

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

Registered Number: OC322580

ANNUAL REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2019

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

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YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

REGISTERED NUMBER: OC322580

MEMBERS AND PARTNERSHIP INFORMATION

Members

Yorkshire Building Society
YBS Covered Bonds Finance Limited

Registered Office

Yorkshire House
Yorkshire Drive
Bradford
Yorkshire
BD5 8LJ

Account Bank

Yorkshire Building Society
Yorkshire House
Yorkshire Drive
Bradford
BD5 8LJ

Standby Account Bank

HSBC Bank plc
8 Canada Square
London
E14 5HQ

Independent Auditors

PricewaterhouseCoopers LLP
Central Square,
29 Wellington Street
Leeds
LS1 4DL

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

MEMBERS' REPORT

The members present their annual report and audited financial statements for Yorkshire Building Society Covered Bonds LLP (the "LLP") for the year ended 31 December 2019.

PRINCIPAL ACTIVITIES

The LLP is a special purpose vehicle whose business is the acquisition and management of mortgage loans and their related security. The principal activities of the LLP are summarised in the LLP Deed dated 1 November 2006. The activities of the LLP are dependent upon the future funding strategies within the partnership's UK controlling undertaking, Yorkshire Building Society.

GOING CONCERN

The LLP has adequate financial resources to be considered as a going concern due to the financial guarantee from Yorkshire Building Society. The activities of the LLP are dependent on the future funding strategies within the LLP's controlling parent undertaking, Yorkshire Building Society. Assessment of the impacts of the UK's withdrawal from the EU has also been conducted by the parent undertaking and the members of the LLP have a reasonable expectation that the LLP will be able to continue in operation and meet its obligations as they fall due. The LLP has Euro denominated liabilities that have been hedged with the use of cross currency swap positions.

There are no plans to terminate the operations of the LLP within the next year. Therefore it is appropriate to adopt the going concern basis in preparing the financial statements.

DESIGNATED MEMBERS

The designated members during the year and to the date of this report were Yorkshire Building Society and YBS Covered Bonds Finance Limited.

In the event of Yorkshire Building Society going into administration or liquidation, the second member, YBS Covered Bonds Finance Limited, will appoint another member.

MEMBERS' INTERESTS

The policy regarding the allocation of profits to members and the treatment of capital contributions is set out in the significant accounting policies note (note 1).

FINANCIAL INSTRUMENTS

The LLP's financial instruments comprise a loan to Yorkshire Building Society (equivalent to the value of the LLP's investment in Yorkshire Building Society mortgages), cash and liquid resources, derivatives, borrowings and various receivables and payables that arise directly from its operations. The main purpose of these financial instruments is to raise finance for Yorkshire Building Society.

It is, and has been throughout the year under review, the LLP's policy that no trading in financial instruments is undertaken. Further discussion of the LLP's approach to financial instruments is set out in the significant accounting policies note (note 1).

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

AUDIT INFORMATION

Each of the persons who is a member at the date of approval of this annual report and financial statements confirms that:

- so far as the member is aware, there is no relevant audit information of which the firm's auditors are unaware; and
- the member has taken all the steps that they ought to have taken as a member in order to make themselves aware of any relevant audit information and to establish that the LLP's auditors are aware of that information.

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

INDEPENDENT AUDITORS

PricewaterhouseCoopers LLP were approved and appointed as auditors by order of the Board of Directors.



A Lenman
on behalf of
Yorkshire Building Society

5 March 2020



C L Parrish
on behalf of
YBS Covered Bonds Finance Ltd

5 March 2020

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

MEMBERS' RESPONSIBILITIES STATEMENT

The members are responsible for preparing the annual report and the financial statements in accordance with applicable law and regulations.

The Limited Liability Partnerships (Accounts & Audit) (Application of Companies Act 2006) Regulations 2008 require the members to prepare financial statements for each financial year. Under that law the members have elected to prepare the financial statements in accordance with IFRSs as adopted by the European Union. The financial statements are also required by law to be prepared in accordance with the Companies Act 2006, as applicable to limited liability partnerships.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the firm's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's 'Framework for the preparation and presentation of financial statements'. In virtually all circumstances, a fair presentation will be achieved by compliance with all applicable IFRSs. However, members are also required to:

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

The members are responsible for keeping adequate accounting records that disclose with reasonable accuracy at any time the financial position of the firm and enable them to ensure that the financial statements comply with the Companies Act 2006, as applicable to limited liability partnerships. They are also responsible for safeguarding the assets of the firm and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

These responsibilities are exercised by the Covered Bond Management Committee on behalf of the members.

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STRATEGIC REPORT

BUSINESS REVIEW

The LLP's business activities, together with the factors likely to affect the future development, performance and position are set out below. The financial position of the LLP, its cash flows, liquidity position and borrowing facilities are set out in the financial statements. The LLP's objectives, policies and processes for managing its capital are described in note 14 to the financial statements.

Details of the LLP's financial risk management objectives, its financial instruments and hedging activities, and its exposures to operational, liquidity risk and other risks are set out in note 13 to the financial statements.

Yorkshire Building Society is required to buy back mortgages that breach Representations and Warranties from the LLP, or if the property has been voluntarily surrendered by the borrower. There is no loss suffered by the LLP, as this buy-back comprises all outstanding amounts, including all arrears on the mortgage accounts. Details of this financial guarantee from Yorkshire Building Society are set out in note 12.

The financial performance and position of the Yorkshire Building Society Group, which includes the LLP, are discussed in the Group's report and financial statements which does not form part of this report.

The LLP made a loss for the year of £3.5m (2018 - £3.5m). This is due to fair value adjustments on financial instruments.

RISK MANAGEMENT

Risk management within the LLP is undertaken by the Yorkshire Building Society. The Group maintains an independent risk management function that applies its risk management policies and techniques to the risks of the Group as a whole and therefore appropriate risk management activities are deployed wherever risks arise.

The Group, through the Treasury function, monitors and manages wholesale credit risk using its own internal rating for all its counterparties and sets individual limits accordingly. These limits are regularly reviewed internally and against external rating agencies, with revocation or suspension taking place where considered appropriate. Wholesale related credit risks are reported and discussed monthly at the Asset and Liability Committee. Market risk within the LLP is minimised by the use of loans and deposits with the Society.

The most significant retail credit risk that the Group is exposed to, which has particular relevance to the LLP, relates to its core business of providing loans secured on residential property. The beneficial interests in the mortgage portfolio represent the collateral for the loan to originator. A robust credit risk framework helps to ensure that lending remains within risk appetite limits. Adherence is monitored regularly through governance committees. The Group lends to households across the UK and does not consider there to be any significant concentration of credit risks in any particular part of the UK.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

In addition to the risk management explained above, the LLP has in place a Covered Bond Management Committee. This committee meets monthly and is chaired by the Director of Treasury. Its objective is to review and approve a number of reports relating to the Covered Bond programme, including the Investor report, Asset and Liability Committee paper and the Asset Coverage Test report.


A Lenman
On behalf of
Yorkshire Building Society

5 March 2020


C L Parrish
On behalf of
YBS Covered Bonds Finance Ltd

5 March 2020

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

INDEPENDENT AUDITORS REPORT TO THE MEMBERS OF YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

Report on the audit of the financial statements

Opinion

In our opinion, Yorkshire Building Society Covered Bonds LLP's financial statements:

- give a true and fair view of the state of the limited liability partnership's affairs as at 31 December 2019 and of its loss and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006 as applied to limited liability partnerships by the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008.

We have audited the financial statements, included within the Annual Report and Financial Statements (the "Annual Report"), which comprise: the statement of financial position as at 31 December 2019; the income statement, the statement of cash flows, the statement of changes in members' interest for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the limited liability partnership in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Conclusions relating to going concern

ISAs (UK) require us to report to you when:

- the members' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the members have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the limited liability partnership's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of the above matters.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the limited liability partnership's ability to continue as a going concern. For example, the terms of the United Kingdom's withdrawal from the European Union are not clear, and it is difficult to evaluate all of the potential implications on the limited liability partnership's trade, customers, suppliers and the wider economy.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The members are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

Responsibilities for the financial statements and the audit

Responsibilities of the members for the financial statements

As explained more fully in the Members' Responsibilities Statement set out on page 4, the members are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The members are also 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.

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

Auditors' responsibilities for the audit of the financial statements

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

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

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

Use of this report

This report, including the opinion, has been prepared for and only for the members of the partnership as a body in accordance with the Companies Act 2006 as applied to limited liability partnerships by the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 as applicable to limited liability partnerships we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the limited liability partnership, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.



Martin Cross (Senior Statutory Auditor)

for and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

Leeds

5 March 2020

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

INCOME STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 £000	2018 £000
Interest receivable and similar income	3	33,811	31,422
Interest payable and similar charges	4	(33,804)	(31,409)
Net interest income		<u>7</u>	<u>13</u>
Operating expenses	5	(7)	(13)
Operating result		<u>-</u>	<u>-</u>
Net losses on fair value volatility on financial instruments	6	(3,470)	(3,451)
Loss before tax		<u>(3,470)</u>	<u>(3,451)</u>
Loss for the year for discretionary division among members		<u>(3,470)</u>	<u>(3,451)</u>

The loss shown above is derived from continuing operations.

The LLP has no income or expense in the year other than the loss stated above. Consequently no Statement of Comprehensive Income has been presented.

The notes on pages 13 to 25 form part of these financial statements.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2019

	Note	2019 £000	2018 £000
Assets			
Loan to originator	7	3,131,766	1,981,219
Derivative financial instruments		170,614	260,168
Loans and advances to credit institutions	8	120,467	83,413
Total assets		3,422,847	2,324,800
Liabilities			
Interest bearing loans and borrowings	9	3,403,148	2,311,778
Other payables	10	12,989	8,497
Derivative financial instruments		5,655	-
Total liabilities		3,421,792	2,320,275
Equity			
Retained surplus	14	1,055	4,525
Total equity		1,055	4,525
Total liabilities and equity		3,422,847	2,324,800

STATEMENT OF CHANGES IN MEMBERS' INTERESTS FOR THE YEAR ENDED 31 DECEMBER 2019

	2019 £000	2018 £000
Net assets attributable to members		
Balance at 1 January	4,525	7,976
Loss for the year	(3,470)	(3,451)
Balance at 31 December	1,055	4,525

The notes on pages 13 to 25 form part of these financial statements.

These financial statements were approved by the members and authorised for issuance on 5 March 2020 and were signed on their behalf by:



A Lenman
On behalf of
Yorkshire Building Society



C L Parrish
On behalf of
YBS Covered Bonds Finance Ltd

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	2019 £000	2018 £000
Cash flows from operating activities			
Loss before tax		(3,470)	(3,451)
Operating assets:			
Net increase/(decrease) in loan to originator		(1,150,547)	263,783
Net decrease in derivative financial instruments		89,554	10,040
Operating liabilities:			
Net decrease in loans and borrowings		(86,190)	(6,109)
Net increase/(decrease) in other payables		4,492	(404)
Net increase in derivative financial instruments		5,655	-
Net cash flows (used in)/generated from operating activities		(1,140,506)	263,859
Cash flows from financing activities			
Proceeds from loans and borrowings	11	1,177,560	(250,000)
Net cash flows generated from/(used in) financing activities		1,177,560	(250,000)
Net increase in cash and cash equivalents		37,054	13,859
Opening balance		83,413	69,554
Total closing cash and cash equivalents		120,467	83,413
Cash and cash equivalents			
Loans and advances to credit institutions		120,467	83,413

The notes on pages 13 to 25 form part of these financial statements.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

NOTES TO THE FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING POLICIES

Introduction

Yorkshire Building Society Covered Bonds LLP (the "LLP") is a special purpose vehicle whose business is the acquisition and management of mortgage loans and their related security. It is a Limited Liability Partnership domiciled and registered in the United Kingdom.

Basis of preparation

The financial statements have been prepared in accordance with international accounting standards, being International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and interpretations issued by the International Accounting Standards Board (IASB) that are effective as at 31 December 2019 and have been endorsed by the European Union (EU).

The financial statements have been prepared on the historical cost basis, as modified by the revaluation of derivative contracts.

Pounds sterling is both the functional currency of the Company and the presentation currency applied to these financial statements.

Except where otherwise stated, all figures in the financial statements are presented in thousands of pounds sterling (£000).

The financial statements have been prepared on the going concern basis as discussed in the Members' Report on page 2, under the heading, 'Going concern'.

The preparation of financial statements under IFRS requires the use of certain critical accounting estimates and judgement. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are set out in Note 2.

Accounting Developments

The following Accounting Standard amendments became mandatorily effective for periods commencing on or after 1 January 2019 and have been adopted in the current year. Their adoption, unless otherwise stated, has not had any impact on the disclosures or on the amounts reported in these financial statements:

- IFRS 16 'Leases' sets out the principles for the recognition, measurement, presentation and disclosure of leases. IFRS 16 eliminates the distinction between operating and finance leases that exists under IAS 17, with virtually all leases recognised on Balance Sheet.
- IFRIC 23 'Uncertainty over Income Tax Treatments', provides guidance on how to determine taxable profit when there is uncertainty over the income tax treatment under IAS 12 'Income Taxes'.
- Amendments to IAS 19 for defined benefit pension schemes. This amendment applies to where settlements, curtailments or amendments occur for the pension plan. This amendment clarifies the treatment of past service cost, current service cost and net interest.
- Amendments to IFRS 9 for prepayment features with negative compensation. This amendment clarifies whether instruments with certain prepayment features meet the 'solely payments of principal and interest' condition within IFRS 9.

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- Amendments to IAS 28 for long-term interests in associates and joint ventures. This amendment clarifies that the IFRS 9 impairment requirements apply to financial interests in an associate or joint venture to which the equity method is not applied.
- Minor amendments to IAS 12 'Income Taxes', IAS 23 'Borrowing costs', IFRS 3 'Business Combinations' and IFRS 11 'Joint Arrangements' under the Annual Improvements to IFRSs 2015-2017 Cycle.

The following Standards which have not been adopted in these financial statements were in issue but not yet effective for the 2019 year end. Except otherwise stated, the adoption of the following new or amended standards are not expected to have material impact on the financial statements.

- IFRS 17 'Insurance Contracts' is due to be effective for periods beginning on or after 1 January 2021 although it may be deferred until 2022. IFRS 17 is the comprehensive IFRS establishing specific accounting requirements for insurance contracts. This replaces IFRS 4 for which entities were permitted to account for insurance contracts differently across jurisdictions.
- Amendments to IFRS 3 providing clarification to the definition of a business which is effective for periods beginning on or after 1 January 2020.
- Amendments to IAS 1 and IAS 8 providing clarification to the definition of material which is effective for periods beginning on or after 1 January 2020.
- Amendments to a number of standards and interpretation guidance to amend references to the revised Conceptual Framework that was published in March 2018. These amendments are effective for annual periods beginning on or after 1 January 2020.

The following is a list of the company's significant accounting policies.

Interest income and expense

Interest income and expense on all financial instruments are recognised within interest receivable or payable on an effective interest rate basis.

The effective interest rate is a method of calculating the amortised cost of financial instruments and of allocating interest income and expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated cash flows (excluding credit losses) through the expected life of the instrument to the net carrying amount at initial recognition.

Tax

Tax is recognised in the Income Statement except to the extent that it relates to items recognised directly in equity, in which case the tax is recognised in the Statement of Comprehensive Income.

Current tax is the expected tax payable on the taxable profits for the year, using tax rates enacted or the substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

Deferred consideration payable

Deferred consideration payable depends on the extent to which the surplus income generated by the underlying mortgage books to which the Company has a beneficial interest, exceeds the administration costs of the mortgage books, and is deducted from interest income, since the Company does not recognise income to which it is not beneficially entitled. Contingent deferred consideration arising in future periods is recorded in the income statement in the period in which it arises.

Financial Instruments

The Company's financial instruments comprise principally of deemed loans due from group undertakings, derivative financial instruments, debt securities in issue and cash and cash equivalents. These financial instruments are classified in accordance with the principles of IFRS as described below.

i. Cash and cash equivalents

The Company holds deposits and a transaction bank account. These financial statements are held in the Company's name and meet the definition of cash and cash equivalents but their use is restricted by a detailed priority of payments set out in the Secured Funding Programme Documentation (the "Programme Documentation"). As the cash can only be used to meet certain specific liabilities and is not available to be used with discretion, it is viewed as restricted cash.

ii. Deemed loan

In accordance with IFRS 9, and IAS 39 in the prior period, where a transfer of a financial asset does not qualify for derecognition in the financial statements of the transferor, the transferee does not recognise the transferred asset as its asset. The transferee derecognises the cash or other consideration paid and recognises a receivable from the transferor. In relation to the mortgage portfolios transferred to the LLP, derecognition is considered to be inappropriate for the Originator's (Yorkshire Building Society) own financial statements as the Originator has retained significant risks and rewards of ownership of that financial asset. The LLP's financial statements are therefore prepared on the basis that those acquisitions of beneficial interests in mortgage portfolios are recognised as a collateralised loan to the Originator.

iii. Deferred consideration

Under the terms of the mortgage sale agreement, the Originator retains the right to receive excess income arising on those loans, after certain higher priority payments have been met by the Company. As per the programme requirements, any surplus receipts from the receivables after servicing the notes and all other obligations of the Company are payable to the originator. These amounts are presented as a deduction of interest income in the income statement with amounts outstanding at year end being recorded as 'Other payables' in the statement of financial position.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

iv. Derivative financial instruments

The Company uses derivative financial instruments to hedge its exposure to interest rate risk arising from investment activities. The Company does not hold or issue derivative financial instruments for trading purposes.

IFRS 9 requires all derivative financial instruments to be recognised initially at fair value in the statement of financial position. Subsequent to initial recognition, derivatives are re-measured to fair value. The gain or loss on re-measurement to fair value is recognised immediately in the income statement. The fair value of interest rate swaps is the estimated amount that the Company would receive or pay to terminate the swap or transfer to another party at the reporting date taking into account current interest rates and the current creditworthiness of the swap counterparty.

Interest income and expense on the swaps is accounted for under the effective interest rate method within interest receivable and payable in the income statement.

v. Hedging

All derivatives entered into by the LLP are for the purposes of providing an economic hedge. Hedge accounting is applied when the specific rules and conditions in IAS 39 are fulfilled. The LLP has classified its derivatives as fair value hedges in order to reduce volatility in the Income Statement.

Where the fair value hedging requirements are met, changes in the fair value of the hedged item arising from the hedged risk are taken to the Income Statement thereby offsetting the effect of the related movements in the fair value of the derivative. Where the hedge no longer meets the criteria, or is terminated for any other reason, the adjustment to the hedged item is released to the Income Statement, over its remaining life, using the effective interest rate method.

vi. Debt securities in issue

Interest-bearing debt securities in issue are recognised initially at fair value. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings under the effective interest rate method. Directly attributable issue costs, including premiums and discounts, commissions and other costs incurred in the issuing of fixed and floating rate notes are amortised using the effective interest rate method.

vii. Financial Liabilities

Financial liabilities are contractual obligations to deliver cash or some other asset to a third party. They include:

- derivatives
- debt securities; and
- other borrowed funds and liabilities

Financial liabilities are recognised initially at fair value. Fair value includes the issue proceeds (the fair value of consideration received) net of issue costs incurred.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

Financial liabilities, other than derivatives, are subsequently stated at amortised cost. Any difference between issue proceeds net of issue costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest rate method. Directly attributable issue costs, including premiums and discounts, commissions and other costs incurred in the issuing of fixed and floating rate notes are amortised using the effective interest rate method.

2. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

The Company makes no key judgements in applying its accounting policies that have a significant impact on the amounts recognised in the financial statements. Estimates and assumptions are used which could affect the reported amounts of assets and liabilities in the next financial year.

The most critical key source of estimation uncertainty relates to fair value.

The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale and are measured at fair value with the resultant profits or losses included in the income statement.

The fair values of the derivatives are based on counterparty valuations, which is the best estimate of the exit value of the derivatives. This is analysed further in Note 13.

3. INTEREST RECEIVABLE AND SIMILAR INCOME

	2019 £000	2018 £000
On deemed loan	33,353	25,102
On other liquid assets	427	277
Derivative financial instruments in hedge relationships	31	6,043
	<u>33,811</u>	<u>31,422</u>

4. INTEREST PAYABLE AND SIMILAR CHARGES

	2019 £000	2018 £000
On deposits from connected undertakings	20,272	23,340
On derivative financial instruments in hedge relationships	13,532	8,069
	<u>33,804</u>	<u>31,409</u>

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

5. OPERATING EXPENSES

	2019 £000	2018 £000
Loss for the year has been arrived at after charging		
Servicer fees	7	13
	7	13

Fees payable of £12,500 (2018 - £5,628) to the LLP's auditors for the audit of the LLP's annual financial statements have been borne by the parent. There were no other fees paid to the auditors.

6. NET LOSSES ON FAIR VALUE VOLATILITY ON FINANCIAL INSTRUMENTS

	2019 £000	2018 £000
Derivative financial instruments and hedging	(3,470)	(3,451)
	(3,470)	(3,451)

7. LOAN TO ORIGINATOR

	Total £000
At 1 January 2019	1,981,219
Pool additions	2,461,127
Repayments	(1,310,580)
At 31 December 2019	3,131,766

Loan to originator is due in over 1 year. This is collateralised by the benefit interests in the underlying mortgage portfolios.

8. LOANS AND ADVANCES TO CREDIT INSTITUTIONS

The LLP places available revenue and principal receipts in a deposit account with an external credit institution. Withdrawals from this account are restricted by the detailed priority of payments set out in the Programme Documentation. The LLP is contractually entitled to a variable rate of interest of 0.25 per cent per annum below LIBOR for one-month Sterling deposits.

The Financial Conduct Authority have informed all market participants that they must remove any dependency on the London Interbank Offered Rate (LIBOR) by end 2021, when the formal publication of LIBOR data will cease. The Company will amend the loan agreements to reflect new alternative measures as appropriate if the notes remain unpaid at this time.

YORKSHIRE BUILDING SOCIETY COVERED BONDS LLP

9. INTEREST BEARING LOANS AND BORROWINGS

Interest-bearing loans and borrowings comprise a series of term advances from Yorkshire Building Society, equivalent to the amounts raised by Yorkshire Building Society under its Covered Bonds Programme.

Yorkshire Building Society will not be relying on repayment of any term advance by the LLP or the interest thereon in order to meet its repayment or interest obligations under the Covered Bonds. The term advances will not be repaid by the LLP until all amounts payable under the corresponding series of Covered Bonds have been repaid in full. Amounts owed by the LLP will be subordinated to amounts owed by the LLP under the Covered Bond Guarantee described below.

The Covered Bonds are unconditionally guaranteed by Yorkshire Building Society. Under the terms of the Trust Deed, the LLP has also provided a guarantee as to payments of interest and principal under the Covered Bonds, where amounts would otherwise be unpaid by Yorkshire Building Society.

The obligations of the LLP under its guarantee constitute direct obligations of the LLP secured against the assets from time to time of the LLP and recourse against the LLP is limited to such assets. The principal asset is the beneficial interest in the mortgage loans acquired from Yorkshire Building Society.

In this respect, the LLP treats the above guarantee contract as a contingent liability until such time as it becomes probable that the LLP will be required to make a payment under the guarantee. The amounts due to Yorkshire Building Society mature on the following dates:

Covered Bond	Maturity Date	Interest Date	2019 £000	2018 £000
9	11 June 2021	Fixed 1.25%	428,400	450,676
10	19 June 2020	Fixed 0.500%	426,583	448,761
11	10 November 2022	Fixed 0.750%	425,887	448,017
12	11 April 2023	Fixed 0.375%	426,591	448,779
13	20 November 2023	SONIA	500,754	500,749
14	08 May 2024	Fixed 0.125%	425,794	-
15	21 November 2024	SONIA	751,061	-
Fair value hedging adjustments			18,078	14,796
			<u>3,403,148</u>	<u>2,311,778</u>

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10. OTHER PAYABLES

	2019	2018
	£000	£000
Deferred consideration	12,983	8,497
Intercompany liability	6	-
	12,989	8,497

11. NOTES TO THE STATEMENT OF CASH FLOWS

The Statement of Cash Flows has been prepared in compliance with 'International Accounting Standard 7 Statement of Cash Flows' and is presented under the indirect method.

The Statement of Cash Flows presents cash flows classified by operating, investing and financing activities. The net cash flows from all three categories are totalled to show the movement in cash and cash equivalents during the year, which is then used to reconcile cash and cash equivalents.

For the purposes of the Statement of Cash Flows, 'cash and cash equivalents' comprise cash and other financial instruments with less than three months original maturity.

Reconciliation of liabilities arising from financing activities	2018	Cash flows		Non cash changes caused by			2019
		Redemption	Issue	Foreign exchange	Accrued interest	Fair value adjustment	
	£000	£000	£000	£000	£000	£000	£000
Loans and Borrowings	2,311,778	-	1,177,560	(90,570)	1,099	3,281	3,403,148

Reconciliation of liabilities arising from financing activities	2017	Cash flows		Non cash changes caused by			2018
		Redemption	Issue	Foreign exchange	Accrued interest	Fair value adjustment	
	£000	£000	£000	£000	£000	£000	£000
Loans and Borrowings	2,567,887	(750,000)	500,000	15,580	(24,876)	3,187	2,311,778

12. FINANCIAL GUARANTEE FROM YORKSHIRE BUILDING SOCIETY

Yorkshire Building Society has provided a financial guarantee to the LLP, the terms of which, as detailed in the Programme Documentation, are described below.

Yorkshire Building Society is required to buy back all mortgages that breach Representations and Warranties from the LLP, or if the property has been voluntarily surrendered by the borrower. There is no loss suffered by the LLP, as this buy-back comprises all outstanding amounts, including all arrears on the mortgage accounts. The maximum potential amount payable to the LLP under the guarantee is equal to the amount outstanding on the loan to originator. The loan to originator amounted to £3.1billion (2018 - £2.0billion).

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13. FINANCIAL INSTRUMENTS

The LLP's financial instruments comprise a loan to Yorkshire Building Society (equivalent to the value of the LLP's investment in Yorkshire Building Society mortgages), cash and liquid resources, derivatives, borrowings and various receivables and payables that arise directly from its operations. The main purpose of these financial instruments is to raise finance for Yorkshire Building Society.

Summary

The table below summarises the main financial instruments, their significant terms and conditions and the accounting treatment adopted.

Financial instrument	Significant terms and conditions	Accounting treatment
Loan to originator	Long term Fixed and variable interest rate	Amortised cost
Cash and loans to credit institutions	Short term cash balances	Amortised cost
Derivative financial instruments	Medium term Value derived from underlying price or rate	Fair value through profit or loss
Interest bearing loans and borrowings	Long term Fixed interest rate	Amortised cost except where hedge accounting allows a fair value adjustment to be made
Amounts owed to credit institutions	Short-term Variable interest rates	Amortised cost

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Fair Values

The following is a comparison of book and fair values of the LLP's financial instruments by category as at the Statement of Financial Position date. Where external market prices are available they have been used to determine fair values, otherwise internal pricing models using external market data have been used.

	2019		2018	
	Book Value £000	Fair value £000	Book Value £000	Fair value £000
31 December 2019				
Assets				
Loan to originator	3,131,766	3,131,766	1,981,219	1,981,219
Derivative financial instruments	170,614	170,614	260,168	260,168
Loans and advances to credit institutions	120,467	120,467	83,413	83,413
Liabilities				
Interest bearing loans and borrowings	3,403,148	3,444,980	2,311,778	2,356,324
Derivative financial instruments	5,655	5,655	-	-

The fair value of the loan to originator and loans and advances to credit institutions are recognised on an amortised cost basis that is considered to be a close approximation to fair value. For other receivables and other payables, no calculation of fair value is prepared as their carrying amount is viewed as a reasonable approximation of fair value. Interest bearing loans and borrowings have been calculated using external quoted prices.

The fair value of the derivative financial instruments is determined by using a discounted cash flow analysis model that is consistent with commonly used market techniques. All inputs into valuation models adopted by the entity, including the sterling zero coupon yield curve used as the discount rate on the swap, are obtained from observable market data.

The table below classifies all financial instruments held at fair value according to the method used to establish the fair value.

Level 1: Quoted prices (unadjusted) 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).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs)

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	Fair Value			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
As at 31 December 2019				
Derivative asset	-	170,614	-	170,614
Derivative liability	-	5,655	-	5,655

	Fair Value			
	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
31 December 2018				
Derivative asset	-	260,168	-	260,168

Market risk

Detail of how the Group manages market risk can be found in the financial statements of the LLP's parent Yorkshire Building Society.

The LLP has been established in such a way that market risk is minimal. Certain derivatives have been documented with notional principals that reference other financial instruments so as to maintain a neutral position.

Liquidity risk

Liquidity risk is managed at a Group level and is monitored on a daily basis by the independent Group Risk function. All liquidity risk in subsidiary companies, including the LLP, is eliminated by the use of appropriate inter-company loans and deposits. The table below illustrates the gross contractual cash flows on the LLP's financial liabilities.

	Repayable on demand and up to one year £000	In more than one year but not more than five years £000	More than five years £000	Total £000
As at 31 December 2019				
Interest bearing loans and borrowings	454,351	3,028,353	-	3,482,704
other payables	12,989	-	-	12,989
Total	467,340	3,028,353	-	3,495,693
As at 31 December 2018				
Interest bearing loans and borrowings	19,431	2,346,727	-	2,366,158
other payables	8,497	-	-	8,497
Total	27,928	2,346,727	-	2,374,655
Credit risk				

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Key concentrations of credit risk to the LLP are in respect of the loan to originator, and more generally, to Yorkshire Building Society in its role as the mortgage administrator and cash manager.

The LLP's financial statements are prepared on the basis that its acquisitions of beneficial interests in mortgage portfolios are recognised as a collateralised loan to the Originator.

To the extent that the mortgage loans in the portfolios do not provide sufficient funds to recover the LLP's investment in the mortgage portfolio, the LLP has no preferential claim on the assets of Yorkshire Building Society. To provide protection for the Covered Bond structure, additional mortgage loan collateral over and above the interest bearing loans and borrowings owed are held. Rating agencies govern the adequate level of this 'over-collateralisation' having considered the quality of the underlying pool of mortgage loans. As at 31 December 2019 the value of its investment in the mortgage portfolio is £4.9billion (2018 - £3.1billion) compared to outstanding interest bearing loans and borrowings of £3.4billion(2018 - £2.3billion).

The LLP's maximum gross exposure to credit loss is equal to the balance on the mortgage portfolio as shown above plus credit risk exposure to the deposit account balance within loans with credit institution and the derivative asset balance.

No further analysis has been provided on the credit quality of deemed loans as the balance is within the stage 1 ECL category, is less than 30 days past due and is deemed to be low risk.

Interest rate risk

Interest rate risk is managed at a Group level and is monitored on a daily basis by the independent Group Risk function. The LLP is protected from the interest rate risk by the provision of interest rate swaps.

Currency risk

The LLP minimises currency risk by matching its currency financial assets and liabilities and through the use of cross currency interest rate swaps.

14. CAPITAL MANAGEMENT

	2019	2018
	£000	£000
Retained surplus	1,055	4,525
Total surplus	1,055	4,525

Capital is managed centrally in the Yorkshire Building Society Group. The entity is not subject to any externally imposed capital requirements.

The committee and the Board therefore believe that the current level of capital is appropriate for the LLP's activities.

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15. RELATED PARTIES

The LLP is a special purpose LLP controlled by Yorkshire Building Society, one of the two designated members. The second designated member is YBS Covered Bonds Finance Ltd. Both members are subsidiary undertakings of Yorkshire Building Society. During the year, the LLP undertook the transactions set out below with companies within the Yorkshire Building Society Group.

The LLP has provided a loan to Yorkshire Building Society (the originator of the mortgages), on which the LLP receives income. In addition, the LLP pays cash management and mortgage loan servicing fees to Yorkshire Building Society in connection with its provision of services defined under the Programme Documentation. Yorkshire Building Society is the counterparty to the interest rate swap agreement, on which there is an associated interest benefit for the LLP.

Yorkshire Building Society has provided a series of term advances to the LLP, on which the LLP pays a variable rate of interest. Certain expenses, which are included in other professional and legal expenses, may subsequently be paid or reimbursed by Yorkshire Building Society.

	Book Value £000	Interest receivable and similar income £000	Interest payable and similar charges £000
31 December 2019			
Assets			
Loan to originator	3,131,766	33,353	-
Liabilities			
Interest bearing loans and borrowings	3,403,148	-	20,272
31 December 2018			
Assets			
Loan to originator	1,981,219	25,102	-
Liabilities			
Interest bearing loans and borrowings	2,311,778	-	23,340

