Scottish Building Society
Report & Accounts

For the year ended 31 January 2015

SCOTTISH BUILDING SOCIETY

REPORT AND ACCOUNTS

for the year ended 31 January 2015

Overview

The year to end January 2015 has been a successful one for Scottish Building Society, with the financial position of the Society being further improved. The balance sheet strength and therefore the financial stability of the Society is always of utmost importance to the Board and I am pleased to report that this has been enhanced whilst also focussing on the continuous improvement of our products and service to customers. The mutual nature of the Society is key and we strive to find ways to deliver fair, simple and transparent products to our members. To this end we are in the process of developing loyalty offerings for our savings and mortgage members. This will be a key initiative for us in the coming year.

Financial Results

In last year's Chairman's Statement, I referred to the fact that we were seeing some improvement in economic conditions, following a long period of very difficult times beginning with the financial crisis seven years ago in 2007.

Whilst the UK as a whole has seen growth in the housing market, this varies greatly by region. We in Scotland have seen a number of encouraging signs for the housing market, with overall activity increasing since 2013.

Unemployment statistics have improved, inflation has fallen and the Bank of England Base Rate has remained at its record low of 0.5% for six years.

During the year the people of Scotland voted on the long awaited Independence Referendum. The Society always maintained a neutral stance on the issue and expected to be able to continue to flourish as an independent mutual in Scotland no matter what the outcome. Having the Referendum behind us enables everyone to focus on more immediate issues to hand and that brings a certain sense of stability which is beneficial.

The Society's underlying profit for the year, at £2.1million, compares very favourably with the previous year and contributes to the further improvement in the financial strength of the Society, through a substantial increase in the capital retained. Capital held by the Society remains high compared both with our peer group and the minimum capital requirements of the regulators. Liquidity also remains high, and in excess of levels required by the regulator, giving us a good base for lending to existing and new members in the new financial year.

Products

The low Bank of England Base Rate continues to hit savers whilst having obvious benefits for mortgage holders. At Scottish Building Society, we are very conscious that the balance of mortgage and savings rates requires constant attention, and to that end we have simplified our savings products and have committed to ensuring that we do not confuse savers by having initially high rates, dropping to lower rates at a later date. We also commit to ensuring that the rate on instant access savings accounts remains at a fair level and that there are no unfair conditions attaching to any of our mortgage or savings products.

Member Communication

Growing our member population and communicating with our members is extremely important to us to ensure that we are delivering the service and products they require. We have redeveloped our member newsletter, and look forward to meeting as many members as are able to attend, at our Annual General Meeting at the National Museum of Scotland in Edinburgh in May.

There will be an opportunity for all those attending to ask questions of the Board at the AGM, but for those who cannot attend, we will continue the practice of asking members to send in questions prior to the meeting. We will then group the questions into themes and aim to cover the answers at the AGM or in the newsletter.

Regulation

The Society is now regulated both by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) and we fully support the aims of both as they promote financial stability and good customer outcomes. We are confident that we are well placed to respond to the demands of the regulatory regime and that our business is operated in a manner which focuses solely on the needs of our members.

The management team and Board dedicate considerable time to ensuring a well-functioning relationship with both regulators and compliance with our regulatory obligations.

The Financial Services Compensation Scheme Levy is a significant cost of operating in the savings business, and this has cost us £201,000 for the year ended January 2015. We see no prospect of a reduction in this levy in the near future. The cost of operating in this environment is therefore a challenge for a small building society, but our dedication to attracting good quality lending and continuous improvements to operational processes give us the confidence that we are very well placed to respond to this challenge.

Our People

During the year the Chief Executive has led an experienced management team in implementing a number of key people initiatives. These included both the completion of an organisational change project to ensure that the most efficient and effective structure is in place to support the Society's business, and also a review of job and pay grades to ensure that our staff are appropriately rewarded and motivated to ensure stability within our workforce.

Both of these have been successfully completed and I would like to thank all of my colleagues working throughout the Society for their dedication and focus on the needs of our members.

Your Board

During the year, Moira Sibbald retired from the Board after six years and I would like to take this opportunity to thank her for the significant contribution she made throughout those years.

We are delighted to welcome two new Non-Executive Directors following a comprehensive recruitment process. Simon Pashby joined the Board in late 2014 and was previously an audit partner with KPMG, concentrating mainly on financial services companies and with a particular interest in the mutual sector. Jim Coyle joined in March 2015 and has over 20 years' experience within the banking sector and is currently Group Financial Controller of Lloyds Banking Group.

Looking Forward

As I noted last year, there are signs of recovery in the economy, and we expect this to continue throughout 2015. Forecasters are now not expecting the Bank of England Base Rate to increase until 2016 which will continue to impact savers. We will continue to focus on good quality lending, on providing fair mortgage and savings products, on improving our customer service experience, and therefore on delivering long term value to our Members.

Alexa H Henderson
Chairman

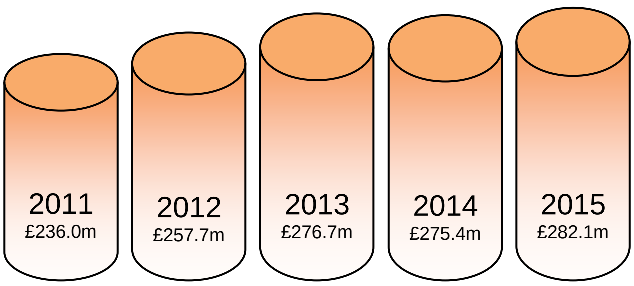
1 April 2015

Total Assets
£377.6million

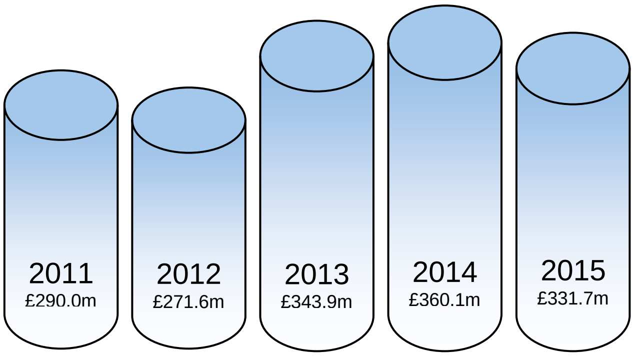
Liquid Assets
£93.2million

Profit Before Tax
(excluding exceptional items)
£2.1million

Mortgage Balances

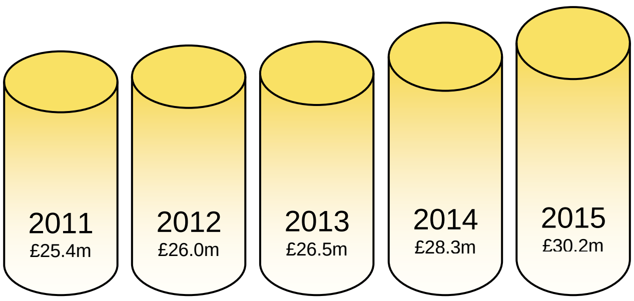


Savings Balances

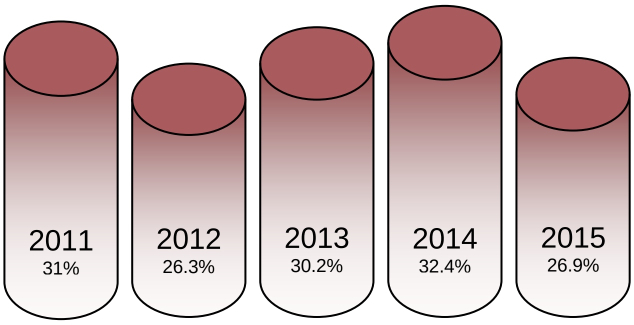


The Society's principal purpose is to provide mortgages for homeowners, funded by savings raised from our members whilst ensuring the Society's financial strength is maintained, as evidenced by strong Capital and Liquidity measures

Capital (Reserves)



Liquid Assets
as % of Shares & Deposits



Our Performance

I am delighted to report on another successful year for your Society where the underlying profit before tax and other items was 34% ahead of the previous year at £2.1million. Our retained profit, which further strengthens our reserves, was also up on last year. The Society's profits for this year have benefited from an upwards revaluation of the 'Century-heritage' mortgage assets which came across to the Society following our merger with Century Building Society on 1 February 2013. This reflects an improvement in the overall credit quality on this part of our mortgage portfolio, resulting from careful management over the past two years.

Besides the strong financial performance, the past year was a period during which a number of changes were made to our operating model, both in order to deliver improvements to our customer service proposition, and to introduce and embed some key regulatory requirements. These enhancements resulted in the re-allocation of a number of responsibilities around my Senior Management Team, which in terms of personnel, remained stable throughout 2014, except for the addition of Alan Searl, who joined the Society in April in the role of Head of Projects, following a career of 40-plus years, latterly with Lloyds Banking Group.

Mortgages

Our competitive strength in mortgages continues to be based upon our traditional approach to lending, where each application is individually assessed by an experienced professional. The employment of this operating model ensured the Society was well placed to implement the widely-reported regulatory changes to 'affordability', brought about by implementation of the Mortgage Market Review (MMR) in April 2014. Your Society will continue with this approach to lending, which often enables us to assist good quality applicants whose circumstances do not fit the computerised processing requirements employed by larger lenders.

The MMR also placed much more focus on the provision of mortgage advice. Our decision to maintain a team of fully-trained mortgage advisors throughout our branch network meant we were able to provide the necessary advice (without delay) to those applicants who chose to approach the Society direct for mortgage finance.

With some positive signs for the housing market, I am pleased to report that your Society played its part in assisting with the provision of finance for home ownership across Scotland, with gross lending in the year, at £51.1million, more than double that in the previous year (2014: £23.6million). Approximately 93% of this year's gross lending was to 'owner-occupiers'.

Recognising that it is principally the income from our mortgage assets that funds the interest paid to our savings members, it is encouraging that our overall net lending increased for the first time in two years to £282.1million (2014: £275.4million). Your Society will seek to increase its mortgage assets over the coming years in a balanced and controlled manner.

The Society's credit quality also remains strong, with the total number of mortgages three months or more in arrears (including possessions) having remained flat compared with last year.

Savings

Over the past year we have continued to work hard to achieve a fair balance between the interests of our savers and mortgage borrowers, recognising that it is very difficult for savers to receive real returns on their investments during this sustained low interest rate environment. We recognise the loyalty shown by our members and will endeavour to pay the best rate we can throughout the term of their relationship with us. By paying a consistently fair rate to our savers, we hope to retain existing members, whilst growing the Society by attracting new savers.

I mentioned in my Chief Executive's Review last year that we had been working to simplify our product range and to bring our rates across a number of like products into line. I am pleased to report that this exercise is almost complete, and that going forward it is our intention to ensure that all future savings products are completely transparent, with no onerous conditions or 'teaser' rates.

The Year Ahead

While I believe your Society has had a very good year, both in terms of its financial performance and in the number of key projects delivered, my Senior Management Team and I fully recognise that more can be achieved through continuous improvement, whether this be in terms of customer service, technology enhancement, or in how the Society engages with its members.

The key focus, however, will continue to be in the delivery of long-term value to our members, principally through the Society's 'Member Loyalty' initiatives, which are currently in the course of being finalised. I fully expect to be able to share details of these, together with what they will mean for our loyal members, in the summer.

Meantime, I firmly believe that your Society and its highly committed staff are well placed to continue to provide you, our members, with long-term value in the years ahead.

Mark L Thomson
Chief Executive

1 April 2015

Introduction

The Directors present their 166th Annual Report, together with the Annual Accounts and Annual Business Statement, for the year ended 31 January 2015.

Our Mission, Vision and Values Statements

The Society's Mission Statement is that "we aim to be the Building Society of choice for every stage in life".

Our Vision is "to remain Scottish, independent and mutual, providing a first class service and quality products for all members".

The values of the Scottish Building Society are:

- To provide professional and friendly service and to be clear and straightforward in all our communications with our members, who are both our customers and the owners of our business.
- To operate in accordance with the highest standards of integrity and transparency in all relationships with members, business partners and regulators.
- To earn the respect and trust of our members and to be socially responsible in everything we do.
- To maintain the Society's financial strength and stability and aim to be as cost-effective as possible.

Business Review

The Business Review is covered in the Chairman's Report and Chief Executive's Review on pages 1 to 5.

Profit and Capital

Profit for the year before tax, excluding the Financial Services Compensation Scheme (FSCS) levy and the upwards revaluation of 'Century-heritage' mortgage assets, amounted to £2.1million compared with £1.6million in 2013-14. This is a strong performance and further strengthens our reserves as a platform for future growth and the provision of member benefit. It also helps to ensure that the Society is well-placed for the stricter capital requirements due to come in under the latest Capital Requirements Directive (known as CRD4).

Gross capital and free capital as a percentage of shares and borrowings stood at 8.7% and 8.2% respectively at 31 January 2015 (2014: 7.7% and 7.2%). This is comparable with other building societies of a similar size to ourselves.

The Society is required to set out its capital position, risk exposures and risk assessment processes in its Pillar 3 disclosures document which is available on the Society's website or from the Society's Head of Finance.

Liquidity

Total cash and investments at 31 January 2015 amounted to £93.2million which represented 26.9% of total shares and borrowings, which compares with £119.2million (32.5%) at 31 January 2014. The Society's continuing aim is to maintain an appropriate level of liquidity at all times, in accordance with prudent management and regulatory requirements.

Interest Rates

The Bank of England base rate fell to an unprecedented 0.50% in March 2009. It has remained at that historical low since that date and there remains (at the time of writing) no firm indication as to when rates might start to rise again. As a result the Society's Standard Variable Rate for mortgages has remained unchanged at 5.29% throughout the financial year and there have also been no global changes to variable savings rates. There have been some changes to individual mortgage and savings products to reflect market conditions or as part of the process of harmonisation and simplification of products which was highlighted in last year's Report. This process saw rates being increased in March 2014 for 8,750 accounts, as a result of the first phase of the harmonisation of Instant Access accounts. Customers with accounts where rates were to be reduced as part of this exercise have been given advance notice of the change and their rates will be changed shortly.

The Society's long-term goal continues to be to generate member value through efficient and prudent management and the ongoing process to harmonise and simplify savings products will result (when completed) in a clear, simple range of products where all accounts on the same terms will receive the same rate of interest.

Mortgage Arrears and Forbearance

At 31 January 2015 the Group had only nine mortgage accounts in arrears for 12 months or more (2014: eleven). The total arrears outstanding on these accounts was £77,627 (2014: £142,748) and the aggregate capital balance was £712,509 (2014: £1,255,221). Five properties were taken into possession during the year, one of which was surrendered by the borrower voluntarily (2014: five).

The Society uses a number of forbearance measures to assist those borrowers who are, or could be, approaching a point of experiencing financial difficulty. Such measures include agreeing a temporary payment concession in order to reduce the borrowers' financial pressures. We expect borrowers to resume normal payments once they become able to do so. As at 31 January 2015 there were 59 cases benefiting from the Society's forbearance measures (2014: 74) with total outstanding capital balances of £4.1million (2014: £5.7million). The Society makes provisions for any expected loss resulting from accounts in arrears in accordance with the Board approved policy.

Key Performance Indicators

The Board and management monitor a range of performance indicators to assess the ongoing health of the Society. The financial indicators are shown in the table below – and some are also shown graphically on page 3. Their significance is explained as:

Total Assets: Consisting primarily of Mortgage Assets and Liquid Assets, these have decreased by 4.9% due to a planned reduction in Liquid Assets.

Mortgage Assets: One of the key reasons for the Society's existence is to promote home ownership through mortgage lending. During the past year Mortgage Assets have increased by 2.4%.

Share Balances: Another key reason for the Society's existence: to encourage saving and investment. Savings balances have been reduced by 7.9% during the past year as a function of the Society's overall balance sheet management referred to above.

Reserves: The accumulated profits of the Society over more than 166 years of operation, which provide the capital which helps to maintain the Society's financial strength. These have increased by £1.9million in the year through the addition of the year's profits.

Net Interest Margin: The income generated by the Society from its operations, expressed as a percentage of mean total assets. This has increased by 0.23 percentage points in the year as a result of a more efficient balance sheet structure.

Liquidity: Total cash and investments held by the Society at the year-end, expressed as a percentage of shares and borrowings. This has decreased by 5.5 percentage points in the year reflecting a more efficient balance sheet structure, but remains at a level well above regulatory requirements.

Gross Capital: This ratio is expressed as a percentage of shares and borrowings and demonstrates the relationship between the Society's capital and its liabilities to investors. It reflects the continuing strength of the Society whilst remaining well within prudent guidelines. This has increased by 1 percentage point as a combined result of increased profits and a reduction in Share Balances.

Asset Growth/Mortgage Asset Growth: The annual increase (decrease) in the Society's Total Assets and Mortgage Assets, shown as a percentage. The 4.9% reduction in Total Assets is primarily a function of the 2.4% increase in Mortgage Assets offset by a 22% decrease in Liquid Assets held.

Group Key Financial Performance Indicators 2011-2015

	2011	2012	2013	2014	2015
Total Assets	£333.1m	£342.7m	£387.8m	£397.2m	£377.6m
Mortgage Assets	£236.0m	£257.7m	£276.7m	£275.4m	£282.1m
Share Balances	£290.0m	£271.6m	£343.9m	£360.1m	£331.7m
Reserves	£25.4m	£26.0m	£26.5m	£28.3m	£30.2m
Net Interest Margin	1.56%	1.73%	1.65%	1.71%	1.94%
Liquidity	31.0%	26.3%	30.2%	32.4%	26.9%
Gross Capital	8.3%	8.2%	7.4%	7.7%	8.7%
Asset Growth	1.8%	2.9%	13.2%	2.4%	(4.9%)
Mortgage Asset Growth	2.1%	9.0%	7.0%	(0.5%)	2.4%

Non-Financial Key Performance Indicators

The Board also monitors a number of other indicators on a regular basis. Amongst these, it is pleasing to report that:

- 74% of mortgage borrowers reaching the end of their initial incentive period have remained with the Society.
- Customer complaints remain relatively low, with only 39 formal complaints registered during the year, of which 97% were resolved within four weeks of receipt.
- Less than 2% of mortgage accounts have arrears greater than 1.5% of their mortgage balance.

Regulation and Compliance

The regulatory landscape within which the Society operates has continued to change during the past year.

The new rules which came out of the Mortgage Market Review (MMR) initiated by the Financial Services Authority (FSA) were fully implemented by its successor body, the Financial Conduct Authority (FCA) in April 2014. The Society's existing operating model using individual assessment of all mortgage applications meant that we were well-placed to ensure that our existing and future customers benefited from these changes. Additional reporting requirements arising from MMR are now in place. The EU Mortgage Credit Directive (MCD) will come into force in the UK in March 2016 and this has necessitated further changes to mortgage regulation which will be implemented during the coming year. The Society is working hard to ensure that it will be ready for these additional changes.

The FSA's other successor body, the Prudential Regulation Authority (PRA) has also made a number of changes to regulations affecting the Society during the past year to implement changes to capital and liquidity regulation at a European level. Further significant changes are due to be implemented during the next twelve months, from both regulators. Whilst the Society continues to ensure that it has the resources to cope with these changes, it should be recognised that many of the new requirements place a disproportionate burden on smaller institutions.

The Society is required to have regard to the principles laid down in the UK Corporate Governance Code. This is covered in more detail in the separate Corporate Governance Report on pages 14 to 17.

Principal Risks and Uncertainties

The Society has a risk-averse strategy and maintains a comprehensive Risk Register reflecting the impact and likelihood of adverse events, which is regularly reviewed by the Board and covers all aspects of the business.

The principal business risks to which the Society is exposed are considered to be:

- **Credit Risk:** This relates to the risk that mortgage borrowers or treasury counterparties, to whom the Society has lent money, default on their obligation to pay. We seek to mitigate credit risk principally through the careful management of our underwriting policy and process, ensuring that all loans meet the criteria laid down in our Lending policy which is reviewed at least annually. The Society's exposure to treasury counterparties is carefully controlled in accordance with the limits set out in our Liquidity policy.
- **Interest Rate Risk:** This is the risk of the Society's financial position deteriorating as interest rates move over time and the failure to preserve interest rate margins arising from an increase in the cost of funds or a decrease in the earning capacity of assets. We seek to manage interest rate risk by matching the characteristics of mortgage and savings products and through the use of financial instruments within defined parameters.
- **Liquidity Risk:** This relates to the Society's ability to meet its financial obligations as they fall due. The Society has policies in place to ensure it maintains sufficient funds in liquid form at all times and stress tests are carried out regularly to confirm that the Society can withstand normal and abnormal cash outflows.
- **Operational Risk:** This is the risk of a loss arising from inadequate or failed internal processes or systems, human error or external events, including cyber risk. Processes and systems are in place to minimise these risks. As noted in the Corporate Governance Report, Board oversight of this area has been strengthened by the establishment of the new Operational Risk Committee chaired by a Non-Executive Director.
- **Strategic and Reputational Risk:** The risk of the Society entering unprofitable markets or offering unprofitable products. The Board has a duty to ensure that the Society makes an adequate amount of profit to maintain capital ratios at a sufficient level to provide long-term financial strength and stability for all members. This also includes risk arising from increased regulation by the financial services regulators.
- **Conduct Risk:** The risk of the Society failing to treat its customers fairly, with resulting detriment to those customers. The Conduct Risk Committee oversees the arrangements already in place to ensure that the Society continues to keep the needs of its members at the heart of everything we do.

A further risk stems from the continuing uncertainty inherent in the current economic environment. There are also additional risks arising from the impact of (a) the outcome of the UK General Election and (b) regulatory changes already mentioned. There remains the potential for further contributions to the FSCS levy which would impact upon the Society's capital and ability to compete over a period of time.

The Society will continue to adopt a cautious approach in the coming financial year, seeking moderate managed growth in order to maintain financial stability, whilst providing suitable mortgage and savings products to customers.

Financial Risk Management Objectives and Policies

The Society has a formal policy for the management of financial risk, including the arrangement of appropriate financial instruments to provide a hedge against identified exposure in fixed-rate lending. Particular risks including credit, liquidity and interest rate risk are considered in Notes 23(e) and 23(f) to the Accounts.

As a key component of the Society's management of financial risk, the Society has established a Management Assets & Liabilities Committee (MALCO) which meets at least monthly to make decisions within Board-prescribed parameters on product pricing, margin policy, hedging strategy and interest rate risk strategy. The MALCO reports to the Board's Assets & Liabilities Committee (ALCO), which in turn reports to the Board.

Capital Requirements

The Board has reviewed its risk assessment to meet the requirements of Basel III and the associated Capital Requirements Regulations and Directive (CRR/CRD4). The Society is required to conduct an assessment of the adequacy of its capital and resources, known as the Internal Capital Adequacy Assessment Process (ICAAP), which is regularly reviewed and revised to reflect the prevailing economic climate.

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 which came into effect on 1 January 2014 place certain reporting obligations on financial institutions that are within the scope of CRD4. The purpose of the regulations is to provide clarity on the source of the Society's income and the location of its operations. The annual reporting requirements for the Society as at 31 January 2015 are provided in Note 25 to the Accounts.

Going Concern

As part of the Society's forward planning process, the Directors have considered forecasts showing the Society's capital, liquidity and financial position for the next five years under normal operating conditions. They have also considered the potential effect on the Society's business, financial position, capital and liquidity under stressed operating conditions.

The Directors are satisfied that the Society has adequate resources to continue in business for the foreseeable future. For this reason, the Accounts continue to be prepared on the going concern basis.

Corporate Social Responsibility (CSR)

The Society recognises that CSR is concerned with how businesses take account of the social, environmental and economic impacts of their operations. We seek to be a good corporate citizen in all aspects of our operations and activities and aim to be recognised as a socially responsible business by our members, our staff and the communities in which we operate. This is articulated in our Corporate Social Responsibility Policy and regularly monitored by the Board.

Customer Service and Conduct of Business

The Society is committed to treating its members fairly and to acting with honesty and integrity in its relationships with members, regulators and the wider community. Continuous review and improvement is used to build on the high level of service throughout the Society and the many positive aspects already in place, as outlined in the Chief Executive's Review.

Donations and Community Support

The Society continues to provide support for local events in areas around its branches, and has chosen designated charities in each of its six branch areas, voted for by the local membership. The charities for 2015 are:

- **CLAN Cancer Care (Aberdeen):** CLAN supports anyone of any age affected by cancer from centres across North East Scotland, Moray, Orkney and Shetland.
- **St Columba's Hospice (Edinburgh):** St Columba's aims to improve the quality of life for people with progressive far advanced disease and to provide support for their families in Edinburgh and the surrounding areas.
- **Callum's Trust (Galashiels):** In addition to supporting the Margaret Kerr hospice at Borders General Hospital, Callum's Trust provides funding, resources and respite grants for blood cancer patients across the Scottish Borders.
- **Cancer Support Scotland (Glasgow):** Based at Gartnavel Hospital in Glasgow, Cancer Support Scotland provides emotional and practical support on a one-to-one basis and through community-based groups to anyone affected by cancer, including family, friends and carers.

- **Munlochy Animal Aid (Inverness):** Opened in 1978, Munlochy provides a sanctuary for unwanted or stray animals with the aim of re-homing them with caring owners.
- **RNLI/Troon Lifeboat (Troon):** RNLI provides, on call, a 24-hour lifeboat search and rescue service around the UK and Ireland, and a seasonal lifeguard service. Troon lifeboat provides rescue services covering the whole of the Clyde Coast.

The Society makes charitable donations to reflect and encourage members' participation in the Society's Annual General Meetings each year. £1,250 was donated in 2014 to Diabetes UK Scotland for postal and online votes received and for members who attended in person at the AGM in Perth. This year's AGM will be held at the National Museum of Scotland in Edinburgh on 27 May and a donation will be made to St Columba's Hospice, made up of £2 for every voting member attending and 50p for every postal and online vote received.

The Society does not make donations for political purposes.

Environmental Issues

The Society aims to minimise the environmental impacts of all our operations by striving to reduce unnecessary consumption, to re-use and recycle where possible, to manage energy usage wisely and to promote the control of environmental issues at all levels. We continue to use paper from sources approved by the Forestry Stewardship Council wherever possible, to recycle waste paper and other materials and to encourage our staff to be environmentally aware at all times. During the year, we replaced the Society's aging PCs and printers with equipment specifically designed to be more environmentally-friendly.

Following the successful introduction of online voting facilities, we also intend to reduce our impact on the environment in the future by allowing members to opt to receive future AGM packs electronically.

Employee Policies

The Society aims to create an environment in which all staff feel valued, where discriminatory behaviour is not tolerated and all employees are encouraged to enhance their skills through personal development and training programmes linked closely to their specific role and annual performance review.

Staff and Agents

The Directors recognise the contribution that staff at all levels make to the continuing success of the Society and would once again like to record their appreciation for the efforts made by everyone, particularly in what has been another very busy and challenging year.

The Directors also wish to acknowledge the assistance provided by our agency network that enables the Society to offer a counter service to members throughout Scotland, particularly in rural areas.

Directors

The following individuals were Directors of the Society during the year to 31 January 2015:

Non-Executive Directors

Alexa H Henderson BSc CA	Chairman
Robert Golbourn MBA FCIBS	Vice-Chairman & Senior Independent Director Chairman of Nomination & Remuneration Committee Chairman of Retail Credit Committee (until August 2014)
Moira R Sibbald LLB *Retired 28 October 2014*	Chairman of Audit Committee (until October 2014)
David Peebles MSc DipM MCIM FCIBS MCT	Chairman of Assets & Liabilities Committee
Raymond J Abbott CA	Chairman of Audit Committee (from October 2014) Chairman of Operational Risk Committee (October to December 2014)
John C Ogston FCIBS	Chairman of Retail Credit Committee (from September 2014)
Simon M Pashby BA FCA *Appointed 15 October 2014*	Chairman of Operational Risk Committee (from January 2015)

Executive Director

Mark L Thomson FCIBS	Chief Executive Chairman of Conduct Risk Committee

None of the Directors had any beneficial interest in the Society's subsidiary undertaking, SBS Mortgages Limited, as at the year end.

The Society maintains liability insurance cover for Directors and Officers as permitted by the Building Societies Act 1986.

Election of Directors

Simon Pashby and James Coyle have joined the Board since the 2014 Annual General Meeting and are retiring in accordance with Rule 25(4).

A proportion of the remaining Directors must retire from office by rotation each year under Rule 26 and Mark Thomson is therefore retiring this year.

Being eligible, all three Directors are offering themselves for election/re-election at the Annual General Meeting to be held on 27 May 2015.

Biographies of all current Directors, including those seeking election/re-election, appear on pages 12 & 13.

Post Balance Sheet Events

The Directors do not consider that there have been any events since the year-end that have a material effect on the financial position of the Society.

Supplier Payment Policy

The Society's continuing policy concerning the payment of its trade creditors is to pay within the agreed terms of credit, once the supplier has discharged their contractual obligations. The average number of days' credit taken to pay suppliers during the year ended 31 January 2015 was ten (2014: ten).

Auditor

Our auditor, KPMG LLP, has expressed their willingness to continue in office. The Board is happy to recommend their re-appointment as auditor and a resolution to that effect will be proposed for consideration at the Annual General Meeting to be held on 27 May 2015.

By order of the Board

Andrew J W Tristram
Secretary

1 April 2015

Alexa Henderson joined the Society's Board in 2001 and has chaired the Audit Committee, the Assets, Liabilities & Planning Committee and has also been Vice-Chairman of the ALCO and the Board itself. She was appointed as Society Chairman in June 2011. Alexa qualified as a Chartered Accountant and worked with KPMG and Arthur Andersen in Edinburgh and Melbourne, primarily in financial services audit. On returning to Edinburgh she joined the WM Company, provider of information services to investment funds. As a past Director of the WM Company, previously a Bankers Trust then Deutsche Bank subsidiary, and as Trustee of their company pension scheme, Alexa has experience in investment, compliance, financial and general management which she brings to the board of Scottish Building Society. Alexa was appointed to the Board of Adam & Company during 2012 and chairs their Audit Committee. She also holds non-executive directorships with James Walker (Leith) Ltd and Dunedin Smaller Companies Investment Trust plc.

Robert (Rob) Golbourn is a Fellow and former Member of Council of the Chartered Institute of Bankers in Scotland. He spent 30 years with Clydesdale Bank, in various management positions and later in senior roles including Regional Manager, Treasurer and Head of Credit. In 1994 he joined Scottish Widows, then an independent mutual, to set up a new banking subsidiary which grew to become a well-established operator in the direct and intermediary markets. He retired as Managing Director of Scottish Widows Bank in 2003. Rob keeps well up to date with financial sector issues through a wide network of contacts established throughout his career. Rob joined the Board in 2006 and is currently Vice-Chairman, Senior Independent Director and Chairman of the Nomination & Remuneration Committee.

David Peebles joined the Board in 2006 and is currently Chairman of the Assets & Liabilities Committee. He is a Fellow of the Chartered Institute of Bankers in Scotland and a Chartered Banker. He has a Postgraduate Diploma and a Masters Degree in Marketing and is also a member of the Association of Corporate Treasurers. As a former bank Treasurer he has an in-depth knowledge of Risk and Balance Sheet management. David is Managing Director of XM International Associates Ltd which provides consultancy advice to a diverse group of financial services organisations worldwide.

Raymond Abbott is a Chartered Accountant by profession and has worked in private equity and investment for over twenty years. As the former managing director of Alliance Trust Equity Partners he was responsible for strategic development. Previously he founded the UK venture investor Albany Ventures and prior to that was Director of Investment at British Linen Bank. Raymond also serves as a non-executive director of Foresight 4 plc, Galleria Holdings Limited and Essex Services Group plc. He therefore brings a wealth of financial experience to the Board. Raymond joined the Board in June 2013 and currently chairs the Audit Committee.

John Ogston joined the Board in July 2013 and chairs the Retail Credit Committee. Jack is a Fellow of the Chartered Institute of Bankers in Scotland, having spent 36 years in management positions with Clydesdale Bank, latterly as Head of Corporate & Structured Finance in Scotland. He has significant board and lending experience and is currently a non-executive director of Vehicle Professionals Ltd.

Simon Pashby qualified as a Chartered Accountant with Price Waterhouse, and then joined KPMG in New Zealand as an auditor to major international banks. On his return to UK in 1990 he specialised in regulated financial services, based in Edinburgh and Glasgow. He has over 25 years' experience in financial services, 15 as the partner responsible for signing audit opinions and advising a wide range of boards on risks and controls. Simon retired from KPMG in 2012, and maintains his current financial knowledge as a Fellow of the Institute of Chartered Accountants. He is also a non-executive director and Vice Chairman of the Medical Protection Society, a members' mutual fund and leading medical defence organisation. Simon joined the Board in October 2014 and currently chairs the Operational Risk Committee.

James Coyle was appointed to the Board in March 2015. He qualified as a Chartered Accountant with KPMG and spent 10 years in the oil industry holding senior positions with BP. Jim joined Bank of Scotland in 1991 and became Group Chief Accountant in 1998. In 2012 Jim was appointed Group Financial Controller at Lloyds Banking Group (LBG), having previously been Divisional Finance Director, Group Operations. Jim is a Fellow of the Chartered Institute of Bankers in Scotland, on the Council of the Institute of Chartered Accountants of Scotland, and a member of the Financial Reporting Council's Financial Reporting Review Panel. Jim is also Chair of the Audit Committee of VocaLink Holdings Ltd, on the Board of Scottish Financial Enterprise and a member of the BBA Audit Committee.

Mark Thomson was appointed as Chief Executive on 1 May 2013, having joined the Society in April 2012 in the role of Chief Operating Officer and been appointed to the Board in October 2012. He is a Fellow of the Chartered Institute of Bankers in Scotland and a Chartered Banker. During his career of 30-plus years, Mark has worked in a variety of roles in retail banking, including 16 years at Scottish Widows Bank, where his responsibilities included credit risk management and compliance, as well as a wide range of operational activities. Mark was appointed to the Board of Scottish Widows Bank in January 2006 as Credit Director – a position he held until joining the Society. Mark currently chairs the Society's Conduct Risk Committee and the Management ALCO.

The Directors are responsible for the governance of the Society, on behalf of the members, and are committed to good practice in Corporate Governance. They have regard to the principles of the UK Corporate Governance Code for listed companies issued in September 2012 ('the Code') as it applies to building societies, in accordance with the expectation of the regulators. They are also mindful of updates to the Code published in September 2014, which will apply to subsequent reporting periods.

The Role of the Board

The principal functions of the Board are to set the Society's strategy, as articulated in the Corporate Plan and annual business plans agreed by the Board, to ensure that the necessary financial and human resources are in place for the Society to meet its objectives, and to review management performance. The Board is responsible for succession planning for both Executive and Non-Executive Director positions. As part of its annual evaluation process, the Board considers the balance of skills and experience it requires, the requirements of the business, and recommends change where appropriate.

The full Board normally meets on a monthly basis with additional meetings as required. In 2014-15 there were thirteen Board meetings and a specific meeting to consider strategy and the Corporate Plan. A table showing details of Directors' attendance during the year in relation to Board and Committee meetings forms part of this report and appears on page 16.

There is a schedule of matters reserved for Board decision and the Board has delegated certain responsibilities to the Committees described below, all of which report to the Board. Minutes of each Committee's meetings are distributed to all Board members and the Chairman of each Committee provides a report at the Board meeting following any meeting of that Committee. The terms of reference for all Committees are available on the Society's website and the membership of committees is reviewed annually. The Society maintains liability insurance cover for Directors and Officers.

Audit Committee: This Committee met on five occasions during the year and is chaired by an independent Director. The Chief Executive, other members of management and internal and external auditors attend by invitation only. The Committee considers regulatory compliance matters and adequacy of internal controls. It also reviews audit reports, monitors the effectiveness of the internal audit function and agrees the annual internal audit plan. It considers and recommends to the Board (for approval by the members) the appointment or re-appointment of the external auditors, and the policy on the engagement of the external auditors for non-audit services and approval of their fees. The Committee also monitors the external auditors' independence, objectivity, competence and effectiveness. It also ensures that the systems of accounting, business control and management of information are adequate for the Society's needs. At least annually the Committee meets with the external auditors without members of the Management team being present. As required by the Code, the Committee provides advice to the Board confirming that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for members to assess the Society's performance, business model and strategy.

The Committee comprises three Non-Executive Directors who all have relevant financial experience. Moira Sibbald chaired the Committee for the first part of the year, and was succeeded by Raymond Abbott; other members during the year were Rob Golbourn and Simon Pashby. The Society Chairman and members of senior management attend by invitation, together with representatives from the internal and external auditors.

Assets & Liabilities Committee (ALCO): This Committee held six meetings during the year and its remit includes monitoring capital and liquidity, balance sheet structure, financial risk management, pricing of new and existing products, and monitoring of treasury activities – including counterparties, interest rate risk and basis risk and performance against the Society's overall Financial Risk Appetite. It also oversees the work of the Management ALCO, which meets monthly.

The Committee comprises three Non-Executive Directors, together with the Chief Executive and Head of Finance. The Committee is chaired by David Peebles and Non-Executive members during the year were Alexa Henderson and Raymond Abbott. Other members of senior management and the Finance team attend by invitation.

Retail Credit Committee: This Committee provides Board oversight of retail credit risk. Membership consists of three Non-Executive Directors, Rob Golbourn, David Peebles and Jack Ogston, and the Chief Executive, and meetings are attended by the Head of Operations & Lending together with other relevant staff as necessary. Rob Golbourn was Chairman for the first part of the year, before passing the baton to Jack Ogston.

The Committee held ten meetings during the year and its remit includes reviewing lending policies, monitoring of mortgage market conditions from a credit risk perspective, reviewing the credit quality and risk profile of the mortgage book, assessing credit risks associated with new and existing mortgage products, overviewing lending decisions, monitoring arrears and reviewing specific and general loss provisions and general oversight of performance against the Society's Credit Risk Appetite. Any recommendations for changes to policies are referred to the Board for approval.

Nomination & Remuneration Committee: This Committee reviews Board constitution, skills, performance, succession plans and Director elections and is responsible for remuneration policy for all Directors and for making recommendations to the Board regarding general remuneration and contractual arrangements. It also supervises the process for appointment of new Directors. All the Non-Executive Directors are members of the Committee, which is chaired by the Senior Independent Director, Rob Golbourn. The Chief Executive attends by invitation but takes no part in any discussion of his own remuneration. There were five meetings during the year.

Conduct Risk Committee: This Committee has been established by the Board to provide assurance that members (or potential members) are being treated fairly and consistently and that Conduct Risks are being appropriately managed by monitoring performance against the Society's Conduct Risk Appetite. The Committee is chaired by the Chief Executive, and consists of one Non-Executive Director, Alexa Henderson (with David Peebles as alternate), the Head of Operations & Lending and the Secretary & Head of Compliance. Other members of the Management team attend as required. The Committee held nine meetings during the year.

Operational Risk Committee: Following a comprehensive review of the Society's Risk Management Framework during the year, it was decided that the existing Risk Management Committee should be replaced by a Board Committee chaired by a Non-Executive Director whose primary role is to monitor performance against the Society's Operational Risk Appetite. This Committee met for the first time in September and has held five meetings since then, initially chaired by Raymond Abbott and latterly by Simon Pashby. In addition to the Committee Chairman, the Committee consists of the Chief Executive, the Head of Finance, the Head of Operations & Lending, the Head of Sales & Marketing and the Secretary & Head of Compliance. Other managers attend as required.

Division of Responsibilities: Chairman and Chief Executive

The offices of Chief Executive and Chairman are distinct and held by different people. The Chief Executive is responsible for managing the Society's business within the parameters set by the Board. The Chairman sets the direction and culture of the Board, facilitating effective contribution from Directors, maintaining constructive relations between Executive and Non-Executive Directors and ensuring that Directors receive accurate, timely and clear advice and information. The current Chairman (Alexa Henderson) was considered independent on her appointment in June 2011, having demonstrated clear commitment, experience, and capability since joining the Board in March 2001.

Non-Executive Directors

Non-Executive Directors are required to have a full understanding of the risks in the business; to show commercial leadership within a framework of prudent and effective risk management controls; to provide an independent perspective, monitoring performance and resources; and to constructively challenge strategic proposals, whilst supporting the Executive management. The Non-Executive Directors meet regularly without the Chief Executive present. The Board has appointed a Senior Independent Director, Rob Golbourn, to provide support for the Chairman and an alternative route for communication from members and staff. His main responsibilities are to chair the Nomination & Remuneration Committee and to carry out the appraisal of the Chairman, taking into account the views of the other Directors.

The Composition of the Board

The Board currently consists of seven Non-Executive Directors plus the Chief Executive, providing a balance of skills and experience appropriate for the requirements of the business. The Board is satisfied that in terms of independence of character, judgement and robustness of challenge to the Society's Management, each Non-Executive Director is considered independent. Factors taken into account when assessing independence include length of service, material business relationships and whether the Director has recently been an employee of the Society.

Although Alexa Henderson has been a Non-Executive Director for more than nine years, the Board is satisfied that her length of service does not impair her independence and that she continues to bring valuable knowledge and experience to the Society.

There are no current business relationships between the Society and firms connected with Directors. No ex-employees are or have been Non-Executive Directors.

Appointments to the Board

The Society values all aspects of diversity, including gender, and ensures that Non-Executive Director appointments are made on merit, based on the specific skills and experience required. Vacancies are advertised within the Society's membership and more widely where appropriate. Members have the right under the Society's Rules to nominate candidates for election to the Board. The Nomination & Remuneration Committee leads the recruitment process, although the final decision rests with the Board as a whole.

All Directors must meet the requirements of fitness and propriety laid down by the regulators and all Directors must be approved by the regulators in order to fulfil their controlled function as a Director.

Commitment

The Nomination & Remuneration Committee evaluates the ability of Non-Executive Directors to commit the time required for their role, prior to appointment. The letter of appointment sets out the expected time commitment and Directors undertake that they have sufficient time to meet those expectations. The formal appraisal process carried out by the Chairman each year also assesses whether Directors have demonstrated this ability during the year.

The attendance record of Board and Committee members during the year is set out below. This table does not reflect Directors' attendance at additional ad hoc meetings, seminars, conferences and courses during the year or time spent on preparation for meetings etc. Generally each Non-Executive Director spends a minimum of 2-3 days each month on Society business and the Chairman's time commitment is considerably more.

Directors' Attendance 2014-15

The table below shows the number of Board meetings attended by each Director and, for each of the Board Committees, the number of meetings and attendance by individuals as members of those Committees.

The figures in brackets denote the number of meetings each Director was eligible to attend.

	Board	Audit Committee	Assets & Liabilities Committee	Retail Credit Committee	Operational Risk Committee	Conduct Risk Committee	Nomination & Remuneration Committee
R J Abbott	14(14)	5(5)	6(6)	-	4(4)	-	5(5)
R Golbourn	14(14)	5(5)	-	10(10)	-	-	5(5)
A H Henderson	11(14)	-	5(6)	-	-	7(9)	4(5)
J C Ogston	13(14)	-	-	9(10)	-	-	5(5)
S M Pashby	4(4)	1(1)	-	-	2(2)	-	1(1)
D Peebles	13(14)	-	5(6)	9(10)	-	2(2)	4(5)
M R Sibbald	8(11)	1(4)	-	-	-	-	2(4)
M L Thomson	14(14)	-	6(6)	9(10)	3(5)	9(9)	-

Development

All new Directors receive induction training, and ongoing training is provided by attendance at courses and seminars organised by outside bodies, in particular the Building Societies Association. Training and development needs are identified as part of the annual appraisal of the Board's and individual Director's performance and effectiveness. The Secretary has specific responsibility for ensuring that Directors are provided with appropriate information and training.

Information and Support

The Chairman ensures that the Board receives sufficient information to enable it to discharge its responsibilities. The quality and content of management information provided to the Board and Committees is constantly reviewed by Directors and management. The Secretary provides support on corporate governance matters and the Board has access to independent professional advice if required.

Evaluation

The Chairman & Vice-Chairman review the performance of the Chief Executive annually. Non-Executive Directors are evaluated by the Chairman using questions based on the FRC guidance on Board Effectiveness issued in March 2011. The Chairman is evaluated by the Senior Independent Director, taking into account the views of the other Directors. The Board evaluates its overall performance and that of each Committee. This process is used to improve the effectiveness of Directors and the Board collectively.

Re-election

The Society's Rules require that Directors are submitted for election at the Annual General Meeting (AGM) following their appointment to the Board. All Directors are required by the Society's Rules to seek re-election if they have not been elected at either of the two previous AGMs. Directors may also submit themselves for re-election voluntarily. The Nomination & Remuneration Committee considers and makes a recommendation to the Board whether each Non-Executive Director should be submitted for re-election, bearing in mind that Director's continued independence and contribution to Board deliberations. The UK Corporate Governance Code specifies that any Director serving for longer than nine years should be subject to annual re-election by the members. The Board considers that annual re-election is not appropriate for the Society, as compliance with the requirements under the Society's Rules has tended to mean Directors standing for re-election every two years.

Financial and Business Reporting

The Statement of Directors' Responsibilities on page 20 sets out the Board's responsibilities in relation to the Society's Annual Report and Accounts and a statement that the Society's business is a going concern is included in the Directors' Report on page 9.

Risk Management and Internal Control

The Board is collectively responsible for determining strategies for risk management and control. Senior management are responsible for designing, operating and monitoring risk management and internal control processes through the Risk Management Committee that reports directly to the Board each month. The Board reviews the adequacy of these processes and the Internal Audit function provides independent and objective assurance that the processes are appropriate and effectively applied. The Society has a strong compliance culture and the Board is satisfied that the Society's systems are effective and appropriate to the scale and complexity of the Society's business.

Remuneration

The Directors' Remuneration Report on pages 18 & 19 sets out the remuneration policies for Executive and Non-Executive Directors and explains how this meets the requirements of the UK Corporate Governance Code.

Dialogue with Shareholders

As a mutual organisation the Society does not have 'shareholders' as referred to in the Code, and the Society's saving and borrowing customers are also its members. The Society seeks the views of its members through membership surveys, members' forums, the Society newsletter and the AGM.

Constructive Use of the Annual General Meeting (AGM)

Each year the Society sends details of the AGM to those members who are eligible to vote. The AGM is held in a different location each year to encourage member attendance and participation. Resolutions include the election of Directors and a separate advisory vote on the Directors' Remuneration Report.

Members are encouraged to exercise their right to vote and a donation to charity is made for each vote cast either in person or by proxy. Members are provided with forms and prepaid envelopes which enable them to appoint a proxy to vote on their behalf if they are unable to attend in person. Proxy voting can also be conducted via a secure website. The proxy form and website provide the opportunity to formally abstain in respect of any resolutions, should the member so wish. The receipt and counting of proxy votes is conducted by independent scrutineers.

At the AGM a poll is called in relation to each resolution and the proxy votes cast are included in the result. The results are subsequently disclosed on the Society's website. Members who cannot attend the meeting are encouraged to submit questions in writing.

Alexa H Henderson
Chairman

1 April 2015

The purpose of this report is to inform members of the Society, in line with the relevant provisions of the UK Corporate Governance Code, of the policy for determining the remuneration of Executive and Non-Executive Directors. The Society has adopted a Remuneration Policy which meets the applicable requirements of the Remuneration Code issued by the Financial Conduct Authority.

A statement of all Directors' Remuneration is included within this report and also appears in the Summary Financial Statement issued annually to all members. An advisory vote on Directors' Remuneration is included in the AGM agenda.

As a mutual organisation, the Society has no share option scheme and none of the Directors has any beneficial interest in, or any rights to subscribe for, shares in or debentures of any connected undertaking of the Society.

Procedure for Developing Policy on Executive & Individual Director Remuneration

The Board has overall responsibility for overseeing arrangements for remuneration. This is done through the Nomination & Remuneration Committee, which is chaired by the Senior Independent Director. All Non-Executive Directors are members of the Committee and the Chief Executive attends meetings and acts as secretary of the Committee but takes no part in discussions on his own remuneration.

The Committee reviews remuneration for Directors and staff annually, using data from comparable organisations and taking advice from external consultants when appropriate.

Non-Executive Directors

The level of fees payable to Non-Executive Directors is assessed annually using market information and data from comparable organisations. The fees payable to the Chairman and Vice-Chairman reflect the additional responsibilities of these positions.

Fees for Non-Executive Directors are non-pensionable and Non-Executive Directors do not participate in any bonus or incentive schemes or receive any other benefits other than reimbursement of expenses incurred in the execution of their duties as Directors.

Executive Director

The Chief Executive’s basic salary is reviewed annually by reference to jobs carrying similar responsibilities in comparable organisations and by reference to market conditions and personal performance.

His contract with the Society includes a non-pensionable executive bonus scheme which is payable dependant on the Society's performance and the individual's personal performance measured against pre-agreed objectives. For Society performance there are a number of key measures set by the Board – including membership numbers, net lending and savings targets, arrears management, risk management and compliance with regulations – all of which are to be achieved within a specified set of financial ratios. The Board also sets four or five individual objectives against which the individual is assessed for personal performance. No single factor can therefore unduly influence the amount of bonus payable.

Bonus payments to the Chief Executive are not guaranteed and are reviewed each year.

The Society makes a minimum contribution of 20% of salary to the Chief Executive’s private pension arrangements and he also receives a further taxable benefit comprising a Society car.

Service Contracts

The Chief Executive has a service contract with the Society which can be terminated by either side giving six months’ notice.

Non-Executive Directors do not have service contracts but serve under letters of appointment subject to election by the Society's members.

Non-Executive Directors

	Fees only	
	To 31 January 2015	To 31 January 2014
R J Abbott (appointed 1 June 2013)	£20,267	£13,333
D W P Chalmers (retired 28 May 2013)	-	£6,087
G B Clark (retired 28 May 2013)	-	£6,087
R Golbourn	£24,320	£23,157
A H Henderson	£33,440	£31,567
J C Ogston (appointed 1 July 2013)	£20,267	£11,667
S M Pashby (appointed 15 October 2014)	£6,120	-
D Peebles	£20,267	£19,420
M R Sibbald (retired 28 October 2014)	£15,167	£19,420
Total	**£139,848**	**£130,738**

The fees shown for Mr Ogston were paid through a third-party service company.

Executive Directors

To 31 January 2015					
	Salary	Bonus	Pension Contributions	Taxable Benefits	Total
M L Thomson	£130,000	£20,000	£26,000	£3,914	£179,914
Total 2015	**£130,000**	**£20,000**	**£26,000**	**£3,914**	**£179,914**

To 31 January 2014					
	Salary	Bonus	Pension Contributions	Taxable Benefits	Total
G J Kay (resigned 30 April 2013)	£25,950	-	£5,839	£2,122	£33,911
M L Thomson	£97,400	£11,500	£19,080	£6,367	£134,347
Total 2014	**£123,350**	**£11,500**	**£24,919**	**£8,489**	**£168,258**

Mr Kay also received a final contractual payment on his resignation as Chief Executive amounting to £122,393.

All pension contributions paid by the Society were in respect of money-purchase pension schemes.

Robert Golbourn
Chairman, Nomination & Remuneration Committee

1 April 2015

Directors' responsibilities for preparing the Annual Report, the Annual Business Statement, the Directors' Report and the Annual Accounts

The Directors are responsible for preparing the Annual Report, Annual Business Statement, Directors' Report and the Annual Accounts in accordance with applicable law and regulations.

The Building Societies Act 1986 ("the Act") requires the Directors to prepare Group and Society Annual Accounts for each financial year. Under that law they have elected to prepare the Group and Society Annual Accounts in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

The Group and Society Annual Accounts are required by law to give a true and fair view of the state of affairs of the Group and of the Society as at the end of the financial year and of the income and expenditure of the Group and of the Society for the financial year.

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

- select appropriate accounting policies and apply them consistently;
- make adjustments 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 Annual Accounts;
- prepare the Annual Accounts on the going concern basis, unless it is inappropriate to presume that the Group and Society will continue in business.

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

Directors' responsibilities for accounting records and internal controls

The Directors are responsible for ensuring that the Group:

- keeps proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and Society, in accordance with the Act; and
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Financial Conduct Authority and Prudential Regulation Authority under the Financial Services and Markets Act 2000 (as amended).

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

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

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SCOTTISH BUILDING SOCIETY

We have audited the Group and Society Annual Accounts of Scottish Building Society for the year ended 31 January 2015 set out on pages 22 to 40. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the Society's members, as a body, in accordance with section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the Society'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 Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 20, the Directors are responsible for the preparation of Annual Accounts which give a true and fair view. Our responsibility is to audit, and express an opinion on, the Annual Accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the Annual Accounts

A description of the scope of an audit of annual accounts is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on Annual Accounts

In our opinion the Annual Accounts:

- give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of affairs of the Group and of the Society as at 31 January 2015 and of the income and expenditure of the Group and of the Society for the year then ended; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and regulations made under it.

Opinion on other matters prescribed by the Building Societies Act 1986

In our opinion:

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

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Building Societies Act 1986 requires us to report to you if, in our opinion:

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

Catherine Burnet (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
20 Castle Terrace
Edinburgh

1 April 2015

INCOME AND EXPENDITURE ACCOUNT
for the year ended 31 January 2015

	Notes	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
Interest receivable and similar income	2	**12,138**	13,157	**12,079**	13,095
Interest payable and similar charges	3	**4,641**	6,435	**4,641**	6,435
Net interest receivable		**7,497**	6,722	**7,438**	6,660
Fees and commissions receivable		**57**	32	**57**	32
Fees and commissions payable		**667**	540	**667**	540
Other operating income		**519**	402	**519**	402
Total Income		**7,406**	6,616	**7,347**	6,554
Administrative expenses	5	**4,909**	4,725	**4,854**	4,665
Depreciation and amortisation	15	**256**	245	**256**	245
Other operating charges	4	**98**	44	**98**	44
Provisions for bad and doubtful debts	12	**54**	43	**54**	43
Profit before movements in acquired assets, FSCS levy and merger costs		**2,089**	1,559	**2,085**	1,557
Net increase in values of acquired assets	13	**439**	-	**439**	-
Provision for FSCS levy	21	**201**	258	**201**	258
Merger costs	26	**-**	235	**-**	235
Profit on ordinary activities before tax		**2,327**	1,066	**2,323**	1,064
Tax on profit on ordinary activities	8	**420**	47	**419**	47
Profit for the financial year	22	**1,907**	1,019	**1,904**	1,017

The Notes on pages 25 to 40 form part of these accounts.

The above results are all derived from continuing operations.

"Profit on ordinary activities before tax" represents the FRS3 caption "Operating profit".

There are no recognised gains or losses other than the profits above and therefore no separate statement of recognised gains or losses has been presented.

BALANCE SHEET
as at 31 January 2015

SCOTTISH BUILDING SOCIETY

	Notes	Group 2015 £000	Group 2014 £000	Society 2015 £000	Society 2014 £000
ASSETS					
Liquid Assets:					
Cash in hand and balances with the Bank of England		**52,145**	54,153	**52,145**	54,153
Loans and advances to credit institutions	*9*	**8,385**	31,841	**8,385**	31,841
Debt securities	*10*	**32,666**	33,169	**32,666**	33,169
		93,196	119,163	**93,196**	119,163
Loans and Advances to Customers:	*11, 12*				
Loans Fully Secured on Residential Property		**265,496**	257,716	**264,424**	256,598
Loans Fully Secured on Land		**16,647**	17,668	**16,647**	17,668
		282,143	275,384	**281,071**	274,266
Investments:					
Investment in subsidiary undertaking	*14*	**-**	-	**10**	10
Tangible Fixed Assets	*15*	**2,007**	2,000	**2,007**	2,000
Other Assets		**28**	273	**28**	273
Prepayments and Accrued Income		**223**	412	**223**	412
TOTAL ASSETS		**377,597**	397,232	**376,535**	396,124
LIABILITIES					
Shares	*16*	**331,726**	360,085	**331,726**	360,085
Amounts owed to Credit Institutions	*17*	**2,502**	-	**2,502**	-
Amounts owed to Other Customers	*18*	**11,622**	7,098	**11,622**	7,098
Other Liabilities	*19*	**598**	689	**1,095**	1,137
Accruals and Deferred Income		**571**	646	**571**	646
Provisions for Liabilities	*21*	**382**	425	**382**	425
Reserves:					
General Reserves	*22*	**30,196**	28,289	**28,637**	26,733
TOTAL LIABILITIES		**377,597**	397,232	**376,535**	396,124

The Notes on pages 25 to 40 form part of these accounts.

These accounts were approved by the Board of Directors on 1 April 2015 and were signed on its behalf by:

Alexa H Henderson
Chairman

Robert Golbourn
Vice Chairman

Mark L Thomson
Chief Executive

GROUP CASH FLOW STATEMENT
for the year ended 31 January 2015

	2015 £000	2014 £000
Net cash (outflow)/inflow from operating activities	(7,508)	4,984
Taxation	(191)	(328)
Capital expenditure and financial investment		
Purchase of debt securities	(29,027)	(33,519)
Sale and maturity of debt securities	29,572	30,561
Purchase of tangible fixed assets	(275)	(361)
Proceeds from disposal of tangible fixed assets	28	714
Acquired on transfer of engagements	-	3,597
(Decrease)/Increase in cash	(7,401)	5,648

Reconciliation of operating profit to net cash (outflow)/inflow from operating activities

	2015 £000	2014 £000
Operating profit	2,327	1,066
Decrease in prepayments and accrued income	210	265
(Decrease) in accruals and deferred income	(859)	(1,015)
Amounts relating to specific provisions written off during the year	(54)	(164)
Provisions for bad and doubtful debts	54	43
Provision for FSCS levy	(43)	14
Depreciation and amortisation	256	245
(Profit) on sale of tangible fixed assets	(16)	(7)
Net cash inflow from trading activities	1,875	447
Loans and advances made to customers	(51,125)	(23,579)
Loans and advances repaid by customers	44,367	40,899
Net (decrease) in shares	(27,561)	(3,873)
Net increase/(decrease) in amounts owed to credit institutions and other customers	7,012	(8,407)
Net decrease/(increase) in loans and advances to credit institutions	18,000	(500)
Net decrease/(increase) in other assets	44	(9)
Net (decrease)/increase in other liabilities	(120)	6
Net cash (outflow)/inflow from operating activities	(7,508)	4,984

Reconciliation of cash balances	2014 £000	Cash Flow	2015 £000
Cash in hand and balances with the Bank of England	54,153	(2,008)	52,145
Loans and advances to credit institutions - repayable on demand	7,753	(5,393)	2,360
	61,906	(7,401)	54,505

	2013 £000	Cash Flow	2014 £000
Cash in hand	34,655	19,498	54,153
Loans and advances to credit institutions - repayable on demand	21,603	(13,850)	7,753
	56,258	5,648	61,906

1. PRINCIPAL ACCOUNTING POLICIES

Accounting convention

The Accounts are drawn up under the historical cost convention.

Format of accounts

The Accounts have been prepared in accordance with the Building Societies Act 1986, the Building Societies (Accounts and Related Provisions) Regulations 1998 and applicable accounting standards.

Basis of consolidation

The Group Accounts comprise the accounts of the Society and its subsidiary undertaking made up to 31 January each year.

Deferred taxation

Provision is made, using the liability method, on a non-discounted basis for taxation at the relevant rate in respect of all items where there is a timing difference between their treatment for accounts and taxation purposes except where, in the opinion of the Directors, it is likely that tax assets would not be recoverable in the foreseeable future.

Tangible fixed assets and depreciation

i) The cost of additions and major alterations to office premises, equipment and fixtures and fittings is capitalised.

ii) The cost of freehold premises is written off over 50 years on a straight-line basis. No depreciation is provided on freehold land.

The cost of other fixed assets is written off over their estimated useful lives as follows:

The cost of tenant's improvements to leasehold premises is written off over 5 years on a straight-line basis.

Office equipment and motor vehicles are depreciated over 4 to 10 years on a straight-line basis.

Liquid assets

Liquid assets are stated at the lower of cost and net realisable value, including debt securities and treasury bills intended for use on a continuing basis. Premia and discounts arising on the purchase of debt securities held as financial fixed assets are amortised on a straight-line basis over the period to maturity.

Pension costs

The Society operates defined contribution pension schemes administered by two British life companies, the funds of which are separate from those of the Society. Contributions are charged to revenue in the year in which they are made and are included in management expenses.

Provisions for bad and doubtful debts

A mortgage loss provision is considered where the Society concludes that a loan might not be recovered in full.

Throughout the year and at the end of the year individual assessments are made of all advances meeting one or more of a number of trigger points that are considered to be indicators of where a potential loss might arise. Specific provisions are made for the extent of the likely loss. Interest continues to be charged to these accounts as it becomes due and is included in the provision. In addition, a general provision is made in respect of advances where a specific provision has not been raised.

The Society uses forbearance tools where they are deemed appropriate for individual customer circumstances. Mortgage balances subject to some form of forbearance are fully covered in the Society's provisioning methodology.

Incentives to new borrowers

Incentives not having the characteristics of interest are written off as they are incurred and are disclosed within other operating charges. Interest rate discounts reduce interest receivable over the term of the discount period.

Leases

Rental charges under "operating leases" are charged to the Income and Expenditure Account evenly over the life of the lease.

Assets held by the Society for use in operating leases are included as tangible fixed assets. Rents receivable under operating leases are recognised in the Income and Expenditure Account as they fall due.

1. PRINCIPAL ACCOUNTING POLICIES (continued)

Off-Balance Sheet Instruments

All interest-related contracts are classified at the balance sheet date as hedging contracts.

All hedging contracts are valued and income or expenditure recognised on an equivalent basis to the assets, liabilities or positions that are being hedged. If the hedging contract is terminated early, the realised gain or loss is charged immediately to the Income and Expenditure Account.

2. INTEREST RECEIVABLE AND SIMILAR INCOME

	Group		Society	
	2015 £000	2014 £000	**2015 £000**	2014 £000
On loans fully secured on residential property	**11,181**	12,029	**11,122**	11,967
On other loans	**743**	827	**743**	827
Net expense on financial instruments	**(466)**	(487)	**(466)**	(487)
On debt securities:				
- interest and other income	**430**	561	**430**	561
On other liquid assets:				
- interest and other income	**250**	227	**250**	227
	12,138	13,157	**12,079**	13,095

3. INTEREST PAYABLE AND SIMILAR CHARGES

Group & Society	**2015 £000**	2014 £000
On shares held by individuals	**4,594**	6,413
On other shares	**9**	13
Net income on financial instruments	**(19)**	(80)
On deposits and other borrowings	**57**	89
	4,641	6,435

4. OTHER OPERATING CHARGES

	Group		Society	
	2015 £000	2014 £000	**2015 £000**	2014 £000
Incentives to borrowers	**98**	44	**98**	44

5. ADMINISTRATIVE EXPENSES

	Group		Society	
	2015	2014	**2015**	2014
	£000	£000	**£000**	£000
Staff costs (Note 6)	**2,637**	2,525	**2,637**	2,525
Other expenses	**2,272**	2,200	**2,217**	2,140
	4,909	4,725	**4,854**	4,665
Included in other expenses are the following charges:				
- property leasing costs	**79**	87	**79**	87
- remuneration of auditors (excl. VAT):				
audit of the Annual Accounts	**39**	50	**38**	49
other services	**20**	6	**20**	6

The amount shown for the audit of the Annual Accounts in 2014 includes £8,000 of costs related to the 2013 audit which was only known and paid for following the publication of the 2013 Report & Accounts. Additional fees paid to the auditors in 2014 in relation to the Century Building Society merger are disclosed in Note 26.

6. STAFF NUMBERS AND COSTS

The average number of persons employed by the Group and Society (including Executive Directors) during the year was as follows:

	Full time		Part time	
	2015	2014	**2015**	2014
Head Office	**28**	26	**7**	4
Branch offices	**23**	21	**9**	12
	51	47	**16**	16

The aggregate costs of employment of these persons were as follows:

	2015	2014
	£000	£000
Wages and salaries	**2,188**	2,091
Social security costs	**204**	212
Pension costs	**245**	222
	2,637	2,525

7. DIRECTORS' REMUNERATION

Group & Society	**2015**	2014
	£000	£000
For services as Non-Executive Directors	**140**	131
For Executive services	**154**	266
Pension contributions	**26**	25
	320	422

The amounts shown above for Executive services in 2014 include the payment made to Mr Kay on his resignation as Chief Executive amounting to £122,000.

Individual Directors' remuneration is detailed in the Directors' Remuneration Report on pages 18 & 19.

8. TAX ON PROFIT ON ORDINARY ACTIVITIES

	Group		Society	
	2015 £000	2014 £000	**2015 £000**	2014 £000
Current tax				
Corporation tax charge for the year at 21.3% (2014: 20%)	**399**	22	**398**	22
Adjustment in respect of prior year	**(3)**	(9)	**(3)**	(9)
Total current tax charge for the year	**396**	13	**395**	13
Deferred tax				
Deferred tax for the year (Note 20)	**24**	34	**24**	34
Total tax charge for the year	**420**	47	**419**	47

It was announced in December 2012 that the main rate of UK corporation tax would reduce from 23% to 21% from 1 April 2014. It was then subsequently announced in March 2013 that the main rate would be subject to a further reduction to 20% from 1 April 2015. Both of these rate reductions were substantively enacted in July 2013. The substantive enactment of these rate reductions has been reflected in the computation of the net deferred tax liability recognised by the Society with account taken of the tax rates that will apply when the various timing differences are expected to reverse.

The tax assessed for the year differs from the statutory rate of corporation tax in the UK of 21.3%; the differences are explained below (in 2014 the taxable profits of the Society fell to be taxed at the small profits rate of 20%):

	Group 2015	Group 2014	Society 2015	Society 2014
Profit on ordinary activities before taxation	**2,327**	1,066	**2,323**	1,064
Profit on ordinary activities multiplied by the statutory rate of corporation tax of 21.3% (2014: 20%)	**496**	213	**495**	213
Effects of:				
Difference between capital allowances and depreciation	**(6)**	(18)	**(6)**	(18)
Expenses not deductible for corporation tax purposes	**2**	52	**2**	52
Net effect of differing tax rates of subsidiary undertaking	**-**	-	**-**	-
Other timing differences	**(14)**	(6)	**(14)**	(6)
Loss relief arising from merger with Century Building Society	**(79)**	(219)	**(79)**	(219)
Adjustment in respect of prior year	**(3)**	(9)	**(3)**	(9)
Total current tax charge for the year	**396**	13	**395**	13

9. LOANS AND ADVANCES TO CREDIT INSTITUTIONS

Group & Society	**2015 £000**	2014 £000
Accrued interest	**25**	88
Repayable on demand	**2,360**	7,753
In not more than three months	**5,000**	12,000
In more than three months but not more than one year	**1,000**	12,000
	8,385	31,841

10. DEBT SECURITIES

Group & Society	2015 £000	2014 £000
Debt Securities		
Issued by other borrowers	**32,666**	33,169
Debt securities have remaining maturities as follows:		
Accrued interest	**165**	122
In not more than one year	**32,501**	29,545
In more than one year	**-**	3,502
	32,666	33,169
Transferable debt securities (excluding accrued interest) comprise:		
Listed	**3,500**	5,008
Unlisted	**29,000**	28,000
Unamortised premia	**2**	39
	32,502	33,047
Market value of listed debt securities	**3,500**	5,044
Movements during the year of debt securities:		
At 1 February 2014	**33,047**	28,515
Acquired on transfer of engagements	**-**	1,574
Additions	**29,027**	33,519
Disposals and maturities	**(29,572)**	(30,561)
As at 31 January 2015	**32,502**	33,047

The Directors of the Society consider that the primary purpose of holding debt securities is prudential. The securities are held as financial fixed assets with the intention of use on a continuing basis in the Society's activities and are therefore classified as financial fixed assets.

11. LOANS AND ADVANCES TO CUSTOMERS

Maturity analysis

The remaining maturity of loans and advances to customers as at the date of the balance sheet is as follows:

	Group		Society	
	2015 £000	2014 £000	**2015 £000**	2014 £000
On call and at short notice	**548**	1,215	**548**	1,215
In not more than three months	**2,626**	2,132	**2,615**	2,120
In more than three months but not more than one year	**7,761**	7,664	**7,727**	7,630
In more than one year but not more than five years	**52,132**	49,432	**51,879**	49,189
In more than five years	**219,417**	215,282	**218,643**	214,453
	282,484	275,725	**281,412**	274,607
Less provisions (Note 12)	**(341)**	(341)	**(341)**	(341)
	282,143	275,384	**281,071**	274,266

12. PROVISIONS FOR BAD AND DOUBTFUL DEBTS

Group & Society	Specific £000	General £000	**Total £000**
Loans fully secured on residential property:			
At 1 February 2014	181	160	**341**
Amounts written off during year	(54)	-	**(54)**
Charge/(credit) to Income and Expenditure Account	106	(52)	**54**
Amounts recovered	-	-	**-**
As at 31 January 2015	**233**	**108**	**341**
At 1 February 2013	280	182	462
Amounts written off during year	(164)	-	(164)
Charge/(credit) to Income and Expenditure Account	65	(22)	43
Amounts recovered	-	-	-
As at 31 January 2014	181	160	341

13. MOVEMENTS IN VALUES OF ACQUIRED ASSETS

Group & Society	**2015 £000**	2014 £000
Further impairment of acquired assets	**56**	145
Increase in value of acquired assets	**(495)**	(145)
	(439)	-

14. INVESTMENT IN SUBSIDIARY UNDERTAKING

The Society has a 100% holding of the ordinary share capital in its sole subsidiary, SBS Mortgages Ltd, a company incorporated in Scotland under the Companies Act. The company's principal activities are mortgage lending and the acquisition of domestic mortgage portfolios from third-party lenders.

The investment by the Society in its subsidiary during the year was as follows:

	Shares £000	Loan £000	**Total £000**
Cost at 1 February 2014	10	(448)	**(438)**
Invested in year	-	55	**55**
Repayments received	-	(105)	**(105)**
Cost at 31 January 2015	**10**	**(498)**	**(488)**

The inter-company creditor balance of £498,000 is shown under Other Liabilities (Note 19).

15. TANGIBLE FIXED ASSETS

Group & Society	Land & Buildings Freehold £000	Land & Buildings Short Leasehold £000	Office Equipment £000	Motor Vehicles £000	Total £000
Cost					
As at 1 February 2014	1,634	178	1,408	160	3,380
Additions	-	-	205	70	275
Disposals	-	-	(179)	(71)	(250)
As at 31 January 2015	1,634	178	1,434	159	3,405
Depreciation					
As at 1 February 2014	283	155	856	86	1,380
Charged in year	34	6	182	34	256
Disposals	-	-	(177)	(61)	(238)
As at 31 January 2015	317	161	861	59	1,398
Net book value					
As at 31 January 2015	**1,317**	**17**	**573**	**100**	**2,007**
As at 31 January 2014	1,351	23	552	74	2,000

The net book value of freehold and leasehold property occupied by the Group and Society for its own activities was as follows:

	2015 £000	2014 £000
As at 31 January	**1,334**	1,374

16. SHARES

Group & Society

	2015 £000	2014 £000
a) Held by individuals	331,074	359,533
Other shares	652	552
	331,726	360,085

b) Repayable from the date of the balance sheet in the ordinary course of business as follows:

	2015 £000	2014 £000
Accrued interest	2,403	3,201
On demand	278,605	278,968
In not more than three months	3,700	27,440
In more than three months but not more than one year	26,479	43,735
In more than one year but not more than five years	20,539	6,741
	331,726	360,085

17. AMOUNTS OWED TO CREDIT INSTITUTIONS

Group & Society

Repayable from the date of the balance sheet in the ordinary course of business as follows:

	2015 £000	2014 £000
Accrued interest	2	-
In not more than three months	2,500	-
In more than three months but not more than one year	-	-
	2,502	-

18. AMOUNTS OWED TO OTHER CUSTOMERS

Group & Society

Repayable from the date of the balance sheet in the ordinary course of business as follows:

	2015 £000	2014 £000
Accrued interest	14	2
Repayable on demand	8,126	6,049
In not more than three months	3,429	893
In more than three months but not more than one year	53	154
	11,622	7,098

19. OTHER LIABILITIES

	Group		Society	
	2015 £000	2014 £000	**2015 £000**	2014 £000
Other liabilities comprise:				
Corporation tax	**5**	-	**4**	-
Income tax	**301**	460	**301**	460
Amounts due to subsidiary (Note 14)	**-**	-	**498**	448
Other creditors	**215**	176	**215**	176
Deferred tax (Note 20)	**77**	53	**77**	53
	598	689	**1,095**	1,137

20. DEFERRED TAX

	2015 £000	2014 £000	**2015 £000**	2014 £000
Provided:				
Timing differences between capital allowances and depreciation	**(99)**	(87)	**(99)**	(87)
General mortgage loss provision	**22**	34	**22**	34
	(77)	(53)	**(77)**	(53)
As at 1 February 2014	**(53)**	(19)	**(53)**	(19)
Deferred tax (charge) for the financial year (Note 8)	**(24)**	(34)	**(24)**	(34)
As at 31 January 2015	**(77)**	(53)	**(77)**	(53)

A deferred tax asset amounting to £147,000 in relation to tax losses incurred by Century Building Society (CBS) as at 31 January 2013 (date of transfer of engagements) has not been recognised due to uncertainty that there will be future notional taxable profits in CBS available for offset.

21. PROVISIONS FOR LIABILITIES

Financial Services Compensation Scheme

Group & Society	2015 £000	2014 £000
As at 1 February 2014	425	382
Acquired on transfer of engagements	-	29
Paid in year	(244)	(244)
Charge to Income and Expenditure Account:		
Increase in Provision	201	258
As at 31 January 2015	382	425

Financial Services Compensation Scheme

Based on its share of protected deposits, the Society, in common with all regulated UK deposit takers, pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. The FSCS levy consists of two parts – a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes using the rights that have been assigned to it.

In September 2008 a claim was triggered against the FSCS by the transfer of Bradford & Bingley plc's retail deposit business to Abbey National plc. In October 2008 a further claim was triggered against the FSCS by the transfer of Kaupthing Singer and Friedlander's (KSF) internet deposit business (Kaupthing Edge) and Heritable Bank's (a subsidiary of Landsbanki hf) deposit business to ING Direct. The FSCS will also be liable to claims from depositors of Landsbanki hf and KSF whose balances have not been transferred to ING Direct but are covered by the FSCS. Additional claims arose relating to the default of London Scottish Bank plc in 2008 and Dunfermline Building Society in 2009.

We understand that the FSCS has met, or will meet, the claims by way of loans received from HM Treasury. The FSCS has, in turn, acquired the rights to the realisation of the assets of these banks. The FSCS is liable to pay interest on the loans from the Bank of England. The term of these loans was interest-only for the first three years, with the FSCS recovering the interest cost, together with its own management expenses, through annual levies on its members. The initial three-year term expired in September 2011, and under the re-negotiated terms, the interest rate was re-set from 12-month Libor + 30bps to 12-month Libor + 100bps.

As a result of notifications it has received from the Financial Conduct Authority, the Society has recognised in this year's results a provision for a levy of £122,000 for the scheme year 2014/2015, and a levy of £130,000 for the scheme year 2015/2016, which are calculated with reference to the protected deposits it held at 31 December 2013 and 31 December 2014, respectively.

With effect from 2013/14, the FSCS started to repay the principal of the Treasury loans and to the extent that there is a shortfall from realisations of the assets of the banks, there will be a further levy in this respect. This is being levied on deposit-takers in three annual instalments. In addition, HM Treasury has requested interim payments in respect of the FSCS liability with regard to the default of Dunfermline Building Society. Accordingly, the Society has also recognised in this year's results a levy of £101,000 for the year 2015/16.

At the date of signing these Accounts there remains uncertainty over the amounts provided. The amounts above do not take account of any compensation levies which may arise from any ultimate payout on claims.

22. GENERAL RESERVES

	Group £000	Society £000
As at 1 February 2014	28,289	26,733
Profit for the year	1,907	1,904
As at 31 January 2015	**30,196**	**28,637**

23. GUARANTEES AND OTHER FINANCIAL COMMITMENTS

a) The Society has a contingent liability in respect of further contributions to the Financial Services Compensation Scheme provided under the Financial Services and Markets Act 2000, in addition to the specific liability detailed in Note 21.

b) Section 22 of the Building Societies Act 1986 was repealed with effect from 11 June 1996 and the Society therefore has no obligation to stand by its subsidiary in respect of liabilities incurred after this date. However it is the intention of the Board to continue to support fully its subsidiary undertaking.

c) At 31 January 2015, annual commitments under operating leases for land and buildings were:

Group & Society	**2015 £000**	2014 £000
Expiring within one year	**-**	31
Expiring between two and five years	**23**	23
Expiring after five years	**56**	25
	79	79

23. GUARANTEES AND OTHER FINANCIAL COMMITMENTS (continued)

d) **Off-Balance Sheet Hedging Instruments**

The Group's core business is to provide its members with financial products appropriate to their needs. The Group uses wholesale financial instruments to invest in liquid assets and to raise funds from wholesale money markets in support of its retail savings operations. These instruments also allow it to manage the financial risks arising from these business activities.

The Group has a well-established formal structure for managing financial risks which includes formal risk policies, risk limits, reporting structures, mandates and control procedures. This structure begins with the Board of Directors and its Assets & Liabilities Committee.

Financial instruments used by the Group for risk management purposes include off-balance sheet derivative instruments. In accordance with the Building Societies Act 1986 such instruments are only used to limit the extent to which the Group will be affected by changes in interest rates.

As part of its responsibilities, the Board approves the use of specified off-balance sheet instruments within approved limits and business activities. The Group does not undertake transactions for trading or speculative purposes and consequently all off-balance sheet financial instruments are classified as hedging contracts.

The Board approves the use of interest rate swaps as off-balance sheet instruments in order to manage the Group's balance sheet risk exposures. These instruments are used to protect the Group from exposures arising principally from fixed-rate mortgage lending, and they could also be used against exposures arising from fixed-rate savings products and deposit funding if the need arose. The duration of the off-balance sheet contracts is generally short to medium term and their maturity profile reflects the nature of exposures arising from underlying business activities.

The notional principal of these instruments reflects the extent of the Group's involvement in the instruments, but does not represent its exposure to credit risk which is assessed by reference to the fair value.

Outstanding Derivative Contracts: The table below shows the notional principal amounts, credit risk weighted amounts and replacement costs of derivatives. Notional principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The credit risk weighted amount is calculated according to rules specified by the Prudential Regulation Authority, and is based on the replacement cost, but also takes into account measures of the extent of potential future exposure and the nature of the counterparty. The replacement cost represents the cost of replacing contracts with a positive value, calculated at market rates current at the balance sheet date, and reflects the Group's maximum exposure should all counterparties default.

Group & Society	**2015 £000**	2014 £000
Unmatured interest rate swaps		
Notional principal amount	**53,000**	61,000
Credit risk weighted amount	**108**	89
Replacement cost	**-**	135

e) **Risk Management**

The main financial risks arising from the Group's activities are credit risk, liquidity risk and interest rate risk. The Board reviews and agrees policies for managing each of these risks, and these are summarised below:

Credit Risk - All loan applications are assessed with reference to the Group's lending policy. Changes to policy are recommended by the Retail Credit Committee and approved by the Board and loan applications are approved in accordance with delegated lending authorities. The Assets & Liabilities Committee is responsible for approving treasury counterparties.

23. GUARANTEES AND OTHER FINANCIAL COMMITMENTS (continued)

Liquidity Risk - The Group's policy is to maintain sufficient funds in a liquid form at all times to ensure that the Group can meet its liabilities as they fall due. The objective of liquidity is to help smooth mismatches between maturing assets and liabilities and to provide a degree of protection against any unexpected developments that might arise.

Interest Rate Risk - The Group is exposed to movements in interest rates reflecting the mismatch between the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rates or, if earlier, the dates on which the instruments mature. The Group manages this exposure continually by using both on-balance sheet and off-balance sheet instruments.

f) **Interest Rate Risk Exposure**

The table below summarises these re-pricing mismatches as at 31 January 2015. Items are allocated to time bands by reference to the earlier of the next interest rate re-pricing date and the maturity date.

Group	Three Months or Less £000	More than Three Months less than Six Months £000	More than Six Months less than One Year £000	More than One Year less than Five Years £000	More Than Five Years £000	Non-interest Bearing £000	Total £000
Assets							
Liquid Assets	72,971	10,000	10,000	-	-	225	93,196
Loans and Advances to Customers	212,605	7,519	5,406	56,613	-	-	282,143
Tangible Fixed Assets	-	-	-	-	-	2,007	2,007
Other Assets	-	-	-	-	-	28	28
Prepayment and Accrued Income	-	-	-	-	-	223	223
Total Assets	285,576	17,519	15,406	56,613	-	2,483	377,597
Liabilities							
Shares	282,305	10,755	15,724	20,539	-	2,403	331,726
Amounts Owed to Credit Institutions	2,500	-	-	-	-	2	2,502
Amounts Owed to Other Customers	11,555	53	-	-	-	14	11,622
Other Liabilities	-	-	-	-	-	598	598
Accruals and Deferred Income	-	-	-	-	-	571	571
Provision for Liabilities	-	-	-	-	-	382	382
Reserves	-	-	-	-	-	30,196	30,196
Total Liabilities	296,360	10,808	15,724	20,539	-	34,166	377,597
Off-Balance Sheet Items (see Note)	48,000	(5,000)	-	(43,000)	-	-	-
Interest Rate Sensitivity Gap	37,216	1,711	(318)	(6,926)	-	(31,683)	-
Cumulative Gap	37,216	38,927	38,609	31,683	31,683	-	

Note:

Off-balance sheet items represents the notional amount on the interest rate swaps entered into by the Society in order to hedge the interest rate risk in fixed-rate mortgages. The maturity dates shown indicate the periods in which the individual contracts expire.

23. GUARANTEES AND OTHER FINANCIAL COMMITMENTS (continued)

g) **Interest Rate Risk Exposure (continued)**

The comparatives as at 31 January 2014 were as follows:

Group	Three Months or Less £000	More than Three Months less than Six Months £000	More than Six Months less than One Year £000	More than One Year less than Five Years £000	More Than Five Years £000	Non-interest Bearing £000	Total £000
Assets							
Liquid Assets	87,021	1,005	30,101	-	-	1,036	119,163
Loans and Advances to Customers	215,690	11,744	8,015	39,935	-	-	275,384
Tangible Fixed Assets	-	-	-	-	-	2,000	2,000
Other Assets	-	-	-	-	-	273	273
Prepayment and Accrued Income	-	-	-	-	-	412	412
Total Assets	302,711	12,749	38,116	39,935	-	3,721	397,232
Liabilities							
Shares	306,408	20,079	23,656	6,741	-	3,201	360,085
Amounts Owed to Credit Institutions	-	-	-	-	-	-	-
Amounts Owed to Other Customers	6,942	154	-	-	-	2	7,098
Other Liabilities	-	-	-	-	-	689	689
Accruals and Deferred Income	-	-	-	-	-	646	646
Provision for Liabilities	-	-	-	-	-	425	425
Reserves	-	-	-	-	-	28,289	28,289
Total Liabilities	313,350	20,233	23,656	6,741	-	33,252	397,232
Off-Balance Sheet Items (see Note)	41,500	(9,500)	(7,000)	(25,000)	-	-	-
Interest Rate Sensitivity Gap	30,861	(16,984)	7,460	8,194	-	(29,531)	-
Cumulative Gap	30,861	13,877	21,337	29,531	29,531	-	

Note:

Off-balance sheet items represents the notional amount on the interest rate swaps entered into by the Society in order to hedge the interest rate risk in fixed-rate mortgages. The maturity dates shown indicate the periods in which the individual contracts expire.

23. GUARANTEES AND OTHER FINANCIAL COMMITMENTS (continued)

h) **Fair Values of Financial Assets and Financial Liabilities**
Set out below is a comparison of carrying values and fair values of some of the Group's financial assets and financial liabilities as at 31 January 2015. The Group does not undertake transactions for trading or speculative purposes. The table excludes certain financial assets and financial liabilities which are not listed or publicly traded, or for which a liquid and active market does not exist. It therefore excludes items such as mortgages, share accounts and deposits with credit institutions.

Financial Assets (Liabilities) for which active financial markets exist:

	Book value £000	Fair value £000	Unrecognised (Loss)/Gain £000
On-Balance sheet instruments			
Debt securities:			
At 31 January 2015	**32,666**	**32,675**	**9**
At 31 January 2014	33,169	33,155	(14)
Off-Balance sheet instruments			
Interest rate swaps:			
At 31 January 2015	**(50)**	**(579)**	**(579)**
At 31 January 2014	59	(142)	(142)

Market values have been used to determine the fair value of interest rate swaps held. Unrealised gains and losses on instruments used for hedging are not booked, as these hedges are accounted for on an accruals basis in line with the underlying instruments being hedged.

Hedges: Hedges which comprise interest rate swaps referred to above are used to reduce the risk of loss arising from changes in interest rates. Gains and losses on instruments used for hedging are recognised in line with the item being hedged and are only recognised in the event of the underlying exposure itself being unwound. The following table sets out the movements in unrecognised and recognised gains and losses in the year to 31 January 2015.

Group	2015 Gains £000	2015 Losses £000	2015 Net Gains/(Losses) £000
Gains and losses unrecognised at the start of the financial year	135	(277)	(142)
Items unrecognised at the start of the year recognised in the year	(135)	144	9
Items unrecognised at the start of the year and unrecognised in the year	-	(133)	(133)
Gains and losses arising in the year unrecognised in the year	-	(446)	(446)
Unrecognised at the end of the financial year	-	(579)	(579)
Of which:			
Expected to be realised in the year to 31 January 2016	-	(23)	(23)
Expected to be realised after 31 January 2016	-	(556)	(556)
Unrecognised at the end of the financial year	-	(579)	(579)

24. DIRECTORS' LOANS AND TRANSACTIONS

The aggregate amount outstanding at 31 January 2015 in respect of loans, transactions and arrangements made by the Society to Directors or persons connected with a Director was £150,747 and comprised one loan to one Director (2014: £243,382 comprising three loans to two Directors) at normal commercial rates.

A Register of loans and transactions subsisting between the Society and its Directors (and connected persons) is maintained. This Register is available for inspection by any member of the Society at the Society's Head Office for a period of fifteen days prior to the Annual General Meeting and at the Annual General Meeting.

25. COUNTRY BY COUNTRY REPORTING

Scottish Building Society and its Subsidiary are both UK-registered entities, with 100% of their activities within the UK.

The Society's total operating income, profit before tax, tax on profit, public subsidies received and the number of full time equivalent employees during the year to 31 January 2015 were:

Group & Society	**2015 £000**	2014 £000
Total operating income	**7,406**	6,616
Profit before tax	**2,327**	1,066
Tax on profit	**420**	47
Public subsidies received	**Nil**	Nil
Number of employees on FTE basis	**61**	57

26. TRANSFER OF ENGAGEMENTS

On 1 February 2013, the Society merged with Century Building Society (CBS). The assets and liabilities acquired, together with fair value adjustments, are set out below. The adjustments relate to the revaluation of tangible fixed assets and loans and advances to customers.

Group & Society	CBS Cessation Accounts £000	Adjustments £000	CBS Take-On Balances £000
Assets			
Liquid assets	5,171	-	5,171
Loans and advances to customers	17,001	(1,080)	15,921
Fixed and other assets	135	547	682
Total Assets	22,307	(533)	21,774
Liabilities			
Shares	20,972	-	20,972
Other liabilities	68	-	68
Reserves	1,267	(533)	734
Total Liabilities	22,307	(533)	21,774

Included within merger costs for 2013/14 is £40,000 (excluding VAT) in relation to assurance services provided by KPMG Audit Plc.

SCOTTISH BUILDING SOCIETY

1. STATUTORY PERCENTAGES

		%	Statutory Limit %
a)	Lending limit	**5.98**	**25.0**
b)	Funding limit	**4.27**	**50.0**

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986. The Lending limit measures the proportion of business assets not in the form of loans fully secured on residential property and the Funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals.

The statutory limits are prescribed in building society legislation and ensure that the principal purpose of a building society is that of making loans which are secured on residential property and are funded substantially by its members.

2. OTHER PERCENTAGES

	2015 %	2014 %
As a percentage of shares and borrowings:		
a) Gross capital	**8.73**	7.70
b) Free capital	**8.18**	7.20
c) Liquid assets	**26.95**	32.45
Profit after tax as a percentage of mean total assets	**0.49**	0.26
Profit after tax (excluding movement in acquired assets, FSCS levy and merger costs after tax) as a percentage of mean total assets	**0.42**	0.32
Management expenses as a percentage of mean total assets	**1.33**	1.27

Explanation of terms

All of the above percentages are based on Group figures.

Shares and borrowings represents the total of shares, amounts owed to credit institutions and amounts owed to other customers (all including accrued interest).

Gross capital is the general reserves as shown in the balance sheet.

Free capital represents gross capital and general mortgage loss provision less fixed assets.

Mean total assets represents the average of total assets shown in the relevant balance sheets. These amounted to £392,514 for 2014, decreasing to £387,414 for 2015.

Management expenses represents the aggregate of administrative expenses and depreciation.

3. DIRECTORS AND OTHER OFFICERS AS AT 31 JANUARY 2015

Directors

Name and Business Occupation	Date of Birth	Date of Appointment	Other Directorships
Raymond J Abbott Company Director	02.03.59	01.06.13	SBS Mortgages Ltd Foresight 3 VCT PLC Galleria Holdings Ltd Essex Group Holdings Ltd Essex Services Group PLC
Robert Golbourn Banker	08.06.45	25.10.06	None
Alexa H Henderson Chartered Accountant	16.02.61	28.03.01	SBS Mortgages Ltd Adam & Company Group PLC Adam & Company PLC Adam & Company Investment Management Ltd James Walker (Leith) Ltd Dunedin Smaller Companies Investment Trust PLC
John C Ogston Chartered Banker	28.04.57	01.07.13	Vehicle Professionals Ltd
Simon M Pashby Chartered Accountant	16.04.58	15.10.14	Medical Protection Society Ltd MPI (London) Ltd
David Peebles Company Director	14.02.62	25.10.06	XM International Associates Ltd
Mark L Thomson Building Society Chief Executive	22.04.66	12.10.12	SBS Mortgages Ltd

Documents may be served on any of the above-named Directors c/o KPMG LLP at the following address: Saltire Court, 20 Castle Terrace, Edinburgh EH1 2EG

Executive Directors' Service Contracts

Mr Thomson has a rolling service contract with the Society dated 2 April 2012 which can be terminated by either party giving six months' notice.

Officers

Name	Business Occupation	Other Directorships
Andrew J W Tristram	Secretary & Head of Compliance	None
Graeme L Chandler	Head of Finance	None
Andrew Moses	Head of Operations & Lending	None
John H Lloyd	Head of Sales & Marketing	None
Alison I Quilter	Head of IT	None
Emily Dixon	Head of Human Resources	None
Alan Searl	Head of Projects	None

Head Office: SBS House, 193 Dalry Road, Edinburgh EH11 2EF.

SCOTTISH BUILDING SOCIETY