss)/Profit before tax	<u>(603,242)</u>	<u>22,034,156</u>
(Loss)/Profit before tax multiplied by the standard rate of corporation tax in the UK of 20% (2013: 20%)	120,648	(4,406,831)
(Over)/under provision of the prior year charge	-	-
Permanent differences relating to application of Taxation of Securitisation Companies Regulations 2006	<u>(120,248)</u>	<u>4,407,258</u>
Total tax charge reported in the Statement of Comprehensive Income	<u>400</u>	<u>427</u>

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

6. MORTGAGE LOANS

	2014 £	2013 £
At 1 January	368,850,910	380,954,114
Decrease /(increase) in the impairment provision during the year	(9,674,281)	(103,690)
Redemptions	(4,727,094)	(11,999,514)
At 31 December	<u>354,449,536</u>	<u>368,850,910</u>

The balance can be analysed as follows:

Current assets	6,310,208	10,361,908
Non-current assets	<u>348,139,328</u>	<u>358,489,002</u>
	<u>354,449,536</u>	<u>368,850,910</u>

The movement of the impairment provision can be analysed as follows:

At 1 January	(5,554,022)	(5,450,332)
Provisions made during the year	(10,273,675)	(151,378)
Reversal during the year	599,394	47,688
At 31 December	<u>(15,228,303)</u>	<u>(5,554,022)</u>

The mortgage loans are classified as “loans and receivables”. The mortgage loans are due for repayment between January 2015 and January 2017. At 31 December 2014, the fixed rate of interest on the mortgage loans ranged from 5.39% to 6.42% (2013: 5.39% to 6.42%). The loans are secured over commercial properties. Deutsche Bank AG, London Branch acts as security trustee for the loans.

The Company assesses at each reporting date whether there is any objective evidence that a financial asset is impaired. A financial asset or portfolio of financial assets is impaired and an impairment loss is incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset. The impairment represents the estimated difference between the market valuation of the collateral and the loan outstanding. As at 31 December 2014 the total impairment provision recognised was £15,228,303 (2013: £5,554,022) and the impairment charge recognised during the year amounted to £9,674,281 (£2013: £103,690).

Borehamwood loan: The loan was placed into special servicing following its default in October 2011 when it breached the interest payment date covenant test. The loan subsequently defaulted on its 21 April 2014 maturity date. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 24 April 2012 by the special servicer and the impairment provision recognised at 31 December 2013 was GBP 5,554,022. The special servicer sold the underlying property in January 2015 and a final amount of GBP 6,235,208 was recovered. These proceeds were used as the estimated market value as at 31 December 2014. An impairment reversal of GBP 599,394 was recognised during the year, based on the final recovery amount and a loan principal of GBP 11,189,836, resulting in an impairment provision recognised at 31 December 2014 of GBP 4,954,628.

2006/2007 Regent Capital Spectrum IV & V loan: The loan was placed into special servicing in March 2015 after the borrower breached an obligation in July 2014. This obligation required the borrower to have secured a tenant contributing a minimum of GBP 830,000 per annum rental income through an occupational lease. As such, an impairment assessment was carried out on the loan for the first time this year end because no impairment provision had been recognised at 31 December 2013. The property was last valued on 19 December 2006. A charge of GBP 10,273,675 was recognised during the year, based on the estimated market value of the collateral at 31 December 2014 of GBP 814,325 and a loan principal of GBP 11,088,000, resulting in an impairment provision recognised at 31 December 2014 of GBP 10,273,675. The estimated market value of the collateral was derived from comparable recent property sales in the area.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

6. MORTGAGE LOANS (Continued)

Tesco Red Partnership loan: The loan is performing as per the terms of the loan agreement and financial covenants and there has been no history of impairment on the loan; therefore, no impairment assessment has been carried out and no impairment is held against the loan at 31 December 2014.

7. TRADE AND OTHER RECEIVABLES

	2014 £	2013 £
Other debtors	2,540	2,540
Prepayments and accrued income	3,484,688	3,815,436
Funds place on deposit	32,431,801	32,230,140
Bank interest income receivable	11,484	-
	<u>35,930,513</u>	<u>36,048,116</u>

The directors consider that the carrying value of trade and other receivables approximates to their fair value.

The comparative figure for 2013 for funds placed on deposit has been reclassified from cash and cash equivalents as the directors believe this to be a more appropriate representation of the balance.

The funds of £32,431,801 (2013: £32,230,140), obtained primarily from the liquidity facility drawing and placed on deposit, were invested in short-term investment securities. These investments attract interest on a daily basis and mature at least one business day prior to the next quarterly interest payment date ("IPD") and have been included in the debtor balance as 'Funds placed on deposit'.

8. CASH AND CASH EQUIVALENTS

	2014 £	2013* £
Cash and cash equivalents	<u>497,145</u>	<u>428,577</u>

*Reclassified - see Note 7.

The directors consider that the carrying value of cash and cash equivalents approximates to their fair value.

9. TOTAL EQUITY

	Issued capital £	Retained loss £	Total £
At 1 January 2014	12,502	(52,867,761)	(52,855,259)
Profit for the year	-	(603,642)	(603,642)
Balance at 31 December 2014	<u>12,502</u>	<u>(53,471,403)</u>	<u>(53,458,901)</u>

There are 50,000 authorised ordinary shares of £1 each. The issued share capital comprises two fully paid £1 shares, and 49,999 ordinary shares quarter paid. Castlewoods CS Holdings Limited holds one fully paid £1 share under a declaration of trust for charitable purposes. The remaining 49,999 shares are held by Deco 12 – UK 4 Holding Limited.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

10. LOAN NOTES

This note provides information about the contractual terms of the Company's interest-bearing loan notes. For more information about the Company's exposure to interest rate risk, see note 12.

	2014 £	2013 £
At 1 January	380,364,232	392,374,317
Redemptions	<u>(4,592,997)</u>	<u>(12,010,085)</u>
	<u>375,771,235</u>	<u>380,364,232</u>
Non-current liabilities		
Loan notes	<u>369,461,027</u>	<u>370,002,324</u>
	<u>369,461,027</u>	<u>370,002,324</u>
Current liabilities		
Loan notes	6,310,208	10,361,908
Interest payable on loan notes	<u>512,480</u>	<u>577,623</u>
	<u>6,822,688</u>	<u>10,939,531</u>

Current liabilities due within one year are paid when cash is available after other commitments have been fulfilled in order of priority in accordance with the Offering Circular.

The loan notes are secured by way of fixed and floating charges over the Company's assets.

On 13 March 2007, an agreement was entered into with Danske Bank A/S (London Branch) for the provision of a liquidity facility for the Company. The facility is in place to allow the Company to meet its obligations should there be a shortfall in the revenue or principal received from the mortgage loans on a temporary basis. At 31 December 2014, an amount of £32,331,838 (2013: £32,285,727) of liquidity facility was drawn. At year-end, the liquidity facility was drawn to accommodate the 'Interest Shortfall' that arose on the defaulted interest payments on mortgage loans.

In 2013, Danske Bank A/S (London Branch) was downgraded below the Requisite Rating and as per Liquidity Facility Agreement; a Stand-by-Drawing amounting to £33,330,644 was made. During the year ended 31 December 2014, an amount of £46,111 (2013: Repayment of £1,044,917) was drawn.

The liquidity facility for £32,331,838 (adjusted for appraisal reduction) was renewed for the period from 5 March 2015 to expire on 2 March 2016. The directors expect this facility to be renewed annually. The liquidity facility is secured by way of fixed and floating charges over the Company's assets including the mortgage loans and loan notes.

The loan notes are denominated in Sterling.

On 13 March 2007, the Company issued the following class of Notes.

Class of Notes	Currency	Issue price	Interest	Margin	Maturity
A1	GBP	475,000,000	3 month Libor	0.16%	January 2020
A2	GBP	115,000,000	3 month Libor	0.19%	January 2020
B	GBP	35,000,000	3 month Libor	0.27%	January 2020
C	GBP	28,000,000	3 month Libor	0.43%	January 2020
D	GBP	16,000,000	3 month Libor	0.75%	January 2020
E	GBP	2,750,000	3 month Libor	1.00%	January 2020
F	GBP	1,133,707	3 month Libor	3.00%	January 2020

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

10. LOAN NOTES (Continued)

At the reporting date, the outstanding amount for each class of Notes were as shown in table below.

Class of Notes	2014	2013
	£	£
A1	180,315,764	184,908,761
A2	113,588,832	113,588,832
B	34,570,514	34,570,514
C	27,656,411	27,656,411
D	15,803,664	15,803,664
E	2,716,255	2,716,255
F	1,119,795	1,119,795
	<u>375,771,235</u>	<u>380,364,232</u>

The notes are secured by way of a fixed and floating charge over the assets of the Company. The proceeds of the notes were used by the Company to acquire the mortgage loans from Deutsche Bank AG in accordance with the terms of the securitisation documents.

11. TRADE AND OTHER PAYABLES

	2014	2013
	£	£
Current liabilities		
Accruals and deferred income	2,985,705	3,074,558
Liquidity facility loan	32,331,838	32,285,727
Deferred consideration	(10,072)	66,632
	<u>35,307,471</u>	<u>35,426,917</u>

Current liabilities due within one year are paid when cash is available after other commitments have been fulfilled, in order of priority in accordance with the Offering Circular.

The directors consider that the carrying amount of trade and other payables approximates to their fair value.

12. FINANCIAL RISK MANAGEMENT

The principal risks and uncertainties are set out in the Strategic Report on pages 2 to 5.

Financial instruments

The Company's financial instruments, other than derivatives, comprise a portfolio of commercial mortgage loans, cash and liquid resources, interest-bearing borrowings and various receivables and payables that arise directly from its operations. The Company also enters into derivative transactions (principally interest rate swaps). The purpose of such transactions is to manage the interest rate risks arising from the Company's operations and its sources of finance. It is, and has been throughout the year under review, the Company's policy that no trading in financial instruments is undertaken.

Interest rate risk

The Company is exposed to movements in interest rates and manages this exposure using interest rate swaps. More specifically, the Company is exposed to basis risk due to the timing difference in interest payment dates on the loan notes and the mortgage loans and interest rate risk due to any variance between the fixed rate of interest receivable on the mortgage loans and the variable rate of interest payable on the loan notes. This risk exposure is hedged using interest rate swaps that are taken out on inception of the securitisation. As such, the directors do not believe that the Company has any significant interest rate re-pricing exposure and therefore have not presented a sensitivity analysis to interest rate risk.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

12. FINANCIAL RISK MANAGEMENT (Continued)

Credit risk

The principal credit risk to the Company is that the borrowers will not be able to meet their obligations as they fall due. The mortgage loans are secured on a number of UK commercial properties which are geographically diverse and include a diverse tenant portfolio.

The most significant concentration of credit risk is considered to be a mortgage loan to Tesco Red Partnership totalling £347,400,000 (2013: Tesco Red Partnership: £347,400,000). At 31 December 2014, the total gross amount outstanding on the mortgage loans was £369,677,836 (2013: £374,404,932). The mortgage loan portfolio consists of three loans secured over 19 properties (2013: 3 loans secured over 22 properties). The three loans are referred to in these financial statements as the Tesco Red Partnership loan, the Borehamwood loan and the 2006/2007 Regent Capital Spectrum IV & V loan.

All 16 of the Tesco Red Partnership loan underlying properties are let to one tenant, Tesco Stores Limited, and the obligations of the latter under related leases are guaranteed by Tesco Plc which is rated BBB- (2013: A-), Ba1- (2013: Baa1), BBB (2013:A-) by Fitch, Moody's and S&P respectively. The downgrade reflected the opinion that Tesco Plc's profitability is expected to continue to weaken because of market competition in the United Kingdom which will remain persistently high over the next 12 months. Nonetheless, the Tesco Red Partnership loan is performing as per the respective terms set out in the loan agreement and the estimated market value of the underlying properties is still higher than the carrying value of the loan. Therefore, the Tesco Red Partnership loan has not been impaired as at year end.

The carrying amount of financial assets represents the maximum credit exposure. See note 6 for impairment analysis.

The underlying mortgage loans are secured by first charge over commercial property located in England, Wales and Scotland.

The table below sets out the carrying amount, the collective impairments and approximate fair value of collateral held against exposures to customers. The estimate of fair value is based on the most recent valuation performed at different dates for each property and are indexed at 31 December 2014 using the UK IPD property index, except for impaired loans where the directors' estimate of the collateral value was lower than the indexed valuation.

The credit quality of the underlying mortgage loans is summarised as follows:

	Gross carrying amount 2014 £	Impairment 2014 £	Fair value of collateral 2014 £	Gross carrying amount 2013 £	Impairment 2013 £	Fair value of collateral 2013 £
Neither past due nor impaired	347,400,000	-	403,550,524	358,563,000	-	377,973,656
Impaired	<u>22,277,838</u>	<u>(15,228,303)</u>	<u>7,049,535</u>	<u>15,841,930</u>	<u>(5,554,020)</u>	<u>10,287,910</u>
	<u>369,677,838</u>	<u>(15,228,303)</u>	<u>410,600,059</u>	<u>374,404,930</u>	<u>(5,554,020)</u>	<u>388,261,566</u>

The allowance for impairment disclosed above excludes impairment relating to written-off mortgage loans, therefore differs from the cumulative impairments disclosed in note 6 of these financial statements.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

12. FINANCIAL RISK MANAGEMENT (Continued)

Credit risk (continued)

With regard to credit risk on derivatives, the directors monitor the credit rating of the swap provider and in case of any downgrade may require the swap provider to provide sufficient collateral or transfer its obligations to another bank of a better credit rating.

Prepayment risk

Prepayment risk on the mortgage loans arises when these are voluntarily prepaid by the relevant borrower or borrowers thereof. With respect to all of the loans, such prepayment is contingent upon the payment of a prepayment fee.

Liquidity risk

Interest receipts on the mortgage loans may, under certain circumstances, be delayed. Such delays could adversely offer the ability of the Company to make timely payments of interest on the loan notes. In order to protect itself against this risk, the Company entered into a liquidity facility agreement with Danske Bank A/S (London Branch) on 13 March 2007, as described in note 10.

Moreover, the maturity of the loan notes is designed to match the maturity of the mortgage loans and hence, there are deemed to be limited liquidity risks facing the Company.

The redemption of the notes is dependent on the receipt of payments on the mortgage loans. In accordance with the respective Prospectus for each of the loan notes, Class A1 Notes will be redeemed in priority to redemption of the remaining classes of notes followed by Class A2, B, C, D, E and Class F.

The table below reflects the undiscounted contractual cash flows of non derivative financial liabilities at the reporting date. Interest payable on loan notes was estimated based on the floating rates as at 31 December 2014.

As at 31 December 2014	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
Loan notes	375,771,235	375,771,235	6,197,686	112,522	369,461,027
Interest payable on loan notes	512,480	6,097,478	717,472	2,271,933	3,108,073
Liquidity drawn down	<u>32,331,838</u>	<u>32,331,838</u>	<u>32,331,838</u>	<u>-</u>	<u>-</u>
Total non-derivative financial instruments	<u>408,615,553</u>	<u>414,200,551</u>	<u>39,246,996</u>	<u>2,384,455</u>	<u>372,569,100</u>

As at 31 December 2013	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
Loan notes	380,364,232	380,364,232	3,702,262	6,659,646	370,002,324
Interest payable on loan notes	577,623	8,579,180	773,845	2,084,675	5,720,660
Liquidity draw down	<u>32,285,727</u>	<u>32,285,727</u>	<u>32,285,727</u>	<u>-</u>	<u>-</u>
Total non-derivative financial instruments	<u>413,227,582</u>	<u>421,229,139</u>	<u>36,761,834</u>	<u>8,744,321</u>	<u>375,722,984</u>

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

12. FINANCIAL RISK MANAGEMENT (Continued)

Liquidity risk (Continued)

The above undiscounted contractual cash flows have been based on the assumptions that the repayment of the loan notes follows the same trend as the principal repayments on mortgage loans. The mortgage loans that are past due their legal maturity date have been assumed to be repayable in full within the next payment date.

The table below reflects the undiscounted contractual cash flows of derivative financial instruments at the reporting date.

As at 31 December 2014	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
	32,743,274	32,264,503	3,919,463	11,758,390	16,586,650
As at 31 December 2013	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
	41,812,314	48,116,099	4,088,199	12,264,596	31,763,304

Currency risk

All of the Company's assets and liabilities are denominated in Pound Sterling therefore there is no foreign currency risk.

Capital risk management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern. The Company is not subject to any external capital requirements. The gearing ratio was 124.4% (2013: 118.8%) for the year ended 31 December 2014.

Fair value, methodology and assumptions

Fair value

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. an exit price). The fair value of financial instruments is always determined on the basis of the listed price on an active market (mark to market) or, if this is not possible, on the basis of industry standard valuation models (mark to matrix or mark to model).

Financial instruments valued using observable market prices

If a quoted market price in an active market is available for an instrument, the fair value is calculated based on the market price.

Financial instruments valued using a valuation technique

In the absence of a quoted market price in an active market, management uses industry standard models to make its best estimate of the price that the market would set for that financial instrument. In order to make these estimations, various techniques are employed, including extrapolation from observable market data and observation of similar financial instruments with similar characteristics. Wherever possible, valuation parameters for each product are based on prices directly observable in active markets or that can be derived from directly observable market prices.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

12. FINANCIAL RISK MANAGEMENT (Continued)

Fair values, methodology and assumptions (Continued)

The Company did not make any material changes to the valuation techniques and industry standard models it used during the year ended 31 December 2014.

Fair value hierarchy

The Company applies the following fair value hierarchy that prioritises the inputs to valuation techniques used in measuring fair value. The hierarchy establishes three categories for valuing financial instruments, giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs.

Level 1 - Unadjusted quoted prices for identical assets or liabilities in an active market that the Company has the ability to access at the measurement date.

Level 2 - Quoted prices in markets that are not active, quoted prices for similar assets or liabilities, recent market transactions, inputs other than quoted market prices for the asset or liability that are observable either directly or indirectly for substantially the full term, and inputs to valuation techniques that are derived principally from or corroborated by observable market data through correlation or other statistical means for substantially the full term of the asset or liability.

Level 3 - Inputs to the pricing or valuation techniques that are significant to the overall fair value measurement of the asset or liability are unobservable.

The methodology and assumptions used in estimating the fair value of financial instruments are disclosed below. The only financial instruments held at fair value on the Statement of Financial Position are derivatives. The derivatives all fall within the level 2 fair value hierarchy.

The fair value of the derivatives held by the Company is calculated using the Overnight Indexed Swap (OIS) methodology which is based on observable inputs. For OIS methodology, discounting is calibrated to the rates structure of the prevailing market interest rate where the derivatives are originated, that is, United Kingdom. Therefore, the Sterling Overnight Interbank Average Rate (SONIA), an index that tracks Sterling Overnight funding rates, is used.

Below are the fair values of the financial instruments of the Company as at 31 December 2014 and 31 December 2013.

	Notes	Carrying amount 2014 £	Fair value 2014 £	Carrying amount 2013 £	Fair value 2013 £
Mortgage loans	6	354,449,536	382,717,303	368,850,910	380,771,273
Trade and other receivables	7	35,930,513	35,930,513	36,048,116*	36,048,116*
Cash and cash equivalents	8	497,145	497,145	428,577*	428,577*
Total assets		<u>390,877,194</u>	<u>419,144,961</u>	<u>405,327,603</u>	<u>417,247,966</u>
Loan notes	10	(375,771,235)	(349,974,029)	(380,364,232)	(338,958,959)
Interest payable	10	(512,480)	(512,480)	(577,623)	(577,623)
Derivative financial instruments	13	(32,743,274)	(32,743,274)	(41,812,314)	(41,812,314)
Trade and other payables	11	(35,307,471)	(35,307,471)	(35,426,917)	(35,426,917)
Current tax liability		(1,635)	(1,635)	(1,776)	(1,776)
Total liabilities		<u>(444,336,095)</u>	<u>(418,538,889)</u>	<u>(458,182,862)</u>	<u>(416,777,589)</u>

*Reclassified - see Note 7.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

12. FINANCIAL RISK MANAGEMENT (Continued)

Fair values, methodology and assumptions (Continued)

The fair value of the loan notes is based on observable inputs given that these notes are listed on the Irish Stock Exchange and hence a market price is available for each class of loan notes excluding Class E and Class F notes. For those classes of notes for which a market price is not available, the percentage market price for the Class D notes has been taken since these notes have all been categorised as junior notes. However, given that the loan notes are thinly traded, the market price is manually adjusted for large moves, backwardation and general price challenges received. Therefore the loan notes have been categorised as level 2 financial instruments.

The fair value of mortgage loans are based on fair value of loan notes and derivatives that wherever possible have been estimated using quoted market prices for instruments as described above. Hence the mortgage loans have been deemed to a level 2 instruments as well. The carrying values of cash and cash equivalents, trade and other receivables, interest payable, trade and other payables and current tax liability are a reasonable approximation of the fair values of these instruments.

Hierarchy levels

Financial instruments recognised and measured at fair value

As at 31 December 2014	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Liabilities				
Derivative financial instruments	<u>(32,743,274)</u>	-	<u>(32,743,274)</u>	-

Financial instruments at amortised cost whose fair value is disclosed

As at 31 December 2014	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Assets				
Mortgage loans	<u>382,717,303</u>	-	<u>382,717,303</u>	-
Liabilities				
Loan notes	<u>(349,974,029)</u>	-	<u>(349,974,029)</u>	-

Financial instruments recognised and measured at fair value

As at 31 December 2013	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Liabilities				
Derivative financial instruments	<u>(41,812,314)</u>	-	<u>(41,812,314)</u>	-

Financial instruments at amortised cost whose fair value is disclosed

As at 31 December 2013	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Assets				
Mortgage loans	<u>380,771,273</u>	-	<u>380,771,273</u>	-
Liabilities				
Loan notes	<u>(338,958,959)</u>	-	<u>(338,958,959)</u>	-

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

12. FINANCIAL RISK MANAGEMENT (Continued)

Fair values, methodology and assumptions (Continued)

During the year ended 31 December 2014, there have been no transfers between fair value hierarchy levels (2013: £none). In addition, there were no financial instruments that have been classified as level 3 and hence there is no need to disclose reconciliation of assets and liabilities categorised as level 3 instruments.

Interest rate risk profile of financial liabilities

All of the Company's financial liabilities are floating rate and carry interest rates based on the relevant three-month LIBOR rate.

Effective interest rates and repricing analysis

The following table details the Company's exposure to interest rate risk by the earlier of contractual maturities or re-pricing:

At 31 December 2014	Weighted average effective interest rate %	Floating interest £	Non- interest bearing £	Fixed rate £	Total £
Assets					
Trade and other receivables	-	32,431,801	3,498,712	-	35,930,513
Mortgage loans	5.2932%	6,235,210	-	348,214,325	354,449,535
Cash and cash equivalents	-	497,145	-	-	497,145
Total assets		<u>39,164,156</u>	<u>3,498,712</u>	<u>348,214,325</u>	<u>390,877,193</u>
Liabilities					
Accruals and tax liabilities	-	-	35,309,106	-	35,309,106
Derivative financial instruments	-	32,743,274	-	-	32,743,274
Loan notes	0.7955%	375,771,235	-	-	375,771,235
Total liabilities		<u>408,514,509</u>	<u>35,309,106</u>	<u>-</u>	<u>443,823,615</u>
At 31 December 2013					
Assets					
Trade and other receivables	-	32,230,140*	3,817,976*	-	36,048,116*
Mortgage loans	5.434%	-	-	368,850,910	368,850,910
Cash and cash equivalents	-	428,577*	-	-	428,577*
Total assets		<u>32,658,717</u>	<u>3,817,976</u>	<u>368,850,910</u>	<u>405,327,603</u>
Liabilities					
Accruals and tax liabilities	-	-	35,428,693	-	35,428,693
Derivative financial instruments	-	41,812,314	-	-	41,812,314
Loan notes	0.7515%	380,364,232	-	-	380,364,232
Total liabilities		<u>422,176,546</u>	<u>35,428,693</u>	<u>-</u>	<u>457,605,239</u>

*Reclassified - see Note 7.

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NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 31 DECEMBER 2014

13. DERIVATIVE FINANCIAL INSTRUMENTS

The net fair values of derivative financial instruments at the reporting date were:

	2014	2013
	£	£
Interest rate swaps fair value at start of year	(41,812,314)	(63,948,024)
Change in fair value	<u>9,069,040</u>	<u>22,135,710</u>
Interest rate swaps fair value at end of year	<u>(32,743,274)</u>	<u>(41,812,314)</u>

The notional principal amount of all the outstanding interest rate swap contracts at 31 December 2014 was £717,957,854 (2013: £740,774,559). The Company pays a fixed rate ranging from 4.89% to 5.17% (2013: 4.89% to 5.17%) and receives 3-month LIBOR (2013: 3-month LIBOR).

In accordance with IAS 39 'Financial instruments: Recognition and measurement', the Company has reviewed all contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard.

The Company has the ability to redeem the loan notes in full or part at their then principal amount outstanding, together with interest accrued to the date of redemption, on any interest payment date. The Company effectively has a call option on the loan notes exercisable on certain dates. The option constitutes an embedded derivative; however, as this is closely related to the underlying host contract (the loan notes) consistent with IAS 39, the option does not require separation. A similar hybrid instrument arises on the mortgage loan whereby the Company has effectively sold a put option on the mortgage loan exercisable on certain dates. As this option is considered to be closely related to the underlying host contract, it does not require separation.

14. RELATED PARTY TRANSACTIONS

The Company is a special-purpose vehicle controlled by its Board of directors; Mr Graham Cox and Mr Graham Hodgkin are directors of the Company. Directors' emoluments during the year amounted to £2,400 (2013: £2,400) for their services as directors to the Company during the year. The Company paid corporate service fee to Deutsche Bank AG, London Branch, in connection with corporate services received. The fees payable to them for their services for the year ended 31 December 2014 amounted to £16,843 (2013: £19,902 with £5,258 (2013: £7,428) still unpaid at year end.

15. ULTIMATE PARENT UNDERTAKING

Deco 12 – UK 4 Plc is a company incorporated in the United Kingdom and registered in England and Wales.

Deco 12 – UK 4 Holding Limited holds 49,999 shares in the Company. Castlewood CS Holdings Limited held one share in Deco 12 – UK 4 Plc and the entire share capital in Deco 12 – UK 4 Holding Limited under a declaration of trust for charitable purposes.

16. SUBSEQUENT EVENTS

In January 2015, the property securing the Borehamwood loan was sold for GBP 6,575,000, with the net proceeds used to repay the loan.