Company Registration No: 09166258

PARAGON MORTGAGES (No.21) PLC

Report and Financial Statements

For the year ended 30 September 2016

STRATEGIC REPORT

BUSINESS REVIEW AND PRINCIPAL ACTIVITIES

Paragon Mortgages (No. 21) PLC ('the Company') is a special purpose company established to act as a funding vehicle within The Paragon Group of Companies PLC ('the Group') and was set up to provide finance for its mortgage loan assets, by issuing mortgage backed floating rate loan notes and using the proceeds to purchase mortgage loans from other group companies of the Group.

On 13 November 2014 the Company issued floating rate notes and used the proceeds to purchase mortgage loans from Paragon Mortgages 2010 Limited, a fellow group company of the Group. During the year the Company operated in the United Kingdom, the principal activity of the Company is the provision of first mortgage loans. There have been no significant changes in the Company's principal activities in the year under review. The directors are not aware, at the date of this report, of any likely major changes in the Company's activities in the next year.

As shown in the Company's profit and loss account on page 7, the profit after tax of £1,000 has stayed consistent with the preceding year.

The balance sheet on page 8 of the Financial Statements shows the Company's financial position at the year end. Loans to customers have decreased by 21% due to customers redeeming their account during the year. As a result the asset backed loan notes have reduced by 17% during the year.

No interim dividend was paid during the year (2015: £nil). No final dividend is proposed (2015: £nil).

The Company has entered into derivative contracts in order to provide an economic hedge against its exposure to fixed rate loans to customers. Although these instruments provide an economic hedge the prescriptive nature of the requirements of by International Accounting Standard 39 – 'Financial Instruments: Recognition and Measurement' ('IAS 39') means that hedge accounting cannot always be achieved. This has led to the Company recognising a fair value net gain of £624,000 (2015: £1,043,000 net loss) due to the ineffectiveness of the hedge relationship. This represents a timing difference and cumulative gains and losses recognised will tend to zero over time.

The Group manages its operations on a centralised basis. For this reason, the Company's directors believe that further key performance indicators for the Company are not necessary or appropriate for an understanding of the development, performance or position of the business. The performance of the Group's mortgage lending operation, which includes the Company, is discussed in the Group's Annual Report, which does not form part of this Report.

PRINCIPAL RISKS AND UNCERTAINTIES

The Company is a securitisation company and has been structured so as to avoid, in as far as is possible, all forms of financial risk with its outstanding loan notes match-funded to maturity. An analysis of the Company's exposure to risk, including financial risk, and the steps taken to mitigate these risks are set out in note 5, and a discussion of critical accounting estimates is set out in note 4.

After considering the above, the directors have a reasonable expectation that the Company will have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Financial Statements.

STRATEGIC REPORT (CONTINUED)

ENVIRONMENT

The Group recognises the importance of its environmental responsibilities, monitors its impact on the environment, and designs and implements policies to reduce any damage that might be caused by the Group's activities. The Company operates in accordance with group policies, which are described in the Group's Annual Report, which does not form part of this Report.

EMPLOYEES

The Company has no employees. All operational services are provided by employees of the Group. The Group's employment policies are described in its Annual Report, which does not form part of this Report.

Approved by the Board of Directors

and signed on behalf of the Board

J Fairrie

Director

26 January 2017

DIRECTORS' REPORT

The directors present their Annual Report prepared in accordance with Schedule 7 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 and the audited Financial Statements of Paragon Mortgages (No.21) PLC, a company registered in England and Wales with registration no: 09166258, for the year ended 30 September 2016.

GOING CONCERN

After making enquiries, the directors believe 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 financial statements.

CORPORATE GOVERNANCE

The directors have been charged with governance in accordance with the transactional documentation detailing the mechanism and structure of the transaction. The structure of the Group is such that the key policies have been predetermined at the time of issuance and the operational roles have been assigned to third parties with their roles strictly governed by the transaction documents.

DIRECTORS

The directors during the period and subsequently were:

J A Harvey

J P Nowacki

SFM Directors Limited

SFM Directors (No.2) Limited

J Fairrie (appointed 21 November 2016)

DIRECTORS' INDEMNITIES

The company has made qualifying third party indemnity provisions for the benefit of its directors which were made during the year and remain in force at the date of this report.

The directors have taken all necessary steps to make themselves and the Company's auditor aware of any information needed in preparing the audit of the Annual Report and Financial Statements for the year, and, as far as each of the directors is aware, there is no relevant audit information of which the auditor is unaware.

This confirmation is given and should be interpreted in accordance with the provisions of Section 418 (2) of the Companies Act 2006.

AUDITOR

A resolution for the re-appointment of KPMG LLP as the auditor of the Company is to be proposed at the forthcoming Annual General Meeting.

DIRECTORS' REPORT (CONTINUED)

INFORMATION PRESENTED IN OTHER SECTIONS

Certain information required to be included in a directors' report by the Companies Act 2006 and regulations made there under can be found in the other sections of the Annual Report, as described below. All of the information presented in these sections is incorporated by reference into this Directors' Report and is deemed to form part of this report.

- Commentary on the likely future developments in the business of the Company is included in the Strategic Report.
- A description of the Company's financial risk management objectives and policies, and its exposure to risks arising from its use of financial instruments are set out in note 5 to the accounts.
- Disclosure on any dividends paid during the year is included in the Strategic Report.

Approved by the Board of Directors

and signed on behalf of the Board

J Fairrie

Director

26 January 2017

Registered Office: 51 Homer Road, Solihull, West Midlands, B91 3QJ

STATEMENT OF DIRECTORS' RESPONSIBILITIES
in relation to Financial Statements

The directors are responsible for preparing the Annual 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 that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to 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 these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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 their profit or loss for that period.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and 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, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of a strategic report and directors' report which comply with the applicable requirements of the Companies Act 2006.

Approved by the Board of Directors and signed on behalf of the Board.

Pandora Sharp

Company Secretary

26 January 2017

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF PARAGON MORTGAGES (No.21) PLC

We have audited the Financial Statements of Paragon Mortgages (No.21) PLC for the year ended 30 September 2016 which comprise the profit and loss account, the balance sheet, the statement of movements in equity and the related notes 1 to 20. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice), including FRS 101 Reduced Disclosure Framework.

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.

Respective responsibilities of directors and auditor

As explained more fully in the Statement of Directors' Responsibilities, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

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

Opinion on Financial Statements

In our opinion the Financial Statements:

- give a true and fair view of the state of the Company's affairs as at 30 September 2016 and of its profit for the 14 month period then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion 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.

Matters on which we are required to report by exception

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

- adequate accounting records have not been kept, 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.

Andrew Walker (Senior Statutory Auditor)

for and on behalf of KPMG LLP, Statutory Auditor

Chartered Accountants

One Snowhill, Snow Hill Queensway, Birmingham, B4 6GH

26 January 2017

PROFIT AND LOSS ACCOUNT

Year ended September 2016

	Note	2016 £000	2015 £000
Interest receivable			
Loans to customers		9,917	10,544
Other		90	93
		10,007	10,637
Interest payable and similar charges	6	(5,463)	(5,170)
Net interest income		4,544	5,467
Other operating income		100	15
Total operating income		4,644	5,482
Operating expenses		(5,267)	(4,438)
		(623)	1,044
Fair value net gain / (loss)	8	624	(1,043)
Operating profit, being profit on ordinary activities before taxation	9	1	1
Tax on profit on ordinary activities	10	-	-
Profit on ordinary activities after taxation	16	1	1

All activities derive from continuing operations.

There are no recognised gains or losses other than the profit for the current year and preceding period, and consequently a separate statement of comprehensive income has not been presented.

BALANCE SHEET

30 SEPTEMBER 2016

	Note	2016 £000	2016 £000	2015 £000	2015 £000
ASSETS EMPLOYED					
FIXED ASSETS					
Financial assets	11		186,765		237,895
CURRENT ASSETS					
Debtors falling due within one year	14	732		21	
Cash at bank		19,098		10,111	
			19,830		10,132
			206,595		248,027
FINANCED BY					
EQUITY SHAREHOLDERS' FUNDS					
Called up share capital	15	12		12	
Profit and loss account	16	2		1	
			14		13
CREDITORS					
Amounts falling due within one year	17	3,624		3,361	
Amounts falling due after more than one year	17	202,957		244,653	
			206,581		248,014
			206,595		248,027

These Financial Statements were approved by the Board of Directors on 26 January 2017.

Signed on behalf of the Board of Directors

J Fairrie

Director

STATEMENT OF MOVEMENTS IN EQUITY

YEAR ENDED 30 SEPTEMBER 2016

	Share capital £000	Profit and loss account £000	Total equity £000
Total comprehensive income for the year			
Profit for the year	-	1	1
Other comprehensive income	-	-	-
Total comprehensive income for the year	-	1	1
Opening equity	12	1	13
Closing equity	12	2	14

YEAR ENDED 30 SEPTEMBER 2015

	Share capital £000	Profit and loss account £000	Total equity £000
Total comprehensive income for the year			
Profit for the year	-	1	1
Other comprehensive income	-	-	-
Total comprehensive income for the year	-	1	1
Transactions with owners			
Issue of shares	12	-	12
Net movement in equity in the year	12	1	13
Opening equity	-	-	-
Closing equity	12	1	13

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

1. GENERAL INFORMATION

Paragon Mortgages (No. 21) PLC ('the Company') is a company domiciled in the United Kingdom and incorporated in England and Wales under the Companies Act 2006 with company number 09166258. The address of the registered office is 51 Homer Road, Solihull, West Midlands, B91 3QJ. The nature of the Company's operations and its principal activities are set out in the Strategic Report.

These financial statements are presented in pounds sterling, which is the currency of the economic environment in which the Company operates

2. ACCOUNTING POLICIES

The Financial Statements have been prepared in accordance with applicable UK accounting standards. Disclosures have been made in accordance with Financial Reporting Standard 101 – 'Reduced Disclosure Framework' ('FRS 101').

As permitted by FRS 100 – 'Application of Financial Reporting Requirements' ('FRS 100') the Company has applied the measurement and recognition requirements of International Financial Reporting Standards ('IFRS') as adopted by the EU, but makes amendments where necessary in order to comply with the Companies Act 2006 and has set out below where advantage of disclosure exemptions provided by FRS 101 has been taken.

On its transition to FRS 101 the Company has applied IFRS 1 – 'First-time Adoption of IFRS' whilst ensuring its assets and liabilities are measured in compliance with FRS 101. An explanation of how the transition to FRS 101 has affected the reported financial position and performance of the Company is provided in note 3.

Accounting convention

The Financial Statements are prepared under the historical cost convention, except as required in the valuation of certain financial instruments which are carried at fair value.

Going concern

The Financial Statements have been prepared on a going concern basis. The directors have a reasonable expectation that the Company will have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the Financial Statements.

Loans to customers

Loans to customers are considered to be 'loans and receivables' as defined by IAS 39. They are therefore accounted for on the amortised cost basis.

Such loans are valued at inception as the amount of initial advance, which is the fair value at that time, inclusive of procuration fees paid to brokers or other business providers and less initial fees paid by the customer. Thereafter they are valued at this amount less the cumulative amortisation calculated using the Effective Interest Rate ('EIR') method. The loan balances are then reduced where necessary by a provision for balances which are considered to be impaired.

The EIR method spreads the expected net income arising from a loan over its expected life. The EIR is that rate of interest which, at inception, exactly discounts the expected future cash payments and receipts arising from the loan to the initial carrying amount.

The Company's policy is to hedge against any exposure to fixed rate loan assets (note 5).

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

2. ACCOUNTING POLICIES (CONTINUED)

Impairment of loans and receivables

Loans and receivables are reviewed for indications of possible impairment throughout the year and at each balance sheet date in accordance with IAS 39. Where loans exhibit objective evidence of impairment (a 'loss event') the carrying value of the loans is reduced to the net present value of their expected future cash flows, including the value of the potential realisation of any security (net of sales costs) discounted at the original EIR.

Within its buy-to-let portfolio the Group utilises a receiver of rent process, whereby the receiver stands between the landlord and tenant and will determine an appropriate strategy for dealing with any delinquency. This strategy may involve the immediate sale of any underlying security or the short or long term letting of the property to cover arrears and principal shortfalls. Properties in receivership are either returned to their landlord owners or sold.

Loss events reflect both loans that display delinquency in contractual payments of principal or interest or, for buy-to-let loans in receivership but up to date at the balance sheet date, properties where the receiver adopts a sale strategy, where a shortfall may or may not arise.

In addition to loans where loss events are evident, loans are also assessed collectively, grouped by risk characteristics and account is taken of any impairment arising due to events which are believed to have taken place but have not been specifically identified at the balance sheet date. Collective impairment provisions are calculated for each key portfolio based on recent historical performance, with adjustments for expected changes in losses based on management's judgement.

For financial accounting purposes provisions for impairments of loans to customers when first recognised in the income statement are held in an allowance account. These balances are released to offset against the gross value of the loan when it is written off to profit and loss on the administration system. After this point a salvage balance may be held in respect of any further recoveries expected on the loan.

Cash at bank

Balances shown as cash at bank in the balance sheet comprise demand deposits and short-term deposits with banks with initial maturities of not more than 90 days.

Current tax

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

Borrowings

Borrowings are carried in the balance sheet on the amortised cost basis. The initial value recognised includes the principal amount received less any discount on issue or costs of issuance.

Interest and all other costs of the funding are expensed to the profit and loss account as interest payable over the term of the borrowing on an Effective Interest Rate basis.

Derivative financial instruments

Derivative instruments utilised by the Company comprise currency swaps and interest rate swaps. All such instruments are used for hedging purposes to alter the risk profile of the existing underlying exposure of the Company in line with the Company's risk management policies (note 5).

The Company does not enter into speculative derivative contracts.

All derivatives are carried in the balance sheet at fair value, as assets where the value is positive or as liabilities where the value is negative. Fair value is based on market prices, where a market exists. If there is no active market, fair value is calculated using present value models which incorporate assumptions based on market conditions and are consistent with accepted economic methodologies for pricing financial instruments. Changes in the fair value of derivatives are recognised in the profit and loss account, except where such amounts are permitted to be taken to equity as part of the accounting for a cash flow hedge.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

2. ACCOUNTING POLICIES (CONTINUED)

Hedging

For all hedges, the Company documents, at inception, the relationship between the hedging instruments and the hedged items, as well as its risk management strategy and objectives for undertaking the transaction. The Company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the hedging arrangements put in place are considered to be 'highly effective' as defined by IAS 39.

For a fair value hedge, as long as the hedging relationship is deemed 'highly effective' and meets the hedging requirements of IAS 39, any gain or loss on the hedging instrument recognised in income can be offset against the fair value loss or gain arising from the hedged item for the hedged risk. For macro hedges (hedges of interest rate risk for a portfolio of loan assets) this fair value adjustment is disclosed in the balance sheet alongside the hedged item, for other hedges the adjustment is made to the carrying value of the hedged asset or liability. Only the net ineffectiveness of the hedge is charged or credited to income. Where a fair value hedge relationship is terminated, or deemed ineffective, the fair value adjustment is amortised over the remaining term of the underlying item.

Where a derivative is used to hedge the variability of cash flows of an asset or liability, it may be designated as a cash flow hedge so long as this relationship meets the hedging requirements of IAS 39. For such an instrument the effective portion of the change in the fair value of the derivative is taken initially to equity, with the ineffective part taken to profit or loss. The amount taken to equity is released to the profit and loss account at the same time as the hedged item affects the profit and loss account. Where a cash flow hedge relationship is terminated, or deemed ineffective, the amount taken to equity will remain there until the hedged transaction is recognised, or is no longer highly probable.

Amounts owed by or to group companies

The balances owed by or to other group companies are carried at the current amount outstanding less any provision.

Revenue

The revenue of the Company comprises interest receivable and other income. The accounting policy for the recognition of each element of revenue is described separately within these accounting policies.

Fee and commission income

Other income includes administration fees charged to borrowers, which are credited to the profit and loss account when the related service is performed.

Deferred purchase consideration

Under the Mortgage sale agreement profits from the company are paid up to the companies which originated the loans by way of deferred purchase consideration. Deferred purchase consideration is recognised in which it becomes payable and is paid when sufficient cash resources allow. Paragon Mortgages (2010) Limited, to whom deferred purchase consideration is paid, is a fellow group company.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

2. ACCOUNTING POLICIES (CONTINUED)

Disclosures

In preparing these financial statements the Company has taken advantage of the exemptions from disclosure provided by FRS 101 in respect of:

- The requirement to produce a cash flow statement and related notes
- The requirement to provide comparative period reconciliations in respect of share capital
- Disclosures in respect of transactions with wholly owned subsidiaries
- Disclosures in respect of capital management
- The effects of new, but not yet effective IFRSs
- Disclosures in respect of key management personnel
- Disclosures of transactions with a management entity which provides key management personnel services to the Company

As the consolidated financial statements of The Paragon Group of Companies PLC, the ultimate parent undertaking of the Company, include equivalent disclosures the Company has also taken advantage of these further exemptions provided by FRS 101:

- Certain disclosures required by IFRS 13 – 'Fair Value Measurement'
- Certain disclosures required by IFRS 7 – 'Financial Instruments Disclosures'

The Company presently intends to continue to apply these exemptions in future periods.

3. TRANSITION TO FRS 101

As stated in note 2 these are the first financial statements prepared by the Company in accordance with FRS 100 and FRS 101. The accounting policies used in drawing up the financial statements for the year ended 30 September 2016 are set out in note 2 and these have also been applied in preparing the comparative information presented in these financial statements.

In preparing these accounts the Company has not been required to adjust amounts presented in its balance sheet under old UK GAAP. This is a result of the old UK Accounting Standards principally affecting the Company's accounting, FRS 25 – 'Financial Instruments: Presentation' and FRS 26 – 'Financial Instruments: Recognition and Measurement' being equivalent to their IFRS counterparts IAS 32 - 'Financial Instruments: Presentation' and IAS 39.

The principal presentational adjustment has been the combination of the Company's short term investment balances, representing investments with original maturities of more than 7 but less than 90 days, with cash balances for disclosure.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

4. CRITICAL ACCOUNTING ESTIMATES

Certain balances reported in the Financial Statements are based wholly or in part on estimates or assumptions made by the directors. There is, therefore, a potential risk that they may be subject to change in future periods. The most significant of these are:

Impairment losses on loans to customers

Impairment losses on loans are calculated based on statistical models. The key assumptions revolve around estimates of future cash flows from customers' accounts, their timing and, for secured accounts, the expected proceeds from the realisation of the property. These key assumptions are based on observed data from historical patterns and are updated regularly based on new data as it becomes available.

In addition the directors consider how appropriate past trends and patterns might be in the current economic situation and make any adjustments they believe are necessary to reflect the current conditions.

The accuracy of the impairment calculations would therefore be affected by unexpected changes to the economic situation, variances between the models used and the actual results or assumptions which differ from the actual outcomes.

In particular, if the impact of economic factors such as employment levels on customers is worse than is implicit in the model then the number of accounts requiring provision might be greater than suggested by the model, while falls in house prices, over and above any assumed by the model might increase the provision required in respect of accounts currently provided.

Effective interest rates

In order to determine the EIR applicable to loans and borrowings an estimate must be made of the expected life of each loan and hence the cash flows relating thereto. For purchased accounts this will involve estimating the likely future performance of the accounts at the time of acquisition. These estimates are based on historical data and reviewed regularly. For purchased accounts historical data obtained from the vendor will be examined. The accuracy of the EIR applied would therefore be compromised by any differences between actual repayment profiles and that predicted, which in turn would depend directly or indirectly on customer behaviour.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

5. FINANCIAL RISK MANAGEMENT

The Company's operations are financed principally by floating rate, asset backed loan notes and, to a lesser extent, by a mixture of share capital and loans from other group companies of the Group. The Company issues financial instruments to finance the acquisition of its portfolio of loans to customers and uses derivative financial instruments to hedge interest rate risk arising from fixed rate lending. In addition, various financial instruments, for example debtors and accruals, arise directly from the Company's operations.

The principal risks arising from the Company's financial instruments are credit risk, liquidity risk and interest rate risk. The board of the Company's holding company reviews and agrees policies for all companies in the Group managing each of these risks and they are summarised below. These policies have remained unchanged throughout the period and since the period end.

Credit risk

The Company's credit risk is primarily attributable to its loans to customers. The maximum credit risk at 30 September 2016 approximates to the carrying value of loans to customers (note 12). There are no significant concentrations of credit risk due to the large number of customers included in the portfolios.

The Company acquired mortgages from Paragon Mortgages (2010) Limited, a fellow group company of the Group which place strong emphasis on good credit management at the time of underwriting new loans.

The acquired mortgages are secured by first charges over residential properties in the United Kingdom. Despite this security, in assessing credit risk an applicant's ability to repay the loan remains the overriding factor in the decision to lend by the originating lender. Additionally, each mortgage has the benefit of one or more life assurance policies and certain mortgages have the benefit of a mortgage guarantee indemnity insurance policy.

Paragon Mortgages (2010) Limited, a fellow group company of the Group, continued to administer the mortgages on behalf of Paragon Mortgages (No.21) PLC and the collections process is the same as that utilised for all companies in the group.

In order to control credit risk relating to counterparties to the Company's financial instruments, the board of the Company's holding company determines on a group basis, which counterparties the group of companies will deal with, establishes limits for each counterparty and monitors compliance with those limits.

Liquidity risk

The Company's assets are principally financed by asset backed loan notes issued through the securitisation process. Details of the Company's borrowings are given in note 18. Securitisation effectively eliminates the Company's liquidity risk by matching the maturity profile of the Company's funding to the profile of the assets to be funded.

Interest rate risk

The Company's policy is to maintain floating rate liabilities and match these with floating rate assets by the use of interest rate swap agreements.

The rates payable on the asset backed loan notes issued by the Company are reset quarterly on the basis of LIBOR. The Company's assets predominantly bear LIBOR linked interest rates or are hedged fixed rate assets. The interest rates charged on the Company's variable rate loan assets are determined by reference to, inter alia, the Company's funding costs and the rates being charged on similar products in the market. Generally this ensures the matching of changes in interest rates on the Company's loan assets and borrowings and any exposure arising on the interest rate resets is relatively short term.

In part, the Company's interest rate hedging objectives are achieved by the controlled mismatching of the dates on which instruments mature, redeem or have their interest rates reset.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

5. FINANCIAL RISK MANAGEMENT (CONTINUED)

Currency risk

The Company has no material exposure to foreign currency risk.

Use of derivative financial instruments

The Company uses derivative financial instruments for risk management purposes. Such instruments are used only to limit the exposure of the Company to movements in market interest rates, as described above.

It is, and has been throughout the period under review, the Company's policy that no trading in financial instruments shall be undertaken, and hence all of the Company's derivative financial instruments are for commercial hedging purposes. These are used to protect the Company from exposures principally arising from fixed rate lending. Hedge accounting is applied where appropriate, though it should be noted that some derivatives, while forming part of an economic hedge relationship, do not qualify for this accounting treatment under IAS 39 either because natural accounting offsets are expected, or obtaining hedge accounting would be especially onerous.

The Company has designated a number of derivatives as fair value hedges. In particular this treatment is used for hedging the interest rate risk of groups of fixed rate prepayable loan assets with interest rate derivatives on a portfolio basis. The Company believes this solution is the most appropriate as it is consistent with the economic hedging approach taken by the Company to these assets.

6. INTEREST PAYABLE AND SIMILAR CHARGES

	2016 £000	2015 £000
Asset backed loan notes	4,087	3,850
Interest rate swaps	1,005	954
Subordinated loan interest	287	263
Interest on fee letter	84	103
	5,463	5,170

7. DIRECTORS AND EMPLOYEES

Directors' remuneration from the Company during the period is stated in note 9.

The Company had no employees in the current period. All administration is performed by employees of the related companies under the servicing agreement described in note 18. One director of the Company is employed by Paragon Finance PLC, a related party, and their remuneration is disclosed within the financial statements of that company, which do not form part of this Report.

8. FAIR VALUE NET GAIN / (LOSS)

The fair value net gain of £624,000 (2015: net loss £1,043,000) represents the accounting volatility on derivative instruments which are matching risk exposure on an economic basis. Some accounting volatility arises on these items due to accounting ineffectiveness on designated hedges, or because hedge accounting has not been adopted or is not achievable on certain items. The gain / (loss) is primarily due to timing differences in income recognition between the derivative instruments and the economically hedged assets and liabilities.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

9. OPERATING PROFIT, BEING PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION

	2016 £000	2015 £000
Operating profit is after charging:		
Directors' fees	10	8
Auditor remuneration - audit services	9	9
Deferred purchase consideration	4,496	2,940

Non audit fees provided to the Group are disclosed in the accounts of the parent company and the exemption from disclosure of fees payable to the Company's auditor in respect to non-audit services in these financial statements has been taken.

10. TAX ON PROFIT ON ORDINARY ACTIVITIES

a) Tax charge for the period

	2016 £000	2015 £000
Current tax		
Corporation tax	-	-

b) Factors affecting the tax charge for the year

	2016 £000	2015 £000
Profit before tax	1	1
UK corporation tax at 20% (2015: 20.5%) based on the profit for the period	-	-

During 2013 the UK Government enacted provisions reducing the rate of corporation tax from 21.0% to 20.0% from 1 April 2015.

During the year ended 30 September 2015 the Government announced provisions further reducing the rate of corporation tax to 19.0% with effect from 1 April 2017 and to 18.0% from 1 April 2020 which were substantially enacted during the year. The tax rate applying from 1 April 2020 was further reduced to 17% during the year.

Therefore the standard rate of corporation tax applicable to the Company for the year ended 30 September 2016 was 20.0%, the rate in the year ended 30 September 2017 is expected to be 19.5%, the rate in the years ending 30 September 2018 and 30 September 2019 are expected to be 19.0%, the rate in the year ending 30 September 2020 is expected to be 18.0% and the rate in subsequent years is expected to be 17.0%.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

11. FINANCIAL ASSETS

	2016 £000	2015 £000
Loans to customers (note 12)	186,765	237,895
Derivative financial assets (note 13)	-	-
	186,765	237,895

12. LOANS TO CUSTOMERS

Loans to customers at 30 September 2016, which are all denominated and payable in sterling, are first mortgages which are secured on residential property within the United Kingdom and are categorised as loans and receivables as defined by IAS 39.

Mortgage loans have a contractual term of up to thirty years, the borrower is entitled to settle the loan at any point and in most cases such early settlement does take place. All borrowers are required to make monthly payments, except where an initial deferred period is included in the contractual terms.

All the mortgage loans are pledged as collateral for asset backed loan notes at 30 September 2016.

	2016 £000	2015 £000
Balance at 1 October 2015	237,895	-
Additions	652	248,105
Other debits	10,048	10,925
Repayments and redemptions	(61,830)	(21,135)
Balance at 30 September 2016	186,765	237,895

Other debits include primarily interest charged to customers on loans outstanding and other changes in the amortised cost of the assets caused by the effective interest rate method.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

13. DERIVATIVE FINANCIAL ASSETS AND LIABILITIES

All of the Company's financial derivatives are held for economic hedging purposes, although not all may be designated for hedge accounting in accordance with the provisions of IAS 39. The analysis below therefore splits derivatives between those accounted for as hedges and those which, while representing an economic hedge do not qualify for this treatment.

	2016	2016	2016	2015	2015	2015
	Notional amount	Assets	Liabilities	Notional amount	Assets	Liabilities
	£000	£000	£000	£000	£000	£000
Other derivatives						
Interest rate swaps	70,350	-	(452)	163,850	-	(1,091)
Total recognised derivative assets / (liabilities)	70,350	-	(452)	163,850	-	(1,091)

14. DEBTORS

	2016	2015
	£000	£000
Amounts falling due within one year:		
Amounts owed by group companies	12	12
Other debtors (note 19)	712	1
Prepayments and accrued income	8	8
	732	21

15. CALLED UP SHARE CAPITAL

	2016	2015
	£	£
Allotted:		
49,999 ordinary shares of £1 each (25p called up and paid)	12,500	12,500
1 ordinary shares of £1 each (fully paid)	1	1
	12,501	12,501

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

16. PROFIT AND LOSS ACCOUNT

	£000
At 7 August 2014	-
Profit for the period	1
At 1 October 2015	1
Profit for the financial year	1
At 30 September 2016	2

17. CREDITORS

	2016 £000	2015 £000
Amounts falling due within one year:		
Other creditors	3,394	3,086
Accruals and deferred income	230	275
	3,624	3,361

	2016 £000	2015 £000
Amounts falling due after more than one year:		
Asset backed loan notes	196,255	237,312
Derivative financial liabilities (note 13)	452	1,091
Intercompany subordinated loan	6,250	6,250
	202,957	244,653

A maturity analysis and further details of the asset backed loan notes are given in note 18.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

18. BORROWINGS

The mortgage backed floating rate notes are secured over a portfolio comprising fixed and variable rate mortgage loans secured by first charges over residential properties in the United Kingdom. The notes are subject to mandatory redemption in part on each interest payment date in an amount equal to the principal received or recovered in respect of the mortgage. As a result of this structure, cash received in respect of loan assets is not immediately available for distribution. At 30 September 2016, the amount of restricted cash and investments held within the Company was £19,098,000 (2015: £10,111,000). The maturity date of the notes matches the maturity date of the underlying assets. It is likely that a substantial proportion of these notes will be repaid within five years.

The Company has the option to repay all of the notes at an earlier date (the 'call date'), or at any interest payment date thereafter, at the outstanding principal amount

Interest is payable at a fixed margin above:

- the London Interbank Offered Rate ('LIBOR') on notes denominated in sterling;

All payments in respect of the notes are required to be made in the currency in which they are denominated.

Notes in issue at 30 September 2016 and 30 September 2015 were:

Notes	Maturity date	Call date / Turbo date	Principal outstanding 2016	Principal outstanding 2015	Note margin 2016	Note margin 2015
			£m	£m		
'A'	Jun 2042	Dec 2018	165.6	207.2	0.80%	0.80%
'B'	Jun 2042	Dec 2018	17.7	17.7	1.40%	1.40%
'C'	Jun 2042	Dec 2018	8.1	8.1	1.75%	1.75%
'D'	Jun 2042	Dec 2018	6.3	6.3	2.10%	2.10%

All of the above notes are listed on the main market of the London Stock Exchange.

If the issuer elects not to call and repay the Class A, B, C and D on or after the Call Date / Turbo date, the excess revenue that otherwise would have been paid to the administrator, such as interest on the subordinated loan, is used to repay the Class 'A' Noteholders.

There is a subordinated loan facility under which an amount was drawn down by the Company to establish the first loss fund, which is repayable to Paragon Finance PLC on the earlier of the last interest payment date in June 2042 or the first day on which there are no notes outstanding, except that on any Interest Payment Date sums borrowed will be repaid to the extent of any amount released from the first loss fund. Interest is payable at the rate of 4% above the London Interbank Offered Rate for three month sterling deposits.

There are no amounts of committed but undrawn facilities at 30 September 2016 and 30 September 2015.

NOTES TO THE ACCOUNTS

YEAR ENDED 30 SEPTEMBER 2016

19. RELATED PARTY TRANSACTIONS

The Company has identified the following transactions which are required to be disclosed under the terms of IAS 24 - 'Related Party Disclosures' ('IAS 24').

Transactions with Paragon Mortgages (2010) Limited (PM2010)

At the balance sheet date PM2010, a company under common control as defined IAS 24, acted as servicer of the mortgages for the Company and earned £689,000 (2015: £626,000) during the period in servicing fees. At the balance sheet date the Company owed £49,000 (2015: £59,000) to PM2010 in relation to servicing fees, which is included in accruals and deferred income.

The Company owed £2,312,000 (2015: £1,279,000) to PM2010 at the balance sheet date in relation to deferred purchase consideration, and £nil for mortgage fees and insurance which is included in other creditors.

The Company was owed £712,000 (2015: £1,000) from PM2010 relating to monies received by the servicer, that are yet to be passed onto the Company, which is included in other debtors.

Transactions with Paragon Finance PLC (PF)

At the balance sheet date PF, a company under common control as defined by IAS 24, was owed £1,083,000 (2015: £1,807,000) from the Company in relation to payments made on behalf of the Company, which is included in other creditors.

At the balance sheet date PF held the subordinated loan and Class D notes issued by the Company as disclosed in notes 17 and 18. During the period PF earned £287,000 (2015: £264,000) in subordinated loan interest and £169,000 (2015: £149,000) in Class D note interest. At the balance sheet date the Company owed £12,000 (2015: £13,000) in relation to subordinated loan interest and £7,000 (2015: £7,000) relating to Class D note interest, which are included in accruals and deferred income.

The Company was owed £1,000 (2015: £nil) from PF relating to monies received by the servicer, that are yet to be passed onto the Company, which is included in other debtors.

20. ULTIMATE PARENT COMPANY

The ultimate parent undertaking is SFM Corporate Services Ltd who holds the entire share capital of the Company on a discretionary trust basis for the benefit of certain charities. The directors regard The Paragon Group of Companies PLC as the ultimate controlling party.

The smallest and largest group into which the Company is consolidated is that of The Paragon Group of Companies PLC, registered in England and Wales.

Copies of the Group's financial statements are available from that company's registered office at 51 Homer Road, Solihull, West Midlands, B91 3QJ.