

WELLESLEY FINANCE PLC

Annual Report and Financial Statements

For the year ended 31 December 2018

Company Number 08331511

WELLESLEY FINANCE PLC

Report and financial statements
for the year ended 31 December 2018

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WELLESLEY FINANCE PLC

Officers and advisers

Directors

Andrew Turnbull
Garret Graham Wellesley

Registered Office

6th Floor, St Albans House, 57/59 Haymarket, London, SW1Y 4QX

Company Registration Number

08331511

Auditors

Haysmacintyre LLP, 10 Queen Street Place, London, EC4R 1AG

Bankers

Barclays, Leicester, Leicestershire, LE87 2BB
Lloyds, Threadneedle Street, London, EC2R 8AY

Legal Advisers

GRM Law, 1 Bedford Row, London, WC1R 4BZ
Memery Crystal LLP, 44 Southampton Buildings, London, WC2A 1AP
Linklaters LLP, One Silk St, London EC2Y 8HQ

WELLESLEY FINANCE PLC

Strategic report for the year ended 31 December 2018

Overview - A Transitional Year for Wellesley Finance Plc (the “Company” or “Wellesley”)

2018 has been a year of transition for Wellesley

Today the loan book reflects the changes in lending strategy that began in 2016. Loans since 2016 have been generally larger (+£10 million), made to better capitalised borrowers and focused on larger housing developments comprising lower unit values (generally less than £400,000 per unit) where the market fundamentals are strong and are also supported by the Government’s “Help to Buy” initiative. Since the 2018 year end Wellesley has commissioned an independent stress test by MIAC on the lending it has made since the 2016 strategy change which has seen encouraging results (MIAC summary results can be seen on the Wellesley website) and also the wider Wellesley Group has obtained an independent ARC Ratings credit rating of BBB - which shows that the business is stable and Wellesley Finance is well positioned to expand its loan book when market demand increases.

- Change of lending strategy in 2016 has resulted in no loan losses or provisions on new lending
- Positive results from independent loan book stress tests
- Accorded a BBB- rating with a stable outlook from an independent ratings agency
- Precautionary reduction in lending in the period leading up to Brexit

Repositioning of the lending strategy

It is helpful to explain the change in lending strategy in numbers.

The original strategy of lending which was employed from inception of the business running up to late 2015 saw Wellesley support 150 development projects with total facilities of £298 million and average loan facility sizes of around £2m. Of these, only 14 loans were impaired with only 4 legacy loans from this strategy are remaining. These are being intensively managed with 3 of these expected to be repaid in early 2020.

Following the repositioning of the lending strategy in 2016 there have been 35 new loans with total facilities of £356 million and an average LTGDV of approximately 65%. So far, 22 of these loans (£189m) have been repaid in full leaving 13 loans (£167m) outstanding with no default or losses expected. Of these 13 loans, a further 6 loans are expected to be repaid in full before the end of 2019. The outstanding loans have also yielded presales and reservations for over 850 units, which is 62% of units under constructions. All these numbers are encouraging.

A bond issuer with a five-year track record

1. Since the first programme commenced in 2014, a total of £136.8m bonds have been issued¹.
2. All payments owed to bond holders have been paid in full and on time with more than £9m paid in interest to date.
3. A decision was made in 2018 to issue all new debt as listed bonds with full regulation under the Prospectus Directive. No listed bonds have yet been issued at the date of these financial statements.
4. Approval has been received to issue bonds under a new £500m bond programme and has been approved by the Central Bank of Ireland.
5. The appointment of an institutional advisor has been made in relation to bond distribution through family offices and fund managers.

Increased revenue potential through loan origination and servicing activities

Following discussions during the period, a conclusion was reached after the year end with a multi-family office joint venture funding relationship for an initial £45m of new lending to be managed by Wellesley. This solidifies the Company’s strategy of diversifying its funding and revenue sources with off-balance sheet funding arrangements.

Financial results 2018

The outlook for new lending opportunities remains positive. Wellesley Finance’s financial results have been impacted by a reduction in lending as the company has taken a more cautious view of the market, particularly in the period of Brexit uncertainty. As a result of reduced lending volumes, total income fell from £11.3 million in 2017 to £6.5 million in 2018 reflecting this caution. These contributed to EBITDA reducing from £5.0m to -£10.2m, along with the write-off of loans and advances of £6.1m and the potential credit loss in respect of inter-company balances of £2.8m, both referred to below.

In keeping with our strategy of exiting the remaining loans originated under the original strategy of lending, there was also a write off of £6.1m against 6 legacy loans originated prior to the 2016 change in strategy, all 6 of which had previously had provision applied.

¹ Figure includes £12.4m raised for and on behalf of Wellesley Secured Finance Plc.

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Furthermore, IFRS 9, which was implemented on 1 January 2018, following the global financial crisis, has changed provision reporting from an incurred credit loss model to an expected credit loss model. This reporting standard impacts Wellesley Finance in that it is required to make a provision against loans that while not currently expected to suffer a credit loss, are deemed to have the potential for a loss given historical credit losses suffered in the business prior to the new strategy being introduced in 2016. As a result, in addition to the known credit losses, an additional potential credit loss of £344k (2017: £87k) has been provided within the 2018 numbers in respect of its other loans that management do not currently expect to suffer a loss and is solely an impact of the introduction of IFRS 9.

Further to this, a potential credit loss of £2.8m has been provided for in respect of balances due from other group companies.

Following the completion of the previous audit, management identified some accounting errors that has led to the Company restating their comparative figures this year. The details of these are detailed more fully in note 25, and the impact of the changes was to reduce the Net Asset Value of the Company at 31 December 2017 from £3.37m to (£0.14m), a reduction of £3.5m.

For the period to 30 November 2019, unaudited management information indicates that the Company has returned a small profit on an EBITDA basis.

Material progression with recoveries not yet flowing through to the accounts

Relating to the Company's original lending strategy, there are a number of recovery strategies underway which may be realised, the benefit of which has not yet been recognised within the accounts. Other than enforcing on physical security, Wellesley has been given personal guarantees from borrowers who have defaulted and are now being pursued for restitution. Furthermore, where professional advisors have, in the opinion of Wellesley, fallen below the standards expected of them which has led to loan losses, the Company has initiated legal proceedings for damages. Whilst not certain, the Directors believe that there is a potential range of such recoveries of £8.9m to £12.6m. These do not meet the recognition criteria of an asset nor the disclosure criteria for a contingent asset as at the year end.

About the Company

Wellesley Finance Plc (the "Company") is engaged in the provision of finance for medium sized developers to enable them to build lower (and mid) value homes in England and Wales where long term demand is supported by strong demographics and Government financial support for new buyers. The loans are structured by our lending team, sanctioned by our credit committee and administered by our credit operations functions. Its development loans tend to have a duration of 18-24 months and encompass both major refurbishments and ground up development. Borrowers are medium sized experienced developers with loans from £5m to £30m in scale.

The Company undertakes four principal activities: loan origination/participation/syndication and debt issuance.

Loan origination

The Company is a recognised lender within the property development segment of the UK SME alternative finance market. It offers borrowers committed loan facilities which are typically secured upon individually evaluated property development projects. Following a period of underwriting and evaluation, the Company enters into a loan facility agreement with a borrower and advances its own corporate funds once all lending conditions have been satisfied. The Company either retains the loans on its balance sheet or it makes them available for syndication.

Loan participation

The Company ordinarily maintains some balance sheet exposure to loans that it originates and therefore is not only acting as an originator of loans but also a lender/investor in the loans it originates. Where the Company retains loan exposure on its balance sheet it normally funds its position from the proceeds of bond issuances (see fourth point below (Issuance of corporate debt)).

Loan syndication

The Company has origination and servicing mandates for two sources of funding to which it syndicates loans which meet the required investment criteria. The origination mandates are for (i) Wellesley Secured Finance Plc (ii) Wellesley & Co Limited (in respect to its legacy Peer-to-Peer (P2P) lending back-book). Following the syndication of a loan, the Company will typically continue to service the loans as described above and remain the facility agent for the loan. The Company may also sell a loan from its portfolio or arrange for syndication of all or part of a loan to other third parties.

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Strategic report for the year ended 31 December 2018

Issuance of corporate debt

The Company finances its origination and loan participation activities through the issuance of bonds. These bonds are distributed as investments to retail customers by Wellesley & Co Limited. The table below summarises the current programmes that the Company has in place.

Programme Name	Description	Programme Size	Outstanding amount issued as at 31 December 2018
The Wellesley Property Mini-Bond	Unlisted, non-transferable, secured programme with use of proceeds restricted (i) to participating in loans originated by the Company; and (ii) to be held in a secured segregated account.	£250,000,000	£38,205,903
The Wellesley Mini-Bond	Unlisted, non-transferable, unsecured programme with use of proceeds being for general corporate purposes.	£100,000,000	£59,661,284

Operating and Financial Review

The Company's total comprehensive loss was £9.3m (2017: loss £5.5m). The Company's administrative expenses for the year were £7.5m (2017: £6.0m). The Company released net impairment on loans that it originated in 2014/15 under its original lending strategy for £0.9m (2017: charge £6.7m) and incurred £6.1m (2017: £0.3m) of write-offs of loans provided for in the prior periods.

Business Review

The Company's total net income decreased by £4.8m to £6.5m (2017: £11.3m). The main driver for the decrease in total income was due to a reduction in the drawn loan book in 2018 and also a significant reduction in impaired loans on the balance sheet which attributed to the prior year's income as a result of their high levels of default interest, otherwise irrecoverable and therefore provided for, being included.

In early 2016 the Company implemented a major change in lending strategy in anticipation to changes it had identified in the UK housing market at an early stage, so moving to make larger loans to better capitalised developers and only those with significant track records in their market segment. Wellesley has moved from a transactional to a relationship lending model and has built the in-house capability to nurture these long-term lending relationships. Since implementing this strategy, Wellesley has experienced no defaults or impairments on the lending generated under this approach to credit. The Company has progressed with exiting from its original lending strategy legacy loans and as at the end of the period had 4 remaining impaired loans. All loan impairment and write-offs incurred during the period were owing to the original lending strategy.

The positive effect of these changes in lending strategy are evidenced by a recent stress test that Wellesley commissioned after the year end by independent consultants, MIAC. The objective of the stress test was to obtain an independent view as to the outcome of a fall in the housing market on the 19 outstanding loans which were completed since the new lending strategy was put in place. The Report can be found on the Company's website (<http://static.wellesley.co.uk/Wellesley-MIAC-Stress-Test.pdf>) but its findings suggest that even with a 33% fall in house prices the Company's cumulative losses over 100 months would be some 1.5% and where personal guarantees had been taken out, and if managing actions were taken these losses could be reduced by 50%. This is a very encouraging indicator.

Due to a greater proportion of loans being retained on the Company's balance sheet, and therefore funded by the proceeds of its bond issuances, the net interest income has increased as the Company generates more income from acting as principal. In the prior year, the Company had syndicated a greater proportion of its loans hence it earned a greater proportion of its income from fees and commission in 2017.

The Company's administrative expenses increased by £1.5m to £7.5m (2017: £6.0m). This was driven by an increase in management charge by £588k to £3.6m (2017: £3.0m) and an increase in advertising & marketing by £1.3m to £1.4m (2017: £2.2k).

The Company's total assets as at 31 December 2018 were £99m (2017: restated £85.2m) principally due to an increase in loans and advances to customers and amounts owed by related parties.

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The Company's total liabilities as at 31 December 2018 were £108.2m (2017: restated £85.1m) because of an increase in interest-bearing loans and borrowings and accrued management charges.

The Directors are satisfied with the overall direction of the business and are hopeful for its future performance. This is after a specific assessment of the entire book for provisions, which identified the requirement for net provisions of £0.9m credit (2017: charge £6.7m) relating to the Company's legacy lending strategy. The Company incurred realised losses of £6.1m (2017: restated £0.3m) on two loans during the year. Lifetime losses to 31 December 2018 as a percentage of facilities originated since inception was 0.89%, higher than 0.04% in 2017. The Directors anticipate this figure to fall as the incidence of loan losses falls and the loan portfolio grows under the new lending strategy.

The Company benefits significantly from the wider Wellesley Group owing to the origination and servicing roles that it performs and also the distribution of its own debt securities through Wellesley & Co Limited.

Key Performance Indicators ("KPIs")

The KPIs of the business at 31 December 2018 are:

- Gross Loan Book – £152m (2017: £171m) of which £88m (2017: £66m) is held on the statement of financial position and £64m (2017: £105m) is held off the statement of financial position. The portion of gross loan book not recognised on the statement of financial position represents assets owned by Peer-to-Peer investors and Wellesley Secured Finance Plc. The Gross Loan Book decreased by £19m primarily as a high volume of redemptions were received during the year, which were not replaced by new loans.
- Net interest margin ("NIM") – NIM is calculated as total income divided by gross loan book (as above). There was a decline in the NIM to 4.29% from 6.60% in the prior year.
- Impairment of loans and advances, net – credit of £0.9m (2017: restated charge £6.7m) and loss before tax % - 48.5% (2017: restated profit before tax % + 6.3%).

The KPIs represent important measures for the directors to monitor the performance of the business. The directors review and consider these KPIs on a monthly basis, and in board meetings, in order to assess the performance. This enables decisions to be made on the direction of the business.

Principal risks and uncertainties

The principal risks to the Company are as follows:

Credit risk

As a loan participant, the Company is exposed to the credit risk of its borrowers. For each loan, the Company obtains a legal charge on the assets it is lending against. It is acknowledged that the property market is cyclical and that the Company is operating in a period of the cycle which would be considered as relatively stable which has resulted in favourable conditions for lending. The board regularly reassesses its view on the risks presented by the market and also the overall stage of the property cycle.

Contractual commitments represent agreements entered into but not advanced as at 31 December 2018.

Collateral based on the underlying development asset is held in relation to secured loans. Total collateral in respect of loans and advances held at 31 December 2018 was £528m (2017: £594m). Where the amount outstanding on a loan and advance exceeds the collateral and is underperforming, the Company will consider including a provision in the financial statements.

Market risk

The Company is exposed to the risk that the value of, or income arising from, the Company's assets and liabilities change as a result of changes to interest rates.

The Company's treasury function is responsible for managing the Company's exposure to all aspects of interest rate risk. The Company's Asset and Liability Committee ("ALCO") regularly convenes to consider reports on all aspects of interest rate risk.

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Reputational risk

The Company has a high level of sensitivity to reputational risks, particularly those which could potentially result in the Company's retail lenders losing confidence in the stability and security of the organisation and ultimately the safety of their investment. It should be noted that a reputational event could be triggered by another participant of the industry and whilst not as a direct result of an issue within the Company's business, customers could have concerns about the industry in general.

Information technology and security risk

The peer to peer platform is an online business and therefore the information technology and information system security is paramount for the successful running of the Company. The following risks are specifically identified:

- Attack to take over accounts and attempt to withdraw funds;
- Attack to steal customer data; and
- Distributed denial of service ("DDOS") rendering the Company's systems temporarily inaccessible.

All these issues are tested by a regular penetration testing service that the Company has performed on information systems.

Operational and people risk

As the Company grows and average loan sizes increase, the Company faces increased operational risk within the lending and fundraising areas of the business. The greatest area of risk relates to the process of releasing advances to borrowers, registering charges on security and managing the repayment/collections of all loans. The Company identified this as an area of risk more than a year ago and has put software in place to manage much of these processes. The software is in the process of being implemented after a period of development that needed to occur in order to ensure it was fit for purpose.

The Company has invested significantly in its people and will strive to ensure that its retention rates are high. The Company has however identified certain key members of staff which would be challenging to replace either as a result of there being scarcity of skillsets or the role requiring familiarisation with a number of internal processes. Management has aimed to mitigate these risks through:

- extended notice periods;
- introduction of a number of documented procedure manuals and simplification of processes through the introduction of software; and
- introduction of an employee incentive scheme which includes medical, critical illness cover, pension etc.

Liquidity Risk

The Company's sources of funding are all retail peer to peer/bond market correlated and as such there is less diversification than what would be considered the norm for a financial services institution. The Company does hold asset terms which are approximately half the duration of its liability terms and therefore does not operate with a funding mismatch. However, it should be noted that the Company does have an unfunded forward liability on its development facility future drawdowns which it expects to fund with the repayment of loans which are due to be repaid.

The Company monitors its forward cash flow position regularly, however it could potentially have difficulty in making its future drawdowns if a number of loans were to be delayed in repayment. This risk is mitigated by the fact that failure to fund the future drawdowns is unlikely to result in a breach of our obligations albeit the development would be delayed which would increase financing costs and ultimately reduce credit quality.

The business has multiple sources of liquidity to draw upon should the forecast cash flow position vary from plan. The uncertainty relating to timing of loan redemptions mean that many such initiatives are prepared but held in reserve until the liquidity forecast identifies a requirement for 'a lever to be pulled.' These liquidity forecasts are reviewed by the Liquidity Committee at least weekly, and more frequently if required, and so enables an informed decision-making process on exactly which lever should be pulled, at which time to remedy the position. The following options are some that have been utilised over the past year.

- Loan sales – The Company's loan agreements allow Wellesley to transfer a facility to another party and can be completed without consent of the borrower. In the last twelve months, the business has completed the sale of loan facilities totalling £35.4m, demonstrating the ability to identify appropriate counterparties and execute transactions in a timely manner should the decision to be taken to do so.

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- Loan refinance - A commonly used transaction in development finance is to refinance with another loan provider. While this requires borrower consent, the prospective transaction is often introduced by the borrower as they approach practical completion of a build when the risk profile has softened and commercially favourable rates become available. Wellesley are able to influence borrower behaviour by varying fees, some of which will not have accrued given their contingent nature. In the last twelve months, the business has completed the refinance of loan facilities totalling £46m.
- Promotional fund raising - A tried and tested route to increase the 'normal' run rate of investment inflows is with promotional offers. These can be executed and closed within a very short timeframe. Successful promotions run over the last twelve months have raised circa £18m.
- Loans outside of contractual terms - For liquidity purposes, the Company forecasts further advances in full for all loans regardless of whether they are operating within contractual terms, or not. There may be some loans that are operating outside of their terms, which is not always a reflection of the credit risk. In those scenarios, there is not a contractual obligation to fund further advances within the contractual period.

Unlike more traditional lending businesses that can estimate future inflows of cash with real certainty, the development lending industry is far more likely to see variations in timing. As a result, the Company will always be subject to liquidity risk. The regular committee meetings, and the varying levers that can be pulled have ensured that, to date, there has always been sufficient liquidity in the business to meet its obligations.

Risk of potential fraud

As an originator of loan assets, the Company is exposed to possible fraud by borrowers, purported borrowers, their professional advisors such as solicitors, accountants or valuers as well as by employees. Attempted fraud typically involves borrowers, either acting alone or in concert with professional advisors, seeking to obtain funds by adopting a false identity or using a false inflated property valuation or purporting to own a property or seeking a release of security without redeeming the underlying loan. In addition, solicitors could abscond with completion monies, although redress under the indemnity arrangements required by the Solicitors Regulation Authority is normally available in such circumstances.

The Company has in place processes and procedures to counter fraud, and insurance in place providing an indemnity against losses arising from dishonest, fraudulent or malicious acts committed by its staff, outside valuers and outside solicitors.

Brexit Risk

As a UK-based business, the Company is particularly exposed to any domestic economic downturn which could affect existing and prospective borrowers and the value of their development projects. The United Kingdom's vote to leave the European Union and subsequent notice under Article 50 of the Treaty on European Union has presented uncertainty to the UK economy. Whilst the precise nature of the risks and uncertainties that the Company may face following the United Kingdom's departure from the European Union cannot be predicted, the Company has identified a concentration of potential risks relating to its lending activities. These risks are primarily focussed upon the construction process involved when its developers are building properties and the residential property values upon which project viability is underpinned.

Brexit may cause increased costs in labour and materials from the European Union. However, as Wellesley appoint their own independent surveyor to each project, any costs will be reviewed and then stressed internally prior to funding the deal. More detailed underwriting of costs would be expected including analysis of the developer's supply chain. In addition, the Company might focus on working more with contractors with UK based supply chains.

The potential impact of a 'Hard Brexit' is something that is under regular review by the Company and Wellesley Group however at this stage it remains satisfied that any downside movement as a result will be mitigated through a combination of the Company's and Wellesley credit policies, regional focus, oversight of the construction process and its drive to ensure the quality track records of its underlying customer base.

The main risks arising from the Company's financial instruments are detailed in note 21.

Graham Wellesley
Director

Approved by order of the Board on 23 December 2019

WELLESLEY FINANCE PLC

Report of the Directors for the year ended 31 December 2018

The Directors present the Strategic Report, Directors' Report and the Financial statements of Wellesley Finance plc for the year ended 31 December 2018. The directors of the Company during the year were those listed on page 1. The Company has indemnity insurance for all directors of the Company.

Results and dividends

The Company's comprehensive loss for the year was £9.3m (2017: £5.5m).

The directors do not recommend the payment of a final dividend (2017: £Nil).

As disclosed in the Strategic report on page 3, it was necessary to restate the 2017 comparatives due to the identification of accounting errors after the completion of the prior year audit.

Principal activities

The Company is engaged in the provision of finance for medium sized property developers in England and Wales.

Principal risks and uncertainties

The principal risks and uncertainties of the Company are disclosed on pages 5 to 7 in the Strategic report. The Directors consider the most material of these to be Liquidity risk given that the timing of cashflows in a Development Lending business can be volatile. As discussed on pages 6 to 7, these are actively managed by the Company's regular Liquidity Committee meetings, and the maintenance of multiple funding options that can be utilised in various scenarios.

Future developments

The future developments of the Company are to continue to grow enduring relationships with high quality borrowers which will enable the Company to drive a robust and sustainable loan portfolio.

Post balance sheet events

On 28 March 2019, the Central Bank of Ireland approved the Company's prospectus for an unsecured listed bond programme. The programme would allow the Company to use proceeds for Corporate purposes. In addition, as disclosed on page 2, a joint venture funding relationship has been agreed for an initial £45m of new lending. No other information has been identified since the year end about conditions existing at the date which is required to be disclosed in these financial statements.

Strategic report

Principal risks and uncertainties and information on the Company's risk management policies are included in the Strategic report.

Going concern

The Company's business activities, together with the factors likely to affect its future development and its financial position are described in the Strategic report. Of particular importance is the Liquidity risk highlighted on pages 6-7 along with the mitigation strategies that would be then applied.

After making enquiries, preparing and reviewing the cashflow forecast and having assessed that sufficient future funding is available to the business to meet its future financial obligations, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual report and financial statements.

Notwithstanding the assessment of the Directors, the fact that the loan portfolio is made up of a smaller number of larger loans (as part of the new lending strategy) means that the impact of one of these larger developments not repaying in line with expectations could have a material impact on the Company. This is because it could impinge the Company's ability to continue to fund other loan facilities or operating expenses. Therefore, the Directors are of the view that there is a material uncertainty on the future cashflows from the development portfolio and, in the absence of current profitability and a negative net asset value, may cast significant doubt about the Company's ability to continue as a going concern.

The Directors are forecasting a return to profitability in the near term, especially as the change in strategy has seen no further loans suffer credit losses up until the signing date of these financial statements. Equally the unaccounted assets discussed on page 3 are expected to further support the Company's position. Finally, the Directors would again point towards the liquidity strategies and mitigants in the Strategic Report that have assured to date that liquidity has always been available.

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Report of the Directors for the year ended 31 December 2018

Statement of directors' responsibilities

The Directors are responsible for preparing the Strategic Report, Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under the law, the Directors have elected to prepare the financial statements in accordance with International Financial Reporting Standard ("IFRS") as adopted by the European Union and applicable law.

Under Company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing those financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with International Financial Reporting Standard ("IFRS") as adopted by the European Union have been followed; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditors

Each of the persons who is a director at the date of approval of this report confirms that:

- so far as the director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

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

It was resolved to appoint Haysmacintyre LLP as auditors. It is proposed to re-appoint Haysmacintyre LLP as auditor at the Annual General Meeting.

Graham Wellesley
Director

Approved by the Board of Directors and signed on behalf of the Board on 23 December 2019.

WELLESLEY FINANCE PLC

Independent auditor's report for the year ended 31 December 2018

Independent auditor's report to the members of Wellesley Finance PLC

Opinion

We have audited the financial statements of Wellesley Finance PLC (the 'company') for the year ended 31 December 2018 which comprise the Statement of profit and loss and other comprehensive income, Statement of financial position, Statement of Changes in Equity, Statement of Cash Flows and the related notes, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as applied in accordance with the provisions of the Companies Act 2006.

In our opinion, the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2018 and of its loss for the year then ended;
- the financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Material uncertainty related to going concern

The company made a net loss of £10,249,314 during the year ended 31 December 2018 and, as of that date, the company's liabilities exceeded its total assets by £9,202,737. We draw attention to note 2.4 in the financial statements. As stated in note 2.4, these events, along with the other matters as set forth in note 2.4, indicate that a material uncertainty exists that may cast significant doubt on the company's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

Emphasis of matter – prior period adjustment

We draw attention to note 25 of the financial statements, which describes the impact of prior year restatements identified during the course of the preparation of these financial statements and the risk that adjustments identified and recognised in the year ended 31 December 2017 may relate to prior periods or vice versa. Our opinion is not modified in this respect.

Emphasis of matter – balances owed by group undertakings

We draw attention to note 15 of the financial statements, in respect of balances owed by group undertakings, which describes the assessment of the recoverability of those balances under various scenarios and the calculation of the expected credit loss. Our opinion is not modified in this respect.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion 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 such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in 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 in this regard.

WELLESLEY FINANCE PLC

Independent auditor's report for the year ended 31 December 2018

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or the directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

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

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 9, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors 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 directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's 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 auditor's 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 Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

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.

Simoin Wilks (Senior Statutory Auditor)
For and on behalf of Haysmacintyre LLP, Statutory Auditors
23 December 2019

10 Queen Street Place
London
EC4R 1AG

WELLESLEY FINANCE PLC

Statement of profit and loss and other comprehensive income for the year ended 31 December 2018

	Notes	2018 £	2017 £ Restated
Interest income		7,675,294	5,720,393
Interest expense		(4,650,953)	(2,637,477)
Net interest income		3,024,341	3,082,916
Fee and commission income	5	6,916,639	13,875,305
Fee and commission expense	5	(4,191,235)	(6,397,427)
Net fee and commission income		2,725,404	7,477,878
Other fee income		770,758	700,170
Total income		6,520,503	11,260,964
Net (expense)/income from derivatives and other financial instruments at fair value through profit or loss		(374,631)	60,121
Total operating income		6,145,872	11,321,085
Administrative expenses	6	(7,521,449)	(6,046,725)
Write off of loans and advances to customers		(6,055,603)	(274,788)
Impairment of inter-company assets	15	(2,800,000)	-
Amortisation of intangible assets	13	(18,166)	(18,166)
(Loss)/profit from operations		(10,249,346)	4,981,406
Bank interest		32	1,142
Exceptional expense	25	-	(3,699,685)
(Loss)/profit before tax		(10,249,314)	1,282,863
Income tax charge	9	-	(105,004)
(Loss)/profit after taxation - attributable to the equity holders of the Company		(10,249,314)	1,177,859
	Notes	2018 £	2017 £ Restated
(Loss)/profit after taxation - attributable to the equity holders of the Company		(10,249,314)	1,177,859
Impairment of loans and advances to customers (net)	11	903,327	(6,715,328)
Tax on other comprehensive income		-	-
Total other comprehensive income/(loss) for the year, net of taxation		903,327	(6,715,328)
Total comprehensive loss for the year, net of taxation		(9,345,987)	(5,537,469)

There are no items in the statement of other comprehensive income which could be reclassified to the statement of profit and loss in subsequent years.

The accounting policies and notes set out on pages 16 to 41 form an integral part of these financial statements.

WELLESLEY FINANCE PLC

Statement of financial position as at 31 December 2018

	Notes	2018 £	2017 £ Restated	1 January 2017 £ Restated
Assets				
<i>Non-current assets</i>				
Intangible assets	13	38,422	56,588	74,754
Investment in joint venture		-	-	3,263,553
Loans and advances to customers	10	23,437,309	24,635,369	25,331,400
Deferred tax asset	14	825	825	12,819
		23,476,556	24,692,782	28,682,527
<i>Current assets</i>				
Cash and cash equivalents		1,780,735	11,997,246	30,497,426
Loans and advances to customers	10	56,249,541	32,133,090	2,495,372
Other assets	15	17,496,662	16,418,125	11,316,841
Total assets		99,003,494	85,241,243	72,992,166
Liabilities				
<i>Current liabilities</i>				
Other liabilities	16	8,080,161	6,074,187	16,838,063
Interest-bearing loans and borrowings	17	25,577,617	10,193,492	3,955,596
		33,657,778	16,267,679	20,793,659
<i>Non-current liabilities</i>				
Interest-bearing loans and borrowings	17	73,962,595	68,258,418	46,083,965
Derivative financial liabilities	12	585,858	571,896	433,823
Total liabilities		108,206,231	85,097,993	67,311,447
Net assets		(9,202,737)	143,250	5,680,719
Equity				
Share capital	18	50,000	50,000	50,000
Retained earnings		(9,252,737)	93,250	5,630,719
Total equity		(9,202,737)	143,250	5,680,719

The notes on pages 16 to 41 are an integral part of these financial statements.

These financial statements were approved by the Board of directors on 23 December 2019 and were signed on its behalf by:

Graham Wellesley

Director
Company number 08331511

WELLESLEY FINANCE PLC

Statement of changes in equity for the year ended 31 December 2018

	Notes	Share capital £	Retained earnings £	Total equity £
Balance at 1 January 2018 as restated		50,000	93,250	143,250
Total comprehensive income for the year				
Loss for the year		-	(10,249,314)	(10,249,314)
Other comprehensive income		-	903,327	903,327
Total comprehensive income for the year		-	(9,345,987)	(9,345,987)
Balance at 31 December 2018		50,000	(9,252,737)	(9,202,737)

		Share capital £	Retained earnings £	Total equity £
Balance at 1 January 2017 as previously stated		50,000	2,762,151	2,812,151
Prior period adjustments	25	-	2,868,568	2,868,568
Balance at 1 January 2017 as restated		50,000	5,630,719	5,680,719
Total comprehensive income for the year				
Profit for the year		-	1,177,859	1,177,859
Other comprehensive income		-	(6,715,328)	(6,715,328)
Total comprehensive income for the year		-	(5,537,469)	(5,537,469)
Balance at 31 December 2017 as Restated		50,000	93,250	143,250

The notes on pages 16 to 41 are an integral part of these financial statements.

WELLESLEY FINANCE PLC

Statement of cash flows for the year ended 31 December 2018

	2018 £	2017 £ Restated
Cash flows from operating activities		
(Loss)/profit before taxation	(10,249,314)	1,282,863
Adjustments for non-cash items:		
Amortisation of intangible assets	18,166	18,166
Interest expense on loans and borrowings	4,650,953	2,637,477
Net expense from derivatives and other financial instruments at fair value through profit or loss	13,963	138,072
Impairment losses on inter-company balances	2,800,000	-
Write off of loans and advances	6,055,603	274,788
Foreign currency revaluation of loans and advances	64,677	159,996
	<u>3,354,048</u>	<u>4,511,362</u>
Adjustments for working capital items and loans & advances:		
Increase in other assets	(3,878,536)	(1,825,737)
Increase/(decrease) in other liabilities	2,005,974	(10,868,880)
Increase in operating assets	(32,958,802)	(40,669,756)
Net cash flows used in operating activities	(31,477,316)	(48,853,011)
Cash flows from investing activities		
Purchase of listed bonds	(5,000)	(225,000)
Sale of portions of loans and advances	4,793,483	5,104,172
Purchase of intangible assets	-	-
Net cash generated by investing activities	4,788,483	4,879,172
Cash flows from financing activities		
Proceeds from interest-bearing loans and borrowings, net of transaction costs	36,390,475	34,245,129
Repayment of interest-bearing loans and borrowings	(16,511,538)	(5,044,050)
Interest payment on loans and borrowings	(3,441,588)	(3,426,205)
Net cash generated by financing activities	16,437,348	25,774,874
Net decrease in cash and cash equivalents	(10,251,484)	(18,198,966)
Cash and cash equivalents at the start of the year	11,997,246	30,497,426
Foreign currency revaluation of cash balances	34,973	(301,214)
Cash and cash equivalents at the end of the year	1,780,735	11,997,246

The notes on pages 16 to 41 are an integral part of these financial statements.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

1 Nature of operations

Wellesley Finance Plc is a public limited Company, limited by shares. It is a provider of finance to medium sized property developers with the funding they need to build mid-market homes in England and Wales. The Company's registered number is 08331511 and registered office at 6th Floor, St Albans House, 57/59 Haymarket, London, SW1Y 4QX.

2 Basis of preparation

2.1 Accounting basis

The financial statements of the Company have been prepared in accordance with the Companies Act 2006 and International Financial Reporting Standards ("IFRS") as developed and published by the International Accounting Standards Board ("IASB") as adopted by the European Union ("EU").

The comparative period is the year ended 31 December 2017 and has been restated as documented in note 25.

The presentational currency of the financial statements is Pound Sterling.

The financial statements have been prepared on the historical cost basis except for the following material items in the financial statements:

- derivative financial instruments are measured at fair value through profit or loss; and
- loans and advances to customers designated at fair value through profit or loss.

The preparation of the financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The accounting policies that have been used in the preparation of these financial statements are described below. The particular accounting policies adopted by the Directors are described below and have been applied consistently year on year.

In accordance with IAS 1 "Presentation of Financial Statements" paragraph 40A (Change in accounting policy, retrospective restatement or reclassification), a third statement of financial position has been prepared for the beginning of the preceding period (as at 1 January 2017). This is required because of the retrospective restatement of the financial statements due to identified errors. Full details regarding these restatements can be found in note 25.

2.2 New accounting standards

New standards and amendments

The following standards and amendments are new and applied for the first time for the annual reporting year commencing 1 January 2018:

- IFRS 9 Financial Instruments
- IFRS 15 Revenue from Contracts with Customers

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

2 Basis of preparation *(Continued)*

2.2 New accounting standards *(Continued)*

IFRS 9 Financial Instruments

The standard includes new requirements in respect of the recognition and measurement, impairment and derecognition of financial assets as well as general hedge accounting. One of the biggest changes sees an expected credit loss model replacing the previous incurred loss model. The standard became effective for accounting periods beginning on or after 1 January 2018.

The Company has adopted the accounting standard as required using the full retrospective approach for transition and as a result it has been necessary to make a retrospective adjustment for comparative purposes. This is further detailed in note 25.

IFRS 15 Revenue from contracts with customers

IFRS 15 Revenue replaced IAS 18 Revenue and IAS 11 Construction Contracts. It applies to all contracts with customers except leases, financial instruments and insurance contracts. IFRS 15 establishes the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer. There has been no material impact from the adoption of IFRS 15 Revenue from Contracts with Customers.

2.3 Future accounting developments

The following standards and amendments to existing standards have been published, but in some cases, not yet adopted by the EU. They are mandatory from the financial period beginning on or after the effective dates shown below.

- IFRS 16 – Leases. Applicable for financial years beginning on or after 1 January 2019. IFRS 16 was enclosed by the EU in October 2018.
- Annual improvements to IFRS Standards 2015-2017 cycle - Annual periods beginning on or after 1 January 2019. Earlier application is permitted.

IFRS 16 Leases

IFRS 16 eliminates the classification of leases as either operating leases or finance leases for a lessee. Instead all leases are treated in a similar way to finance leases applying IAS 17. Leases are 'capitalised' by recognising the present value of the lease payments and showing them either as lease assets (right-of-use assets) or together with property, plant and equipment. If lease payments are made over time, a company also recognises a financial liability representing its obligation to make future lease payments. The Company holds operating leases for small items such as office printers. On review of IFRS 16 in respect of these leases, there will not be a material impact on the Company.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

2 Basis of preparation *(Continued)*

2.4 Going concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the Company has the resources to continue in business for the foreseeable future (which has been taken as 12 months from the date of approval of the financial statements). In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the statement of financial position, future projections of profitability, cash flows and capital resources and the longer-term strategy of the business. The Directors have also reviewed the planned mitigating responses to liquidity issues as discussed in the Strategic report.

The Company's forecasts and projections show that it will be able to operate at adequate levels of both liquidity and capital for the foreseeable future. The Directors are satisfied that the liquidity of the Company will be met by any future issuance of bonds. Full details of the Liquidity risk of the Company and its mitigation strategies can be found on pages 6 and 7.

Notwithstanding the assessment of the Directors, the fact that the loan portfolio is made up of a smaller number of larger loans (as part of the new lending strategy) means that the impact of one of these larger developments not repaying in line with expectations could have a material impact on the Company. This is because it could impinge the Company's ability to continue to fund other loan facilities or operating expenses. Therefore, the Directors are of the view that there is a material uncertainty on the future cashflows from the development portfolio and, in the absence of current profitability and a negative net asset value, may cast significant doubt about the Company's ability to continue as a going concern.

The Directors are forecasting a return to profitability in the near term, especially as the change in strategy has seen no further loans suffer credit losses up until the signing date of these financial statements. Equally the unaccounted assets discussed on page 3 are expected to further support the Company's position. Finally, the Directors would again point towards the liquidity strategies and mitigants in the Strategic Report that have assured to date that liquidity has always been available.

3 Significant accounting policies

3.1 Interest income and expense

Interest income and expense is recognised in the statement of profit and loss on an effective interest rate ("EIR") basis in accordance with IFRS 9. The EIR is the rate that, at the inception of the financial asset or liability, exactly discounts expected future cash payments and receipts over the expected life of the instrument back to the initial carrying amount. When calculating the EIR, the Company estimates cash flows considering all contractual terms of the instrument but does not consider the assets' future credit losses.

The EIR is applied to the amortised cost of the loan asset. Where a loan asset becomes impaired, the amortised cost of the loan is reduced by the expected loss for income calculation purposes.

At each reporting date, management makes an assessment of the expected remaining life of its financial assets and where there is a change in those assessments the remaining amount of any unamortised discount or premiums is adjusted so that the interest continues to be recognised prospectively on the amortised cost of the financial asset at the original EIR. The adjustment arising is recognised within interest income in the statement of profit and loss of the current period.

The calculation of the EIR includes all transaction costs and fees paid or received that are an integral part of the interest rate, together with the discounts or premium arising on the acquisition of loan portfolios.

Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the statement of profit and loss include interest on financial assets and financial liabilities measured at amortised cost calculated on an EIR basis.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

The Company recognises its portion of each sterling denominated loan and advance originated on its statement of financial position. The remainder of each sterling denominated loan relates to the funding from P2P investors and Wellesley Secured Finance Plc. Interest income and interest expense is recognised on these balances as outlined above. Any principal funded by P2P investors or purchased by Wellesley Secured Finance Plc is derecognised further described in note 3.6.

3.2 Fees and commission income

For the remaining portion of originated loans and advances, the Company acts as an agent on behalf of Peer to Peer ("P2P") customers who are fully exposed to the risks and rewards of these loans and advances. As a result, the Company presents its fees and commissions income net.

3.3 Other operating income

Arrangement fees, administration fees and contracted exit fees relating to loans and advances to customers are included within interest income as part of the EIR calculation.

Undrawn fees, legal fees, valuation fees and early access fees which are not considered integral to the EIR are recognised on an accruals basis when the service has been provided or received.

3.4 Fees payable

Fees and expenses which are costs directly attributable to the issue of a financial instrument (*i.e.* direct promotional costs, legal fees) are included in interest expense as part of the EIR calculation. When they are not incremental costs that are directly attributable, they are recognised within fees as the services are received.

3.5 Financial instruments – recognition and de-recognition

Recognition

The Company initially recognises loans and advances, interest-bearing loans and borrowings issued on the date they are originated, at fair value less transaction costs.

De-recognition

De-recognition of financial assets and liabilities is the point at which an asset or liability is removed from the statement of financial position.

Financial assets are derecognised when:

- the rights to receive cash flows from the assets have ceased; and
- the Company has transferred substantially all the risk and rewards of ownership of the assets.

A financial liability is derecognised when the obligation is discharged, cancelled or expires. Any difference between the carrying amount of a financial liability derecognised and the consideration paid is recognised through the statement of profit and loss.

The Company's accounting policy is as follows:

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These are initially measured at fair value plus transactions costs that are directly attributable to the financial asset. Subsequently, they are measured at fair value which is calculated as the NPV of future cashflows, discounted using the original EIR. Loans and receivables mainly comprise loans and advances to customers.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

3 Significant accounting policies (Continued)

3.6 Financial instruments

Financial Assets

The Company classifies its financial assets (excluding derivatives) as loans and receivables.

The Company recognises its portion of each sterling denominated loan and advance originated on its statement of financial position. As for the remaining portion of originated loans and advances, the Company acts solely as an agent on behalf of P2P customers who are fully exposed to the risks and rewards of these loans and advances. The remainder of each sterling denominated loan and advance is held "off balance sheet".

Expected Credit Losses ("ECL") – Development loan portfolio

IFRS 9 introduces a three-stage model for impairment based on changes in credit quality since initial recognition with each stage representing a change in the credit risk of financial instrument. If a significant increase in credit risk is identified, the financial instrument is moved from stage one to two but is not yet deemed to be credit impaired. Financial instruments that are deemed to be credit impaired are then moved to stage three. The expected credit loss for financial instruments which are in stage one equals to the portion of lifetime expected credit losses that result from default events within the next twelve months. The expected credit loss for financial instruments in stages two and three is equal to the expected lifetime credit losses.

Wellesley consider that the primary trigger of a significant increase in its credit risk is where the internal credit rating, decreases by 2 rating categories since initial recognition. The borrowers to whom the loans purchased were originally made to are not rated by external agencies, and so internal ratings are the most appropriate key drivers.

ECL's are calculated in a way that reflects:

- An unbiased and probability weighted amount that evaluates several potential outcomes, including scenarios where a loss does and does not occur, and based on the maximum contractual period (including extension options) that Wellesley is exposed to credit risk. For undrawn loan commitments, Wellesley's ability to demand repayment and cancel the undrawn commitment does not limit the exposure of credit losses to the notice period;
- The time value of money; and
- Reasonable and supportable information, available without undue cost or effort, about past events, current conditions and future economic conditions.

On an on-going basis the Company assesses whether there is objective evidence that a financial asset is impaired. A financial asset is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the assets (a "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Expected Credit Losses ("ECL") – Inter-company receivables

Inter-company loans provided by the Company to other group entities are repayable on demand and do not carry an interest rate. For the calculation of the ECL, Wellesley need to consider the ability of these entities to repay the debt at the reporting date and, if this is not likely, what the debt recovery plan would be. The Company has no intention of calling this debt in the foreseeable future.

The Company have used a 5-scenario approach in its assessment of its ECL.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

3 Significant accounting policies (Continued)

3.6 Financial instruments (Continued)

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

- delinquency in contractual payments of principal or interest;
- cash flow or other trading difficulties experienced by the borrower;
- initiation of bankruptcy proceedings; and
- change in market value of assets

The Company's portion of 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 profit and loss.

When a financial asset is uncollectible, it is written off against the related provision for impairment. Such financial assets 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 impairment in the statement of profit and loss. Allowances for impairment losses are released at the point when it is deemed that, following a subsequent event, the risk has reduced such that an allowance is no longer required.

Financial Liabilities

Financial liabilities are contractual obligations to deliver cash or another financial asset.

Financial liabilities at amortised cost are recognised initially at fair value, which equates to issue proceeds net of transaction costs incurred. They are subsequently stated at amortised cost. Any difference between proceeds net of transaction costs and the redemption value is recognised in the statement of profit and loss over the period of the borrowings using the EIR method.

Interest-bearing loans and borrowings issued by the Company are assessed as to whether they should be treated as equity or financial liabilities. Where there is a contractual obligation to deliver cash or other financial assets, they are treated as a financial liability and measured at amortised cost using the EIR after taking account of any discount or premium on the issue and directly attributable costs that are an integral part of the EIR. The amount of any discount or premium is amortised over the period to the expected call date of the instrument. All interest-bearing loans and borrowings issued by the Company are classified as financial liabilities at amortised cost.

3.7 Financial instruments and fair values

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 in the principal, or in its absence, the most advantageous market to which the Company has access at that date. The fair value of a liability reflects its non-performance risk.

When applicable, the Company measure the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide a fair value on an ongoing basis.

When there is no quoted price in an active market, the Company uses valuation techniques that maximise the use of relevant observable inputs and minimise the issue of unobservable inputs. The chosen valuation techniques incorporate all the factors that market participants would take in to account in pricing a transaction.

The best evidence of fair value of a financial instrument at initial recognition is normally the transaction price – *i.e.* the fair value of the consideration received or given.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

3 Significant accounting policies *(Continued)*

3.8 Derivative financial instruments

The Company enters into derivative transactions only for the purpose of reducing exposure to fluctuations in exchange rates; they are not used for proprietary trading purposes.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at fair value.

Fair values are obtained from quoted market prices in active markets and, where they are not available, from valuation techniques, discounted cash flow models and option pricing models. Derivatives are measured as assets where the fair value is positive and liabilities where their fair value is negative.

3.9 Provisions

A provision is recognised if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

3.10 Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of transaction. Monetary assets and liabilities held at the statement of financial position date are translated into sterling at the exchange rates ruling at the statement of financial position date. Non-monetary assets carried at historical cost should be reported using the exchange rate at the date of the transaction.

Non-monetary assets carried at fair value should be reported at the rate that existed when the fair values were determined

Exchange differences are charged or credited to the statement of income.

3.11 Taxation

The tax expense represents the sum of the tax currently payable and deferred tax. It is recognised in the statement of comprehensive income except to the extent that it relates to a business combination, or items recognised directly in equity or in equity through other comprehensive income.

Current tax

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

Deferred tax

Deferred tax is recognised in respect of all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised for all deductible temporary difference, the carry forward of unused tax credits and any unused losses. Such assets and liabilities are not recognised if they arise from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit. Deferred tax liabilities are recognised for taxable differences arising on investments in subsidiaries except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at the end of each reporting date and reduced to the extent that it is not probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

3 Significant accounting policies *(Continued)*

3.11 Taxation *(Continued)*

Deferred tax liabilities and assets are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on the tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right of offset exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

3.12 Intangible assets

Database software

Expenditure on database software relates to the customer relationship management ("CRM") software which enables customers to invest in investment products marketed by the Company.

Expenditure on database software is recognised as an asset when the Company is able to demonstrate its intention and ability to complete the development and use the database software in a manner that will generate future economic benefits and can reliably measure the costs to complete the development.

Database software assets are amortised on a straight-line basis in the statement of profit and loss over its useful life from the date it is available for use. The estimated useful life of database software assets is five years.

3.13 Equity instruments

The Company classifies instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. Where an instrument contains no obligation on the Company to deliver cash or other financial assets or to exchange financial asset or financial liabilities with another party under conditions that are potentially unfavourable to the Company, or where the instrument will or may be settled in the Company's own equity instruments but includes no obligation to deliver a variable number of the Company's own equity instruments then it is treated as an equity instrument. Accordingly, the Company's share capital is presented as a component of equity within shareholders' funds. Any dividend or other distributions on equity instruments are recognised in equity. Related income tax is accounted for in accordance with IAS 12.

3.14 Cash and cash equivalents

Cash and cash equivalents comprise cash balance and bank balances with a maturity of three months or less from the acquisition date, which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

4 Critical accounting estimates and judgements

The preparation of financial information requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. The judgement and assumptions that are considered to be the most important to the portrayal of the Company's financial condition are those relating to loan impairment provisions.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

4 Critical accounting estimates and judgements (Continued)

The following are deemed to be judgements:

IFRS 9 – business model assessment

IFRS 9 requires the Company to determine how to classify its loan assets in the context of its business model for managing those loans assets to generate cash flows. This business model assessment is determined at a level that reflects how the group of loan assets (rather than intentions for an individual loan) are managed together to achieve its business objective. While this may need determining at the entity level (as the Company may have several business models for differing assets), the Company considers that all loans should be grouped together under one business model, as all loans are originated and managed for the same purpose, to generate cash flows of interest, fees and returns of principal.

The Company considers it integral to the business objective that portions of originated loans are sold to other parties, while also maintaining a portion for itself. This is because it facilitates the opening of differing funding sources, which is important given that Peer-to-Peer funding is in run-off. Therefore, without the differing funding streams that Wellesley open by selling portions of its loans, it would not be able to meet its business objectives.

IFRS 9 gives further guidance on areas that might help support a business model assessment and include: (a) the level at which the business model is assessed and reported; (b) the risks affecting performance of the business model and how they are managed; and (c) how managers of the business are compensated. In addition to these, the Company also included the following considerations in assessing their business model: (a) how performance of the business is evaluated and reported; (b) the primary business objective; and (c) the level and driver of sales.

When reviewing all of these factors, the Directors have assessed that the business model for holding loan assets is, for accounting purposes, to both collect contractual cash flows and to sell financial assets. This assessment then requires the Company to measure its loan asset portfolio at Fair value through other comprehensive income (“FVTOCI”) rather than Fair value through profit and loss (“FVTPL”).

The fair value of the Company’s loan assets is difficult to assess because they are not publicly traded and there is not a highly liquid secondary market on which to obtain prices. In addition, loans are normally issued to support bespoke developments and so benchmarking the loans against loans on similar developments in similar locations is very challenging.

Ultimately the value of the loan asset depends on the ability of the borrower to repay the principal, fees, and interest as well any expenses suffered on their behalf which have been added to the loan balance. The Company’s experience it that there is only a movement in the fair value of the loan where there is a risk that Company does not receive full repayment of all amounts it is due. When this is the case, a provision for an expected credit loss would be recognised, with a corresponding FV adjustment made to the value of the loan.

IFRS 9 states that for assets measured at FVTOCI, the amount recognised in the P&L should be the same as the amounts that would have been recognised if accounted for at amortised cost. In that sense, the fair value of loans will be equal to the NPV of the expected future cash-flows, discounted using the initial EIR of the loan.

What this means for the financial statements is that any provisions made for expected credit losses no longer appear in the statement of profit and loss account, and instead appear in the statement of other comprehensive income. If the expected loss crystallises into an actual loss, then the loss is recognised through the statement of profit and loss, with the provision for expected credit losses reversed from the statement of other comprehensive income.

EIRs

IFRS 9 requires interest earned/incurred from loans and advances/financial liabilities to be measured under the EIR method. Management must therefore use judgement to estimate the expected life of each instrument and hence the expected cash flows relating to it. The carrying value of loans and advances/financial liabilities would therefore be affected by unexpected market movements resulting in altered customer behaviour models used to compare to actual outcomes and incorrect assumptions. Transaction costs should be incorporated in the EIR method. Management identifies these costs as those which relate directly to acquiring the loan and advance/financial liabilities as transaction costs.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

4 Critical accounting estimates and judgements (Continued)

Loan impairment provisions

Loan portfolios across the Company are reviewed on at least a monthly basis to assess for impairment. In determining whether an impairment provision should be recorded, judgements are made as to whether there is objective evidence that a financial asset is impaired as a result of loss events that occurred after recognition of the asset and by the reporting date. The calculation of the impairment loss is management's best estimate of losses incurred in the portfolio at the statement of financial position date and reflects expected future cash flows based on both the likelihood of a loan or advance being written off and the estimated loss on such a write-off. Please see note 11 for details of the provisions carried forward at the year end and the amounts charged as an expense and released during the year.

Balances owed by group undertakings

The Company is owed £18.5m from other group companies. Of this amount, £11.3m is due from group holding entities whose assets are investments in various subsidiaries. Therefore, it might appear that there is an uncertainty as to whether these balances will be recoverable.

These inter-company debts are repayable on demand but the Directors have no plans to demand repayment in the foreseeable future. Such inter-company funding is not unusual when businesses are in early stage and/or pre-IPO.

The Company continues to fund the wider group's expenses as it is the main operating entity in the structure. All expenses paid (most of which are payroll related) are for the ultimate benefit of the Group and are considered to add corporate value. There are various initiatives in place to ensure that all entities are appropriately funded, and these are being actively reviewed. In the absence of such plans coming to fruition, the ultimate repayment will need to be through a future liquidity event.

Notwithstanding this assessment, IFRS 9's implementation requires the Directors to make an assessment as to what potential future losses could be suffered. As a result, an assessment of various scenarios was completed and this led to an expected credit loss of £2.8m being recognised, reducing the inter-company recoverable balance to £15.7m.

Acting as agent

The Company acts as agent on behalf of its Peer to Peer investors. Management apply the EIR method in calculating the fee and commission income and expense for acting as agent. Management must therefore use judgement to estimate the expected life of each instrument and hence the expected cash flows relating to it. The carrying value of loans and advances/financial liabilities would therefore be affected by unexpected market movements resulting in altered customer behaviour models used to compare to actual outcomes and incorrect assumptions.

The following is deemed to require a certain level of judgement by the directors:

Intangible assets

The Company assesses its intangible assets at least annually for evidence of impairment. Where the asset is under development, the Company considers whether it is reasonably likely to complete the asset and bring it to use. The Company also considers if the asset will generate sufficient economic benefit over the and above the current carrying value of the asset. See note 13 for details.

5 Fee and commission income/expense

	2018	2017
	£	£
		Restated
Income on loans and advances to customers - agent	6,916,639	13,875,305
Fee expense on Peer-to-Peer capital - agent	(4,191,235)	(6,397,427)
	2,725,404	7,477,878

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

6 Administrative expenses

	Note	2018 £	2017 £ Restated
Staff costs	7	1,326,731	1,801,855
Advertising & marketing		1,410,690	62,802
Legal & professional		302,034	218,033
Irrecoverable VAT		66,485	232,412
FX on foreign currency loans		64,677	159,996
Management charge	22	3,622,574	3,034,613
Other administrative expenses		728,258	537,014
		7,521,449	6,046,725

All other administrative expenses are incurred in the normal course of business.

7 Staff costs

Staff cost have been allocated per department as follows:

	2018 £	2017 £
<i>Wages and salaries</i>		
Central functions	124,710	137,836
Operations	37,526	214,160
Credit operations	345,876	550,944
Loan origination	638,517	715,080
	1,146,629	1,618,020
Social security costs	134,261	142,852
Pension costs	30,232	12,438
Employee benefits	15,609	28,545
	1,326,731	1,801,855

Average staff numbers in the year have been allocated per department as follows:

	2018	2017
Central functions	1	2
Operations	1	1
Credit operations	5	6
Loan origination	6	8
	13	17

The Company's Directors are remunerated by other companies within the Group.

8 Auditor's remuneration

	2018 £	2017 £
Auditor's remuneration for audit services provided	94,247	53,411
	94,247	53,411

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

9 Taxation

	2018	2017
	£	£
		Restated
Current tax:		
UK corporation tax at 19% (2017: 19.26%)	-	-
Total current tax	-	-
Deferred tax:		
Current year	-	105,641
Adjustment in respect of previous periods	-	(12,819)
Effect of changes in tax rate	-	12,182
Total deferred tax	-	105,004
Total tax charge/(credit)	-	105,004
Reconciliation of tax charge:		
Profit on ordinary activities before tax	(10,249,314)	1,282,863
Tax on profit on ordinary activities at standard corporation tax rate of 19% (2017: 19.26%)	(1,947,370)	247,079
Effects of:		
Adjustments in respect of prior years	-	12,819
Expenses not deductible	6,986	7,803
Tax rate changes	(97)	(12,182)
Effects of group relief/ other reliefs	(1,525)	(31,369)
Unutilised expenses	1,939,583	-
Non qualifying asset	2,423	-
Utilisation of carry back losses	-	(119,146)
Total tax charge/(credit)	-	105,004
Deferred tax assets		
Provision at start of period	825	105,829
Adjustment in respect of prior years	-	12,819
Effect of changes in tax rate	-	(12,182)
Additional charge to Statement of profit and loss for the period	-	(105,641)
Provision at end of period	825	825

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

10 Loans and advances to customers

	2018 £	2017 £ Restated
Gross loan receivables	88,127,151	66,112,087
Less provisions	(8,440,301)	(9,343,628)
	79,686,850	56,768,459
Amounts falling due:		
Within one year	56,249,541	32,133,090
In the second to fifth year inclusive	23,437,309	24,635,369
	79,686,850	56,768,459

11 Provisions on loans and advances to customers

The movement in provisions in respect of loans during the year was as follows:

	2018 £	2017 £ Restated
At the beginning of the year	9,343,628	2,628,300
Charge for provisions	8,098,069	7,010,115
Write back of provisions	(9,001,396)	(294,787)
At the end of the year	8,440,301	9,343,628

The provision is made against loans and advances to customers. The provision is estimated to realise in the next twelve months.

12 Derivatives held for risk management

Amounts included in the statement of financial position are analysed as follows:

	2018		2017	
	Assets £	Liabilities £	Assets £	Liabilities £ Restated
Foreign exchange	-	585,858	-	571,896
	-	585,858	-	571,896

The Company uses forward foreign exchange derivatives, not designated in qualifying hedge relationships, to manage its exposure to foreign exchange risk on a currency loan provided to customers in Spain.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

13 Intangible assets

	Database software 2018 £	Database software 2017 £
<i>Cost</i>		
At the beginning of the year	90,830	90,830
Additions	-	-
Disposals	-	-
At the end of the year	90,830	90,830
<i>Amortisation</i>		
At the beginning of the year	34,242	16,076
Amortisation charge for the year	18,166	18,166
Disposals	-	-
At the end of the year	52,408	34,242
Net book value		
At the beginning of the year	56,588	74,754
At the end of the year	38,422	56,588

14 Deferred tax asset

	2018 £	2017 £
Deferred tax asset	825	825
	825	825
Analysis of Deferred tax asset:		
Corporation tax	825	825
	825	825

15 Other assets

	2018 £	2017 £
Other receivables	688,077	1,357,230
Prepayments	11,943	12,035
Balance owed by group undertakings	15,704,674	14,490,555
Balance owed by affiliate entity	1,091,968	558,305
	17,496,662	16,418,125

The balance owed by group undertakings of £15,704,674 is net of an expected credit loss of £2,800,000, following an assessment of the recoverability of those inter-company balances, based on five scenarios, each with a probability weighting and an estimate of the potential loss.

The amounts owed from related parties are unsecured, have no fixed repayment date and are interest free.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

16 Other liabilities

	2018 £	2017 £ Restated
Trade payables	1,493,025	1,828
Other taxation and social security costs	191,006	200,287
Accruals and deferred income	488,663	178,331
Other payables	5,437,132	5,566,578
Balance owed to group undertakings	470,335	127,163
	8,080,161	6,074,187

The amounts owed to group undertakings are unsecured, have no fixed repayment date and are interest free.

17 Interest-bearing loans and borrowings

	2018 £	2017 £ Restated
At the beginning of the year (as restated)	78,451,910	50,039,561
Issued in the year	36,738,362	34,548,953
Redeemed in the year	(16,511,538)	(5,044,050)
Net accrued interest movement	1,209,366	(788,730)
Transaction costs, net	(347,888)	(303,824)
Total interest-bearing loans and borrowings at the end of the year	99,540,212	78,451,910
Due within one year	25,577,617	10,193,492
Due over one year	73,962,595	68,258,418
	99,540,212	78,451,910

The capital outstanding within Interest-bearing loans and borrowings is for Minibond £97,867,187 (2017: £72,217,885) and an Irish Listed ISA bond £nil (2017: £5,383,000). The Minibond is comprised of both secured and unsecured bonds.

Interest rates range from 2.9% to 8% on the Minibond.

18 Share capital

	2018 £	2017 £
50,000 issued ordinary shares at £1 each (50,000 authorised ordinary shares at £1 each)	50,000	50,000
	50,000	50,000

The 50,000 ordinary shares at £1 each are fully paid up at the year end.

The shares have full voting, dividend and capital distribution (including winding up) rights and are not redeemable. The only reserves at the year end are the retained earnings which represent all retained profits and losses.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

19 Financial instruments and fair values

The following tables summarise the classification and carrying amounts of the Company's financial assets and liabilities:

2018	Loans and receivables £	Fair value through profit or loss £	Liabilities at amortised cost £	Total £
Loans and advances to customers	79,686,850	-	-	79,686,850
Cash and cash equivalents	-	1,780,735	-	1,780,735
Deferred tax asset	-	825	-	825
Other assets	700,019	-	-	700,019
Balance owed by group undertakings	15,704,674	-	-	15,704,674
Balance owed by affiliate entity	1,091,968	-	-	1,091,968
Total financial assets	97,183,511	1,781,560	-	98,965,072
Derivative financial liabilities	-	585,858	-	585,858
Interest-bearing loans and borrowings	-	-	99,540,212	99,540,212
Other payables	-	-	7,609,826	7,609,826
Balance owed to group undertakings	-	-	470,335	470,335
Total financial liabilities	-	585,858	107,620,373	108,206,231
2017	Loans and receivables £	Fair value through profit or loss £	Liabilities at amortised cost £	Restated Total £
Loans and advances to customers	56,768,460	-	-	56,768,460
Cash and cash equivalents	-	11,997,245	-	11,997,245
Deferred tax asset	-	825	-	825
Other assets	1,369,265	-	-	1,369,265
Balance owed by group undertakings	14,490,555	-	-	14,490,555
Balance owed by affiliate entity	558,305	-	-	558,305
Total financial assets	73,186,585	11,998,070	-	85,184,654
Derivative financial liabilities	-	571,895	-	571,895
Interest-bearing loans and borrowings	-	-	78,451,910	78,451,910
Other payables	-	-	5,947,024	5,947,024
Balance owed to group undertakings	-	-	127,163	127,163
Total financial liabilities	-	571,895	84,526,097	85,097,992

The Company uses amortised cost as an approximation for the fair value of loans and advances. Amortised cost is a reasonable proxy for fair value due to the following: (i) application of the current interest rate in the EIR calculation; and (ii) the term of the loans and advances are short term.

Fair values of financial assets and financial liabilities are based on quoted market prices. If the market is not active, the Company establishes a fair value by using appropriate valuation techniques. 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 have been agreed between active market participants in an arm's length transaction. For financial liabilities held at fair value, the Company takes into account changes in credit risk and other observable data in order to reflect the measurement of financial liabilities.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

19 Financial instruments and fair values (continued)

The Company 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); and
- Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Fair value of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Company determines fair values using valuation techniques.

The following table provides an analysis of financial liabilities (there are no equivalent financial assets) held on the statement of financial position at fair value, into Level 1 to Level 3 based on the degree to which the fair value is observable:

2018	Level 1 £	Level 2 £	Level 3 £	Total £
Financial liabilities				
Derivative financial liabilities	-	585,858	-	585,858
Total financial liabilities	-	585,858	-	585,858
2017	Level 1 £	Level 2 £	Level 3 £	Total £
Financial liabilities				
Derivative financial liabilities	-	571,896	-	571,896
Total financial liabilities	-	571,896	-	571,896

20 Commitments and contingent liabilities

At 31 December 2018, the Company had undrawn commitments to lend of £107,641,206 (2017: £166,890,340).

The below details the split of amounts falling due in respect of total contractual cashflows on loans and advances:

	2018 £	2017 £
Amounts falling due:		
Within one year	41,950,213	102,687,460
In the second to fifth year inclusive	65,690,993	64,202,880
After five years	-	-
	107,641,206	166,890,340

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

21 Risk management

The main areas of risk that the business is exposed to are:

- Credit risk;
- Liquidity risk;
- Market risk;
- Reputational risk;
- Information technology and security; and
- Operational and people risk

Credit risk

The Company's principal business activity is providing residential property loans. For each loan, the Company obtains a legal charge on the assets it is lending against. It is acknowledged that the property market is cyclical and that the Company is operating in a period of the cycle which would be considered as relatively stable with inflating property prices which has resulted in favourable conditions for lending. The board regularly reassesses its view on the risks presented by the market and also the overall stage of the property cycle.

During the year there was a change in internal credit rating policy which saw a 4-category system replaced by a 5-category system. The new system rates loans as either: Strong, Good, Satisfactory, Weak or Default.

Factors that help determine and define the categories of credit rating include: the loan to gross development value %; the loan to original land value %; the level and quality of security obtained; the repayment period; compliance with loan covenants; and the progress of development work.

The prior year's credit policy was more subjective in nature, whereas the current policy is more prescriptive. As a result, mapping the new policy to the old policy would not provide a useful or meaningful comparative. There are therefore 2 disclosures below: the first being the current loan portfolio broken down per internal credit rating at 31 December 2018; and the prior year's comparative reflecting loan portfolio valuation at 31 December 2017 using the prior internal credit ratings.

The below details the credit quality of the loans and advances to customers:

2018	Total
Loans and advances to customers - internal categorisation	£
Strong	8,785,772
Good	17,958,799
Satisfactory	20,129,373
Weak	32,813,915
Default	8,409,292
Loans and advances to customers (Refer to note 10)	88,097,151
Loans and advances to customers - IFRS 9 staging categorisation	
Stage 1	26,744,571
Stage 2	52,943,288
Stage 3	8,409,292
Loans and advances to customers (Refer to note 10)	88,097,151

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

21 Risk management (continued)

Following application of new internal credit rating methodology, it is challenging to present comparative information under the updated 5-category system. As a result, comparative information is presented under the historical 4-category system:

2017	Total
Loans and advances to customers	£
Performing within terms	39,035,395
Performing in arrears	13,011,798
Non performing - full recovery expected	4,337,267
Impaired	9,343,628
Loans and advances to customers (Refer to note 10)	65,728,088
Loans and advances to customers - IFRS 9 Staging categorisation	
Stage 1	52,047,193
Stage 2	4,337,267
Stage 3	9,343,628
Loans and advances to customers (Refer to note 10)	65,728,088

The above does not include a capital balance of £30,000 (2017: £384,000) for investment by Wellesley Finance plc in Irish Listed ISA bond.

The below details the ageing of loans and advances past due but not impaired:

	2018	2017
	£	£
Overdue by three months	-	3,154,375
Overdue between three months to six months	-	-
Overdue by greater than six months	-	14,194,690
	-	17,349,065

At 31 December 2018, all loans and advances to customers are operating under a 'Rolled' interest basis meaning that the loan interest is added to value of the loan, rather than being paid regularly ("Serviced"). As a result, there are no overdue amounts as at 31 December 2018.

The Company reviews its portfolio under the following metrics:

- (i) Performing within terms: a loan which is performing within the terms and conditions set down in the loan agreement. Any payments of principal or interest have been made on time and the Company expects the loan to be fully repaid within the original agreed timescale. Wellesley customers will be matched to loans in this category;
- (ii) Performing (enhance monitoring): a loan which is performing within the terms and conditions set down in the loan agreement. It is expected to deliver a full return of principal and interest, although it may have an increased risk profile and it requires closer management from Wellesley Finance to maintain the expectation of a full return of principal and interest. This category of loans is where the Company have identified a factor which gives a cause for concern and it is closely examined so that the Company can determine whether or not it represents a threat to the full repayment of the loan facilities. Wellesley customers will be matched to loans in this category;
- (iii) Non-performing: loan where the Company does not expect the loan security to be enough to cover all of the loan principal and interest. This normally only happens when something has gone seriously wrong with the underlying development, or there has been a severe downturn in the overall market, and the value of the underlying asset has deteriorated considerably.

The directors have carried out a full review of each individual loan and anything past due is closely monitored.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

21 Risk management (continued)

The Company's maximum exposure to credit risk after provisions for impairment is as follows:

	2018	2017
	£	£
Financial assets		
Cash and cash equivalents	1,780,735	11,997,245
Loans and advances to customers	79,686,850	56,768,460
Other assets	17,496,661	16,418,125
	98,964,246	85,183,830
Contractual commitments	107,641,206	166,890,340
Total credit risk	206,605,452	252,074,170
Financial liabilities		
Interest-bearing loans and borrowings	99,540,212	78,451,910
Derivative financial liabilities	585,858	571,895
Total counterparty risk	100,126,070	79,023,805

Contractual commitments represent agreements entered into but not advanced as at 31 December 2018.

Collateral, based on the underlying development asset, held in relation to secured loans is capped at the amount outstanding on an individual basis. Total collateral in respect of loans and advances held at 31 December 2018 was £528m (2017: £594m). Where the amount outstanding on a loan and advance exceeds the collateral and is underperforming, the Company will consider including a provision in the financial statements.

Liquidity risk

The Company's sources of funding are all retail peer to peer/bond market correlated and as such there is less diversification than what would be considered the norm for a financial services institution. The Company does hold asset terms which are approximately half the duration of its liability terms and therefore does not operate with a funding mismatch. However, it should be noted that the Company does have an unfunded forward liability on its development facility future drawdowns which it expects to fund with the repayment of loans which are due to be repaid.

The below details when the contractual Euro/Sterling cash outflows and corresponding Sterling/Euro cash inflows are due on the forward exchange derivative positions:

	2018	2017
	€	€
Amounts falling due:		
Within one year	16,344,197	16,152,730
In the second to fifth year inclusive	-	-
After five years	-	-
	16,344,197	16,152,730
	2018	2017
	£	£
Amounts falling due:		
Within one year	14,167,925	13,816,684
In the second to fifth year inclusive	-	-
After five years	-	-
	14,167,925	13,816,684

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

21 Risk management (continued)

The below details the split of amounts falling due in respect of liabilities:

At 31 December 2018	Up to 3 months £	Between 3 and 12 months £	Between 1 and 2 years £	Between 2 and 5 years £
Trade payables	1,493,026	-	-	-
Other taxation and social security costs	191,006	-	-	-
Accruals and deferred income	381,830	106,833	-	-
Other payables	5,437,132	-	-	-
Balance owed to group undertakings	470,335	-	-	-
Interest-bearing loans and borrowings	4,228,164	21,349,453	40,629,193	33,333,402
Derivative financial liabilities	585,858	-	-	-
	12,787,351	21,456,286	40,629,193	33,333,402
At 31 December 2017	Up to 3 months £	Between 3 and 12 months £	Between 1 and 2 years £	Between 2 and 5 years £
Trade payables	1,828	-	-	-
Other taxation and social security costs	200,287	-	-	-
Accruals and deferred income	47,108	47,106	70,659	13,458
Other payables	5,566,578	-	-	-
Balance owed to group undertakings	127,163	-	-	-
Interest-bearing loans and borrowings	1,794,150	8,399,342	27,742,958	35,089,104
Derivative financial liabilities	266,391	305,504	-	-
	8,003,505	8,751,952	27,813,617	35,102,562

The Company monitors its forward cash flow position however could potentially have difficulty in making its future drawdowns if a number of loans were to be delayed in repayment. This being said, this risk is mitigated by the fact that failure to fund the future drawdowns is unlikely to result in a breach of our obligations albeit the development would be delayed which would increase financing costs and ultimately reduce credit quality.

Market risk

Market risk is the risk that the value of, or income arising from, the Company's assets and liabilities change as a result of changes in market prices, the principal element being the interest rate risk.

The Company has minimal foreign currency exposure and engages in hedging strategies to minimise risk.

The Company's treasury function is responsible for managing the Company's exposure to all aspects of market risk within the operational limits set out in the Company's treasury policies. ALCO approves the Company's treasury policies and receives regular reports on all aspects of market risk exposure, including interest rate risk.

Interest rate risk

Interest rate risk is the risk of loss arising from adverse movements in market interest rates. Interest rate risk arises from the loan and lending products that we offer.

In particular, changes to interest rates could potentially impact the value of the properties to which the loans and advances of the Company are secured against.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

21 Risk management (continued)

Basis risk

Basis risk is the risk of loss arising from changes in the relationship between interest rates which have similar but not identical characteristics. This is monitored closely and regularly reported to ALCO. The risk is managed by matching and where appropriate, through the use of derivatives, with established risk limits and other control procedures.

The Company's forecasts and plans take account of the risk of interest rate changes and are prepared and stressed accordingly.

Foreign exchange risk

Foreign exchange risk is the risk that the value of, or net income arising from, assets and liabilities changes as a result of movements in exchange rates. The Company has low levels of foreign exchange risk which is managed by use of cross-currency derivatives. The table below sets out the Company's exposure to foreign exchange risk:

Assets and liabilities in euros at sterling carrying values	2018	2017
	£	£
Loans and advances to customers	972,242	9,926,693
Cash and cash equivalents	1,661,781	720,097
Deferred income	-	-
Net position	2,634,023	10,646,790

The Company estimates that a 2% movement in the value of the euro would have the following impact on the statement of financial position values:

- Euro strengthened by 2%: +£53,756 (2017: +£217,281)
- Euro weakened by 2%: (£51,648) (2017: (£208,761))

Interest rate sensitivity gap

The interest rate on the total value of the loan portfolio of £79,686,350 (2017: £56,768,460) is fixed. The Company has no exposure to floating interest rates on the loan portfolio. The Company considers a 200 basis points ("bps") movement to be appropriate for scenario testing given the guidance by the Bank of England Monetary Policy Committee on expectations of future long-term interest rates. The Company estimates that a +/- 200 bps movement in interest rates paid / received would have impacted the overall balance sheet net asset values as follows:

- +/- 200 bps - +/-£60,487 (2017: restated +/-£61,658)

Capital risk

The Company's objective is to maintain a strong capital base to support its current operations in line with relevant forecasts. Capital base for these purposes comprises shareholders' equity plus interest-rate bearing loans and borrowings. The details are below:

	2018	2017
	£	£
Share capital	50,000	50,000
Retained earnings	(6,452,737)	93,250
Common equity capital	(6,402,737)	143,250
Interest-bearing loans and borrowings	99,540,212	78,451,910
Other capital	99,540,212	78,451,910
Total capital base	93,137,475	78,595,160

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

21 Risk management (continued)

The Company is not subject to external regulatory capital requirements. The Company is meeting its objectives for managing capital by issuing shares and raising debt where necessary. However, the capital levels are monitored both at a Company level and throughout the Wellesley Group. There have been no changes in the Company's objectives, policies and processes for managing capital from the previous period.

22 Related party transactions

Related parties of the Company include 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. Key management personnel are defined as the Directors.

The balances with fellow subsidiaries of Wellesley Group Investors Limited:

	2018	2017
	£	£
Balance owed by fellow subsidiaries	7,189,748	5,629,233
Balance owed by parent	135,498	22,828
Balance owed by ultimate parent	11,179,429	8,838,494
Balance owed by affiliate entity	1,091,968	558,305
Balance owed to fellow subsidiaries	(470,335)	(127,163)

Wellesley Secured Finance plc is a related party to the Company as it is the servicer and originator for loans purchased by Wellesley Secured Finance plc. Wellesley Secured Finance plc purchased portions of loans from Wellesley Finance plc during the year. The amount owed at 31 December 2018 is split between two amounts:

- (i) Expenses Facility Agreement dated 12 April 2017: £605,496 (2017: £333,496); and
- (ii) Subordinated Loan Facility: £428,829 (2017: £202,104).

Included in trade payables in note 16 was an amount of £1,485,423 (2017: £Nil) owed to Wellesley & Co. Limited in respect of inter-company management charge payable by Wellesley Finance plc. The total amount charged for the year ended 31 December 2018 was £3,622,574 (2017: £3,034,613).

In addition, Wellesley Finance plc invested £3,000 and £2,000 in Series 6 and A respectively of the Irish Listed ISA bond issued by Wellesley Secured Finance plc during the year. Wellesley Finance plc continues to hold £10,000 and £15,000 in 3 and 5 respectively from prior year. Details are below:

	2018	2017
	£	£
<i>Investment by Wellesley Finance plc in Irish Listed ISA bond</i>		
Opening balance	236,092	-
Advances	5,000	225,000
Repayments	(204,977)	(436)
Interest owed	8,657	11,528
	44,772	236,092

The maximum balance during the year was £243,305 (2017: £236,092).

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

23 Ultimate controlling party

Wellesley Group Limited, a company incorporated in England, is the immediate parent of the Company. The ultimate controlling party of the immediate parent is IFX Group Trust. Neither the immediate parent or ultimate controlling party prepare consolidated financial statements. Wellesley Group Investors Limited, parent of Wellesley Group Limited, prepares consolidated financial statements which includes the results of the Company for the year.

Registered addresses:

Wellesley Group Limited and Wellesley Group Investors Limited - 6th Floor St Albans House, 57/59 Haymarket, London, SW1Y 4QX

IFX Group Trust – 14/15 Mount Havelock, Douglas, Isle of Man, IM1 2QG.

24 Reconciliation of liabilities arising from financing activities

	Cashflows		Non - cash changes		
	1 January 2018		Interest payable	Other	31 December 2018
	£	£	£	£	£
Interest-bearing loans and borrowings	78,451,910	20,226,824	1,209,366	(347,888)	99,540,212
	78,451,910	20,226,824	1,209,366	(347,888)	99,540,212

	Cashflows		Non - cash changes		
	1 January 2017		Interest payable	Other	31 December 2017
	£	£	£	£	£
Interest-bearing loans and borrowings	50,039,561	29,504,903	(788,730)	(303,824)	78,451,910
	50,039,561	29,504,903	(788,730)	(303,824)	78,451,910

	Cashflows		Non - cash changes		
	1 January 2018		Interest payable	Other	31 December 2018
	£	£	£	£	£
Interest-bearing loans and borrowings	78,451,910	20,226,824	1,209,366	(347,888)	99,540,212
	78,451,910	20,226,824	1,209,366	(347,888)	99,540,212

	Cashflows		Non - cash changes		
	1 January 2017		Interest payable	Other	31 December 2017
	£	£	£	£	£
Interest-bearing loans and borrowings	50,039,561	29,504,903	(788,730)	(303,824)	78,451,910
	50,039,561	29,504,903	(788,730)	(303,824)	78,451,910

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

25 Prior period restatement

1. Interest payable on the Wellesley ISA Bond (redeemed in full in 2018) and on the Wellesley Mini-Bond was over-accrued at 31 December 2017 by £1,365,699. This difference was found to relate to the financial years ended 31 December 2016 and 31 December 2017. The impact of this restatement for the year ended 31 December 2017 was £544,189, with the balance of £821,510 being an adjustment to brought forward reserves.
2. Fees payable to Peer-to-Peer investors were under-accrued at 31 December 2017 by £86,316 and as such this adjustment was made for the year ended 31 December 2017.
3. The calculation of realised and unrealised gains on Derivatives held for risk management was incorrectly calculated during the year ended 31 December 2017. As a result, an adjustment of £818,479 has been required for the year ending 31 December 2017.
4. Following the introduction of IFRS 9 on 1 January 2018, the Company is required to calculate provisions in a different way than under the previous accounting standard (IAS39). The requirement is now to calculate on an expected loss basis, rather than an incurred loss model. As a result, a comparative amount has been required for the year ended 31 December 2017, and the amount was calculated as £86,937.
5. The accounting model used for the Company's loan assets was found to be incorrect during the year. This was due to a misinterpretation of the accounting standard at the time the model was built. The misinterpretation relates to the incorrect use of the current IRR as the discount factor in the revenue model, whereas it should have used the original IRR. This meant that the amortised cost of the Company's loans was incorrect and led to differences being noted in the recognition of income, provisions, and write off of bad loans. Accordingly, adjustments have been made in each of these cases.
6. In addition to the errors highlighted in the income model above, the model was also found to have input errors. This led to some transactions being duplicated and led to the statement of financial position being overstated by £3.7m. This issue was identified by management during 2018, and as a result requires the write off of this unsubstantiated asset as an exceptional item. The exceptional item has been recognised in the 2017 Statement of profit and loss but there is a risk that it relates to periods prior to 1 January 2017. The issue went unnoticed in part due to the way that the loan book and Peer to Peer liabilities were historically recognised. As each loan may be partly owned by Peer to Peer customers and partly by Wellesley, calculations were completed in order to assess the amount that should appear on the statement of financial position, and how much should be derecognised. During 2018 a full reconciliation exercise was conducted, and a new CASS process implemented, to bring all loan assets and Peer to Peer liabilities onto the Statement of Financial Position (for internal reconciliation purposes only) and this identified the overstatement of assets. Updated reconciliation processes are now in place to ensure such errors cannot occur again.
7. An internal VAT review identified a further liability of the Company to a related party and hence the liability has been recognised.
8. When Wellesley received retail funding via Peer to Peer investors in the past, the capital invested is matched to loans originated by Wellesley. At that point, Wellesley derecognise that part of the loan that they no longer own. The fee payable to Peer to Peer customers is however the liability of Wellesley and should be represented as a liability on the balance sheet. At the end of 2017 the accrued fees due to Peer to Peer customer of £5.4m was, for accounting purposes only, incorrectly matched to loans rather than appearing as a liability on the balance sheet. The net effect to the statement of profit and loss and statement of financial position is nil in both cases, but this has impacted the presentation of loan assets and liabilities accordingly.

WELLESLEY FINANCE PLC

Notes forming part of the financial statements for the year ended 31 December 2018

25 Prior period restatement (continued)

The effect on the statement of comprehensive income and statement of Financial Position is shown below:

	Note	Impact on Statement of comprehensive income	
		Period to 31 December 2017	Period to 31 December 2016
		£	£
Decrease in Interest expense	1	544,189	821,510
Increase in Fee and commission expense	2	(86,316)	-
Decrease in Income from derivatives and other financial instruments at fair value through profit or loss	3	(818,479)	-
Increase in Impairment of loans and advance to customers (net)	4	(86,937)	-
(Decrease)/increase in Interest income/Fee and commission income	5	(5,696,618)	2,069,803
Decrease/(increase) in Impairment of loans and advance to customers (net)	5	3,807,835	(22,745)
Decrease in Write off of loans and advances to customers	5	66,222	-
Exceptional expense	6	(3,699,685)	-
Increase in Administrative expenses	7	(127,133)	-
Impact for the year		(6,096,922)	2,868,568

	Note	Impact on Statement of financial position	
		As at 31 December 2017	As at 31 December 2016
		£	£
Decrease in Interest-bearing loans and borrowings	1	544,189	821,510
Increase in Other liabilities		(86,316)	-
Decrease in Derivative financial assets	3	(818,479)	-
Decrease in Loans and advances to customers	4	(86,937)	-
(Decrease)/increase in Loans and advances to customers	5	(5,696,618)	2,069,803
Increase/(decrease) in Loans and advances to customers	5	3,807,835	(22,745)
Increase in Loans and advances to customers	5	66,222	-
Decrease in Loans and advances to customers	6	(3,699,685)	-
Increase in Other liabilities	7	(127,133)	-
Increase in Loans and advances to customers	8	5,248,075	-
Decrease in Other liabilities	8	(5,248,075)	-
Impact on equity		(6,096,922)	2,868,568