ARBUTHNOT BANKING GROUP PLC

28 March 2018

For immediate release

ARBUTHNOT BANKING GROUP (“Arbuthnot”, “the Group” or “ABG”)
Audited Final Results for the year to 31 December 2017

Increased profitability as capital successfully deployed

Arbuthnot Banking Group today announces an increase in underlying profit of 91%.

Arbuthnot Banking Group PLC is the holding company for Arbuthnot Latham & Co., Limited and has an 18.6% shareholding in Secure Trust Bank PLC.

FINANCIAL HIGHLIGHTS

- Profit Before Tax £7.0m (2016: £0.2m)*
- Underlying profit before tax £7.7m (2016: £4.0m)
- Operating income increased by 32% to £54.6m (2016: £41.5m)
- Earnings per share 43.9p (2016: (3.7p))*
- Final dividend per share 19p (2016: 18p), an increase of 6%
- Total full year dividend per share 33p (2016: 31p)**
- Underlying net assets £236m (2016: £234m)
- Net assets per share 1547p (2016: 1534p)
- Underlying return on deployed equity 10.0% (2016: 9.6%)

OPERATIONAL HIGHLIGHTS

Arbuthnot Latham

- Profit before tax £11.0m (2016: £9.1m) an increase of 21%
- Average net margin at 4.8% (2016: 4.8%)
- Customer loans exceeded £1bn increasing 38% to £1,049m (2016: £759m)
- Written loan volume increased 105% to £466m (2016: £227m)
- Customer deposits exceeded £1bn increasing 39% to £1,391m (2016: £998m)
- Assets under management exceeded £1bn increasing 13% to £1,044m (2016: £920m)
- Completed acquisition of Renaissance Asset Finance Limited on 28 April 2017
- Installed Oracle Flexcube operating system at a total investment of £8m

Secure Trust Bank – Associated Undertaking

- Shareholding maintained at 18.6%
- Treated as an associated undertaking due to significant influence via three board members
- Reported £4.4m of profit from associate (2016: £2.1m)

Commenting on the results, Sir Henry Angest, Chairman and Chief Executive of Arbuthnot, said: “The Group had a good year, with profits increasing substantially, supported by the deployment of capital into the business. Arbuthnot Latham reached a creditable milestone of surpassing £1bn in its key business metrics: Customer Loans, Customer Deposits and Assets under Management. With a new banking system successfully installed, strong capital and a good liquidity surplus, the Group is well set for further growth.”

Note: * The prior year profit and EPS excludes profit from discontinued operations of £228m.
** The total dividend for 2016 excludes special dividend payments of 325p.

ENQUIRIES:

Arbuthnot Banking Group	
Sir Henry Angest, Chairman and Chief Executive	0207 012 2400
Andrew Salmon, Chief Operating Officer	
James Cobb, Group Finance Director	
Stifel Nicolaus Europe Ltd trading as KBW (Nomad and Joint Broker)	0207 710 7600
Robin Mann	
Gareth Hunt	
Stewart Wallace	
Numis Securities Ltd (Joint Broker)	
Chris Wilkinson	0207 260 1000
Stephen Westgate	
Maitland (Financial PR)	
Neil Bennett	
Jais Mehaji	
Sam Cartwright	0207 379 5151

The 2017 Annual Report and Notice of Meeting will be posted and available on the Arbuthnot Banking Group website http://www.arbuthnotgroup.com on or before 13 April 2018. Copies may be obtained from the Company Secretary, Arbuthnot Banking Group PLC, Arbuthnot House, 7 Wilson Street, London, EC2M 2SN.

Consolidated statement of comprehensive income

	Note	Year ended 31 December 2017 £000	2016 £000
Interest income	8	47,427	38,071
Interest expense		(6,334)	(7,626)
Net interest income		**41,093**	**30,445**
Fee and commission income	9	13,805	11,430
Fee and commission expense		(282)	(425)
Net fee and commission income		**13,523**	**11,005**
Operating income		**54,616**	**41,450**
Net impairment loss on financial assets	10	(394)	(474)
Profit from associates	27	4,437	2,145
Other income	11	3,033	3,169
Operating expenses	12	(54,721)	(46,111)
Profit before tax from continuing operations		**6,971**	**179**
Income tax expense	13	(448)	(720)
Profit / (loss) after tax from continuing operations		6,523	(541)
Profit from discontinued operations after tax	14	-	228,110
Profit for the year		**6,523**	**227,569**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Available-for-sale reserve		128	(2,377)
Available-for-sale reserve - Associate		389	(389)
Tax on other comprehensive income		(104)	456
Other comprehensive income for the period, net of tax		**413**	**(2,310)**
Total comprehensive income for the period		**6,936**	**225,259**
Profit attributable to:			
Equity holders of the Company		6,523	166,143
Non-controlling interests		-	61,426
Profit for the year		**6,523**	**227,569**
Total comprehensive income attributable to:			
Equity holders of the Company		6,936	164,320
Non-controlling interests		-	60,939
Total comprehensive income for the period		**6,936**	**225,259**
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in pence per share):			
Basic earnings per share - Continuing operations	16	43.9	(3.7)
Basic earnings per share - Discontinued operations	16	-	1,130.9
Basic earnings per share	16	**43.9**	**1,127.2**
Diluted earnings per share - Continuing operations	16	43.9	(3.7)
Diluted earnings per share - Discontinued operations	16	-	1,130.4
Diluted earnings per share	16	**43.9**	**1,126.7**

Consolidated statement of financial position

	Note	At 31 December 2017 £000	2016 £000
ASSETS			
Cash and balances at central banks	17	313,101	195,752
Loans and advances to banks	18	70,679	36,951
Debt securities held-to-maturity	19	227,019	107,300
Assets classified as held for sale	20	2,915	-
Derivative financial instruments	21	2,551	1,516
Loans and advances to customers	22	1,049,269	758,799
Other assets	24	20,624	11,939
Financial investments	25	2,347	2,145
Deferred tax asset	26	1,527	1,665
Interests in associates	27	83,804	82,574
Intangible assets	28	15,995	8,522
Property, plant and equipment	30	3,962	4,782
Investment property	31	59,439	53,339
Total assets		**1,853,232**	**1,265,284**
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	37	153	153
Retained earnings	38	237,171	235,567
Other reserves	38	(949)	(1,362)
Total equity		**236,375**	**234,358**
LIABILITIES			
Deposits from banks	32	195,097	3,200
Derivative financial instruments	21	931	227
Deposits from customers	33	1,390,781	997,649
Current tax liability		705	147
Other liabilities	34	16,239	17,082
Debt securities in issue	35	13,104	12,621
Total liabilities		**1,616,857**	**1,030,926**
Total equity and liabilities		**1,853,232**	**1,265,284**

Chairman's statement

I am pleased to report that Arbuthnot Banking Group ("ABG" or the "Group") has achieved a profit before tax for 2017 of £7.0m (2016: £0.2m), which reflects the financial result of the deployment of part of our surplus capital into expanding the businesses of our principal banking subsidiary Arbuthnot Latham & Co., Ltd ("AL" or the "Bank").

Overview

It has been a notable year for many reasons, not just that of the financial results. During the year AL reached the creditable milestone of surpassing £1bn in three of its key business metrics: Customer Loans, Customer Deposits and Assets under Management. This was achieved while undertaking a significant IT infrastructure project that touched all parts of the Bank.

Over the May Bank Holiday weekend, the Bank installed its new banking platform Flexcube, supplied by Oracle, as part of an investment programme worth in excess of £8m. The weekend was a culmination of two years of careful planning and preparation by a significant number of our employees. Over the weekend 120 employees, approximately one third of the Group, gave up their time to achieve a successful transition.

As I mentioned in last year's statement our intention, after having sold a significant stake in Secure Trust Bank, is to develop and diversify the business lines within AL. During 2017 we took two significant steps with this aim in mind. Firstly, we completed the acquisition of Renaissance Asset Finance Limited ("RAF") in April. This business has been successfully integrated into the Group and has returned to growth after being constrained by the limited access to funding it suffered as an independent entity. AL has meanwhile benefited from gaining RAF's expertise in the asset finance markets, by being able to refer a number of lending deals that previously we might not have been able to complete.

Secondly, our development of the Commercial Banking business continues at a robust pace. We hired a number of new bankers and expanded into new business areas and regions during the year. This business closed the year with over £300m of customer loans, a significant achievement given the fact it was only launched in early 2016.

We plan to continue our diversification in 2018 as we work with the team that we have hired to establish Asset Based Lending and others with whom we are currently developing plans. These are new start-up ventures that in time should make strong contributions to the Group, but will require a degree of initial investment. I also look forward to our Commercial Property Fund becoming established during 2018.

I initially thought when the financial crisis weakened the larger banks, the major benefit to us would be that the smaller banks would be able to compete more equally in their chosen specialist markets. I hope this may still come to pass, but it has become much clearer to me that the real benefit of the weakening of the larger banks has been our ability to attract talented employees to develop further the success of our Group. We have made a number of key hires during the year and they are helping to enhance our business and make the operational structures more resilient and provide a sound foundation for expansion.

Regulation

Previously I have commented on how unfair I believe both the regulatory and taxation systems can be when they introduce retrospective changes. During 2017 we saw a prime example of this when the Bank of England announced the introduction of a 1% Countercyclical Capital Buffer, to be effective in 2018. This is applicable to the back book of lending as well as new business to be written. How can banks plan over the long term when their capital requirements can be increased by nearly 10% without warning? Keeping significant surplus capital for such moments is inefficient for both the banks and the economy. This buffer on top of the Capital Conservation Buffer, which will be fully phased in within a year from now, has increased the capital requirement by up to 35% for loans that may have been originated prior to these requirements. This can result in inefficient pricing decisions and below target returns on equity. Surely it would make more sense to apply these new capital requirements only to new written business, so that banks can decide if they want to continue to lend? In this way they can make fully informed decisions based on the capital requirements that will be applicable to a loan, rather than trying to anticipate how regulation will evolve over its lifespan.

I am also concerned about the unintended consequences of regulatory change. The Countercyclical Capital Buffer was reportedly introduced by the Bank of England with the intention of dampening a perceived bubble that may have been developing in the unsecured credit markets, in particular those related to credit card loans. If this was the case, would it not have made sense to apply the buffer to those institutions that actually carry out unsecured lending? Instead, the buffer has been imposed on all banks and all types of lending, which is a very blunt instrument to correct a very specific threat. This will result in all credit markets being constrained and ultimately putting a strain on the whole economy.

As banks see their returns on equity falling, due to these higher capital levels, their inclination will be either to charge customers more or to move up the risk curve to maintain their target returns. This may over time increase the risks within the banking sector rather than reduce them, entirely contrary to the primary objective of the Bank of England.

The fact that banks shape their business models around the regulatory rules should be no surprise to both the regulators and the Government. Thus, you would expect that both of these bodies would ensure that the rules are complementary to Government policy. However, there seems to have been a significant breakdown in this co-ordination regarding the current housing policy. The regulators have increased the capital requirements for development funding by at least 50%, so at the time the Government is calling for more houses to be built, the banks are withdrawing their lending for property developers. I believe that the Government and regulators should revisit these rules to ensure the best outcome for the economy overall.

In the final quarter of the year, the Basel Committee published its revised Basel III capital rules; in particular, the changes to the standardised credit risk methodology. From the outset the Regulators had stated that their objective in these revised rules was not to increase total capital within the banking system, but to redistribute it toward credit risks that they felt had been underestimated in the prior model.

It will come as no surprise, given our long stated conservative view on risk taking and our business model, that the revised rules will overall be beneficial to our business. However, I am disappointed by the fact that these rules will not be effective until 2022. Once again, I fear that intense lobbying from the big banks has favoured them to the detriment of the smaller specialist banks.

Board Changes and Personnel

Once again I would like to thank my colleagues on the Board for their continued support and the dedication they have shown to the Group.

The performance of the Group also reflects the hard work and commitment of the members of staff. On behalf of the Board I extend our thanks to all of them for their dedicated efforts in 2017.

Dividend

The Board is proposing a final dividend of 19p, an increase of 1p on last year. Together with the interim dividend of 14p it gives a total dividend of 33p (2016: 356p, including special dividends of 325p), which represents an increase of 2p on the ordinary dividend.

If approved, the dividend will be paid on 18 May 2018 to shareholders on the register at close of business on 27 April 2018.

Outlook

During 2017 and early 2018 the stock markets reached record levels as the global economy continued its recovery, underpinned by loose fiscal policies and the introduction of business-friendly tax regimes, in particular in the US. However, more recently those markets have seen more volatility and corrections to values.

We take note of this macro-economic environment, but remain focused on developing our current and new businesses within the Group. This will bring greater diversity to the earnings of Arbuthnot and should provide greater balance and stability to the Group for the future, which looks promising.

By the time you receive my next Chairman's report we will be on the verge of Britain's official exit from the EU. This I believe should not be the major worry for Britain's business community or economy and indeed should present an opportunity. The greater risk must be that of a hard left Labour government. This could have a significant impact on our clients and business. Such a threat is something that we all, and in particular businesses and entrepreneurs, must take very seriously.

Strategic Report

Business Review

Arbuthnot Latham & Co., Ltd

	2017	2016
Operating income	£54.9m	£41.8m
Other income	£3.9m	£4.4m
Operating expenses	£47.4m	£36.6m
Profit before tax	£11.0m	£9.1m
Customer loans	£1,049.3m	£758.8m
Customer deposits	£1,390.8m	£997.6m
Total assets	£1,783.7m	£1,199.2m
Assets under management	£1,044.3m	£919.8m
Average net margin	4.8%	4.8%
Loan to deposit ratio	75.4%	76.0%

Arbuthnot Latham and Co., Limited has reported a profit before tax of £11m (2016: £9.1m), which is an increase of 21%. However, the increase in underlying profit is 48%, if the one off gain of £1.6m from the sale of Visa Europe shares in 2016 is removed.

Overall, the increased financial performance of the Bank is an indicator of the growth of the three key business metrics: Customer Loans, Customer Deposits and Assets under Management. Significantly, as well as achieving good growth in annual profits, the Bank achieved a major milestone during the year, with each of the key metrics increasing beyond the £1bn level. Customer Loans and Deposits increased by 38% and 39% respectively and Asset under Management grew by 13%.

A contributing factor to the strong financial performance of the Bank was the completion of the acquisition of RAF. This niche asset finance lending business specialises in financing high value cars and other business assets. Prior to the acquisition it had been an independent business, but was wholly reliant on its funding from a single banking line. The growth ability of the business was therefore constrained, and indeed in the period of time between the announcement of our intention to acquire the operation and the final completion in April, the lending balances declined as the original banking line was gradually withdrawn.

At the time of acquisition the customer loan balances were £58m. Once the company became part of the Group, this growth constraint was removed and it was able to return to the market with new vigour and was quickly able to re-energise its relationship with brokers and business introducers, thus returning to a growth trajectory and closed the year with loan balances of £71m.

During its eight full months of ownership it directly contributed £1.6m and a further £0.8m to the Group via the funding benefit achieved by the new banking facilities.

The business saw no significant change in impairments during the year, with losses running at 20bps.

To support the future growth plans of RAF and the resultant increase in activities, the business will be moving to new premises in Basildon toward the end of the first quarter of 2018.

Private Banking

The Private Bank increased loan origination by 22% to a record of £201m. However, this was not sufficient to offset repayment of loans. Overall the loan portfolio closed the year at £578m (2016: £607m). However, more than half of this reduction is due to the natural amortisation of the acquired loan portfolios, namely those from Duncan Lawrie and the Dunfermline Building Society. These portfolios continue to perform ahead of our expected cash flow forecasts, but still contributed £16m of the reduction in overall balances. The remaining core private banking book reduced by 3%. We expect that the portfolio will return to growth in 2018, with more emphasis on finding niche bespoke lending deals rather than vanilla lending, which has become an increasingly competitive area in recent years.

The credit performance of the book remained well within our expected risk tolerance levels with impairments remaining steady during the year at £0.4m (2016: £0.4m). This reflects our conservative lending policies, which focus on not only the standing of the borrower but also the quality of the collateral that we take as security. Our experience to date in managing problem debt positions is that in almost all cases we recover our lending and expect that this will remain the case for the foreseeable future.

The Private Bank continued to see a good flow of new client introductions and was able to increase customer deposit balances by 14% to £1,082m (2016: £946m).

Many of the new clients transferred their balances into the Wealth Management division of the Private Bank. The Investment Management team saw assets under management increase by a net 13% reaching £1,044m (2016: £920m). The gross client inflow of funds was £166m, which offset natural withdrawals of £135m and the remaining balance is accountable to market increases in clients funds under management.

Finally, the Private Bank was the most impacted by the replacement of our banking platform with a new Oracle sourced product, Flexcube. A significant number of employees showed true dedication and commitment to ensure that this project ran as smoothly as could be expected. The Bank now has the modern infrastructure it needs on which to build for the future.

Commercial Bank

The Commercial Bank has traded robustly during 2017. Customer loan balances increased by over 300% to close the year at £305m (2016: £76m), as the investment in new bankers resulted in good quality commercial lending opportunities. The commercial banking proposition of quality service and relationship banking has also proved successful in being able to attract deposits, with the deposit book growing by more than 500% to close the year at £308m (2016: £51m).

Now that the business has an established loan portfolio and with it the resultant positive revenue stream, which supports our central overheads, the Commercial Bank will focus on generating higher returns on the capital employed to ensure that this area of growth continues to add to the Group's targeted return on equity.

Dubai (included in Private Banking above)

The office in Dubai continued to perform well, contributing £1.8m to the Group's profit. The customer loan balances closed at £94m (2016: £74m), deposits were £94m (2016: £64m) and AUMs were £95m (2016: £78m). With a growing confidence that our business can trade in the region, the office is expanding both with larger premises and additional private bankers being recruited. The expansion will double the footprint of the office located in the Dubai Financial Centre. With EXPO 2020 on the horizon, the business is well placed to build and develop the proposition in the UAE and wider region.

Funding

Early in 2018, access to further capacity from the Bank of England for liquidity schemes (Funding for Lending Scheme and Term Funding Scheme) was closed. This will leave banks four more years before funding benefits provided by the schemes fully unwind.

The Bank has participated in these schemes but only to modest levels. The Bank remains highly liquid with a loan to deposit ratio of 75%. Importantly, it has also managed to develop a good mix of customer deposits with call, notice and term balances. This should give the Bank an advantage over time as interest rates rise. We anticipate that margins should see a benefit, with our surplus liquidity balances becoming more valuable and providing greater strength to the Bank than relying on "best buy" tables for deposit gathering.

Business Development

During 2018 the Bank plans to continue to diversify its income sources by developing further businesses.

The first of these is the creation of an Asset Based Lending (“ABL”) business. The core team of seven to establish this have been hired and are based in offices near Gatwick. The Managing Director, Tim Hawkins, has a long and respected track record in this business area and was most recently the head of ABL at Shawbrook. This business expects to write its first customer loans in late Q2 2018.

We also have plans to launch a Commercial Property Investment Fund for professional investors and to establish other new lending businesses that have a synergy with our current business and help diversify our revenue streams.

A key strength of AL is its ability to raise deposits at attractive margins. The Private Bank has over the years built a significant deposit base and recently this has grown well. Since commencing the Commercial Banking business, the Bank has also created a good SME deposit base. To supplement this, the Bank is now developing a direct to market retail deposit offering. The proposition will further diversify the Bank’s sources of funding, with the ability to raise fixed term deposits from the best buy and aggregator platforms. “Arbuthnot Direct” is expected to soft launch in the middle of the year and be available to depositors in the third quarter. It is planned only to raise a modest amount of funding from this platform, but it is being put in place, principally, so that if a compelling acquisition proposition became available to the Bank, it would be able to raise additional liquidity at short notice. The platform will be administered from our Exeter office with two additional staff being directly employed and a third party service provider adding additional capacity where needed.

Strategic Report - Financial Review

Arbuthnot Banking Group adopts a pragmatic approach to risk taking and seeks to maximise long term revenues and returns. Given its relative size, it is nimble and able to remain entrepreneurial and capable of taking advantage of favourable market opportunities when they arise.

The Group provides a range of financial services to clients and customers in its chosen markets of Private and Commercial Banking and specialist lending. The Group's revenues are derived from a combination of net interest income from lending, deposit taking and treasury activities, fees for services provided and commission earned on the sale of financial instruments and products.

Highlights

Summarised Income Statement	2017 £000	2016 £000
Net interest income	41,093	30,445
Net fee and commission income	13,523	11,005
Operating income	54,616	41,450
Profit from associates	4,437	2,145
Other income	3,033	3,169
Operating expenses	(54,721)	(46,111)
Impairment losses - financial investments	-	(47)
Impairment losses - loans and advances to customers	(394)	(427)
Profit before tax from continuing operations	6,971	179
Income tax expense	(448)	(720)
Profit after tax from continuing operations	6,523	(541)
Profit from discontinued operations after tax	-	228,110
Profit for the year	**6,523**	**227,569**
Basic earnings per share (pence) - Continuing operations	43.9	(3.7)
Basic earnings per share (pence) - Discontinuing operations	-	1,130.9
Basic earnings per share (pence)	**43.9**	**1,127.2**

Underlying profit reconciliation 31 December 2017	Arbuthnot Latham & Co. £000	Retail Banking Associate £000	Group Centre	Arbuthnot Banking Group £000
Profit before tax from continuing operations	10,959	4,437	(8,425)	6,971
AL investment in operating systems	78	-	-	78
AL acquisition costs	108	-	-	108
RAF - full year equivalent income*	466	-	-	466
Underlying profit	**11,611**	**4,437**	**(8,425)**	**7,623**
Underlying basic earnings per share (pence) - Continuing operations				47.5
Underlying basic earnings per share (pence)				**47.5**

* - RAF profit contribution adjustment as if received from 1 January 2017 and not as currently included from 28 April 2017 (pro forma basis).

Underlying profit reconciliation	Arbuthnot Latham & Co.	Retail Banking Associate	Group Centre	Arbuthnot Banking Group
31 December 2016	£000	£000	£000	£000
Profit before tax from continuing operations	9,053	2,145	(11,019)	179
ABG Group bonuses relating to sale of ELL	-	-	2,304	2,304
STB full year equivalent associate income*	-	1,732	-	1,732
AL realised profit on AFS investment (Visa)	(1,624)	-	-	(1,624)
AL investment in operating systems	21	-	-	21
AL commercial banking investment	999	-	-	999
AL acquisition costs	398	-	-	398
Underlying profit	**8,847**	**3,877**	**(8,715)**	**4,009**
Underlying basic earnings per share (pence) - Continuing operations				17.1
Underlying basic earnings per share (pence)				**1,148.1**

** - STB associate income adjustment (excl. ELL & bonuses relating to ELL sale) as if received from 1 January 2016 and not as currently included from 16 June 2016 (pro forma basis).*

The Group has reported a profit before tax of £7.0m (2016: £0.2m). This is a good increase from the prior year and is the result of the continued deployment of part of the significant capital surplus that was created following the part sale of Secure Trust Bank ("STB") shares in 2016.

On an underlying basis the Group has generated profits of £7.6m compared to £4m in the prior year, which represents an increase of nearly 91%, reflecting the improving scale being generated in the business.

The deployment of capital has largely been focused on increasing the lending portfolio of the Group's businesses and notably during the year the customer loan balances once again exceeded the £1bn mark.

In line with ABG's long standing belief that diversification gives the Group strength, a portion of the capital was allocated to complete the acquisition of RAF. This deal was completed on 28 April following the receipt of approval from the relevant regulatory bodies. At the time of completion the customer balances of RAF stood at £58m. During the eight months that RAF formed part of the Group, it contributed £1.6m at an operating level.

The total Basic Earnings per share ("EPS") of the Group are 43.9p (2016: 1,127.2p). The reduction is largely due to the impact of the STB transactions in the prior year. On an underlying basis the EPS is 47.5p (2016: 17.1p), an increase of 177%. The total dividend is covered 1.33 times by the earnings.

At the time of the sale of a substantial part of the Group's ownership of STB, it was determined that the remaining investment (18.6%) should be treated as an associate, as ABG was considered to have "significant influence" by way of three directors of Arbuthnot Banking Group also being directors of STB. The determination remained consistent throughout 2017 and as a result the income statement has included a full year of our share of the profit after tax of STB, which contributed a further £2.3m as opposed to a half year impact in 2016.

The Group's expense base increased to £54.7m (2016: £46.1m), an increase of 19%. This increment is largely due to the continued investment in the diversification of businesses within the Group. The Commercial Banking business has expanded its numbers in London, Exeter and Manchester and opened a small office in Bristol. Also, the acquisition of RAF added £1.5m to the expense book in 2017. Additionally, the Bank has been strengthening its control and oversight functions to provide a sound foundation from which to continue to grow the business. The increase in expenses compares favourably to the 30% increase in operating income, resulting in a 10% positive operating leverage or increase in "Jaws".

Impairment losses on loans remained consistent at £0.4m (2016: £0.4m) but the overall loss rate declined to 4 bps on the total lending book.

Overall, the Return on Equity of the Group was 2.8%, though this is distorted by the significant unutilised capital within the Group. However, in the long run the Group remains committed to its target of 20%, though this will depend on reaching a sufficient level of operational scale regarding its overhead and also how the Regulators view the level of capital buffers they require from time to time.

Balance Sheet Strength

Summarised Balance Sheet	2017 £000	2016 £000
Assets		
Loans and advances to customers	1,049,269	758,799
Liquid assets	610,799	340,003
Other assets	193,164	166,482
Total assets	**1,853,232**	**1,265,284**
Liabilities		
Customer deposits	1,390,781	997,649
Other liabilities	226,076	33,277
Total liabilities	1,616,857	1,030,926
Equity	236,375	234,358
Total equity and liabilities	**1,853,232**	**1,265,284**

During the year total assets increased to £1.9bn (2016: £1.3bn), driven almost entirely by the increase in customer loan balances and the incremental treasury assets that arise from our ability to raise surplus customer deposits, which are then held at the Bank of England. Customer deposits increased to £1.4bn (2016: £1.0bn), an increase of 39%.

The net assets of the Group now stand at £15.47 per share (2016: £15.34).

Segmental Analysis

The segmental analysis is shown in more detail in Note 44. The operating segments are Arbuthnot Latham & Co., Limited and Retail Banking Associate (being the Group's 18.6% investment in STB). Group costs and intercompany elimination journals are shown separately to reconcile back to Group consolidated results.

The analysis presented below, and in the business review, is before any consolidation adjustments to reverse the impact of the intergroup operating activities and also intergroup recharges and is a fair reflection of the way the Directors manage the Group.

Arbuthnot Latham

Summarised Income Statement	2017 £000	2016 £000
Net interest income	41,402	30,771
Net fee and commission income	13,523	11,005
Operating income	54,925	41,776
Other income	3,870	4,353
Operating expenses	(47,442)	(36,602)
Impairment losses - financial investments	-	(47)
Impairment losses - loans and advances to customers	(394)	(427)
Profit before tax	**10,959**	**9,053**

The profit before tax for AL has reached £11m (2016: £9.1m), which is an increase of 21% on a reported basis. However, on an underlying basis the increase is 48% after the impact of the profit on sale of Visa Europe shares is excluded from 2016.

Operating income of the Bank increased by 31% as the capital deployment drove higher lending revenues.

Average net margin has remained stable at 4.8%.

Operating expenses increased by 30% as the expansion of the Commercial Bank continued and RAF was incorporated from April 2017.

Impairment losses were £0.4m (2016: £0.4m) as the lending portfolios continued to perform well.

Summarised Balance Sheet	2017 £000	2016 £000
Assets		
Loans and advances to customers	1,049,269	758,799
Liquid assets	610,785	339,990
Other assets (including Group balances)	123,621	100,373
Total assets	**1,783,675**	**1,199,162**
Liabilities		
Customer deposits	1,390,781	997,649
Other liabilities (including Group balances)	259,957	120,815
Total liabilities	1,650,738	1,118,464
Equity	132,937	80,698
Total equity and liabilities	**1,783,675**	**1,199,162**

AL reached a creditable milestone during 2017, with all of its key business metrics exceeding £1bn: Customer Loans, Customer Deposits and Assets under Management.

Total customer assets increased by 38% to close the year at £1,049m (2016: £759m). At the same time the total volume of loans written in the year increased to £466m (2016: £227m), an increase of 105%. Overall, the loan books remain well served with an average LTV of 53% (2016: 45%) for the Private and Commercial Banking business.

Total deposits increased by 39% to close the year at £1.4bn (2016: £1.0bn).

The investment management business was able to grow its assets under management by 13% to reach £1,044m (2016: £920m).

The net assets of the Bank now stand at £133m (2016: £81m), an increase of 65% as ABG made further capital contribution to facilitate additional growth and also to complete the acquisition of RAF. Additionally, retained reserves from the earnings of the Bank have contributed to give Arbuthnot Latham a total and core tier 1 capital ratio of 11.9% (2016: 12.3%).

Group & Other Costs

Summarised Income Statement	2017 £000	2016 £000
Net interest income	51	26
Subordinated loan stock interest	(360)	(352)
Operating income	(309)	(326)
Other income	160	120
Operating expenses	(8,276)	(10,813)
Profit after tax	**(8,425)**	**(11,019)**

The Group costs reduced to £8.4m (2016: £11m) as the impact of the bonuses paid in 2016 relating to the STB transaction recurring. The Group centre continues to oversee the Group operations, including the remaining investment in STB.

IFRS 9

The provisions of IFRS 9 – Financial Instruments will apply to the Group for the year ending 31 December 2018.

As a result of the implementation of IFRS 9, accounting for credit losses will fundamentally change, moving from an "incurred" to an "expected" basis. This has required the development of credit loss models, which will be used to estimate credit impairments by taking into account the composition of individual loan portfolios and the macro economic outlook at each reporting date. Also, the future economic environment will be "stressed" in varying scenarios to ensure the provisions are appropriate.

The initial models have been developed and are currently being validated and refined ahead of the full implementation.

The introduction of IFRS 9 will result in an initial increase in impairment provisions and may potentially increase volatility in the Group's Income Statement in the future (see Note 3.27).

It is expected that the opening entries as at 1 January 2018 required for the implementation will require an adjustment to shareholder reserves of between £2.4m to £3.2m. Under new capital regulations, the impact of IFRS 9 on regulatory capital will be phased over a period of 5 years. The Group has a strong capital position and the impact of IFRS 9 is not considered significant.

Capital

The Group's capital management policy is focused on optimising shareholder value over the long term. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

The Group's lead regulator, the Prudential Regulation Authority ("PRA"), sets and monitors capital requirements for the Group as a whole and for the individual banking operations. The lead regulator adopted the Basel III capital requirements with effect from 1 January 2014. As a result, the Group's regulatory capital requirements have been based on Basel III since 2014.

In accordance with the EU's Capital Requirements Directive ("CRD") and the required parameters set out in the PRA Handbook, the Individual Capital Adequacy Assessment Process ("ICAAP") is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management. The Group's regulated entity is also the principal trading subsidiary as detailed in Note 43.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a "Pillar I plus" approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations deliver a sufficient capital sum adequate to cover management's anticipated risks. Where the Board considers that the Pillar I calculations do not reflect the risk, an additional capital add-on in Pillar II is applied, as per the Individual Capital Guidance ("ICG") issued by the PRA.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders' funds and revaluation reserves, after deducting goodwill, other intangible assets and the deduction for a significant investment in a financial institution (STB). The portion of the investment representing up to 10% of ABG's Tier 1 is added back to capital resources and then risk weighted at 250%, while anything above this 10% is deducted.
- Lower Tier 2 comprises qualifying subordinated loan capital. Lower Tier 2 capital cannot exceed 50% of Tier 1 capital.

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. All regulated trading entities have complied with all of the externally imposed capital requirements to which they are subject.

Capital ratios	2017 £000	2016 £000
Core Tier 1 capital	236,375	234,358
Deductions	(77,761)	(67,639)
Tier 1 capital after deductions	158,614	166,719
Tier 2 capital	13,104	12,621
Total capital	**171,718**	**179,340**
Core Tier 1 capital ratio (Net Core Tier 1 capital/Basel III Total Risk Exposure)	**17.3%**	**28.1%**
Total Capital Ratio (Capital/Basel III Total Risk Exposure)	**18.7%**	**30.2%**

Risks and Uncertainties

The Group regards the monitoring and controlling of risks and uncertainties as a fundamental part of the management process. Consequently, senior management are involved in the development of risk management policies and in monitoring their application. A detailed description of the risk management framework and associated policies is set out in note 6.

The principal risks inherent in the Group's business are strategic, credit, market, liquidity, operational, cyber, conduct and regulatory.

Strategic risk

Strategic risk is the risk that may affect the Group's ability to achieve its corporate and strategic objectives. This risk is important to the Group as it continues its growth strategy. However, the Group seeks to mitigate strategic risk by focusing on a sustainable business model which is aligned to the Group's business strategy. Also, the Board of Directors meets once a year to hold a two day board meeting to ensure that the Group's strategy is appropriate for the market and economy.

Credit risk
Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. This risk exists in Arbuthnot Latham, which currently has a loan book of £1,049m. The lending portfolio in AL is extended to clients, the majority of which is secured against cash, property or other assets. Credit risk is managed through the Credit Committee of AL.

Market risk
Market risk arises in relation to movements in interest rates, currencies and equity markets. The Group's treasury function operates mainly to provide a service to clients and does not take significant unmatched positions in any market for its own account. As a result, the Group's exposure to adverse movements in interest rates and currencies is limited to interest earnings on its free cash and interest rate re-pricing mismatches. The Group actively monitors its exposure to future interest rate rises.

The Group is exposed to changes in the market value of properties. The current carrying value of Investment Property is £59m. Any changes in the market value of the property will be accounted for in the Income Statement and as a result could have a significant impact on the profit or loss of the Group.

The Group has an 18.6% interest in STB. This is currently recorded in the Group's balance sheet as an interest in associates and at 31 December 2017 was carried at £83.8m or the equivalent of £24.33 per share. At the year end the market price of STB was £17.97 per share. The Board has determined that the current carrying value remains appropriate after having carried out extensive analysis to be satisfied that the long term value in use does not suggest that this carrying value is impaired. These valuations included the Gordon's Growth model and Dividend Discount model. The resultant output from the models indicated valuations in a range that was in excess of £24 but this will be ultimately dependent on the surplus capital within STB being deployed in the business over the long term. There is a risk that the output of the value in use models could require an impairment charge to be recognised in the future.

If the Group was considered to no longer have significant influence over STB it would lead to the investment being accounted for as a financial asset at fair value. The value would then be marked to market with changes in the share price giving rise to gains or losses being recorded in Other Comprehensive Income or Profit or Loss – see Note 3.8(d) and Note 3.10(b).

Liquidity risk
Liquidity risk is the risk that the Group cannot meet its obligations as they fall due. The Group takes a conservative approach to managing its liquidity profile. Retail client deposits and drawings from the Bank of England Term Funding Scheme fund the Group. The loan to deposit ratio is maintained at a prudent level, and consequently the Group maintains a high level of liquidity. The Arbuthnot Latham Board annually approves the Individual Liquidity Adequacy Assessment Process ("ILAAP"). The Directors model various stress scenarios and assess the resultant cash flows in order to evaluate the Group's potential liquidity requirements. The Directors firmly believe that sufficient liquid assets are held to enable the Group to meet its liabilities in a stressed environment.

Operational risk
Operational risk is the risk that the Group may be exposed to financial losses from conducting its business. The Group is exposed to operational risks from its Information Technology and Operations platforms. There are additional internal controls in these processes that are designed to protect the Group from these risks. The Group's overall approach to managing internal control and financial reporting is described in the Corporate Governance section of the Annual Report.

Cyber risk
Cyber risk is an increasing risk that the Group is subject to within its operational processes. This is the risk that the Group is subject to some form of disruption arising from an interruption to its IT and data infrastructure. The Group regularly test the infrastructure to ensure that it remains robust to a range of threats, and have continuity of business plans in place including a disaster recovery provision.

Conduct risk
As a financial services provider we face conduct risk, including selling products to customers which do not meet their needs; failing to deal with customers' complaints effectively; not meeting customers' expectations; and exhibiting behaviours which do not meet market or regulatory standards.

The Group adopts a zero risk appetite for any unfair customer outcomes. It maintains clear compliance guidelines and provides ongoing training to all staff. Periodic spot checks and internal audits are performed to ensure these guidelines are being followed. The Group also has insurance policies in place to provide some cover for any claims that may arise.

Regulatory risk
Regulatory risk is the risk that the Group will have insufficient capital resources to support the business or does not comply with regulatory requirements. The Group adopts a conservative approach to managing its capital. The Board approves an Individual Capital Adequacy Assessment Process ("ICAAP") annually, which includes the performance of stringent stress tests to ensure that capital resources are adequate over a three year horizon. Capital and liquidity ratios are regularly monitored against the Board's approved risk appetite as part of the risk management framework.

Regulatory change also exists as a risk to the Group’s business. Notwithstanding the assessments carried out by the Group to manage the regulatory risk, it is not possible to predict how regulatory and legislative changes may alter and impact the business. Significant and unforeseen regulatory changes may reduce the Group’s competitive situation and lower its profitability.

Macroeconomic and competitive environment

The Group is also exposed to indirect risks that may arise from the macroeconomic and competitive environment. The economic environment is relatively stable in the UK. However, the international landscape is increasingly uncertain. The uncertain performance of the economies in the EU and the increasingly protectionist stance being taken by other major economies may have an adverse affect on the UK. In particular, this may cause a further softening of central London property prices, which may spread out further to the South East.

The Group monitors its exposure to future interest rate rises and currently has minimal lending to customers in products that would be directly sensitive to interest rate rises. However, at the current levels of interest rates, the affordability enjoyed by the Group’s customers is beneficial.

Brexit

It is currently difficult to analyse the impacts that Brexit may have on Arbuthnot Banking Group. However, our only overseas operation is in Dubai, so the vast majority of the Group’s income and expenditure is based in the UK. It is therefore anticipated that the financial impact would be minimal, assuming no significant macro economic shock in the UK.

Group Directors' Report

The Directors submit their annual report and the audited consolidated financial statements for the year ended 31 December 2017.

Principal Activities and Review

The principal activities of the Group are banking and financial services. A strategic review in accordance with Section 414 C of the Companies Act 2006 forming part of this report is set out on pages 4 to 14.

Results and Dividends

The results for the year are shown on page 1. The profit after tax for the year of £6.5m (2016: £227.6m) is included in reserves.

The Directors recommend the payment of a final dividend of 19p on the ordinary shares which, together with the interim dividend of 14p paid on 29 September 2017, represents total dividends (other than special dividends) for the year of 33p (2016: 31p). The final dividend, if approved by members at the Annual General Meeting, will be paid on 18 May 2018 to shareholders on the register at close of business on 27 April 2018.

Going Concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see note 6) and capital resources (see note 7), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on the going concern basis.

Share Capital

Shareholders will also be asked to approve a Special Resolution renewing the authority of the Directors to make market purchases of shares not exceeding 10% of the existing issued share capital. The Directors will keep the position under review in order to maximise the Company's resources in the best interests of shareholders.

Financial Risk Management

Details of how the Group manages risk are set out in in the Strategic Report and in note 6.

Substantial Shareholders

The Company was aware at 26 March 2018 of the following substantial holdings in the ordinary shares of the Company, other than those held by one director shown below:

Holder	Ordinary Shares	%
Liontrust Asset Management	924,228	6.0
Prudential plc	633,554	4.1
Slater Investments	595,638	3.9
Miton Asset Management	540,896	3.5
Mr. R Paston	529,130	3.5

Directors

Sir Henry Angest	*Chairman & CEO*
J R Cobb	*Finance Director*
I A Dewar	
I A Henderson	
P A Lynam	
Sir Christopher Meyer	
A A Salmon	*Chief Operating Officer*
Sir Alan Yarrow	

All these are currently directors and served throughout the year.

Mr. Cobb and Mr. Dewar retire under Article 78 of the Articles of Association and, being eligible, offer themselves for re-election. Mr. Cobb has a service agreement terminable on twelve months' notice. Mr. Dewar, an independent non-executive director, has a letter of appointment terminable on three months' notice.

According to the information kept under Section 3 of the Disclosure and Transparency Rules 2006 and the Market Abuse Regulation 2016, the interests of directors and their families in the ordinary 1p shares of the Company at the dates shown were, and the percentage of the current issued share capital held is, as follows::

Beneficial Interests	1 January 2017	31 December 2017	27 March 2018	%
Sir Henry Angest	8,200,901	8,351,401	8,351,401	54.7
J.R. Cobb	5,000	6,000	6,000	-
P.A. Lynam	10,000	10,000	10,000	0.1
A.A. Salmon	51,699	51,699	51,699	0.3

On 14 June 2016 Mr. Salmon, Mr. Cobb and Mr. Henderson were granted phantom options to subscribe for 200,000, 100,000 and 100,000 ordinary 1p shares respectively in the Company at 1591p. 50% of each director's individual holding of phantom options is exercisable at any time after 15 June 2019 and the other 50% is exercisable at any time after 15 June 2021. The fair value of the options at the grant date was £1.3m.

Apart from the interests disclosed above, no director was interested at any time in the year in the share capital of Group companies.

No director, either during or at the end of the financial year, was materially interested in any contract with the Company or any of its subsidiaries or associated companies, which was significant in relation to the Group's business. At 31 December 2017, one director had loans from Arbuthnot Latham & Co., Limited amounting to £508,000 and one director had a loan from Secure Trust Bank PLC amounting to £409,000, on normal commercial terms as disclosed in note 42 to the financial statements. At 31 December 2017, six directors had deposits with Arbuthnot Latham & Co., Limited amounting to £3,233,000 and two directors had deposits with Secure Trust Bank PLC amounting to £403,000, all on normal commercial terms as disclosed in note 42 to the financial statements.

The Company maintains insurance to provide liability cover for directors and officers of the Company.

Board Committees

The report of the Remuneration Committee on pages 24 to 25 will be the subject of an Ordinary Resolution at the Annual General Meeting.

Information on the Audit, Nomination and Political Donations Committees is included in the Corporate Governance section of the Annual Report on pages 19 to 22.

As explained in the Corporate Governance section of the Annual Report, the Board now maintains direct responsibility for issues of risk, as responsibility for large lending proposals has become a direct responsibility of its subsidiary, Arbuthnot Latham & Co., Limited.

Employees

The Company gives due consideration to the employment of disabled persons and is an equal opportunities employer. It also regularly provides employees with information on matters of concern to them, consults on decisions likely to affect their interests and encourages their involvement in the performance of the Company through share participation and in other ways.

Political Donations

The Company made political donations of £32,000 to the Conservative Party during the year (2016: £67,000).

Branches outside of the UK

During the year Arbuthnot Latham & Co., Ltd operated a branch in Dubai which is regulated by the Dubai Financial Services Authority.

Events after the balance sheet date

On 3 January 2018, Arbuthnot Latham entered into a 12 year lease (up to 16 October 2029) to occupy the first, second and third floors of 10 Dominion Street London, with a break clause on 16 October 2024. The initial rent is £0.7m per annum. This is reflected in contingent liabilities Note 36.

Auditor

A resolution for the re-appointment of KPMG LLP as auditor will be proposed at the forthcoming Annual General Meeting at a fee to be agreed in due course by the directors.

Statement of Disclosure of Information to the Auditor

The Directors confirm that:

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

This confirmation is given and shall be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Corporate Governance

Introduction and Overview

Arbuthnot Banking Group has a strong and effective Corporate Governance framework. This section of the Report and Accounts summarises key elements of the governance arrangements applicable to the Group and its compliance with the UK Corporate Governance Code.

As an AIM company, ABG is not bound by the UK Corporate Governance Code. However, the Board endorses the principles of openness, integrity and accountability, which underlie good corporate governance and takes into account both the provisions of the UK Corporate Governance Code in so far as they are considered appropriate to the Group's size and circumstances and in particular the role and overall holding of the majority shareholder. Moreover, the Group contains two subsidiaries authorised to undertake regulated business under the Financial Services and Markets Act 2000, one of which is regulated by the Prudential Regulatory Authority and the Financial Conduct Authority and is an authorised deposit-taking business. It in turn has a subsidiary, Renaissance Asset Finance Limited, which is regulated by the Financial Conduct Authority. Accordingly, the Group operates to the high standards of corporate accountability and regulatory compliance appropriate for such a business.

The Group is led by an effective Board which comprises four executive directors, two independent non-executive directors and two other non-executive directors.

Sir Henry Angest is the Chairman of the Group. The Chairman sets the long term focus and customer oriented culture of the Group and his role is to ensure good corporate governance. His responsibilities include leading the Board, ensuring the effectiveness of the Board in all aspects of its role, ensuring effective communication with shareholders, setting the Board's agenda and ensuring that all Directors are encouraged to participate fully in the activities and decision-making process of the Board.

There were no changes in Board membership during the year. Paul Lynam was appointed to the Board when Secure Trust Bank PLC ("STB") was a subsidiary of the Group, and remains a director of the Group, in a non-executive role, as well as Chief Executive of STB, following the reduction in the Group's holding in STB to 18.6%.

The directors seeking re-election are James Cobb and Ian Dewar, who have served on the Board for 9 years and 2½ years respectively. The contribution of James Cobb as the Group Financial Director has been very valuable in determining the capital and liquidity requirements of the Group. Ian Dewar, with a wealth of experience as a partner in a major accounting firm, has successfully chaired the Audit Committee. Accordingly, the Board fully supports the resolutions for their reappointment.

In 2016, the Board commissioned an independent Board Effectiveness Review. The Directors were satisfied with the conduct and outcome of the review and have since implemented its recommendations.

The Board

The Board meets regularly throughout the year, holding six formal meetings during the year as well as a two day strategy meeting. Substantive agenda items have briefing papers, which are circulated in a timely manner before each meeting. The Board ensures that it is supplied with all the information that it requires and requests, in a form and of a quality to fulfil its duties.

In addition to determining and overseeing the implementation of the strategy and management of the Company and of the Group, the Board has determined certain items which are reserved for decision by itself. These matters include the acquisition and disposal of other than minor businesses, the issue of capital by any Group company, monitoring overall regulatory requirements of its subsidiary companies, and their adherence thereto, and any transaction by a subsidiary company that cannot be made within its own resources or that is not in the normal course of its business.

The Company Secretary is responsible for ensuring that the Board processes and procedures are appropriately followed and support effective decision making. All directors have access to the Company Secretary's advice and services. There is an agreed procedure for directors to obtain independent professional advice in the course of their duties, if necessary, at the Company's expense.

All directors receive induction training upon joining the Board, with individual AIM training provided by the Company's Nominated Adviser, regulatory and compliance training provided by the Group Head of Compliance or an external firm of lawyers, risk management training (including that in relation to the ICAAP and ILAAP) with an overview of credit and its associated risks and mitigation by the Head of Credit Risk in Arbuthnot Latham & Co., Limited.

Board Committees

The Board has established Audit, Nomination, Remuneration and Donations Committees, each with formally delegated duties and responsibilities and with written terms of reference, which require consideration of the committee's effectiveness. The Board keeps the governance arrangements under review. Further information in relation to these committees is set out below. The Board now maintains direct responsibility for issues of Risk without the need for its own Risk Committee, since responsibility for large lending proposals became a direct responsibility of its subsidiary, Arbuthnot Latham & Co., Limited.

Audit Committee

Membership and meetings

Membership of the Audit Committee is restricted to non-executive directors and comprises Ian Dewar (as Chairman), Sir Christopher Meyer and Sir Alan Yarrow. The Committee met four times during the year.

The Audit Committee oversees, on behalf of the Board, the financial reporting, the appropriateness and effectiveness of systems and controls, the work of Internal Audit and the arrangements for and effectiveness of the external audit. The ultimate responsibility for reviewing and approving the annual report and accounts and the half-yearly report remains with the Board. The Audit Committee also reviews procedures for detecting fraud and preventing bribery, reviews whistleblowing arrangements for employees to raise concerns in confidence, and reviews, as necessary, arrangements for outsourcing significant operations.

The present auditors, KPMG LLP, have held office since 2009. The Senior Statutory Auditor changed in 2013 and will change again in 2018, following a five-year association with the Parent Company. The Board is satisfied with the effectiveness of their audit and endorses the comments made by the Committee in relation to the Audit Report set out below. The Committee received a report showing the level of non-audit services provided by the external auditors during the year and members were satisfied that the extent and nature of these did not compromise auditor independence.

Activity in 2017

Internal Audit

On behalf of the Board, the Audit Committee monitors the effectiveness of systems and controls. To this end, Internal Audit provides the Audit Committee and the Board with detailed independent and objective assurance on the effectiveness of governance, risk management and internal controls. Since Arbuthnot Latham & Co., Limited established its own Audit Committee, the role of the Group Audit Committee has been mainly supervisory in relation to internal audit matters, though it receives items of material note deriving from Arbuthnot Latham & Co., Limited’s internal audits, including an assessment of culture which forms part of every internal audit.

The Audit Committee approves the Internal Audit risk based programme of work and monitors progress against the annual plan. The Committee reviews Internal Audit resources and the arrangements that ensure Internal Audit faces no restrictions or limitations to conducting its work, that it continues to have unrestricted access to all personnel and information, and that Internal Audit remains objective and independent from business management.

The Head of Internal Audit provides reports on the outcomes of Internal Audit work directly to the Committee and the Committee monitors progress against actions identified in these reports.

The Committee is satisfied with Internal Audit arrangements during 2017.

Integrity of Financial Statements and oversight of external audit

In 2017, for the first time, the Group Financial Statements include a long form audit report and with this change, it is appropriate to include further information on the role that the Audit Committee has played in the approval of these accounts. The Committee:

- Received and agreed the Audit Plan prepared by the external auditors;
- Considered and formed a conclusion on the critical judgements underpinning the Financial Statements, as presented in papers prepared by management. In respect of all of these critical judgements, the Committee concluded that the treatment in the Financial Statements was appropriate.
- Received reports from the external auditors on the matters arising from their work, the key issues and conclusions they had reached;
- The Chairman of the Committee attended, as an observer, Audit Committees of Arbuthnot Latham & Co., Limited, the Company’s operating subsidiary;
- In addition, the Committee considered changes to financial reporting requirements that are not yet effective but that are likely to impact on the reported results or financial position of the Group and Company in future. The most notable being the implementation of IFRS 9 (from 1 January 2018) and the carrying value and disclosure of the Group’s interest in Secure Trust Bank PLC. The Committee has reviewed Management’s methodology, and is satisfied with the disclosures as set out in Note 3.27 and Note 27 to the financial statements.

The Audit Committee also receives reports from the external auditors which include details of internal control matters that they have identified as part of the annual statutory Financial Statements audit. Certain aspects of the system of internal control are also subject to regulatory supervision, the results of which are monitored closely by the Committee and the Board. In addition, the ICAAP and ILAAP are key control documents and received detailed consideration by the board of Arbuthnot Latham & Co., Limited. The Committee receives reports on these by exception.

The Committee approved the terms of engagement and the remuneration to be paid to the external auditors in respect of their audit services.

Significant areas of judgement

The Audit Committee considered the following significant issues and accounting judgements in relation to the Financial Statements:

Impairment review of interest in associate

The Group has an 18.6% interest in STB. This is currently recorded in the Group's Statement of Financial Position as an interest in associate and at 31 December 2017 was carried at £83.8m or the equivalent of £24.33 per share. At the year end the market price of STB was £17.97 per share.

The Committee reviewed the carrying value to ensure it was still appropriate. This included reviewing the valuation models and underlying assumptions used to substantiate the current value as reflected in the Statement of Financial Position. No impairment was considered necessary.

Refer to Note 4.1 (e) of the Notes to the Financial Statements for more information.

Impairment of loans and advances to customers

The Committee reviewed presentations from management detailing the provisioning methodology across the Group as part of the full year results process. The Committee considered and challenged the provisioning methodology applied by management, including timing of cash flows, valuation and recoverability of supporting collateral on impaired assets. The Committee concluded that the impairment provisions, including management's judgements, were appropriate.

The charge for impaired loans and advances totalled £0.4m for the year ended 31 December 2017. The disclosures relating to impairment provisions are set out in Note 4.1(a) to the financial statements.

Effective Interest rate

Interest earned on loans and receivables is recognised using the Effective Interest Rate ("EIR") method. The EIR is calculated on the initial recognition of a loan through a discounted cash flow model that incorporates fees, costs and other premiums or discounts. There have been no changes to the EIR accounting policies during the year.

The Committee considered and challenged the EIR methodology applied by management and specifically in relation to acquired loan portfolios. The Committee considered management assumptions including expected future customer behaviours and concluded that the EIR methodology was appropriate as at 31 December 2017.

The disclosures relating to EIR are set out in Note 4.1(b) to the financial statements.

Valuation of Investment Property

The two investment properties are held at fair value. The Committee reviewed the assumptions used in the valuation of the properties including capital expenditure, incentive periods, rental income, and yields.

As at 31 December, the Group's property investment portfolio totalled £59.4m, as detailed in Note 31. The disclosures relating to the fair value of investment property are set out in Note 4.1(c) to the financial statements.

Acquisition Accounting

During the year Arbuthnot Latham acquired the entire share capital of Renaissance Asset Finance Limited. The consideration consisted of an upfront and deferred payment based on future profits.

The Committee reviewed the accounting and the disclosures for the acquisition. This included reviewing the assumptions used in the valuation and identification of the separately identifiable intangible assets. An intangible asset relating to goodwill on acquisition was recognised totalling £3.5m (see Note 28).

Refer to Note 4.1 (d) of the Notes to the Financial Statements for more information.

Going Concern

The financial statements are prepared on the basis that the Group and Company are each a going concern. The Audit Committee reviewed management's assessment, and is satisfied that the going concern basis was appropriate.

Other Committee activities

During 2017 the Audit Committee received and reviewed reports from management relating to:

- The procedures for detecting fraud and prevention of bribery, and any instances of non-compliance;
- Whistleblowing arrangements for employees to raise concerns in confidence;

- Arrangements involving outsourcing of significant operations.

The Committee met separately with each of the Finance Director, Head of Internal Audit and the External Audit Partner without any other executives present. There were no issues or concerns raised by them in regard to discharging their responsibilities.

In September 2017, the Committee performed a review of its effectiveness by means of a self-assessment framework and completion of a questionnaire by members of the Committee. The review did not highlight any material concerns.

Nomination Committee

Membership and meetings

The Nomination Committee is chaired by Sir Henry Angest and its other members are Sir Christopher Meyer and Sir Alan Yarrow. The Committee met once during the year. It is required to meet formally at least once per year and otherwise as required.

The Nomination Committee assists the Board in discharging its responsibilities relating to the composition of the Board. The Nomination Committee is responsible for and evaluates on a regular basis the balance of skills, experience, independence and knowledge on the Board, its size, structure and composition, retirements and appointments of additional and replacement directors and will make appropriate recommendations to the Board on such matters. The Nomination Committee also considers succession planning, taking into account the skills and expertise that will be needed on and beneficial to the Board in the future.

Activity in 2017

The Committee reviewed the terms of service of the Group Finance Director. It has also reviewed and reconfirmed Sir Christopher Meyer's independence. It has examined the balance of executive and non-executive directors in relation to succession planning and the extent to which the requirements of a board diversity policy are met.

Remuneration Committee

Membership and meetings

Membership is detailed in the Remuneration Report on page 24. The Committee met twice during the year. It is required to meet formally at least once per year and otherwise as required.

The Remuneration Committee assists the Board in determining its responsibilities in relation to remuneration including, inter alia, in relation to the Company's policy on executive remuneration determining the individual remuneration and benefits package of each of the Executive Directors, and the fees for Non-Executive Directors.

The Committee also deals with remuneration-related issues under the Prudential Regulation Authority's Remuneration Code applicable to the Company.

A separate Remuneration Report gives further information and details of each Director's remuneration.

Donations Committee

Membership and meetings

The Donations Committee is chaired by Sir Henry Angest and its other members are Sir Christopher Meyer and Sir Alan Yarrow. The Committee met once during the year.

The Committee considers any political donation or expenditure as defined within sections 366 and 367 of the Companies Act 2006.

Internal Control and Financial Reporting

The Board of directors has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against the risk of material misstatement or loss.

The Directors and senior management of the Group have formally adopted a Group Risk and Controls Policy which sets out the Board's attitude to risk and internal control. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board. In addition, key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention.

Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are well-established budgeting procedures in place and reports are presented regularly to the Board detailing the results, in relation to Arbuthnot Latham & Co., Limited, of each principal business unit, variances against budget and prior year, and other performance data.

Shareholder Communications

The Company maintains ongoing communications via one to one meetings as appropriate with its major shareholders and makes full use of the Annual General Meeting and other General Meetings (when held) to communicate with investors. The Company aims to present a balanced and understandable assessment in all its reports to shareholders, its regulators, other stakeholders and the wider public. Key announcements and other information can be found at www.arbuthnotgroup.com.

Statement of Directors' Responsibilities in Respect of the Strategic Report and the Directors' Report and the Financial Statements

The Directors are responsible for preparing the Strategic Report, the Directors' Report and the Financial Statements in accordance with applicable law and regulations. Company law requires the Directors to prepare Group and Parent Company Financial Statements for each financial year. As required by the AIM Rules of the London Stock Exchange they are required to prepare the Group Financial Statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the EU and applicable law and have elected to prepare the Parent Company Financial Statements on the same basis.

Financial Statements

Under company law the Directors must not approve the Financial Statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and the Company and of the Group profit or loss for that period. In preparing each of the Group and Parent Company Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the Group and Parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they intend either to liquidate the Group or the Parent Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its Financial Statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and 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 Company's website. Legislation in the UK governing the preparation and dissemination of Financial Statements may differ from legislation in other jurisdictions.

Remuneration Report

Remuneration Committee

Membership of the Remuneration Committee is limited to non-executive directors together with Sir Henry Angest as Chairman. The present members of the Committee are Sir Henry Angest, Sir Christopher Meyer and Sir Alan Yarrow. The Committee met twice during the year.

The Committee has responsibility for producing recommendations on the overall remuneration policy for directors for review by the Board and for setting the remuneration of individual directors. Members of the Committee do not vote on their own remuneration.

Remuneration Policy

The Remuneration Committee determines the remuneration of individual directors having regard to the size and nature of the business; the importance of attracting, retaining and motivating management of the appropriate calibre without paying more than is necessary for this purpose; remuneration data for comparable positions, in particular the rising remuneration packages at challenger banks; the need to align the interests of executives with those of shareholders; and an appropriate balance between current remuneration and longer-term performance-related rewards. The remuneration package can comprise a combination of basic annual salary and benefits (including pension), a discretionary annual bonus award related to the Committee's assessment of the contribution made by the executive during the year and longer-term incentives, including executive share options. Pension benefits take the form of annual contributions paid by the Company to individual money purchase schemes. The Remuneration Committee reviews salary levels each year based on the performance of the Group during the preceding financial period. This review does not necessarily lead to increases in salary levels. For the purposes of the FCA Remuneration Code, all the provisions of which have been implemented, the Group and its subsidiaries are all considered to be Tier 3 institutions.

The Remuneration Committee reviewed the operation of the policy, having regard to the performance of the Company during the year, with particular regard to the level of discretionary bonus awarded and the level of inflation impacting on salaries.

Directors' Service Contracts

Sir Henry Angest, Andrew Salmon, James Cobb and Ian Henderson each have service contracts terminable at any time on 12 months' notice in writing by either party.

Long Term Incentive Schemes

At the Annual General Meeting in May 2015, shareholders voted by Ordinary Resolution to extend the Company's Unapproved Executive Share Option Scheme for a further period of 10 years. No such options were subsequently granted prior to the setting up of the Phantom Option Scheme.

On 14 June 2016, the Company announced a Phantom Share Option Scheme ("Phantom Option Scheme"), intended to replace the Unapproved Executive Share Option Scheme. The value of each phantom option is related to the market price of an ordinary share of 1p in the Company. An increase in the market value of an ordinary share of 1p in the Company over the market value per share at the date of grant of the phantom option will give rise to an entitlement to a cash payment by the Company on the exercise of a phantom option.

On 14 June 2016 Mr. Salmon was granted a phantom option pursuant to the Phantom Option Scheme to acquire 200,000 ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in market value. On 14 June 2016 Mr. Cobb and Mr. Henderson were each granted phantom options pursuant to the Phantom Option Scheme to acquire 100,000 ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in market value. The fair value of the options at the grant date was £1.3m.

Directors' Emoluments

	2017	2016
	£000	£000
Fees (including benefits in kind)	205	215
Salary payments (including benefits in kind)	4,533	7,731
Pension contributions	105	119
Long term incentive	-	992
	4,843	**9,057**

	Salary £000	Bonus £000	Benefits £000	Pension £000	Fees £000	Long term incentive £000	Total 2017 £000	Total 2016 £000
Sir Henry Angest	1,200	-	89	-	-	-	1,289	1,260
JR Cobb	550	250	17	35	-	-	852	1,583
IA Dewar	-	-	-	-	75	-	75	75
JW Fleming (to 14/04/2016)	-	-	-	-	-	-	-	145
IA Henderson (from 06/05/2016)	488	300	17	35	-	-	840	543
Ms RJ Lea (to 05/05/2016)	-	-	-	-	-	-	-	45
PA Lynam	-	-	-	-	-	-	-	1,493
Sir Christopher Meyer	-	-	-	-	60	-	60	60
AA Salmon	1,200	400	22	35	-	-	1,657	3,818
Sir Alan Yarrow (from 10/06/2016)	-	-	-	-	70	-	70	35
	3,438	**950**	**145**	**105**	**205**	**-**	**4,843**	**9,057**

Details of any shares or options held by directors are presented on page 16.

The emoluments of the Chairman were £1,289,000 (2016: £1,260,000). The emoluments of the highest paid director were £1,657,000 (2016: £3,818,000) including pension contributions of £35,000 (2016: £35,000).

Secure Trust Bank was paid a fee of £60,000 (2016: £33,000 from 15 June 2016) for the services of Mr. Lynam rendered as a non-executive director.

Retirement benefits are accruing under money purchase schemes for four directors who served during 2017 (2016: five directors).

Independent auditor's report

to the members of Arbuthnot Banking Group PLC

1. Our opinion is unmodified

We have audited the financial statements of Arbuthnot Banking Group PLC ("the Company") for the year ended 31 December 2017 which comprise the consolidated statement of comprehensive income, consolidated statement of financial position, company statement of financial position, consolidated statement of changes in equity, company statement of changes in equity, consolidated statement of cashflows, company statement of cashflows, and the related notes, including the accounting policies in notes 2 & 3.

In our opinion:

— the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 December 2017 and of the Group's profit for the year then ended;

— the group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);

— the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and

— the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

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

Overview	
Materiality: group financial statements as a whole	£570,000 (2016:£526,000) 8% (2016: based on an aggregation of individual component materialities) of Group Profit Before Tax
Coverage	100% (2016:100%) of Group Profit Before Tax.

Risks of material misstatement		**vs 2016**
Recurring risks	Loan Impairment Provisioning	◄►
	Effective Interest Rate Accounting	◄►
	Investment Property	◄►
New risks	Fair value of net assets acquired as part of business combination	▲
	Valuation of Investment in Associate	▲

2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. In arriving at our audit opinion above, the key audit matters, in decreasing order of audit significance, were as follows:

	The risk	Our response
Loan Impairment Provisioning Consolidated allowance for impairment of loans and advances: £1,362,000 (2016: £973,000) Consolidated net impairment loss on financial assets: £394,000 (2016: £474,000) *Refer to page 20 (Audit Committee Report), page 47 (accounting policy) and pages 56, 97 & 99 (financial disclosures).*	**Subjective estimate** The impairment provision relating to the Group's loans and advances requires the directors to make significant judgements in relation to the recoverability of loans and advances. Impairment provisions are assessed on an individual and collective basis. *Individual impairment:* Individual impairment provisions are determined by assessing the quantum and timing of future cashflows on loans identified as impaired on the watchlist. The directors judge individual impairments by reference to loans where the borrower has experienced cash flow difficulties, there has been delinquency in contractual payments of principal or interest or the account is under forbearance. *Collective impairment:* Collective impairment is assessed by applying judgement in the light of the Group's historical experience and other wider market factors due to there being limited loss experience.	Our procedures included: • **Controls:** We tested the controls over the acceptance, monitoring and reporting of credit risk; • **Independent re-performance:** We re-performed the calculations of impairment assessments and agreed the key data inputs to third party documentation; namely projected selling price and discount rates to the effective interest rate of the loan; • **Our sector experience:** We challenged and assessed the reasonableness of the key judgemental areas of the calculation, being forecast sale value of the collateral and the time to sale of the property, through stress testing by applying our own expectations based on our knowledge of the Group and experience of the industry in which it operates; • **Assessing valuers' credentials:** We evaluated the competence of the valuers engaged by the directors to support the valuation of collateral. This included consideration of their qualifications and expertise. • **Historical comparisons:** We critically assessed the Group's assumptions on past payment behaviour, collateral valuations and timing of realisation of cashflows by comparing them to the Group's historical experience; • **Sensitivity analysis:** We performed sensitivity analysis over the Group's collateral valuations based up our findings from the above procedures; and • **Test of details:** We performed credit reviews on a risk-based sample of loans; • **Assessing transparency:** We critically assessed the adequacy of the Group's disclosures in respect of the degree of estimation involved in arriving at the balance and sensitivity of the impairment of loans and advances to changes in key assumptions reflected in the inherent risk. **Our results** We found the resulting estimate of the allowance for impairment of loans and advances to be acceptable.

	The risk	Our response
Effective Interest Rate Accounting Consolidated interest income: £47,427,000 (2016: £38,071,000) *Refer to page 20 (Audit Committee Report), page 45 (accounting policy) and pages 56 & 83 (financial disclosures).*	**Subjective estimate** The recognition of revenue (interest receivable) on loans and advances to customers under the effective interest rate ('EIR') method requires the directors to apply judgement, with the most critical estimate being the loans' expected behavioural life. *Originated assets:* The expected life assumptions utilise repayment profiles which represent when customers are expected to repay based on past customer behaviour. *Acquired loan portfolios:* For the Group's acquired loan portfolios, the risk is that future cash collections estimated at acquisition are not reflected in actual cash receipts. Given the nature of the acquired loan portfolios, estimation of future cash collections requires significant estimation with regard to the value and timing of expected future cash flows.	Our procedures included: *Originated assets:* • **Historical comparison:** We critically assessed the Group's analysis and key assumptions for the repayment profiles by comparing them to the Group's historical trends and actual portfolio behaviour; • **Our sector experience:** We challenged the Group's repayment profiles by applying our own expectations based on our knowledge of the Group and experience of the industry in which it operates; *Acquired loan portfolios:* • **Historical comparison:** We critically assessed the Group's cash flow forecasts by comparing them to current and past performance of the Group's portfolios, including recent cash collections. • **Our sector experience:** We compared the profile of future cashflows to our own expectations based on our knowledge of the Group and experience of the industry in which it operates; *Both portfolios:* • **Assessing transparency:** We critically assessed the adequacy of the Group's disclosures about the sensitivity of the revenue recognition on loans and advances to changes in key assumptions reflected in the inherent risk. **Our results** We found the resulting estimate of the revenue recognition on loans and advances to be acceptable.

	The risk	Our response
Investment Property Group Investment Property: £59,439,000 (2016: £53,339,000) *Refer to page 20 (Audit Committee Report), page 49 (accounting policy) and pages 57 & 110 (financial disclosures).*	**Subjective valuation** The investment property requires the directors to apply significant judgments and estimates to its fair value assessment. The directors have prepared a model with input from professional advisors to calculate the fair value of the investment property. As a result there is an inherent risk that the data and assumptions used in the calculation are not complete or accurate.	Our procedures included: • **Assessing valuer's credentials**: We evaluated the competence of the expert engaged by the directors to support the valuation methodology and key assumptions. This included consideration of their qualifications and expertise. • **Tests of detail:** We performed testing of source documentation provided by the Group. This included agreeing a sample of this documentation back to underlying lease data. • **Our property valuation expertise:** We included property valuation specialists in our audit team who challenged the valuation approach and assumptions determined by the directors. • **Benchmarking assumptions:** Our property valuation specialists compared the yields applied to an expected range of yields taking into account market data and asset-specific considerations. They also considered whether the other assumptions applied by the directors, such as the estimated rental values, voids, tenant incentives and refurbishment costs were reasonable and supported by available market data such as recent lettings and occupancy levels. • **Sensitivity analysis:** We have undertaken sensitivity analysis over the key valuation assumptions (i.e. yields, renovation costs & post renovation rental uplift). • **Historical comparisons:** We carried out analytical procedures by comparing assumptions used for the valuation of the property on a year-on-year basis, by reference to our understanding of the UK commercial real estate market and external market data to evaluate the appropriateness of the valuations adopted by the directors. • **Assessing transparency:** We assessed the adequacy of the investment property disclosures by reference to the requirements in IAS 40. **Our results** The results of our testing were satisfactory and we considered the valuation of investment property to be acceptable.

	The risk	Our response
Fair value of net assets acquired as part of business combination 2017: £4,420,000 (2016: £nil) *Refer to page 21 (Audit Committee Report), page 43 (accounting policy) and pages 57 & 107 (financial disclosures).*	**Subjective estimate** The Company acquired Renaissance Asset Finance Limited during the year. The Group prepared the acquisition balance sheet based on estimates of the fair value of assets and liabilities acquired. In particular, the Group prepared discounted cash flow models to arrive at estimates of the acquired intangible assets including customer relationships, broker relationships and brand. This required the directors to exercise judgement in determining the expected cash flows from the assets and the discount rates to be applied.	Our procedures included: • **Assessing valuer's credentials**: We evaluated the competence of the expert engaged by the directors to support the valuation methodology and key assumptions. This included consideration of their qualifications and expertise. • **Our sector experience:** We challenged the assumptions, including value, probability and timing of cash flows, made in calculating the fair value assigned to the acquired loan portfolio and intangibles with reference to the business plan, existing customer contracts and actual performance achieved. • **Benchmarking assumptions:** We assessed whether the discount rate used in calculating the fair value of the acquired intangibles reflected market conditions based on our knowledge of the industry. • **Test of details:** We tested the prospective financial information utilised in the valuation calculations by reference to our knowledge of the business. • **Assessing transparency:** We assessed the adequacy of the business combination disclosures by reference to the requirements in IFRS 3. **Our results** The results of our testing were satisfactory and we considered the RAF acquisition purchase price allocation to be acceptable.

	The risk	Our response
Carrying Value of Investment in Associate Investment in Associate: £83,804,000 (2016: £82,574,000) *Refer to page 20 (Audit Committee Report), page 44 (accounting policy) and pages 58 & 102 (financial disclosures).*	**Subjective Estimate** The Group has an investment in Secure Trust Bank PLC ("STB") which is accounted for as an associate. The directors have assessed whether there is any impairment of the investment in light of the level of STB's share price. They have determined that the recoverable amount of the investment would be more appropriately determined through a 'value in use' calculation by reference to the expected dividend stream. The directors have prepared a bespoke model with input from professional advisors to calculate the value in use of the investment. As a result there is an inherent risk that the data and assumptions used in the calculation are not complete or accurate.	Our procedures included: • **Assessing valuer's credentials**: We evaluated the competence of the expert engaged by the directors to support the valuation methodology and key assumptions. This included consideration of their qualifications and expertise. • **Our corporate finance expertise:** We included corporate finance specialists in our audit team who challenged the valuation approach and assumptions determined by the directors. • **Our sector experience:** We challenged and assessed the reasonableness of the key judgemental areas of the calculation such as earnings and dividend growth based on our knowledge of the Group and experience of the industry in which it operates; • **Sensitivity analysis:** We have undertaken sensitivity analysis over the key valuation assumptions (i.e. return on equity, cost of equity, earnings and dividend growth). • **Assessing transparency:** We critically assessed the adequacy of the Group's disclosures in respect of the degree of estimation involved in arriving at the balance and sensitivity of the value in use calculation to changes in key assumptions. **Our results** The results of our testing were satisfactory and we considered the valuation of investment in associate to be acceptable.

3. Our application of materiality and an overview of the scope of our audit

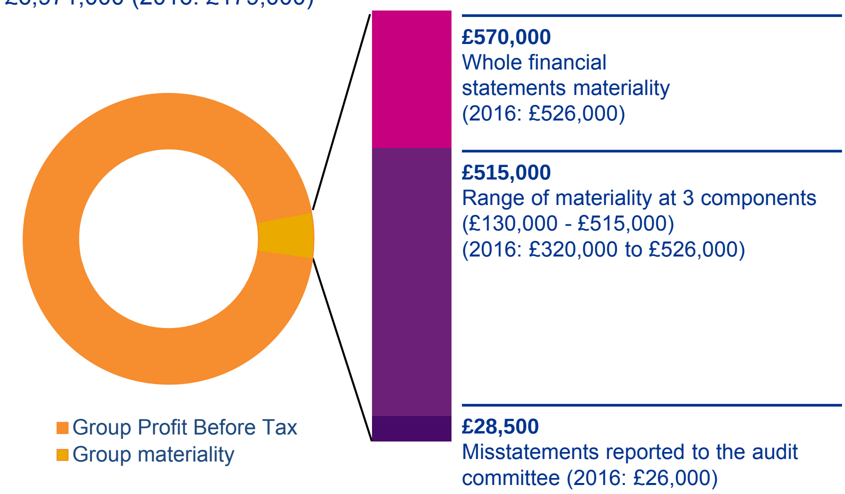
Materiality for the Group financial statements as a whole was set at £570,000 (2016: £526,000), determined with reference to a benchmark of Group profit before tax which it represents 8% (2016: based on an aggregation of individual component materialities).

Materiality for the parent Company financial statements as a whole was set at £406,000 (2016: £526,000), determined with reference to a benchmark of parent company profit before tax, of which it represents 5% (2016: 4.5% of parent Company profit before tax).

We reported to the Audit Committee any corrected or uncorrected identified misstatements exceeding £28,500 (2016: £26,000), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Group Profit Before Tax
£6,971,000 (2016: £179,000)

Group Materiality
£570,000 (2016: £526,000)



How we scoped our audit:

Audits for group reporting purposes were performed on all three (2016: two) reporting components, which were:

- Group holding company;
- Private banking subsidiary; and
- Asset finance subsidiary.

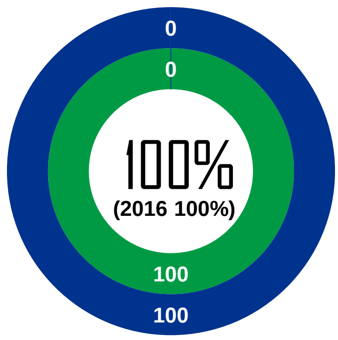
The components scoped in for Group reporting purposes accounted for 100% of Group revenue, 100% of Group profit before tax and 100% of Group total assets (2016: 100%).

The audit of the asset finance subsidiary was performed by a UK component audit team. The audit of the Group holding company, private banking subsidiary and consolidation was performed by the Group audit team.

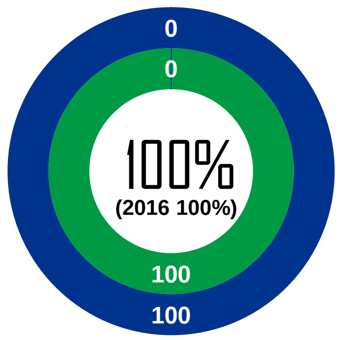
The Group audit team managed and co-ordinated the component auditor in the following way:

- During the audit the Group audit team held regular telephone calls and face-to-face discussions with the component audit team to challenge audit risks and audit strategy. Through the calls and meetings, the findings and observations reported to the Group audit team were discussed in more detail and any further work required by the Group audit team was then performed by the component auditor.
- In addition, the Group audit team participated in the audit close out meeting with the component team to ensure all material issues affecting the Group were identified and communicated back to the parent company. We challenged and reviewed audit approaches to impairment provisioning and revenue recognition.

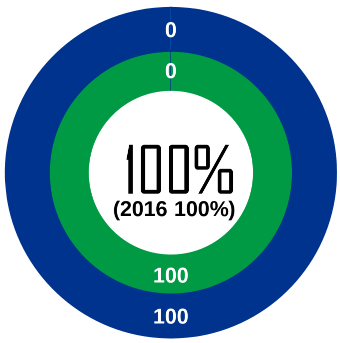
Group revenue



Group profit before tax



Group total assets



Full scope for group audit purposes 2017

Full scope for group audit purposes 2016

KPMG

Scope – Disclosure of IFRS9 Effect

The Group is adopting IFRS 9 Financial Instruments from 1 January 2018 and has included an estimate of the financial impact of the change in accounting standard in accordance with *IAS 8 Changes in Accounting Estimates and Errors* as set out in note 3.27. This disclosure notes that the Group continues to refine its expected credit loss model and embed its operational processes which may change the actual impact on adoption. While further testing of the financial impact will be performed as part of our 2018 year end audit, we have performed sufficient audit procedures for the purposes of assessing the disclosures made in accordance with IAS 8. Specifically we have:

- Considered the appropriateness of key technical decisions, judgements, assumptions and elections made by management
- Considered key Classification and Measurement decisions, including Business Model Assessments and Solely Payment of Principal and Interest (SPPI) outcomes
- Considered credit risk modelling decisions and macroeconomic variables, including forward economic guidance and generation of multiple economic scenarios
- Considered transitional controls and governance processes related to the approval of the estimated transitional impact

4. We have nothing to report on going concern

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

5. We have nothing to report on the strategic report and the directors' report

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

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

— we have not identified material misstatements in those reports;

— in our opinion the information given in the strategic report and the directors' report for the financial year is consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. We have nothing to report on the other matters on which we are required to report by exception

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

— adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or

— the parent Company financial statements are not in agreement with the accounting records and returns; or

— certain disclosures of directors' remuneration specified by law are not made; or

— we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 23, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

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

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our sector experience, through discussion with the directors and other management (as required by auditing standards), and from inspection of the group's regulatory correspondence.

We had regard to laws and regulations in areas that directly affect the financial statements including financial reporting (including related company legislation) and taxation legislation. We considered the extent of compliance with those laws and regulations as part of our procedures on the related financial statements items.

In addition we considered the impact of laws and regulations in the specific areas of regulatory capital & liquidity and conduct recognising the financial and regulated nature of the Groups activities. With the exception of any known or possible non-compliance, and as required by auditing standards, our work in respect of these was limited to enquiry of the directors and other management and inspection of regulatory correspondence. We considered the effect of any known or possible non-compliance in these areas as part of our procedures on the related annual accounts items.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

As with any audit, there remained a higher risk of non-detection of non-compliance with relevant laws and regulations, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

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

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

Richard Gabbertas (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL
27 March 2018

Company statement of financial position

	Note	At 31 December 2017 £000	2016 £000
ASSETS			
Loans and advances to banks	18	36,103	89,072
Financial investments	25	140	121
Deferred tax asset	26	641	397
Property, plant and equipment	30	157	183
Other assets	24	199	887
Interests in associates	27	5,056	5,056
Interests in subsidiaries	43	97,802	54,602
Total assets		**140,098**	**150,318**
EQUITY AND LIABILITIES			
Equity			
Share capital	37	153	153
Other reserves	38	(1,111)	(1,111)
Retained earnings	38	124,659	133,847
Total equity		**123,701**	**132,889**
LIABILITIES			
Current tax liability		152	-
Other liabilities	34	3,141	4,808
Debt securities in issue	35	13,104	12,621
Total liabilities		**16,397**	**17,429**
Total equity and liabilities		**140,098**	**150,318**

The Company has elected to take the exemption under section 408 of the Companies Act 2006 not to present the Parent Company profit and loss account. The profit for the Parent Company for the year is presented in the Statement of Changes in Equity.

Consolidated statement of changes in equity

	Attributable to equity holders of the Group							
	Share capital	Revaluation reserve	Capital redemption reserve	Available -for-sale reserve	Treasury shares	Retained earnings	Non-controlling interests	Total
	£000	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2017	**153**	**-**	**20**	**(251)**	**(1,131)**	**235,567**	**-**	**234,358**
Total comprehensive income for the period								
Profit for 2017	-	-	-	-	-	6,523	-	6,523
Other comprehensive income, net of tax								
Available-for-sale reserve - net change in fair value	-	-	-	128	-	-	-	128
Available-for-sale reserve - Associate - net change in fair value	-	-	-	389	-	-	-	389
Tax on other comprehensive income	-	-	-	(104)	-	-	-	(104)
Total other comprehensive income	-	-	-	**413**	-	-	-	**413**
Total comprehensive income for the period	-	-	-	**413**	-	**6,523**	-	**6,936**
Transactions with owners, recorded directly in equity								
Contributions by and distributions to owners								
Equity settled share based payment transactions	-	-	-	-	-	(155)	-	(155)
Final dividend relating to 2016	-	-	-	-	-	(2,680)	-	(2,680)
Interim dividend relating to 2017	-	-	-	-	-	(2,084)	-	(2,084)
Total contributions by and distributions to owners	-	-	-	-	-	**(4,919)**	-	**(4,919)**
Balance at 31 December 2017	**153**	**-**	**20**	**162**	**(1,131)**	**237,171**	**-**	**236,375**

	Attributable to equity holders of the Group							
	Share capital	Revaluation reserve	Capital redemption reserve	Available -for-sale reserve	Treasury shares	Retained earnings	Non-controlling interests	Total
	£000	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2016	**153**	**98**	**20**	**1,047**	**(1,131)**	**123,330**	**67,887**	**191,404**
Total comprehensive income for the period								
Profit for 2016	-	-	-	-	-	166,143	61,426	227,569
Other comprehensive income, net of tax								
Available-for-sale reserve - net change in fair value	-	-	-	(1,890)	-	-	(487)	(2,377)
Available-for-sale reserve - Associate - net change in fair value	-	-	-	(389)	-	-	-	(389)
Tax on other comprehensive income	-	-	-	456	-	-	-	456
Total other comprehensive income	-	-	-	**(1,823)**	-	-	**(487)**	**(2,310)**
Total comprehensive income for the period	-	-	-	**(1,823)**	-	**166,143**	**60,939**	**225,259**
Transactions with owners, recorded directly in equity								
Contributions by and distributions to owners								
Equity settled share based payment transactions	-	-	-	-	-	(1,074)	31	(1,043)
Secure Trust Bank loss of control	-	(98)	-	525	-	(427)	(124,046)	(124,046)
Final dividend relating to 2015	-	-	-	-	-	(2,531)	(4,811)	(7,342)
Special dividend relating to 2016	-	-	-	-	-	(3,722)	-	(3,722)
Interim dividend relating to 2016	-	-	-	-	-	(1,936)	-	(1,936)
Special dividend relating to 2016	-	-	-	-	-	(44,216)	-	(44,216)
Total contributions by and distributions to owners	-	**(98)**	-	**525**	-	**(53,906)**	**(128,826)**	**(182,305)**
Balance at 31 December 2016	**153**	**-**	**20**	**(251)**	**(1,131)**	**235,567**	**-**	**234,358**

Company statement of changes in equity

	Share capital	Capital redemption reserve	Treasury shares	Retained earnings	Total
	Attributable to equity holders of the Company				
	£000	£000	£000	£000	£000
Balance at 1 January 2016	**153**	**20**	**(1,131)**	**46,537**	**45,579**
Total comprehensive income for the period					
Profit for 2016	-	-	-	140,826	140,826
Other comprehensive income, net of income tax	-	-	-	-	-
Total comprehensive income for the period	-	-	-	**140,826**	**140,826**
Transactions with owners, recorded directly in equity					
Contributions by and distributions to owners					
Equity settled share based payment transactions	-	-	-	(1,111)	(1,111)
Final dividend relating to 2015	-	-	-	(2,531)	(2,531)
Special dividend relating to 2016	-	-	-	(3,722)	(3,722)
Interim dividend relating to 2016	-	-	-	(1,936)	(1,936)
Special dividend relating to 2016	-	-	-	(44,216)	(44,216)
Total contributions by and distributions to owners	-	-	-	**(53,516)**	**(53,516)**
Balance at 31 December 2016	**153**	**20**	**(1,131)**	**133,847**	**132,889**
Total comprehensive income for the period					
Loss for 2017	-	-	-	(4,269)	(4,269)
Other comprehensive income, net of income tax	-	-	-	-	-
Total comprehensive income for the period	-	-	-	**(4,269)**	**(4,269)**
Transactions with owners, recorded directly in equity					
Contributions by and distributions to owners					
Equity settled share based payment transactions	-	-	-	(155)	(155)
Final dividend relating to 2016	-	-	-	(2,680)	(2,680)
Interim dividend relating to 2017	-	-	-	(2,084)	(2,084)
Total contributions by and distributions to owners	-	-	-	**(4,919)**	**(4,919)**
Balance at 31 December 2017	**153**	**20**	**(1,131)**	**124,659**	**123,701**

Consolidated statement of cash flows

	Note	Year ended 31 December 2017 £000	Year ended 31 December 2016 £000
Cash flows from operating activities			
Interest received		43,389	109,311
Interest paid		(6,093)	(19,372)
Fees and commissions received		8,682	37,511
Other income		3,033	-
Cash payments to employees and suppliers		(47,600)	(101,217)
Taxation paid		(379)	(3,020)
Cash flows from operating profits before changes in operating assets and liabilities		1,032	23,213
Changes in operating assets and liabilities:			
- net (increase)/decrease in derivative financial instruments		(331)	66
- net (increase)/decrease in loans and advances to customers		(233,175)	855,436
- net (increase)/decrease in other assets		(7,952)	41,780
- net increase/(decrease) in amounts due to customers		392,937	(932,189)
- net decrease in other liabilities		(843)	(23,595)
Net cash inflow/(outflow) from operating activities		**151,668**	**(35,289)**
Cash flows from investing activities			
Disposal of financial investments		-	1,078
Purchase of computer software	28	(2,641)	(5,155)
Purchase of property, plant and equipment	30	(666)	(354)
Purchase of investment property	31	(6,421)	(53,339)
Disposal of Tarn Crag (Holdings) Limited	27	900	-
Purchase of Renaissance Asset Finance Limited	29	(2,072)	-
Cash balance acquired through Renaissance Asset Finance Limited acquisition	29	2,815	-
Proceeds from sale of Everyday Loans Group, net of cash and cash equivalents disposed		-	101,723
Proceeds from sale of Secure Trust Bank shares		-	147,999
Reduction in cash balance with deconsolidation of Secure Trust Bank		-	(194,344)
Purchases of debt securities		(211,080)	(89,384)
Proceeds from redemption of debt securities		90,410	71,899
Net cash outflow from investing activities		**(128,755)**	**(19,877)**
Cash flows from financing activities			
Increase/(decrease) in borrowings		132,928	(52,105)
Dividends paid		(4,764)	(57,215)
Net cash inflow/(outflow) from financing activities		**128,164**	**(109,320)**
Net increase/(decrease) in cash and cash equivalents		151,077	(164,486)
Cash and cash equivalents at 1 January		232,703	397,189
Cash and cash equivalents at 31 December	41	**383,780**	**232,703**

Company statement of cash flows

	Note	Year ended 31 December 2017 £000	Year ended 31 December 2016 £000
Cash flows from operating activities			
Dividends received from subsidiaries		2,618	11,468
Interest received		202	283
Interest paid		(513)	(611)
Other income		1,643	1,816
Cash payments to employees and suppliers		(7,977)	(10,107)
Taxation paid		-	(488)
Cash flows from operating (losses)/profits before changes in operating assets and liabilities		(4,027)	2,361
Changes in operating assets and liabilities:			
- net (increase)/decrease in group company balances		(1,788)	526
- net decrease in other assets		690	104
- net increase in other liabilities		120	48
Net cash (outflow)/inflow from operating activities		**(5,005)**	**3,039**
Cash flows from investing activities			
Increase investment in subsidiary	43	(43,200)	(22,000)
Disposal of share in subsidiaries	43	-	147,999
Purchase of property, plant and equipment	30	-	(5)
Net cash (outflow)/inflow from investing activities		**(43,200)**	**125,994**
Cash flows from financing activities			
Dividends paid		(4,764)	(52,405)
Net cash used in financing activities		**(4,764)**	**(52,405)**
Net (decrease)/increase in cash and cash equivalents		(52,969)	76,628
Cash and cash equivalents at 1 January		89,072	12,444
Cash and cash equivalents at 31 December	41	**36,103**	**89,072**

Notes to the Consolidated Financial Statements

1. Reporting entity

Arbuthnot Banking Group PLC is a company domiciled in the United Kingdom. The registered address of Arbuthnot Banking Group PLC is 7 Wilson Street, London, EC2M 2SN. The consolidated financial statements of Arbuthnot Banking Group PLC as at and for the year ended 31 December 2017 comprise Arbuthnot Banking Group PLC and its subsidiaries (together referred to as the "Group" and individually as "subsidiaries"). The Company is the holding company of a group primarily involved in banking and financial services.

2. Basis of presentation

(a) Statement of compliance

The Group’s consolidated financial statements and the Company’s financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs as adopted and endorsed by the EU) and the Companies Act 2006 applicable to companies reporting under IFRS.

The consolidated financial statements were authorised for issue by the Board of Directors on 27 March 2018.

(b) Basis of measurement

The consolidated and company financial statements have been prepared under the historical cost convention, as modified by the revaluation of land and buildings, investment property, available-for-sale financial assets, derivatives, and financial assets and financial liabilities at fair value through profit or loss.

(c) Functional and presentational currency

Items included in the financial statements of each of the Group’s entities are measured using the currency of the primary economic environment in which the entity operates (‘the functional currency’). The consolidated financial statements are presented in Pounds Sterling, which is the Company’s functional and the Group's presentational currency.

(d) Use of estimates and judgements

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

(e) Accounting developments

The accounting policies adopted are consistent with those of the previous financial year. There were no new or amended standards or interpretations that resulted in a change in accounting policy.

(f) Going concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see Note 6) and capital resources (see Note 7), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on the going concern basis.

3. Significant accounting policies

The accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

3.1. Consolidation

(a) Subsidiaries

Subsidiaries are all investees (including special purpose entities) controlled by the Group. The Group controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired, liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group’s shares of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the Statement of Comprehensive Income as a gain on bargain purchase.

The Parent's investments in subsidiaries are recorded at cost less, where appropriate, provisions for impairment in value.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Changes in ownership and non-controlling interests
Changes in ownership interest in a subsidiary that do not result in the loss of control are accounted for as equity transactions and no gain or loss is recognised. Adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary.

When control of a subsidiary is lost, the Group derecognises the assets, liabilities, non-controlling interest and all other components of equity relating to the former subsidiary from the consolidated statement of financial position. Any resulting gain or loss is recognised in profit or loss. Any investment retained in the former subsidiary is recognised at its fair value at the date when control is lost.

(c) Special purpose entities
Special purpose entities ("SPEs") are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets or the execution of a specific borrowing or lending transaction. SPEs are consolidated when the investor controls the investee. The investor would only control the investee if it had all of the following:

• power over the investee;
• exposure, or rights, to variable returns from its involvement with the investee; and
• the ability to use its power over the investee to affect the amount of the investor's returns.

The assessment of whether the Group has control over an SPE is carried out at inception and the initial assessment is only reconsidered at a later date if there were any changes to the structure or terms of the SPE, or there were additional transactions between the Group and the SPE.

(d) Associates
Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20 and 50 percent of the voting power of another entity. Associates are accounted for using the equity method and are initially recognised at cost. The Group's investment includes goodwill identified on acquisition, net of any accumulated impairment losses. The consolidated financial statements include the Group's share of the total comprehensive income and equity movements of equity accounted investees, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an equity accounted investee, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee.

3.2. Segment reporting
Operating segments are reported in a manner consistent with the internal reporting provided to the Group Board. The Group Board, which is responsible for allocating resources and assessing performance of the operating segments, has been identified as the chief operating decision maker. All transactions between segments are conducted on an arm's length basis. Income and expenses directly associated with each segment are included in determining segment performance. There are three main operating segments:

• Retail Banking
• Private Banking
• Group Centre

3.3. Foreign currency translation
Foreign currency transactions are translated into the functional currency using the spot exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Comprehensive Income. Foreign exchange differences arising from translation of available-for-sale equity instruments are recognised in Other Comprehensive Income.

3.4. Interest income and expense
Interest income and expense are recognised in the Statement of Comprehensive Income for all instruments measured at amortised cost using the effective interest rate method.

The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group takes into account all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income continues to be recognised using the original effective interest rate applied to the impaired carrying amount.

3.5. Fee and commission income

Fees and commissions which are not considered integral to the effective interest rate are generally recognised on an accrual basis when the service has been provided.

Asset and other management, advisory and service fees are recognised on an accruals basis as the related services are performed. The same principle is applied for financial planning and insurance services that are continuously provided over an extended period of time.

3.6. Rental income

Rental income is recognised on a straight line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income over the term of the lease.

3.7. Discontinued operations

A discontinued operation is a component of the Group's business, the operations and cash flows of which can be clearly distinguished from the rest of the Group and which:

- represents a separate major line of business or geographical area of operations;
- is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is a subsidiary acquired exclusively with a view to re-sale.

Classification as a discontinued operation occurs on disposal or when the operation meets the criteria to be classified as held for sale (see note 3.14), if earlier. When an operation is classified as a discontinued operation, the comparative Statement of Comprehensive Income is re-presented as if the operation had been discontinued from the start of the comparative year.

3.8. Financial assets and financial liabilities

The Group classifies financial assets and financial liabilities in the following categories: financial assets and financial liabilities at fair value through profit or loss; loans and receivables; held-to-maturity investments; available-for-sale financial assets and other financial liabilities. Management determines the classification of its investments at acquisition. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(a) Financial assets and financial liabilities at fair value through profit or loss

This category comprises listed securities and derivative financial instruments. Derivative financial instruments utilised by the Group include embedded derivatives and derivatives used for hedging purposes. Financial assets and liabilities at fair value through profit or loss are initially recognised on the date from which the Group becomes a party to the contractual provisions of the instrument. Subsequent measurement of financial assets and financial liabilities held in this category are carried at fair value through profit or loss.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. Loans are recognised when cash is advanced to the borrowers. Loans and receivables, other than those relating to assets leased to customers, are carried at amortised cost using the effective interest rate method. The accounting for assets leased to customers, is set out under Note 3.18 (a).

(c) Held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has the positive intent and ability to hold to maturity and that have not been designated at fair value through profit or loss or as available-for-sale investments. Held-to-maturity investments are carried at amortised cost using the effective interest rate method, less any impairment loss.

(d) Available-for-sale

Available-for-sale ("AFS") investments are those not classified as another category of financial assets. These include investments in special purpose vehicles and equity investments in unquoted vehicles. They may be sold in response to liquidity requirements, interest rate, exchange rate or equity price movements. AFS investments are initially recognised at cost, which is considered as the fair value of the investment including any acquisition costs. AFS securities are subsequently measured at fair value in the statement of financial position. Fair value changes in the AFS securities are recognised directly in equity (AFS reserve) until the investment is sold or impaired. Once sold or impaired, the cumulative gains or losses previously recognised in the AFS reserve are recycled to the profit or loss.

(e) Current financial assets held for sale

Current financial assets held for sale are measured at the lower of their carrying amount and fair value less costs to sell except where measurement and remeasurement is outside the scope of IFRS 5. Where investments that have initially been recognised as current financial assets held for sale, because the Group has been deemed to hold a controlling stake, are subsequently disposed of or diluted such that the Group's holding is no longer deemed a controlling stake, the investment will subsequently be classified as fair value through profit or loss investments in accordance with IAS 39. Subsequent movements will be recognised in accordance with the Group's accounting policy for the newly adopted classification.

(f) Other financial liabilities

Other financial liabilities are non-derivative financial liabilities with fixed or determinable payments. Other financial liabilities are recognised when cash is received from the depositors. Other financial liabilities are carried at amortised cost using the effective interest rate method. The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the Statement of Financial Position date.

Amortised cost measurement

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, minus principal payments, plus or minus the cumulative amortisation using the effective interest rate method of any difference between the initial amount recognised and the maturity amount, less any reduction for impairment.

Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis. In the instance that fair values of assets and liabilities cannot be reliably measured, they are carried at cost.

For measuring derivatives that might change classification from being an asset to a liability or vice versa such as interest rate swaps, fair values take into account both credit valuation adjustment (CVA) and debit valuation adjustment (DVA) when market participants take this into consideration in pricing the derivatives.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all risks and rewards of ownership. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the Statement of Financial Position. In transactions in which the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset. There have not been any instances where assets have only been partially derecognised.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled, expire, are modified or exchanged.

3.9. Derivative financial instruments

All derivatives are recognised at their fair value. Fair values are obtained from quoted market prices in active markets, including recent arm's length transactions or using valuation techniques such as discounted cash flow models. Derivatives are shown in the Statement of Financial Position as assets when their fair value is positive and as liabilities when their fair value is negative.

Embedded derivatives

Embedded derivatives arise from contracts ('hybrid contracts') containing both a derivative (the 'embedded derivative') and a non-derivative (the 'host contract'). Where the economic characteristics and risks of the embedded derivatives are not closely related to those of the host contract, and the host contract is not at fair value through profit or loss, the embedded derivative is bifurcated and reported at fair value and gains or losses are recognised in the Statement of Comprehensive Income.

3.10. Impairment of financial assets

(a) Assets carried at amortised cost

On an ongoing basis the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence is the occurrence of a loss event, after the initial recognition of the asset, that impacts on the estimated contractual future cash flows of the financial asset or group of financial assets, and can be reliably estimated.

The criteria that the Group uses to determine whether there is objective evidence of an impairment loss include, but are not limited to, the following:

• Delinquency in contractual payments of principal or interest;
• Cash flow difficulties experienced by the borrower;
• Initiation of bankruptcy proceedings;
• Deterioration in the value of collateral;
• Deterioration of the borrower's competitive position.

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows discounted at the financial asset’s original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the Statement of Comprehensive Income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

The Group considers evidence of impairment for loans and advances at both a specific asset and collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. In assessing collective impairment the Group uses historical trends of the probability of default, emergence period, the timing of recoveries and the amount of loss incurred, adjusted for management’s judgement as to whether current economic and credit conditions are such that the actual losses are likely to be significantly different to historic trends.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the Statement of Comprehensive Income.

A customer’s account may be modified to assist customers who are in or have recently overcome financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. Loans that have renegotiated or deferred terms, resulting in a substantial modification to the cash flows, are no longer considered to be past due but are treated as new loans recognised at fair value, provided the customers comply with the renegotiated or deferred terms.

(b) Assets classified as available-for-sale

The Group assesses at each Statement of Financial Position date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the profit or loss. Impairment losses recognised in the profit or loss on equity instruments are reversed through other comprehensive income.

(c) Renegotiated loans

Loans that are neither subject to collective impairment assessment nor individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans.

(d) Forbearance

Under certain circumstances, the Group may use forbearance measures to assist borrowers who are experiencing significant financial hardship. Any forbearance support is assessed on a case by case basis in line with best practice and subject to regular monitoring and review. The Group seeks to ensure that any forbearance results in a fair outcome for both the customer and the Group.

3.11. Impairment of non-financial assets

The carrying amounts of the Group’s non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset’s recoverable amount is estimated. Impairment for goodwill is discussed in more detail under note 3.15(a).

3.12. Term Funding Scheme

The Term Funding Scheme (“TFS”) was announced by the Bank of England on 4 August 2016 and became effective from 19 September 2016. The TFS allows participants to borrow central bank reserves in exchange for eligible collateral. Amounts drawn from the TFS are included within “Deposits from banks” on the Statement of Financial Position as detailed in Note 32.

3.13. Inventory

Land acquired through repossession of collateral which is subsequently held in the ordinary course of business with a view to develop and sell is accounted for as inventory.

Inventory is measured at the lower of cost or net realisable value. The cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

3.14. Assets classified as held for sale

Assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. These assets and liabilities are subsequently measured at the lower of carrying amount and fair value less costs to sell. Once classified as held for sale, intangible assets and property, plant and equipment are no longer amortised or depreciated.

3.15. Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group’s share of the net identifiable assets of the acquired subsidiary or associate at the date of acquisition. Goodwill on acquisitions of subsidiaries or associates is included in ‘intangible assets’. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

The Group reviews the goodwill for impairment at least annually or more frequently when events or changes in economic circumstances indicate that impairment may have taken place and carries goodwill at cost less accumulated impairment losses. Assets are grouped together in the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or "CGU"). For impairment testing purposes goodwill cannot be allocated to a CGU that is greater than a reported operating segment. CGUs to which goodwill has been allocated are aggregated so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination. The test for impairment involves comparing the carrying value of goodwill with the present value of pre-tax cash flows, discounted at a rate of interest that reflects the inherent risks of the CGU to which the goodwill relates, or the CGU’s fair value if this is higher.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives (three to ten years).

Costs associated with maintaining computer software programs are recognised as an expense as incurred.

Costs associated with developing computer software which are assets in the course of construction, which management has assessed to not be available for use, are not amortised.

(c) Other intangibles

Other intangibles include trademarks, customer relationships, broker relationships, technology and banking licences acquired. These costs are amortised on the basis of the expected useful lives (three to fourteen years).

3.16. Property, plant and equipment

Land and buildings comprise mainly branches and offices and are stated at the latest valuation with subsequent additions at cost less depreciation. Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, applying the following annual rates, which are subject to regular review:

Freehold buildings	50 years
Office equipment	3 to 10 years
Computer equipment	3 to 5 years
Motor vehicles	4 years

Leasehold improvements are depreciated over the term of the lease (until the first break clause). Gains and losses on disposals are determined by deducting carrying amount from proceeds. These are included in the Statement of Comprehensive Income. Depreciation on revalued freehold buildings is calculated using the straight-line method over the remaining useful life. Revaluation of assets and any subsequent disposals are addressed through the revaluation reserve and any changes are transferred to retained earnings.

3.17. Investment property

Investment property is initially measured at cost. Transaction costs are included in the initial measurement. Subsequently, investment property is measured at fair value, with any change therein recognised in profit and loss within other income.

If a change in use occurs and investment property is transferred to owner-occupied property, the property's deemed cost for subsequent reporting is its fair value at the date of change in use.

3.18. Leases

(a) As a lessor

Assets leased to customers under agreements which transfer substantially all the risks and rewards of ownership, with or without ultimate legal title, are classified as finance leases. When assets are held subject to finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

Assets leased to customers under agreements which do not transfer substantially all the risks and rewards of ownership are classified as operating leases. When assets are held subject to operating leases, the underlying assets are held at cost less accumulated depreciation, The assets are depreciated down to their estimated residual values on a straight-line basis over the lease term. Lease rental income is recognised on a straight line basis over the lease term.

(b) As a lessee

Rentals made under operating leases are recognised in the Statement of Comprehensive Income on a straight-line basis over the term of the lease.

Leases in which the Group assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Leased assets by way of finance leases are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation. Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

3.19. Cash and cash equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents comprises cash on hand and demand deposits, and cash equivalents are deemed highly liquid investments that are convertible into cash with an insignificant risk of changes in value with a maturity of three months or less at the date of acquisition.

3.20. Employee benefits

(a) Post-retirement obligations

The Group contributes to a defined contribution scheme and to individual defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees.

The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

There are no post-retirement benefits other than pensions.

(b) Share-based compensation

The fair value of equity settled share-based payment awards is calculated at grant date and recognised over the period in which the employees become unconditionally entitled to the awards (the vesting period). The amount is recognised as personnel expenses in the profit and loss, with a corresponding increase in equity. The Group adopts a Black-Scholes valuation model in calculating the fair value of the share options as adjusted for an attrition rate for members of the scheme and a probability of pay-out reflecting the risk of not meeting the terms of the scheme over the vesting period. The number of share options that are expected to vest are reviewed at least annually.

The fair value of cash settled share-based payments is recognised as personnel expenses in the profit or loss with a corresponding increase in liabilities over the vesting period. The liability is remeasured at each reporting date and at settlement date based on the fair value of the options granted, with a corresponding adjustment to personnel expenses.

When share-based payments are changed from equity settled to cash settled and there is no change in the fair value of the replacement award, it is seen as a modification to the terms and conditions on which the equity instruments were granted and is not seen as the settlement and replacement of the instruments. Accordingly, on the date of modification, the Group recognises the entire liability as a reclassification from equity and does not recognise any profit or loss in the Statement of Comprehensive Income.

(c) Deferred cash bonus scheme

The Bank has a deferred cash bonus scheme for senior employees. The cost of the award is recognised to the income statement over the period to which the performance relates.

3.21. Taxation

Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise. Income tax recoverable on tax allowable losses is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits.

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax is not accounted for if it arises from the initial recognition of goodwill, the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the Statement of Financial Position date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, when they intend to settle current tax liabilities and assets on a net basis or the tax assets and liabilities will be realised simultaneously.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

3.22. Issued debt and equity securities

Issued financial instruments or their components are classified as liabilities where the contractual arrangement results in the Group having a present obligation to either deliver cash or another financial asset to the holder, to exchange financial instruments on terms that are potentially unfavourable. Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Company. The components of issued financial instruments that contain both liability and equity elements are accounted for separately with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component.

Financial liabilities, other than trading liabilities at fair value, are carried at amortised cost using the effective interest rate method as set out in policy 3.4. Equity instruments, including share capital, are initially recognised as net proceeds, after deducting transaction costs and any related income tax. Dividend and other payments to equity holders are deducted from equity, net of any related tax.

3.23. Share capital

(a) Share issue costs

Incremental costs directly attributable to the issue of new shares or options or the acquisition of a business by Arbuthnot Banking Group or its subsidiaries, are shown in equity as a deduction, net of tax, from the proceeds.

(b) Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are approved.

(c) Share buybacks

Where any Group company purchases the Company’s equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company’s equity holders until the shares are cancelled or reissued.

3.24. Financial guarantees and loan commitments

Financial guarantees represent undertakings that the Group will meet a customer's obligation to third parties if the customer fails to do so. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. The Group is theoretically exposed to loss in an amount equal to the total guarantees or unused commitments. However, the likely amount of loss is expected to be significantly less; most commitments to extend credit are contingent upon customers maintaining specific credit standards. Liabilities under financial guarantee contracts are initially recorded at their fair value, and the initial fair value is amortised over the life of the financial guarantee. Subsequently, the financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure to settle obligations.

3.25. Fiduciary activities

The Group commonly acts as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

3.26. Provisions and contingent liabilities

Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event, it is probable that an outflow of economic resources will be required from the Group and amounts can be reliably measured.

Onerous contract provisions are recognised for losses on contracts where the forecast costs of fulfilling the contract throughout the contract period exceed the forecast income receivable. In assessing the amount of the loss to provide on any contract, account is taken of the Group's forecast results which the contract is servicing. The provision is calculated based on discounted cash flows to the end of the contract.

Contingent liabilities are disclosed when the Group has a present obligation as a result of a past event, but the probability that it will be required to settle that obligation is more than remote, but not probable.

3.27. New standards and interpretations not yet adopted

The following standards, interpretations and amendments to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 January 2018 or later periods, but the Group has not early adopted them:

IFRS 9, 'Financial instruments' (effective from 1 January 2018).

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments (IFRS 9). IFRS 9 replaces IAS 39 Financial instruments: "Recognition and measurement", and is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. The Group will initially apply IFRS 9 on 1 January 2018. In October 2017, the IASB issued "Prepayment Features with Negative Compensation" (Amendment to IFRS 9). The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted. This Amendment does not have an impact on Group's financial assets' classification and measurement. The Group will take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. The changes in measurement arising on initial application of IFRS 9 will be incorporated through an adjustment to the opening reserves and retained earnings position as at 1 January 2018.

The assessment below is preliminary and not all transition work has been finalised yet. The actual impact of adopting IFRS 9 on 1 January 2018 may change because the Group is still refining its models and methodology for Expected Credit Loss ("ECL") calculations, and revisions of governance and internal controls (including IT systems) required for adoption of IFRS 9 are not yet complete and neither is the testing of these controls. Further, the assumptions, judgements and estimation techniques employed are subject to change until the Bank finalises its first financial statements that include the date of initial application.

<u>i) Classification and Measurement of Financial Assets and Liabilities</u>

There are three measurement classifications under IFRS 9: amortised cost, fair value through profit and loss ("FVTPL") and for financial assets, fair value through other comprehensive income ("FVOCI"). The existing IAS 39 financial asset categories have been removed. Financial assets are classified into these measurement classifications based on the business model within which they are held, and their contractual cash flow characteristics. The business model reflects how groups of financial assets are managed to achieve a particular business objective.

Financial assets can only be held at amortised cost if the instruments are held in order to collect the contractual cash flow ("held to collect") and where those contractual cash flows are solely payments of principal and interest ("SPPI"). Financial asset debt instruments where the business model objectives are achieved by both collecting the contractual cash flows and selling the assets ("held to collect and sell"), are held at FVOCI, with unrealised gains and losses deferred within reserves until the asset is derecognised. All financial assets not classified as measured at amortised cost or FVOCI, as described above, are measured at FVTPL.

The Group has assessed the business models that it operates and most of the loans to banks and customers are held within a "held to collect" business model. Investment debt securities categorised as held-to-maturity under IAS 39 are held within a "held to collect" portfolio. The majority of the remaining investment debt securities are held within a "held to collect and sell" business model or trading portfolio. Where the objective of a business is to hold the assets to collect the contractual cash flows or where the objective is to hold the assets to collect contractual cash flows and sell, a further assessment has been undertaken to determine whether the cash flows of the assets are deemed to meet the SPPI criteria. Where these instruments have cash flows that meet the SPPI criteria, the instruments are measured at amortised cost (for held to collect business models) or FVOCI (for held to collect and sell business models). Instruments that do not meet the SPPI criteria are measured at FVTPL regardless of the business model in which they are held.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities, except for changes in presentation of fair value changes of financial liabilities designated at FVTPL attributable to changes in liability credit risk (under IFRS 9 these changes are presented within other comprehensive income). There has been no change in the way the Group classifies and measures its financial liabilities.

ii) Impairment of Financial Assets, Loan Commitments and Financial Guarantee Contracts

IFRS 9 introduces a new forward-looking ECL impairment framework for all financial assets not measured at FVTPL and certain off-balance sheet loan commitments and guarantees. It replaces the "incurred loss model" from IAS 39. The new ECL framework will result in an allowance for expected credit losses being recorded on financial assets regardless of whether there has been an actual loss event. This differs from the current approach where the allowance recorded on performing loans is designed to capture only losses that have been incurred, whether or not they have been specifically identified. The new impairment model applies to the following financial instruments that are not measured at fair value through profit or loss:

- Financial assets that are debt instruments; and;
- Loan commitments and financial guarantee contracts issued.

The IFRS 9 impairment model adopts a three stage approach based on the extent of credit deterioration since origination:

- Stage 1: 12-month ECL applies to all financial assets that have not experienced a significant increase in credit risk ("SICR") since origination and are not credit impaired. The ECL will be computed based on the probability of default events occurring over the next 12 months. This Stage 1 approach is different from the current approach which estimates a collective allowance to recognise losses that have been incurred but not reported on performing loans.

- Stage 2: When a financial asset experiences a SICR subsequent to origination but is not credit impaired, it is considered to be in Stage 2. This requires the computation of ECL based on the probability of all possible default events occurring over the remaining life of the financial asset. Provisions are higher in this stage because of an increase in credit risk and the impact of a longer time horizon being considered (compared to 12 months in Stage 1).

- Stage 3: Financial assets that exhibit objective evidence of impairment are included in this stage. Similar to Stage 2, the allowance for credit losses will continue to capture the lifetime expected credit losses. At each reporting date, the Group will assess whether financial assets carried at amortised cost are credit impaired. A financial asset will be considered to be credit impaired when an event(s) that has a detrimental impact on estimated future cash flows have occurred. Evidence that a financial asset is credit impaired includes the following observable data:
  - Initiation of bankruptcy proceedings;
  - Notification of bereavement;
  - Identification of loan meeting debt sale criteria; or
  - Initiation of repossession proceedings.

  In addition, a loan that is 90 days or more past due will be considered credit impaired for all portfolios. The credit risk of financial assets that become credit impaired are not expected to improve such that they are no longer considered credit impaired.

The ECL requirements of IFRS 9 are complex and require management judgments, estimates and assumptions, particularly in the areas of assessing whether the credit risk of an instrument has increased significantly since initial recognition and incorporating forward-looking information into the measurement of ECLs.

Under IFRS 9, the Group will consider a financial asset to be in default when:

- The borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising collateral (if any is held); or
- The borrower is more than 90 days past due on any material credit obligation to the Group.

This definition is largely consistent with the definition that is used for the Group's credit risk management process and for regulatory purposes.

Significant increase in credit risk
Under IFRS 9, when determining whether the credit risk (risk of default) on a financial instrument has increased significantly since initial recognition, the Group will consider reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Group's historical experience, expert credit assessment and forward-looking information.

The Group has established a methodology and framework that incorporates both quantitative and qualitative information to determine whether the credit risk on a particular financial instrument has increased significantly since initial recognition and this is aligned to the internal credit risk management process.

The criteria for determining whether credit risk has increased significantly will vary according to the individual circumstances of each loan, given the nature of the loan book, but will also include a backstop based on delinquency of 30 days past due. In certain instances, using its judgement and, where possible, relevant historical experience, the Group may determine that an exposure has undergone a significant increase in credit risk if particular qualitative factors indicate so, as the quantitative analysis may not always capture this on a timely basis.

Measuring ECL
The key inputs to the measurement of ECLs are the following variables:

• Probability of default ("PD");
• Loss given default ("LGD"); and
• Exposure at default ("EAD").

Off-balance sheet items, such as financial guarantees and loan commitments, are included within the ECL computation.

Forward-looking information ("FLI")
IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluating a range of possible outcomes that incorporates forecasts of future economic conditions. FLI is required to be incorporated into the measurement of ECL as well as the determination of whether there has been a significant increase in credit risk since origination. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions. Forecasts for key macroeconomic variables that most closely correlate with the Bank's portfolio are used to produce five economic scenarios, comprising a central case, upside case, downside case, moderate stress and severe stress, and the impacts of these scenarios are then probability weighted. The estimation and application of this forward-looking information will require significant judgement. External information is used to produce the forecast information.

iii) Hedge Accounting
IFRS 9 introduces a new hedge accounting model that expands the scope of hedged items and risks eligible for hedge accounting and aligns hedge accounting more closely with risk management. The new model no longer specifies quantitative measures for effectiveness testing and does not permit hedge de-designation.

iv) Transitional impact, including impact on capital
The Group will record an adjustment to its opening retained earnings as at 1 January 2018 to reflect the application of the new requirements at the adoption date and will not restate comparative periods. The Group estimates the IFRS 9 transition amount will reduce shareholders' equity by between £2.4m and £3.2m before tax as at 1 January 2018.

Under IFRS 9, it is estimated that the Group's CET1 ratio would reduce by approximately 2 basis points after transitional relief (between 26 and 35 basis points before transitional relief). This is mainly driven by the increase in IFRS 9 ECL for standardised portfolios that directly impacts CET1 as there is no regulatory deduction to absorb the increase.

CET 1 ratio:
• 17.29% under IAS 39 at 31 December 2017;
• Between 16.93% and 17.03% under IFRS 9 at 1 January 2018 before transitional relief;
• 17.27% under IFRS 9 at 1 January 2018 after transitional relief.

Transitional relief relates to the phasing of the impact of the initial adoption of ECL as permitted by Regulation (EU) 2017/2395 of the European Parliament and Council. The Group is planning to adopt the transitional relief. Under this approach, the balance of ECL allowances in excess of the regulatory excess EL and standardised portfolios are phased into the CET1 capital base over 5 years. The proportion phased in for the balance at each reporting period is 2018: 5%; 2019 15%; 2020 30%; 2021 50%; 2022 75%. From 2023 onwards, there is no transitional relief.

v) Impact on Governance and Controls

The Group plans to apply its existing governance framework to ensure that appropriate controls and validations are in place over key processes and judgments to determine the ECL. As part of the implementation, the Group is in the process of refining existing internal controls and implementing new controls where required in areas that are impacted by IFRS 9, including controls over the development and probability weighting of macroeconomic scenarios, credit risk data and systems, and the determination of a significant increase in credit risk.

IFRS 15, 'Revenue from contracts with customers' (effective 1 January 2017).

This standard replaces IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfer of Assets from Customers and SIC-31 Revenue – Barter of Transactions Involving Advertising Services. IFRS 15 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted.

The standard contains a single model that applies to contracts with customers and two approaches to recognising revenue: at a point in time or over time. The model features a contract-based five step analysis of transactions to determine whether, how much and when revenue is recognised. IFRS 15 is not expected to have a significant impact on the Group, but further analysis is continuing.

IFRS 16, 'Leases' (effective from 1 January 2019).

This standard sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e the customer ('lessee') and the supplier ('lessor'). IFRS 16 eliminates the classification of leases as required by IAS 17 and introduces a single lease accounting model. Applying that model, a lessee is required to recognise:

• Assets and liabilities for leases with a term of more than 12 months, unless the underlying asset is of low value;
• Depreciation of lease assets separately from interest on lease liabilities in profit or loss.

The standard is effective for annual periods beginning on or after 1 January 2019. The Group is currently in the process of assessing the impact that the initial application would have on its business and will adopt the standard for the year ending 31 December 2019.

4. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

4.1 Estimation uncertainty

(a) Credit losses

The Group reviews its loan portfolios and held-to-maturity investments to assess impairment at least on a quarterly basis. The basis for evaluating impairment losses is described in accounting policy 3.10. Where financial assets are individually evaluated for impairment, management uses its best estimates in calculating the net present value of future cash flows. Management has to make judgements on the financial position of the counterparty and the net realisable value of collateral (where held), in determining the expected future cash flows.

The recoverable amount is typically dependent on the sale of the collateral. The amount recoverable is determined with reference to:

• The property valuation, which is typically updated every 12 months.
• The time taken to realise the sale proceeds (UK property is assumed to take 12 months and Non-UK property 24 months).
• The property marketing costs (UK property is assumed to be at 3% of property value and Non-UK at 7%).
• The legal costs of sale (UK legal sales costs are assumed to be £5k, whilst Non-UK are assumed to be €10k).

Any change in timing of estimated future cash flows (other than impairment) will adjust carrying value with gain or loss in profit or loss. The revised carrying amount will be recalculated by discounting the revised estimated future cash flows at the loan's original effective interest rate.

A sensitivity analyses was done on the two main assumptions used to calculate the recoverable amount and therefore the impairments required:

• If the value of the collateral increased or decreased by 10%, impairments would decrease or increase by £1.6m (2016: £1.7m);
• If the time taken to sell the properties were increased or decreased by 12 months, impairments would increase or decrease by £0.8m (2016: £0.8m).

In determining whether an impairment loss should be recorded in the Statement of Comprehensive Income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans or held-to-maturity investments with similar credit characteristics, before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

In assessing collective impairment the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be significantly different to historic trends. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

(b) Effective Interest Rate
Acquired loan books are initially recognised at fair value. Subsequently they are measured under the effective interest rate method, based on cash flow models which require significant judgement assumptions on prepayment rates, late payments, the probability and timing of defaults and the amount of incurred losses. Management review the expected cash flows against actual cash flows to ensure future assumptions on customer behaviour and future cash flows remain valid. If the estimates of future cash flows are revised, the adjustment to the carrying value of the loan book is recognised in the Statement of Comprehensive Income.

If the acquired loan books were modelled to repay 6 months earlier, it would increase interest income in 2017 by £0.3m (2016: £0.1m), while a 10% increase in credit losses would reduce interest income in 2017 by £0.2m (2016: £0.3m), both as a result of AG8 adjustments.

IAS 39 requires interest earned from lending to be measured under the effective interest rate method. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset.

Management must therefore use judgement to estimate the expected life of each instrument. The accuracy of the effective interest rate would therefore be affected by unexpected market movements resulting in altered customer behaviour, inaccuracies in the models used compared to actual outcomes and incorrect assumptions.

If customer loans repaid 6 months earlier than anticipated, interest income would increase by £0.3m (2016: £0.3m).

(c) Investment property
The valuations that the Group places on its investment properties are subject to a degree of uncertainty and are calculated on the basis of assumptions in relation to prevailing market rents and effective yields. These assumptions may not prove to be accurate, particularly in periods of market volatility. The Group currently owns two investment properties, as outlined in Note 31.

The King Street property is currently fully tenanted, with the main lease ending in 2019 at which point the offices will be refurbished and re-let at prevailing market rents. The valuation model considers the net present value of net cash flows to be generated from the property, taking into account expected rental growth rate, void periods, occupancy rate, lease incentive costs such as rent-free periods and other costs not paid by tenants. The expected net cash flows are discounted using risk-adjusted discount rates. Among other factors, the discount rate estimation considers the quality of a building and its location, tenant quality and lease terms. Management judgement is required for significant unobservable inputs used in the discounted cash flow model, which have been assessed as follows:

• refurbishment period: 6 months
• void period after refurbishment: 6 months
• rent free period: 18 months
• estimated refurbishment costs: £2.4m
• yield rate: 4%
• expected rental income uplift following re-let: 15%

If the discount rate went up by 25bps, there would be a reduction in fair value of £4.8m, while a decrease in the discount rate would have a positive fair value impact through the Profit or Loss of £4.0m. If the expected rental uplift following the re-let of the building is reduced to 10%, there would be a reduction in fair value through the Profit or Loss of £2.4m, while an increase in the rental uplift to 20%, would have a positive fair value impact through the Profit or Loss of £2.2m.

The St Philips Place property was acquired on 24 November 2017. As the property was bought shortly before the year end, the cost of acquisition is considered to remain a good estimate of fair value.

(d) Acquisition accounting
The Group recognises identifiable assets and liabilities at their acquisition date fair values. The exercise of attributing a fair value to the balance sheet of the acquired entity requires the use of a number of assumptions and estimates, which are documented at the time of the acquisition. These fair value adjustments are determined from the estimated future cash flows generated by the assets.

Loans and advances to customers
The methodology of attributing a fair value to the loans and advances to customers involves discounting the estimated future cash flows, using a risk adjusted market rate discount factor. A fair value adjustment is then applied to the carrying value in the acquirers balance sheet.

Intangible assets
Identifying the separately identifiable intangible assets of an acquired company is subjective and based upon discussions with management and a review of relevant documentation. During the year, there were three separately identifiable intangible assets which met the criteria for separation from goodwill, these being Customer Relationships, Broker Relationships and Brand.

Customer Relationships are valued through the application of a discounted cash flow methodology to net anticipated renewal revenues. The valuation of Broker Relationships is derived from a costs avoided methodology, by reviewing costs incurred on non-broker platforms versus costs which are incurred in broker commission. The Brand is valued considering a market participant's view on the likely period over which it might be utilised, and its fair value was estimated using the relief from royalty methodology.

In calculating the fair value of the assets and liabilities acquired, management judgement is required as discussed above, in particular for the discount rate applied to the economic life of the intangibles assets of £2.3m. A 1% movement in the discount rate applied, would result in a £0.06m increase or decrease in the intangible recognised with an equal and opposite increase or decrease in goodwill on acquisition.

(e) Impairment review of interest in associate
The Group has an 18.6% interest in STB. This is currently recorded in the Group's balance sheet as an interest in associates and at 31 December 2017 was carried at £83.8m or the equivalent of £24.33 per share. At the year end the market price of STB was £17.97 per share. The Board have determined that the current carrying value remains appropriate after having carried out extensive analysis to be satisfied that the long term value in use does not suggest that this carrying value is impaired. These valuations included the Gordon's Growth model and Dividend Discount model. The resultant output from the models indicated valuations in a range that was in excess of £24 per share, but this will be ultimately dependent on the surplus capital within STB being deployed in the business over the long term.

Various judgements were made in the application of the models used. The following sensitivity analyses were also done on the assumptions used in the two main models used:

Gordon's Growth Model
- 1% change in return on equity would change the calculated valuation by £2.77 per share
- 1% change in cost of equity/discount factor would change the calculated valuation by £6.92 per share
- 0.5% change in GDP would change the calculated valuation by £1.54 per share

Dividend Discount Model
- 1% change in cost of equity/discount factor would change the calculated valuation by £3.38 per share
- 10% change in earnings/dividend growth would change the calculated valuation by £2.11 per share

Based on the current output of the valuation models, reviewing sensitivity analyses on assumptions applied in the models and taking into account the current market consensus on the shares, the Board is satisfied that the current carrying value remains appropriate.

There is a risk that the output of the value in use models could require an impairment charge to be recognised in the future.

If the Group was considered to no longer have significant influence over STB it would lead to the investment being accounted for as a financial asset at fair value. The value would then be marked to market with changes in the share price giving rise to gains or losses being recorded in Other Comprehensive Income or Profit or Loss – see Note 3.8(d) and Note 3.10(b).

4.2 Judgements
(a) Valuation of financial instruments
The Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions. If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis. The objective of valuation techniques is to determine the fair value of the

financial instrument at the reporting date as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. In the event that fair values of assets and liabilities cannot be reliably measured, they are carried at cost.

The Group measures fair value using the following fair value hierarchy that reflects the significance of the inputs used in making measurements:

- Level 1: Quoted prices in active markets for identical assets or liabilities.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads assists in the judgement as to whether a market is active. If in the opinion of management, a significant proportion of the instrument's carrying amount is driven by unobservable inputs, the instrument in its entirety is classified as valued using significant unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the level at which an arm's length transaction would be likely to occur. It generally does not mean that there is no market data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

The tables below analyse financial instruments measured at fair value by the level in the fair value hierarchy into which the measurement is categorised:

At 31 December 2017	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	2,551	-	2,551
Financial investments	144	-	2,203	2,347
	144	**2,551**	**2,203**	**4,898**
LIABILITIES				
Derivative financial instruments	-	931	-	931
	-	**931**	-	**931**

At 31 December 2016	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Derivative financial instruments	-	1,516	-	1,516
Financial investments	133	-	2,012	2,145
	133	**1,516**	**2,012**	**3,661**
LIABILITIES				
Derivative financial instruments	-	227	-	227
	-	**227**	-	**227**

There were no transfers between level 1 and level 2 during the year.

The following table reconciles the movement in level 3 financial instruments measured at fair value (financial investments) during the year:

Movement in level 3	2017 £000	2016 £000
At 1 January	2,012	2,548
Consideration received	-	494
Disposals	-	(1,310)
Movements recognised in Other Comprehensive Income	136	75
Movements recognised in the Income Statement	55	205
At 31 December	**2,203**	**2,012**

Visa Inc. investment
Arbuthnot Latham currently holds preference shares in Visa Inc., valued at £706k as at 31 December 2017. The valuation includes a 31 % haircut, comprising 25% due to a contingent liability disclosed in Visa Europe's accounts in relation to litigation and 6% based on a liquidity discount.

A 5% increase in valuation would lead to a 35k increase in the gain through Other Comprehensive Income. A 5% decrease would lead to a £35k decrease in the gain through Other Comprehensive Income.

Investment in overseas property company
For those financial investments measured at fair value, the Group uses proprietary valuation models which are developed from recognised valuation techniques. Some or all of the significant inputs into these models may not be observable in the market. Valuation models that employ significant unobservable inputs require a higher degree of management judgement and estimation in the determination of fair value.

The Group has established a valuation methodology for measuring level 3 financial investments which are categorised as available for sale. Unobservable inputs used include: yield of 4.60% (2016: 4.90%) and occupancy rates of 90.0% (2016: 95.3%). These inputs are taken from online real estate reports available from BNP Paribas. The inputs are stressed to ensure that the fair value is robust. Increases in the yield or decreases in annual rental value or occupancy rate would result in lower fair values (an increase in yield by 0.5% would lead to a decrease in fair value of £126k). Another indicator of appropriate fair value would be if a reasonable offer were to be made on the value of the property. Management analyse and investigate any significant movements in the unobservable inputs which impact the valuation of level 3 instruments.

The tables below analyse financial instruments not measured at fair value by the level in the fair value hierarchy:

At 31 December 2017	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	313,101	-	313,101
Loans and advances to banks	-	70,679	-	70,679
Debt securities held-to-maturity	-	227,019	-	227,019
Loans and advances to customers	-	-	1,049,269	1,049,269
Other assets	-	-	11,964	11,964
	-	**610,799**	**1,061,233**	**1,672,032**
LIABILITIES				
Deposits from banks	-	195,097	-	195,097
Deposits from customers	-	1,390,781	-	1,390,781
Other liabilities	-	-	1,207	1,207
Debt securities in issue	-	-	13,104	13,104
	-	**1,585,878**	**14,311**	**1,600,189**

At 31 December 2016	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
ASSETS				
Cash and balances at central banks	-	195,752	-	195,752
Loans and advances to banks	-	36,951	-	36,951
Debt securities held-to-maturity	-	107,300	-	107,300
Loans and advances to customers	-	42,691	716,108	758,799
Other assets	-	-	1,197	1,197
	-	**382,694**	**717,305**	**1,099,999**
LIABILITIES				
Deposits from banks	-	3,200	-	3,200
Deposits from customers	-	997,649	-	997,649
Other liabilities	-	-	1,812	1,812
Debt securities in issue	-	-	12,621	12,621
	-	**1,000,849**	**14,433**	**1,015,282**

(b) Associate accounting

An associate is an entity over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture. It is presumed that the investor does not have significant influence if it has less than 20% of the voting power of the investee, unless proven otherwise. ABG holds 18.64% of the voting power of STB, but has retained Board representation (two directors out of eight) and as a result the Board believes ABG has significant influence. The interest in STB is therefore accounted for as an associate.

If significant influence is lost, the shareholding will be accounted for as an available-for-sale financial investment.

5. Maturity analysis of assets and liabilities

The table below shows the maturity analysis of assets and liabilities of the Group as at 31 December 2017:

At 31 December 2017	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash	313,101	-	313,101
Loans and advances to banks	70,679	-	70,679
Debt securities held-to-maturity	122,236	104,783	227,019
Assets classified as held for sale	2,915	-	2,915
Derivative financial instruments	950	1,601	2,551
Loans and advances to customers	224,954	824,315	1,049,269
Other assets	16,188	4,436	20,624
Financial investments	128	2,219	2,347
Deferred tax asset	-	1,527	1,527
Interests in associates	-	83,804	83,804
Intangible assets	-	15,995	15,995
Property, plant and equipment	-	3,962	3,962
Investment property	-	59,439	59,439
	751,151	**1,102,081**	**1,853,232**
LIABILITIES			
Deposits from banks	195,097	-	195,097
Derivative financial instruments	931	-	931
Deposits from customers	1,333,423	57,358	1,390,781
Current tax liability	705	-	705
Other liabilities	16,239	-	16,239
Debt securities in issue	-	13,104	13,104
	1,546,395	**70,462**	**1,616,857**

The table below shows the maturity analysis of assets and liabilities of the Group as at 31 December 2016:

At 31 December 2016	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash	195,752	-	195,752
Loans and advances to banks	36,951	-	36,951
Debt securities held-to-maturity	85,782	21,518	107,300
Derivative financial instruments	85	1,431	1,516
Loans and advances to customers	337,376	421,423	758,799
Other assets	7,708	4,231	11,939
Financial investments	-	2,145	2,145
Deferred tax asset	-	1,665	1,665
Investment in associate	900	81,674	82,574
Intangible assets	-	8,522	8,522
Property, plant and equipment	-	4,782	4,782
Investment property	-	53,339	53,339
	664,554	**600,730**	**1,265,284**
LIABILITIES			
Deposits from banks	3,200	-	3,200
Derivative financial instruments	227	-	227
Deposits from customers	906,083	91,566	997,649
Current tax liability	147	-	147
Other liabilities	17,082	-	17,082
Debt securities in issue	-	12,621	12,621
	926,739	**104,187**	**1,030,926**

The table below shows the maturity analysis of assets and liabilities of the Company as at 31 December 2017:

At 31 December 2017	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Loans and advances to banks	6	-	6
Loans and advances to banks - due from subsidiary undertakings	36,097	-	36,097
Financial investments	128	12	140
Deferred tax asset	-	641	641
Property, plant and equipment	-	157	157
Other assets	199	-	199
Interests in associates	-	5,056	5,056
Interests in subsidiaries		97,802	97,802
	36,430	**103,668**	**140,098**
LIABILITIES			
Current tax liability	152	-	152
Other liabilities	3,141	-	3,141
Debt securities in issue	-	13,104	13,104
	3,293	**13,104**	**16,397**

The table below shows the maturity analysis of assets and liabilities of the Company as at 31 December 2016:

At 31 December 2016	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Loans and advances to banks	6	-	6
Loans and advances to banks - due from subsidiary undertakings	89,066	-	89,066
Financial investments	-	121	121
Deferred tax asset	-	397	397
Property, plant and equipment	-	183	183
Other assets	254	633	887
Interests in associates	-	5,056	5,056
Interests in subsidiaries	-	54,602	54,602
	89,326	**60,992**	**150,318**
LIABILITIES			
Other liabilities	4,808	-	4,808
Debt securities in issue	-	12,621	12,621
	4,808	**12,621**	**17,429**

6. Financial risk management

Strategy

By their nature, the Group's activities are principally related to the use of financial instruments. The Directors and senior management of the Group have formally adopted a Group Risk and Controls Policy which sets out the Board's attitude to risk and internal controls. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board, in addition to which key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

The principal non-operational risks inherent in the Group's business are credit, market and liquidity risks.

(a) Credit risk

The Company and Group take on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment provisions are provided for losses that have been incurred at the balance sheet date. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration in the Company and Group's portfolio, could result in losses that are different from those provided for at the balance sheet date. Credit risk is managed through the Credit Committee of the banking subsidiary.

The Company and Group structure the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to products, and one borrower or groups of borrowers. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. The limits are approved periodically by the Board of Directors and actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral, and corporate and personal guarantees.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of collateral to secure advances, which is common practice. The principal collateral types for loans and advances include, but are not limited to:

- Charges over residential and commercial properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities;
- Charges over other chattels; and
- Personal guarantees

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In order to minimise any potential credit loss the Group will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances. Repossessed collateral, not readily convertible into cash, is made available for sale in an orderly fashion, with the proceeds used to reduce or repay the outstanding indebtedness, or held as inventory where the Group intends to develop and sell in the future. Where excess funds are available after the debt has been repaid, they are available either for other secured lenders with lower priority or are returned to the customer.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

The Group's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

	2017	2016
	£000	£000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Cash and balances at central banks	313,101	195,752
Loans and advances to banks	70,679	36,951
Debt securities held-to-maturity	227,019	107,300
Derivative financial instruments	2,551	1,516
Loans and advances to customers	1,049,269	758,799
Other assets	11,964	1,197
Financial investments	2,347	2,145
Credit risk exposures relating to off-balance sheet assets are as follows:		
Guarantees	2,976	274
Loan commitments and other credit related liabilities	131,963	54,934
At 31 December	**1,811,869**	**1,158,868**

The Company's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

	2017	2016
	£000	£000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Loans and advances to banks	36,103	89,072
Financial investments	140	121
Other assets	162	791
At 31 December	**36,405**	**89,984**

The above tables represent the maximum credit risk exposure (net of impairment) to the Group and Company at 31 December 2017 and 2016 without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures are based on the net carrying amounts as reported in the Statement of Financial Position.

The table below represents an analysis of the loan to values of the exposures secured by property for the Group:

	31 December 2017		31 December 2016	
	Loan Balance	Collateral	Loan Balance	Collateral
Loan to value	£000	£000	£000	£000
Less than 60%	455,398	1,108,363	438,076	1,219,532
60% - 80%	343,864	524,256	167,765	253,550
80% - 100%	69,826	80,998	76,289	88,598
Greater than 100%*	45,242	34,354	32,022	21,387
Total	**914,330**	**1,747,971**	**714,152**	**1,583,067**

*In addition to property, other security is taken, including charges over Arbuthnot Latham Investment Management portfolios, other chattels and personal guarantees.

Property valuations used are those from the loan origination date or updated 3rd party valuations where applicable.

The table below represents an analysis of loan commitments compared to the values of properties for the Group:

	31 December 2017		31 December 2016	
	Committed	Collateral	Committed	Collateral
Loan commitments and other credit related liabilities	£000	£000	£000	£000
Less than 60%	62,775	274,643	26,988	73,659
60% - 80%	26,340	38,796	23,940	42,102
80% - 100%	29,579	32,737	-	-
Greater than 100%	5,090	4,104	-	-
Total	**123,784**	**350,280**	**50,928**	**115,761**

Renegotiated loans and forbearance

The contractual terms of a loan may be modified due to factors that are not related to the current or potential credit deterioration of the customer (changing market conditions, customer retention, etc.). In such cases, the modified loan may be derecognised and the renegotiated loan recognised as a new loan at fair value.

As at 31 December 2017, loans for which forbearance measures were in place totalled 0.13% (2016: 0.50%) of total loans to customers for the Group. These are set out in the following table:

	2017		2016	
	Number	Loan Balance £000	Number	Loan Balance £000
Transfer to interest only	-	-	3	115
Interest temporarily not being charged	-	-	1	3,607
Long term extension	1	84	-	-
Payment holiday	5	1,237	1	78
Total forbearance	**6**	**1,321**	**5**	**3,800**

Concentration risk

The Group is well diversified in the UK, being exposed to retail banking, private banking and commercial banking. Management assesses the potential concentration risk from a number of areas including:

- Product concentration;
- Geographical concentration; and
- High value residential properties.

Due to the well diversified nature of the Group and the significant collateral held against the loan book, the Directors do not consider there to be a potential material exposure arising from concentration risk.

The tables below show the concentration in the loan book based on the most significant type of collateral held for each loan. Where multiple types of collateral are held with no significant majority, the loan is shown within “mixed collateral”.

	Loans and advances to customers		Loan Commitments	
	2017	2016	2017	2016
	£000	£000	£000	£000
Concentration by product				
Cash collateralised	17,747	5,245	-	-
Commercial Lending	202,912	71,674	24,371	18,260
Asset finance	71,425	-	-	-
Residential mortgages	633,003	626,751	99,413	32,668
Investment portfolio secured	49,667	34,014	4,222	4,006
Non-Performing	-	15,953	-	-
Other Collateral	70,954	2,103	3,957	-
Unsecured	3,561	3,059	-	-
At 31 December	**1,049,269**	**758,799**	**131,963**	**54,934**
Concentration by location				
East Anglia	18,438	2,714	-	-
East Midlands	-	7,245	-	-
London	407,805	422,901	56,777	27,161
Midlands	42,484	3,800	800	-
North East	25,741	2,100	-	-
North West	44,630	14,288	825	4,590
Northern Ireland	2,903	-	-	-
Scotland	10,988	13,410	-	-
South East	203,305	117,805	23,462	12,560
South West	116,692	89,018	15,236	3,468
Wales	8,002	7,460	-	-
West Midlands	-	14,436	-	108
Yorkshire & Humber	-	6,398	-	-
Overseas	21,556	20,136	-	-
Other	146,725	37,088	34,863	7,047
At 31 December	**1,049,269**	**758,799**	**131,963**	**54,934**

Commercial lending and Mixed collateral reflect the growth in the Commercial bank. All non-property loans are disclosed in “Other” in the concentration by location table above.

(b) Operational risk (unaudited)

The Group's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness and to avoid control procedures that restrict initiatives and creativity. Operational risk arises from all of the Group's operations.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the senior management within each subsidiary.

Compliance with Group standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of the Internal Audit reviews are discussed with senior management, with summaries submitted to the Arbuthnot Banking Group Audit Committee.

(c) Market risk

Price risk

The Company and Group are exposed to price risk from equity investments and derivatives held by the Group and classified in the Consolidated Statement of Financial Position either as available-for-sale or at fair value through the profit and loss. The Group is not exposed to commodity price risk.

Based upon the financial investment exposure in Note 25, a stress test scenario of a 10% (2016: 10%) decline in market prices, with all other things being equal, would result in a £32,000 (2016: £11,000) decrease in the Group's income and a decrease of £231,000 (2016: £172,000) in the Group's equity. The Group considers a 10% stress test scenario appropriate after taking the current values and historic data into account.

Based upon the financial investment exposure given in Note 25, a stress test scenario of a 10% (2016: 10%) decline in market prices, with all other things being equal, would result in a £13,000 (2016: £11,000) decrease in the Company's income and a decrease of £11,000 (2016: £10,000) in the Company's equity.

Currency risk

The Company and Group take on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. This is managed through the Group entering into forward foreign exchange contracts. The Board sets limits on the level of exposure for both overnight and intra-day positions, which are monitored daily. The table below summarises the Group's exposure to foreign currency exchange rate risk at 31 December 2017. Included in the table below are the Group's assets and liabilities at carrying amounts, categorised by currency.

At 31 December 2017	GBP (£) £000	USD ($) £000	Euro (€) £000	Other £000	Total £000
ASSETS					
Cash and balances at central banks	313,101	-	-	-	313,101
Loans and advances to banks	6,027	40,870	16,944	6,838	70,679
Debt securities held-to-maturity	170,723	56,296	-	-	227,019
Derivative financial instruments	2,525	1	25	-	2,551
Loans and advances to customers	997,025	14,912	37,332	-	1,049,269
Other assets	11,964	-	-	-	11,964
Financial investments	140	706	1,501	-	2,347
	1,501,505	**112,785**	**55,802**	**6,838**	**1,676,930**
LIABILITIES					
Deposits from banks	195,067	-	-	30	195,097
Derivative financial instruments	914	1	-	16	931
Deposits from customers	1,228,878	112,731	42,733	6,439	1,390,781
Other liabilities	1,207	-	-	-	1,207
Debt securities in issue	-	-	13,104	-	13,104
	1,426,066	**112,732**	**55,837**	**6,485**	**1,601,120**
Net on-balance sheet position	**75,439**	**53**	**(35)**	**353**	**75,810**
Credit commitments	131,963	-	-	-	131,963

The table below summarises the Group's exposure to foreign currency exchange risk at 31 December 2016:

At 31 December 2016	GBP (£) £000	USD ($) £000	Euro (€) £000	Other £000	Total £000
ASSETS					
Cash and balances at central banks	195,669	35	40	8	195,752
Loans and advances to banks	2,197	24,494	5,062	5,198	36,951
Debt securities held-to-maturity	94,299	13,001	-	-	107,300
Derivative financial instruments	1,516	-	-	-	1,516
Loans and advances to customers	701,165	21,927	35,707	-	758,799
Other assets	1,197	-	-	-	1,197
Financial investments	120	569	1,456	-	2,145
	996,163	**60,026**	**42,265**	**5,206**	**1,103,660**
LIABILITIES					
Deposits from banks	3,198	-	-	2	3,200
Derivative financial instruments	227	-	-	-	227
Deposits from customers	903,687	59,916	28,535	5,511	997,649
Other liabilities	1,812	-	-	-	1,812
Debt securities in issue	-	-	12,621	-	12,621
	908,924	**59,916**	**41,156**	**5,513**	**1,015,509**
Net on-balance sheet position	**87,239**	**110**	**1,109**	**(307)**	**88,151**
Credit commitments	54,934	-	-	-	54,934

A 10% strengthening of the pound against the US dollar would lead to a £5,000 increase (2016: £3,000 increase) in Group profits and equity, while a 10% weakening of the pound against the US dollar would lead to the same decrease in Group profits and equity. Similarly, a 10% strengthening of the pound against the Euro would lead to a £4,000 increase (2016: £6,000 increase) in Group profits and equity, while a 10% weakening of the pound against the Euro would lead to the same increase in Group profits and equity. The above results are after taking into account the effect of derivative financial instruments (see Note 21), which cover most of the net exposure in each currency.

The table below summarises the Company's exposure to foreign currency exchange rate risk at 31 December 2017:

At 31 December 2017	GBP (£) £000	Euro (€) £000	Total £000
ASSETS			
Loans and advances to banks	22,734	13,369	36,103
Financial investments	140	-	140
Other assets	162	-	162
	23,036	**13,369**	**36,405**
LIABILITIES			
Other liabilities	1,840	-	1,840
Debt securities in issue	-	13,104	13,104
	1,840	**13,104**	**14,944**
Net on-balance sheet position	**21,196**	**265**	**21,461**

The table below summarises the Company's exposure to foreign currency exchange rate risk at 31 December 2016:

	GBP (£)	Euro (€)	Total
At 31 December 2016	£000	£000	£000
ASSETS			
Loans and advances to banks	76,037	13,035	89,072
Financial investments	121	-	121
Other assets	791	-	791
	76,949	**13,035**	**89,984**
LIABILITIES			
Other liabilities	3,624	-	3,624
Debt securities in issue	-	12,621	12,621
	3,624	**12,621**	**16,245**
Net on-balance sheet position	**73,325**	**414**	**73,739**

A 10% strengthening of the pound against the Euro would lead to £3,000 (2016: £41,000) decrease in the Company profits and equity, conversely a 10% weakening of the pound against the Euro would lead to the same increase in the Company profits and equity.

Interest rate risk

Interest rate risk is the potential adverse impact on the Company and Group's future cash flows from changes in interest rates, and arises from the differing interest rate risk characteristics of the Company and Group's assets and liabilities. In particular, fixed rate savings and borrowing products expose the Group to the risk that a change in interest rates could cause either a reduction in interest income or an increase in interest expense relative to variable rate interest flows. The Group seeks to "match" interest rate risk on either side of the Statement of Financial Position. However, this is not a perfect match and interest rate risk is present in: Money market transactions of a fixed rate nature, fixed rate loans and fixed rate savings accounts. There is interest rate mismatch in Arbuthnot Latham. Interest rate risk is measured throughout the maturity bandings of the book on a parallel shift scenario for a 200 basis points movement. Interest rate risk is managed to limit value at risk to be less than £1m. The current position of the balance sheet is such that it results in a favourable impact on the economic value of equity of £0.8m (2016: £2.0m) for a positive 200bps shift and an adverse impact of £0.8m (2016: £0.5m) for a negative 200bps movement capped at the Bank of England base rate (50bps). The Company has no fixed rate exposures, but an upward change of 50bps on variable rates would increase pre-tax profits and equity by £10,000 (2016: increase pre-tax profits and equity by £7,000).

The following tables summarise the re-pricing periods for the assets and liabilities in the Company and Group, including derivative financial instruments which are principally used to reduce exposure to interest rate risk. Items are allocated to time bands by reference to the earlier of the next contractual interest rate re-price and the maturity date.

Group **As at 31 December 2017**	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Cash and balances at central banks	313,101	-	-	-	-	-	313,101
Loans and advances to banks	61,211	579	8,889	-	-	-	70,679
Debt securities held-to-maturity	185,926	35,093	6,000	-	-	-	227,019
Derivative financial instruments	950	-	-	1,601	-	-	2,551
Loans and advances to customers	880,822	6,938	10,774	143,979	-	6,756	1,049,269
Other assets	-	-	-	-	-	188,266	188,266
Financial investments	-	-	-	-	-	2,347	2,347
	1,442,010	**42,610**	**25,663**	**145,580**	**-**	**197,369**	**1,853,232**
LIABILITIES							
Deposits from banks	195,097	-	-	-	-	-	195,097
Derivative financial instruments	931	-	-	-	-	-	931
Deposits from customers	1,061,442	162,503	109,478	57,358	-	-	1,390,781
Other liabilities	-	-	-	-	-	16,944	16,944
Debt securities in issue	13,104	-	-	-	-	-	13,104
Equity	-	-	-	-	-	236,375	236,375
	1,270,574	**162,503**	**109,478**	**57,358**	**-**	**253,319**	**1,853,232**
Interest rate sensitivity gap	**171,436**	**(119,893)**	**(83,815)**	**88,222**	**-**	**(55,950)**	
Cumulative gap	**171,436**	**51,543**	**(32,272)**	**55,950**	**55,950**	**-**	

Group **As at 31 December 2016**	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Cash and balances at central banks	195,752	-	-	-	-	-	195,752
Loans and advances to banks	36,951	-	-	-	-	-	36,951
Debt securities held-to-maturity	78,994	6,813	21,493	-	-	-	107,300
Derivative financial instruments	85	-	-	1,431	-	-	1,516
Loans and advances to customers	624,468	120,311	8,755	5,265	-	-	758,799
Other assets	-	-	-	-	-	162,821	162,821
Financial investments	-	-	-	-	-	2,145	2,145
	936,250	**127,124**	**30,248**	**6,696**	**-**	**164,966**	**1,265,284**
LIABILITIES							
Deposits from banks	3,200	-	-	-	-	-	3,200
Derivative financial instruments	227	-	-	-	-	-	227
Deposits from customers	813,047	61,519	84,480	38,603	-	-	997,649
Other liabilities	-	-	-	-	-	17,229	17,229
Debt securities in issue	12,621	-	-	-	-	-	12,621
Equity	-	-	-	-	-	234,358	234,358
	829,095	**61,519**	**84,480**	**38,603**	**-**	**251,587**	**1,265,284**
Impact of derivative instruments	3,800	(3,800)	-	-	-	-	
Interest rate sensitivity gap	**110,955**	**61,805**	**(54,232)**	**(31,907)**	**-**	**(86,621)**	
Cumulative gap	**110,955**	**172,760**	**118,528**	**86,621**	**86,621**	**-**	

Company **As at 31 December 2017**	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Loans and advances to banks	35,944	-	-	-	-	159	36,103
Other assets	-	-	-	-	-	103,855	103,855
Financial investments	-	-	-	-	-	140	140
	35,944	-	-	-	-	**104,154**	**140,098**
LIABILITIES							
Other liabilities	-	-	-	-	-	3,293	3,293
Debt securities in issue	13,104	-	-	-	-	-	13,104
Equity	-	-	-	-	-	123,701	123,701
	13,104	-	-	-	-	**126,994**	**140,098**
Interest rate sensitivity gap	**22,840**	-	-	-	-	**(22,840)**	
Cumulative gap	**22,840**	**22,840**	**22,840**	**22,840**	**22,840**	-	

Company **As at 31 December 2016**	Within 3 months £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000	Non interest bearing £000	Total £000
ASSETS							
Loans and advances to banks	88,914	-	-	-	-	158	89,072
Other assets	-	-	-	-	-	61,125	61,125
Financial investments	-	-	-	-	-	121	121
	88,914	-	-	-	-	**61,404**	**150,318**
LIABILITIES							
Other liabilities	-	-	-	-	-	4,808	4,808
Debt securities in issue	12,621	-	-	-	-	-	12,621
Equity	-	-	-	-	-	132,889	132,889
	12,621	-	-	-	-	**137,697**	**150,318**
Interest rate sensitivity gap	**76,293**	-	-	-	-	**(76,293)**	
Cumulative gap	**76,293**	**76,293**	**76,293**	**76,293**	**76,293**	-	

(d) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. The liquidity requirements of the Group are met through withdrawing funds from its Bank of England Reserve Account to cover any short-term fluctuations and longer term funding to address any structural liquidity requirements.

The Group has formal governance structures in place to manage and mitigate liquidity risk on a day to day basis. The Board of AL sets and approves the liquidity risk management strategy. The Assets and Liabilities Committee ("ALCO"), comprising senior executives of the Group, monitors liquidity risk. Key liquidity risk management information is reported by the finance teams and monitored by the Chief Executive Officer and Finance Director on a daily basis. The ALCO meets monthly to review liquidity risk against set thresholds and risk indicators including early warning indicators, liquidity risk tolerance levels and Individual Liquidity Adequacy Assessment Process ("ILAAP") metrics.

The PRA requires the Board to ensure that the Group has adequate levels of liquidity resources and a prudent funding profile, and that it comprehensively manages and controls liquidity and funding risks. The Group maintains deposits placed at the Bank of England, and highly liquid unencumbered assets that can be called upon to create sufficient liquidity to meet liabilities on demand, particularly in a period of liquidity stress.

Arbuthnot Latham & Co., Limited (“AL”) has a Board approved ILAAP, and maintains liquidity buffers in excess of the minimum requirements. The ILAAP is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. At a minimum, the ILAAP is undated annually. The Liquidity Coverage Ratio (“LCR”) regime has applied to the Group from 1 October 2015, requiring management of net 30 day cash outflows as a proportion of high quality liquid assets. The actual LCR has significantly exceeded the regulatory minimum throughout the year.

The Group is exposed to daily calls on its available cash resources from current accounts, maturing deposits and loan draw-downs. The Group maintains significant cash resources to meet all of these needs as they fall due. The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates.

The tables below show the undiscounted contractual cash flows of the Group's financial liabilities and assets as at 31 December 2017:

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Deposits from banks	195,097	(195,097)	(195,097)	-	-	-
Deposits from customers	1,390,781	(1,395,770)	(1,040,893)	(293,425)	(61,452)	-
Other liabilities	1,207	(1,207)	(1,207)	-	-	-
Debt securities in issue	13,104	(19,381)	(87)	(262)	(1,395)	(17,637)
Issued financial guarantee contracts	-	(2,976)	(2,976)	-	-	-
Unrecognised loan commitments	-	(131,963)	(131,963)	-	-	-
	1,600,189	**(1,746,394)**	**(1,372,223)**	**(293,687)**	**(62,847)**	**(17,637)**
Derivative liabilities						
Risk management:	931					
- Outflows	-	(931)	(931)	-	-	-
	931	**(931)**	**(931)**	-	-	-

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Cash and balances at central banks	313,101	313,101	313,101	-	-	-
Loans and advances to banks	70,679	70,679	61,211	579	8,889	-
Debt securities held-to-maturity	227,019	227,166	22,886	101,277	103,003	-
Loans and advances to customers	1,049,269	1,187,665	126,689	121,493	800,091	139,392
Other assets	11,964	11,964	11,964	-	-	-
Financial investments	2,347	2,347	2,335	-	12	-
	1,674,379	**1,812,922**	**538,186**	**223,349**	**911,995**	**139,392**
Derivative assets						
Risk management:	2,551					
- Inflows	-	2,551	-	-	-	2,551
	2,551	**2,551**	-	-	-	**2,551**

The tables below show the undiscounted contractual cash flows of the Group's financial liabilities and assets as at 31 December 2016:

At 31 December 2016	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Deposits from banks	3,200	(3,200)	(3,200)	-	-	-
Deposits from customers	997,649	(1,000,384)	(716,285)	(243,247)	(40,852)	-
Other liabilities	1,812	(1,812)	(223)	-	-	(1,589)
Debt securities in issue	12,621	(14,345)	(86)	(259)	(1,379)	(12,621)
Issued financial guarantee contracts	-	(274)	(274)	-	-	-
Unrecognised loan commitments	-	(54,934)	(54,934)	-	-	-
	1,015,282	**(1,074,949)**	**(775,002)**	**(243,506)**	**(42,231)**	**(14,210)**
Derivative liabilities						
Risk management:	227					
- Outflows	-	(227)	(227)	-	-	-
	227	**(227)**	**(227)**	-	-	-

At 31 December 2016	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Cash and balances at central banks	195,752	195,752	195,752	-	-	-
Loans and advances to banks	36,951	36,951	36,951	-	-	-
Debt securities held-to-maturity	107,300	130,360	70,082	41,334	18,944	-
Loans and advances to customers	758,799	841,283	218,427	130,870	447,253	44,733
Other assets	1,197	1,197	1,197	-	-	-
Financial investments	2,145	2,145	2,025	-	120	-
	1,102,144	**1,207,688**	**524,434**	**172,204**	**466,317**	**44,733**
Derivative assets						
Risk management:	1,516					
- Inflows	-	1,516	85	-	-	1,431
- Outflows	1,516	-	-	-	-	-
	3,032	**1,516**	**85**	-	-	**1,431**

The table below sets out the components of the Group's liquidity reserves:

	31 December 2017		31 December 2016	
	Amount	Fair value	Amount	Fair value
Liquidity reserves	£000	£000	£000	£000
Cash and balances at central banks	313,101	313,101	195,752	195,752
Loans and advances to banks	70,679	70,679	36,951	36,951
Debt securities held-to-maturity	227,019	227,951	107,300	108,757
Undrawn credit lines	10,000	10,000	12,500	12,500
	620,799	**621,731**	**352,503**	**353,960**

Assets pledged as collateral or encumbered

The total financial assets recognised in the statement of financial position that had been pledged as collateral for liabilities at 31 December 2017 were £208.7m (2016: £112.0m).

Financial assets are pledged as collateral as part of sales and repurchases, securities borrowing and securitisation transactions under terms that are usual and customary for such activities. In addition, as part of these transactions, the Group has received collateral that it is permitted to sell or repledge in the absence of default.

The table below analyses the contractual cash flows of the Company's financial liabilities and assets as at 31 December 2017:

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Other liabilities	1,840	(1,840)	(251)	-	-	(1,589)
Issued financial guarantee contracts	13,104	(19,381)	(87)	(262)	(1,395)	(17,637)
	14,944	**(21,221)**	**(338)**	**(262)**	**(1,395)**	**(19,226)**

At 31 December 2017	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Loans and advances to banks	36,103	36,103	36,103	-	-	-
Financial investments	140	140	128	-	12	-
Other assets	162	162	162	-	-	-
	36,405	**36,405**	**36,393**	**-**	**12**	**-**

The table below analyses the contractual cash flows of the Company's financial liabilities and assets as at 31 December 2016:

At 31 December 2016	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial liability by type						
Non-derivative liabilities						
Other liabilities	3,624	(3,624)	(2,035)	-	-	(1,589)
Debt securities in issue	12,621	(14,345)	(86)	(259)	(1,379)	(12,621)
	16,245	**(17,969)**	**(2,121)**	**(259)**	**(1,379)**	**(14,210)**

At 31 December 2016	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Financial asset by type						
Non-derivative assets						
Loans and advances to banks	89,072	89,072	89,072	-	-	-
Financial investments	121	121	-	-	121	-
Other assets	791	791	791	-	-	-
	89,984	**89,984**	**89,863**	**-**	**121**	**-**

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates and exchange rates.

Fiduciary activities

The Group provides investment management and advisory services to third parties, which involve the Group making allocation and purchase and sale decisions in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these financial statements. These services give rise to the risk that the Group may be accused of maladministration or underperformance. At the balance sheet date, the Group had investment management accounts amounting to approximately £1,044m (2016: £920m). Additionally, the Group provides investment advisory services.

(e) Financial assets and liabilities

The tables below set out the Group's financial assets and financial liabilities into their respective classifications:

At 31 December 2017	Fair value through profit or loss £000	Held-to-maturity £000	Loans and receivables £000	Available-for-sale £000	Liabilities at amortised cost £000	Total carrying amount £000	Fair value £000
ASSETS							
Cash and balances at central banks	-	-	313,101	-	-	313,101	313,101
Loans and advances to banks	-	-	70,679	-	-	70,679	70,679
Debt securities held-to-maturity	-	227,019	-	-	-	227,019	227,951
Derivative financial instruments	2,551	-	-	-	-	2,551	2,551
Loans and advances to customers	-	-	1,049,269	-	-	1,049,269	1,022,816
Other assets	-	-	11,964	-	-	11,964	11,964
Financial investments	-	-	-	2,347	-	2,347	2,347
	2,551	**227,019**	**1,445,013**	**2,347**	-	**1,676,930**	**1,651,409**
LIABILITIES							
Deposits from banks	-	-	-	-	195,097	195,097	195,097
Derivative financial instruments	931	-	-	-	-	931	931
Deposits from customers	-	-	-	-	1,390,781	1,390,781	1,390,781
Other liabilities	-	-	1,207	-	-	1,207	1,207
Debt securities in issue	-	-	-	-	13,104	13,104	13,104
	931	-	**1,207**	-	**1,598,982**	**1,601,120**	**1,601,120**

At 31 December 2016	Fair value through profit or loss £000	Held-to-maturity £000	Loans and receivables £000	Available-for-sale £000	Liabilities at amortised cost £000	Total carrying amount £000	Fair value £000
ASSETS							
Cash and balances at central banks	-	-	195,752	-	-	195,752	195,752
Loans and advances to banks	-	-	36,951	-	-	36,951	36,951
Debt securities held-to-maturity	-	107,300	-	-	-	107,300	108,757
Derivative financial instruments	1,516	-	-	-	-	1,516	1,516
Loans and advances to customers	-	-	758,799	-	-	758,799	742,894
Other assets	-	-	1,197	-	-	1,197	1,197
Financial investments	-	-	-	2,145	-	2,145	2,145
	1,516	**107,300**	**992,699**	**2,145**	-	**1,103,660**	**1,089,212**
LIABILITIES							
Deposits from banks	-	-	-	-	3,200	3,200	3,200
Derivative financial instruments	227	-	-	-	-	227	227
Deposits from customers	-	-	-	-	997,649	997,649	997,649
Other liabilities	-	-	1,812	-	-	1,812	1,812
Debt securities in issue	-	-	-	-	12,621	12,621	12,621
	227	-	**1,812**	-	**1,013,470**	**1,015,509**	**1,015,509**

Cash, loans and advances to banks, debt securities held-to-maturity, deposits from banks and deposits from customers are classified as level 2 financial instruments, on the basis that they are liquid but not traded in an active market. Loans and advances to customers and debt securities in issue are classified as level 3 as there is no observable market data for these instruments.

7. Capital management

The Group’s capital management policy is focused on optimising shareholder value. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

The Group’s lead regulator, the Prudential Regulatory Authority (“PRA”), sets and monitors capital requirements for the Group as a whole and for the individual banking operations. The lead regulator adopted the Basel III capital requirements with effect from 1 January 2014. As a result, the Group’s regulatory capital requirements were based on Basel III in 2014.

In accordance with the EU's Capital Requirements Directive (“CRD”) and the required parameters set out in the PRA Handbook (BIPRU 2.2), the Individual Capital Adequacy Assessment Process (“ICAAP”) is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management. The Group's regulated entities are also the principal trading subsidiaries as detailed in Note 43.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a “Pillar I plus” approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequately to cover management’s anticipated risks. Where the Board considered that the Pillar I calculations did not reflect the risk, an additional capital add-on in Pillar II is applied, as per the Individual Capital Guidance (“ICG”) issued by the PRA.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders’ funds and revaluation reserves, after deducting goodwill, other intangible assets and the deduction for a significant investment in a financial institution (STB). The portion of the investment representing up to 10% of ABG’s Tier 1 is added back to capital resources and then risk weighted at 250%, while anything above this 10% is deducted.
- Lower Tier 2 comprises qualifying subordinated loan capital and collective provisions. Lower Tier 2 capital cannot exceed 50% of Tier 1 capital.

The following table shows the regulatory capital resources as managed by the Group:

	2017 £000	2016 £000
Tier 1		
Share capital	153	153
Retained earnings	237,171	235,567
Deduction for significant investment	(83,804)	(81,674)
Add back 10% of CET1 (risk weighted at 250%)	22,038	22,557
Capital redemption reserve	20	20
Treasury shares	(1,131)	(1,131)
Goodwill	(5,202)	(1,682)
Deductions for other intangibles	(10,793)	(6,840)
Available-for-sale reserve	162	(251)
Total tier 1 capital resources	**158,614**	**166,719**
Tier 2		
Debt securities in issue	13,104	12,621
Total tier 2 capital resources	**13,104**	**12,621**
Total tier 1 & tier 2 capital resources	**171,718**	**179,340**

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The PRA sets ICG for each UK bank calibrated by reference to its Capital Resources Requirement, broadly equivalent to 8 percent of risk weighted assets and thus representing the capital required under Pillar I of the Basel III framework. The ICAAP is a key input into the PRA's ICG setting process, which addresses the requirements of Pillar II of the Basel III framework. The PRA's approach is to monitor the available capital resources in relation to the ICG requirement. Each entity maintains an extra internal buffer and capital ratios are reviewed on a monthly basis to ensure that external requirements are adhered to. All regulated entities have complied with all of the externally imposed capital requirements to which they are subject.

Pillar III complements the minimum capital requirements (Pillar I) and the supervisory review process (Pillar II). Its aim is to encourage market discipline by developing a set of disclosure requirements which will allow market participants to assess key pieces of information on a firm's capital, risk exposures and risk assessment processes. Our Pillar III disclosures for the year ended 31 December 2017 are published as a separate document on the Group website under Investor Relations (Announcements & Shareholder Info).

8. Net interest income

	2017	2016
	£000	£000
Cash and balances at central banks	801	873
Loans and advances to banks	258	124
Debt securities held-to-maturity	1,353	844
Loans and advances to customers	45,015	36,230
	47,427	**38,071**
Deposits from banks	(35)	(297)
Deposits from customers	(5,939)	(6,977)
Debt securities in issue	(360)	(352)
Interest expense	**(6,334)**	**(7,626)**
Net interest income	**41,093**	**30,445**

In 2017, the Group recognised £0.1m (2016: £0.3m) of additional interest income to reflect actual cash flows received on the aquired loan portfolios having been in excess of forecast cash flows.

9. Fee and commission income

	2017	2016
	£000	£000
Banking commissions	2,263	1,947
Investment management fees and commissions	7,887	7,122
Wealth planning fees and commissions	2,593	2,156
Other fee income	1,062	205
	13,805	**11,430**

10. Net impairment loss on financial assets

	2017	2016
	£000	£000
Net Impairment losses on loans and advances to customers	394	427
Impairment losses on financial investments	-	47
	394	**474**

During the year, the Group recovered £116k (2016: £nil) of loans which had previously been written off.

11. Other income

Other income mainly consists of rental income from the investment property (see Note 31) of £2.1m (2016: £1.1m) and premises recharges of £0.7m (2016: £0.4m) to Secure Trust Bank for office space occupied. In 2016, other income also included £1.6m realised on the investment in Visa Europe Ltd (see Note 25).

12. Operating expenses

Operating expenses comprise:	2017 £000	2016 £000
Staff costs, including Directors:		
Wages, salaries and bonuses	30,937	26,708
Social security costs	3,576	3,154
Pension costs	1,558	1,247
Share based payment transactions (note 39)	189	215
Amortisation of intangibles (note 28)	1,036	521
Depreciation (note 30)	1,508	1,146
Financial Services Compensation Scheme Levy	190	233
Operating lease rentals	3,087	2,610
Operating expenses for investment property	230	115
Acquisitions costs	108	398
Other administrative expenses	12,302	9,764
Total operating expenses from continuing operations	**54,721**	**46,111**

Details on Directors remuneration are disclosed in the Remuneration Report on page ##RREP.

Remuneration of the auditor and its associates, excluding VAT, was as follows:	2017 £000	2016 £000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	105	99
Fees payable to the Company's auditor and its associates for other services:		
Audit of the accounts of subsidiaries	221	237
Audit related assurance services	85	157
Taxation compliance services	-	36
Taxation advisory services	-	99
Other assurance services	17	170
Other non-audit services	-	15
Total fees payable	**428**	**813**

Other assurance services include regulatory assessments. Corporate finance services include due diligence work on a potential corporate transaction.

13. Income tax expense

United Kingdom corporation tax at 19.25% (2016: 20%)	2017 £000	2016 £000
Current taxation		
Corporation tax charge - current year	472	179
Corporation tax charge - adjustments in respect of prior years	(141)	457
	331	**636**
Deferred taxation		
Origination and reversal of temporary differences	(135)	11
Adjustments in respect of prior years	252	73
	117	**84**
Income tax expense	**448**	**720**
Tax reconciliation		
Profit before tax	6,971	179
Tax at 19.25% (2016: 20%)	1,342	36
Permanent difference - Tax on associate income	(854)	(429)
Other permanent differences	(152)	496
Tax rate change	1	87
Prior period adjustments	111	530
Corporation tax charge for the year	**448**	**720**

Permanent differences mainly relate to associate income which is reflected after tax.

The tax charge on discontinuing operations is disclosed in note 14.

On 26 October 2015 the Government substantively enacted a reduction in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017). An additional reduction to 17% (effective from 1 April 2020) was substantively enacted on 6 September 2016. This will reduce the Bank's future current tax charge accordingly. The deferred tax asset at 31 December 2017 has been calculated based on the rate of 19%.

14. Discontinued operations

The profit after tax from discontinued operations is made up as follows:

Discontinued operations	Year ended 31 December 2017 £000	Year ended 31 December 2016 £000
Profit after tax from discontinued operations - ELL (up to 13 April 2016)	-	2,027
Profit after tax on sale of discontinued operations - ELL	-	116,754
Profit after tax from discontinued operations - STB (up to 15 June 2016)	-	9,149
Profit after tax on sale of discontinued operations - STB	-	100,180
Profit after tax from discontinued operations	**-**	**228,110**

On 4 December 2015, STB agreed to the conditional sale of its non-standard consumer lending business, ELL, which comprises Everyday Loans Holdings Limited and subsidiary companies Everyday Lending Limited and Everyday Loans Limited, to Non Standard Finance PLC (NSF) for £106.9 million in cash subject to a net asset adjustment and £16.3 million in NSF ordinary shares. The Disposal completed on 13 April 2016, and on completion, NSF repaid intercompany debt of £108.1 million to STB. After selling costs of £6.2m, this resulted in a gain recognised on disposal of £116.8m.

Details of the profits of discontinued operations, net assets disposed of and consequential gain recognised on disposal and cash flow from discontinued operations are set out below.

		From 1 January to 13 April 2016 £000
Interest income		11,137
Net interest income		**11,137**
Fee and commission income		147
Fee and commission expense		(124)
Net fee and commission income		**23**
Operating income		**11,160**
Net impairment loss on financial assets		(2,610)
Operating expenses		(6,016)
Profit before tax		**2,534**
Tax expense		(507)
Profit after tax		**2,027**
Profit on sale of business		116,754
Total profit from discontinued operation		**118,781**
Profit attributable to:		
Equity holders of the Company		61,667
Non-controlling interests		57,114
Profit after tax		**118,781**
Earnings per share for profit attributable to the equity holders of the Company from discontinued operations during the year (expressed in pence per share):		
- basic	16	418.4
- diluted	16	418.2

The following assets were sold as part of the sale of ELL:

	Recognised values on sale 2016 £000
Loans and advances to banks	457
Loans and advances to customers	116,744
Property, plant and equipment	452
Intangible assets	1,258
Deferred tax assets	371
Prepayments and accrued income	451
Other assets	11
Total assets	**119,744**
Intercompany funding	108,088
Current tax liability	3,212
Other liabilities	4,748
Total liabilities	**116,048**
Net identifiable assets / (liabilities)	**3,696**
Consideration	123,206
Costs	(2,756)
Profit on sale of ELL	**116,754**

The intercompany funding was repaid by NSF at the time of completion.

Cash flow from discontinued operations - ELL

	From 1 January to 13 April 2016 £000
Cash flows from operating activities	
Interest received	11,137
Fees and commissions received	23
Cash payments to employees and suppliers	(8,626)
Taxation paid	(507)
Cash flows from operating profits before changes in operating assets and liabilities	2,027
Changes in operating assets and liabilities:	
- net increase in loans and advances to customers	(3,618)
- net increase in other assets	(249)
- net increase in other liabilities	2,621
Net cash inflow from operating activities	**781**
Cash flows from investing activities	
Purchase of property, plant and equipment	(9)
Net cash outflow from investing activities	**(9)**
Net increase in cash and cash equivalents	772
Cash and cash equivalents at 1 January	1,661
Cash and cash equivalents at 13 April	**2,433**

On 15 June 2016 ABG sold 6 million shares in STB, which reduced its shareholding in STB from 51.92% to 18.93%. From this date the Group accounted for its remaining shareholding in STB as an associate. After the sale of the 6 million shares, the Group retained Board representation and as such is seen to have significant influence over STB. The profit and cash flow from discontinued operations relating to ELL have been shown in the tables above. The ELL entities were subsidiaries of STB and therefore formed part of the STB result reported in the operating segments of ABG. The tables below therefore reflect the profit and cash flow from the STB group excluding ELL. The combined impact can be seen in the operating segments (see note 44 – Retail banking).

		From 1 January to 15 June 2016 £000
Interest income		57,498
Interest expense		(12,107)
Net interest income		**45,391**
Fee and commission income		7,981
Fee and commission expense		(779)
Net fee and commission income		**7,202**
Operating income		**52,593**
Net impairment loss on financial assets		(12,172)
Operating expenses		(29,073)
Profit before tax		**11,348**
Tax expense		(2,199)
Profit after tax		**9,149**
Profit on sale of shares		100,180
Total profit from discontinued operation		**109,329**
Profit attributable to:		
Equity holders of the Company		105,017
Non-controlling interests		4,312
Profit after tax		**109,329**
Earnings per share for profit attributable to the equity holders of the Company from discontinued operations during the year (expressed in pence per share):		
- basic	16	712.5
- diluted	16	712.2

The following assets were deconsolidated as part of the sale of 6 million shares in STB:

	Recognised values on sale 2016 £000
Cash and balances at central banks	176,647
Loans and advances to banks	27,618
Loans and advances to customers	1,117,700
Other assets	5,805
Financial investments	15,030
Deferred tax asset	606
Intangible assets	7,017
Property, plant and equipment	8,606
Total assets	**1,359,029**
Deposits from banks	25,000
Deposits from customers	1,046,009
Current tax liability	293
Other liabilities	29,748
Total liabilities	**1,101,050**
Net identifiable assets	**257,979**

Profit on sale of shares was calculated as follows:

	2016 £000
Consideration received	150,000
Less costs	(2,001)
Less net identifiable assets	(257,979)
Add back non-controlling interest	124,046
Add back fair value of remaining investment in STB	86,114
Profit on sale of STB	**100,180**

Cash flow from discontinued operations - STB excluding ELL	From 1 January to 15 June 2016 £000
Cash flows from operating activities	
Interest received	68,635
Interest paid	(12,107)
Fees and commissions received	7,226
Cash payments to employees and suppliers	(51,552)
Taxation paid	(6,034)
Cash flows from operating profits before changes in operating assets and liabilities	6,168
Changes in operating assets and liabilities:	
- net increase in loans and advances to customers	(165,976)
- net decrease in other assets	117,395
- net decrease in deposits from banks	(10,000)
- net increase in amounts due to customers	12,936
- net decrease in other liabilities	(5,031)
Net cash outflow from operating activities	**(44,508)**
Cash flows from investing activities	
Purchase of computer software	(1,754)
Purchase of property, plant and equipment	(531)
Disposal of property, plant and equipment	2,179
Proceeds from disposal of businesses	106,912
Proceeds from sale of property, plant and equipment	456
Net cash inflow from investing activities	**107,262**
Cash flows from financing activities	
Dividends paid	(10,005)
Net cash used in financing activities	**(10,005)**
Net increase in cash and cash equivalents	52,749
Cash and cash equivalents at 1 January	141,595
Cash and cash equivalents at 15 June	**194,344**

15. Average number of employees

	2017	2016
Central	161	146
Private banking	136	108
Commercial banking	38	14
Renaissance Asset Finance	13	-
Group	17	19
	365	**287**

As STB was deconsolidated during 2016, the employees have been removed from the above averages in 2016.

16. Earnings per ordinary share

Basic

Basic earnings per ordinary share are calculated by dividing the profit after tax attributable to equity holders of the Company by the weighted average number of ordinary shares 14,852,763 (2016: 14,738,548) in issue during the year.

Diluted

Diluted earnings per ordinary share are calculated by dividing the dilutive profit after tax attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, as well as the number of dilutive share options in issue during the year. The number of dilutive share options in issue at the year end was nil (2016: 50,000).

Profit attributable	2017 £000	2016 £000
Total profit after tax attributable to equity holders of the Company	6,523	166,143
Profit/(loss) after tax from continuing operations attributable to equity holders of the Company	6,523	(541)
Profit after tax from discontinued operations attributable to equity holders of the Company (STB excl. ELL)	-	105,017
Profit after tax from discontinued operations attributable to equity holders of the Company (ELL)	-	61,667

Dilutive profit attributable	2017 £000	2016 £000
Total profit after tax attributable to equity holders of the Company	6,523	166,143
Loss after tax from continuing operations attributable to equity holders of the Company	6,523	(541)
Profit after tax from discontinued operations attributable to equity holders of the Company (STB excl. ELL)	-	105,017
Profit after tax from discontinued operations attributable to equity holders of the Company (ELL)	-	61,667

Basic Earnings per share	2017 p	2016 p
Total Basic Earnings per share	43.9	1,127.2
Basic Earnings per share from continuing operations	43.9	(3.7)
Basic Earnings per share from discontinued operations (STB excl. ELL)	-	712.5
Basic Earnings per share from discontinued operations (ELL)	-	418.4

Diluted Earnings per share	2017 p	2016 p
Total Diluted Earnings per share	43.9	1,126.7
Diluted Earnings per share from continuing operations	43.9	(3.7)
Diluted Earnings per share from discontinued operations (STB excl. ELL)	-	712.2
Diluted Earnings per share from discontinued operations (ELL)	-	418.2

17. Cash and balances at central banks

Group	2017 £000	2016 £000
Cash and balances at central banks	**313,101**	**195,752**

Surplus funds are mainly held in the Bank of England reserve account, with the remainder held in certificates of deposit, fixed rate notes and money market deposits in highly rated banks (the majority held in UK clearing banks).

18. Loans and advances to banks

Group	2017 £000	2016 £000
Placements with banks included in cash and cash equivalents (note 41)	**70,679**	**36,951**

The table below presents an analysis of loans and advances to banks by rating agency designation as at 31 December, based on Moody's long term ratings:

Group	2017 £000	2016 £000
Aa3	39,871	-
A1	20,553	20,696
A2	10,012	15,582
A3	-	110
Baa1	235	563
Unrated	8	-
	70,679	**36,951**

None of the loans and advances to banks are either past due or impaired (2016: £nil).

Company	2017 £000	2016 £000
Placements with banks included in cash and cash equivalents (note 41)	**36,103**	**89,072**

Loans and advances to banks include bank balances of £36.1m (2016: £89.1m) with Arbuthnot Latham & Co., Ltd.

19. Debt securities held-to-maturity

Debt securities represent certificates of deposit. The Group's intention is to hold them to maturity and, therefore, they are presented in the Statement of Financial Position at amortised cost.

The movement in debt securities held to maturity may be summarised as follows:

Group	2017 £000	2016 £000
At 1 January	107,300	87,728
Exchange difference	(951)	2,087
Additions	211,080	89,384
Redemptions	(90,410)	(68,103)
Deconsolidation of STB	-	(3,796)
At 31 December	**227,019**	**107,300**

The table below presents an analysis of debt securities by rating agency designation at 31 December, based on Moody's long term ratings:

Group	2017 £000	2016 £000
Aaa	100,106	40,337
Aa1	51,389	23
Aa2	5,946	26,089
Aa3	18,384	6,000
A1	18,187	31,953
A3	33,007	2,898
	227,019	**107,300**

None of the debt securities held-to-maturity are either past due or impaired.

20. Assets classified as held for sale

	Group	
	2017	2016
	£000	£000
Seed capital investments held for sale	-	-
Repossessed property held for sale	2,915	-
	2,915	-

Seed capital investments held for sale
The Group considers itself a sponsor of an investment fund when it facilitates the establishment of a fund in which the Group is the investment manager. The Group ordinarily provides seed capital in order to provide initial scale and facilitate marketing of the funds to third-party investors. The fund is then financed through the issue of units to investors. Aggregate interests held by the Group include seed capital, management fees and performance fees. The Group generates management and performance fee income from managing the assets on behalf of third-party investors.

The Group has an investment of £1 in the share capital of the SPV created to administer the fund. At 31 December 2017, the Group has a receivable of £6.8m from the SPV, which is reflected in Note 24.

Repossessed property held for sale
During the year a property held as collateral on a loan was repossessed. The property is expected to be sold within 12 months and is therefore classified in the accounts as held for sale.

21. Derivative financial instruments

	2017			2016		
	Contract/ notional amount	Fair value assets	Fair value liabilities	Contract/ notional amount	Fair value assets	Fair value liabilities
Group	£000	£000	£000	£000	£000	£000
Currency swaps	9,614	950	931	6,566	85	218
Interest rate swaps	17,824	-	-	3,800	-	9
Structured notes	1,607	1,601	-	1,607	1,431	-
	29,045	**2,551**	**931**	**11,973**	**1,516**	**227**

The principal derivatives used by the Group are over the counter exchange rate contracts. Exchange rate related contracts include currency swaps and interest rate swaps.

A forward foreign exchange contract is an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate. Currency swaps generally involve the exchange of interest payment obligations denominated in different currencies; exchange of principal can be notional or actual. The currency swaps are settled net and therefore the fair value is small in comparison to the contract/notional amount. Interest rate swaps are used to hedge against the Profit or Loss impact resulting from the movement in interest rates, due to some exposures having fixed rate terms.

Also included in derivative financial instruments are structured notes. These notes contain embedded derivatives (embedded options to buy and sell indices) and non-derivative host contracts (discounted bonds). Both the host and embedded derivatives are presented net within derivative financial instruments. The Group invested in the structured notes, which are maturing in 2021.

The Group only uses investment graded banks as counterparties for derivative financial instruments. None of the contracts are collateralised.

The table below presents an analysis of derivative financial instruments contract/notional amounts by rating agency designation of counterparty bank at 31 December, based on Moody's long term ratings:

Group	2017 £000	2016 £000
A1	26,521	10,366
A2	2,524	-
Baa1	-	1,607
	29,045	**11,973**

22. Loans and advances to customers

Group	2017 £000	2016 £000
Gross loans and advances	1,050,631	759,772
Less: allowances for impairment on loans and advances (note 23)	(1,362)	(973)
	1,049,269	**758,799**

For a maturity profile of loans and advances to customers, refer to note 6.

Loans and advances to customers can be further summarised as follows:

Group	2017 £000	2016 £000
Neither past due nor impaired	888,332	719,515
Past due but not impaired	131,247	23,379
Impaired	31,052	16,878
Gross	1,050,631	759,772
Less: allowance for impairment	(1,362)	(973)
Net	**1,049,269**	**758,799**

Loans and advances to customers include finance lease receivables as follows:

Group	2017 £000	2016 £000
Gross investment in finance lease receivables:		
- No later than 1 year	28,911	-
- Later than 1 year and no later than 5 years	53,766	-
	82,677	-
Unearned future finance income on finance leases	(11,412)	-
Net investment in finance leases	**71,265**	-
The net investment in finance leases may be analysed as follows:		
- No later than 1 year	23,170	-
- Later than 1 year and no later than 5 years	48,095	-
	71,265	-

(a) Loans and advances past due but not impaired

Gross amounts of loans and advances to customers that were past due but not impaired were as follows:

Group	2017 £000	2016 £000
Past due up to 30 days	115,126	961
Past due 30 - 60 days	11,043	5,689
Past due 60 - 90 days	5,078	638
Over 90 days	-	16,091
Total	**131,247**	**23,379**

The newly implemented banking system has enabled the Group to establish a more sophisticated tracking of early stage arrears. The majority of loans and advances up to 30 days past due were subsequently up to date post year end.

Loans and advances typically fall into this category when there is a delay in either the sale of the underlying collateral or the completion of formalities to extend the credit facilities for a further period. Management have no material concerns regarding the quality of the collateral that secures the lending.

Additionally, the Group updated its impairment policy in the year to include all loans and advances over 90 days past due within impaired loans. Interest income on loans classified as impaired totalled £338,000 (2016: £126,000).

(b) Loans and advances renegotiated

Restructuring activities include external payment arrangements, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Renegotiated loans that would otherwise be past due or impaired totalled £nil (2016: £nil).

(c) Collateral held

Collateral is measured at fair value less costs to sell.

Most of the loans are secured by property. The fair value of the collateral held against past due but not impaired or impaired balances is £302.9m (2016: £103.7m) against loans of £162.3m (2016: £40.3m), giving an average loan-to-value of 54% (2016: 39%). The weighted average loan-to-value is 46% (2016: 61%). The net amount of individually impaired loans and advances to customers after impairment but before taking into account the cash flows from collateral held is £29.7m (2016: £15.9m).

23. Allowances for impairment of loans and advances

Reconciliation of specific allowance for impairments:

Group	2017 £000	2016 £000
At 1 January	973	35,696
Impairment losses	329	474
On acquisition of RAF (see note 29)	51	-
De-consolidation of STB	-	(34,285)
Loans written off during the year as uncollectible	(15)	(962)
Amounts recovered during the year	(116)	50
At 31 December	**1,222**	**973**

Reconciliation of collective allowance for impairments:

Group	2017 £000	2016 £000
At 1 January	-	3,141
On acquisition of RAF (see note 29)	75	-
Impairment losses	65	-
De-consolidation of STB	-	(3,141)
At 31 December	**140**	-

24. Other assets

Group	2017 £000	2016 £000
Trade receivables	5,208	1,197
Inventory	4,436	5,213
Receivable from investment fund held for sale	6,756	-
Prepayments and accrued income	4,224	5,529
	20,624	**11,939**

Inventory

Land acquired through repossession of collateral which is subsequently held in the ordinary course of business with a view to develop and sell is accounted for as inventory. The land is currently in the process of being redeveloped and will ultimately be sold off as individual residential plots. The proceeds from the sale of these plots will be used to repay the outstanding loans. Pinnacle Universal is a special purpose vehicle, 100% owned by the Group, which owns this land.

Company	2017 £000	2016 £000
Trade receivables	3	633
Due from subsidiary undertakings	159	158
Prepayments and accrued income	37	96
	199	**887**

25. Financial investments

Group	2017 £000	2016 £000
Designated at fair value through profit and loss		
- Listed securities	128	108
Available-for-sale		
- Listed securities	4	13
- Debt securities	1,497	1,443
- Unlisted securities	718	581
Total financial investments	**2,347**	**2,145**

Listed securities

The Group holds investments in listed securities which are valued based on quoted prices.

Debt securities

The Group has made an investment in an unlisted special purpose vehicle, set up to acquire and enhance the value of a commercial property. This investment is of a medium term nature. There is no open market for the investment and therefore the Group has valued it using appropriate valuation methodologies (see Note 4.2 (a)), which include net asset valuations and discounted future cash flows. The Directors intend to dispose of the underlying asset when a suitable buyer has been identified and when the Directors believe that the underlying asset has reached its optimal value.

Unlisted securities

On 23 June 2016 Arbuthnot Latham received €1.3m cash consideration following Visa Inc.'s completion of the acquisition of Visa Europe. As part of the deal Arbuthnot Latham also received preference shares in Visa Inc., these have been valued at their future conversion value into Visa Inc. common stock. Management has assessed the fair value of the Group’s investment as £706k (2016: £569k). This valuation includes a 31% haircut, as referred to in Note 4.

Company	2017 £000	2016 £000
Financial investments comprise:		
- Listed securities (at fair value through profit and loss)	128	108
- Unlisted securities (available-for-sale)	12	13
Total financial investments	140	121

26. Deferred taxation

The deferred tax asset comprises:

Group	2017 £000	2016 £000
Accelerated capital allowances and other short-term timing differences	372	943
Movement in fair value of available-for-sale securities	(40)	(14)
Unutilised tax losses	1,195	736
Deferred tax asset	**1,527**	**1,665**
At 1 January	1,665	1,784
On acquisition of RAF	5	-
Other Comprehensive Income - available-for-sale securities	(26)	456
Profit and loss account - accelerated capital allowances and other short-term timing differences	(576)	(21)
Profit and loss account - tax losses	459	(64)
Deconsolidate / Transfer to assets classified as held for sale	-	(490)
Deferred tax asset at 31 December	**1,527**	**1,665**

Company	2017 £000	2016 £000
Accelerated capital allowances and other short-term timing differences	346	397
Tax losses	295	-
Deferred tax asset	**641**	**397**
At 1 January	397	418
Profit and loss account - accelerated capital allowances and other short-term timing differences	(51)	(21)
Profit and loss account - tax losses	295	-
Deferred tax asset at 31 December	**641**	**397**

Deferred tax assets are recognised for tax losses to the extent that the realisation of the related tax benefit through future taxable profits is probable.

27. Interests in associates

Group	2017 £000	2016 £000
Tarn Crag	-	900
Secure Trust Bank PLC	83,804	81,674
Interests in associates	**83,804**	**82,574**

Tarn Crag

On 11 October 2013, AL together with Praxis (Holding) Limited, formed a special purpose vehicle in the form of a separate legal entity (Tarn Crag Limited). The purpose of this legal entity was to refurbish and re-let a property in Glasgow, with the intention to exit via a sale to an institutional investor in circa 5 years time. The investment was accounted for using the equity method.

On 28 March 2017 AL sold its investment in Tarn Crag to Praxis (Holding) Ltd at book value of £900k.

During the year the associate recorded a loss of £nil (2016: loss of £197k). Legal costs of £nil (2016: £43k), previously capitalised against the carrying value of the associate, were written off in the year.

The summarised balance sheet for Tarn Crag at the previous year end is set out below:

At 31 December	2016 £000
ASSETS	
Cash and balances at central banks	3,468
Other assets	656
Property, plant and equipment	9,201
	13,325
EQUITY AND LIABILITIES	
Deposits from banks	12,474
Other liabilities	1,484
Debt securities in issue	1,400
Revaluation reserve	(1,418)
Retained Earnings	(615)
	13,325

Secure Trust Bank

On 15 June 2016 Arbuthnot Banking Group sold 6 million shares in Secure Trust Bank PLC ('STB') for £150m, which reduced its shareholding in STB from 51.92% to 18.93%. From this date the Group accounted for its remaining shareholding in STB as an associate. After the sale of the 6 million shares, the Group retained Board representation and as such is seen to have significant influence over STB. The principal place of business of STB is the United Kingdom. Subsequent to initial recognition at fair value, the investment is accounted for using the equity method. The fair value of the investment as at 31 December 2016 was £75.4m. STB recorded a profit after tax of £11.4m in the period from 16 June to 31 December 2016. The carrying value of the interest in STB is shown as the fair value at the date of sale adjusted for the share of the Group's profit after tax and dividends received. STB is listed on the main market of the London Stock Exchange.

(a) Significant restrictions

The Group does not have significant restrictions on its ability to access funds, other than the liquidity in the market for the sale of the shares.

(b) Risks associated with interests

As STB is a publicly listed company, there are a number of risks, e.g. conduct risk, regulatory risk and macroeconomic and competitive environment risks that could have an impact on the share price and ultimate recoverability of the investment.

(c) Changes in ownership interest

On 15 June 2016 Arbuthnot Banking Group sold 6 million shares in STB for £150m, which reduced its shareholding in STB from 51.92% to 18.93%. From this date the Group accounted for its remaining shareholding in STB as an associate. After the sale of the 6 million shares, the Group retained Board representation and as such is seen to have significant influence over STB.

On 7 November 2016, 460,419 share options in STB vested. On the same date 283,335 share options were exercised with admission of the shares on the stock market on 9 November. This increased STB's shares in issue from 18,191,894 to 18,475,229 and as a result ABG's shareholding was diluted from 18.93% to 18.64%. If the remaining 177,084 share options were exercised, ABG's shareholding would further dilute to 18.47%.

The summarised Income Statement and Balance Sheet for STB is set out below (STB reports in millions):

	Year ended 31 December	
	2017	2016
	£m	£m
Interest income	141.3	118.8
Interest expense	(26.7)	(26.3)
Net interest income	**114.6**	**92.5**
Fee and commission income	16.0	16.3
Fee and commission expense	(1.1)	(1.8)
Net fee and commission income	**14.9**	**14.5**
Operating income	**129.5**	**107.0**
Net impairment loss on financial assets	(33.5)	(23.3)
Other income	0.3	-
Operating expenses	(71.3)	(64.3)
Profit before tax	**25.0**	**19.4**
Income tax expense	(5.1)	(5.2)
Profit after tax	19.9	14.2
Profit from discontinued operations after tax	3.9	123.3
Profit for the year	**23.8**	**137.5**
Other comprehensive income		
Items that will not be reclassified to profit or loss		
Revaluation reserve	0.1	1.2
Tax on other comprehensive income	-	(0.2)
	0.1	**1.0**
Items that are or may be reclassified to profit or loss		
Available-for-sale reserve	2.8	(2.8)
	2.8	**(2.8)**
Other comprehensive income for the period, net of tax	**2.9**	**(1.8)**
Total comprehensive income for the period	**26.7**	**135.7**
Profit attributable to:		
Equity holders of the Company	**23.8**	**137.5**
Total comprehensive income attributable to:		
Equity holders of the Company	**26.7**	**135.7**

	At 31 December 2017 £m	2016 £m
ASSETS		
Cash and balances at central banks	226.1	112.0
Loans and advances to banks	34.3	18.2
Loans and advances to customers	1,598.3	1,321.0
Debt securities held-to-maturity	5.0	20.0
Financial investments	-	13.5
Property, plant and equipment	11.5	11.4
Intangible assets	10.4	9.0
Deferred tax asset	0.6	-
Other assets	5.4	4.9
Total assets	**1,891.6**	**1,510.0**
EQUITY AND LIABILITIES		
Equity attributable to owners of the parent		
Share capital	7.4	7.4
Share premium account	81.2	81.2
Retained earnings	159.2	149.0
Other reserves	1.3	(1.6)
Total equity	**249.1**	**236.0**
LIABILITIES		
Deposits from banks	113.0	70.0
Deposits from customers	1,483.2	1,151.8
Current tax liability	3.0	1.7
Deferred tax liability	-	0.2
Other liabilities	43.3	50.3
Total liabilities	**1,642.5**	**1,274.0**
Total equity and liabilities	**1,891.6**	**1,510.0**

Interest in associate for the Company is set out below:

Company	2017 £000	2016 £000
Secure Trust Bank PLC	5,056	5,056
Interests in associates	**5,056**	**5,056**

28. Intangible assets

Group	Goodwill £000	Computer software £000	Other intangibles £000	Total £000
Cost				
At 1 January 2016	2,695	12,653	2,414	17,762
Additions	-	5,155	-	5,155
Transfer out on deconsolidation - STB	(1,013)	(9,301)	(2,200)	(12,514)
At 31 December 2016	**1,682**	**8,507**	**214**	**10,403**
Additions	-	2,641	-	2,641
On Acquisition - RAF (see note 29)	3,520	-	2,348	5,868
At 31 December 2017	**5,202**	**11,148**	**2,562**	**18,912**
Accumulated amortisation				
At 1 January 2016	-	(6,048)	(840)	(6,888)
Amortisation charge	-	(478)	(43)	(521)
Transfer out on deconsolidation - STB	-	4,794	734	5,528
At 31 December 2016	-	**(1,732)**	**(149)**	**(1,881)**
Amortisation charge	-	(830)	(206)	(1,036)
At 31 December 2017	-	**(2,562)**	**(355)**	**(2,917)**
Net book amount				
At 31 December 2016	1,682	6,775	65	8,522
At 31 December 2017	5,202	8,586	2,207	15,995

Included within Computer Software additions is an amount of £2.6m (2016: £5.5m) relating to the new banking system which went live in 2017.

The accounting policy for goodwill is described in note 3.15 (a). The Group reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. Significant management judgements are made in estimations, to evaluate whether an impairment of goodwill is necessary. Impairment testing is performed at CGU level and the following two items, with judgements surrounding them, have a significant impact on the estimations used in determining the necessity of an impairment charge:

• Future cash flows - Cash flow forecasts reflect management's view of future business forecasts at the time of the assessment. A detailed three year budget is done every year and management also uses judgement in applying a growth rate. The accuracy of future cash flows is subject to a high degree of uncertainty in volatile market conditions. During such conditions, management would perform impairment testing more frequently than annually to ensure that the assumptions applied are still valid in the current market conditions.

• Discount rate - Management also apply judgement in determining the discount rate used to discount future expected cash flows. The discount rate is derived from the cost of capital for each CGU.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. There are currently two CGUs (2016: one) with goodwill attached; the core Arbuthnot Latham CGU (£1.7m) and RAF CGU (£3.5m).

Management considers the value in use for both CGUs to be the discounted cash flows over 5 years with a terminal value (2016: 5 years with a terminal value). The 5 year discounted cash flows with a terminal value are considered to be appropriate as the goodwill relates to an ongoing well established business and not underlying assets with finite lives. The terminal value is calculated by applying a discounted perpetual growth model to the profit expected in 2020 as per the approved 3 year plan. A growth rate of 12.5% (2016: 11%) was used for income and 18% (2016: 13%) for expenditure from 2018 to 2020 (these rates were the best estimate of future forecasted performance), while a 3% (2016: 3%) percent growth rate for income and expenditure (a more conservative approach was taken for latter years as these were not budgeted for in detail as per the three year plan approved by the Board of Directors) was used for cash flows after the approved three year plan.

Management considers the value in use for the RAF CGU to be the discounted cash flows over 5 years with a terminal value. The 5 year discounted cash flows with a terminal value are considered to be appropriate as the goodwill relates to an ongoing, well established, business and not underlying assets with finite lives. The terminal value is calculated by applying a discounted perpetual growth model to the profit expected in 2022 as per the approved budget. A growth rate of 5% was used (this rate was the best estimate of future forecasted performance).

The growth rates used are above the forecast UK growth rate of 1.8% to reflect the Bank's current growth strategy enabled by capital available at parent level.

Cash flows were discounted at a pre-tax rate of 12% (2016: 12%) to their net present value. The discount rate of 12% is considered to be appropriate after evaluating current market assessments of the time value of money and the risks specific to the assets or CGUs.

Currently, the value in use and fair value less costs to sell of both CGUs exceed the carrying values of the associated goodwill and as a result no sensitivity analysis was performed.

29. Acquisition of Renaissance Asset Finance Ltd

On 28 April 2017, Arbuthnot Latham & Co. Ltd completed the acquisition of 100% of the share capital of Renaissance Asset Finance Limited ("RAF") from its founders following receipt of regulatory approval.

RAF is a provider of finance for a range of specialist assets which includes vintage and expensive cars and SME business assets. The acquisition supported ALs strategy to diversify its proposition within the specialist financial services sector.

The consideration will be paid in four staged amounts, all of which will be in cash. The first payment was equal to the net assets at completion of £2.1m. The remaining three payments are performance related and will be based on the profits of RAF in each of the three calendar years 2018 to 2020. The maximum amount payable for the performance based payments is limited to £6.5m. AL has also provided an intercompany loan to RAF at completion of £57m to re-finance RAF's existing finance liabilities. The consideration and the refinancing of RAF's funding liabilities have been satisfied from the Group's current cash resources.

The assets acquired and resulting goodwill on acquisition are set out in the table below. The fair value of intangibles acquired include £0.4m relating to customer relationships, £1.5m relating to broker relationships and £0.4m for the brand. The resultant goodwill represented the assembled specialist workforce, established process and control environment, cross selling opportunities between the two companies and the opportunity cost of a fully operational company within the sector.

The acquisition contributed £4.2m to interest income and £1.6m to profit before tax.

	Acquired assets / liabilities £000	Fair value adjustments £000	Recognised values on acquisition £000
Loans and advances to banks	2,815	-	2,815
Loans and advances to customers	57,684	-	57,684
Other asset	1,341	-	1,341
Deferred tax assets	5	-	5
Intangible assets	-	2,348	2,348
Property, plant and equipment	23	-	23
Total assets	61,868	2,348	64,216
Deposits from banks	58,969	-	58,969
Current tax liability	195	-	195
Other liabilities	632	-	632
Total liabilities	**59,796**	-	**59,796**
Net identifiable assets	**2,072**	**2,348**	**4,420**
Consideration			7,940
Goodwill			**3,520**

30. Property, plant and equipment

Group	Freehold land and buildings £000	Leasehold improvements £000	Computer and other equipment £000	Motor Vehicles	Total £000
Cost or valuation					
At 1 January 2016	7,488	4,686	12,443	97	24,714
Additions	-	127	227	-	354
Transfer out on deconsolidation - STB	(7,488)	(226)	(9,929)	-	(17,643)
At 31 December 2016	-	**4,587**	**2,741**	**97**	**7,425**
Additions	-	408	258	-	666
On acquisition - RAF (see note 29)	-	20	52	-	72
Disposals	-	-	(10)	-	(10)
At 31 December 2017	-	**5,015**	**3,041**	**97**	**8,153**
At 1 January 2016	(1,037)	(530)	(9,121)	(22)	(10,710)
Depreciation charge	-	(697)	(425)	(24)	(1,146)
Transfer out on deconsolidation - STB	1,037	10	8,166	-	9,213
At 31 December 2016	-	**(1,217)**	**(1,380)**	**(46)**	**(2,643)**
Depreciation charge	-	(944)	(540)	(25)	(1,509)
On acquisition - RAF (see note 29)		(16)	(33)	-	(49)
Disposals	-	-	10	-	10
At 31 December 2017	-	**(2,177)**	**(1,943)**	**(71)**	**(4,191)**
Net book amount					
At 31 December 2016	-	**3,370**	**1,361**	**51**	**4,782**
At 31 December 2017	-	**2,838**	**1,098**	**26**	**3,962**

The Group's opening freehold property in 2016 is also the Registered Office of Secure Trust Bank and was fully utilised for the Group's own purposes. Included within the depreciation charge for the year is £78k (2016: £nil) of additional depreciation in relation to the early termination of a property lease.

Company	Computer and other equipment £000	Motor Vehicles £000	Total £000
Cost or valuation			
At 1 January 2016	209	97	306
Additions	5	-	5
At 31 December 2016	**214**	**97**	**311**
At 31 December 2017	**214**	**97**	**311**
Accumulated depreciation			
At 1 January 2016	(80)	(22)	(102)
Depreciation charge	(2)	(24)	(26)
At 31 December 2016	**(82)**	**(46)**	**(128)**
Depreciation charge	(2)	(24)	(26)
At 31 December 2017	**(84)**	**(70)**	**(154)**
Net book amount			
At 31 December 2016	**132**	**51**	**183**
At 31 December 2017	**130**	**27**	**157**

31. Investment property

Group	2017 £000	2016 £000
Opening balance	53,339	-
Additions	6,100	50,200
Acquisition costs	321	3,139
Fair value adjustment	(321)	-
At 31 December 2017	**59,439**	**53,339**

King Street London

Arbuthnot Latham & Co., Limited acquired premises in the West End of London (namely 20 King Street/10 St James's Street) on 23 June 2016. The property comprises 22,450 square feet of office space and approximately 7,000 square feet of retail space. The property is held by way of leasehold from The Crown Estate Commissioners with 119 years unexpired and with a rent review every five years.

The property is currently fully tenanted, with the main lease ending in 2019. It is accounted for as investment property and the Group has elected to apply the fair value model. It is therefore initially recognised at cost and then subsequently at fair value. The fair value is determined using the rental income on the property and the associated effective yield of similar properties in the surrounding area (see note 4.1(d)). At 31 December 2017 there was no material difference between the cost of the property and the fair value. No independent valuation was undertaken at year end.

The Group received £2.1m (2016: £1.1m) rental income during the year and incurred £0.2m (2016: £0.1m) of direct operating expenses.

St Philips Place Birmingham

On 24 November 2017, Arbuthnot Latham & Co., Limited acquired leasehold premises in Birmingham (St Philips House, 4 St Philips Place). The property comprises 24,286 square feet of office space.

The property is unoccupied and will be refurbished at an estimated cost of £3.4m. After refurbishment the property will be let out. It is accounted for as investment property and the Group has elected to apply the fair value model. It is therefore initially recognised at cost and then subsequently at fair value. As the property was bought shortly before yearend, the capitalised acquisition costs of £0.3m were written off and the cost at acquisition was deemed to be the fair value. No independent valuation was undertaken at year end.

No property interests are held under operating leases and accounted for as investment property.

32. Deposits from banks

Group	2017 £000	2016 £000
Deposits from other banks	**195,097**	**3,200**

Deposits from banks include £188m obtained through the Bank of England Term Funding Scheme ("TFS"). For a maturity profile of deposits from banks, refer to Note 6.

33. Deposits from customers

Group	2017 £000	2016 £000
Current/demand accounts	868,855	610,512
Notice accounts	101,909	141,728
Term deposits	420,017	245,409
	1,390,781	**997,649**

Included in customer accounts are deposits of £29.2m (2016: £8.4m) held as collateral for loans and advances. The fair value of these deposits approximates their carrying value.

For a maturity profile of deposits from customers, refer to Note 6.

34. Other liabilities

Group	2017 £000	2016 £000
Trade payables	1,207	1,814
Accruals and deferred income	15,032	15,268
	16,239	**17,082**

Financial Services Compensation Scheme Levy

In common with all regulated UK deposit takers, AL pays levies to the Financial Services Compensation Scheme ("FSCS") to enable the FSCS to meet claims against the Scheme. The FSCS levy consists of two parts: a management expenses levy and a more significant compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation and associated interest the Scheme pays, net of any recoveries it makes using the rights that have been assigned to it.

The Group's FSCS provision reflects market participation up to the reporting date and the accrual of £0.1m (2016: £0.1m) relates to the interest levy for the Scheme year 2017/18 which is payable in September 2017. This amount was calculated on the basis of the Group's share of protected deposits and the FSCS's estimate of total interest levies payable for each Scheme year.

Company	2017 £000	2016 £000
Due to subsidiary undertakings	1,840	3,624
Accruals and deferred income	1,301	1,184
	3,141	**4,808**

35. Debt securities in issue

Group and Company	2017 £000	2016 £000
Subordinated loan notes	**13,104**	**12,621**

`The subordinated loan notes were issued on 7 November 2005 and are denominated in Euros. The principal amount outstanding at 31 December 2017 was €15,000,000 (2016: €15,000,000). The notes carry interest at 3% over the interbank rate for three month deposits in euros and are repayable at par in August 2035 unless redeemed or repurchased earlier by the Company.

The contractual undiscounted amount that will be required to be paid at maturity of the above debt securities is €15,000,000.

Given the fact that the Group has never been subject to a published credit rating by any of the relevant agencies and the notes in issue are not quoted, it is not considered possible to estimate a fair value for these notes.

36. Contingent liabilities and commitments

Contingent liabilities

The Group is subject to extensive regulation in the conduct of its business. A failure to comply with applicable regulations could result in regulatory investigations, fines and restrictions on some of the Group's business activities or other sanctions. The Group seeks to minimise this risk through the adoption of compliance and other policies and procedures, continuing to refine controls over business practices and behaviour, employee training, the use of appropriate documentation, and the involvement of outside legal counsel where appropriate.

Capital commitments

At 31 December 2017, the Group had capital commitments of £nil (2016: £nil) in respect of equipment purchases.

Credit commitments

The contractual amounts of the Group’s off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

Group	2017 £000	2016 £000
Guarantees and other contingent liabilities	2,976	274
Commitments to extend credit:		
- Original term to maturity of one year or less	131,963	54,934
	134,939	**55,208**

Operating lease commitments

Where a Group company is the lessee, the future aggregate lease payments under non-cancellable operating leases are as follows:

Group	2017 £000	2016 £000
Expiring:		
Within 1 year	2,330	2,635
Later than 1 year and no later than 5 years	10,943	8,422
Later than 5 years	5,384	5,745
	18,657	**16,802**

In 2013, Arbuthnot Latham & Co., Ltd entered into a 16 year lease on 7 Wilson Street, London (the head office for Arbuthnot Banking Group PLC, the principal location for Arbuthnot Latham & Co., Ltd and London offices for Secure Trust Bank PLC), with a break at 11 years and rent reviews after 5, 10 and 15 years. The initial rent is £1.75m per annum. This lease forms the most significant part of the operating leases disclosed in the table above.

In 2015, the Bank entered into a 10 year lease to occupy part of the ground floor of The Senate, Southernhay Gardens, Exeter, with a break clause and rent review after 5 years. The initial rent is £0.1m per annum.

In 2017, the Bank entered into a 10 year lease to occupy part of the eighth floor of 82 King Street, Manchester, with a break clause and rent review after 5 years. The initial rent is £0.1m per annum.

On 3 January 2018, Arbuthnot Latham entered into a 12 year lease (up to 16 October 2029) to occupy the first, second and third floor of 10 Dominion Street London, with a break clause on 16 October 2024. The initial rent is £0.7m per annum. This is reflected in the table above as an adjusting post balance sheet event.

Prior to the year end, the Bank reached agreement on the early termination of a property lease, which gave rise to an onerous lease provision of £0.3m (2016: £nil).

In addition to the above commitments, ground rent of £0.2m per annum is payable for the remaining term of 119 years of the King Street investment property.

37. Share capital

Group and Company	Number of shares	Ordinary share capital £000	Share premium £000
At 1 January 2016	15,279,322	153	-
At 31 December 2016 & December 2017	**15,279,322**	**153**	-

The Ordinary shares have a par value of 1p per share (2016: 1p per share). At 31 December 2017 the Company held 390,274 shares (2016: 390,274) in treasury.

38. Reserves and retained earnings

Group	2017 £000	2016 £000
Capital redemption reserve	20	20
Available-for-sale reserve	162	(251)
Treasury shares	(1,131)	(1,131)
Retained earnings	237,171	235,567
Total reserves at 31 December	**236,222**	**234,205**

The capital redemption reserve represents a reserve created after the Company purchased its own shares which resulted in a reduction of share capital.

Company	2017 £000	2016 £000
Capital redemption reserve	20	20
Treasury shares	(1,131)	(1,131)
Retained earnings	124,659	133,847
Total reserves as 31 December	**123,548**	**132,736**

39. Share-based payment options

Company – equity settled
The Company had no equity settled share-based payment awards outstanding at 31 December 2017.

On 1 April 2014 Mr Fleming was granted an option to subscribe for 50,000 ordinary 1p shares in the Company between April 2017 and April 2022 at 1185p. The fair value of these shares at grant date was £53,000. On 11 April 2017 Mr. Fleming exercised all his options granted on 1 April 2014 at a price of 1457p. The Board agreed to make a cash settlement rather than allot new shares.

On 16 April 2013 Mr. Salmon and Mr. Cobb were granted options to subscribe between April 2016 and April 2021 for 100,000 and 50,000 ordinary 1p shares respectively in the Company at 930p. The fair value of the options at grant date was £125,000. On 14 June 2016 Mr. Salmon and Mr. Cobb each exercised all their respective options granted on 16 April 2013 at a price of 1591p. The Board agreed to make a cash settlement rather than allot new shares.

No equity settled share options were granted, forfeited, or expired during the year. ABG incurred an expense in relation to share based payments of £4,000 during 2017 (2016: £31,000), as disclosed in Note 12. In line with the Group accounting policy, where the equity settled scheme was modified to cash settled, the entire liability totalling £155,000 (2016: £1,128,000) was accounted for as a reserves reclassification, with no profit or loss recognised in the Income Statement.

Measurement inputs and assumptions used in the Black-Scholes model are as follows:

	2016
Expected Stock Price Volatility	17%
Expected Dividend Yield	2.7%
Risk Free Interest Rate	1.20%
Average Expected Life (in years)	0.25

Company – cash settled
On 14 June 2016 Mr. Salmon was granted phantom options pursuant to the Phantom Option Scheme to acquire 200,000 ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in value. On 14 June 2016 Mr. Cobb and Mr. Henderson were each granted phantom options pursuant to the Phantom Option Scheme to acquire 100,000 ordinary 1p shares in the Company at 1591p exercisable in respect of 50% on or after 15 June 2019 and in respect of the remaining 50% on or after 15 June 2021 when a cash payment would be made equal to any increase in market value. The fair value of the options at grant date was £1.3m. At 31 December 2017, the fair value of the options was £0.8m.

The performance conditions of the Scheme are that for the duration of the vesting period, the dividends paid by ABG must have increased in percentage terms when compared to an assumed dividend of 29p per share in respect of the financial year ending 31 December 2016, by a minimum of the increase in the Retail Prices Index during that period.

Also from the grant date to the date the Option is exercised, there must be no public criticism by any regulatory authority on the operation of ABG or any of its subsidiaries which has a material impact on the business of ABG.

Options are forfeited if they remain unexercised after a period of more than 7 years from the date of grant. If the participant ceases to be employed by the Group by reason of injury, disability, ill-health or redundancy; or because his employing company ceases to be a shareholder of the Group; or because his employing business is being transferred out of the Group, his option may be exercised within 6 months after such cessation. In the event of the death of a participant, the personal representatives of a participant may exercise an option, to the extent exercisable at the date of death, within 6 months after the death of the participant.

On cessation of employment for any other reason (or when a participant serves, or has been served with, notice of termination of such employment), the option will lapse although the Remuneration Committee has discretion to allow the exercise of the option for a period not exceeding 6 months from the date of such cessation.

In such circumstances, the performance conditions may be modified or waived as the Remuneration Committee, acting fairly and reasonably and taking due consideration of the circumstances, thinks fit. The number of Ordinary Shares which can be acquired on exercise will be pro-rated on a time elapsed basis, unless the Remuneration Committee, acting fairly and reasonably and taking due consideration of the circumstances, decides otherwise. In determining whether to exercise its discretion in these respects, the Remuneration Committee must satisfy itself that the early exercise of an option does not constitute a reward for failure.

The probability of payout has been assigned based on the likelihood of meeting the performance criteria, which is 100%. The Directors consider that there is some uncertainty surrounding whether the participants will all still be in situ and eligible at the vesting date. Therefore the directors have assumed a 9% attrition rate for the share options vesting in June 2019 and 15% attrition rate for the share options vesting in June 2021. The attrition rate will increase by 3% per year until the vesting date. ABG incurred an expense in relation to share based payments of £0.2m during 2017 (2016: £0.2m), as disclosed in Note 12.

Measurement inputs and assumptions used in the Black-Scholes model are as follows:

	2017	2016
Expected Stock Price Volatility	27.0%	33.0%
Expected Dividend Yield	2.5%	2.3%
Risk Free Interest Rate	0.5%	0.4%
Average Expected Life (in years)	2.46	3.46

40. Dividends per share

Final dividends are not accounted for until they have been approved at the Annual General Meeting. At the meeting on 10 May 2017, a dividend in respect of 2017 of 19p per share (2016: actual dividend 18p per share) amounting to a total of £2.83m (2016: actual £2.68m) is to be proposed. The financial statements for the year ended 31 December 2017 do not reflect the final dividend which will be accounted for in shareholders' equity as an appropriation of retained profits in the year ending 31 December 2018.

41. Cash and cash equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents are comprised of the following balances with less than three months maturity from the date of acquisition.

Group	2017 £000	2016 £000
Cash and balances at central banks (Note 17)	313,101	195,752
Loans and advances to banks (Note 18)	70,679	36,951
	383,780	**232,703**

Company	2017 £000	2016 £000
Loans and advances to banks	**36,103**	**89,072**

42. Related party transactions

Related parties of the Company and Group include subsidiaries, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

Other than the directors' remuneration (see Remuneration Report pages 20 to 21), payment of dividends and transactions with subsidiaries and associates, there were no related party transactions within the Parent Company. A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits. Except for the directors' disclosures, there were no other Key Management Personnel disclosures; therefore the tables below relate to directors and their close family members.

Group - subsidiaries	2017 £000	2016 £000
Loans		
Loans outstanding at 1 January	1,361	3,123
Loans advanced during the year	150	2,076
Loan repayments during the year	(3)	(3,429)
Transferred to loans with associates	(1,000)	(409)
Loans outstanding at 31 December	**508**	**1,361**
Interest income earned	**23**	**122**

Group - associates	2017 £000	2016 £000
Loans		
Loans outstanding at 1 January	404	-
Loans advanced during the year	5	5
Loan repayments during the year	-	(10)
Transferred from loans with subsidiaries	1,000	409
Loans outstanding at 31 December	**1,409**	**404**
Interest income earned	**5**	**5**

The loans to directors are mainly secured on property, shares or cash and bear interest at rates linked to base rate. No provisions have been recognised in respect of loans given to related parties (2016: £nil).

	2017	2016

Group - subsidiaries	£000	£000
Deposits		
Deposits at 1 January	3,398	2,692
Deposits placed during the year	3,563	6,644
Deposits repaid during the year	(2,728)	(5,623)
Transferred to deposits with associates	(1,000)	(315)
Deposits at 31 December	**3,233**	**3,398**
Interest expense on deposits	**46**	**12**

	2017	2016
Group - associates	£000	£000
Deposits		
Deposits at 1 January	318	-
Deposits placed during the year	85	3
Transferred from deposits with subsidiaries	1,000	315
Deposits at 31 December	**1,403**	**318**
Interest expense on deposits	**5**	**3**

Details of directors' remuneration are given in the Remuneration Report. The Directors do not believe that there were any other transactions with key management or their close family members that require disclosure.

Details of principal subsidiaries are given in Note 43. Transactions and balances with subsidiaries are shown below:

	2017		2016	
	Highest balance during the year	Balance at 31 December	Highest balance during the year	Balance at 31 December
	£000	£000	£000	£000
ASSETS				
Due from subsidiary undertakings	89,150	36,256	150,776	89,224
Shares in subsidiary undertakings	97,802	97,802	54,602	54,602
	186,952	**134,058**	**205,378**	**143,826**
LIABILITIES				
Due to subsidiary undertakings	4,011	1,570	3,650	3,357
	4,011	**1,570**	**3,650**	**3,357**

The disclosure of the year end balance and the highest balance during the year is considered the most meaningful information to represent the transactions during the year. The above transactions arose during the normal course of business and are on substantially the same terms as for comparable transactions with third parties.

The Company undertook the following transactions with other companies in the Group during the year:

	2017	2016
	£000	£000
Arbuthnot Latham & Co., Ltd - Recharge of property and IT costs	1,087	1,087
Arbuthnot Latham & Co., Ltd - Recharge for costs paid on the Company's behalf	1,501	4,015
Arbuthnot Latham & Co., Ltd - Group recharges for shared services	(1,483)	(1,483)
Secure Trust Bank PLC (up to 15 June 2016 as subsidiary) - Group recharges for shared services	-	(212)
Secure Trust Bank PLC (up to 15 June 2016 as subsidiary) - Dividends received	-	(5,195)
Secure Trust Bank PLC (from 16 June 2016 as associate) - Group recharges for shared services	(813)	(490)
Secure Trust Bank PLC (from 16 June 2016 as associate) - Dividends received	(2,618)	(6,273)
Total	**(2,326)**	**(8,551)**

43. Interests in subsidiaries

Company	Investment at cost £000	Impairment provisions £000	Net £000
At 1 January 2016	49,030	(2,564)	46,466
Capital contributions to Arbuthnot Latham & Co., Limited	22,000	-	22,000
Disposal of Secure Trust Bank PLC	(13,864)	-	(13,864)
At 31 December 2016	**57,166**	**(2,564)**	**54,602**
Capital contributions to Arbuthnot Latham & Co., Limited	43,200	-	43,200
At 31 December 2017	**100,366**	**(2,564)**	**97,802**

Company	2017 £000	2016 £000
Subsidiary undertakings:		
Bank	95,502	52,302
Other	2,300	2,300
Total	**97,802**	**54,602**

(a) List of subsidiaries

Arbuthnot Latham & Co., Limited is the only significant subsidiary of Arbuthnot Banking Group. Arbuthnot Latham is incorporated in the United Kingdom, has a principal activity of Private and Commercial Banking and is 100% owned by the Group.

Secure Trust Bank PLC became an associate company of the Group from 15 June 2016.

The table below provides details of other subsidiaries and related undertakings of Arbuthnot Banking Group PLC at 31 December:

	% shareholding	Country of incorporation	Principal activity
Direct shareholding			
Arbuthnot Fund Managers Limited	100.0%	UK	Dormant
Arbuthnot Investments Limited	100.0%	UK	Dormant
Arbuthnot Limited	100.0%	UK	Dormant
Arbuthnot Properties Limited	100.0%	UK	Dormant
Arbuthnot Unit Trust Management Limited	100.0%	UK	Dormant
Gilliat Financial Solutions Limited	100.0%	UK	Dormant
Peoples Trust and Savings Plc	100.0%	UK	Dormant
Secure Trust Bank PLC*	18.6%	UK	Retail banking
West Yorkshire Insurance Company Limited	100.0%	UK	Non-trading
Windward Insurance Company PCC Limited	100.0%	Guernsey	Insurance
Indirect shareholding via intermediate holding companies			
Arbuthnot Latham (Nominees) Limited	100.0%	UK	Dormant
Arbuthnot Latham Real Estate Holdco Limited	100.0%	Jersey	Property Investment
Arbuthnot Latham Real Estate Holdings Limited	100.0%	UK	Property Investment
Arbuthnot Latham Real Estate PropCo Limited	100.0%	Jersey	Property Investment
Arbuthnot Real Estate Capital Limited	100.0%	Jersey	Property Investment
Arbuthnot Real Estate Capital GP 1 Limited	100.0%	Jersey	Property Investment
Arbuthnot Real Estate Capital Fund 1 Limited	100.0%	Jersey	Property Investment
Arbuthnot Securities Limited	100.0%	UK	Dormant
Artillery Nominees Limited	100.0%	UK	Dormant
Debt Managers (Services) Limited*	18.6%	UK	Debt collection company
John K Gilliat & Co., Limited	100.0%	UK	Dormant
Pinnacle Universal Limited	100.0%	BVI	Property development
Renaissance Asset Finance Limited	100.0%	UK	Asset Finance
Secure Homes Services Limited*	18.6%	UK	Property rental
STB Leasing Limited*	18.6%	UK	Leasing
V12 Finance Group Limited*	18.6%	UK	Holding company
V12 Personal Finance Limited*	18.6%	UK	Dormant
V12 Retail Finance Limited*	18.6%	UK	Sourcing and servicing of unsecured loans

* Treated as interests in associates.

All the subsidiary and related undertakings above are unlisted and none are banking institutions, except for Secure Trust Bank PLC. All 100% owned entities are included in the consolidated financial statements and have an accounting reference date of 31 December. All other entities are disclosed in the consolidated financial statements under interests in associates (see note 27). On 16 January 2018, Artillery Nominees Limited was dissolved.

All Jersey entities have their registered office as 26 New Street, St Helier, Jersey, JE2 3RA. Pinnacle Universal Limited's registered office is 9 Columbus Centre, Pelican Drive, Road Town, Tortola, BVI. The companies treated as associates have their registered office as One Arleston Way, Solihull, West Midlands, B90 4LH. All other entities listed above have their registered office as 7 Wilson Street, London, EC2M 2SN.

(b) Non-controlling interests in subsidiaries

There were no non-controlling interests at the end of 2016 or 2017.

(c) Significant restrictions

The Group does not have significant restrictions on its ability to access or use its assets and settle its liabilities other than those resulting from the supervisory frameworks within which banking subsidiaries operate. The supervisory frameworks require banking subsidiaries to keep certain levels of regulatory capital and liquid assets, limit their exposure to other parts of the Group and comply with other ratios. The carrying amounts of the banking subsidiary's assets and liabilities are £1,784m and £1,651m respectively (2016: £1,199m and £1,118m respectively).

(d) Risks associated with interests

During the year Arbuthnot Banking Group PLC made £43.2m (2016: £22m) capital contributions to Arbuthnot Latham & Co., Ltd. The contributions were made to assist the Bank during a period of growth to ensure that all regulatory capital requirements were met.

(e) Changes in ownership interest

On 15 June 2016 Arbuthnot Banking Group sold 6 million shares in Secure Trust Bank PLC ('STB') for £150m, which reduced its shareholding in STB from 51.92% to 18.93%. From this date the Group accounted for its remaining shareholding in STB as an associate. After the sale of the 6 million shares, the Group retained Board representation and as a result is seen to have significant influence over STB.

44. Operating segments

The Group is organised into three main operating segments, arranged over three separate companies with each having its own specialised banking service, as disclosed below:

1) Retail banking (associate) — incorporating household cash management, personal lending and banking and insurance services.
2) UK Private banking — incorporating private banking, commercial banking and wealth management.
3) Group Centre – ABG Group Centre management

Transactions between the operating segments are on normal commercial terms. Centrally incurred expenses are charged to operating segments on an appropriate pro-rata basis. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balance sheet.

	Continuing operations			
Year ended 31 December 2017	Retail Bank Associate Income £000	UK Private banking £000	Group Centre £000	**Total £000**
Interest revenue	-	47,601	204	**47,805**
Inter-segment revenue	-	(174)	(204)	**(378)**
Interest revenue from external customers	-	47,427	-	**47,427**
Fee and commission income	-	13,805	-	**13,805**
Revenue from external customers	-	**61,232**	-	**61,232**
Interest expense	-	(6,199)	225	**(5,974)**
Add back inter-segment revenue	-	174	(174)	-
Subordinated loan note interest	-	-	(360)	**(360)**
Fee and commission expense	-	(282)	-	**(282)**
Segment operating income	-	54,925	(309)	**54,616**
Impairment losses	-	(394)	-	**(394)**
Other income	-	3,870	(837)	**3,033**
Income from associates	4,437			**4,437**
Operating expenses	-	(47,442)	(7,279)	**(54,721)**
Segment profit / (loss) before tax	4,437	10,959	(8,425)	**6,971**
Income tax (expense) / income	-	(540)	92	**(448)**
Segment profit / (loss) after tax	**4,437**	**10,419**	**(8,333)**	**6,523**
Segment profit / (loss) after tax	**4,437**	**10,419**	**(8,333)**	**6,523**
Loans and advances to customers		1,049,269	-	**1,049,269**
Other assets		734,406	69,557	**803,963**
Segment total assets		**1,783,675**	**69,557**	**1,853,232**
Customer deposits		1,390,781	-	**1,390,781**
Other liabilities		259,957	(33,881)	**226,076**
Segment total liabilities		**1,650,738**	**(33,881)**	**1,616,857**
Other segment items:				
Capital expenditure		(3,307)	-	**(3,307)**
Depreciation and amortisation		(2,354)	(26)	**(2,380)**

The "Group Centre" segment above includes the parent entity and all intercompany eliminations.

Year ended 31 December 2016	Discontinued operations (Retail Banking) ELL £000	STB £000	Total £000	Continuing operations UK Private banking £000	UK Private banking £000	Group Centre £000	Total £000	Group Total £000
Interest revenue	11,137	57,498	**68,635**	-	38,245	285	**38,530**	
Inter-segment revenue	-	-	-	-	(174)	(285)	**(459)**	
Interest revenue from external customers	11,137	57,498	**68,635**	-	38,071	-	**38,071**	
Fee and commission income	147	7,981	**8,128**	-	11,430	-	**11,430**	
Revenue from external customers	11,284	65,479	**76,763**	-	**49,501**	-	**49,501**	
Interest expense	-	(12,107)	**(12,107)**	-	(7,474)	200	**(7,274)**	
Add back inter-segment revenue	-	-	-	-	174	(174)	-	
Subordinated loan note interest	-	-	-	-	-	(352)	**(352)**	
Fee and commission expense	(124)	(779)	**(903)**	-	(425)	-	**(425)**	
Segment operating income	11,160	52,593	**63,753**	-	41,776	(326)	**41,450**	
Impairment losses	(2,610)	(12,172)	**(14,782)**	-	(474)	-	**(474)**	
Other income	-	-	-	-	4,353	(1,184)	**3,169**	
Income from associates	-	-	-	2,145	-	-	**2,145**	
Operating expenses	(6,016)	(29,073)	**(35,089)**	-	(36,602)	(9,509)	**(46,111)**	
Segment profit / (loss) before tax	2,534	11,348	**13,882**	2,145	9,053	(11,019)	**179**	**14,061**
Income tax (expense) / income	(507)	(2,199)	**(2,706)**	-	(211)	(509)	**(720)**	**(3,426)**
Segment profit / (loss) after tax	2,027	9,149	**11,176**	**2,145**	**8,842**	**(11,528)**	**(541)**	**10,635**
Profit on sale of discontinued operations	116,754	100,180	**216,934**	-	-	-	-	**216,934**
Segment profit / (loss) after tax	118,781	109,329	**228,110**	**2,145**	**8,842**	**(11,528)**	**(541)**	**227,569**
Loans and advances to customers				-	758,799	-	**758,799**	
Other assets				-	440,363	66,122	**506,485**	
Segment total assets				-	**1,199,162**	**66,122**	**1,265,284**	**1,265,284**
Customer deposits				-	997,649	-	**997,649**	
Other liabilities				-	120,815	(87,538)	**33,277**	
Segment total liabilities				-	**1,118,464**	**(87,538)**	**1,030,926**	**1,030,926**
Other segment items:								
Capital expenditure				-	(5,504)	(5)	**(5,509)**	
Depreciation and amortisation				-	(1,641)	(26)	**(1,667)**	

Segment profit is shown prior to any intra-group eliminations.

The UK private bank has a branch in Dubai, which generated £4.5m (2016: £3.1m) fee income and had operating costs of £2.7m (2016: £2.2m). All Dubai branch income is booked in the UK. Other than the Dubai branch, all operations of the Group are conducted wholly within the United Kingdom and geographical information is therefore not presented.

45. Country by Country Reporting

Article 89 of the EU Directive 2013/36/EU otherwise known as the Capital Requirements Directive IV ('CRD IV') was implemented into UK domestic legislation through statutory instrument 2013 No. 3118, the Capital Requirements (Country-by-Country Reporting) Regulations 2013 (the Regulations), which were laid before the UK Parliament on 10 December 2013 and which came into force on 1 January 2014.

Article 89 requires credit institutions and investment firms in the EU to disclose annually, specifying, by Member State and by third country in which it has an establishment, the following information on a consolidated basis for the financial year: name, nature of activities, geographical location, turnover, number of employees, profit or loss before tax, tax on profit or loss and public subsidies received.

31 December 2017			Turnover	Number FTE	Profit/(loss)	Tax paid
Name	Nature of activity	Location	(£m)	employees	before tax (£m)	(£m)
Arbuthnot Banking Group PLC	Banking Services	UK	54.6	350	9.8	-
Arbuthnot Banking Group PLC	Banking Services	Dubai	-	16	(2.7)	-

31 December 2016			Turnover	Number FTE	Profit/(loss)	Tax paid
Name	Nature of activity	Location	(£m)	employees	before tax (£m)	(£m)
Arbuthnot Banking Group PLC	Banking Services	UK	105.2	272	247.1	6.1
Arbuthnot Banking Group PLC	Banking Services	Dubai	-	15	(2.2)	-

The Dubai branch income is booked through the UK, hence the turnover is nil in the above analysis. Offsetting this income against Dubai branch costs would result in a £1.8m profit (2016: £0.9m). No public subsidies were received during 2017 or 2016.

46. Ultimate controlling party

The Company regards Sir Henry Angest, the Group Chairman and Chief Executive Officer, who has a beneficial interest in 54.7% of the issued share capital of the Company, as the ultimate controlling party. Details of his remuneration are given in the Remuneration Report and Note 42 of the consolidated financial statements includes related party transactions with Sir Henry Angest.

47. Events after the balance sheet date

On 3 January 2018, Arbuthnot Latham entered into a 12 year lease (up to 16 October 2029) to occupy the first, second and third floors of 10 Dominion Street London, with a break clause on 16 October 2024. The initial rent is £0.7m per annum. This is reflected in contingent liabilities (Note 36) as an adjusting post balance sheet event.

Five Year Summary

		2013	2014	2015	2016	2017
		£000	£000	£000	£000	£000
Profit for the year after tax		11,515	17,016	26,524	227,569	6,523
Profit before tax from continuing operations*		(1,480)	(3,824)	(2,606)	179	6,971
Total Earnings per share						
Basic (p)		53.8	58.6	86.3	1,127.2	43.9
Earnings per share from continuing operations*						
Basic (p)		(5.7)	(24.8)	(16.9)	(3.7)	43.9
Dividends per share (p)	- ordinary	26.0	27.0	29.0	31.0	33.0
	- special	18.0	-	-	325.0	-

Other KPI:

	2013	2014	2015	2016	2017
	£000	£000	£000	£000	£000
Net asset value per share (p)	570.5	1,136.0	1,252.7	1,533.8	1,547.0

* - Prior year numbers have been restated for continuing operations.