

PARAGON SEVENTH FUNDING LIMITED

Report and Financial Statements

Year ended 30 September 2018



STRATEGIC REPORT

BUSINESS REVIEW AND PRINCIPAL ACTIVITIES

Paragon Seventh Funding Limited ('the Company') is a special purpose company established to act as a funding vehicle within Paragon Banking Group PLC ('the Group'). During September 2015 the Company entered into a sterling credit facility of £200 million and used the facility to provide funding of mortgage loans acquired or underwritten by the Group. Subsequently, the mortgage loans will be sold to other group companies. During the year the Company operated in the United Kingdom.

On 9 October 2017 the Company sold its mortgages loans to a fellow group company and used the proceeds to repay its outstanding credit facility. The Company continues to manage its residual assets.

As shown in the Company's profit and loss account on page 8, the net interest income decreased from £2,695,000 to £208,000. This was due to a reduction of mortgage interest income as loans were sold at the beginning of the year. The result after tax has decreased from a retained profit of £210,000 to a result of £nil due to the decrease in net interest income.

The balance sheet on page 9 of the Financial Statements shows the Company's financial position at the year end. Net assets stayed consistent with the preceding year. Loans to customers have decreased to £nil due to the Company selling its mortgage loans with the sale proceeds used to repay the credit facility.

No interim dividend was paid during the year. No final dividend is proposed.

The Company has entered into derivative contracts in order to provide an economic hedge against its exposure to fixed rate loans to customers. Although these instruments provide an economic hedge the prescriptive nature of the requirements of International Accounting Standard 39 – 'Financial Instruments: Recognition and Measurement' (IAS 39), means that hedge accounting cannot always be achieved. This has led to the Company recognising a fair value net gain of £118,000 (2017: £1,099,000) in the year due to the ineffectiveness of the hedge relationship. This represents a timing difference and cumulative gains and losses recognised will tend to zero over time.

The Group manages its operations on a centralised basis. For this reason, the Company's directors believe that further key performance indicators for the Company are not necessary or appropriate for an understanding of the development, performance or position of the business.

PRINCIPAL RISKS AND UNCERTAINTIES

The Company is a securitisation company and has been structured so as to avoid, in as far as is possible, all forms of financial risk with its outstanding term loan match-funded to maturity. An analysis of the Company's exposure to risk, including financial risk, and the steps taken to mitigate these risks are set out in note 4, and a discussion of critical accounting estimates is set out in note 3.

After considering the above, the directors have a reasonable expectation that the Company will have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Financial Statements.

STRATEGIC REPORT (CONTINUED)

ENVIRONMENT

The Group recognises the importance of its environmental responsibilities, monitors its impact on the environment, and designs and implements policies to reduce any damage that might be caused by the Group's activities. The Company operates in accordance with group policies, which are described in the Group's Annual Report, which does not form part of this Report.

EMPLOYEES

The Company has no employees. All operational services are provided by employees of the Group. The Group's employment policies are described in its Annual Report, which does not form part of this Report.

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



per pro Intertrust Directors 1 Limited

Director

15 January 2019

DIRECTORS' REPORT

The directors present their Annual Report prepared in accordance with Schedule 7 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 and the audited Financial Statements of Paragon Seventh Funding Limited, a company registered in England and Wales with registration no: 09580619, for the year ended 30 September 2018.

GOING CONCERN

After making enquiries, the directors believe that the company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the financial statements.

CORPORATE GOVERNANCE

The directors have been charged with governance in accordance with the transactional documentation detailing the mechanism and structure of the transaction. The structure of the Group is such that the key policies have been predetermined at the time of issuance and the operational roles have been assigned to third parties with their roles strictly governed by the transaction documents.

DIRECTORS

The directors during the year and subsequently were:

Intertrust Directors 2 Limited

Intertrust Directors 1 Limited

J Fairrie (resigned 19 November 2018)

J P Giles

H Whitaker

DIRECTORS' INDEMNITIES

The Company has made qualifying third party indemnity provisions for the benefit of its directors which were made during the Year and remain in force at the date of this report.

The directors have taken all necessary steps to make themselves and the Company's auditor aware of any information needed in preparing the audit of the Annual Report and Financial Statements for the year, and, as far as each of the directors is aware, there is no relevant audit information of which the auditor is unaware.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 (2) of the Companies Act 2006.

INDEPENDENT AUDITOR

No notice from members under section 488 of the Companies Act 2006 having been received, the directors intend that the auditor, KPMG LLP, shall be deemed to be reappointed in accordance with section 487(2) of the Act.

DIRECTORS' REPORT CONTINUED

INFORMATION PRESENTED IN OTHER SECTIONS

Certain information required to be included in a directors' report by the Companies Act 2006 and regulations made there under can be found in the other sections of the Annual Report, as described below. All of the information presented in these sections is incorporated by reference into this Directors' Report and is deemed to form part of this report.

- Commentary on the likely future developments in the business of the Company is included in the Strategic Report.
- A description of the Company's financial risk management objectives and policies, and its exposure to risks arising from its use of financial instruments are set out in note 4 to the accounts.
- Disclosure on any dividends paid during the year is included in the Strategic Report.

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



per pro Intertrust Directors 1 Limited

Director

15 January 2019

Registered Office: 51 Homer Road, Solihull, West Midlands, B91 3QJ

STATEMENT OF DIRECTORS' RESPONSIBILITIES
in relation to Financial Statements

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to 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:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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 their profit or loss for that period.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets, for the Company's systems of internal control and for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a strategic report and directors' report which comply with the applicable requirements of the Companies Act 2006.

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



Pandora Sharp
Company Secretary
15 January 2019

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PARAGON SEVENTH FUNDING LIMITED

Opinion

We have audited the Financial Statements of Paragon Seventh Funding Limited year ended 30 September 2018 which comprise the profit and loss account, the balance sheet, the statement of movement in equity and the related notes 1 to 20, including the accounting policies in note 2.

In our opinion the Financial Statements:

- give a true and fair view of the state of the company's affairs as at 30 September 2018 and of its result for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including Financial Reporting Standard 101 – 'Reduced Disclosure Framework'; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We have fulfilled our ethical responsibilities under, and are independent of the company in accordance with, UK ethical requirements including the FRC Ethical Standard. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion.

Going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

Strategic report and directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

Matters on which we are required to report by exception

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

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

We have nothing to report in these respects.

Directors' responsibilities

As explained more fully in their statement set out on page 5, the directors are responsible for: the preparation of the financial statements and for being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the company'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 they either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PARAGON SEVENTH FUNDING LIMITED (CONTINUED)

Auditor's responsibilities

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 our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not 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 aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

The purpose of our audit work and to whom we owe our responsibilities

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.



Matthew Rowell (Senior Statutory Auditor)

for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants

One Snowhill, Snow Hill Queensway, Birmingham, B4 6GH

15 January 2019

PARAGON SEVENTH FUNDING LIMITED

PROFIT AND LOSS ACCOUNT

YEAR ENDED 30 SEPTEMBER 2018

	Note	2018 £000	2017 £000
Interest receivable			
Mortgages		152	7,119
Other	5	130	132
		<u>282</u>	<u>7,251</u>
Interest payable and similar charges	6	(74)	(4,556)
Net interest income		<u>208</u>	<u>2,695</u>
Other operating income		4	52
		<u>212</u>	<u>2,747</u>
Operating expenses		(330)	(3,635)
Fair value gain	8	118	1,099
Operating loss, being loss on ordinary activities before taxation	9	-	211
Tax on loss on ordinary activities	10	-	(1)
Loss on ordinary activities after taxation	16	<u>-</u>	<u>210</u>

All activities derive from continuing operations.

There are no recognised gains or losses other than the result for the current year and the profit for the preceding year, and consequently a separate statement of comprehensive income has not been presented.

PARAGON SEVENTH FUNDING LIMITED

BALANCE SHEET

30 SEPTEMBER 2018

	Note	2018 £000	2018 £000	2017 £000	2017 £000
ASSETS EMPLOYED					
FIXED ASSETS					
Financial assets	11		-		165,507
CURRENT ASSETS					
Debtors falling due with one year	14	3		1,381	
Cash at bank		9		5,826	
			12		7,207
			12		172,714
FINANCED BY					
EQUITY SHAREHOLDERS' FUNDS / (DEFICIT)					
Called up share capital	15	-		-	
Profit and loss account	16	3		3	
			3		3
CREDITORS					
Amounts falling due within one year	17	9		249	
Amounts falling due after more than one year	17	-		172,462	
			9		172,711
			12		172,714

These financial statements of the Company (registered number 09580619) were approved by the Board of Directors 15 January 2019.

Signed on behalf of the Board of Directors


per pro Intertrust Directors 1 Limited
Director

PARAGON SEVENTH FUNDING LIMITED

STATEMENT OF MOVEMENT IN EQUITY

YEAR ENDED 30 SEPTEMBER 2018

	Share capital £000	Profit and loss account £000	Total equity £000
<i>Total comprehensive income for the year</i>			
Result for the year	-	-	-
Other comprehensive income	-	-	-
Total comprehensive income for the year	-	-	-
Opening equity	-	3	3
Closing equity	-	3	3

PERIOD ENDED 30 SEPTEMBER 2017

	Share capital £000	Profit and loss account £000	Total equity £000
<i>Total comprehensive income for the year</i>			
Profit for the year	-	210	210
Other comprehensive income	-	-	-
Total comprehensive income for the year	-	210	210
Opening equity	-	(207)	(207)
Closing equity	-	3	3

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

1. GENERAL INFORMATION

Paragon Seventh Funding Limited ('the Company') is a company domiciled in the United Kingdom and incorporated in England and Wales under the Companies Act 2006 with company number 09580619. The address of the registered office is 51 Homer Road, Solihull, West Midlands, B91 3QJ. The nature of the Company's operations and its principal activities are set out in the Strategic Report.

These financial statements are presented in pounds sterling, which is the currency of the economic environment in which the Company operates

2. ACCOUNTING POLICIES

The Financial Statements have been prepared in accordance with applicable UK accounting standards. Disclosures have been made in accordance with Financial Reporting Standard 101 – 'Reduced Disclosure Framework' ('FRS 101').

As permitted by FRS 100 – 'Application of Financial Reporting Requirements' ('FRS 100') the Company has applied the measurement and recognition requirements of International Financial Reporting Standards ('IFRS') as adopted by the EU, but makes amendments where necessary in order to comply with the Companies Act 2006 and has set out below where advantage of disclosure exemptions provided by FRS 101 has been taken.

Accounting convention

The Financial Statements are prepared under the historical cost convention, except as required in the valuation of certain financial instruments which are carried at fair value.

Going concern

The Financial Statements have been prepared on a going concern basis. the directors have a reasonable expectation that the Company will have adequate resources to continue in operational existence for the foreseeable future. This is further supported by the Group holding sufficient cash resources to support the Company's obligations as they fall due. For this reason, they continue to adopt the going concern basis in preparing the Financial Statements.

Loans to customers

Loans to customers are considered to be 'loans and receivables' as defined by IAS 39. They are therefore accounted for on the amortised cost basis.

Such loans are valued at inception as the amount of initial advance, which is the fair value at that time, inclusive of procurement fees paid to brokers or other business providers and less initial fees paid by the customer. Thereafter they are valued at this amount less the cumulative amortisation calculated using the Effective Interest Rate ('EIR') method. The loan balances are then reduced where necessary by a provision for balances which are considered to be impaired.

The EIR method spreads the expected net income arising from a loan over its expected life. The EIR is that rate of interest which, at inception, exactly discounts the expected future cash payments and receipts arising from the loan to the initial carrying amount.

The Company's policy is to hedge against any exposure to fixed rate loan assets (note 4).

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

2. ACCOUNTING POLICIES (CONTINUED)

Impairment of loans and receivables

Loans and receivables are reviewed for indications of possible impairment throughout the year and at each balance sheet date in accordance with IAS 39. Where loans exhibit objective evidence of impairment (a 'loss event') the carrying value of the loans is reduced to the net present value of their expected future cash flows, including the value of the potential realisation of any security (net of sales costs) discounted at the original EIR.

Within its buy-to-let portfolio the Group utilises a receiver of rent process, whereby the receiver stands between the landlord and tenant and will determine an appropriate strategy for dealing with any delinquency. This strategy may involve the immediate sale of any underlying security or the short or long term letting of the property to cover arrears and principal shortfalls. Properties in receivership are either returned to their landlord owners or sold.

Loss events reflect both loans that display delinquency in contractual payments of principal or interest or, for buy-to-let loans in receivership but up to date at the balance sheet date, properties where the receiver adopts a sale strategy, where a shortfall may or may not arise.

In addition to loans where loss events are evident, loans are also assessed collectively, grouped by risk characteristics and account is taken of any impairment arising due to events which are believed to have taken place but have not been specifically identified at the balance sheet date. Collective impairment provisions are calculated for each key portfolio based on recent historical performance, with adjustments for expected changes in losses based on management's judgement.

For financial accounting purposes provisions for impairments of loans to customers when first recognised in the income statement are held in an allowance account. These balances are released to offset against the gross value of the loan when it is written off to profit and loss on the administration system. After this point a salvage balance may be held in respect of any further recoveries expected on the loan.

Cash at bank

Balances shown as cash at bank in the balance sheet comprise demand deposits and short-term deposits with banks with initial maturities of not more than 90 days.

Current tax

Current tax, including UK corporation tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Borrowings

Borrowings are carried in the balance sheet on the amortised cost basis. The initial value recognised includes the principal amount received less any discount on issue or costs of issuance.

Interest and all other costs of the funding are expensed to the profit and loss account as interest payable over the term of the borrowing on an Effective Interest Rate basis.

Derivative financial instruments

Derivative instruments utilised by the Company comprise interest rate swaps. All such instruments are used for hedging purposes to alter the risk profile of the existing underlying exposure of the Company in line with the Company's risk management policies (note 4).

The Company does not enter into speculative derivative contracts.

All derivatives are carried in the balance sheet at fair value, as assets where the value is positive or as liabilities where the value is negative. Fair value is based on market prices, where a market exists. If there is no active market, fair value is calculated using present value models which incorporate assumptions based on market conditions and are consistent with accepted economic methodologies for pricing financial instruments. Changes in the fair value of derivatives are recognised in the profit and loss account, except where such amounts are permitted to be taken to equity as part of the accounting for a cash flow hedge.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

2. ACCOUNTING POLICIES (CONTINUED)

Hedging

For all hedges, the Company documents, at inception, the relationship between the hedging instruments and the hedged items, as well as its risk management strategy and objectives for undertaking the transaction. The Company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the hedging arrangements put in place are considered to be 'highly effective' as defined by IAS 39.

For a fair value hedge, as long as the hedging relationship is deemed 'highly effective' and meets the hedging requirements of IAS 39, any gain or loss on the hedging instrument recognised in income can be offset against the fair value loss or gain arising from the hedged item for the hedged risk. For macro hedges (hedges of interest rate risk for a portfolio of loan assets) this fair value adjustment is disclosed in the balance sheet alongside the hedged item, for other hedges the adjustment is made to the carrying value of the hedged asset or liability. Only the net ineffectiveness of the hedge is charged or credited to income. Where a fair value hedge relationship is terminated, or deemed ineffective, the fair value adjustment is amortised over the remaining term of the underlying item.

Where a derivative is used to hedge the variability of cash flows of an asset or liability, it may be designated as a cash flow hedge so long as this relationship meets the hedging requirements of IAS 39. For such an instrument the effective portion of the change in the fair value of the derivative is taken initially to equity, with the ineffective part taken to profit or loss. The amount taken to equity is released to the profit and loss account at the same time as the hedged item affects the profit and loss account. Where a cash flow hedge relationship is terminated, or deemed ineffective, the amount taken to equity will remain there until the hedged transaction is recognised, or is no longer highly probable.

Fee and commission income

Other income includes administration fees charged to borrowers, which are credited to the profit and loss account when the related service is performed.

Revenue

The revenue of the Company comprises interest receivable and other income. The accounting policy for the recognition of each element of revenue is described separately within these accounting policies.

Disclosures

In preparing these financial statements the Company has taken advantage of the exemptions from disclosure provided by FRS 101 in respect of:

- The requirement to produce a cash flow statement and related notes
- Disclosures in respect of transactions with wholly owned subsidiaries
- Disclosures in respect of capital management
- The effects of new, but not yet effective IFRSs
- Disclosures in respect of key management personnel
- Disclosures of transactions with a management entity which provides key management personnel services to the Company

As the consolidated financial statements of Paragon Banking Group PLC, the ultimate parent undertaking of the Company, include equivalent disclosures the Company has also taken advantage of these further exemptions provided by FRS 101:

- Certain disclosures required by IFRS 13 – 'Fair Value Measurement'
- Certain disclosures required by IFRS 7 – 'Financial Instruments Disclosures'

The Company presently intends to continue to apply these exemptions in future periods.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

3. CRITICAL ACCOUNTING ESTIMATES

Certain balances reported in the Financial Statements are based wholly or in part on estimates or assumptions made by the directors. There is, therefore, a potential risk that they may be subject to change in future periods. The most significant of these are:

Impairment losses on loans to customers

Impairment losses on loans are calculated based on statistical models. The key assumptions revolve around estimates of future cash flows from customer's accounts, their timing and, for secured accounts, the expected proceeds from the realisation of the property. These key assumptions are based on observed data from historical patterns and are updated regularly based on new data as it becomes available.

In addition the directors consider how appropriate past trends and patterns might be in the current economic situation and make any adjustments they believe are necessary to reflect the current conditions.

The accuracy of the impairment calculations would therefore be affected by unexpected changes to the economic situation, variances between the models used and the actual results or assumptions which differ from the actual outcomes.

In particular, if the impact of economic factors such as employment levels on customers is worse than is implicit in the model then the number of accounts requiring provision might be greater than suggested by the model, while falls in house prices, over and above any assumed by the model might increase the provision required in respect of accounts currently provided.

Effective interest rates

In order to determine the EIR applicable to loans and borrowings an estimate must be made of the expected life of each loan and hence the cash flows relating thereto. For purchased accounts this will involve estimating the likely future performance of the accounts at the time of acquisition. These estimates are based on historical data and reviewed regularly. For purchased accounts historical data obtained from the vendor will be examined. The accuracy of the EIR applied would therefore be compromised by any differences between actual repayment profiles and that predicted, which in turn would depend directly or indirectly on customer behaviour.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

4. FINANCIAL RISK MANAGEMENT

The Company's operations were financed principally by a sterling credit facility and, to a lesser extent, by a mixture of share capital and loans from other related entities. The Company drew down the facility to acquire loans. In addition, various financial instruments, for example debtors and accruals, arise directly from the Company's operations.

The principal risks arising from the Company's financial instruments were credit risk, liquidity risk and interest rate risk. The board of the Company's controlling company reviews and agrees policies for all companies in the Group managing each of these risks and they are summarised below.

Credit risk

The Company's credit risk was primarily attributable to its loans to customers. The maximum credit risk at 30 September 2017 approximates to the carrying value of loans to customers (note 12). There were no significant concentrations of credit risk due to the large number of customers included in the portfolios.

Mortgages acquired by the Company are secured by first charges over residential properties in the United Kingdom. Despite this security, in assessing credit risk an applicant's ability to repay the loan remains the overriding factor in the decision to lend by the originator. Additionally, each mortgage had the benefit of one or more life assurance policies and certain mortgages have the benefit of a mortgage guarantee indemnity insurance policy.

Paragon Mortgages (2010) Limited, a fellow related entity, continued to administer any loans owned by Paragon Seventh Funding Limited on its behalf and the collections process is the same as that utilised for all companies in the Group.

In order to control credit risk relating to counterparties to the Company's financial instruments, the board of the Company's controlling company determines on a group basis, which counterparties the group of companies will deal with, establishes limits for each counterparty and monitors compliance with those limits.

Liquidity risk

The Company's assets were principally financed by drawing down on the credit facility. Details of the Company's borrowings are given in note 17.

The securitisation process and the terms of the credit facility effectively limit liquidity risk from the funding of the Group's loan assets. It remains to ensure that sufficient funding was available to fund the Group's participation in the SPVs, provide capital support for new loans and working capital for the Group. This responsibility rests with the Asset and Liability Committee which sets the Group's liquidity policy and uses detailed cash flow projections to ensure that an adequate level of liquidity is available at all times.

Interest rate risk

The Company's policy was to maintain floating rate liabilities and match these with floating rate assets by the use of interest rate swaps.

The rates payable on the sterling credit facility were reset on the basis of LIBOR. The Company's assets predominantly bear LIBOR linked interest rates or are hedged fixed rate assets. The interest rates charged on the Company's variable rate loan assets were determined by reference to, inter alia, the Company's funding costs and the rates being charged on similar products in the market. Generally this ensured the matching of changes in interest rates on the Company's loan assets and borrowings and any exposure arising on the interest rate resets is relatively short term.

Currency risk

The Company has no material exposure to foreign currency risk.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

4. FINANCIAL RISK MANAGEMENT (CONTINUED)

Use of derivative financial instruments

The Company used derivative financial instruments for risk management purposes. Such instruments were used only to limit the exposure of the Company to movements in market interest or exchange rates, as described above.

It is, and has been throughout the period under review, the Company's policy that no trading in financial instruments shall be undertaken, and hence all of the Company's derivative financial instruments are for commercial hedging purposes. These are used to protect the Company from exposures principally arising from fixed rate lending or borrowing. Hedge accounting is applied where appropriate, though it should be noted that some derivatives, while forming part of an economic hedge relationship, do not qualify for this accounting treatment under IAS 39 either because natural accounting offsets are expected, or obtaining hedge accounting would be especially onerous.

The Company had designated a number of derivatives as fair value hedges. In particular this treatment is used for hedging the interest rate risk of groups of fixed rate prepayable loan assets with interest rate derivatives on a portfolio basis. The Company believes this solution is the most appropriate as it is consistent with the economic hedging approach taken by the Company to these assets.

5. INTEREST RECEIVABLE - OTHER

	2018 £000	2017 £000
Other interest	130	132

6. INTEREST PAYABLE AND SIMILAR CHARGES

	2018 £000	2017 £000
Mortgage backed bank loans	50	2,222
Interest rate swaps	18	701
Subordinated loan interest	-	1,306
Commitment fee	6	326
Interest payable to related parties	-	1
	74	4,556

7. DIRECTORS AND EMPLOYEES

Directors' remuneration from the Company during the current year preceding period is listed in note 9.

The Company had no employees in the current year. All administration is performed by employees of related companies under the servicing agreement described in note 18. One director of the Company is employed by Paragon Finance PLC, a related party, and their remuneration is disclosed within the financial statements of that company, which do not form part of this Report.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

8. FAIR VALUE NET GAIN

The fair value net gain of £118,000 (2017: £1,099,000) represents the accounting volatility on derivative instruments which are matching risk exposure on an economic basis. Some accounting volatility arises on these items due to accounting ineffectiveness on designated hedges, or because hedge accounting has not been adopted or is not achievable on certain items. The gain is primarily due to timing differences in income recognition between the derivative instruments and the economically hedged assets and liabilities.

9. OPERATING PROFIT, BEING PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

	2018 £000	2017 £000
Operating profit is after charging:		
Directors' fees - Intertrust	9	9
Auditor remuneration - audit services	8	8
Deferred purchase consideration	294	3,136

Non audit fees provided to the Group are disclosed in the accounts of Paragon Banking Group Plc and the exemption from disclosure of fees payable to the Company's auditor in respect to non-audit services in these Financial Statements has been taken.

10. TAX ON PROFIT ON ORDINARY ACTIVITIES

a) Tax charge for the year

	2018 £000	2017 £000
Current tax		
Corporation tax	-	1

b) Factors affecting the tax charge for the year

	2018 £000	2017 £000
Profit before tax	-	211
UK corporation tax at 19% (2017: 19.5%) based on the profit for the year	-	41
Effects of:		
Current year profit for which no deferred tax asset was recognised	-	(40)
Tax charge for the year	-	1

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

10. TAX ON PROFIT ON ORDINARY ACTIVITIES (CONTINUED)

The current rate of corporation tax applicable to the Company for the year ended 30 September 2018 is 19.0%. Legislation has been enacted that will reduce this to 17% with effect from 1 April 2020.

Therefore, the standard rate of corporation tax is expected to be 19% for the year ended 30 September 2019, 18% for the year ending 30 September 2020 and 17% thereafter.

11. FINANCIAL ASSETS

	2018 £000	2017 £000
Loans to customers (note 12)	-	165,400
Derivative financial assets (note 13)	-	107
	<u>-</u>	<u>165,507</u>

12. LOANS TO CUSTOMERS

Loans to customers at 30 September 2018 and 30 September 2017, which are all denominated and payable in sterling, are first mortgages which are secured on residential property within the United Kingdom and are categorised as loans and receivables as defined by IAS 39.

Mortgage loans have a contractual term of up to thirty years, the borrower is entitled to settle the loan at any point and in most cases such early settlement does take place. All borrowers are required to make monthly payments, except where an initial deferred period is included in the contractual terms.

All the mortgage loans are pledged as collateral for liabilities at 30 September 2017.

	2018 £000	2017 £000
Balance at 30 September 2017	165,400	147,776
Additions	-	23,530
Securitisation and other sales	(165,315)	-
Other debits	4	7,177
Repayments and redemptions	(89)	(13,083)
Balance at 30 September 2018	<u>-</u>	<u>165,400</u>

Other debits include primarily interest charged to customers on loans outstanding and other changes in the amortised cost of the assets caused by the effective interest rate method.

On 9 October 2017, the Company sold its mortgages loans to a fellow group company and used the proceeds to repay its outstanding credit facility.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

13. DERIVATIVE FINANCIAL ASSETS AND LIABILITIES

All of the Company's financial derivatives are held for economic hedging purposes, although not all may be designated for hedge accounting in accordance with the provisions of IAS 39. The analysis below therefore splits derivatives between those accounted for as hedges and those which, while representing an economic hedge do not qualify for this treatment.

	2018	2018	2018	2017	2017	2017
	Notional amount £000	Assets £000	Liabilities £000	Notional amount £000	Assets £000	Liabilities £000
Other derivatives						
Interest rate swaps	-	-	-	149,000	107	(406)
Total recognised derivative assets / (liabilities)	-	-	-	149,000	107	(406)

14. DEBTORS

	2018 £000	2017 £000
Amounts falling due within one year:		
Other debtors	3	1,370
Prepayments and accrued income	-	11
	<u>3</u>	<u>1,381</u>

15. CALLED UP SHARE CAPITAL

	2018 £	2017 £
Allotted:		
1 ordinary share of £1 (fully paid)	<u>1</u>	<u>1</u>

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

16. PROFIT AND LOSS ACCOUNT

	£000
At 1 October 2016	(207)
Profit for the financial year	210
At 30 September 2017	3
Result for the financial year	-
At 30 September 2018	3

17. CREDITORS

	2018 £000	2017 £000
Amounts falling due within year:		
Corporation tax	-	1
Accruals and deferred income	9	248
	<u>9</u>	<u>249</u>

	2018 £000	2017 £000
Amounts falling due after more than one year:		
Bank loan	-	143,000
Derivative financial liabilities (note 13)	-	406
Subordinated loan	-	29,056
	<u>-</u>	<u>172,462</u>

As at 30 September 2017, the Company held a sterling credit facility of £200,000,000. This facility was available for drawing and redrawing until 8 October 2018 for the purpose of funding new first charge mortgage loans. After that the loan has a further one-year workout period for the assets funded to be sold or refinanced. Repayment of the principal drawn is not required unless amounts are realised from the sale or repayment of assets, even after the one-year workout period. The balance outstanding under this credit facility agreement was £nil (2017: £143,000,000). The facility was repaid during the current year.

Interest is payable at a fixed margin, 1.75% above the London Interbank Offered Rate ('LIBOR') on the loan denominated in sterling.

There is a subordinated loan facility repayable to Paragon Mortgages (2010) Limited, a related company, on the first day on which all of the loan has been repaid. Interest is charged at a rate of 4% above LIBOR.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2018

18. RELATED PARTY TRANSACTIONS

The Group has identified the following transactions which are required to be disclosed under the terms of International Accounting Standard 24, 'Related Party Disclosures' ('IAS 24').

Transactions with Paragon Mortgages (2010) Limited ('PM2010')

The subordinated loan made to the Company by PM2010, a company under common control as defined by IAS24, is described in note 17 and interest charged on it is shown in note 6. At the balance sheet date the Company owed £nil in relation to subordinated loan interest and £nil in relation to interest earned on this balance.

The Company was owed £3,000 (2017: £1,265,000) from PM2010 at the balance sheet date, relating to monies paid to PM2010.

The Company was owed £nil (2017: £105,000) from PM2010 relating to monies received by the servicer, that are yet to be passed onto the Company, which is included in other debtors.

Transactions with Paragon Finance PLC ('PF')

At the balance sheet date PF, a company under common control as defined by IAS 24, acted as servicer of the mortgages for the Company and earned £nil (2017: £467,000) during the year in servicing fees. At the balance sheet date the Company owed £nil (2017: £nil) to PF in relation to servicing fees.

19. ULTIMATE PARENT COMPANY

The ultimate parent undertaking is Intertrust Corporate Services Limited who holds the entire share capital of the Company on a discretionary trust basis for the benefit of certain charities. The directors regard Paragon Banking Group PLC as the ultimate controlling party.

The smallest and largest group in which the Company is consolidated is that of the Paragon Banking Group PLC.

Copies of the Group's financial statements are available from that company's registered office at 51 Homer Road, Solihull, West Midlands, B91 3QJ.