



ESTABLISHED 1877

Annual Review
of the
year ended 31st December 2011

PENRITH BUILDING SOCIETY

Member of the Building Societies Association.

Eligible for investment by Trustees Authorised and regulated by the Financial Services Authority



ESTABLISHED 1877

Directors

P O'M Campbell, BVM & S, MRCVS (Chairman), J S Hollins-Gibson, FCA,
D Driver, FCA, C Hayward, BSc, ACIB, A. G Waterfield, BA, CIMA,
A Fazal, BA, FCIB, G M Rigg, BSc, G Silburn, BSc, MRPharms

Solicitors

Gaynham King & Mellor, 2 Mason Court, Gillan Way, Penrith 40 Business Park, Penrith

Auditor

KPMG Audit Plc, Leeds, LS1 4DW

Bankers: NatWest Bank Plc

Chief Executive: C Hayward, BSc, ACIB

Deputy Chief Executive: A Fazal, BA, FCIB

Branch Manager: Mrs S J Askew

**ANNUAL REVIEW
OF THE YEAR ENDED 31ST DECEMBER 2011**

Summary Directors' Report

Trading conditions remained difficult throughout 2011 and this is likely to continue. The Society made a small profit but is for the first time reporting a small asset reduction.

Interest rates on savers' accounts were maintained at previous year's levels throughout 2011 and the Society's standard variable rate on mortgages was also unchanged and remains very competitive. The Directors believe that the need to balance the needs of savers and borrowers in the current economic climate is paramount. This has been demonstrated by data showing that the interest rate spread between savers and borrowers of the Society is far below the average within its peer group. As a mutual organisation profit maximisation is not a target nor is asset growth. Rather the Society is able to use the accrued profits from previous years to protect existing savers from rate reductions and existing borrowers from rate rises and increased outgoings in these more difficult times. Competition on both sides of the balance sheet has been intense with the market offering premium rates on savings accounts and heavily discounted and/or no fee mortgage products available. The Directors consider that the Society continues to offer a competitive range of straightforward and easy to understand products backed up by exceptional levels of service.

There was a reduction in balances on savers' accounts of over £1.64m as savers looking to maximise returns were attracted by the premium rates offered by some other institutions anxious to maintain or extend market share. Some of these products offer introductory bonus rates which are reduced after an initial period or involve tying up funds for extended periods. These types of account have traditionally not been offered by the Society but the product range is continually monitored and new products will be introduced when it is considered necessary. Two new products were offered towards the end of the year: the Junior ISA account and the limited edition Christmas Saver account which proved to be extremely popular.

Gross lending was just under £8.3m, a reduction on 2010 (£8.7m). There was a reduction of over £2.7m in mortgage balances over the year. This was due mainly to exceptional levels of redemptions with borrowers being attracted by the aggressive marketing of highly competitive products from larger lenders in particular. Borrowers also continued to take advantage of the low interest rates by reducing levels of debt. The spectre of higher unemployment levels, talk of double-dip recession and the subdued housing market also contributed to increasing the impulse to reduce debt.

As in previous years, one of the advantages of operating a prudent Lending Policy is demonstrated by the Society's arrears position. There were again no repossessions in the year and there were only two mortgages twelve or more months in arrear at 31st December 2011. Levels of arrears across all accounts increased slightly over the year although the number of cases over three months in arrear reduced and there would appear to be no underlying trend to cause concern. The majority of the Society's arrears cases relate to owner occupied residential properties and there are minimal arrears in the Society's commercial mortgage book.

The Society uses a number of forbearance measures to assist those borrowers approaching or at the point of experiencing financial difficulties. Such measures include the acceptance of reduced or suspended payments for a concessionary period. Borrowers are expected to resume normal payments where able once any such concessionary period expires.

At 31st December 2011 there were no accounts (2010 – 4) subject to forbearance measures. Where the Society considers there is a risk of loss in such cases, provisions are assessed as detailed in Note 1 to the accounts.

It is appreciated that borrowers' circumstances can and do change over the term of a mortgage and the Society will continue wherever possible to assist borrowers experiencing repayment difficulties.

The Society has not had the need to seek funding from the wholesale markets for many years and this continued in 2011. The Society was able to finance its activities from the high levels of liquidity held and the increased mortgage repayments noted above.

Bank base rate remained at 0.50% throughout the year and most commentators are not expecting any increase until 2013 at the earliest. This provides a challenge to the Society as its traditionally high level of liquidity means that the returns of interest earned remain much reduced from previous years. The Society seeks to maximise the interest due from this source but is not prepared to reduce its criteria for lending to other financial institutions in search of higher returns. The vast majority of its investments are with UK clearing banks and building societies and this will continue to be the case.

As mentioned in previous reports the Society is required to pay interest on loans made by the Government to the Financial Services Compensation Scheme (FSCS) in respect of bank defaults. The Society paid an amount of £25,661 into the scheme in 2011 and it is forecast that an amount of approximately £29,760 will be payable in 2012. There are negotiations ongoing regarding the continuance of the loan arrangement from 2012 and it is likely that the rate of interest charged to the FSCS will increase substantially and this will be passed on to the financial institutions. The latest estimate of this Society's contribution for scheme year 2012/2013 payable in 2013 is approx £48,700. The Society therefore needs to increase the provision in these accounts to the sum of those amounts which means that a charge of £51,986 appears in the income and expenditure account for this year. Whilst no information is available to predict amounts for future years it seems likely that such payments will continue and it is thought that these are likely to increase, particularly if and when any form of capital repayment of the loan is required.

In early 2011 the Society appointed a new Deputy Chief Executive and an updated succession plan has been approved by the Board. An organisational review has been carried out on the efficiency of systems and procedures taking the Society forward to the next stage of development and the resources needed to achieve this have been recognised.

The Society's Directors continue to believe that the members' best interests will be served by the Society remaining an independent mutual organisation and are therefore committed to ensuring the Society's continued existence. The Society's objectives are to provide a friendly and efficient service to the local community whilst offering attractive rates of interest and to continue to concentrate on the provision of traditional products and services.

There have been no material subsequent events between 31 December 2011 and the approval of this Annual Review by the Board.

SUMMARY FINANCIAL STATEMENT
For the year ended 31st December 2011

This financial statement is a summary of information in the audited Annual Accounts, the Directors' Report and Annual Business Statement, all of which will be available to members and depositors free of charge on demand at Penrith Building Society from 9th March 2012.

Summary Directors' Report

A summary of the events and business of the Society during the year can be found on pages 3 to 5.

RESULTS FOR THE YEAR	2011 £	2010 £
Net Interest Receivable	1,105,795	1,103,800
Other Income and Charges	47,831	36,039
Administrative Expenses	(1,070,720)	(1,021,990)
Provisions	(57,052)	(8,544)
Profit for the Year before Taxation	25,854	109,305
Taxation	(439)	(23,295)
Profit for the Year	<u>25,415</u>	<u>86,010</u>

FINANCIAL POSITION AT END OF YEAR	2011 £	2010 £
Assets		
Liquid Assets	34,969,614	33,763,053
Mortgages	51,994,666	54,730,703
Fixed and Other Assets	<u>444,745</u>	<u>509,067</u>
Total Assets	<u>87,409,025</u>	<u>89,002,823</u>
Liabilities		
Shares	76,086,949	77,815,666
Borrowings	791,994	704,766
Other Liabilities	207,291	185,015
Reserves	<u>10,322,791</u>	<u>10,297,376</u>
Total Liabilities	<u>87,409,025</u>	<u>89,002,823</u>

Approved by the Board of Directors on 17th February 2012 and signed on its behalf by:-

P O'M Campbell, Chairman
J S Hollins-Gibson, Director
C Hayward, Director and Chief Executive

SUMMARY OF KEY FINANCIAL RATIOS

	2011	2010
Gross capital as a percentage of shares and borrowings (Note 1)	13.43%	13.11%
Liquid assets as a percentage of shares and borrowings (Note 2)	45.49%	43.00%
Profit for the year as a percentage of mean total assets (Note 3)	0.03%	0.10%
Management expenses as a percentage of mean total assets (Note 4)	1.21%	1.15%

NOTES TO THE SUMMARY FINANCIAL STATEMENT

1. The gross capital ratio measures the proportion which the Society's capital bears to the Society's shares and borrowings. The Society's gross capital consists of reserves, which are the Society's profits accumulated over many years.
Capital provides a financial cushion against difficulties which might arise in the Society's business and therefore protects investors.
2. The liquid assets ratio measures the proportion which the liquid assets held in the form of cash, short term deposits and government securities bears to the Society's shares and borrowings. Liquid assets are utilised by the Society in its cash management enabling the Society to meet requests by investors for withdrawals from their accounts, to make new mortgage loans to borrowers and to fund its general business activities.
3. The ratio of profit for the year as a percentage of mean total assets measures the proportion which the profit after taxation for the year bears to the average of the total assets at the beginning and end of the financial year. The ratio is similar to a company's return on assets. Profit is transferred to reserves, thus forming the capital which is essential in order to protect investors.
4. The ratio of management expenses as a percentage of mean total assets measures the proportion which administrative expenses as reported in this document (which include depreciation) bear to the mean of total assets in accordance with the Accounts Regulations.

INDEPENDENT AUDITOR'S STATEMENT TO THE MEMBERS AND DEPOSITORS OF PENRITH BUILDING SOCIETY

We have examined the summary financial statement of Penrith Building Society for the year ended 31st December 2011 on pages 6 to 7.

This auditor's statement is made solely to the Society's members, as a body, and to the Society's depositors, as a body, in accordance with section 76 of the Building Societies Act 1986. Our work has been undertaken so that we might state to the Society's members and depositors those matters we are required to state to them in such a statement and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body and the Society's depositors as a body, for our work, for this statement, or for the opinions we have formed.

Respective responsibilities of directors and auditor

The directors are responsible for preparing the summary financial statement within the Annual Review, in accordance with applicable United Kingdom law.

Our responsibility is to report to you our opinion on the consistency of the summary financial statement within the Annual Review with the full Annual Accounts, Annual Business Statement and Directors' Report and its conformity with the relevant requirements of section 76 of the Building Societies Act 1986 and regulations made under it.

We also read the other information contained in the Annual Review and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the summary financial statement.

Basis of opinion

We conducted our work in accordance with Bulletin 2008/3 *The auditor's statement on the summary financial statement in the United Kingdom* issued by the Auditing Practices Board. Our report on the Society's full Annual Accounts describes the basis of our opinions on those Annual Accounts, the Annual Business Statement and Directors' Report.

Opinion on financial statement

In our opinion the summary financial statement is consistent with the full Annual Accounts, the Annual Business Statement and Directors' Report of Penrith Building Society for the year ended 31 December 2011 and conforms with the applicable requirements of section 76 of the Building Societies Act 1986 and regulations made under it.

Richard Gabbertas

for and on behalf of KPMG Audit Plc, Statutory Auditor

Chartered Accountants

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Neville Street

Leeds

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17th February 2012

Key Performance Indicators

Total Assets

The Society experienced asset shrinkage of 1.79% during 2011 with total assets reducing from £89,002,823 to £87,409,025. The Board considers that whilst it is disappointing that for the first time in memory a reduction in assets is being reported this is a result of the risk adverse approach adopted in the current market and also a reflection of the consideration given to members on both sides of the balance sheet.

Liquid Assets

Liquid assets, in the form of cash and securities at 31st December 2011 were £34,969,614 representing 40.01% of total assets and 45.49% of total shares and borrowings.

Mortgages

During 2011 mortgage lending totalled £8,291,842. There were 106 advances, including 28 further advances.

Mortgage balances reduced by 5.00% over the year.

At 31st December 2011 there were 2 mortgages (2010 – 2) where the repayment of principal and interest was 12 or more months in arrears. The total amount of arrears in these cases was £22,105 (2010 – £20,963) on balances totalling £188,500 (2010 – £187,177). Both of these cases have low loan to value ratios. At 31st December 2011 the Society had no properties in possession (2010 – 0).

Administrative Expenses

Administrative expenses including depreciation rose to £1,070,720, an increase of 4.76%.

Administrative expenses expressed as a ratio of mean total assets stood at 1.21% (2010 – 1.15%).

Funding

Share and deposit balances at 31st December 2011 totalled £76,878,943, a reduction of £1,641,489 over 2010 levels.

Capital

At 31st December 2011, free capital (aggregate of General Reserve and general provision for bad and doubtful debts less tangible fixed assets) amounted to £10,291,779, or 13.39% of total shares and borrowings. Gross capital amounted to 13.43% of total shares and borrowings. These remain amongst the highest such ratios in the industry.

Staff

The Directors are pleased to record their appreciation to management and staff for the loyal service rendered during the year.

CORPORATE GOVERNANCE

The United Kingdom Corporate Governance Code (2010 Version) issued by the Financial Reporting Council applies to listed companies. The Financial Services Authority however advises that building societies should pay regard to the provisions of the Code in drawing up corporate governance procedures. The Building Societies Association has provided guidance on how those provisions should be interpreted by building societies and the Society has followed that guidance where the Board has considered it appropriate.

The Board

The Board of Directors provides leadership and direction in achieving the Society's Objectives and Activities and is responsible for the continued success of the Society.

It is responsible for devising strategy, formulating policies and providing guidance on the management of the Society. It regularly reviews financial performance and ensures that there are effective risk management controls and procedures in place.

The Board meets at least once per calendar month and there is a formal schedule of matters which are reserved for Board approval.

Board Composition and Independence

The Board currently comprises two Executive Directors and six Non-Executive Directors. The Chief Executive and Deputy Chief Executive are Executive Directors and are responsible for the management of the Society within guidelines set by the Board. Non-Executive Directors are essential to the governance of the Society providing, amongst other things, challenge to the Executive Directors and Management, setting objectives, monitoring performance and determining remuneration of the Executive Directors. There are ever increasing burdens on Non-Executive Directors. They must devote considerable time to the Society. As well as attendance at Board Meetings there must be a commitment to develop skills and knowledge from both internal and external sources to enable them to fulfil their duties and responsibilities.

The Chairman is elected annually by the Board from the complement of Non-Executive Directors. The main role of the Chairman is to lead the Board and ensure its effective operation in all aspects of its role.

The Board considers that all of its Non-Executive Directors are independent. The majority of the Board reside within the Penrith area and are well known within the community; all are readily accessible either in person, by telephone or by correspondence. Mr G Silburn continues as Senior Independent Director and is available to members having any concerns which they consider would be inappropriate to discuss with senior managers and executives.

Five of the Society's Non-Executive Directors, Messrs Campbell, Hollins-Gibson, Driver, Silburn and Rigg will have served on the Board for periods over nine years at the date of the coming Annual General Meeting. In addition to having extensive local knowledge, those Directors have developed a thorough understanding of the practice of building societies and each has individual talents which continue to serve the Society well. The Board considers that those Directors make valuable contributions to the Society and continue to maintain their independence.

The Board has however agreed that any Director with over nine years' service should seek annual re-election and therefore those five, together with Mr Hayward, who has also served over nine years, will stand for re-election at the forthcoming AGM.

Mr Aryn Fazal was co-opted onto the Board with effect from 30th March 2011.

Appointments

Where the need for a new Director is identified for any reason the Chief Executive prepares a description of the person required based on the skills, qualifications and experience needed to ensure an adequate balance of skills at board level. A formal recruitment process will be employed and will include the advertising of the position in appropriate media and canvassing the Society membership. A Board Sub-Committee, including the Chairman, will be established to oversee the recruitment of all Directors. It is necessary for Board appointments to be approved by the FSA under the Approved Persons regime and this may include a personal interview with the FSA.

The Rules provide for a minimum number of Directors to retire by rotation or otherwise each year and that no Director may serve for over 3 years without offering themselves for re-election.

Performance Evaluation

A formal process exists to evaluate, on an annual basis, the performance and effectiveness of individual Directors and of the Board as a whole. In 2011 the appraisal of the Chairman was carried out by the Chief Executive and the Senior Independent Director. The appraisal of the Chairman of Audit and Compliance was carried out by the Chief Executive and Chairman. The other Non-Executive Directors' appraisals were carried out by the Chief Executive, Chairman and Chairman of Audit and Compliance. These appraisals are based on a number of factors including attendance at meetings and external events, contribution and performance at meetings and challenge to the Executive.

Appraisals of the Executive Directors are carried out by the Non-Executive Directors.

The effectiveness of the Board as a whole and its committees is reviewed annually by the Board.

Fitness and Propriety

All Directors must meet the fitness and propriety requirements under the Approved Person regime and must complete a questionnaire confirming their continued compliance with this requirement.

All Directors have access to the advice of the Secretary. In addition any Director may take independent professional advice at the Society's expense should this be considered necessary.

All Directors are provided with clear, timely and accurate information to enable them to fulfil their duties and responsibilities.

All new Directors are provided with induction training and all Directors are encouraged to attend training courses, seminars and other events to maintain up to date knowledge of the matters affecting building societies as a whole and the Penrith Building Society in particular.

Directors

Main Board Meetings are held monthly. Additional meetings may be called as required. There were fourteen meetings of the full Board in 2011.

The following persons were Directors of the Society during the year:

	<u>NUMBER OF MAIN BOARD MEETINGS ATTENDED</u>
P O'M Campbell, BVM & S, MRCVS (Chairman)	14
J S Hollins-Gibson, FCA (Vice Chairman)	14
G M Rigg, BSc	14
A G Waterfield, BA, CIMA	12
G Silburn, BSc MRPharms	13
D Driver, FCA	13
C Hayward, BSc, ACIB	14
A Fazal, BA, FCIB (Appointed 30 th March 2011)	10
P Richardson, MBA (Resigned 7 th January 2011)	0

Mr Fazal retires under Rule 25(4) and being eligible offers himself for election under Rule 25(5).

Messrs Campbell, Hollins-Gibson, Rigg, Silburn, Driver and Hayward having served on the Board for over 9 years have agreed to retire under Rule 26(1) and being eligible offer themselves for re-election.

During the 12 months ended 31st December 2011 there were no associated bodies in which the Society or its Directors had an interest.

In adhering to the principles of good corporate governance the Board has established certain committees to advise on various issues. The terms of reference for these committees may be obtained from the Deputy Chief Executive. The committees in question are:

Audit & Compliance Committee

The Audit and Compliance Committee consists of Messrs J S Hollins-Gibson, G Silburn, D Driver and G M Rigg.

Mr Hollins-Gibson was Chairman of the committee for the whole of the financial year ended 31st December 2011. He is a retired Chartered Accountant, as is Mr Driver.

Four meetings were held within the year and these were attended as follows:

	<u>NUMBER OF MEETINGS ATTENDED</u>
J S Hollins-Gibson	4
G Silburn	3
D Driver	4
G M Rigg	4

In addition representatives of the Internal and External Auditor and the Executive Directors attend most of these meetings

The principal purposes of this committee include ensuring that the Society complies with all regulatory and prudential requirements and to review the Society's internal controls and management systems. The committee has responsibility for monitoring the Compliance function including approval of an annual compliance monitoring plan. The committee is also responsible for the review of the effectiveness and of the internal audit function and the monitoring of the External Auditor's independence, objectivity and effectiveness

Remuneration Committee

This is comprised of the Society's Non-Executive Directors. During the financial year ending 31st December 2011 the Chairman of the Remuneration Committee was the Chairman of the Society. The committee is responsible for setting the Society's remuneration policy for Executive Directors. The committee also settles all other benefits and matters relevant to Executive Directors including contracts of employment with the Society. There were two meetings of the Remuneration Committee in 2011 which were held as part of main Board meetings. All Non-Executive Directors were present at those meetings.

Conduct Risk Committee

This committee comprised of Messrs Silburn and Fazal and three members of the Society's staff. This committee reviews the Society's policies and procedures in all areas having impact on the Society's members and makes recommendations thereon to the Board and management.

DIRECTORS' REMUNERATION POLICY AND REPORT

The Society's remuneration policy is to reward Directors through salary and fees according to their skills, expertise, experience and overall contribution, taking into account fee and salary levels in comparable organisations.

The Board will include an advisory vote on the Directors' Remuneration Report at the forthcoming Annual General Meeting.

Executive Directors

The Society's policy is to set remuneration at levels sufficient to attract and retain executives of sufficient calibre and expertise.

Executive Directors' remuneration comprises basic salary and pension benefits. The Society does not have bonus or share option schemes.

Executive salaries are considered by the Remuneration Committee which meets at least once yearly. Salary levels are set having regard to job content and responsibilities, the performance of the individual and salaries in similar organisations.

The Society does not have a defined benefit/final salary pension scheme. The Society makes contributions to the private pension arrangements of the Executive Directors.

The Chief Executive and Deputy Chief Executive's contracts of employment require a 12 month notice period.

Non-Executive Directors

The remuneration of all Non-Executive Directors is reviewed annually by the Board. The remuneration consists of annual fees assessed by comparison with similar organisations and other external factors. The Chairman of the Board, Chairman of the Audit and Compliance Committee and the Senior Independent Director receive higher fees than other Non-Executive Directors in recognition of the additional workload and responsibilities incumbent on those positions.

Non-Executive Directors do not participate in any performance pay scheme, pension arrangements or other benefits and do not have service contracts.

The Society's remuneration policy is to reward Directors through salary and fees according to their skills, expertise, experience and overall contribution, taking into account fee and salary levels in comparable organisations.

The Board will include an advisory vote on the Directors' Remuneration Policy and Report at the forthcoming Annual General Meeting.

Details of Remuneration

	2011	2010	
For Services as Non-Executive Directors:			
P O'M Campbell (Chairman)	14,720	14,290	
J S Hollins-Gibson (Vice Chairman and Chairman of Audit and Compliance Committee)	11,440	11,110	
D Driver	9,510	9,230	
G M Rigg	9,510	9,230	
G Silburn	10,300	10,000	
A G Waterfield	9,510	4,615	
Lord Hothfield (Retired 31st March 2010)	-----	<u>2,230</u>	
Total Non-Executive Directors	<u>64,990</u>	<u>60,705</u>	
For Services as Executive Directors:			
C Hayward	Salary	74,763	72,704
	Pension Contributions	<u>84,000</u>	<u>84,000</u>
		<u>158,763</u>	<u>156,704</u>
A Fazal	Salary	58,334	-----
(Appointed 30 th March 2011)	Pension Contributions	<u>5,833</u>	-----
		<u>64,167</u>	-----
P Richardson	Salary	1,278	64,058
(Resigned 7 th January 2011)	Pension Contributions	<u>518</u>	<u>6,220</u>
		<u>1,796</u>	<u>70,278</u>
Total Executive Directors		<u>224,726</u>	<u>226,982</u>
Grand Total		<u>289,716</u>	<u>287,687</u>

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