Castle Trust Bank

# Castle Trust Capital plc

## Annual financial statements for the year ended 30 September 2022

## Registered No: 07454474

Macfarlanes LLP
20 Cursitor Street
London
EC4A 1LT

# Castle Trust Capital plc

## Strategic report, directors' report and financial statements

**For the year ended 30 September 2022**

**Contents** | **Page**

## Corporate information

**Registered No: 07454474**

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Mr Richard Alan Pym

Mr Andrew Spencer Doman

Mr Timothy John Hanford

Mr Martin Paul Bischoff

Mr Paul Lloyd-Jones

Ms Marian Macdonald Martin

Mr Eric Edward Anstee

Ms Melba Margaret Montague

Mr Tughan Alioglu

Mr Kenneth John Stannard (Appointed 1 July 2022)

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Mr Andrew Macdonald

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# Strategic report

The directors present their strategic report and financial statements of Castle Trust Capital plc (the "Company", "Castle Trust Bank", the "Bank" or "CTC") for the year ended 30 September 2022.

In October 2020, the share capital of the Company was sold by Castle Trust Holdings (Jersey) Limited to Castle Trust Holdings Limited ("CTH") which became the Company's new immediate parent. CTH is now the Group consolidating entity. ("the Group").

## Our Purpose

Castle Trust Bank is a specialist bank with a simple purpose: to help customers achieve their financial goals. Our purpose is particularly significant because many of our customers are not well served by mainstream financial services. We are here to help customers by:

- Doing our bit to alleviate the UK's housing crisis by financing the building of new homes,
- *Providing homeowners and landlords with specialist solutions to match their individual financial needs, and*
- Providing a secure home for people's savings.

**Did you know?**
Castle Trust Bank:

- Helped to build more than 300 new homes over the last two years;
- Assisted more than 1,000 homeowners and landlords in 2022; and
- Provided a safe and secure home for the savings of approximately 19,000 savers in the last year.

Everyone who works for Castle Trust Bank contributes to our purpose, creating a unique One Bank culture which is critical to the business's success. Castle Trust Bank's culture is underpinned by its values, which are celebrated and promoted whether it is the little things we do on a daily basis or recognising colleagues who have gone above and beyond in our monthly and annual awards. Castle Trust Bank wants to be The Place To Work, a place where all colleagues can thrive and grow as they contribute to our purpose. Our home is in Basingstoke, and in 2022 we became a core sponsor of Destination Basingstoke, a not-for-profit organisation that creates community events. We plan to grow our contribution to the community whilst becoming the employer of choice in the district of Basingstoke and Deane.

**Our Values**
We are passionate about living our values which are:

- Putting Customers First
- Forward Thinking
- Professional Pride
- Achieve Together
- Open and Transparent

# Business Model and Strategy

Castle Trust Bank is a specialist finance provider in the UK and considers its expertise is its ability to deliver products that are valuable for customers but not offered by the traditional banking industry. The Bank competes in business segments that are experiencing sector specific growth and have the ability to deliver attractive shareholder returns relative to the risks that they represent. This is supplemented by knowledge of the distribution networks in which the Bank operates, the strength of Castle Trust Bank's underwriting and superior market insight. This has enabled the Bank to deliver competitive pricing in both lending and deposit taking products relative to its peers.

Castle Trust Bank principally provides mortgage finance (which includes residential development finance ("RDF")). These flexible lending solutions are currently funded using savings from retail customers.

The way we do business is underpinned by our values. We place the highest importance on treating our customers, and colleagues fairly, not just because it's the right thing to do but because we know that the trust of our customers and colleagues is crucial to the Company's future success.

**Property – one of the leading specialist UK property lenders**

We are one of the leading specialist UK property lenders. We are doing our bit to help alleviate the UK's housing crisis by financing the provision of new homes and providing homeowners and landlords with specialist solutions to match their individual financial needs. Our property business is based on innovative products with attractive returns, high repeat business and an established position in growing segments. We are competitively priced across the specialist mortgage sector and look to dominate in target areas. The return we earn more than compensates for the risk we take, and we have the confidence to amend volumes as opportunities arise. We serve the full spectrum of the lending cycle from bridging through to development, bridge to let exit and buy-to-let.

We source business from our strong and growing relationships with the main specialist intermediaries and the main networks and mortgage club panels. We work with a trusted panel of solicitors for introducing title insurance and offer exclusive products to our key introducers. We are recognised for our high service levels (speed and certainty of lending) enabled by technology, with a pragmatic approach to underwriting utilising digital technology. This is exemplified by our broker portal, which enables online submission and management of cases. It is important that we continually invest in new technology to capture further opportunities to accelerate our lending decisions and the quality of service we offer to our customers. With this in mind, we have set aside a significant budget to invest in the latest origination technology. Not only will this deliver an enhanced customer experience, but it will also automate more of our lending and provide the capability for us to launch new products.

In Property Finance, the product range encompasses both first and second charge lending secured against a range of residential property including specialist assets such as houses in multiple occupation, buy-to-let portfolios, holiday lets and apartment blocks. Target customers include portfolio investors and high net worth individuals. Castle Trust Bank has a flexible and innovative approach to structuring including the ability for interest to be rolled up on some, or all, of the loan. This focus enables Castle Trust Bank to deliver attractive and sustainable risk adjusted returns in excess of those which are available in the mainstream mortgage market.

For Residential Development Finance, Castle Trust Bank serves property developers by offering senior financing to experienced professionals, who want to enhance their returns through the efficient use of their equity capital. A broad range of schemes are considered including refurbishment, conversions under permitted development rights and new build houses/apartments.

**Savings - a broad proposition with modern digital technology**

Our Savings business is based on a recently developed digital savings platform, which we launched in 2020. Over the last year we made full use of our modern mobile app and self-service portal by raising approximately £350m of funding through our e-saver proposition. Customers can open accounts in a matter of minutes using the latest digital facial and fingerprint recognition technology and swiftly fund accounts through Faster Payments. Our mobile app is available from the Apple App Store and Google Play. New accounts are for fixed terms typically ranging from 1 to 5 years providing customers with certainty over the interest they earn and providing Castle Trust Bank with certainty over our funding. When a fixed term product matures, it becomes an easy access account enabling customers to choose to reinvest their funds into another fixed term product, keep them in the easy access account whilst they decide what to do or return the funds to their nominated bank account.

Unlike many of our competitors, Castle Trust Bank can serve both the ISA and non-ISA savings markets and we have deep experience in executing pricing strategies in both arenas to achieve our funding requirements. This was particularly important in 2022 as interest rates rose We raise funding at low acquisition costs by working with price comparison websites and work with a funding partner, Flagstone, to provide us with an additional way to raise funding. This year we started using QR codes in our literature to help customers quickly access the information they need. We continue to capture automation opportunities and joined the Pay UK Cash ISA Transfer Service, which will make ISA transfer more efficient for both our customers and our colleagues.

Our understanding of our saving customers is developed further through regular customer surveys. In our latest survey we received a net promoter score of +20. We understand that the most important thing for our customers is knowing that their savings are safe. Customers benefit from saving with a bank with a robust business model and retail customers are protected by the Financial Services Compensation Scheme ("FSCS") up to a maximum of £85,000 per eligible investor.

# Business review

**Overview**

Following the UK economy's recovery from Covid-19, new challenges emerged in the current financial year with inflationary pressures leading to the wider cost of living challenge that many UK households now face. This has resulted in interest rates rising at levels not seen for many years. Castle Trust Bank has been able to respond robustly to these challenges and has seen continued growth in its lending base. This, along with careful management of Castle Trust Bank's credit and other risk exposures, has enabled us to report an improved financial result in the current year with Profit Before Tax increasing to £4.5m (2021: loss before tax of £2.3m).

On the lending side, in Property the repositioning of the product offering both in Mortgages and Residential Development in the prior year led to strong new originations flows with the Property assets growing 15% year on year to £457.9m.

Savings balances increased through attractive pricing in the year to support this asset growth. As at year end our customers held £724.5m of savings with us (2021: £557.4m).

**Recent market developments**

The economic outlook has deteriorated throughout 2022 with the forecasts for inflation rising just as the forecasts for UK output have fallen. A key component of inflation has been the rise in energy prices, and this has been greatly exacerbated by the economic impact of Russia's invasion of Ukraine. The war has significantly raised the wholesale prices of both gas and many agricultural commodities. In China, the zero covid policy and associated lockdowns made it harder and more expensive to import goods. However, not all of the UK's inflation can be attributed to global events. The UK labour market remains tight as the number of people who are not active in the labour market has remained much higher than before the pandemic. At the same time, post- Brexit, it is harder for citizens of EU states to come to the UK for work.

These headwinds create a difficult environment for policymakers as monetary tightening puts downward pressure on both prices and output. The Bank of England started by raising interest rates in December 2021 for the first time since 2018. Then, in each subsequent meeting, the base rate rose further and is expected to continue to rise into 2023. The political instability in the UK has further depressed economic sentiment and raised yields on gilts. As interest rates rose throughout the year, the rates on savings accounts rose from being typically below 1% to more than 4% for a one-year fixed term account. Similarly, the rates on a typical two-year mortgage rose from around 2% to more than 6%. This will help to dampen inflation by encouraging people to save and reducing demand. However, there will be knock-on effects for house prices. House prices remained robust during 2022 but many forecasters are expecting a decline in 2023.

Prices are likely to continue to rise faster than income for many people creating a cost-of-living challenge. Inflationary pressures, along with interest rate rises may put additional constraints on household income which potentially impacts both new lending affordability and the ability of customers to service their payment commitments with us. Castle Trust Bank will continue to assess its credit risk appetite for these factors and support customers where they experience financial difficulty through our robust forbearance policies. Castle Trust Bank continues to monitor its pricing for both lending and savings products to ensure that in a changing interest rate environment, our products remain competitive and attractive to customers.

**Cost of living**

In 2022 inflationary pressures started to emerge creating a cost-of-living challenge for colleagues and customers. This was at the same time as the economic outlook weakened. Castle Trust Bank was one of the first banks to act to help its colleagues. This was done through a permanent, out of cycle, pay rise of £1,000 for all colleagues below Executive Committee level. This was well received and has supported high levels of colleague engagement and retention. Castle Trust Bank monitors colleague turnover at Board level through regular People reports and our balanced scorecard. Employee turnover was within appetite at the end of the financial year.

To help our vulnerable customers, our colleagues received mental health training from the Samaritans, and we updated the tools we have in place to help customers who find themselves in financial difficulty. We continuously adjust our credit policies to make sure our lending is affordable and aligned to the latest economic forecasts. In Property, we have reduced LTVs for new lending and adjusted our lending criteria for areas that are likely to find the rise in the cost of living most challenging. For our Savings customers, our fixed rate term products allow early access if customers find themselves in financial difficulty.

**Covid-19 impact**

Although 2022 has seen the impact of Covid-19 reduce significantly for both the Castle Trust Bank's customers and colleagues, the longer-term impacts continue to be felt through the knock-on related impact in the wider macro-economic environment. At the height of the pandemic, Castle Trust Bank provided specific forbearance to support customers following regulatory guidance. This was typically in the form of payment holidays for a period of 1-6 months or, for mortgages maturing, some customers were offered an extension to their mortgage settlement. This support was discontinued in the prior financial year following the opening up after lockdown, where in most cases we saw customers returning to their existing contractual payment arrangements. Where financial difficulties continued, they were managed sensitively through the Bank's standard forbearance measures.

If Covid-19 or a variant were to significantly re-emerge in the future, Castle Trust Bank is in a strong position to respond to any disruption this may cause. During the pandemic Castle Trust Bank maintained high levels of support provided to customers whilst ensuring the safety and wellbeing of colleagues. Operational effectiveness was maintained throughout lockdowns with the office environment being made Covid-19 safe. Since the pandemic, colleagues have been encouraged to find a balance between home and office working and these working practices are now considered to be business as usual.

Castle Trust Bank now has extensive experience of quickly rolling out targeted forbearance measures to support customers who find themselves in financial difficulty and we remain confident that we can support customers effectively if Covid-19 disruption were to increase once again.

**Brexit**

The United Kingdom left the EU single market and customs union in December 2020. To date, the impact of Brexit on our core products and customers has not been significant. However, the Bank remains exposed to Brexit risk as a period of significant disruption to supply chains, movement of labour and demand for residential properties could affect credit losses. In light of this, Castle Trust Bank continues to monitor the impact of Brexit on its business.

### Credit and remediation

Castle Trust Bank continues to focus on improving the quality of lending, moderating its risk appetite across all lending classes. With a challenging external environment because of the cost of living and affordability concerns, careful underwriting decisions have been adopted which should improve credit performance and ensure the Bank remains a responsible lender. Whilst experienced credit performance remains strong and in line with recent periods, the wider macro-economic environment has become more challenging. This has resulted in an increase in the cost of risk year on year, as provisioning levels increase against the backdrop of worsening economic forecasts. See Note 23.1 for more details.

### Group evolution

The function and role of the Castle Trust Holdings Ltd, the Company and its subsidiary entities ("The Group") has changed significantly over the last few years as the business embarked on the journey to become a bank. A key part of the process was a group simplification exercise where the activities of several subsidy entities were either wound down or transferred to other subsidiaries, principally CTC.

The first stage of the simplification took place with the sale of the house price derivative component of the HPI mortgage book and several house price option contracts to a related entity on 30 September 2019. Once completed, this left a de-risked conventional mortgage book with minimal exposure to the related house price index component of the HPI mortgage product.

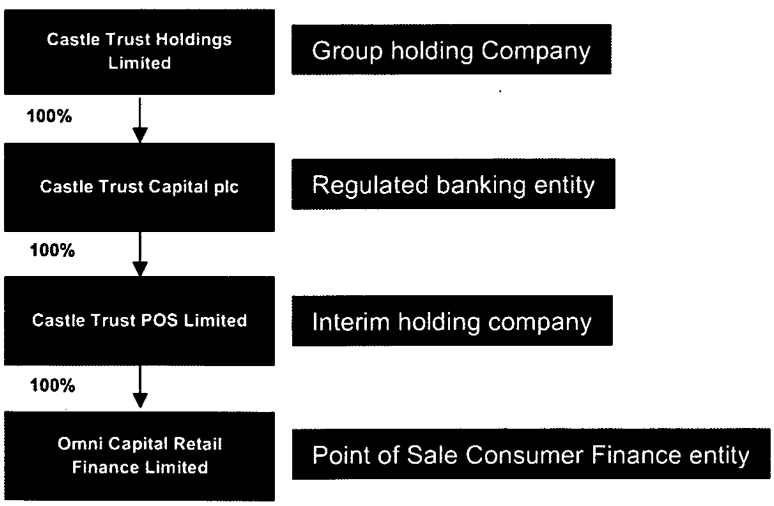
The second stage of the group simplification saw the treasury activity for the Group transferring to the CTC from another subsidiary Castle Trust Treasury Limited ("CTT"). From this point, CTC became the principal funding entity for the Group's lending activities, in particular the consumer loan business and wholesale loan activities in Omni.

As a result of the first and second stages being completed, two subsidiary entities, CTT and Castle Trust Finance Limited ("CTF") ceased trading activities and were dissolved on 6 October 2020.

The final stage of the group simplification was intrinsically linked to banking licence approval, as the Company launched bank deposits to replace the legacy Fortress Bonds and Housa investment products. Prior to being authorised by the regulators, the Group undertook a legal process to convert customers holdings in Fortress Bonds and Housas issued into new fixed term and structured deposit accounts.

This stage was completed successfully in June 2020. As a result, several subsidiary entities including Castle Trust Capital Management Limited ("CTCM"), Castle Trust Direct plc ("CTD"), Castle Trust Income House plc ("CTIH") and Castle Trust Growth Housa PC ("the PC") had no ongoing trading activity and were dissolved.

The current operating structure of the Group is as follows:




### Colleagues

Castle Trust Bank's people are what makes the business work, creating great, bespoke solutions for its customers and developing the business for the future. We pride ourselves on our One Bank culture which is how we describe colleagues working together across the business to help deliver for our customers. This creates a vibrant working atmosphere, which is reinforced by a range of events including our regular townhalls, annual conference and delivery of our ESG plan.

The business has a strong management team in position and working well together, bringing experience from a range of small banks, high street banks and building societies, regulators and specialist lenders. We strive to be an inclusive and diverse workplace. This year we set up our LGBTQ+ network, Rainbow At Castle Trust Bank, which has met regularly generating further ideas and suggestions on how we can help colleagues bring their whole selves to work.

We continue to embed our values based on a bottom-up approach using colleague generated feedback. Colleagues are asked to complete regular surveys to aid and inform management of what is working well and where the business needs to do more to improve empowerment and engagement. In our most recent colleague survey, 92% of colleagues participated and the engagement score rose from 7.9 to 8.2. All colleagues have performance agreements which contain both objectives and the behaviours colleagues are expected to display by living our values.

**ESG and Climate Change**

The way we execute our business strategy is consistent with the plans we are developing for our Environment, Social and Governance (ESG) strategy. In 2022, we partnered with a specialist firm, Sancroft, to develop our ESG plan, which was approved by the Board and our commitments are now publicly available on our website. In relation to our environmental goals, we source our electricity from renewable sources and divert waste away from landfill to be recycled. In 2022 we launched an electric car scheme for colleagues enabling colleagues to lease Electric Vehicles (EVs) through salary sacrifice at a significant discount.

Through our Omni business we help customers finance the purchase of energy efficient products and make it more affordable by allowing them to spread the cost. We currently help finance products such as A-rated efficient windows and doors, new hydrogen ready boilers and A-rated household appliances.

We are looking at ways to reduce the amount of paper we use both across our three business lines and through general office use. We estimate that we use approximately one million sheets of paper a year and plan to reduce this by introducing paperless options for customers and making greater use of electronic signatures. We already incorporate some ESG considerations into our decision-making process when selecting which suppliers we work with and will engage further with suppliers to determine their ESG strategies. Our approach to climate change risk is detailed on page 20 and the Streamlined Energy and Carbon Report Regulations disclosure within the Directors' Report can be found on page 32.

We became a core sponsor of a not-for-profit organisation, Destination Basingstoke, which organises community events in the local area. Over the course of the year, colleagues took part in the Basingstoke 5km, 10km and half marathon races. Our Chief Compliance Officer is on the Board of Destination Basingstoke and was a key contributor to the Place To Be Proud Of Awards, which recognise local residents who have gone above and beyond for the Basingstoke community. There is an ESG committee, which is a colleague led forum for delivering our ESG plan. The ESG Committee coordinated a sustainable barbecue and fund-raising events for Red Nose Day and Macmillan. Castle Trust Bank has donated almost £20,000 to good causes over the last three years.

Strong governance is vital to make sure the bank is delivering it objectives. The Board undertook an evaluation working with a Board advisory firm, which provides objective and independent counsel. On around 30 comparable measures, Castle Trust Bank performed at or above the average scores of 100 European financial services firms. Our Governance framework is supported by a range of policies to protect colleagues and the business from bribery and corruption, look after vulnerable customers and make sure products are designed to deliver strong outcomes for customers. The Executive team all have ESG deliverables as part of their individual performance agreements. Our ESG plan will be refreshed annually, and our performance reviewed by the Board.

**Outlook and Future Developments**

Future developments are also disclosed on page 32 of the Directors' Report.

**Principal risks and uncertainties**

Principal risks and uncertainties are carefully monitored by the Company to ensure all risks undertaken are aligned to the Company's overall objectives and future direction of the Company. Risks are ultimately managed by the Chief Risk Officer who, whilst ensuring risks to the Company are understood and controlled, also ensures risks undertaken are commensurate with the approved risk appetite. All risks undertaken by the Company are done so with our values at heart to ensure that both customers and colleagues are treated fairly.

The principal risks of the business are managed by Castle Trust Bank's Risk Management Framework which is further detailed in the Risk Management Report on page 17.

Further, principal uncertainties are defined as Emerging Risks in the Risk Management Report on page 19.

## Key Financial Performance Indicators

The following Key Financial Performance Indicators ("KPIs") are used by management to track how the business is performing.

| Key performance indicator | At 30 September 2022 | At 30 September 2021 | Variance |
|---|---|---|---|
| Loan book balances (£'000s) | | | |
| Property finance | 457,909 | 398,997 | 58,912 |
| Savings/Investment balances (£'000s) | 724,595 | 557,956 | 166,639 |
| Liquid assets (£'000s) | 148,706 | 74,543 | 74,163 |
| Unaudited Liquidity Coverage ratio | 335% | 321% | 14% |
| Unaudited CET1 Capital Ratio | 19.7% | 20.1% | (0.4%) |
| Impairment coverage ratio | 2.1% | 2.2% | (0.1%) |
| Cost of Risk (Basis Points) | 35 | 44 | (9) |
| Net interest income (£'000s) | 25,539 | 24,254 | 1,285 |
| Profit / (loss) before tax (£'000s) | 4,460 | (2,265) | 6,725 |

The property finance loan book represents the value of assets loaned to mortgage and RDF customers net of related impairments. The increase in the loan balance in the year is due to new originations, principally through serviced first charge buy to let mortgages. The legacy book continues its run off as expected and the pipeline of new business remains strong.

Savings/investment balances relate principally to fixed deposits held by customers. The increase in this balance has been driven by increased loan volumes and liquidity required to be held to support the strong Property new business pipeline.

Liquid assets are a measure of readily available liquid funds that Castle Trust Bank can utilise to meet customer and business needs. The increase of £74m in the year reflects the requirement to hold sufficient liquidity to support the growth in the balance sheet, in particular the new business pipeline for Property loans.

The liquidity coverage ratio is an unaudited key regulatory metric which requires banks to hold enough high-quality liquid assets ("HQLA") that can be sold during a 30-day stress scenario. The unaudited year-end position of 335% (2021: 321%) compares favourably with the regulator's target guidance of 100%.

The CET1 Capital ratio is a key metric used throughout the industry to measure the capital adequacy of a business. It shows the ratio between the calculated risk weighted assets and Tier 1 capital. Risk weighted assets have grown in the year following the continued growth in the loan book. This has resulted in a decrease of the unaudited ratio of 0.4% year on year and we remain comfortably above our regulatory requirement.

The impairment coverage ratio details the impairment provision as a percentage of the total loan book and is an indicator of changes to the credit profile of the loan portfolio. This year has seen a decrease in comparison to prior year despite the impact of additional impairment taken at year end following the worsening economic environment, interest rate shocks and cost of living challenges. These increases have been offset by the changing shape of the mortgage book with the majority of new originations relating to first charge serviced mortgages which represent a lower credit risk and associated impairment than the higher risk legacy portfolio.

Cost of Risk is calculated by looking at the cost of loan impairment per the income statement as a proportion of average loan assets. Similar to the coverage ratio movements above, the additional impairment taken at year end has been offset by the lower risk mix of the mortgage book. This has resulted in a fall in the cost of risk fall in the year.

Net interest income demonstrates the income generated on the loan book less the associated cost of funding paid to savings customers and is a key indicator in assessing underlying profitability. This has increased year on year to £25.5m (2021: £24.3m) due to lower cost of funds as the Bank benefits from lower front book savings rates in comparison to the higher paying maturing balances, much of which originated prior to the Company receiving its banking licence.

Profit Before Tax is a measure of profitability and business performance. Current Profit Before Tax is £4.5m (2021: loss before tax of £2.3m) with the growth broken down as follows:

- Net interest income improving by £1.3m, as detailed above.
- Fair value movements on financial instruments saw a £4.0m upside, principally due to gains on interest rate swaps used to manage interest rate risk in the banking book.
- Reduction in administration expenses of £1.3m principally relating to professional fees.

## Section 172(1) Statement

S172 of the Companies Act 2006 requires a director of a company to act in the way he or she considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole and in doing so, have regard, amongst other matters, to the:

- Likely consequences of any decisions in the long-term;
- Interests of the company's colleagues;
- Need to foster the company's business relationships with suppliers, customers and others;
- Impact of the company's operations on the community and environment;
- Desirability of the company maintaining a reputation for high standards of business conduct; and
- Need to act fairly between members of the company.

The Board of directors of Castle Trust Bank consider they have discharged this duty ensuring decisions made during the year ended 30 September 2022 were in good faith and likely to promote the success of the company for the benefit of its members as a whole. In addition to incorporating the above-mentioned factors, the Board incorporates the Company's purpose statement, key values and strategic priorities into its decision making.

During the year, the Board reviews matters relating to business strategy, financial and operational performance, key risks and legal, regulatory and compliance matters. The Board delegates authority for the day-to-day running of the business to the CEO, and through him, to Senior Management and various sub-committees to oversee the execution of the Bank's strategy and related policies.

**Purpose statement**

Castle Trust Bank is a specialist bank with a simple purpose: to help customers achieve their financial goals. Our purpose is particularly significant because many of our customers are not well served by mainstream financial services. We are here to help customers by:

- Doing our bit to help alleviate the UK's housing crisis by financing the building of new homes;
- Providing homeowners and landlords with specialist solutions to match their individual financial needs; and
- Providing a secure home for people's savings.

**Stakeholders**

Engaging with the Bank's stakeholders is an important element to ensuring the Board has the relevant information when making decisions. Key stakeholder management is maintained via regular dialogue throughout the year. The table below sets out the Bank's key stakeholders, the main method by which the Board and Management engage, and how the Board assess the effectiveness of engagement and receive feedback.

| Stakeholder | Description | Engagement | Assessment and feedback |
|---|---|---|---|
| **Shareholders** | The Bank has one shareholder holding the majority of the Bank's ordinary share capital. | The shareholder is represented on the Board and Board subcommittees by Non-Executive Directors and is therefore fully involved in the decision making of the company. | By having representation on the Board, direct feedback is provided enabling the shareholder to be continuously engaged. |
| **Customers** | The Bank has around 19,000 deposit customers and over 1,000 lending customers. | The Bank undertakes regular customer feedback surveys. The results of these inform product and business line strategies.<br><br>Customer journeys and customer interactions are regularly reviewed and quality assured. This helps inform staff training plans and improve the experience of our customers. | Results of the customer feedback surveys are shared with the Board with actions identified and monitored at a Board or sub-committee level. |

| Stakeholder | Description | Engagement | Assessment and feedback |
|---|---|---|---|
| **Colleagues** | The average number of people employed by the Bank during the year was 214. | The Bank undertakes a semiannual Colleague Opinion Survey. Colleague engagement is high and the results are positive. The survey is a key input for the staff engagement strategy.<br><br>In addition to the fortnightly CEO Blog, staff are engaged through regular 'meet the CEO' sessions and monthly all staff 'Townhalls'.<br><br>The Bank is also a signatory of the Women in Finance Charter.<br><br>To support the mental health and wellbeing of the colleagues, the Bank has signed up to the Mortgage Industry Mental Health Charter. | The findings of the colleague surveys are detailed to the Board with action plans determined on the key drivers identified which will enhance overall engagement with colleagues.<br><br>Throughout the year, the Chairman of the Board hosts regular meetings with groups of colleagues from all levels and departments. This enables colleagues to provide feedback direct to the Chairman. |
| **Suppliers** | Businesses and individuals who provide the Bank with services and goods. | Management regularly meets the Bank's key suppliers particularly those providing important business services and information technology systems. | Outcomes of key supplier reviews are communicated to the Board with material items and related actions monitored. |
| **Brokers/inter mediaries** | Partnerships with third parties who introduce new business and help support the Bank's existing customers. | All new lending in both Property is introduced through partnerships with intermediaries and brokers. Strong relationships with these partners are vital to the ongoing success of the Bank. Regular dialogue with our distribution partners facilitates our ability to ensure a continued understanding of our customers' needs and drives ongoing product evolution. | Any significant items arising following discussions with third party intermediaries are raised at Board meetings with agreed upon actions monitored. |
| **Regulators** | The Bank is regulated by the PRA and FCA. | The Bank's management has regular meetings with its Supervisory teams to discuss its strategy, plan and performance. | Board members meet separately with the regulators on a periodic basis. At these meetings feedback on the Bank is provided by the regulator, enabling the Board to determine the effectiveness of engagement. |
| **Communities** | The geographic locations in which the Bank has offices, colleagues and customers. | The Bank is a member of a number of trade bodies and Industry Groups in the regions in which we operate.<br><br>A key focus of the Bank's ESG plan is engagement with the community of Basingstoke where most of our employees live and work. Our ongoing partnership with Destination Basingstoke, a not-for profit community events company, has seen the Bank support several community initiatives throughout the year (see ESG section of Strategic report). | The Board is kept updated as to the process of community initiatives and in some cases join other colleagues at events to experience first hand the impact the Bank is having with the local community. |

**Key Decisions**

In terms of key decisions undertaken by the Board in the year, the following have been identified as having the greatest impact on the stakeholders described above:

- Approval of the business strategy and plan
- Strategic growth opportunities and acquisitions
- Approval of the ESG plan

**Approval of the Business plan**

In September 2022, the Board approved the Business Strategy and Medium-Term Plan. This sets out product growth targets in key business lines with related capital, resourcing and investment requirements defined. The plan is set to grow the business on a sustainable level and forms the baseline of the Internal Capital Adequacy Assessment Process ("ICAAP") and the Internal Liquidity Adequacy Assessment Process ("ILAAP").

The business plan outcomes will have impacted some of our key stakeholders. This was considered by the Board in detail before deciding to approve the business plan.

| **Stakeholder** | **Impact** |
|---|---|
| Customers | The plan targets growth in all key business line through the provision of competitively priced and innovative products that Castle Trust Bank believes will meet customers' diverse needs. |
| Colleagues | The business plan provides growth and opportunities to the Bank's staff with detailed resourcing requirements embedded to ensure that business growth is aligned with the growth of a high functioning and motivated workforce. |
| Brokers/intermediaries | The business plan will detail new business origination targets with changes to product mix, pricing and distribution strategies. This will shape our ongoing relationship and engagement with third party intermediaries. |
| Regulators | The ICAAP and ILAAP documents provide comfort to the regulator that the business plan and strategy ensure that Castle Trust Bank will continue to meet its stringent capital and liquidity requirements until September 2025. This provides protection to customers and the wider financial services market. |
| Shareholders | The strategy and plan provide the shareholder with a clear direction of how Castle Trust Bank will grow in a sustainable manner, deliver a growing positive return on equity and therefore meet its investment objectives. |

**Strategic growth opportunities and acquisitions**

Growth opportunities are being actively pursued by the Bank as it continues its strategic priority to expand the business, either organically or through acquisition/merger opportunities. During the year, a number of strategic prospects were considered and reviewed by the Board, who in turn make the ultimate decision whether to proceed or not. The Board also approve and monitor additional out of budget expenditure relating directly to these opportunities. Although no prospects successfully crystalised in the year, the Board and senior management continue to explore opportunities as they arise.

| **Stakeholder** | **Impact** |
|---|---|
| Customers | The Bank would use growth opportunities to establish a larger scaled operation. This in turn would offer customers a wider product set, improved pricing and opportunities and an enhanced customer journey. |
| Colleagues | A growing Bank offers colleagues wider development and career opportunities. This will enhance retention rates and improve attractiveness of the Bank for future recruitment. |
| Brokers/intermediaries | A strategic acquisition or merger may introduce additional product lines or growth in the Bank's existing product set. This may incorporate new third party intermediary relationships and presents opportunities to existing partners to work together to deliver our products to our customers. |
| Regulators | The Bank remains open and has a constant dialogue with the Regulators as strategic opportunities are pursued. Ultimately Regulatory approval is required for any acquisition/ merger undertaken. |
| Shareholders | The intention of pursuing a strategic priority of growth is to increase the market valuation of the Bank and in return maximise shareholder value. |

**ESG Plan**

Castle Trust Bank recognises it plays an important role in helping to protect the environment and support social initiatives whilst making sure our business is well governed.

| Stakeholder | Impact |
|---|---|
| Colleagues | The ESG plan highlights our commitment to be a family friendly employer who embraces flexible working, colleague development and guarantees to pay the national living wage. Castle Trust Bank is a signatory to the Woman in Finance charter, which aims to improve gender balance in senior management. |
| Communities | The plan details our ongoing commitment to the community in Basingstoke through the support of several local initiatives. On an environmental basis, The Bank is committed to supporting customers through responsible lending. |
| Regulators | The plan details the governance arrangements in place to ensure the Bank has appropriate oversight of their regulatory obligations. The includes product governance, whistleblowing policy, anti-bribery and corruption, financial crime prevention, and how we treat vulnerable customers. |
| Shareholders | The plan provides assurance to the shareholders that the Bank is meeting it regulatory requirements and that there is strong oversight and governance over their investment. |

## Strategic Report Approval

Approved by the Board of Directors and signed on behalf of the Board

Mr Andrew Macdonald
Company Secretary
14 December 2022

# Risk Management and Governance

## Risk Management Report

### Purpose of Risk Management

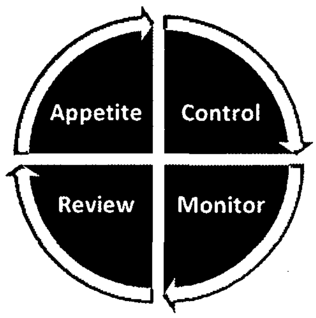
The purpose of Castle Trust Bank's Risk Management Framework is to give stakeholders confidence that risk is understood, monitored and controlled and that the level of risk that Castle Trust Bank takes is aligned to its objectives, including operational, conduct and prudential risk. This ensures that the risks are commensurate to the returns and financial resources of the institution and that treating customers fairly is embedded into its culture and operational processes. The Risk Management Framework ensures that:

- In the normal course of business, Castle Trust Bank's operations, customer outcomes and prudential metrics are stable and in line with objectives; and
- Under stress, Castle Trust Bank can continue to operate, to fulfil its obligations to customers and to meet its prudential requirements.

The Risk Management Framework is owned by the CRO and overseen by the Board Risk Committee. The following sections of the report explain how the Risk Management Framework is applied in Castle Trust Bank.

### Risk Management Process Lifecycle

Castle Trust Bank's Risk Management Framework operates alongside a comprehensive suite of risk-specific policies, manuals and procedures to specify the Risk Management Processes the bank is required to follow in respect of each risk. The framework groups the Risk Management Processes into four phases as set out in the following diagram and table.




| Lifecycle Phase | Intended outcome | Description |
|---|---|---|
| **Appetite** | To identify Castle Trust Bank's objectives and set appetite for deviation from objectives in relation to specific risks. | A combination of annual, regular and ad hoc processes which ensure that Castle Trust Bank has clear objectives and has the resources and processes in place to meet its objectives. Setting of risk appetite is part of the Plan phase. Examples include<br>• Setting of operational resilience standards<br>• New product approval<br>• Regular risk appetite and limit calibrations and reviews of the annual corporate plan, ICAAP and ILAAP |
| **Control** | To operate robust controls that ensure that the objectives, including risk appetite, are met. | Regular processes or mechanisms which are designed to control risk and deliver Castle Trust Bank's objectives. Examples include:<br>• Business continuity and disaster recovery scenario test exercises<br>• Affordability and credit checks<br>• Vulnerable customer procedures<br>• Quality assurance<br>• Board limits |

| | | |
|---|---|---|
| **Monitor** | To provide management with clear measures as to execution of the objectives, the risk incurred and the effectiveness of controls. | Regular information and governance processes that ensure each risk has appropriate monitoring information and that there is a regular forum which has responsibility for reviewing that information. Castle Trust Bank provides regular reporting against operational, customer and prudential objectives. |
| **Review** | To undertake periodic stock takes to ensure that the Risk Management Framework is delivering the objectives and risk appetite as intended. | A combination of annual, regular and ad hoc processes which ensure that Castle Trust Bank is meeting the objectives it has set during its Planning processes.<br>• Risk based Compliance Monitoring or Internal Audit Reviews<br>• Annual product reviews<br>• Annual CRO reports |

**Culture, Lines of Defence and Responsibilities**

Responsibility for risk management lies with every colleague of Castle Trust Bank. All colleagues are expected to manage the risks of their own area in accordance with the Risk Management Framework and to escalate issues and emerging risks appropriately.

Primary ownership for risk management sits with the 1st line business areas that manage their own specific risks and controls. The 2nd line is responsible for providing independent challenge, specialist advice, risk monitoring and ensuring the Risk Management Framework is operating effectively. The 3rd line provides independent assurance that the Risk Management Framework is working as intended.

| Line of defense | Owner | Oversight | Functional areas | Responsibilities aligned to Risk Management Process Lifecycle |
|---|---|---|---|---|
| 1st | CEO | Board | Business units, HR, Technology and Finance | • Control – to operate controls prescribed in the Risk Management Framework<br>• Monitor – to identify and escalate emerging risks<br>• Monitor – to track performance, risk and control effectiveness |
| 2nd | CRO | Risk and Audit Committees[1] | Risk and Compliance | • Appetite – to manage the risk appetite<br>• Control – to provide independent advice and challenge in respect of key decisions / judgements and specialist risk areas<br>• Monitor – to track performance, risk and control effectiveness<br>Review – to provide periodic stock takes as to effectiveness of Risk Management Framework |
| 3rd | Head of Internal Audit | Audit Committee | Internal Audit | • Review – to provide assurance as to the effectiveness of the Risk Management Framework |

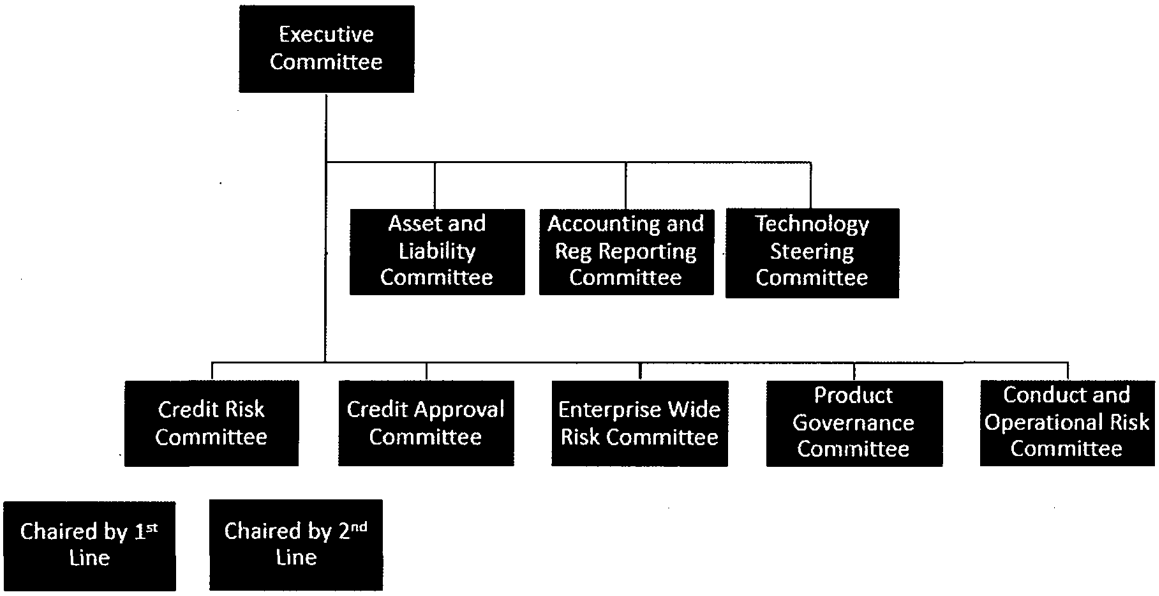
1. Audit Committee has oversight of Compliance Monitoring; otherwise Risk Committee has oversight.

The Board Risk Committee is responsible for agreeing Risk Appetite on behalf of the Board and providing oversight of the application of the Risk Management Framework.

**Governance**

Castle Trust Bank has a comprehensive suite of governance arrangements to ensure that each risk is effectively managed and has appropriate oversight.

In order to ensure that there is independent challenge, all Executive Committees require the CRO or Chief Compliance Officer to attend.




Below the Executive Committees there is a hierarchy of sub-committees and working groups with responsibility for managing specific risks.

**Risk Groups**

Castle Trust Bank allocates every individual risk to a Risk Group.

Each Risk Group has an owner, an Executive Committee member responsible for its oversight and a tailored suite of processes aligned to the Risk Management Process life cycle described above. The appetite and exposure to each Risk is monitored at the executive risk committees and also at the Enterprise Wide Risk Committee where the risks are considered in aggregate.

| Risk Group | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Strategic** | The risk that Castle Trust Bank is unable to achieve its long-term objectives due to changes in its key markets or in the economic or regulatory context. | CEO | Executive Committee |

| Exposure Description (as at the 30 Sept 2022) | Overview of Risk Management Framework as specifically applied to the Risk Group |
|---|---|
| Castle Trust Bank has significant experience and well-established franchises in its chosen markets and plans to continue controlled growth in those markets. Economic or regulatory change may mean it is unable to meet its objectives or that the risk profile of those markets' changes. | Castle Trust Bank undertakes a detailed planning process at least annually and more frequently when required by changes to the external environment. Supporting the plan, there are detailed assessments of the adequacy of capital and liquidity and of recovery options available in case of stress as well as 2nd line challenge and review.<br><br>The plan is then monitored for performance and risk levels with key risk indicators triggering management review and recovery options when necessary. |

| Risk Group | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Property Credit Risk** | The risk of credit losses arising from the inability of a customers to meet their obligations or of Castle Trust Bank to liquidate collateral in a timely and effective manner. | MD Property | Credit Risk Committee |

| Exposure Description (as at the 30 Sept 2022) | Overview of Risk Management Framework as specifically applied to the Risk Group |
|---|---|
| Castle Trust Bank has £464m of exposure to mortgages and residential development of which £63m are classified as non-performing. (See also Note 12). | Limits and Policies covering origination and portfolio are set by the Board Risk Committee.<br><br>Origination is controlled by a risk-based mandate.<br><br>Origination characteristics and performance are monitored monthly against portfolio limits and risk indicators.<br><br>Annual and ad-hoc reviews are undertaken by the 2nd line and 3rd line. |

| Risk Group | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Market & Funding Risk** | The risk of loses occurring due to market movements, or the inability of a counterparty to meet its obligations.<br><br>Also the risk that Castle Trust Bank is unable to meet its obligations due to a shortfall of Capital or Liquidity. | CFO | Asset and Liability Committee |

| Exposure Description | Overview of Risk Management Framework as specifically applied to the Risk Group |
|---|---|
| Castle Trust Bank has £67m of exposure to non-governmental counterparties. (See also Note 8).<br><br>Castle Trust Bank has £601m of contractual liabilities falling due over the next year (see Note 24). It is also exposed to interest rate risk and Castle Trust Bank is subject to individual Capital and Liquidity arrangements. Castle Trust Bank had total liquidity of £151m at 30 Sept 2022. | Limits and Policies covering origination and portfolio are set by the Board Risk Committee.<br><br>Exposures to market movements and customer behaviour against limits and risk indicators are monitored daily with the ability to mitigate through market transactions. |

| Risk Group | Description | Owners | Executive Committee responsible for oversight |
|---|---|---|---|
| **Customer Conduct and Operational Risk** | The risk of customers not being treated fairly or losses occurring because of operational or conduct failings in Castle Trust Bank's dealings with customers or processes. | MD Property<br>MD Omni<br>CTOO | Conduct and Operational Risk Committee |

| Exposure Description | Overview of Risk Management Framework as specifically applied to the Risk Group |
|---|---|
| Castle Trust Bank supports approximately 1,000 customer accounts in its Property business unit; approximately 19,000 customers in its Savings business unit.<br><br>Customers are supported through a variety of automated and manual operational process which are also variously subject to regulatory requirements. | All Products are subject to a structured approval process controlled by Product Governance Committee and are then reviewed on annual basis.<br><br>A wide variety of controls are deployed including quality assurance, customer satisfaction surveys and complaints root cause analysis.<br><br>Key risk indicators designed to identify unsuitability of the product or poor customer outcomes are monitored at least monthly.<br><br>Regular, annual and ad-hoc reviews are undertaken by the 2nd line and 3rd line. |

| Risk Group | Description | Owners | Executive Committee responsible for oversight |
|---|---|---|---|
| **Group Operational Risk** | The risk of losses occurring because of operational failings in Group operations and infrastructure. | Various | Enterprise Wide Risk Committee |

| Exposure Description (as at the 30 Sept 2022) | Overview of Risk Management Framework as specifically applied to the Risk Group |
|---|---|
| Castle Trust Bank operates a wide range of internal processes to support its business; the primary risks relate to people (including retention and conduct), data and cyber, financial processes (including the operation of complex financial models) and operational resilience which are also variously subject to regulatory requirements. | This Risk Group consists of a broad range of individual risks, each meriting its own bespoke processes to control that risk. |

### Emerging Risks

As well as the overarching Risk Groups noted above, the following emerging risks have been noted for enhanced monitoring and the Risk Management Framework continues to evolve to manage these risks.

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Elevated Inflation Risk** | The risk that Castle Trust Bank incurs losses or is otherwise unable to meet its objectives due to inflation and the UK Cost of Living Crisis. | CRO | Enterprise Wide Risk Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| Castle Trust Bank is primarily exposed to the elevated level of inflation, especially for fuel costs, through its credit exposures as noted in the Property Credit Risk Group above.<br><br>The property credit exposure is fully secured on residential property which has seen a significant dislocation due to wholesale interest rate changes and for which the outlook is uncertain. Within the portfolio a small proportion of underlying tenants are more likely to be vulnerable to elevated inflation and have adjusted ECL accordingly; a similar approach has been undertaken for customer's approaching maturity who are at risk of not being able to meet affordability criteria for a re-finance<br><br>Elevated inflation expectations are also the cause of steeply increasing interest rates (see Emerging Risk Macroeconomic Conditions).<br><br>Operational and conduct risks also exist in the potential for an increased volume of existing customers to find themselves in financial difficulty . and requiring additional support due to the effects of the cost of living crisis. | Castle Trust Bank has assigned certain customers who it deems to be most vulnerable to inflation to Stage 2 for the purposes of calculating impairment.<br><br>Castle Trust Bank has instituted enhanced monitoring of its portfolios, in particular for requests for forbearance linked to Cost of Living.<br><br>Additionally, the bank has undertaken a self-assessment and made a number of [minor] changes to its processes in preparedness for responding to an increased number of customers requiring support. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Competitor Risk** | The risk that Castle Trust Bank is unable to meet its objectives because of competitor action and in particular the underpricing of cost of risk. | MD Property<br>CTOO | Executive Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| Castle Trust Bank is exposed to competition in all areas it operates in. It is exposed to future pricing and product feature competition in its originations of assets and liabilities. As markets have recovered during the second half of the year, competition and pricing in certain markets has intensified. | Castle Trust Bank continues to monitor the impact of competitor risk appetite and pricing on its objectives and risks. It has continued to evolve and diversify its product mx so as to be less exposed to competition in any specific product. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Climate Change Risk** | The risk that Castle Trust Bank incurs losses or is otherwise unable to meet its objectives due to climate change and associated regulatory or other Government intervention. | CRO | Executive Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| Castle Trust Bank is primarily exposed to climate change risk through its credit risk exposure. A significant change in the UK climate may result in property collateral being down valued due to changes in environmental risk or prevailing mortgage and insurance markets.<br><br>Castle Trust Bank may also be required to make changes to its business model and / or processes due to new regulation or market expectations in respect of Climate Change.<br><br>Castle Trust Bank has identified a small segment of BTL exposures that are most vulnerable to potential new BTL regulation due to a combination of low Energy Performance Certificates ("EPCs") rating and low property values. | Castle Trust Bank has set origination policy restrictions in respect of property collateral with specific exposure to climate change (specifically in respect of Flood Risk and EPC ratings).<br><br>Castle Trust Bank continues to monitor policy evolution to identify risks to its existing property collateral value or liquidity and to the viability of its Omni intermediaries. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Regulatory Change Risk** | The risk that Castle Trust Bank is unable to meet its objectives or regulatory requirements, because of the costs or restrictions associated with regulatory requirements, or due to inability to adapt to changes in the regulatory framework. | CRO | Enterprise Wide Risk Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| Castle Trust Bank is subject to several different regulatory type regimes, including Bank of England, PRA, FCA, HMRC and ICO, which variously have the power to institute change requirements, levy fines or require specific remediation activity.<br><br>There are a number of pending changes to legislation pertaining to BTL property which is Castle Trust Bank's largest asset class (£382m of exposure) including changes to the 1988 Housing Act and to requirements for EPC Certificates.<br><br>The FCA's Consumer Duty comes into effect from July 2023, setting higher and clearer standards for consumer protection across financial services and there is a series of other early-stage changes from the regulators that Castle Trust Bank is monitoring (e.g. changes to treatment of capital under Basel 3.) | Castle Trust Bank continues to work closely with its regulators, adopting an open and co-operative approach at all times.<br><br>Regulatory Change is tracked through the committee structure; Change Programmes are instituted to manage required changes to business model, operations and technology.<br><br>An implementation plan for Consumer Duty has been outlined. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Macro-Economic Conditions** | The risk that Castle Trust Bank incurs losses or is otherwise unable to meet its objectives due to unforeseen changes in the levels of economic activity. | CRO | Executive Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| The UK is in a period of rapid economic adjustment. In particular inflation is at an elevated level due to a combination of the War in Ukraine, degraded supply chains, fiscal stimulus during the COVID pandemic and rapid growth in some parts of the economy. There are several areas of indirect exposure:<br><br>Castle Trust and its peers have seen significant inflationary pressure in pricing from suppliers, including from inflation linked uplifts in multi-year supplier contracts and in the recruitment market to attract and retain staff.<br><br>The Bank of England base rate has rapidly increased during the year. Castle Trust Bank is exposed in its existing stock of fixed rate lending and in its ability to pass on previous and / or anticipated rate rises to new or renewing customers. Castle Trust has identified a small segment of BTL landlords due to refinance in the next year who are most likely to be vulnerable to elevated interest rates.<br><br>Higher interest rates and elevated spend on utilities and fuel will inevitably trigger a reduction in general consumer spending, to the extent it is not offset by inflationary wage increases. It is unclear as to whether this will lead to a generalised recession with accompanying unemployment and falls in house prices; however, it is likely that some sub-segments will be adversely impacted. | Castle Trust Bank increased the salaries of all colleagues not on the Executive Committee by £1,000 in April 22 and continues to review the competitiveness of its compensation arrangements. Particular emphasis has been placed upon identifying and supporting high performing colleagues with a total of 12% of the workforce having received internal promotions during the year.<br><br>Castle Trust Bank continues to manage its supplier base to ensure it achieves optimal value and to support its target unit economics.<br><br>Castle Trust Bank seeks to originate a blend of assets and liabilities pre-dominantly with fixed interest rates of one year or more; it has the capability to use interest rate swaps to balance this mix where appropriate.<br><br>Castle Trust Bank continues to monitor the overall economic situation and has applied post model adjustments to ECL calculations where appropriate. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Cyber Risk** | The risk that Castle Trust Bank is unable to operate, incurs losses or breaches customer confidentiality due to the misuse or misappropriation of data it holds. | CTOO | Technology Steering Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| Castle Trust Bank is exposed to cyber risk through its holding of personal data in respect of its customers and colleagues.<br><br>Castle Trust Bank operates and holds data upon a combination of in-house platforms and 3rd party platforms which may be hosted by Castle Trust Bank (dedicated Cloud hosting) or by 3rd parties. These platforms require multiple levels of controls over access and data sharing. | Castle Trust Bank continually monitors existing customer data and systems for indicators of an external breach.<br><br>Specialised IT Security software is utilised across all systems and is continually updated.<br><br>Operational software operates on a cycle of upgrades to ensure that the latest IT security controls are embedded.<br><br>Independent third parties are periodically engaged to test the resilience of key systems to Penetration and Cyber Attacks.<br><br>There is a rolling programme of review over access controls. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Data & model risk (including change management)** | The risk that Castle Trust Bank is unable to operate, takes inappropriate decisions or otherwise incurs losses due to deficiencies in internal or third-party models, data, system changes and / or reporting. | CFO<br>CTOO<br>CRO | EWRC |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| Castle Trust Bank is exposed to data and model risk in multiple areas of operations with the greatest exposure in financial and regulatory reporting and prudential risk management.<br><br>The risk is classified as emerging primarily due to the continued evolution and growth of the business. In particular: increased diversity / complexity of product set; increased reliance upon complex models due to the requirements of IFRS 9; evolution of customer strategies and data requirements necessitating manual workarounds; continued expansion of technology estate, reliance upon 3rd parties and deployment of third-party integrations increases complexity and downstream impact of change. | Castle Trust Bank has introduced additional policy requirements and controls during this year in respect of all End User Computing Applications and Models; it continues to build out a data environment that allows for controls and easy access to its data.<br><br>Castle Trust Bank expects to comply, on a proportionate basis, with the principles set out in the PRA's current consultation is respect of Model Risk Management during the course of this year. |

| Emerging Risk | Description | Owner | Executive Committee responsible for oversight |
|---|---|---|---|
| **Capital Risk** | The risk that Castle Trust Bank is unable to meet its objectives or regulatory requirements, because of a shortfall in its capital resources or an uplift in its capital requirements. | CFO<br>CRO | Asset & Liability Committee |

| Exposure | Key developments to the Risk Management Framework in respect of Emerging Risks |
|---|---|
| As a growing institution, Castle Trust Bank is deploying surplus capital and retained earnings into support for new lending. Any reduction in profitability and / or increase in capital requirement (whether regulatory or internal risk appetite) will reduce the potential quantum of lending that can be supported without raising additional capital.<br><br>During the year the Bank of England Financial Policy Committee has twice voted to increase the Countercyclical Buffer that applies to all banks by 1% of risk weighted assets. This has been partially offset by other movements in the PRA requirement for Castle Trust Bank.<br><br>The last two years have seen relatively benign credit conditions and stable interest rates, supported by rising house prices and strong employment markets. It is now likely that the environment will deteriorate which will constrain Castle Trust Bank's ability to generate capital from retained earnings. | Each year and with regular interim updates, Castle Trust Bank undertakes a detailed forward-looking projection of its financial position, taking into account the prevailing economic expectations. In the event that it cannot demonstrate its ability to meet its own risk appetite through the forecast, then management will agree an action plan with the Board to secure the necessary resources and / or take other mitigating actions. |

# Corporate Governance Report

**Purpose**

Castle Trust Bank's corporate governance is designed to give stakeholders confidence that the bank's objectives have been subject to thorough challenge and review and that performance against objectives is continually monitored, resulting in regular review and evolution of strategy.

Castle Trust Bank's strategy includes the following specific objectives:

| Area | Objective | Outcome |
|---|---|---|
| Customers | Castle Trust Bank identifies and meets its customer needs and provides a high quality service | The place to do business with |
| Commercial | Castle Trust Bank has a suite of attractive products with appropriate pricing, and effective distribution | |
| Technology | Castle Trust Bank has the right technology to deliver its objectives in a secure, resilient, cost efficient and customer friendly manner | |
| People | Castle Trust Bank's Board, senior management team and wider workforce have the skills, experience and motivation to deliver its objectives | The place to work |
| Financial Sustainability | Castle Trust Bank has the right financial resources to achieve its objectives, including capital and liquidity resources and generation of sustainable, attractive returns from its activities | The place to invest |
| Risk | Castle Trust Bank controls and monitors the risks that it takes in order to meet its objectives, including customer, conduct, operational and financial risks, and ensure that the risks are commensurate to the returns and financial resources of the institution | |

**The Board**

The Board of directors has the ultimate responsibility for all aspects of Castle Trust Bank. It has instituted four sub-committees which are explained in the next section. The Board holds formal meetings ten times per year and these are variously supplemented by ad-hoc workshops, site visits, strategy reviews and private meetings of the Non-Executive Directors.

The most important decisions are reserved to the Board, with advice from sub-committees where appropriate. The Board delegates more routine decisions to the Executive Directors who in turn delegate decisions to individuals (as determined by specific mandates) or to committees (as determined by the relevant policy). Executive decisions are taken within the framework of a comprehensive range of Board approved policies and an annual plan setting Group and subsidiary budgets, and product and organisational strategies.

At least annually, and more frequently if required, the Board agrees a corporate plan which sets out the specific objectives of the business and forecasts the financial position based upon that plan and taking into account the prevailing economic outlook. The forecasts must demonstrate that Castle Trust Bank is able to meet its risk appetite.

The Board overseas the effectiveness of the corporate plan delivery through a combination of regular qualitative and quantitative reports summarised into key performance and risk indicators covering all of the key areas in the business, as well as periodic deep dives.

The Board has access to all Executives and any information it requires. The Executives responsible for the 2nd and 3rd lines of defence (see Risk Management Report) have direct access to the Board Chair and the Chairs of Risk and Audit.

### Independent Directors

Castle Trust Bank is not subject to the UK Corporate Governance Code; however, it still places a significant value on the independence of its directors and it has deemed the following directors to be independent:

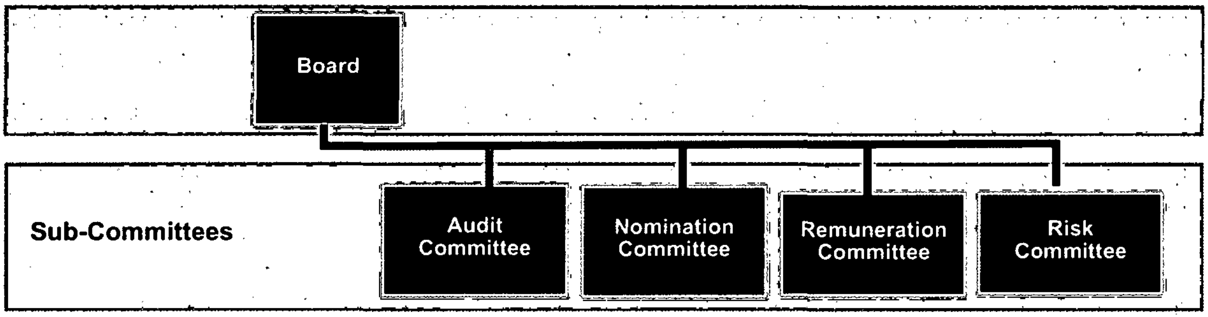
Richard Pym (Chairman)
Eric Anstee (Senior Independent Director)
Marian Martin
Andrew Doman
Melba Montague
Ken Stannard

The Chair of the Board, the Risk Committee and the Audit Committee are deemed to be independent.

The Senior Independent Director is responsible for ensuring that the collective views of the Independent Directors are reflected at the Board; the Chair is effective; and the Board meetings, information and training meets the needs of the Independent Directors and allows them to exercise appropriate influence.

### Board Sub-Committees

The Board operates four standing sub-committees, which enable additional focus to be given to areas of complexity or detail, approving business plans, making recommendations to management and to the Board as appropriate.




| Sub-committee | Chair | Other Members |
|---|---|---|
| Audit | Eric Anstee | Marian Martin, Melba Montague, Tim Hanford, Ken Stannard |
| Nomination | Richard Pym | Andrew Doman, Tim Hanford |
| Remuneration | Andrew Doman | Richard Pym, Tim Hanford |
| Risk | Marian Martin | Richard Pym, Eric Anstee, Andrew Doman, Tim Hanford, Ken Stannard |

Each sub-committee has its own Terms of Reference setting out its objectives.

## Board of Directors

**Overview**

The Castle Trust Board of Directors is the main decision making body at the Group level. The Board considers all issues and risks of a strategic nature and is ultimately responsible for management of the business of the Group and the establishment of Group strategy. The Board also has ultimate responsibility for the oversight of the Group's compliance with the Financial Conduct Authority (FCA) and Prudential Regulation Authority's (PRA) Principles for Business and is to fulfil a role in facilitating relationships between the Group and the FCA and PRA.

The Board monitors and is ultimately responsible for the Group's operations, ensuring professional and prudent management, sound planning, appropriate procedures for the maintenance of accounting and other records and systems of internal control, and for compliance with all statutory and regulatory obligations.

The Board leads the development of the Group's values, culture and standards and is responsible for ensuring that these values, culture and standards are understood and met at each level of the business.

**Meeting frequency and attendance**

| Member | Meetings |
|---|---|
| Richard Pym | 11/11 |
| Eric Anstee | 11/11 |
| Marian Martin | 11/11 |
| Andrew Doman | 11/11 |
| Melba Montague | 11/11 |
| Ken Stannard (joined July 2022) | 2/2 |
| Tim Hanford | 10/11 |
| Tughan Alioglu | 11/11 |
| Martin Bischoff | 11/11 |
| Paul Lloyd-Jones | 11/11 |

**Achievements and decisions made**

- Approval of the Group and subsidiary entity annual financial statements for the period ended 30 September 2022 including key accounting judgements and the going concern assessment. These were approved following the clearance by the external auditors and the recommendation of the Audit Committee.
- Approving the overall strategy of the Group and business lines as well as receiving and reviewing periodic updates from the business on its performance against the agreed strategy.
- Ongoing monitoring of the performance of the business including the wider context of performance as well as the financial performance against plan.
- Reviewing and adapting to changes in the external landscape with approval of revised forecasts and plans which were presented by Management.
- Reviewing and adapting to changes in the legal and regulatory landscape with review of actual and proposed changes such as the proposed regulation of Buy Now Pay Later and the FCA's new Consumer Duty.
- Reviewing and making decisions over potential inorganic opportunities for the business including the potential acquisition of a listed bank which was reviewed during the period.
- Monitoring and reviewing interactions with the FCA and PRA and management's proposed approach to its regulators more widely.
- Approval of the ICAAP and ILAAP for publication following the work and discussions around these which occurred as part of the Risk Committee.
- Monitoring and reviewing the Technology estate of the Group including Cyber awareness as well as in relation to change and projects.
- Monitoring and oversight of the new Operational Resilience framework which has been adopted including the ongoing review of Operational Resilience.
- Receiving and reviewing annual reports on money laundering, financial crime and CASS.

- Reviewing and responding to material incidents which occurred within the Group with approval of remediation activities where required.
- Approval of new ISDA documentation with NatWest Markets plc to enable the Group to begin hedging out interest rate exposures.
- Review and approval of the overall ESG policy and approach including associated activities such as the approval of the Modern Slavery Statement.
- Monitoring Colleague satisfaction and engagement through receipt and review of updates on the regular Peakon surveys which are conducted as well as by hosting informal sessions with Colleagues to give Directors a chance to meet and listen to Colleagues directly.

## Risk Committee

**Overview**

Castle Trust Bank has set its own objectives and is also subject to multiple statutory requirements; as well as various risks. If these were to crystalise or fail to be managed effectively, it may prevent Castle Trust Bank from meeting its objectives or statutory requirements.

The Castle Trust Board Risk Committee is the board level committee responsible for recommending a risk appetite and overseeing the development of risk management frameworks which support the business in managing its risk profile. This Committee oversees the development, implementation and maintenance of the Bank's Risk Management framework, compliance with relevant regulations and law, whistle blowing and proper functioning of controls over the prevention of money laundering, bribery and fraud.

**Meeting frequency and attendance**

| Member | Meetings |
|---|---|
| Richard Pym | 5/5 |
| Eric Anstee | 5/5 |
| Marian Martin | 5/5 |
| Andrew Doman | 5/5 |
| Ken Stannard (joined July 2022) | 2/2 |
| Tim Hanford | 4/5 |

***Achievements and decisions taken***

Oversight of the Risk Management Framework

- Review of the Risk Management Framework and management's action plan to support the evolution of its risk management as the business grows in size and diversity.
- Review of the key models relied upon in determining Expected Credit Loss and oversight of the follow up actions agreed as part of that review.
- Review of management proposals in respect of new products including technology, regulatory and credit strategies to manage the risks of new products.
- Review of the framework for managing Interest Rate Risk.
- Review of the Company funding plan, supporting business growth and liquidity management.
- Review of the AML and Financial Crime policies and approaches.
- In addition, the Risk Committee undertook an assessment of its own effectiveness and agreed specific follow up actions.

Responses to emerging risks

- Review of the key conduct risks and management's responses to the Cost of Living crisis including changes to the affordability criteria applied to Property as well as changes to forbearance strategies.
- Review of management's framework in respect of Climate Change risk and the anticipated impact of both the direct consequences of changing climate and the impact of public sector intervention as the UK transitions to net zero upon Castle Trust Bank's own business and its customer base.
- Review of in-year adjustments to Expected Credit Loss to reflect the Cost of Living crisis.
- Periodic review of latest financial and capital forecasts which through the year incorporated several material changes including: regulatory requirements in respect of the Counter Cyclical Buffer; interest rate outlook & market pricing; inflation in the cost base and customer demand.
- Review of Interest Rate Risk in the Banking Book approach, positions and reactions to changing market positions.

Challenge to key decisions

- Review of the ICAAP, ILAAP and Recovery Plan and recommendation to the Board to adopt these documents.
- Review of a small number of credit exposures outside of management mandate levels.

Engaging with management

- During the year the Risk Committee held a series of workshops / briefings which enabled members to engage and challenge management on detailed issues. The topics covered were:
    - Macro-Economic Scenarios for stress testing
    - Liquidity Stress Assumptions
    - Medium term unsecured lending risk
    - Risk based pricing
    - Conduct Risk Appetite framework and risk appetite

## Audit Committee

**Overview**

The Audit Committee is responsible for evaluating and making recommendations to the Castle Trust Bank Board in relation to accounting, internal control and financial reporting functions.

The Committee reviews and monitors the external auditor's independence and objectivity and the effectiveness of the audit process and provides advice to the Board on whether the annual report and accounts are fair, balanced, and clear.

The Committee monitors and review the effectiveness of the Company's Internal Audit function and reviews all internal audit reports and oversees the Compliance programme.

**Meeting frequency and attendance**

| Member | Meetings |
|---|---|
| Eric Anstee | 6/6 |
| Marian Martin | 6/6 |
| Melba Montague | 6/6 |
| Ken Stannard (joined July 2022) | 1/1 |
| Tim Hanford | 5/6 |

**Achievements and decisions made**

- Review of the Group and subsidiary entity annual financial statements for the year ended 30 September 2022 including key accounting judgements and the going concern assessment. This was recommended for signing to the Board following full clearance by the external auditors.
- Ongoing monitoring of impairment and IFRS 9 model outputs, parameters, and macro-economic forecasts. There was significant focus in the year around the cost of living and customer affordability challenges with post model adjustments and overlays considered where appropriate.

- Monitoring and review of external auditors control observations with management responses and agreed remediation plans and dates.
- Discussed the various regulations and laws having an impact on the Bank and the Group's Internal Audit, Compliance, Finance, and Regulatory Reporting processes.
- Ongoing review of updates from Compliance in relation to compliance monitoring, compliance advisory, financial crime, data protection and regulatory change.
- Review of the external audit plan presented by Deloitte for the financial year ended 30 September 2022.
- Oversight of the Bank's client assets safeguarding procedures and controls to ensure that the rules set out in the FCA's Client Asset Sourcebook (CASS) are fully adhered to.
- Ongoing review of updates from Internal Audit including the review of internal audit reports and the monitoring of external audit, internal audit, compliance monitoring and other assurance actions against agreed delivery dates.
- Endorsed the Compliance risk-based monitoring programme and the Internal Audit plan for the 2022 financial year.
- The Committee confirmed satisfactory implementation of actions agreed in response to an External Quality Assurance review of the Internal Audit function concluding that the work of Internal Audit continued to generally conform to standards and guidelines from Institute of Internal Auditors and that they were satisfied with the level of internal audit resources.
- Review and approval of key internal policies covering financial crime, regulatory reporting, use of external Auditors, provisioning, whistleblowing, travel and business expenses, data protection and compliance.
- Discussed the outcomes of a first line self-assessment of regulatory reporting, following the publication of a 'Dear CEO' letter on the matter by the PRA in October 2021.
- Approval of the publication onto the Castle Trust website of the Pillar 3 disclosures, providing information on the Bank's capital adequacy and risk profile.

## Remuneration Committee and Nomination Committee overview 2022

**Overview**

The Remuneration Committee oversee Castle Trust Bank's Group Remuneration and Reward Policy and approve, review and make remuneration recommendations in relation to senior executives.

Remuneration Committee review levels of remuneration across the firm to ensure that the firm remains competitive in attracting and retaining individuals of high calibre, whilst also ensuring that the right behaviours are rewarded.

The Nomination Committee reviews the composition and performance of the board and executive management teams and their succession plans.

**Meeting frequency and attendance**

| | Nomination Committee | Remuneration Committee |
|---|---|---|
| Richard Pym | 3/3 | 4/4 |
| Andrew Doman | 3/3 | 4/4 |
| Tim Hanford | 3/3 | 4/4 |

**Achievements and decisions made**

During the year the Remuneration Committee undertook the following activities:

- Discussed and approved both financial and strategic targets for the Executive Directors recorded in the Executive Performance Plans.
- Reviewed and approved the Executive Performance Plans for all Executive Committee members. Discussed and approved remuneration for the Managing Director, Omni.
- Considered and approved the treatment of leavers who are participant in the Long Term Incentive Plan (LTIP) scheme.

- Reviewed and approved the appointment of FIT Remuneration Consultants as advisors to the committee.
- Engaged with Ridgeway Advisors in support of the search for an additional Independent Non Executive Directos (iNED). Approved the terms for the appointment of Ken Stannard as independent Non-Executive Director.
- Reviewed and approved the mid-year and year-end performance review ratings and distribution curves.
- Approved the annual salary review and discretionary bonus allocation.
- Reviewed and approved the annual Remuneration Policy Statement and supporting documentation in relation to the firm's Material Risk Takers (MRTs).
- Approved the rules and performance scorecards relating to the quarterly Sales Bonus Schemes for Omni and Property.
- Had oversight of the annual Gender Pay Gap Report and Women in Finance Charter submission.
- Had oversight of the job levelling, job grade and salary range framework.
- Reviewed the total compensation benchmark review of Executive Committee roles and approved any recommendations for changes.
- Reviewed and approved the Terms of Reference of the Committee.
- Approved the updated Group Remuneration & Reward Policy, Remuneration Risk Adjusted Framework Policy and Group People Policy.

During the year the Nominations Committee undertook the following activities:

- Approved external advisor to conduct the external Board Effectiveness Review.
- Approved the appointment of Ken Stannard as independent Non-Executive Director.
- Established an appropriate succession plan for the CEO role.
- Coordinated a face to face awareness and regulatory update session provided by Deloitte to directors and management (including SMCR).

# Directors' report

The directors present their report for Castle Trust Capital plc for the year ended 30 September 2022. The information on page 1 forms part of this report.

**Directors**

Details of directors who served during the year and up to the date of signing are provided on page 1.

**Regulatory environment**

CTC is authorised and regulated by the PRA and FCA.

**Results and dividends**

The results of the Company for the year are set out in the statement of comprehensive income on page 45. The Company has made a profit before tax in the current financial year of £4.5 million (2021: loss before tax of £2.3 million).

The directors do not recommend the payment of a dividend (2021: £nil). Please refer to note 25 for details of allotted share capital.

**Financial risk management and exposure to risk**

The Company measures and monitors risk on a regular basis and formally reviews its risk position at the Risk Committee every quarter. The main financial risk to which the Bank is exposed to as at 30 September 2022 is credit risk as set out in the strategic report. Castle Trust is also exposed to other market risks (primarily interest rate risk and house price risk) and liquidity risk as these risks are inherent in the business. Each of these risks are regularly measured and monitored, and appropriately managed. Refer to the Risk Management Report on page 14 and note 23 for full details.

The Risk Function helps to set risk appetite, develops an appropriate risk management framework and oversees exposures. It is independent of the business areas responsible for managing these risks and has direct access to the Risk Committee responsible for setting and oversight of risk strategy and policies. The Risk Committee (which has formally met 5 times during the financial year with a number of ad-hoc discussions and workshops held in addition to address specific issues) has delegated various decision making and monitoring responsibilities to the following executive committees: the monthly Credit Risk Committee, the monthly Customer and Operational Risk Committee, and the Credit Approval Committee.

**Principle Risks and uncertainties**

The principal risks of the business have been defined as Risk Groups in the Risk Management report on page 17 which details the oversight and mitigation the company has undertaken.

Principal uncertainties are defined as Emerging Risks in the Risk Management report on page 19.

**Going concern assessment**

The financial statements of Castle Trust Capital plc have been prepared on a going concern basis. In assessing whether the going concern assumption remains appropriate, the directors have focussed on the liquidity and funding position for the next 12 months. This assessment has been undertaken at both a Group and Company level and accordingly the directors considered the going concern of both the Group and the Company.

The Company is strongly capitalised with total equity of £94 million, total assets of £833 million and liquidity of £149 million.

The Group undertakes an annual planning round which assesses the Group's profitability, capital and liquidity position over a 4 year time horizon. As part of the going concern assessment, stress scenarios are applied to the base case financial plan, the outcomes of which determine whether the group remain a going concern under these scenarios over the assessment period.

The stress scenarios applied incorporate the following assumptions:

- Capital stress – Increase in the capital requirement prescribed by the regulator with no additional capital injected into the Group by the Shareholder.
- Liquidity funding stress – The Group is required to pay significantly above market rates to attract new deposit funding. The increase in funding costs is not able to be passed onto lending assets.
- Liquidity outflow stress – The Group is unable to attract new deposits for a period, a high proportion of maturing deposit accounts leave the Group and loan repayments from customers are reduced.
- Market Stress – 2022 Annual Cyclical Stress ("ACS") as prescribed by the Bank of England is applied. This results in increased cost of funding, higher impairment charges and a significant reduction in business volumes.

To each of these stress scenarios, management actions were considered to assess the Group and Company's response. These actions included:

- Tightening of risk appetite in response to worsening credit environment.
- Reduction in origination targets to reduce Risk Weighted Assets.
- Flexible pricing on deposit products to respond to liquidity needs.
- Tighter cost control in line with reduced revenue to maintain profitability.

Furthermore, a reverse stress scenario was performed that considers similar risk drivers in more severe but less plausible scenarios, which if unmitigated would render the business model unviable. The directors consider the possibility of this outcome to be remote and have identified mitigation that would be adopted in such circumstances.

The ability of the Group to attract new savings customers is continuously assessed, together with sensitivity analysis on potential changes in the interest rate offered on new fixed term deposits which may occur as a result of changes in the macro economic environment and alternative rates available in the market. The Group has further diversified its sources of funding through offering of its deposit products through financial intermediaries in 2022 and will be seeking to access to the Bank of England's Sterling Monetary Framework in the future.

The directors have also considered the following as part of the going concern assessment:

- Risk management policies and how the Company is placed to manage business risks.
- The overall regulatory risk of the business including the risks associated with the current business model, potential exposure to conduct risk and the impact of changes in the regulatory landscape.
- The control environment of the Group in assessing the likelihood of operational failures.

The directors are satisfied that the Group and Company has the resources to continue in business for the foreseeable future and meet its liabilities as they fall due in the next 12 months. Furthermore, the directors are not aware of any material uncertainties that may cast significant doubt upon the Group's and Company's ability to continue as a going concern.

**Events since the balance sheet date**

No significant adjusting or non-adjusting events after the reporting date have been identified. Please refer to note 33.

**Capital management**

CTC is regulated by the Financial Conduct Authority ("FCA") and Prudential Regulatory Authority ("PRA") and is subject to the requirements of the Capital Requirements Regulation which governs capital levels. Regulatory capital requirements are monitored as part of the overall management of capital, with Key Risk Indicators assigned and monitored for regulatory capital ratios. Omni is also subject to FCA regulation over its consumer credit activities.

Capital management disclosures, to the extent they are not included in the financial statements are published in a Supplementary Regulatory Capital and Remuneration Disclosure on Castle Trust Bank's website (www.castletrust.co.uk).

**Future Developments**

Despite the challenges facing the UK economy and financial services sector following the Covid-19 pandemic, Castle Trust Bank remains well capitalised with significant levels of surplus liquidity. This robust balance sheet will enable Bank to pursue its growth plan and to be in a strong position to engage in strategic opportunities were they to arise in the market.

Castle Trust Bank's business model will continue to be centred around its two main business lines – Property and Savings. Castle Trust is approaching three years of being a bank and has operated in its core markets for many years before that. It knows its customers and markets well. The Bank has navigated the unprecedented challenges of recent years well and so is optimistic that any further disruptions to business conditions can be overcome.

Despite the challenges facing the UK economy, Castle Trust Bank remains well capitalised with significant levels of surplus liquidity. This robust balance sheet will enable the Bank to pursue its growth plan and to be in a strong position to engage in strategic opportunities were they to arise in the market.

**Streamlined Energy and Carbon Report Regulations ("SECR") disclosure (unaudited)**

The SECR disclosure presents the Company's carbon footprint, together with an appropriate intensity metric and total energy use of electricity and gas. For shared premises spaces, the Company receives an allocation of energy usage based on gross internal floor area. All emissions are Scope 2.

| | **2022** | **2021 (Restated)** |
|---|---|---|
| **Gross Internal Floor Area ($m^2$)** | 1,803 | 1,416 |
| **Scope 2 emissions and indirect energy use** (kWh)<br>- Energy use of purchased electricity | 690,876 | 666,365 |
| **Emissions and energy use totals** | | |
| Absolute emissions (kg $CO_2e$) | 128,575 | 127,221 |
| Total energy use (kWh) | 690,876 | 666,365 |
| **Intensity measures** | | |
| Emissions per $m^2$ gross internal area ($kgCO_2e/m^2$/year) | 71.32 | 89.85 |
| Energy use per $m^2$ gross internal area ($kWh/m^2$/year) | 383.20 | 470.60 |

The 2021 comparative has been restated to include gas consumption under a revised methodology. The prior year methodology only incorporated electricity usage. Emissions and energy use per $m^2$ are used to monitor energy usage as the Bank expends the majority of its energy through the premises it operates in.

During the year initiatives to reduce the Company's carbon footprint were undertaken including a review of energy consumption, reduction in paper usage and implementation of proposals from the Company's ESG Committee, a committee of colleagues responsible for ensuring sustainable business practices are implemented and promoted.

**Political contributions and donations**

The Company has made no political contributions or donations during the current and prior year.

### Branches outside the UK

The Company has no branches outside the UK.

### Directors' indemnity and directors' & officers' liability insurance

Castle Trust maintains a directors' and officers' liability insurance policy. In accordance with Castle Trust's Articles of Association, the Board may also indemnify a director from the assets of Castle Trust against any costs or liability incurred as a result of their office, to the extent permitted by law. Neither the insurance policy nor any indemnities that may be provided by Castle Trust provide cover for fraudulent or dishonest actions by the directors.

There were no provisions made in the current or prior year in relation to directors' indemnity.

### Disclosure of information to the auditors

So far as each person who was a director at the date of approving this report is aware, there is no relevant information, being information needed by the auditor in connection with preparing its report, of which the auditor is unaware. Having made enquiries of fellow directors and the Company's auditor, each director has taken all the steps that they are obliged to take as a director in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information. The confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

### Appointment of Auditors

Deloitte have expressed their willingness to continue in office as auditor and a resolution to re-appoint them will be considered at the next Annual General Meeting.

Approved by the Board of Directors and signed on behalf of the Board

Mr Andrew Macdonald,
Company Secretary,
14 December 2022

## Statement of directors' responsibilities

The directors are responsible for preparing the strategic report, the directors' 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 accounting standards in conformity with the requirements of the Companies Act 2006 and applicable law.

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, the directors are required to:

- Present fairly the financial positions, financial performance and cash flows of the Company
- Select suitable accounting policies in accordance with IAS 8: Accounting Policies, *Changes in Accounting Estimates and Errors* and then apply them consistently;
- Present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- Make judgements that are reasonable
- Provide additional disclosures when compliance with the specific requirements of international accounting standards in conformity with the requirements of the Companies Act 2006 is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Company's financial position and financial performance; and
- State whether the Company's financial statements have been prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006, subject to any material departures disclosed and explained in the financial statements.
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business

The strategic report and the directors' report include a fair review of the development and performance of the business and the position of the Company together with a description of the principal risks and uncertainties faced by the Company.

The directors are responsible for ensuring that the Company keeps proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company, in accordance with the Companies Act 2006. The directors have general responsibility for safeguarding the assets of the Company and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF CASTLE TRUST CAPITAL PLC

## Report on the audit of the financial statements

### 1. Opinion

In our opinion the financial statements of Castle Trust Capital Plc (the 'Bank'):
- give a true and fair view of the state of the Bank's affairs as at 30 September 2022 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom adopted international accounting standards; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:
- the statement of comprehensive income;
- the statement of financial position;
- the statement of changes in equity;
- the cash flow statement; and
- the related notes 1 to 34.

The financial reporting framework that has been applied in their preparation is applicable law, and United Kingdom adopted international accounting standards.

### 2. Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the Bank in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

The non-audit services provided to the Bank for the year are disclosed in note 6 to the financial statements. We confirm that we have not provided any non-audit services prohibited by the FRC's Ethical Standard to the Bank.
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### 3. Summary of our audit approach

| | |
|---|---|
| **Key audit matters** | The key audit matters that we identified in the current year were:<br>• Expected credit loss on loans to customers; and<br>• Effective interest rate income recognition<br><br>Within this report, key audit matters are identified as follows:<br>Newly identified<br>Increased level of risk<br>Similar level of risk<br>Decreased level of risk |

| | |
|---|---|
| **Materiality** | The materiality that we used in the current year was £1.4m (2021: £1.1m) which was determined on the basis of 1.5% of net assets. |
| **Scoping** | Audit work to respond to risks of material misstatement was performed directly by the audit engagement team in the UK. |
| **Significant changes in our approach** | We have made the following amendments in key audit matters on expected credit loss ('ECL') provision:<br>• There is a risk that the ECL models, that were designed and implemented in a relatively benign credit environment, do not appropriately capture expected defaults in the current unprecedented economic uncertainty arising from Covid-19 and the macroeconomic environment. Therefore, we have identified management overlays as an additional area within ECL key audit matter in the current year. |

## 4. Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Our evaluation of the directors' assessment of the Bank's ability to continue to adopt the going concern basis of accounting included:

- We evaluated management's going concern assessment paper to determine whether it appropriately captures all key business risks, such as operational, financial, liquidity and capital risks;
- We obtained management's four-year profitability plan and capital and liquidity forecasts and challenged key assumptions and their projected impact on capital and liquidity ratios, particularly with respect to loan book growth and potential credit losses;
- Supported by our regulatory specialists, we read the most recent ICAAP and ILAAP submissions, considered management's capital and liquidity projections, evaluated the results of management's stress testing, and challenged key assumptions and methods used in the stress testing;
- We read correspondence with regulators to understand the capital and liquidity requirements imposed by the Bank's regulators, evidence any changes and consider those requirements as part of our overall going concern assessment;
- We met with the Group's and the Bank's lead regulator, the Prudential Regulation Authority, and discussed their views on existing and emerging risks to the Group and the Bank and we considered whether these were reflected appropriately in management's forecasts and stress tests;
- We assessed the historical accuracy of profitability forecasts prepared by management; and
- We considered the adequacy of the disclosures made in the financial statements in view of the requirements of applicable financial reporting framework.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Bank's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

## 5. Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

### 5.1. Expected credit loss on loans to customers

| | |
|---|---|
| **Key audit matter description** | IFRS 9 *Financial Instruments* requires loan provisions to be calculated using an expected credit loss ('ECL') model. As at 30 September 2022, the Bank had an outstanding balance of loans to customers at amortised cost, net of ECL provision, amounting to £454m (2021: £395m) (see note 12) with the total ECL provision balance of £9.9m (2021: £8.7m) (see note 12). ECLs are calculated both for individually significant loans and collectively on a portfolio basis which require the use of statistical models incorporating loss data and assumptions on the recoverability of customers' outstanding balances.<br><br>The current macroeconomic environment, along with current inflationary pressure, has increased the complexity in estimating ECLs, particularly with regards to determining appropriate forward-looking macroeconomic scenarios and appropriately identifying significant increases in credit risk. In addition, significant judgement is expected to be involved in estimating the impact of rising inflation on delinquencies and determining the appropriate probability of defaults ('PD') in the current economic environment.<br><br>The ECL provision requires management to make significant judgements and estimates. We therefore consider this to be a key audit matter due to fraud or error in respect of the Bank's ECL provision.<br><br>We identified five specific areas in relation to the ECL that require significant management judgement or relate to assumptions to which the overall ECL provision is particularly sensitive.<br><br>i. **Significant increase in credit risk ('SICR'):** The assessment of whether there has been a significant increase in credit risk between the date of origination of the exposure to 30 September 2022. There is a risk that management's staging criteria, for example being 30 days past due, does not capture SICR and/or are applied incorrectly.<br><br>ii. **Macroeconomic scenarios:** As set out in note 22.1, the Bank sources economic forecasts from a third-party economics specialist and considers a minimum of five probability weighted scenarios, including base, mild upside, upside, downside, and severe downside scenarios. Due to the economic uncertainty arising from the macroeconomic environment, increases in the Bank of England base rate and increasing cost of living, there have been significant changes to the economic assumptions in each of the scenarios. The key economic variables were determined to be the house price index ('HPI'), Gross domestic product ('GDP') growth, unemployment rates and base rate. There is significant judgement in determining the probability weighting of each scenario and the assumptions and characteristics of each scenario applied.<br><br>iii. **Haircut rate assumption:** Hair-cut rate assumption measures the difference between the expected sale proceeds and the expected collateral value used in IFRS 9 ECL model at reporting date, commonly referred to as 'forced sale discount'. Management uses an internally developed matrix to determine the appropriate haircut rates as an input to the loss given default ('LGD') calculation within ECL model and is highly sensitive to the haircut rate assumption<br><br>iv. **Collateral valuation used in individually assessed loan:** Management uses third-party valuers or house price indices to estimate the market value of collaterals on a case-by-case basis for individually assessed loans. The use of incorrect or inappropriate indices or stale valuations could lead to a material misstatement of the ECL. |

v. **Management overlays:** There is a risk that the ECL models, that were designed and implemented in a relatively benign credit environment, do not appropriately capture expected defaults in the current unprecedented economic uncertainty arising from Covid-19 and the macroeconomic environment. We have seen an increased number of financial institutions use management overlays to mitigate the risk that the models do not accurately estimate expected credit losses in the current stressed environment. Determining whether a management overlay is required and its estimation process involves significant management judgement.

**How the scope of our audit responded to the key audit matter**

We obtained an understanding of the relevant controls over the ECL provision with particular focus on controls over significant management assumptions and judgements used in the ECL determination.

To challenge the Bank's SICR criteria, we:

- Evaluated the Bank's SICR policy and assessed whether it complies with IFRS 9 *Financial Instruments*;
- Assessed the quantitative thresholds used in the SICR assessment by reference to standard validation metrics including the proportion of transfers to stage two driven solely by being 30 days past due, the volatility of loans in stage two and the proportion of loans that spend little or no time in stage two before moving to stage three;
- With the assistance of our credit modelling specialists, we assessed whether SICR assumption methodology and code script used in the ECL model is consistent with the approved SICR methodology;
- Tested whether the quantitative and qualitative thresholds set by management had been appropriately applied in practice as at 30 September 2022; and
- Performed an assessment for a sample of loans, including a focused sample of forborne loans, to determine whether they have been appropriately allocated to the correct stage.

To challenge the Bank's macroeconomic scenarios and the probability weightings applied we:

- Agreed the macroeconomics scenarios used in the ECL model to reports prepared by the third-party economics specialist;
- Assessed the competence, capability and objectivity of the third-party economics expert, which included making specific inquiries to understand their approach and modelling assumptions to derive the scenarios;
- Supported by our economic specialists, assessed and challenged management's assessment of scenarios, forecasting of selected economic variables, and considered the probability weightings assigned to them in light of the economic position as at 30 September 2022;
- Involved our economic specialists to challenge the Bank's economic outlook by reference to other available economic outlook data;
- Assessed whether macroeconomics methodology and code script used in the ECL model is consistent with the macroeconomic assessment approved by the Audit Committee. We were supported by our credit modelling specialists; and
- Performed a benchmarking exercise to compare the appropriateness of selected macroeconomic variables and weightings to those used by peer lenders, as part of stand back assessment. The key economic variables were the house price index, GDP growth, unemployment and base rate.

To challenge the Bank's haircut rate assumption we:

- with the assistance of our credit modelling specialists we assessed whether the haircut rate assumption, methodology and code script used in the ECL model is consistent with the LGD methodology approved by the Impairment Committee;
- Recalculated the haircut rates observed on defaulted cases between 2019 and 2022 and compared them with the rates used by the Bank in the ECL models; and
- Assessed the appropriateness of the haircut rate assumption adopted by management through benchmarking to industry peers.

| | |
|---|---|
| | We performed the following procedures to challenge the Bank's case by case estimate of the market value of collateral for individually assessed loans:<br><br>• Supported by our property valuation specialists, examined management's valuation policies, tested a sample of collateral valuations for individually assessed loans by reference to available market data; and<br>• For a sample of collaterals, reviewed third-party valuation reports used by the Bank to test the appropriateness of the assumptions and valuation methodology.<br><br>We performed the following audit procedures to address the completeness and accuracy of management overlays:<br><br>• We involved our credit modelling specialists to assess the ECL model findings highlighted in our review, those reported in the latest model validation report and latest performance monitoring reports to identify model deficiencies that may require management overlays.<br>• With the assistance of our credit modelling specialists we evaluated the methodology adopted by the Bank to recognise cost of living and maturity cap overlays and tested the accuracy of these PMAs by independent recalculation;<br>• We assessed the impact of known data deficiencies to determine whether there is any need to book post model adjustments to cover any ECL model data deficiencies;<br>• We substantively tested the completeness and accuracy of the underlying loan data and inputs used in the calculation of management overlays; and<br>• We performed qualitative assessment on the Group's lending portfolio, including assessing the impact of emerging risks in the banking and lending business, as part of our stand back assessment to identify any factor that may require additional management overlays. |
| **Key observations** | We determined that the methodology used and the SICR criteria, haircut rate assumption, and management overlays, used in determining the ECL provision as at 30 September 2022 were reasonable. We determined management's collateral valuations to be reasonable.<br><br>Notwithstanding that estimating the probability and impact of future economic outcomes is inherently judgemental and that there is heightened economic uncertainty, on balance, we consider that the macroeconomic scenarios selected by the management and the probability weightings applied are appropriate.<br><br>We therefore determined that ECL provision on loans to customers are appropriately stated. |

### 5.2. Effective interest rate income recognition

| | |
|---|---|
| **Key audit matter description** | In accordance with the requirements of IFRS 9 *Financial Instruments*, management is required to spread directly attributable fees, discounts, incentives and commissions on a constant yield basis ("effective interest rate, EIR") over the shorter of the behavioural and contractual life of the loan assets. EIR calculations are complex and the Bank's approach to determining the EIR involves the use of models and significant estimation in determining the behavioural life of loan assets. Given the complexity and judgement involved in accounting for EIR, there is an opportunity and incentive for management to manipulate the amount of interest income reported in the financial statements and revenue recognition is an area susceptible to fraud.<br><br>The Bank's net interest income for the year ended 30 September 2022 was £34.0m (2021: £35.1m) (see note 3).<br><br>EIR adjustments arise from revisions to estimated cash receipts or payments for loan assets that occur for reasons other than a movement in market interest rates or credit losses. They result in an adjustment to the carrying amount of the loan to customers, with the adjustment recognised in the income statement in interest income and similar income. As the EIR |

| | |
|---|---|
| | adjustments reflect changes to the timing and volume of forecast customer redemptions, they are inherently judgemental. The level of judgement exercised by management is increased given the limited availability of historical repayment information. The EIR adjustments are sensitive to changes in the behavioural life "curves" or "conditional prepayment rate" ('CPR') assumption.<br><br>The current macroeconomic environment, including Covid-19, and the changes in the Bank's mortgage portfolio, have introduced additional uncertainty with regards to forecasting expected behavioural lives and prepayment rates. There is management judgement involved in establishing whether customer behaviour observed in the recent period is indicative or not of future expected behaviour. We have therefore identified a significant risk on estimation of the CPR assumption of property mortgages. |
| **How the scope of our audit responded to the key audit matter** | We obtained an understanding of the relevant controls over EIR, focusing on the calculation and review of EIR adjustments and the determination of CPR curves.<br><br>To challenge the Bank's prepayment rate and behavioural life assumptions, we:<br><br>• With the assistance of our analytics and modelling specialists we ran the Bank's loan data for all products through our own independent EIR model, using the behavioural life curves derived by the Bank. We compared our calculation of the EIR adjustment required to the amount recorded by management;<br><br>• Independently derived a CPR curve using the Bank's repayment data over recent periods, with the help of analytics and modelling specialists. We used these curves in our own independent EIR model to derive an independent output showing the EIR adjustments that should have been recorded in 2022. We compared this output to the amounts recorded by management; and<br><br>• Tested the completeness and accuracy of a sample of inputs into the EIR model. |
| **Key observations** | Notwithstanding that estimating the future behaviour of loan to customers is inherently judgemental and that there is heightened economic uncertainty due to the macroeconomic conditions, we determined that the EIR models and assumptions used were appropriate and that interest income for the year is appropriately recognised. |

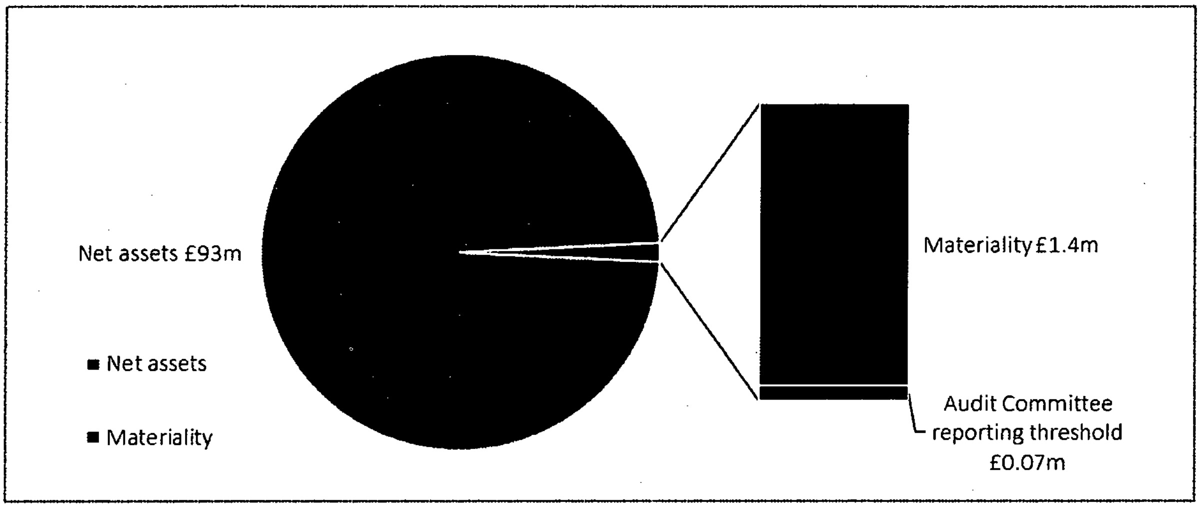
## 6. Our application of materiality

### 6.1. Materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

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

| | |
|---|---|
| **Materiality** | £1.4m (2021: £1.1m) |
| **Basis for determining materiality** | 1.5% of net assets (2021: 1.5% of net assets) |
| **Rationale for the benchmark applied** | Net assets is a key metric within the financial statements on which the users, being the owner of the Bank, lenders, and regulatory body tends to focus and is a good proxy for regulatory capital. |




### 6.2. Performance materiality

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole. Performance materiality was set at 70% of materiality for the 2022 audit (2021: 70%). In determining performance materiality, we considered the Bank's control environment, including entity-level controls, our understanding of the business through our work performed; and the low level of corrected and uncorrected misstatements identified in the prior year.

### 6.3. Error reporting threshold

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £71,300 (2021: £ 57,800), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

## 7. An overview of the scope of our audit

### 7.1. Scoping

Our audit was scoped by obtaining an understanding of the Bank and its environment, including internal controls, and assessing risks of material misstatements. Audit work to respond to risks of material misstatement was performed directly by the audit engagement team in the UK.

### 7.2. Our consideration of the control environment

We identified the key IT systems relevant to the audit to be those used in the financial reporting, lending, expected credit losses, and savings businesses. For these controls we involved our IT specialists to perform testing over the general IT controls, including testing of user access and change management systems.

We performed walkthroughs with management to understand the process and controls and identified and tested relevant controls that address risks of material misstatement in financial reporting. Whilst the Bank continues to improve and implement a more robust system of internal control, we adopted a fully substantive audit approach.

## 8. Other information

The other information comprises the information included in the annual report other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit, or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

## 9. Responsibilities of directors

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, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Bank's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

## 10. Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

## 11. Extent to which the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

### 11.1. Identifying and assessing potential risks related to irregularities

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we considered the following:

- the nature of the industry and sector, control environment and business performance including the design of the Bank's remuneration policies, key drivers for directors' remuneration, bonus levels and performance targets;
- results of our enquiries of management, internal audit, and the Audit Committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the Bank's documentation of their policies and procedures relating to:
  - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
  - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
  - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations;

- the matters discussed among the audit engagement team and relevant internal specialists, including tax, valuations, economic, credit, financial instruments, IT, real estate and analytics and modelling specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in the following areas: expected credit loss and effective interest rate income recognition. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory frameworks that the Bank operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the financial statements. The key laws and regulations we considered in this context included the UK Companies Act, pensions legislation, the Capital Requirements (Country-by-Country Reporting) Regulations 2013, and tax legislation.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the Bank's ability to operate or to avoid a material penalty. These included the Bank's compliance with the Prudential Regulation Authority ('PRA') Rulebook and the Financial Conduct Authority ('FCA') Handbook.

**11.2. Audit response to risks identified**

As a result of performing the above, we identified expected credit loss on loans to customers and effective interest rate income recognition as key audit matters related to the potential risk of fraud. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters.

In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- enquiring of management, the Audit Committee and in-house legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with HMRC, FCA and PRA; and
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists, and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

# Report on other legal and regulatory requirements

## 12. Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- 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; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

## 13. Opinion on other matter prescribed by the Capital Requirements (Country-by-Country Reporting) Regulations 2013

In our opinion the information given in note 34 to the financial statements for the financial year ended 30 September 2022 has been properly prepared, in all material respects, in accordance with the Capital Requirements (Country-by-Country Reporting) Regulations 2013.

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

### 14.1. Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- 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.

We have nothing to report in respect of these matters.

### 14.2. Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made.

We have nothing to report in respect of this matter.

## 15. Other matters which we are required to address

### 15.1. Auditor tenure

Following the recommendation of the Audit Committee, we were appointed by the Board of Directors on 23 March 2021 to audit the financial statements for the year ending 30 September 2021 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is two years, covering the years ending 30 September 2021 to 30 September 2022

### 15.2. Consistency of the audit report with the additional report to the Audit Committee

Our audit opinion is consistent with the additional report to the Audit Committee we are required to provide in accordance with ISAs (UK).

## 16. Use of our report

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.

Atif Yusuf

Atif Yusuf (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom
14 December 2022

## Statement of comprehensive income

**For the year ended 30 September 2022**

| | Notes | Year ended 2022 £'000 | Year ended 2021 £'000 |
|---|---|---|---|
| Interest and similar income | 3 | **34,047** | 35,127 |
| Interest and similar expense | 4 | **(8,508)** | (10,873) |
| **Net interest income** | | **25,539** | 24,254 |
| Fees and commission income | | **812** | 643 |
| Fees and commission expense | | | (48) |
| Realised / unrealised gain / (loss) on financial instruments at fair value through profit or loss | 5 | **2,680** | (1,328) |
| **Total operating (expense) / income** | | **29,031** | 23,521 |
| Administrative expenses | 6 | **(21,001)** | (22,281) |
| Impairment losses | 12 | **(1,530)** | (1,892) |
| Impairment charge on investments in subsidiaries | 17 | **-** | (18,001) |
| Depreciation and amortisation | 16, 18 | **(2,040)** | (1,613) |
| **Total operating expenses** | | **(24,571)** | (43,787) |
| **Other income - dividends received** | | **-** | 18,001 |
| **Profit / (loss) before tax** | | **4,460** | (2,265) |
| Corporation tax (charge) / credit | 7 | **(2,479)** | 9,018 |
| **Total profit** | | **1,981** | 6,753 |
| **Other comprehensive income** | | | |
| ***Items not reclassified to profit or loss in subsequent periods*** | | | |
| Fair value of own credit risk changes of financial liabilities at FVPL | | **(25)** | (4) |
| **Total other comprehensive (expense) for the year** | | **(25)** | (4) |
| **Total comprehensive income for the year** | | **1,956** | 6,749 |

The results for all years presented comprise continuing operations.

Notes on pages 49 to 95 are an integral part of these financial statements.

## Statement of financial position

**Registered number: 07454474**
**As at 30 September 2022**

| Assets | Notes | 2022 £'000 | 2021 £'000 |
|---|---|---|---|
| Cash and cash equivalents | 8 | **143,706** | 54,544 |
| Due from credit institutions | 9 | **1,970** | - |
| Debt instruments | 10 | **5,000** | 19,999 |
| Trade and other receivables | 11 | **1,003** | 817 |
| Loans to customers | | | |
| At amortised cost | 12 | **453,815** | 394,523 |
| Designated at fair value through profit or loss | 13 | **4,094** | 4,474 |
| Derivative assets | 14 | **3,123** | - |
| Prepayments | | **1,589** | 1,575 |
| Deferred tax | 7 | **6,898** | 9,043 |
| Amounts due from group companies | 15 | **189,221** | 152,451 |
| Property and equipment | 16 | **1,593** | 1,450 |
| Investment in subsidiaries | 17 | **16,206** | 16,206 |
| Intangible assets | 18 | **4,679** | 4,186 |
| **Total assets** | | **832,897** | 659,268 |
| **Liabilities** | | | |
| Trade and other payables | 19 | **8,815** | 8,033 |
| Amounts due to credit institutions | 9 | **4,100** | |
| Amounts due to customers | | | |
| At amortised cost | 20 | **724,595** | 557,956 |
| At fair value through profit or loss | 21 | **1,433** | 1,317 |
| **Total liabilities** | | **738,943** | 567,306 |
| **Equity** | | | |
| Share capital | 25 | **15,217** | 15,217 |
| Share premium | 25 | **124,195** | 124,195 |
| Equity share based payment reserve | | **207** | 171 |
| Own credit revaluation reserves | | **8** | 33 |
| Retained earnings | | **(45,673)** | (47,654) |
| Issued capital and reserves attributable to owners of the parent | | | |
| **Total equity** | | **93,954** | 91,962 |
| **Total equity and liabilities** | | **832,897** | 659,268 |

Notes on pages 49 to 95 are an integral part of these financial statements.

The financial statements were approved by the Board of Directors and authorised for issue on 14 December 2022 and were signed on its behalf by:

Martin Bischoff
Chief Executive Officer
14 December 2022

## Statement of changes in equity

**For the year ended 30 September 2022**

| | Share capital | Share premium | Equity settled share based payment reserve | Own credit revaluation reserves | Retained earnings | Total |
|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| At 1 October 2021 | 15,217 | 124,195 | 171 | 33 | (47,654) | 91,962 |
| Total profit for the year | - | - | - | - | 1,981 | 1,981 |
| *Other comprehensive income* | | | | | | |
| Fair value of own credit risk changes of financial liabilities at fair value through profit or loss | - | - | - | (25) | - | (25) |
| *Total comprehensive income* | - | - | - | (25) | 1,981 | 1,956 |
| Equity settled share based payment reserve | - | - | 36 | - | - | 36 |
| **At 30 September 2022** | 15,217 | 124,195 | 207 | 8 | (45,673) | 93,954 |

For the year ended 30 September 2021

| | Share capital | Share premium | Equity settled share based payment reserve | Own credit revaluation reserves | Retained earnings | Total |
|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| At 1 October 2020 | 15,217 | 124,915 | 155 | 37 | (54,407) | 85,197 |
| Total profit for the year | - | - | - | - | 6,753 | 6,753 |
| *Other comprehensive income* | | | | | | |
| Fair value of own credit risk changes of financial liabilities at fair value through profit or loss | - | - | - | (4) | - | (4) |
| *Total comprehensive income* | - | - | - | (4) | 6,753 | 6,749 |
| Equity settled share based payment reserve | - | - | 16 | - | - | 16 |
| At 30 September 2021 | 15,217 | 124,195 | 171 | 33 | (47,654) | 91,962 |

Notes on pages 49 to 95 are an integral part of these financial statements.

## Statement of cash flows

### For the year ended 30 September 2022

| | Notes | 2022 £'000 | 2021 £'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Profit / (loss) before tax | | 4,460 | (2,265) |
| **Adjustments for non-cash items :** | | | |
| Depreciation and amortisation | 16, 18 | 2,040 | 1,617 |
| Loss on disposal of intangibles and property and equipment | | | 78 |
| Dividends received | | | (18,001) |
| Share based payment expense | 29 | 36 | 16 |
| Net interest income | | (25,436) | (24,254) |
| Impairment losses | 12 | 1,530 | 1,892 |
| R&D tax credits released against tax charge | | (220) | - |
| Fair value losses on loans to customers at fair value | 13 | 427 | 1,032 |
| Fair value losses on amounts due to customers at fair value | 21 | 112 | 158 |
| Net unrealised gain on derivative assets | | (3,219) | |
| Impairment charge on investments in subsidiaries | 17 | | 18,001 |
| **Changes in operating assets and liabilities:** | | | |
| (Increase) / decrease in trade and other receivables (excluding corporation tax receivable) | | (186) | 201 |
| (Increase) / decrease in loans to customers at amortised cost | | (47,624) | 48,663 |
| (Increase) / decrease in prepayments | | (14) | 466 |
| Increase / (decrease) in trade and other payables (excluding corporation tax payable and lease liability) | | 772 | (16,013) |
| Decrease in loans to customers at fair value | | (47) | - |
| Decrease in amounts due to customers at fair value | | (21) | (289) |
| Increase in derivatives assets | | 96 | - |
| Increase / (decrease) in amounts due to customers at amortised cost | | 168,780 | (93,538) |
| (Increase) in amounts due from credit institutions | 9 | (1,970) | - |
| Increase in amounts due to credit institutions | 9 | 4,100 | - |
| Tax paid | | (26) | - |
| Interest received | | 20,746 | 35,127 |
| Interest paid (including interest on lease liabilities and MILA loan) | | (10,649) | (10,873) |
| **Net cash generated from / (used in) operating activities** | | 113,687 | (57,981) |
| **Cash flows from investing activities** | | | |
| Purchase of intangible assets | 18 | (1,862) | (1,027) |
| Sale of debt instruments | | 14,999 | 96,919 |
| Purchase of property, plant and equipment | 16 | (493) | (73) |
| Purchase of leased asset on transfer | | | (17) |
| **Net cash generated from investing activities** | | 12,644 | 95,802 |
| **Cash flows from financing activities** | | | |
| Principal repayment of MILA loan | | (36,770) | (14,813) |
| Lease payments of principal | | (399) | (293) |
| **Net cash (used in) financing activities** | | (37,169) | (15,106) |
| **Net increase in cash and cash equivalents** | | 89,162 | 22,714 |
| Cash and cash equivalents at beginning of the year | | 54,544 | 31,830 |
| **Cash and cash equivalents at end of the year** | 8 | 143,706 | 54,544 |

Certain items in operating activities have been reclassified in the prior year comparatives for presentational purposes. The changes had no impact on the net cashflows from operating activities.

Notes on pages 49 to 95 are an integral part of these financial statements.

## 1. Corporate information

CTC is incorporated and domiciled in the UK. The Company is registered in England and Wales and is a public company limited by shares. These financial statements for the year ended 30 September 2022 were authorised for issue in accordance with a resolution of directors on 14 December 2022. The Company has only one class of business.

## 2. Accounting policies

### 2.1 Basis of preparation

The Company's statutory financial statements for the year ended 30 September 2022 have been prepared under IFRS. as issued by the IASB in conformity with the requirements of the Companies Act 2006. The Company has consistently applied the same accounting policies as at 30 September 2022 as in the prior year.

These financial statements have been prepared on a historical cost basis, except for financial assets and liabilities that are measured at fair value. The financial statements are presented in sterling which is the Company's functional currency and all values are rounded to the nearest one thousand pounds (£'000) except where otherwise indicated.

The Company is a wholly-owned subsidiary of Castle Trust Holdings Limited ("CTH"), which is incorporated within the European Economic Areas. The results of the Company are included within the consolidated financial statements of CTH. The company has availed exemption under section 400 of the Companies Act 2006 to prepare and deliver group accounts.

### 2.2 Going Concern

**Going concern assessment**
The financial statements of Castle Trust Capital plc have been prepared on a going concern basis. In assessing whether the going concern assumption remains appropriate, the directors have focussed on the liquidity and funding position for the next 12 months. This assessment has been undertaken at both a Group and Company level and accordingly the directors considered the going concern of both the Group and the Company.

The Company is strongly capitalised with total equity of £94.0 million, total assets of £832.9 million and liquidity of £148.7 million.

The Group undertakes an annual planning round which assesses the Group's profitability, capital and liquidity position over a 4 year time horizon. As part of the going concern assessment, stress scenarios are applied to the base case financial plan, the outcomes of which determine whether the group remain a going concern under these scenarios over the assessment period.

The stress scenarios applied incorporate the following assumptions:

- Capital stress – Increase in the capital requirement prescribed by the regulator with no additional capital injected into the Group by the Shareholder.
- Liquidity funding stress – The Group is required to pay significantly above market rates to attract new deposit funding. The increase in funding costs is not able to be passed onto lending assets.
- Liquidity outflow stress – The Group is unable to attract new deposits for a period, a high proportion of maturing deposit accounts leave the Group and loan repayments from customers are reduced.
- Market Stress – 2022 Annual Cyclical Stress ("ACS") as prescribed by the Bank of England is applied. This results in increased cost of funding, higher impairment charges and a significant reduction in business volumes.

To each of these stress scenarios, management actions were considered to assess the Group and Company's response. These actions included:

- Tightening of risk appetite in response to worsening credit environment.
- Reduction in origination targets to reduce Risk Weighted Assets.

- Flexible pricing on deposit products to respond to liquidity needs.
- Tighter cost control in line with reduced revenue to maintain profitability.

Furthermore, a reverse stress scenario was performed that considers similar risk drivers in more severe but less plausible scenarios, which if unmitigated would render the business model unviable. The directors consider the possibility of this outcome to be remote and have identified mitigation that would be adopted in such circumstances.

The ability of the Group to attract new savings customers is continuously assessed, together with sensitivity analysis on potential changes in the interest rate offered on new fixed term deposits which may occur as a result of changes in the macro economic environment and alternative rates available in the market. The Group has further diversified its sources of funding through offering of its deposit products through financial intermediaries in 2022 and will be seeking to access to the Bank of England's Sterling Monetary Framework in the future.

The directors have also considered the following as part of the going concern assessment:

- Risk management policies and how the Company is placed to manage business risks.
- The overall regulatory risk of the business including the risks associated with the current business model, potential exposure to conduct risk and the impact of changes in the regulatory landscape.
- The control environment of the Group in assessing the likelihood of operational failures.

The directors are satisfied that the Group and Company has the resources to continue in business for the foreseeable future and meet its liabilities as they fall due in the next 12 months. Furthermore, the directors are not aware of any material uncertainties that may cast significant doubt upon the Group's and Company's ability to continue as a going concern.

### 2.3 Significant accounting judgements, estimates and assumptions

The preparation of the Company's financial statements requires management to make judgements, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosures of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods.

In the process of applying the Company's accounting policies, management has made the following judgements and key assumptions concerning the future, as well as other key sources of estimation uncertainty at the reporting date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

The Company based its assumptions and estimates on parameters available when the financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances beyond the control of the Company. Such changes are reflected in the assumptions when they occur. The following items are considered to be the significant accounting judgements, estimates and assumptions relevant to the Company.

***Critical judgements in applying the Company's accounting policies***

The following are the critical judgements, apart from those involving estimations (which are dealt with separately below), that the directors have made in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognised in financial statements:

**(i) Impairment losses on loans to customers**

The Company uses internal models in estimating Expected Credit Loss ("ECL"). Judgement is applied in identifying the most appropriate model for each type of asset, as well as for determining the assumptions used in these models, including assumptions that relate to key drivers of credit risk.

(ii) Judgement is also required in:

- Determining the appropriate segmentation of the Company's portfolio so that the appropriate model is used and the assumptions used in that model have been derived from historic data that is representative of the current portfolio in the current economic climate.

- Identifying which stage a loan is in (for example by determining what constitutes a significant deterioration in credit quality) and the criteria for movement between the stages. Please also see note 23 for further details surrounding methodology.

Where there is little prospect of a recovery being made for a Stage 3 financial asset, the impairment provision is utilised and the carrying value of the loan is then directly reduced. The impairment loss on loans to customers is disclosed in more detail in note 12.

**(iii) Fair value measurement of financial assets and liabilities**

The Company measures certain financial instruments at fair value through profit or loss. Fair value is 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. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or;
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible by the Company. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data is available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. Where the fair values of financial assets and financial liabilities cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from some observable market data but some judgement is required to establish fair values. The judgements include considerations such as liquidity, discount rates and early redemption assumptions.
There is one mortgage designated at fair value retained in the Company as at 30 September 2022 (2021: one mortgage). As the strike date of the embedded House Price Option has passed for this loan, its fair value is no longer sensitive to any changes in inputs into the model and its fair value has been estimated as the amount recoverable. It has been moved out of Level 2 and reclassified as Level 3 in the year due to a reduction in observable inputs and increased uncertainty in the macroeconomic environment.
Structured deposit liabilities at fair value are measured using various inputs, principally the movement in the house price index ("HPI") and a house price risk premium. They are classified as level 3 in the fair value hierarchy.

Fair value related disclosures for financial instruments that are measured at fair value or amortised cost are disclosed in note 22.

**(iv) Effective Interest Rate (EIR) method**

The EIR methodology recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected behavioural life of relevant financial instruments and recognises the effect of potentially different interest rates charged at various stages and other characteristics of the product life cycle (including prepayments and penalty interest and charges). This estimation, by nature, requires an element of judgement regarding the expected behaviour and life-cycle of the instruments.

**(v) Deferred tax assets**

The status, measurements and treatment of deferred tax assets recognised in the financial statements are disclosed in note 7. The decision to recognise the assets is based on the Company's estimation of profits arising in the short to medium term against which the brought forward losses might be relieved. The status, measurement and treatment of these assets are monitored at each reporting date.

**(vi) Recognition of amounts due to customers at amortised cost**

As a result of the group simplification exercise, the Company launched bank deposits to replace the legacy Fortress Bonds and Housa investment products issued by subsidiary entities. Prior to being authorised by the regulators, the Group undertook a legal process to convert customers holdings in Fortress Bonds and Housas issued by subsidiary entities into new fixed term and structured deposit accounts in the Company. As a result of this transaction, intercompany funding liabilities under a Borrower Lending Agreement (BLA) were extinguished and a new external customer liability for deposits was recognised.

The new bank deposits were initially recognised at fair value and held subsequently at amortised cost. In assessing the fair value, a calculation range was determined using expected cash flows discounted using issuance rates, external and internal funding rates. The discount rates are unobservable inputs and therefore the fair value assessment has been categorised as level 3 in the fair value hierarchy as detailed in note 22.

***Key sources of estimation uncertainty***

The following are key estimations that the directors have used in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognised in financial statements:

**(i) Impairment losses on loans to customers**

Internal models are used to determine Probability of Default ("PD"), Loss Given Default ("LGD"), Exposure at Default ("EAD") and forecast economic scenarios.

Key estimates underpinning the models when determining Expected Credit Losses ("ECLs") as explained below:

- **Mortgage Stage 1 and Stage 2 LGD** – the Company uses a number of models to assess the likelihood of a recovery from default and the resulting proceeds from following that recovery. Key estimates for mortgage Stage 1 and Stage 2 accounts are the Cure Rate (the likelihood of a defaulted account resuming payments), the Valuation Haircut (the discount applied to the valuation as a result of a forced sale) and the Time to Sell (the time taken for any collateral of a defaulted mortgage to be sold.
- **Mortgage Stage 3 LGD** – For mortgage accounts which are in default, a specific individual assessment is made of future recoverability. Key estimates in this assessment are the Collateral Valuation and the Valuation Haircut (discount applied to the Collateral Valuation).
- **Mortgage PDs** – the Company uses an economic scenarios model when determining the forward-looking assumptions to be used in different economic scenarios and the weighting of the likelihood of those scenarios. The development of this model requires estimates when assessing the correlations between macroeconomic scenarios and economic inputs (such as unemployment levels and collateral values) and the effect on PDs.

For sensitivity analysis, see note 23.1.10.

**(ii) Effective Interest Rate (EIR) method**

In calculating the EIR for mortgages, a conditional prepayment rate ("CPR"), being a loan prepayment rate equivalent to the proportion of a loan's principal that is assumed to be paid off ahead of time in each period, is estimated. The calculation of this estimate is based on a number of factors, such as historical prepayment rates for previous loans similar to ones and future economic outlooks. For the legacy Interest Roll-up and House Price Index mortgages, the current calculation uses a 3-year product time window to assess the most appropriate rate to apply. If a 4-year time window were to be used, the amortised cost of mortgage loan balances would reduce by £61,000. A separate CPR curve is applied to the first charge serviced mortgage book, where the greatest sensitivity relates to the early repayment assumptions used. The current calculation assumes 30% of the first charge serviced mortgage book repays prior to the end of the fixed term. If this falls to 10% the amortised cost of mortgage loan balances would reduce by £436,000.

## 2.4 Significant accounting policies

### 2.4.1 Interest and similar income

#### *2.4.1.1 Interest and similar income calculated using EIR*

The Company calculates interest income by applying the EIR to the gross carrying amount of financial assets other than credit-impaired assets.

When a financial asset becomes credit-impaired and is, therefore, regarded as 'Stage 3', the Company calculates interest income by applying the EIR to the net amortised cost of the financial asset. If the financial asset cures and is no longer credit-impaired, the Company reverts to calculating interest income on a gross basis.

If expectations are revised, the carrying amount of the asset is adjusted with an associated increase or reduction recorded in interest income. The adjustment is subsequently amortised through interest and similar income in the statement of comprehensive income.

For acquired loan books the EIR calculated at acquisition is not changed for subsequent variances in actual to expected cash flows. The Company monitors the actual cash flows for each acquired book and where they diverge significantly from expectation, the future cash flows are reset (an 'AG8' adjustment). In assessing whether to adjust future cash flows on an acquired portfolio, the Company considers the cash variance on an absolute basis. Where cash flows for an acquired portfolio are reset, they are discounted at the EIR to derive a new carrying value, with changes taken to profit or loss as interest income.

***2.4.1.2 Other interest and similar income***

Interest income and expense on financial assets and financial liabilities at fair value though profit or loss are presented in the statement of comprehensive income within other interest and similar income, and interest and similar expense, respectively (except for one product named Partnership mortgages). Interest income and expense is calculated based on similar principles to the EIR basis. Partnership mortgages differ from the other products in that none of the Partnership mortgages have a minimum repayment amount or fixed interest rate, and are potentially subject to greater variability given Castle Trust is obliged to make payments to the customer in the event of a fall in valuation of the underlying property, in certain cases.

**2.4.2 Financial assets and liabilities**

***2.4.2.1 Initial recognition***

Financial assets and liabilities, with the exception of loans to customers, are initially recognised on the trade date, i.e., the date that the Company becomes a party to the contractual provisions of the instrument. Loans to customers are recognised when funds are transferred to the customers' accounts.

Financial assets and liabilities are initially measured at their fair value and transaction costs are added to, or subtracted from, this amount, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss ("FVPL"), where transaction costs are expensed.

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instrument as set out below.

***2.4.2.2 Subsequent measurement of financial assets and liabilities***

The Company classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either amortised cost, fair value through profit or loss ("FVPL") or fair value through comprehensive income ("FVOCI").

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVPL (when they are held for trading, derivative instruments or the fair value designation is applied).

**Debt instruments, loans and advances to credit institutions, loans to customers, amounts due from group companies and trade and other receivables**

From 1 October 2018, the Company only measures financial instruments at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

The details of these conditions are outlined below. The Company classifies the following financial assets at amortised cost:

- Loans and advances to credit institutions;
- Loans to customers (for those not accounted for at FVPL as set out below);
- Amounts due from group companies;
- Debt instruments and
- Trade and other receivables.

***Business model assessment***

The Company determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective (not on an instrument-by-instrument basis) and is based on observable factors such as:

- How the performance of the business model and the financial assets held are evaluated and reported to key management personnel;
- The risks that affect the performance of the business model and the financial assets held and, in particular, the way those risks are managed;
- How managers of the business are compensated; and
- The expected frequency, value and timing of sales.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Company's original expectations, the Company does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

***The Solely Payments of Principal and Interest ("SPPI") test***

As a second step of its classification process the Company assesses the contractual terms of financial assets to identify whether they meet the SPPI test.

'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium/discount).

The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Company applies judgement and considers relevant factors such as early repayment features.

In contrast, contractual terms that introduce a more than *de minimis* exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement do not give rise to contractual cash flows that are solely payments of principal and interest on the amount outstanding. In such cases, the financial asset is required to be measured at FVPL.

After initial measurement, these are measured at amortised cost using the EIR methodology, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The EIR amortisation is included in interest and similar income calculated using EIR in the statement of total comprehensive income.

**Financial assets and liabilities at fair value through profit or loss**

Financial assets and liabilities classified in this category include those that have been designated upon initial recognition or are mandatorily required to be measured at fair value under IFRS 9 as further described below. The Company has only designated an instrument at fair value through profit or loss upon initial recognition when the designation eliminates, or significantly reduces, the inconsistent treatment that would otherwise arise from measuring the assets or recognising gains or losses on them on a different basis.

Financial assets and financial liabilities at fair value through profit or loss are recorded in the statement of financial position at fair value. Changes in fair value are recorded in profit and loss.

The Company classified the following financial assets and liabilities at fair value through profit or loss:

Amounts due to customers at fair value through profit or loss

- These comprise structured deposit liabilities recognised in the prior year following the extinguishment of the swap agreement to Castle Trust Income Housa plc ("CTIH") and the Castle Trust Growth Housa PC ("PC").

- During the prior year, following the successful Schemes of arrangement, the customers linked to the swap arrangement with CTIH and PC agreed to give up their rights against CTIH and PC in return for getting the right to an equivalent value deposit in the Company. These new structured deposits remain in this classification.

Historically, loans to customers at fair value through profit or loss included house price linked products: Partnership Mortgages ("PMs"), Index Profit Share mortgages ("IPS") and Buy-to-let equity loans ("BTLEL").

- PMs were only available to owner occupiers with a term of c15 years and more. The repayment amount incorporated a profit/loss share based on any change in the value of the individual's mortgaged property.
- BTLELs were available to buy-to-let investors only with a term of up to 10 years. The repayment amount incorporated a profit share based on any change in the value of the individual's mortgaged property.
- IPS mortgages were available to buy-to-let investors and owner occupiers (who are exempt from the Consumer Credit Act ("CCA") (via the high net worth / business exemption tests)) with a term of typically 5 years. The original amount of the loan is repayable at redemption plus a deferred interest component (typically 5% pa where applicable) plus typically one times the increase in value of the national Halifax House Price Index ("HHPI"), if the property has increased in value, or the minimum repayment amount (typically 3.5% pa), whichever is greater.

In 2019, the embedded house price derivatives of all the mortgages designated at fair value through profit or loss were sold to CTC Holdings (Cayman) Limited except for two mortgages which were not sold. In the prior year, the terms and conditions of one of these two loans were amended so that it became substantially remodified. It was thus derecognised from "Designated at fair value" and re-recognised as "At amortised cost." There is consequently one loan left designated at fair value at the year end and no other assets at fair value through profit or loss.

**Financial liabilities at amortised cost**

Financial liabilities at amortised cost are non-derivative financial liabilities with fixed or determinable payments that are not quoted in an active market. The Company classifies the following financial liabilities at amortised cost:

- Trade and other payables
- Amounts due to customers
  - During the prior year, following the successful Schemes of arrangement, the customers linked to the Borrower Loan agreement with Castle Trust Direct Limited ("CTD") agreed to give up their rights against CTD in return for getting the right to an equivalent value deposit in the Company. These new fixed term deposits remain in this classification.
- Funding due to group companies
  - the Borrower Loan Agreement liability to its subsidiary Castle Trust Direct Limited ("CTD"), in order to allow CTD to pay interest on and the amount due on the relevant maturity date of the Fortress Bonds sold to customers, and the Master Intra Group Lending Agreement ("MILA") comprising intercompany loans for general operational funding to Omni Capital Retail Finance Limited ("OMNI") and Castle Trust Capital Management Limited ("CTCM").

After initial measurement, financial liabilities at amortised cost are subsequently measured at amortised cost using the EIR methodology. Amortised cost is calculated by taking into account any discount or premium on issue funds, and costs that are an integral part of the EIR. A compound financial instrument which contains both a liability and an equity component is separated at the issue date. The EIR amortisation is included in interest and similar expense in the statement of comprehensive income.

***2.4.2.3 Derecognition***

*Derecognition due to substantial modification of terms and conditions*

The Company derecognises a financial asset when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan, with the difference recognised as a derecognition gain or loss, to the extent that an impairment loss has not already been recorded. The newly recognised loans are classified as Stage 1 for ECL measurement purposes, unless the new loan is deemed to be Purchased or Credit Impaired ("POCI").

When assessing whether or not to derecognise a financial asset, amongst others, the Company considers the following factors: introduction of an equity feature; change in counterparty and if the modification is such that the instrument would no longer meet the SPPI criterion.

If the modification does not result in cash flows that are substantially different, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, the Company records a modification gain or loss, to the extent that an impairment loss has not already been recorded.

*Derecognition other than for substantial modification*

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when the rights to receive cash flows from the financial asset have expired. The Company also derecognises the financial asset if it has both transferred the financial asset and the transfer qualifies for derecognition.

The Company has transferred the financial asset if, and only if, either:

- The Company has transferred its contractual rights to receive cash flows from the financial asset; or
- It retains the rights to the cash flows, but has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass–through' arrangement

Pass-through arrangements are transactions whereby the Company retains the contractual rights to receive the cash flows of a financial asset (the 'original asset'), but assumes a contractual obligation to pay those cash flows to one or more entities (the 'eventual recipients'), when all of the following three conditions are met:

- The Company has no obligation to pay amounts to the eventual recipients unless it has collected equivalent amounts from the original asset, excluding short-term advances with the right to full recovery of the amount lent plus accrued interest at market rates;
- The Company cannot sell or pledge the original asset other than as security to the eventual recipients; and
- The Company has to remit any cash flows it collects on behalf of the eventual recipients without material delay.

In addition, the Company is not entitled to reinvest such cash flows, except for investments in cash or cash equivalents including interest earned, during the period between the collection date and the date of required remittance to the eventual recipients.

A transfer only qualifies for derecognition if either:

- The Company has transferred substantially all the risks and rewards of the asset; or
- The Company has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

The Company considers control to be transferred if and only if, the transferee has the practical ability to sell the asset in its entirety to an unrelated third party and is able to exercise that ability unilaterally and without imposing additional restrictions on the transfer.

When the Company has neither transferred nor retained substantially all the risks and rewards and has retained control of the asset, the asset continues to be recognised only to the extent of the Company's continuing involvement, in which case, the Company also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Company has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration the Company could be required to pay. If continuing involvement takes the form of a written or purchased option (or both) on the transferred asset, the continuing involvement is measured at the value the Company would be required to pay upon repurchase. In the case of a written put option on an asset that is measured at fair value, the extent of the entity's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

*Derecognition of financial liabilities*

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in the statement of comprehensive income.

### 2.4.3 Derivative held for risk management

The Company uses derivative financial instruments (interest rate swaps) to manage its exposure to interest rate risk. In accordance with the Group Market and Liquidity Risk Policy, the Company does not hold or issue derivative financial instruments for proprietary trading.

Derivative financial instruments are recognised at their fair value with changes in their fair value taken to profit or loss. Fair values are calculated by discounting cash flows at the prevailing interest rates. All derivatives are classified as assets when their fair value is positive and as liabilities when their fair value is negative. If a derivative is cancelled, it is derecognised from the Consolidated Statement of Financial Position.

### 2.4.4 Impairment of financial assets

The Company records the allowance for expected credit losses for all financial assets, together with loan commitments and financial guarantee contracts, in this section all referred to as 'financial instruments'. Equity instruments are not subject to impairment under IFRS 9. Cash and cash equivalents follow the low credit risk regime.

***Overview of the ECL principles***

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12m ECL). The Company's policies for determining if there has been a significant increase in credit risk are set out in Note 23.1.

The 12m ECL is the portion of LTECLs that represent the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Both LTECLs and 12m ECLs are calculated on an individual basis.

The Company has established a policy to perform an assessment, half-yearly, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument.

Based on the above process, the Company groups its loans into Stage 1, Stage 2 and Stage 3, as described below:

- Stage 1: When loans are first recognised, the Company recognises an allowance based on 12m ECLs. Stage 1 loans also include facilities where the credit risk has improved and the loan has been reclassified from Stage 2.
- Stage 2: When a loan has shown a significant increase in credit risk since origination, the Company records an allowance for the LTECLs. Stage 2 loans also include facilities, where the credit risk has improved and the loan has been reclassified from Stage 3.
- Stage 3: Loans considered credit-impaired (as outlined in Note 23.1). The Company records an allowance for the LTECLs.

Please also refer to note 23.1.5.

For financial assets for which the Company has no reasonable expectations of recovering either the entire outstanding amount, or a proportion thereof, the gross carrying amount of the financial asset is reduced. This is considered a (partial) derecognition of the financial asset.

***The calculation of ECLs***

The Company calculates ECLs based on five probability-weighted scenarios to measure the expected cash shortfalls, discounted at the EIR. A cash shortfall is the difference between the cash flows that are due in accordance with the contract and the cash flows that are expected to be received.

The mechanics of the ECL calculations are outlined below and the key elements are, as follows:

- PD: The Probability of Default is an estimate of the likelihood of default over a 12 month period then extrapolated over the life of each loan.
- EAD: The Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.
- LGD: The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that are expected to be received, including from the realisation of any collateral.
- Loan commitments: When estimating LTECLs for undrawn loan commitments, the Company estimates the expected portion of the loan commitment that will be drawn down over its expected life. The ECL is then based on the present value of the expected shortfalls in cash flows if the loan is drawn down, based on a probability-weighting of the five scenarios. The expected cash shortfalls are discounted at the EIR of the loan.

When estimating the ECLs, the Company considers five scenarios (a base case, a mild upside, an upside, a downside and a severe downside). Each of these is associated with different PDs, EADs and LGDs. When relevant, the assessment of multiple scenarios also incorporates how defaulted loans are expected to be recovered, including the probability that the loans will cure and the value of collateral or the amount that might be received for selling the asset. The maximum period for which the credit losses are determined is the contractual life of a financial instrument unless the Company has the legal right to call it earlier.

Impairment losses and releases are accounted for and disclosed separately from modification losses or gains that are accounted for as an adjustment of the financial asset's gross carrying value. Provisions for ECLs for undrawn loan commitments are assessed as part of the ECL calculation.

***Forward looking information***

In its ECL models, the Company uses the following forward-looking information as economic inputs:

- GDP growth;
- Unemployment rates;
- Central Bank base rates; and
- House price index.

The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are material.

***Collateral valuation***

To mitigate its credit risks on financial assets, the Company seeks to use collateral, where possible. The collateral comes in various forms, such as guarantees, real estate, receivables, inventories and other non-financial assets. The Company's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same is it was under IAS 39. Collateral, unless repossessed, is not recorded on the Company's statement of financial position. However, the fair value of collateral affects the calculation of ECLs. It is generally assessed, at a minimum, at inception and at default with values modelled through the lifetime of the loan.

To the extent possible, the Company uses active market data for valuing financial assets held as collateral. Other financial assets which do not have readily determinable market values are valued using models. Non-financial collateral, such as real estate, is valued based on data provided by third parties such as mortgage brokers, or based on housing price indices.

***Write-offs***

Financial assets are written off either partially or in their entirety only when the Company has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

***Forborne and modified loans***

The Company sometimes makes concessions or modifications to the original terms of loans as a response to the borrower's financial difficulties. Derecognition decisions and classification between Stage 2 and Stage 3 are determined on a case-by-case basis. If modifications are substantial, the loan is derecognised, as explained above.

When the loan has been renegotiated or modified but not derecognised, the Company also reassesses whether there has been a significant increase in credit risk. The Company also considers whether the assets should be classified as Stage 3. Once an asset has been classified as forborne, it will remain forborne for a minimum 1 year probation period. In order for the loan to be reclassified out of the forborne category, the customer has to meet all of the following criteria:

- All of its facilities have to be considered performing;
- The probation period of one year has passed from the date the forborne contract was considered performing; and
- Regular payments of more than an insignificant amount of principal or interest have been made during the probation period.

Details of forborne assets are disclosed in Note 23.1.

**2.4.5 Cash and cash equivalents**

Cash and cash equivalents comprise cash and highly liquid financial assets with original maturities of less than three months from the date of acquisition subject to an insignificant risk of changes in their fair value.

**2.4.6 Property and equipment and right-of-use assets**

Property and equipment is stated at cost excluding the costs of day-to-day servicing, less accumulated depreciation and accumulated impairment in value. Changes in the expected useful life are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

Depreciation is calculated using the straight-line method to write down the cost of property and equipment to their residual values over their estimated useful lives. The estimated useful lives are as follows:

- Computer equipment: 3 years
- Office equipment: 3 years
- Leasehold improvements Over the term of the lease
- Right of use assets Over the term of the lease

Property and equipment is derecognised on disposal or when no future economic benefits are expected from its use. Any gain or loss arising on the derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is recognised in other operating income in the statement of comprehensive income in the year the asset is derecognised.

Right-of-use assets are presented as described in note 2.4.9.

**2.4.7 Intangible assets**

Intangible assets are identifiable non-monetary assets without physical substance. An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Company.

***Internally generated***

In some instances, the Company develops its own operational systems, primarily a suite of systems that allow the Company to operate, record and value its products. These systems are developed in separate releases. The cost of each release can be measured reliably and the future economic benefits can be assessed as certain to flow to Castle Trust.

Research costs are expensed as incurred. Development expenditures on an individual project are recognised as an intangible asset when the requirements of IAS 38 are met.

In some instances, a number of technical releases are required before the system can be said to achieve the requirements of IAS 38 Intangible Assets, in which case, the related expenses are capitalised as research and development costs as long as the technical and operational feasibility of the asset has been established. Once the resultant system(s) meets the definition as such under IAS 38, the assets are transferred into the computer software category of intangible assets.

The estimated useful lives are as follows:

- Internally developed software: 5 years

Amortisation of the asset begins when development is complete and the asset is available for use.

Each asset, or related group of assets, is assessed as to its expected useful life and the expected pattern of benefits to the Company over that period. Each asset is amortised on a systematic (straight line) basis and the amortisation share is recorded in depreciation and amortisation. Research and development costs are not amortised until the resultant system has met the criteria of a computer system and has been transferred into that category.

**2.4.8 Provisions**

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to any provision is presented in the statement of comprehensive income net of any reimbursement. A contingent liability is disclosed where this is not probable but more likely than remote.

**2.4.9 Leases**

The Company assesses at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Company does not act as a lessor.

The Company recognises right-of-use assets at the commencement date of the lease (i.e. the date the underlying asset is available for use). Right-of-use assets are measured at cost, less and accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less and lease incentives received. Right-of-use assets are depreciated in a straight-line basis over the lease term.

The right-of-use assets are presented within Note 16 Property and equipment and right-of-use assets and are subject to impairment in line with the Company's policy as described in note 2.4.11 Impairment of non-financial assets.

At the commencement date of the lease, the Company recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (less any lease incentives receivable), variable lease payments that depend on an index or rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Company and payments of penalties for terminating the lease, if the lease term reflects exercising the option to terminate. Variable lease payments that do not depend on an index or a rate are recognised as expenses in the period in which the event or condition that triggers the payment occurs.

There were no concessions, payment holidays or breaches of lease contract as a result of the Covid-19 pandemic.

The Company cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate ('IBR') to measure lease liabilities. The IBR is the rate of interest that the Company would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Company 'would have to pay', which requires estimation when no observable rates are available (such as for subsidiaries that do not enter into financing transactions) or when they need to be adjusted to reflect the terms and conditions of the lease (for example, when leases are not in the subsidiary's functional currency).The Company estimates the IBR using observable inputs (such as market interest rates) when available and is required to make certain entity-specific adjustments (such as the subsidiary's stand-alone credit rating, or to reflect the terms and conditions of the lease).

The average lease term is 5.8 years.

### 2.4.10 Taxes

**Current tax**

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date.

**Deferred tax**

Deferred tax is provided on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit and loss
- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that temporary differences will not reverse in the foreseeable future

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

- Where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that the future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes related to the same taxable entity and the same taxation authority.

See note 7 for further description of the current status of deferred tax assets.

### 2.4.11 Impairment of non-financial assets

The Company assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Company estimates the asset's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of comprehensive income.

Both internal and external sources of information have been used to assess impairment. As a result of the continued uncertainty as to recoverable amounts in the light of the pandemic, the Company continues to monitor the impairment of non-financial assets closely.

### 2.4.12 Impairment of other financial assets

IFRS 9 allows a simplified approach to assess impairment of trade receivables, contract assets and lease receivables. The simplified approach allows lifetime expected losses on trade receivables, contract assets and lease receivables to be recognised without the need to identify significant increases in credit risk. The Company has adopted this simplified approach in its assessment of impairment of other financial assets by determining the appropriate grouping of receivables by product type and rating, determining the period over which historical loss rates are appropriate and then determining the historical loss rates based on the forward looking macro-economic factors identified for the Company. The Company determined the appropriate Probability of Default ("PD") estimate for trade receivables. contract assets and lease receivables by reference to publicly available credit ratings, the Loss Given Default by comparison with other similar exposures without eligible collateral and the Exposure at Default by using the outstanding balance at the reporting date.

### 2.4.13 Equity-settled transactions

The cost of equity-settled transactions is determined by the fair value at the date when the grant is made using an appropriate valuation model.

That cost is recognised in staff costs, together with a corresponding increase in equity (retained earnings), over the period in which the service and, where applicable, the performance conditions are fulfilled (the vesting period). The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Castle Trust's best estimate of the number of shares that will ultimately vest. The expense or credit in the statement of profit or loss for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

Service and non-market performance conditions are not taken into account when determining the grant date fair value of awards, but the likelihood of the conditions being met is assessed as part of Castle Trust's best estimate of the number of shares that will ultimately vest. Market performance conditions are reflected within the grant date fair value. Any other conditions attached to an award, but without an associated service requirement, are considered to be non-vesting conditions. Non-vesting conditions are reflected in the fair value of an award and lead to an immediate expensing of an award unless there are also service and/or performance conditions.

No expense is recognised for awards that do not ultimately vest because non-market performance and/or service conditions have not been met. Where awards include a market or non-vesting condition, the transactions are treated as vested irrespective of whether the market or non-vesting condition is satisfied, provided that all other performance and/or service conditions are satisfied.

When the terms of an equity-settled award are modified, the minimum expense recognised is the grant date fair value of the unmodified award, provided the original terms of the award are met. An additional expense, measured as at the date of modification, is recognised for any modification that increases the total fair value of the share-based payment transaction, or is otherwise beneficial to the employee. Where an award is cancelled by the entity or by the counterparty, any remaining element of the fair value of the award is expensed immediately through profit or loss.

The Covid-19 pandemic has had no material impact on the probability of satisfying non-market performance vesting conditions over the vesting period under share-based payment arrangements.

#### *i. Classification and measurement*

As described in note 2.4.2.2 above, IPS mortgages issued subsequent to 1 October 2014 are no longer bifurcated.

### 2.4.14 Government Grants

The Company has taken advantage of the Government furlough scheme during the year.

Government grants are recognised in profit or loss on a systematic basis over the periods in which the Company recognises as expenses the related costs for which the grants are intended to compensate. Direct cash assistance or subsidies were measured at fair value.

There are no unfulfilled conditions and other contingencies that have been recognised.

Grants related to income are presented as a deduction in reporting the related expense. The total value of government grants is not material in current year and therefore has not been separately disclosed in the financial statements.

### 2.5 New and amended standards and interpretations

The nature and effect of the changes as a result of adoption of this new accounting standard are described in Note 2.6 below. Several other amendments and interpretations apply for the first time in 2022, but do not have an impact on the Company's financial statements.

The new and amended standards and interpretations are effective for annual periods beginning on or after1 January 2022, unless otherwise stated. The Company has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective.

### 2.6 Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Company's consolidated financial statements do not affect the Company. The Company does not intend to adopt these standards early, so they will be adopted in the relevant year of mandatory adoption.

***IFRS 9 Financial Instruments – Fees in the '10 per cent' test for derecognition of financial liabilities***

As part of its 2018-2020 Annual Improvements to IFRS standards process, the IASB issued an amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment. The amendment is effective for annual reporting periods beginning on or after 1 January 2022 with earlier adoption permitted. The Company will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual period in which it will first apply the amendment and does not expect this will result in a material impact on its financial statements.

***Definition of Accounting Estimates - Amendments to IAS 8***

In February 2021, the IASB issued amendments to IAS 8, in which it introduces a definition of 'accounting estimates'. The amendments clarify the distinction between changes in accounting estimates and changes in accounting policies and the correction of errors. Also, they clarify how entities use measurement techniques and inputs to develop accounting estimates. The amendments are effective for annual reporting periods beginning on or after 1 January 2023 and apply to changes in accounting policies and changes in accounting estimates that occur on or after the start of that period. Earlier application is permitted as long as this fact is disclosed. The amendments are not expected to have a material impact on the Company.

***Disclosure of Accounting Policies - Amendments to IAS 1 and IFRS Practice Statement 2***

In February 2021, the IASB issued amendments to IAS 1 and IFRS Practice Statement 2 Making Materiality Judgements, in which it provides guidance and examples to help entities apply materiality judgements to accounting policy disclosures. The amendments aim to help entities provide accounting policy disclosures that are more useful by replacing the requirement for entities to disclose their 'significant' accounting policies with a requirement to disclose their 'material' accounting policies and adding guidance on how entities apply the concept of materiality in making decisions about accounting policy disclosures. The amendments to IAS 1 are applicable for annual periods beginning on or after 1 January 2023 with earlier application permitted. Since the amendments to the Practice Statement 2 provide non-mandatory guidance on the application of the definition of material to accounting policy information, an effective date for these amendments is not necessary. The Company is currently assessing the impact of the amendments to determine the impact they will have on the Company's accounting policy disclosures.

There are other standards and amendments that will apply in future periods but which will also not have a material impact on the Company:

| New or amended standard or interpretation | Effective date – for annual periods beginning on or after |
|---|---|
| Amendments to IAS 1 Classification of liabilities as current or non-current and Classification of Liabilities as Current or Non-current- Deferral of Effective Date | 1 January 2023 |
| Amendments to IFRS 10 and IAS 28 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture | 1 January 2023 |
| Amendments to IAS 8 Definition of Accounting Estimates | 1 January 2023 |
| Amendments to IAS 12 Deferred Tax related to Assets and Liabilities arising from a Single Transaction | 1 January 2023 |
| IFRS 17 (including the June 2020 Amendments to IFRS 17) Insurance Contracts | 1 January 2023 |

## 3 Interest and similar income

The following table summarises the components of interest and similar income:

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| **Interest and similar income calculated using EIR** | | |
| **On financial assets at amortised cost** | | |
| Loans to customers | 27,632 | 30,403 |
| | 27,632 | 30,403 |
| **Other interest and similar income** | | |
| MILA interest | 5,390 | 4,687 |
| Debt instruments | 19 | 35 |
| Bank of England interest | 903 | 2 |
| Other income | 103 | - |
| | 6,415 | 4,724 |
| **Total interest and similar income** | 34,047 | 35,127 |

## 4 Interest and similar expense

The following table summarises the components of interest and similar expense:

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Interest expense on financial liabilities at fair value through profit or loss: Housas | 20 | 32 |
| Customer deposits interest expense | 8,245 | 10,789 |
| Interest expense on leases | 49 | 52 |
| Other interest expense | 194 | - |
| | 8,508 | 10,873 |

## 5 Realised and unrealised (loss) on financial instruments at fair value through profit or loss

The following tables summarise the components of realised and unrealised gains and losses:

### 5.1 Realised (losses)

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Net realised (loss) on financial liabilities designated at fair value through profit or loss | - | (84) |
| Net realised (loss) on financial instruments at fair value through profit or loss | - | (84) |

### 5.2 Unrealised (losses) / gains

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Net unrealised (loss) / gain on financial assets designated at fair value through profit or loss | (427) | (1,086) |
| Net unrealised (loss) / gain on financial liabilities designated at fair value through profit or loss | (112) | (158) |
| Net unrealised gain on derivatives at fair value through profit or loss | 3,219 | - |
| Net unrealised (loss) / gain on financial instruments at fair value through profit or loss | 2,680 | (1,244) |
| | | |
| **Total realised/ unrealised (loss) /gain on financial instruments at fair value through profit or loss** | 2,680 | (1,328) |

Gains and losses for financial liabilities relate to fair value movements on the structured deposits. Gains and losses on financial assets related to fair value movements on the mortgage held at fair value.

## 6 Administrative expenses

The following tables summarise the components of staff and other administrative expense:

| **Staff expenses** | **2022 £'000** | 2021 £'000 |
|---|---|---|
| Wages and salaries | **14,365** | 12,808 |
| Social security costs | **1,524** | 1,238 |
| Company contributions to defined contribution pension plan | **504** | 410 |
| Termination costs | **-** | - |
| Other personnel costs | **562** | 557 |
| **Total staff expenses** | **16,955** | 15,013 |

| **Other operating expenses** | **2022 £'000** | 2021 £'000 |
|---|---|---|
| Advertising and marketing | **380** | 367 |
| Professional fees and other operating expenses | **2,178** | 4,812 |
| Non-recoverable VAT expense | **1,021** | 1,799 |
| Bank charges and similar expense | **467** | 290 |
| **Total operating expenses** | **4,046** | 7,268 |
| **Total administrative expenses** | **21,001** | 22,281 |

The Company operates a defined contribution pension plan for eligible employees and contributes 6% of an employee's salary.

Operating expenses decreased in the year due to a reduction in professional fees and cost associated with special projects.

Included within professional fees are the costs of contractors of £480,000 (2021: £177,000).

Included within professional fees are the following expenses related to services provided by the Company's auditors:

| | **2022 £'000** | 2021 £'000 |
|---|---|---|
| Audit of the Company's statutory financial statements | **460** | 484 |
| **Non-audit services:** | | |
| Audit related assurance services | **85** | 30 |
| **Total company auditors' remuneration** | **545** | 514 |

### 6.1 Employee numbers

The following table summarises the monthly average number of people employed by the Company during the year.

| | **2022 Number** | 2021 Number |
|---|---|---|
| **Monthly average number of people employed in:** | | |
| Legal, compliance and risk | **20** | 21 |
| Sales and marketing | **31** | 27 |
| Operations | **163** | 154 |
| Monthly average number of people employed during the year | **214** | 202 |

### 6.2 Key management compensation

The Company considers that directors and members of the executive committee of the Company meet the definition of key management whose remuneration was received wholly from the Company. These costs were not recharged to other group undertakings. The following table presents key management personnel's compensation excluding directors as *director's compensation is set out separately below.*

| | **2022 £'000** | 2021 £'000 |
|---|---|---|
| **Compensation of key management personnel:** | | |
| Short-term employee benefits | **2,173** | 1,976 |
| Post-employment benefits | **60** | 44 |
| | **2,233** | 2,020 |

*The comparatives have been updated to align with the revised group allocation methodology.

### 6.3 Directors' remuneration

The directors of the Company are also directors of other group undertakings. The directors received their total remuneration from the Company, with the costs not recharged to other group undertakings

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Aggregate remuneration in respect of qualifying services | 1,749 | 1,569 |
| Highest paid director's remuneration | 847 | 708 |
| Company contributions to defined contribution pension plan | | - |

Included within directors' remuneration are amounts of £nil (2021: £nil) as compensation for loss of office. 2 directors are entitled to contributions to pension plans.

## 7 Corporation tax

The following tables set out the components of income tax and the reconciliation of the total tax charge to the tax charge that would apply if all profits had been charged at the Company's corporate tax rate for the current and prior year.

**Total tax**

| | Year ended 30 September 2022 | Year ended 30 September 2021 |
|---|---|---|
| **Profit** | | |
| *Analysis of tax charge on ordinary activities* | £'000 | £'000 |
| UK corporation tax on results for the current year | 261 | 25 |
| Adjustment in respect of prior years | 73 | - |
| ***Total current tax*** | 334 | 25 |
| *Deferred Tax* | | |
| Origination and reversal of temporary differences | 1,173 | - |
| Changes in tax rates | (32) | - |
| Recognition of previously unrecognised deferred tax asset | 659 | (9,043) |
| Adjustment in respect of prior years | 345 | - |
| **Total deferred tax** | 2,145 | (9,043) |
| **Total tax charge / (credit)** | 2,479 | (9,018) |
| **Factors affecting tax charge for the current year** | | |
| Profit / (loss) on ordinary activities before tax | 4,460 | (2,265) |
| UK corporation tax at 19% (2021: 19%) | 847 | (430) |
| Effects of: | | |
| Adjustments in respect of prior years | 417 | - |
| Disallowable expenses | 179 | 3,901 |
| Income not taxable | (21) | (3,489) |
| Transfer pricing adjustment | 430 | - |
| Impact of movements in unrecognised deferred tax | 659 | (9,000) |
| Impact of change in tax rate | (32) | - |
| **Total tax charge / (credit)** | 2,479 | (9,018) |

**Analysis of deferred tax asset**

| **Deferred tax** | **Year ended 30 September 2022** | Year ended 30 September 2021 |
|---|---|---|
| *Movement on deferred taxation balance in the year* | **£'000** | £'000 |
| Opening asset | **(9,043)** | - |
| Recognised in profit and loss | **2,145** | (9,043) |
| Adjustments in respect of prior years | **-** | - |
| **Closing asset** | **(6,898)** | (9,043) |
| | | |
| **Analysis of deferred tax asset** | | |
| Assets | | |
| Losses | **(6,714)** | (8,752) |
| Other temporary differences | **(270)** | (300) |
| Fixed assets | **(217)** | (213) |
| | **(7,201)** | (9,265) |
| | | |
| Liabilities | | |
| Other temporary differences | **-** | - |
| Fixed assets | **303** | 222 |
| | **303** | 222 |
| | **-** | |
| **Net deferred tax asset** | **(6,898)** | (9,043) |

**Temporary differences on which deferred tax has not been recognised**

| | | |
|---|---|---|
| Losses | **2,636** | 4,146 |
| | **2,636** | 4,146 |

A deferred tax asset in respect of corporation tax losses is recognised based on the expected utilisation of the loss against forecast profits based on the Company's current business plan for the period up to 30 September 2026.

As at 30 September 2022, the Company had trading losses of £30,140,000 (2021: £41,516,000), short term timing differences of £1,099,000 (2021: £1,257,000) and decelerated capital allowances of £881,000 (2021: £856,000). The Company has limited recognition of deferred tax to the value of four years forecasted profit; hence deferred tax has not been recognised on £2,635,000 (2021: £4,146,000) of losses. A deferred tax asset of £7,201,000 (2021: £9,265,000) has thus been recognised, which is disclosed net of a deferred tax liability giving a net deferred tax asset of £6,898,000 (2021: £9,043,000).

An increase in the UK corporation rate from 19% to 25% (effective 1 April 2023) was substantively enacted on 24 May 2021. This will increase the Company's corporation tax charge accordingly. The deferred tax asset at 30 September 2022 has been calculated based on these rates, reflecting the expected timing of reversal of the related temporary differences.

## 8 Cash and cash equivalents

The following table sets out each component of cash and cash equivalents:

| | **2022** | 2021 |
|---|---|---|
| | **£'000** | £'000 |
| Loans and advances to central banks | **78,607** | 18,502 |
| Loans and advances to banks | **65,099** | 36,042 |
| **Total cash and cash equivalents** | **143,706** | 54,544 |

Loans and advances to central banks constitute balances held with the Bank of England. Loans and advances to banks constitute balances held with NatWest and HSBC to facilitate operating requirements.

The carrying value of loans and advances to central banks and loans and advances to banks are carried at amortised cost which approximates to fair value. The expected credit losses on these balances are considered to be immaterial as detailed in note 23.1.

## 9 Amounts due to and from credit institutions

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Amounts held as cash margin | 1,000 | - |
| Variation margin paid | 970 | - |
| **Total amounts due from credit institutions** | **1,970** | - |

The amount of £1,000,000 represents net margin held for interest rate swaps. This is an encumbered balance given to a credit institution against derivatives contracts. The £970,000 represents variation margin paid on interest rate swaps.

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Variation margin received | 4,100 | - |
| **Total amounts due to credit institutions** | **4,100** | - |

The £4,100,000 represents variation margin received.

Amounts due to and from credit institutions are valued at amortised cost which approximates to fair value.

## 10 Debt instruments

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Treasury Bills | 5,000 | 19,999 |
| **Total debt instruments** | **5,000** | 19,999 |

Debt instruments comprise Treasury Bills held at amortised cost purchased during the year. The carrying value of these balances approximates to fair value. The reduction in the current year is due to the Company being able to access the Bank of England Reserve account from October 2021. The expected credit losses on these balances are considered to be immaterial as detailed in note 23.1.

## 11 Trade and other receivables

The following table sets out carrying amount of trade and other receivables:

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Trade and other receivables | 1,003 | 817 |
| Impairment | - | - |
| **Total trade and other receivables** | **1,003** | 817 |

The fair value of trade and other receivables approximates to the carrying value as presented in the statement of financial position as the receipt of the related cash is not more than three months from the date of the recognition of the asset and is not subject to significant credit risk.

## 12 Loans to customers at amortised cost

Loans to customers at amortised cost comprise property loans (Serviced & Interest Roll Up mortgages, RDF loans) and the fixed income component of all house price linked loans.

The following table sets out the carrying value of loans to customers by product type:

| | Amortised Cost 30 September 2022 £'000 | Gross 30 September 2022 £'000 | ECL 30 September 2022 £'000 |
|---|---|---|---|
| Property loans | 453,815 | 463,683 | (9,868) |
| **Total loans to customers at amortised cost** | 453,815 | 463,683 | (9,868) |

| | Amortised Cost 30 September 2021 £'000 | Gross 30 September 2021 £'000 | ECL 30 September 2021 £'000 |
|---|---|---|---|
| Property loans | 394,523 | 403,196 | (8,673) |
| **Total loans to customers at amortised cost** | 394,523 | 403,196 | (8,673) |

| **Movement in impairment provision in year** | 30 September 2021 £'000 | 30 September 2022 £'000 |
|---|---|---|
| Property loans | 1,500 | 1,195 |
| **Total movement in impairment provisions** | 1,500 | 1,195 |
| **Write-offs in year** | 392 | 335 |
| ***Total impairment losses on loans to customers*** | 1,892 | 1,530 |

No assets that have been written off are still subject to enforcement activity. For fair values, fair value hierarchy classifications, sensitivities and modelling techniques refer to Note 22.

### Reconciliation of gross loan and ECL movements in the year

The following tables set out a reconciliation, from the start to the end of the year, of the movement in gross loan balance and ECL movement balance in the statement of financial position for loans and advances at amortised cost.

| | Stage 1 | | Stage 2 | | Stage 3 | | Total | |
|---|---|---|---|---|---|---|---|---|
| **Property loans** | Gross £'000 | ECL £'000 | Gross £'000 | ECL £'000 | Gross £'000 | ECL £'000 | Gross £'000 | ECL £'000 |
| **Gross carrying amount as at 1 Oct 2021** | 224,629 | (684) | 116,924 | (1,034) | 61,643 | (6,955) | 403,196 | (8,673) |
| New assets originated or purchased | 240,378 | (226) | 3,670 | (29) | 833 | (112) | 244,881 | (367) |
| Assets derecognised or repaid | (106,508) | 283 | (67,877) | 499 | (23,206) | 708 | (197,591) | 1,490 |
| Transfers to Stage 1 | 1,115 | (37) | (1,115) | 37 | - | - | - | - |
| Transfers to Stage 2 | (17,651) | 65 | 19,046 | (145) | (1,395) | 80 | - | - |
| Transfers to Stage 3 | (12,437) | 211 | (9,076) | 103 | 21,513 | (314) | - | - |
| Amortisation of interest | 5,541 | - | 3,775 | - | 3,881 | - | 13,197 | - |
| Change in ECL on commitments | - | (3) | - | - | - | - | - | (3) |
| Impact on period end ECL of exposures transferred between stages during the period | - | 100 | - | (536) | - | (1,879) | - | (2,315) |
| **Total gross carrying amount at 30 September 2022** | 335,067 | (291) | 65,347 | (1,105) | 63,269 | (8,472) | 463,683 | (9,868) |

| Property loans | Stage 1 Gross £'000 | Stage 1 ECL £'000 | Stage 2 Gross £'000 | Stage 2 ECL £'000 | Stage 3 Gross £'000 | Stage 3 ECL £'000 | Total Gross £'000 | Total ECL £'000 |
|---|---|---|---|---|---|---|---|---|
| Gross carrying amount as at 1 Oct 2020 | 361,533 | (2,292) | 43,087 | (371) | 47,631 | (4,510) | 452,251 | (7,173) |
| Transfers in staging to adjust opening balances | | | | | | | - | - |
| New assets originated or purchased | 97,183 | (126) | 8,902 | (157) | 171 | (54) | 106,256 | (337) |
| | | | | | | | - | - |
| Assets derecognised or repaid | (142,858) | 614 | (14,470) | 82 | (19,048) | 489 | (176,376) | 1,185 |
| Transfers to Stage 1 | 653 | (8) | (653) | 8 | - | - | - | - |
| Transfers to Stage 2 | (77,048) | 410 | 77,048 | (410) | - | - | - | - |
| Transfers to Stage 3 | (24,975) | 400 | (2,875) | 23 | 27,850 | (423) | - | - |
| Interest accrual | 10,141 | - | 5,885 | | 5,039 | - | 21,065 | - |
| Change in ECL on commitments | - | 55 | - | - | - | - | - | 55 |
| Impact on period end ECL of exposures transferred between stages during the period | - | 263 | - | (209) | - | (2,457) | - | (2,403) |
| Total gross carrying amount at 30 September 2021 | 224,629 | (684) | 116,924 | (1,034) | 61,643 | (6,955) | 403,196 | (8,673) |

Interest income recognised during the year on Stage 3 impaired loans was £3,638,000 (2021: impaired loans £4,837,000)

## 13 Financial asset designated at fair value through profit or loss

A mortgage designated at fair value through profit or loss together is measured at fair value because it is managed and its performance is evaluated on a fair value basis. The mortgage asset is measured at fair value on a recurring basis and their valuation is categorised at Level 3. For fair value hierarchy classifications, modelling and sensitivities disclosures refer to Note 22.

The following tables show a reconciliation from the opening balances to the closing balances, including the total gains for the year that are recognised in the statement of comprehensive income within 'Realised / unrealised gain on financial instruments at fair value through profit or loss'.

In 2019, the embedded house price derivatives of all the mortgages designated at fair value through profit or loss were sold to CTC Holdings (Cayman) Limited except for two mortgages which were not sold. The remaining financial instruments, having been substantially modified, were thus derecognised. New financial instruments, being the remaining fixed income host contracts, were recognised as loans at amortised cost. Of the two mortgages which were not sold, one was substantially modified in the prior year, derecognised and re-recognised as a loan at amortised cost, leaving only one mortgage still recognised at fair value through profit or loss as at 30 September 2022. This one mortgage is classified as Level 3 in the fair value hierarchy in the year due to the significance of observable inputs used in the fair valuation.

| **Movements in the year to 30 September 2022** | **Index Profit Share mortgages £'000** | **Total £'000** |
|---|---|---|
| At 1 October 2021 | 4,474 | 4,474 |
| Net unrealised loss on financial assets designated at fair value through profit or loss | (427) | (427) |
| Movement in capitalised fees | 47 | 47 |
| **Closing balance at 30 September 2022** | 4,094 | 4,094 |

| Movements in the period to 30 September 2021 | Index Profit Share mortgages £'000 | Total £'000 |
|---|---|---|
| At 1 October 2020 | 5,506 | 5,506 |
| Net loss on financial assets designated at fair value through profit or loss | (1,032) | (1,032) |
| Closing balance at 30 September 2021 | 4,474 | 4,474 |

The total unrealised loss during the year were £(427,000) (2021: (£1,032,000)).

## 14 Derivatives assets

During the year the Company used interest rate swaps.

Margin of £1,000,000 (2021:nil) is included as loan and advances to credit institutions.

| | 2022 | | | | 2021 |
|---|---|---|---|---|---|
| | Contract or underlying principal amount | Positive market value | Negative market value | Total | Total |
| **Derivatives held for risk management** | £'000 | £'000 | £'000 | £'000 | £'000 |
| Interest rate swaps (not in hedging relationships) | 60,000 | 3,123 | - | 3,123 | - |
| **Total** | 60,000 | 3,123 | - | 3,123 | - |

The interest rate swaps are valued using a discounted cash flow model. The model is based on observable market inputs. The most significant input is the forward rate which is observed from the interest rate swap market.

For fair value hierarchy classifications and sensitivities disclosure refer to note 22.

## 15 Amounts due from group companies

| | 2022 | 2021 |
|---|---|---|
| | £'000 | £'000 |
| Amounts due under MILA from Omni | 188,795 | 152,074 |
| Omni intercompany loan | 426 | 377 |
| **Total amounts due from group companies** | 189,221 | 152,451 |

For fair value and fair value hierarchy classifications disclosure refer to note 22.

MILA funding is fixed rate intercompany funding designed to reduce interest rate risk in the Company. The terms of the MILA are up to 5 years (2021: 5 years). Interest is compounded daily based on the funds transfer pricing rate determined by CTC, based on underlying market conditions, which ranges from approximately 2.6% to 5.3% (2021: 2.4% to 5.3%). Interest is paid at maturity with the principal amount of the MILA. Refer to note 24 for details on the maturity profile of the MILA.

The combined ECL calculated across all intercompany exposures and the individual intercompany ECLs themselves are considered immaterial.

The intercompany loan relates to operating expenses recharges.

## 16 Property and equipment and right-of-use assets

The following table sets out components of property and equipment and a reconciliation of the cost and net book value during the year:

| | Office and computer equipment | Leasehold improvements | Right of Use Assets | Total |
|---|---|---|---|---|
| **Cost** | **£'000** | **£'000** | | **£'000** |
| At 1 October 2020 | 530 | 186 | 923 | 1,639 |
| Additions in year | 73 | - | - | 73 |
| Transferred from CTCM | 5 | - | 733 | 738 |
| Disposals in year | (63) | (18) | - | (81) |
| At 30 September 2021 | 545 | 168 | 1,656 | 2,369 |
| Additions in year | 102 | 391 | 321 | 814 |
| Written off in year | (45) | | - | (45) |
| **At 30 September 2022** | **602** | **559** | **1,977** | **3,138** |
| **Depreciation and impairment** | | | | |
| At 1 October 2020 | 259 | 168 | 12 | 439 |
| Depreciation charge for the year | 173 | - | 370 | 543 |
| Depreciation charge on disposed assets | (63) | - | - | (63) |
| At 30 September 2021 | 369 | 168 | 382 | 919 |
| Depreciation charge for the period | 138 | 59 | 474 | 671 |
| Depreciation on amounts written off | (45) | | - | (45) |
| **At 30 September 2022** | **462** | **227** | **856** | **1,545** |
| **Net book value** | | | | |
| At 30 September 2021 | 176 | - | 1,274 | 1,450 |
| **At 30 September 2022** | **140** | **332** | **1,121** | **1,593** |

Right of use assets relate to property leases capitalised in line with IFRS 16. The related lease liability is detailed in note 19.

There was no impairment necessary for the property and equipment as at 30 September 2022

## 17 Investment in subsidiaries

The following table sets out the carrying value of subsidiaries.

| Cost | £'000 |
|---|---|
| At 1 October 2020 | 73,941 |
| **At 30 September 2021** | **73,941** |
| Dissolved | (57,735) |
| **At 30 September 2022** | **16,206** |

| Impairment | |
|---|---|
| At 1 October 2020 | 39,734 |
| Impairment of investment in CTCM | 17,501 |
| Impairment of investment in CTD | 500 |
| **At 30 September 2021** | **57,735** |
| Dissolved | (57,735) |
| **At 30 September 2022** | **-** |

| Net book value | |
|---|---|
| At 30 September 2021 | 16,206 |
| **At 30 September 2022** | **16,206** |

The reversal of impairment of investment in CTCM and CTD arose following the winding up of these entities. An equivalent final dividend was received following a capital reconstruction in these subsidiaries as disclosed in the Income Statement.

The Company holds the following proportion of the nominal value (£0.10) of shares in the following Company subsidiary undertakings included in the consolidated accounts of the Castle Trust Holdings Group:

| Name of Company | Holding | Proportion of voting rights & nominal value of shares held | Nature of business | Country of incorporation |
|---|---|---|---|---|
| Castle Trust Capital Management Limited | Ordinary shares | 100% | Dissolved 11 January 2022 | UK |
| Castle Trust Direct plc | Ordinary shares | 100% | Dissolved 26 April 2022 | UK |
| Castle Trust Capital Nominees Limited* | Ordinary shares | 100% | Dissolved 2 November 2021 | UK |
| Castle Trust POS Limited | Ordinary shares | 100% | Holding company | UK |
| Omni Capital Retail Finance Limited** | Ordinary shares | 100% | Point of sale consumer finance provider | UK |
| Castle Trust Belfry Limited | | 0% | Dissolved 9 December 2021 | UK |

*The holding of CTCN was held indirectly via CTCM.

**The holding of Omni is held indirectly via CTPOS.

The registered office for all these companies is 10 Norwich Street, London, EC4A 1BD with the exception of Castle Trust Income Housa plc whose registered office and Castle Trust Belfry Limited whose registered office was 40a Station Road, Upminster, Essex, RM14 2TR.

## 18 Intangible assets

The following table sets out the net book value of intangible assets recorded in the statement of financial position by category of intangible asset. Software includes mortgage operations, valuation, administration and customer deposit systems.

| Cost | Internally developed software £'000 |
|---|---|
| At 1 October 2020 | 6,101 |
| Additions in the year | 1,027 |
| Written off in the year | (64) |
| At 30 September 2021 | 7,064 |
| Additions in the year | 1,862 |
| **At 30 September 2022** | **8,926** |
| **Accumulated amortisation and impairment** | |
| At 1 October 2020 | 1,808 |
| Amortisation charge for the year | 1,074 |
| Amortisation on written off assets | (4) |
| At 30 September 2021 | 2,878 |
| Amortisation charge for the year | 1,369 |
| **At 30 September 2022** | **4,247** |
| **Net book value** | |
| At 30 September 2021 | 4,186 |
| **At 30 September 2022** | **4,679** |

The remaining amortisation period of internally developed software is 3.4 years.

Amounts written off relate to systems that are no longer operational. There was no impairment necessary in the value of intangible assets as at 30 September 2022.

## 19 Trade and other payables

The following table sets out the components of trade and other payables.

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Trade creditors | 2,455 | 1,876 |
| Accruals and deferred income | 4,998 | 4,805 |
| Tax payable | 114 | 26 |
| Lease liabilities | 1,248 | 1,326 |
| **Total trade and other payables** | **8,815** | 8,033 |

Trade and other payables consist of expenses paid in relation to the on-going costs of the business. They are recorded at cost, which approximates to fair value due to the short payment terms on which Castle Trust operates, with the majority of trade liabilities being extinguished within 30 days of the recognition of the liability.

Lease liabilities relate to the occupation of premises in London and Basingstoke. The maturity profile this lease liabilities is detailed in Note 24.

## 20 Amounts due to customers at amortised cost

Amounts due to customers at amortised cost comprise of savings balances due to customers

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Amounts owed to customers | 724,595 | 557,956 |
| **Total amounts owed to customers at amortised cost** | **724,595** | 557,956 |

Refer to Note 23 for details on the maturity profile of the deposit accounts.

For fair value, fair value hierarchy classifications and sensitivities disclosure refer to note 22.

The hierarchy position is considered to be Level 3, as the lowest level input, being the discount rate, is unobservable.

## 21 Amounts due to customers at fair value through profit or loss

Financial liabilities at fair value through profit or loss include structured deposits that are designated at fair value through profit or loss.

On 22 June 2020, by Schemes of Arrangement, Housa customers with investments issued by subsidiary companies transferred their investment into new banking structured deposit products in the Company, the structure of which (return and maturity profile) matched their existing investment holding. For each series of Housas, CTC opened a corresponding structured deposit. These structured deposits replaced and exactly matched the previous intercompany swaps the Company held with Castle Trust Growth Housa PC and Castle Trust Income Housa PLC. These structured deposits, consistent with the Housas, are valued at fair value as the performance continues to be evaluated on a fair value basis.

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Structured deposits | 1,433 | 1,317 |
| **Total amounts due to customers at fair value through profit or loss** | **1,433** | 1,317 |

The existing book is in run-off. However, there were three main variants of the Housa issued which converted into structured deposits, as explained below.

Income Housas were Loan Notes issued up to July 2014 by Castle Trust Income Housa plc which paid investors a quarterly coupon. Growth Housas were participating preference shares of Castle Trust PCC issued up to October 2015 which paid investors a coupon at the maturity of the Housa. The Housa was a retail investment product of fixed term between 2 and 10 years.

The returns (and potentially share in losses) for both Growth and Income Housas were also linked to the movement in the Halifax House Price Index. Foundation Housas were participating preference shares of Castle Trust PCC issued up to October 2015 where the capital amount investors subscribed to was guaranteed.

Structured deposits/ Housas are measured at fair value (on a recurring basis) because they are managed and their performance is evaluated on a fair value basis. The following table shows a reconciliation from the opening balance to the closing balance, including the loss for the period that is recognised in the statement of comprehensive income.

| Structured Deposits | 2022<br>£'000 | 2021<br>£'000 |
|---|---|---|
| **Opening balance at beginning of year** | 1,317 | 1,444 |
| Net loss on financial liabilities at fair value through profit or loss | 137 | 158 |
| Redemptions in the year | (21) | (285) |
| **Closing balance at end of year** | 1,433 | 1,317 |

The total unrealised losses as at year end was £701,000 (2020 £565,000). For fair value hierarchy classifications and sensitivities disclosure refer to Note 22. There were no transfers into Level 3 assets other than the completions in the period, and no transfers out other than redemptions.

The change in fair value attributable to change in credit risk for financial liabilities designated at fair value through profit or loss is a loss of £(25,000) (2021: loss of £4,000). The difference between fair value and the amount contractually due at maturity is cumulatively £88,000 (2021: £421,000).

The changes in fair value attributable to changes in credit risk for financial liabilities designated at fair value through profit or loss have been calculated by determining the changes in credit spread implicit in the fair value of financial instruments issued by entities with similar credit characteristics.

For fair value hierarchy classifications, modelling and sensitivities disclosure refer to Note 22.

## 22 Fair value modelling, sensitivities and fair value hierarchy

### 22.1 Fair value modelling & sensitivities

The Company has developed a model to value its financial assets, liabilities and derivatives at fair value. The model uses stochastic techniques to calculate the net present value of expected future cash flows. The cash flows are based on assumptions about the range of possible future events and information concerning the terms of the financial instruments. It is run on a monthly basis for internal management information and board reporting purposes. It is run by a specialist team within Castle Trust within a control framework. Model assumptions are reviewed by the Board.

The models make use of certain significant model inputs. The inputs could be market quoted levels or unobservable inputs which are calibrated using a set of methodologies developed in conjunction with the valuation models. The most significant inputs are set out in the table below.

Level 1 inputs are quoted prices in active markets for identical assets or liabilities that the Company can access at the measurement date. Level 2 inputs are inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for the asset or liability.

There is significant correlation between model parameters where movements in a parameter would likely result in opposing movement in other parameters creating offsetting valuation impacts.

The fair value sensitivity to changes in the model inputs have been assessed using reasonable upward and downwards shifts to the model inputs while keeping all remaining inputs constant. The following tables set out the relevant sensitivities.

Sensitivity analysis has been provided below where a reasonable change in each input has a material impact on the reported figures. In determining this, a sensitivity range is defined for each parameter, such as the standard error of the estimated parameter value. In certain circumstances management's judgement is used where this is not always possible (such as where there is not sufficient data for each parameter). A threshold is defined and where the valuation sensitivity is greater than the threshold the parameter is included in the sensitivity disclosure below. The threshold applied is 1% of total mortgage assets.

**Mortgage fair value measurement**

The model was applied to mortgage product lending. As disclosed in note 13, there is one mortgage designated at fair value retained in the Company as at 30 September 2022 (2021: one mortgage). As the strike date of the embedded House Price Option has passed for this loan, its fair value is no longer sensitive to any changes in inputs into the model and its fair value has been estimated as the amount recoverable. The loan is classed as Level 3 due to low levels of observable inputs and increased uncertainty in the macroeconomic environment.

**Structured deposits liabilities fair value measurement**

The model, as applied to structured deposits, incorporates various inputs, of which the most significant are as follows:

| | | Range | | | | | Sensitivity | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | September 2022 | | September 2021 | | | September 2022 | | September 2021 | |
| Input | Description | Min | Max | Min | Max | Sensitivity Range | Min | Max | Min | Max |
| | | | | | | | £'000 | £'000 | £'000 | £'000 |
| Movement in HPI | Percentage movement since origination to indexed value | 43.8% | 92.1% | 34.4% | 73.0% | +-10% | (180) | 180 | (127) | 127 |
| Expected house price growth | Assumed annual rate of future HPI growth | 0.1% | -7.2% | 3.1% | 11.1% | | | | | |
| Volatility of the movement in HPI | Assumed annualised volatility of the future HPI returns | 0.0% | -2.5% | 11.2% | 11.2% | | | | | |
| Discount rates : | Derived to be consistent with future house price growth. | | | | | | | | | |
| | Risk free discount rates | 2.2% | 5.3% | 0.1% | 1.5% | | | | | |
| | Credit premium discount rate | 0.7% | 1.3% | 0.3% | 0.6% | | | | | |
| | House price risk premium | n/a | n/a | 21.1% | 21.1% | +-10% | n/a | n/a | (143) | 112 |

The assumption for house price growth is currently 1.7% which has been based on external forecasts and market consensus of the expected growth in house prices. This is a long-term average growth rate and as such a short term drop in house price growth rates as a result of recent economic uncertainty and interest rate rises will have a lesser impact on this long term average. However, it is expected that uncertainty will be higher in the near term as a result of these factors. A sudden drop in house prices of up to 10% is considered a reasonably possible due to recent macro-economic factors and this is reflected in the note under the sensitivity for movement in HPI.

### 22.2 Fair values and fair value hierarchy analysis

Fair value is 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. The tables below show the determination of fair value according to a three-level valuation hierarchy. All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole.

For loans and receivables and financial liabilities held at amortised cost fair values are determined according to the most recent and where possible published interest rates, adjusted for the time value of money and credit spread risk, using a discounted cash flow model. The hierarchy position is considered to be Level 3, as the lowest level input, being the discount rate, is unobservable.

For amounts due to customers for deposits a range of fair value is determined using the latest issuance rate and both an external and internal funding rate. The carrying value of the deposits sits within the range of calculated fair values and so is used as an approximation of fair value. The hierarchy position is considered to be Level 3, as the lowest level input that is significant to the valuation, being the discount rate, is unobservable.

The Company recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

For financial instruments where the receipt of the related cash is not more than three months from the date of the recognition of the asset/liability and which are not subject to significant credit risk, carrying value approximates fair value, and they are consequently not included in the fair value analysis below.

**As at 30 September 2022**

| Assets | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 | Carrying value £'000 |
|---|---|---|---|---|---|
| ***Non-recurring items*** | | | | | |
| Debt instruments | 5,000 | - | - | 5,000 | 5,000 |
| Loans to customers | | | | | |
| At amortised cost | - | - | 456,691 | 456,691 | 453,815 |
| ***Recurring item*** | | | | | |
| Loans to customers | | | | | |
| Designated at fair value through profit or loss | - | - | 4,094 | 4,094 | 4,094 |
| Derivative assets | - | 3,123 | - | 3,123 | 3,123 |
| **Total** | 5,000 | 3,123 | 460,785 | 468,908 | 466,032 |
| **Liabilities** | | | | | |
| ***Non-recurring items*** | | | | | |
| Amounts due to customers at amortised cost | - | - | 724,595 | 724,595 | 724,595 |
| ***Recurring item*** | | | | | |
| Amounts due to customers at fair value through profit or loss | - | - | 1,433 | 1,433 | 1,433 |
| **Total** | - | - | 726,028 | 726,028 | 726,028 |

As at 30 September 2021

| Assets | Level 1 £'000 | Level 2 £'000 | Level 3 £'000 | Total £'000 | Carrying value £'000 |
|---|---|---|---|---|---|
| *Non-recurring items* | | | | | |
| Debt instruments | 19,999 | - | - | 19,999 | 19,999 |
| Loans to customers | | | | | |
| At amortised cost | - | - | 405,424 | 405,424 | 394,523 |
| *Recurring item* | | | | | |
| Designated at fair value through profit or loss | - | - | 4,474 | 4,474 | 4,474 |
| Total | 19,999 | - | 409,898 | 429,897 | 418,996 |
| Liabilities | | | | | |
| *Non-recurring items* | | | | | |
| Amounts due to customers at amortised cost | - | - | 557,956 | 557,956 | 557,956 |
| *Recurring item* | | | | | |
| Amounts due to customers at fair value through profit or loss | - | - | 1,317 | 1,317 | 1,317 |
| Total | - | - | 559,273 | 559,273 | 559,273 |

There were no transfers in or out of Level 3 in the year.

**Movement table for recurring Level 3 instruments**

| | Mortgage designated at fair value through profit or loss £'000 | Financial liabilities at fair value through profit or loss £'000 |
|---|---|---|
| Opening balance at 1 October 2021 | 4,474 | (1,317) |
| Capitalised fees | 47 | - |
| Redemptions | - | 21 |
| Fair value movement | (427) | (137) |
| **Closing balance at 30 September 2022** | 4,094 | (1,433) |

| | Mortgage designated at fair value through profit or loss £'000 | Financial liabilities at fair value through profit or loss £'000 |
|---|---|---|
| Opening balance at 1 October 2020 | 5,506 | (1,444) |
| Capitalised fees | - | (158) |
| Redemptions | | 285 |
| Fair value movement | (1,032) | - |
| Closing balance at 30 September 2021 | 4,094 | (1,317) |

**Movement table for recurring Level 2 instruments**

| | Derivative Assets |
|---|---|
| | £'000 |
| Opening balance at 1 October 2021 | - |
| Net margin settlement | (96) |
| Fair value movement | 3,219 |
| **Closing balance at 30 September 2022** | 3,123 |

## 23 Risk management

The Company's activities expose it to various types of financial risk that are associated with the financial instruments and markets in which it participates. The main risk to which the Company is exposed is credit risk. In addition, the Company is also exposed to liquidity risk and market risk as these risks are inherent in the business. The Company use a comprehensive risk management approach across each business and risk type which is outlined in the risk management framework. The risk management framework is designed to ensure risks are identified, actively monitored, and support sustainable growth of the business with sound strategic decision making. The Company continues to actively review and develop its risk management framework and enhance its approach to managing risk with clear accountabilities. The Board is ultimately responsible for setting the risk appetite for each of these risks with the Company measuring its exposure to risk on a continual basis. The Company assesses its risks using stress-testing procedures, which is a key part of its risk management, capital adequacy and liquidity planning. Stress testing provides management with key insights into the impacts of severely adverse events identified by the Company and provides confidence to the Board, shareholders, and regulators on the Company's financial stability. The section below provides further details on financial risks only.

### 23.1 Credit risk

#### 23.1.1 Overview

Credit risk is the risk that a counterparty will fail to meet its obligations in accordance with agreed terms. In general, it arises from the counterparty being either unwilling or unable to settle its obligations. This risk is managed in the loan origination and servicing processes. In addition, mortgage credit risk is monitored via performance monitoring, including past due, maturity and concentration risk assessment. RDF loans are individually reviewed and monitored by the credit committee or the main Risk Committee if larger in size.

The Company manages its credit risk in accordance with policies set by the Board to ensure that the credit risk assumed is commensurate with the return required. The Company is exposed to credit risk from its loans to customers, cash and cash equivalents and its loans and advances to credit institutions. The Company's maximum exposure to credit risk is set out in the table below.

| As at 30 September 2022 | Stage 1 | Stage 2 | Stage 3 | ECL | Total |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Financial assets** | | | | | |
| Cash and cash equivalents | 143,706 | - | - | - | 143,706 |
| Debt instruments | 5,000 | - | - | - | 5,000 |
| Trade and other receivables | 1,003 | - | - | - | 1,003 |
| Loans to customers | | | | | |
| At amortised cost | | | | | |
| - Property loans | 335,067 | 65,347 | 63,269 | (9,868) | 453,815 |
| Designated at fair value through profit or loss | - | - | - | - | 4,094 |
| Derivative assets | - | - | - | - | 3,123 |
| Amounts due to group companies | 189,221 | - | - | - | 189,221 |
| | 673,997 | 65,347 | 63,269 | (9,868) | 799,962 |
| Loan commitments | 44,737 | - | - | - | 44,737 |

| As at 30 September 2021 | Stage 1 | Stage 2 | Stage 3 | ECL | Total |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| Financial assets | | | | | |
| Cash and cash equivalents | 54,544 | - | - | - | 54,544 |
| Debt instruments | 19,999 | | | | 19,999 |
| Trade and other receivables | 817 | - | - | - | 817 |
| Loans to customers | | | | | |
| At amortised cost | | | | | |
| - Property loans | 224,629 | 116,924 | 61,643 | (8,673) | 394,523 |
| Designated at fair value through profit or loss | - | - | - | - | 4,474 |
| Amounts due to group companies | 152,451 | - | - | - | 152,451 |
| | 452,440 | 116,924 | 61,643 | (8,673) | 626,808 |
| Loan commitments | 12,575 | - | - | - | 12,575 |

The fall in Stage 2 balances is principally due to the repayment of mortgage cases moved to stage 2 in the prior year following expiry of their initial COVID 19 extension.

Financial Instruments held at amortised cost are within the scope of the IFRS 9 impairment policy described in Note 2.4.12. IFRS 9 permits a simplified approach where it may be assumed that an instrument's credit risk has not increased significantly since initial recognition if it is determined to have a low credit risk at the reporting date. Such low risk instruments are categorised as stage 1, with the provision based upon a 12 month probability of default. The Company has applied this simplified approach to its cash and cash equivalents and debt instruments in accordance with its accounting policy (note 2.4.12) which is evidence that the instrument is of low risk. Trade and other receivables follows a simplified metrics based provision.

The Company assesses impairment on offers which have been made at year end, but not yet accepted. Whilst the offer value is only reflected on the balance sheet upon acceptance, the related impairment is included in Stage 1 above.

The impairment provisioning applied to the loan book provides an indicator of the overall credit quality of the loan portfolio. Movements in the coverage ratio (impairment provision value as a percentage of the gross loan value) can be used to understand how the credit position of the loans has evolved. The table below compares the coverage ratios by stage at the year-end date with the prior year.

**Coverage ratios**

| **30 September 2022** | **Stage 1** | **Stage 2** | **Stage 3** | **Total** |
|---|---|---|---|---|
| **Property** | **0.09%** | **1.69%** | **13.39%** | **2.13%** |

| 30 September 2021 | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| Property | 0.30% | 0.88% | 11.28% | 2.15% |

The fall in stage 1 coverage ratios is due to a change in the business mix of the lending portfolio with most new business originations being lower risk first charge serviced mortgages which attract a lower PD as well as revised modelling methodology which provides more detailed product segmentation. The large increase in stage 2 coverage ratios principally is due to the significant reduction in the overall balance which has almost halved year on year as multiple cases on short term extensions which carried lower PDs repaid. The residual balance in stage 2 contains cases which have yet to be resolved and carry a higher individual impairment charge. The increase in Stage 3 coverage ratios is due to the year end forecast in future house price movements which are now set to fall in 2023 and the continued run-off of the RDF book. This has reduced the potential recoverability of defaulted accounts.

### 23.1.2 Credit concentration

Credit concentration risk arises when a number of counterparties are engaged in similar business activities, or activities in the same geographical region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. The Company manages its exposure to credit concentration risk by monitoring the level of concentration on each of its portfolios through several dimensions and in some cases limiting the exposure.

The Company's exposure to credit risk arising from cash and cash equivalents and loans and advances to credit institutions is managed by the treasury function. The credit ratings for counterparties used by the Company are summarised below.

| | Fitch | | Moody's | | S&P | |
|---|---|---|---|---|---|---|
| | Rating | Outlook | Rating | Outlook | Rating | Outlook |
| HSBC Bank plc | AA- | Stable | A1 | Stable | A+ | Stable |
| National Westminster Bank plc | A+ | Stable | A1 | Stable | A | Stable |
| United Kingdom | AA- | Stable | Aa3 | Negative | AA | Negative |

These exposures are not considered to result in significant credit risk.

At 30 September 2022 the Company was exposed to credit risk in terms of its holdings in Treasury Gilts. The Company performed its own credit analysis and considered the counterparty to be creditworthy.

Credit risk associated with Serviced and Interest Roll Up mortgages, RDF loans and other loans designated at fair value through profit or loss is mitigated by the collateral that the Company holds a charge over. This totalled £1.12 billion (2021: £1.21 billion), which represents the expected collateral value in case of loans that are assessed individually and indexed collateral in case of loans that are assessed in collective ECL model. In some cases, the Company's charge over this collateral is subordinated by another lender's charge.

The following table shows the loan balance by combined first and second charge loan to value analysis for all loans by band held at the end of the period:

| LTV band % | 2022 £'000 | 2022 % | 2021 £'000 | 2021 % |
|---|---|---|---|---|
| 0 - 20 | 3,836 | 1% | 13,470 | 3% |
| 21 - 50* | 52,220 | 11% | 55,464 | 14% |
| 51 - 70 | 176,027 | 37% | 208,450 | 50% |
| 71 - 85 | 190,145 | 41% | 104,477 | 26% |
| 86 - 90 | 5,396 | 1% | 2,384 | 1% |
| 91+ | 40,153 | 9% | 23,425 | 6% |
| Carrying value before impairment provision | 467,777 | 100% | 407,670 | 100% |

* Band includes loan designated at fair value

The increase in the 71-85% LTV cohort is due to new business volumes for first charge serviced mortgages which typically will have an LTV on origination of between 70-75%.

The LTV used in the table above for RDF is based on the Gross Development Value (the estimated value at completion). Total exposure to Development finance is £35m (2021: £51m) with an average LTV of 87% (2021: 48%).

The breakdown of LTV by region is shown below:

| London<br>LTV band % | 2022 £'000 | 2022 % | 2021 £'000 | 2021 % |
|---|---|---|---|---|
| 0 - 20 | 2,411 | 1% | 2,744 | 1% |
| 21 - 50 | 29,301 | 15% | 25,435 | 13% |
| 51 - 70* | 86,426 | 46% | 108,499 | 54% |
| 71 - 85 | 59,197 | 31% | 50,288 | 25% |
| 86 - 90 | 1,892 | 1% | 1,893 | 1% |
| 91+ | 12,009 | 6% | 11,242 | 6% |
| Carrying value before impairment provision | 191,236 | 100% | 200,101 | 100% |

* Band includes loan designated at fair value

| South<br>LTV band % | 2022 £'000 | 2022 % | 2021 £'000 | 2021 % |
|---|---|---|---|---|
| 0 - 20 | 1,179 | 1% | 7,609 | 6% |
| 21 - 50 | 11,346 | 10% | 23,752 | 20% |
| 51 - 70 | 50,476 | 43% | 39,618 | 34% |
| 71 - 85 | 47,575 | 42% | 34,998 | 30% |
| 86 - 90 | 3,179 | 3% | 437 | 0% |
| 91+ | 684 | 1% | 11,288 | 10% |
| Carrying value before impairment provision | 114,439 | 100% | 117,702 | 100% |

| Rest of UK<br>LTV band % | 2022 £'000 | 2022 % | 2021 £'000 | 2021 % |
|---|---|---|---|---|
| 0 - 20 | 246 | 0% | 3,117 | 3% |
| 21 - 50 | 11,574 | 7% | 6,277 | 7% |
| 51 - 70 | 39,123 | 24% | 60,332 | 67% |
| 71 - 85 | 83,373 | 51% | 19,192 | 21% |
| 86 - 90 | 326 | 0% | 54 | 0% |
| 91+ | 27,460 | 17% | 894 | 1% |
| Carrying value before impairment provision | 162,102 | 100% | 89,866 | 100% |

Castle Trust Bank assesses the underlying credit risk of customers, determining high, standard, and sub-standard risk grades based on underlying loan characteristics. The table below shows this credit assessment and the related impairment staging for loans at amortised cost:

| Total | Stage 1 £'000 | Stage 2 £'000 | Stage 3 £'000 | Total £'000 |
|---|---|---|---|---|
| High grade | 31,099 | 19,389 | 1,473 | 51,961 |
| Standard grade | 302,833 | 41,859 | 17,314 | 362,006 |
| Sub-standard grade | 1,135 | 4,099 | 44,482 | 49,716 |
| **Total gross carrying amount at 30 September 2022** | 335,067 | 65,347 | 63,269 | 463,683 |

| Total | Stage 1 £'000 | Stage 2 £'000 | Stage 3 £'000 | Total £'000 |
|---|---|---|---|---|
| High grade | 24,517 | 29,825 | 14,475 | 68,817 |
| Standard grade | 188,770 | 85,016 | 23,277 | 297,063 |
| Sub-standard grade | 11,342 | 2,083 | 23,891 | 37,316 |
| Total gross carrying amount at 30 September 2021 | 224,629 | 116,924 | 61,643 | 403,196 |

The loan designated at fair value amounting to £4.1m (2021: £4.5m) was assessed as standard grade.

For property loans, Castle Trust has utilised the current Loan To Value (LTV) of exposures as the rating criteria for the property portfolio.

The following criteria was applied.
- High grade exposures have an LTV of less than 50%;
- Standard grade exposures have an LTV between 50% and 80%; and
- Substandard grade exposures have an LTV in excess of 80%.

The Company limits its maximum exposure to individual obligors and certain product types (1st line mortgages versus 2nd line mortgages for example). Regional concentration and other concentration risks are also monitored by the Group Credit Risk Committee.

Mortgage assets have a maximum loan exposure which limits concentration risk. The maximum single counterparty exposure is to the Bank of England.

### 23.1.3 Impact of Covid-19 pandemic on credit risk

Following the start of the Covid-19 outbreak in early 2020, the Company provided specific forbearance to support customers in line with regulatory guidelines. This was typically in the form of payment holidays for a period of 1-6 months. Consistent with the prior year, all such arrangements have now been concluded with customers then affected now being assessed for forbearance measures in accordance with normal procedures. As at September 2022, there were no customers assessed as forborne resulting from Covid-19 forbearance measures.

### 23.1.4 Impact of Cost of Living on credit risk

The UK is currently facing challenging circumstances with political turmoil and macroeconomic uncertainty (due to increased levels of inflation, rising energy costs and interest rates) resulting in instability and affordability issues for many households, including our customers. The Company is committed to supporting its customers and has put robust measures in place to offer to those who are affected by cost of living challenges. Additionally, these measures ensure the bank continues to comply with its regulatory requirements to provide assistance to vulnerable customers.

The Company remains cautious around the macroeconomic outlook of the UK and are managing the associated risks prudently, remaining alert for signs of distress amongst our customers. In property, the Company has reviewed its loan portfolio assessing its exposure against underlying collateral to identify customers who are higher risk from potential future impacts.

### 23.1.5 Staging overview

**Significant increase in credit risk ('SICR') (composition of stage 2)**

The Company's transfer criteria as described below, determine what constitutes a significant increase in credit risk, which results in an exposure being moved from stage 1 to stage 2.

| Analysis of Stage 2 loans | Backstop only | | Missed payment in the | | Watchlist | | Forborne / Extensions | | Other qualitative | | Multiple criteria | | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 31-60 DPDs | 61-90 DPDs | <30 DPDs | >30 DPDs | <30 DPDs | >30 DPDs | <30 DPDs | >30 DPDs | <30 DPDs | >30 DPDs | Qualitative Only | Qualitative & >30 DPDs | |
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| Property Loans | - | - | 2,193 | - | - | - | 29,878 | - | 5,370 | - | 16,268 | 11,638 | 65,347 |
| **Total** | - | - | 2,193 | - | - | - | 29,878 | - | 5,370 | - | 16,268 | 11,638 | 65,347 |

The Company regularly monitors the ongoing appropriateness of the transfer criteria, where any proposed amendments will be reviewed and approved by the Company's Management Committees and the Risk and Audit Committees at least semi-annually or more frequently if required.

IFRS 9 includes a rebuttable presumption that if an account is more than 30 days past due it has experienced a significant increase in credit risk. The Company considers more than 30 days past due to be an appropriate back stop measure and therefore has not rebutted this presumption.

For mortgages and RDF, other credit related criteria are considered in assessing whether a significant increase in credit risk has occurred. This includes changes to a customer's credit profile through reference to external credit agencies, changes to the current product terms offered to the customer, payment holidays, and extension of term. Customers who have no outstanding arrears but who have fallen more than 30 days in arrears within the last 12 months, continue to be classified as having a significantly increased credit risk and will remain within Stage 2.

A borrower will move back into Stage 1 where the SICR definition is no longer satisfied and when payments are up to date.

**Definition of default (movement to stage 3)**

The Company uses a number of quantitative and qualitative criteria to determine whether an account meets the definition of default and therefore moves to stage 3.

The rebuttable assumption is that more than 90 days past due (for property - on either primary or secondary mortgage) is an indicator of default. The Company has not rebutted this assumption and therefore deems that more than 90 days past due is an indicator of default. This acts as an appropriate back stop measure as it agrees with the observed performance and known behaviour of accounts reviewed.

For mortgages and residential development finance, additional criteria are considered in the assessment as to whether a loan meets the definition of default. This includes increased likeness of repossession, defaulted arrangements on other properties the customer may hold, significant fall in the valuation of a property, reduced or frozen interest charges and other criteria assessed by management which indicate an increased likelihood of default.

A borrower will move out of stage 3 when their credit risk improves such that any outstanding payments on the loan are less than 90 days in arrears. The borrower will move to stage 1 or stage 2 dependent on whether the SICR applies.

The following table shows the maturity profile of the Company's past due or impaired financial assets.

| As at 30 September 2022 | Total | ECL | <30 days | 30-60 days | 61-90 days | 91-120 days | >120 days |
|---|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Financial assets** | | | | | | | |
| Cash and cash equivalents | 143,706 | - | 143,706 | - | - | - | - |
| Debt instruments | 5,000 | - | 5,000 | - | - | - | - |
| Loans and advances to credit institutions | 1,970 | - | 1,970 | - | - | - | - |
| Trade and other receivables | 1,003 | | 1,003 | - | - | - | - |
| Loans to customers | | | | | | | |
| - At amortised cost | 453,815 | (9,868) | 404,420 | 4,474 | 625 | 61 | 53,985 |
| - Designated at fair value through profit or loss | 4,094 | - | - | - | - | - | 4,094 |
| Amounts due from group companies | 189,221 | - | 189,221 | - | - | - | - |
| Derivative assets | 3,123 | - | 3,123 | - | - | - | - |
| | 801,932 | (9,868) | 748,443 | 4,474 | 625 | 61 | 58,079 |

| As at 30 September 2021 | Total | ECL | <30 days | 30-60 days | 61-90 days | 91-120 days | >120 days |
|---|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Financial assets** | | | | | | | |
| Cash and cash equivalents | 54,544 | - | 54,544 | - | - | - | - |
| Debt instruments | 19,999 | - | 19,999 | - | - | - | - |
| Trade and other receivables | 817 | - | 817 | - | - | - | - |
| Loans to customers | | | | | | | |
| - At amortised cost | 394,523 | (8,673) | 340,246 | 5,833 | 2,802 | 9,128 | 45,187 |
| - Designated at fair value through profit or loss | 4,474 | - | - | - | - | - | 4,474 |
| Amounts due from group companies | 152,451 | - | 152,451 | - | - | - | - |
| | 626,808 | (8,673) | 568,057 | 5,833 | 2,802 | 9,128 | 49,661 |

### 23.1.6 Forbearance

The Company sometimes makes concessions to borrowers with respect to the original terms of mortgages as a response to a borrower's financial difficulties. All forborne loans will be classified as either stage 2 or stage 3.

Within property, forbearance may take the form of a change of contractual terms (e.g. transfer to interest only, extension of term, payment holiday or further advance) made as a concession to a borrower who is unable to meet the original contractual terms of the mortgage. In addition, other activities are also considered to be indicative of forbearance such as paying costs to support a voluntary sale of the property, waiving of Early Redemption Charges and providing a reduced concessionary interest rate that would not normally have been done had the borrower not been in financial difficulties. Forbearance offered by the primary mortgage provider does not necessarily result in Castle Trust's mortgage being forborne.

Forbearance provided by the Company is considered to be an indicator of impairment. Forbearance provided by other lenders to the Company's borrowers is not automatically considered to be an indicator of impairment of the Company's mortgage but is considered on a case by case basis if further information is available.

The forbearance classification on property loans is discontinued when all the following conditions are met:

- The contract is considered as performing, including if it has been reclassified from the non-performing category after an analysis of the financial condition of the debtor showed it no longer met the conditions to be considered as nonperforming.
- A minimum 2-year period has passed from the date the forborne exposure was considered as performing.
- None of the exposures to the debtor is more than 30 days past-due at the end of the probation period.

The following tables show the loans in forbearance at the year end.

| | Stage 1 | | Stage 2 | | Stage 3 | | ECL | Total | Forborne % |
|---|---|---|---|---|---|---|---|---|---|
| | Performing | Forborne | Not forborne | Forborne | Not forborne | Forborne | | | |
| As at 30 September 2022 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 | |
| **Financial assets** | | | | | | | | | |
| Loans to customers | | | | | | | | | |
| - At amortised cost | 335,067 | - | 45,089 | 20,258 | 50,993 | 12,276 | (9,868) | 453,815 | 7.02% |
| - Designated at fair value through profit or loss | - | - | - | - | 4,094 | - | - | 4,094 | |
| | 335,067 | - | 45,089 | 20,258 | 55,087 | 12,276 | (9,868) | 457,909 | |

| As at 30 September 2021 | Stage 1 Performing £'000 | Stage 1 Forborne £'000 | Stage 2 Not forborne £'000 | Stage 2 Forborne £'000 | Stage 3 Not forborne £'000 | Stage 3 Forborne £'000 | ECL £'000 | Total £'000 | Forborne % |
|---|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | | |
| Loans to customers | | | | | | | | | |
| - At amortised cost | 224,629 | - | 84,076 | 32,848 | 53,747 | 7,896 | (8,673) | 394,523 | 10.11% |
| - Designated at fair value through profit or loss | - | - | - | - | 4,474 | - | - | 4,474 | |
| | 224,629 | - | 84,076 | 32,848 | 58,221 | 7,896 | (8,673) | 398,997 | |

### 23.1.7 Modelling assumptions and approach

The modelling assumptions and approach are defined by the accounting policy as shown in note 2.4.3. The mortgage model was rebuilt during the financial year, undergoing both internal governance approval and an external 2nd line review prior to the model being signed off and used to calculate the impairment results for 30 September 2022. During the financial year, the macroeconomic parameters were updated within models on a quarterly basis with the results reflected in the quarterly financial results. All parameters were individually recalibrated as at 30 September 2022.

The results of the quarterly parametrisation, significant modelling changes and post model adjustments and overlays are scrutinised first by internal review and then through governance committees. The final outcome is then reviewed by the Audit Committee prior to any updates being adopted.

### 23.1.8 Forward looking macroeconomic scenarios

IFRS 9 requires firms to consider the risk of default and impairment loss taking into account expectations of economic changes that are reasonable.

The Company uses a bespoke macroeconomic model to determine the most significant factors which may influence the likelihood of an exposure defaulting in the future. At present, the most significant macroeconomic factors relate to the house price index ('HPI'), unemployment and the Bank of England Base Rate.

The Company has derived an approach for factoring probability weighted macroeconomic forecasts into ECL calculations, adjusting PD and LGD estimates. The macroeconomic scenarios feed directly into the ECL calculation, as the adjusted PD, lifetime PD and LGD estimates are used within the individual account ECL allowance calculations.

The Company currently does not have an in-house economics function and therefore sources economic forecasts from an appropriately qualified third party. The Company considers five probability weighted scenarios; base, upside, mild upside, downside and severe downside scenarios.

The models are then weighted to the base, upside and downside scenarios based on the severity of the modelled outcomes and underlying parameters. A benchmarking assessment is undertaken considering the economic parameters and related scenario weightings to provide additional support to the final weightings applied. However, the Company will constantly monitor the ongoing appropriateness of its approach referencing industry best practise.

The base case is also utilised within the Company's impairment forecasting process which in turn feeds the wider business planning processes. This economic forecast is also used within analysis to set the Company's credit risk appetite thresholds and limits.

The Company's approach to macroeconomic scenarios is to rely upon its third-party supplier which provides quarterly forecasts aligned to quarter ends; it should only deviate from this approach when there has been a severe macro-economic shock. Market interest rates are the primary short-term transmission mechanism for market shocks to impact upon Castle Trust Banks's key credit exposures. Since the September 2022 macroeconomic forecast was published, the UK Government's mini-budget and Bank of England communication relating to inflation produced a shock to market interest rates prior to the end of the financial year. A revised base case scenario was then published in October 2022 which in the view of management better represents the prevailing economic view at year end. Therefore, a post model adjustment has been applied to reflect the October 2022 base case within all ECL models. The remaining macroeconomic scenarios were maintained based on the expectations in late September 2022.

Castle Trust Bank

**Analysis of inputs to the ECL model under multiple economic scenarios**

An overview of the approach to estimating ECL's is set out in Note 2.4.3. To ensure completeness and accuracy, the Company obtains the data used from third party sources and the Credit Risk group verifies the accuracy of inputs to the Company's ECL models including determining the weights attributable to the multiple scenarios. The following tables set out the key drivers of expected credit loss and the assumptions, and the number of scenarios utilised, and the weightings applied to each scenario at 30 September 2022 and 30 September 2021

The tables show the value of the key forward looking economic variables at the end of the calendar year (31 December) as used in each of the economic scenarios for the ECL calculations. Subsequent years are calculated by taking the average of the calendar year end values for the outer years provided within the forecast data set. The base case reflects the post model adjustment for the October economic forecast as detailed in note 23.1.8.

As at 30 September 2022

| Key Drivers | ECL Scenario | Assigned Probabilities % | 2022 % | 2023 % | 2024 % | 2025 % | 2026 % | Subsequent years % |
|---|---|---|---|---|---|---|---|---|
| GDP growth % | | | | | | | | |
| | Upside | 10% | 2.8% | 3.9% | 4.4% | 3.4% | 1.7% | 1.3% |
| | Mild Upside | 10% | 1.9% | 2.6% | 4.0% | 3.1% | 1.8% | 1.3% |
| | Base Case (Oct) | 60% | 0.8% | -0.5% | 3.0% | 2.6% | 1.7% | 1.4% |
| | Downside | 10% | -1.7% | -2.1% | 2.7% | 2.3% | 2.0% | 1.5% |
| | Severe Downside | 10% | -2.9% | -3.5% | 2.4% | 2.0% | 2.0% | 1.6% |
| Unemployment rates % | | | | | | | | |
| | Upside | 10% | 3.6% | 3.3% | 2.5% | 2.1% | 2.2% | 2.5% |
| | Mild Upside | 10% | 3.9% | 4.3% | 3.9% | 3.6% | 3.6% | 3.7% |
| | Base Case (Oct) | 60% | 3.9% | 4.8% | 4.3% | 3.9% | 3.8% | 3.8% |
| | Downside | 10% | 4.5% | 6.4% | 7.0% | 6.9% | 6.7% | 6.0% |
| | Severe Downside | 10% | 4.6% | 6.7% | 7.4% | 7.2% | 7.0% | 6.3% |
| 10-Yr UK Government Bond Yield % | | | | | | | | |
| | Upside | 10% | 3.5% | 3.8% | 3.3% | 3.0% | 3.0% | 3.0% |
| | Mild Upside | 10% | 3.4% | 3.6% | 3.2% | 2.8% | 2.8% | 2.8% |
| | Base Case (Oct) | 60% | 4.2% | 4.2% | 3.7% | 2.8% | 2.3% | 2.3% |
| | Downside | 10% | 3.2% | 2.6% | 1.9% | 1.8% | 1.7% | 1.7% |
| | Severe Downside | 10% | 3.2% | 2.0% | 1.1% | 1.0% | 1.0% | 1.0% |
| House Price Index | | | | | | | | |
| | Upside | 10% | 9.2% | -0.7% | -0.2% | 8.1% | 7.6% | 3.5% |
| | Mild Upside | 10% | 8.2% | -2.5% | -1.5% | 7.0% | 7.7% | 3.6% |
| | Base Case (Oct) | 60% | 7.3% | -9.8% | -2.5% | 4.3% | 6.8% | 3.9% |
| | Downside | 10% | 4.5% | -10.6% | -8.4% | 1.2% | 8.3% | 4.1% |
| | Severe Downside | 10% | 3.4% | -13.5% | -11.3% | -1.5% | 8.5% | 4.4% |

As at 30 September 2021

| Key Drivers | ECL Scenario | Assigned Probabilities % | 2021 % | 2022 % | 2023 % | 2024 % | 2025 % | Subsequent years % |
|---|---|---|---|---|---|---|---|---|
| GDP growth % | | | | | | | | |
| | Upside | 10% | 10.3% | 6.4% | 2.4% | 1.8% | 1.4% | 1.2% |
| | Mild Upside | 10% | 9.2% | 5.5% | 2.2% | 1.7% | 1.5% | 1.3% |
| | Base Case | 60% | 7.9% | 3.7% | 1.8% | 1.5% | 1.5% | 1.3% |
| | Downside | 10% | 4.4% | 2.6% | 1.3% | 1.3% | 1.6% | 1.4% |
| | Severe Downside | 10% | 2.7% | 1.7% | 1.1% | 1.2% | 1.7% | 1.5% |
| Unemployment rates % | | | | | | | | |
| | Upside | 10% | 3.3% | 2.6% | 2.5% | 2.5% | 2.4% | 2.7% |
| | Mild Upside | 10% | 4.0% | 3.7% | 3.7% | 3.7% | 3.6% | 3.6% |
| | Base Case | 60% | 4.8% | 4.4% | 4.2% | 4.0% | 3.8% | 3.7% |
| | Downside | 10% | 5.9% | 6.2% | 6.4% | 6.4% | 6.1% | 5.5% |
| | Severe Downside | 10% | 6.3% | 6.6% | 6.7% | 6.7% | 6.4% | 5.7% |
| 10-Yr UK Government Bond Yield % | | | | | | | | |
| | Upside | 10% | 0.9% | 2.1% | 2.7% | 2.7% | 2.7% | 2.7% |
| | Mild Upside | 10% | 0.9% | 1.7% | 2.2% | 2.2% | 2.2% | 2.2% |
| | Base Case | 60% | 0.8% | 1.2% | 1.7% | 1.8% | 1.9% | 2.1% |
| | Downside | 10% | 0.7% | 0.6% | 0.7% | 0.9% | 1.1% | 1.5% |
| | Severe Downside | 10% | 0.6% | 0.2% | 0.2% | 0.3% | 0.5% | 0.8% |
| House Price Index | | | | | | | | |
| | Upside | 10% | 7.1% | 3.1% | 8.5% | 9.1% | 3.5% | 2.9% |
| | Mild Upside | 10% | 5.4% | 0.8% | 5.8% | 7.2% | 3.6% | 3.1% |
| | Base Case | 60% | 3.0% | -1.8% | 1.5% | 3.3% | 3.8% | 3.3% |
| | Downside | 10% | -0.4% | -10.0% | -6.3% | -2.0% | 4.4% | 3.9% |
| | Severe Downside | 10% | -2.3% | -14.1% | -11.2% | -6.1% | 4.9% | 4.3% |

### 23.1.9 Sensitivity Analysis

The calculation of ECLs is complex and involves use of estimates in reaching the calculated results. Sensitivity analysis has been performed on the material estimates of PD and LGD as detailed in note 2.3 to illustrate the impact on ECLs of any changes to the main components of the calculation.

Within the Property portfolio, the Stage 1 and Stage 2 LGD calculations use a current blended cure rate of defaulted loans of 60%. An increase/decrease of 10% would result in a decrease/increase in impairment by £0.4m. The LGD calculations also use a time to sell for defaulted loan estimate of 18 months. An increase/decrease by 6 months would result in an increase/decrease in impairment of £0.1m. Within the LGD calculations a valuation haircut is also applied. A 5% increase/decrease in the haircut would result in an increase/decrease in impairment of £0.2m.

On the Mortgage Stage 3 specific loan assessments (excluding RDF loans), the key estimates relating to LGD are the collateral value, the valuation haircut applied and time to sell assumptions. Decreasing and increasing the collateral value by 10% on these loans increases and decreases impairment by £2.4m and £1.2m respectively. A 5% increase and decrease in the valuation haircut would result in an increase and decrease in ECL of £1.2m and £0.7m respectively. The LGD calculations also use a time to sell estimate for defaulted loans. An increase/decrease by 6 months would result in an increase/decrease in impairment of £1.2m and £1.0m respectively.

For PD, the key estimate relates to the macroeconomic scenarios and the associated weightings. The following table shows the ECL impact of 100% weighting to base/upside/downside in comparison to the weighted ECL. Weighting the scenarios accordingly, the baseline and upside scenarios reduce the ECL whereas the downside scenarios result in an increase. The impacts have been performed on a consistent staging basis.

| | Property ECL Impact £'000 |
|---|---|
| 100% Base | 145 |
| 100% Downside | (1,715) |
| 100% Severe Downside | (2,824) |
| 100% Mild Upside | 822 |
| 100% Upside | 1,068 |

Further sensitivity analysis has been performed on the post-model adjustments and overlays (refer to note 23.1.10).

### 23.1.10 Post-model adjustments and overlays

The Company reviews the modelled impairment outcomes through a detailed governance process. In some instances, adjustments to the model are applied where it is felt the modelled outcome does not to represent the underlying credit risk appropriately. In the current economic environment, with continued political and economic uncertainty and cost of living pressures, this has resulted in an additional adjustment and overlay assumption being applied to account for significant increases in credit risk.

The key post-model adjustment and overlay applied by management is detailed below:

| | Modelled impact | Post model adjustments and overlays |
|---|---|---|
| **Significant Increase in Credit Risk** | Significant increases in credit risk are calculated based on additional criteria for Property loans. This increases ECL by £0.07m. | Whilst arrears performance remains the key indicator of credit risk, additional criteria are considered in the assessment of significant increases in credit risk for customers currently within Stage 1. |
| **Cost of Living** | Assessment of exposure to customers who may be impacted by the higher cost of living. This increases ECL by £0.02m. | An assessment based on the identification of customers at risk of potential affordability challenges resulting from the increases in the cost of living. and the likely impact on impairments. Further details can be found in Note 23.1.4. |
| **October base case** | October 2022 base case macroeconomic forecasts adopted. This increases ECL by £0.2m. | Published forecast did not capture the shock to the UK market resulting from the UK Government's mini-budget and BoE communication relating to inflation in late September 2022. Models updated to apply the October 2022 base case forecast. Further details can be found in Note 23.1.8 |
| **Property maturity cap** | Cure rates for loans with a maturity date of 12 months (or less) is capped at a lower cure rate than experienced cure rates. This increases ECL by £0.2m. | In response to the rapid interest rate hikes seen in updated forecasts, an additional PMA has been applied to mortgage accounts which mature in the next 12 months. The cure rate for these accounts has been reduced as we expect potential difficulties for customers upon refinancing. |

The net impact of the adjustment and overlay detailed above as at 30 September 2022 is an additional ECL of £0.5 million (2021: £0.3 million).

Sensitivity analysis has been performed on the key assumptions and judgements used to calculate the post-model adjustments and overlays.

The cost-of-living post-model adjustment on the property portfolio was estimated using the index of deprivation deciles, in conjunction with specific borrower and property credit risk measures. Adjusting the index of deprivation by +/- 1 decline results in a variance in ECL of +/-£0.01m.

The property maturity stressed cure rate is applied to accounts due to mature within the next 12 months. Increasing / decreasing the stressed cure rate by 10% results in a decrease / increase in ECL of £0.08m.

### 23.2 Liquidity risk

Liquidity risk is the risk that a firm is unable to meet its liabilities as they fall due, without incurring unacceptably large losses. In general, the risk arises from mismatches between the maturity profile of assets and liabilities and the ability of the firm to liquidate its holding in certain assets.

The Company is exposed to liquidity risk due to nature of its business activities. The exposure is monitored regularly and formally reviewed by the Board on an annual basis. The Company regularly conducts stress testing assessments of the balance sheet to measure its exposure. The exposure is controlled by active management of the amount, type and maturity profile of its assets and liabilities. In addition, the Company maintains a liquidity buffer to ensure it has adequate liquidity to meet its liabilities as they fall due.

The current political and macroeconomic uncertainty poses unique challenges for the banking sector and wider economy. The liquidity stress scenarios that are applied as part of the annual ILAAP assessment and ongoing liquidity monitoring capture downside scenarios in relation to potential macroeconomic outcomes. This includes a material reduction in the ability to source funding through deposits and reductions in loan repayments caused by affordability hardship to customers. The Company is able to maintain liquidity above Board prescribed limits through all periods assessed in these scenarios.

Please refer to note 24 for details of the maturity profile of assets and liabilities.

#### 23.3.1 Market risk

Market risk is the risk that the fair value of future cash flows from financial instruments will fluctuate as a result of changes in market variables. Interest rate risk is a type of market risk where variability arises from interest rates. Similarly, house price risk is a type of market risk where the variability arises from changes in house prices. The Company are not impacted by exchange rate fluctuations as all transactions are denominated in sterling.

The Company is exposed to market risk in the form of interest rate risk and house price risk. This exposure is monitored regularly and formally reviewed by the Board, as part of its ICAAP and ILAAP, on an annual basis. The Company's exposure to market movements are captured through macroeconomic forecasts and have been further assessed as part of the SICR process, specifically in the cost of living and affordability assessment performed. Refer to cost of living assessment explained in 23.1.4 and the overlay in 23.1.10.

Interest rate risk is the exposure which arises because of differences in the repricing profile of the Company's assets and liabilities. Primarily, Interest Rate Risk in the Banking Book (IRRBB) sensitives take the following forms:

- Valuation sensitivity measured by DV100, Economic value of Equity (EVE), or similar metrics
- Earnings exposure measured by Net Interest Income (NII) sensitivity metrics.

The organic business practices of the Company expose it to both valuation and earnings risk, which arise as repricing and basis risk mismatches develop.

The Company does not actively seek Interest Rate Risk; however, it acknowledges that this risk is inherent in its business model. The Company seeks to minimise exposure to this risk by designing complimentary asset and liability products which mitigate interest rate risk and through interest rate hedging.

Management of interest rate risk is a key part of the Company's business model. The Company's management of interest rate risk has the following key components:

- Active hedging of the balance sheet using interest rate swaps to reduce the exposure to interest rate risk;
- Management of the asset and liability pricing to control the differences in the duration profile of the assets and liabilities;
- Management of the LAB within the LAB Tenor Limit to reduce interest rate risk exposure; and
- Designing products which mitigate interest rate risk, for example by inclusion of early repayment charges in the products.

The Company manages its IRRBB to an agreed risk appetite, which is set out in the Company's ICAAP document. Balance Sheet Interest Rate Sensitivity Limit: The balance sheet's exposure to interest rate risk is managed so that the economic impact of a 100bp parallel shift in the yield curve must be less than the equivalent Pillar 2A capital allocation. This is reviewed at least annually as part of the ICAAP process and can only be changed with Board approval. The Company regularly monitors and reports its exposure to IRRBB, which consist of risk appetite metrics and a suite of Early Warning Indicators (EWIs) to senior management, including the ALCO, and the Board.

Following the sale of the house price derivatives relating to PM, BTL and IPS mortgages, the Comapny's direct exposure to house price risk is immaterial.

## 24 Maturity profile of all financial assets and liabilities

Debt instruments, trade and other receivables, cash and cash equivalents, trade and other payables are all carried at historic cost for maturity analysis purposes. As they are all short term items that will crystallise within one month or less, this is a close if not exact cash equivalent value.

Financial assets at fair value (mortgages) are discounted for up to 30 years, therefore the undiscounted cash values as at 30 September 2022 are significantly higher than the fair value. The timing of the cash flows also reflects Castle Trust's expectations in terms of early repayments based on expected customer behaviour, alongside contractual maturity dates. Amounts due to customers at amortised cost comprise principally of term deposits which are often reinvested upon maturity.

The analysis is based on the remaining period to the contractual maturity date based on undiscounted cash flows. The tables below indicate the maturity profile of the Company's financial assets and liabilities as at 30 September 2022:

| As at 30 September 2022 | Within 1 year | 1 - 3 years | 3 - 5 years | 5-10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Financial assets** | | | | | | |
| Cash and cash equivalents | 143,706 | | | | | 143,706 |
| Amounts due from credit institutions | 1,970 | | | | | 1,970 |
| Trade and other receivables | 1,003 | - | - | - | - | 1,003 |
| Debt instruments | 5,000 | - | - | - | - | 5,000 |
| Loans to customers | | | | | | |
| At amortised cost | 188,462 | 185,202 | 74,020 | 56,852 | 1,586 | 506,122 |
| Designated at fair value through profit or loss | 4,094 | - | - | - | - | 4,094 |
| Derivative assets | 3,123 | | - | | | 3,123 |
| Amounts due from group companies for MILA | 88,268 | 106,146 | 2,924 | 1,604 | - | 198,942 |
| | 435,626 | 291,348 | 76,944 | 58,456 | 1,586 | 863,960 |
| **Financial liabilities** | | | | | | |
| Lease liabilities | 538 | 755 | - | - | - | 1,293 |
| Trade payables | 7,567 | - | - | - | - | 7,567 |
| Amounts due to customers | 592,131 | 120,978 | 10,046 | - | - | 723,155 |
| Amounts due to customers through profit and loss - structured deposits | 591 | 880 | 50 | - | - | 1,521 |
| | 600,827 | 122,613 | 10,096 | - | - | 733,536 |
| Cumulative liquidity gap | (165,201) | 168,735 | 66,848 | 58,456 | 1,586 | 130,424 |
| Loan commitments | 44,737 | - | - | - | - | 44,737 |

| As at 30 September 2021 | Within 1 year | 1 - 3 years | 3 - 5 years | 5-10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 | £'000 |
| Financial assets | | | | | | |
| Loans and advances to central banks | 18,502 | - | - | - | - | 18,502 |
| Loans and advances to banks | 36,042 | | | | | 36,042 |
| Trade and other receivables | 817 | - | - | - | - | 817 |
| Debt instruments | 19,999 | - | - | - | - | 19,999 |
| At amortised cost | 273,368 | 76,641 | 49,605 | 36,992 | 8,217 | 444,823 |
| Designated at fair value through profit or loss | 8,126 | - | - | - | - | 8,126 |
| Amounts due from group companies for MILA | 84,625 | 66,165 | 5,018 | 3,110 | - | 158,918 |
| | 441,479 | 142,806 | 54,623 | 40,102 | 8,217 | 687,227 |
| Financial liabilities | | | | | | |
| Amounts due to group companies for BLA | - | - | - | - | - | - |
| Lease liabilities | 429 | 857 | 208 | - | - | 1,494 |
| Trade payables | 6,681 | - | - | - | - | 6,681 |
| Amounts due to customers | 338,254 | 166,026 | 53,716 | - | - | 557,996 |
| Amounts due to customers through profit and loss - structured deposits | - | 1,482 | 224 | - | - | 1,706 |
| | 345,364 | 168,365 | 54,148 | - | - | 567,877 |
| Cumulative liquidity gap | 96,115 | (25,559) | 474 | 40,102 | 8,217 | 119,350 |
| Loan commitments | 12,575 | - | - | - | - | 12,575 |

## 25 Share capital

The following table sets out the movement in share capital during the year.

| | 2022 Issued capital £'000 | 2021 Issued capital £'000 |
|---|---|---|
| **Issued and fully paid:** | | |
| At end of the year 152,174,659 (2021: 152,174,659) ordinary shares of £0.10 each | 15,217 | 15,217 |

| | 2022 Issued capital £'000 | 2022 Share premium £'000 | 2021 Issued capital £'000 | 2021 Share premium £'000 |
|---|---|---|---|---|
| **Issued and fully paid:** | | | | |
| At beginning of the period | 15,217 | 124,195 | 15,217 | 124,195 |
| **At 30 September** | 15,217 | 124,195 | 15,217 | 124,195 |

## 26 Reconciliation of financing liabilities

This section sets out an analysis of net debt and the movements in net debt for each of the years presented.

| | At 1 Oct 2021 £'000 | Cash flows £'000 | Interest accretion £'000 | Other non-cash movements £'000 | Fair value changes £'000 | At 30 September 2022 £'000 |
|---|---|---|---|---|---|---|
| Lease liabilities | 1,326 | (449) | 49 | 322 | | 1,248 |
| | 1,326 | (449) | 49 | 322 | | 1,248 |

| | At 1 Oct 2020 £'000 | Cash flows £'000 | Interest accretion £'000 | Other non-cash movements £'000 | Fair value changes £'000 | At 30 September 2021 £'000 |
|---|---|---|---|---|---|---|
| Lease liabilities | 898 | (346) | 52 | 722 | - | 1,326 |
| | 898 | (346) | 52 | 722 | - | 1,326 |

## 27 Commitments

In 2022, the Company had future aggregate minimum lease payments under non-cancellable operating leases that fell due as follows:

| | 2022 £'000 | 2021 £'000 |
|---|---|---|
| Within one year | 538 | 429 |
| Between one and five years | 755 | 1,065 |
| | 1,293 | 1,494 |

Non-cancellable mortgage loan commitments total £44,737,000 (2021 : £12,575,000).

## 28 Ultimate controlling party

Castle Trust's immediate parent undertaking is Castle Trust Holdings Limited which is incorporated in the United Kingdom and registered at 10 Norwich Street, London, EC4A 1BD. Castle Trust Holdings Limited is the smallest and largest group for which the results of the Company are consolidated. The registered address is disclosed on page 1. Castle Trust's ultimate parent company is CTC Holdings (Cayman) Limited which is incorporated in the Cayman Islands. The ultimate controlling party of the Company is Mr James Christopher Flowers.

## 29 Long Term Incentive Scheme

Castle Trust Bank operates a management incentive scheme. Members of management can be awarded B Ordinary shares of Castle Trust's holding company, Castle Trust Holdings (Caymans) Limited. The B shares vest at the grant date, which is the date that the award is communicated to the employee.

The following table summarises the number of shares, brought forward, granted in the period, forfeited and cancelled/redeemed and carried forward. B shares were redeemed at nil value.

**Year ended 30 September 2022**

| | Brought forward | Granted in the year | Forfeited, cancelled | Redeemed | Carried forward |
|---|---|---|---|---|---|
| Highest paid director | 25,600 | 0 | 0 | 0 | 25,600 |
| Directors | 15,000 | 0 | 0 | 0 | 15,000 |
| Other | 31,746 | 7,500 | 0 | 0 | 39,246 |
| **Total** | 72,346 | 7,500 | 0 | 0 | 79,846 |

Year ended 30 September 2021

| | | Granted in the year | Forfeited, cancelled | Redeemed | Carried forward |
|---|---|---|---|---|---|
| Highest paid director | 25,600 | 0 | 0 | 0 | 25,600 |
| Directors | 10,000 | 5,000 | 0 | 0 | 15,000 |
| Other | 34,545 | 2,750 | (5,549) | 0 | 31,746 |
| Total | 70,145 | 7,750 | (5,549) | 0 | 72,346 |

The fair value of all B shares granted in the period was £39,000 (2021: £16,000). £45,000 has been transferred to the tax authorities in respect of the issue of the shares. Based on the current valuation of Castle Trust Bank there would be no payment due in respect of the shares on an exit event. As such an independent valuation was commissioned which calculated the fair value based on a Black Scholes model using the current value of Castle Trust Bank and the volatility of comparative banks to calculate the option value of the shares.

There are 3 directors (2021: 3 directors) with interests in the scheme.

There was a charge to the profit and loss account of £39,000 (2021: £16,000) in relation to share based payments.

The weighted average share price of shares granted and forfeited was £2.10. 10 (2021: £2.10). The exercise price of shares is nil (2021: nil).

## 30 Related party transactions

### *Key management personnel*

Key management personnel are those individuals who have the authority and responsibility for planning and exercising power to directly or indirectly control the activities of the Company and its employees. The Company considers the members of the Board of Directors and the Executive Committee to be key management personnel for the purposes of IAS 24 Related Party Disclosures. Please refer to note 6 for details of transactions with them.

The following outstanding balances arose from the ordinary course of business. The interest rates charged to, and by, related parties are at normal commercial rates. Outstanding balances at the year-end are unsecured. There have been no guarantees provided or received for any related party receivables or payables. For the year ended 30 September 2022 the Company has not made any provision for doubtful debts relating to amounts owed by related parties (2021 Nil).

| | Nature | Amount of transactions | | Amount outstanding at year end | |
|---|---|---|---|---|---|
| | | 2022 £'000 | 2021 £'000 | 2022 £'000 | 2021 £'000 |
| Transactions with: | | | | | |
| Subsidiary | Interest and amounts due in relation to intercompany funding to Omni | | - | 426 | 377 |
| | Interest and amounts due under the MILA with Omni | 5,390 | 4,687 | 188,795 | 152,073 |

## 31 Capital management

The primary objectives of Castle Trust's capital management policy are to ensure that Castle Trust complies with externally imposed capital requirements and maintains an appropriate capital position, relative to its risk, in order to support its business.

Castle Trust Capital plc is subject to FCA and PRA regulation and are subject to the requirements of the Capital Requirements Regulation which governs capital levels. Regulatory capital requirements of 8% of risk weighted assets ("RWAs") are monitored as part of the overall management of capital, with Key Risk Indicators assigned and monitored for regulatory capital ratios. During the current and prior period Castle Trust complied with all external regulatory capital requirements.

Castle Trust manages its capital structure to reflect changes in the prevailing economic conditions and the risk characteristics of its activities. Castle Trust may adjust the quantum, tenor or riskiness of its activities and hedging strategies in order to reduce the risk that it runs, including exposures to house price, credit, interest rate, and operational risk. Castle Trust may also seek to issue additional capital instruments. Castle Trust's Board regularly reviews its capital position and has instituted objectives, policies and procedures for the sound management of its capital position.

Regulatory capital consists of CET 1 capital, which comprises share capital, share premium, retained earnings.

As at 30 September 2022, the Company's total equity was £94.0m (2021: £92.0m).

## 32 Contingent liabilities

The Company operates in a legal and regulated environment that exposes it to litigation and regulatory risks. As a result, Castle Trust Bank receives complaints, is subject to threatened or actual legal proceedings and manages regulatory enquiries and investigations, and is in continual dialogue with the Regulator, Financial Ombudsman and HMRC to ensure the compliance of our products. Where it is concluded that it is more likely than not that a payment will be made a provision is raised based on management's best estimate of the amount payable. All material matters, if any, are subject to periodic review to determine if they can be reasonably estimated. The Company does not expect the ultimate resolution of any matters to have a materially adverse impact on its financial statements.

## 33 Events after the reporting date

As at the date of signing the financial statements no impact has been identified which would be deemed an adjusting or non-adjusting event, however it has been considered by the Directors in their assessment of risk and the Company's ability to continue as going concern. There are no other adjusting or non-adjusting events after the reporting date.

## 34 Country-By-Country Reporting as at 30 September 2022

Castle Trust Capital plc is an authorised credit institution and specialty finance provider. The Bank is a wholly owned subsidiary of Castle Trust Holdings Limited and is headquartered in London, United Kingdom and provides services to its clients in the United Kingdom.

### Subsidiaries

As at 30 September 2022, Castle Trust Capital plc has the following subsidiaries incorporated, all located in the United Kingdom:

- Castle Trust POS Limited
- Omni Capital Retail Finance Limited

### Turnover

The net operating income of Castle Trust Capital plc for the year ended 30 September 2022 was £29.0m (2021: £23.5m).

### Average number of employees

The average number of employees was 214 for the year ended 30 September 2022 (2021: 202)

**Country-by-country breakdown 2022**

| Country | Type of operation | Turnover | Profit before tax | Corporation tax paid | Average number of employees | Public subsidies received |
|---|---|---|---|---|---|---|
| | | £'000 | £'000 | £'000 | £'000 | £'000 |
| United Kingdom | Property lending and retail savings | 29,031 | 4,460 | 26 | 214 | - |
| | | 29,031 | 4,460 | 26 | 214 | - |

Country-by-country breakdown 2021

| Country | Type of operation | Turnover | Loss before tax | Corporation tax paid | Average number of employees | Public subsidies received |
|---|---|---|---|---|---|---|
| | | £'000 | £'000 | £'000 | £'000 | £'000 |
| United Kingdom | Property lending and retail savings | 23,521 | 2,265 | - | 202 | - |
| | | 23,521 | 2,265 | - | 202 | - |