

**BRITANNIA BUILDING SOCIETY**

**TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS  
AND ACCOUNTING POLICIES**

**6 MONTHS ENDED 30 JUNE 2005**

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## **Basis of Preparation**

Prior to 2005, the Group prepared its audited financial statements and unaudited interim financial statements under UK Generally Accepted Accounting Principles (UK GAAP). From 1 January 2005, the Group is required to prepare its annual consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and implemented in the UK. The date of transition to IFRS for the Group was 1 January 2004 and the Group prepared its opening IFRS balance sheet as at that date.

The IFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations that will be applicable as at 31 December 2005, including those that will be applicable on an optional basis, are not yet known with certainty at the time of preparing this report, however, no significant changes are expected between the accounting policies adopted in preparing this report and those that will be adopted in the 2005 audited financial statements.

The Directors have assumed that the EU will endorse the amendment to International Accounting Standard No. 19 (Employee benefits – actuarial gains and losses, group plans and disclosure) (IAS 19) and International Accounting Standard (Financial instruments – the fair value option) (IAS 39).

The comparative figures in respect of 2004 have been prepared in compliance with IFRS. Reconciliations and explanations of the effect of adopting IFRS compliant accounting policies on the Group's equity (net assets), profits and cash flows are provided in the section entitled Transition to IFRS.

This report does not comply with all the disclosures of International Accounting Standard No. 34 (Interim financial reporting) (IAS 34) which is not currently required to be applied under the Listing Rules.

Set out below are the Group's key accounting policies under IFRS which differ from UK GAAP. As a result of the Group's decision to adopt the IFRS1 exemption and not restate comparatives for International Accounting Standard No. 32 (Disclosure and presentation) (IAS 32) and IAS 39, certain accounting policies will only apply from 1 January 2005 and not to the 2004 comparatives. These policies have been denoted with an asterisk. Accounting policies for these items used in the preparation of the 2004 comparatives are as set out in the 2004 Annual Report and Accounts.

## **Consolidation**

The financial information of the Group incorporates the assets, liabilities, and results of Britannia Building Society and its subsidiary undertakings, which includes securitisation vehicles.

### **Subsidiaries**

Entities are regarded as Subsidiaries from the date control is transferred to the Group, with control being where the company has the power to govern the financial and operating policies of an entity so as to obtain benefits from their activities.

Inter-company transactions and balances are eliminated upon consolidation.

### **Interests in joint ventures**

The Group's interests in joint ventures are accounted for using the equity method. Under this method the Group's share of profits or losses is recognised in the income and expenditure account and in the carrying value of the investment.

## **Intangible assets**

### Goodwill

The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost is measured at the fair value of the assets given, shares issued and liabilities undertaken at the date of acquisition, plus costs directly attributable to the acquisition.

Goodwill is the excess cost of acquisition over the fair value of the entity acquired, and is capitalised as an intangible asset with an indefinite life. Any excess of the fair value of net assets acquired over the cost of acquisition is recognised immediately in income.

Under the International Financial Reporting Standard No. 1 (First time adoption of IFRS) (IFRS 1) exemption, the Group has not applied International Financial Reporting Standard No. 3 (Business combinations) (IFRS3), retrospectively. As a result, in the 1 January 2004 opening balance sheet, goodwill arising from past business combinations remains as stated in UK GAAP as at that date after having been tested for impairment.

For an acquisition where provisional figures are used in the financial statements, adjustments to these figures are made within 12 months of the acquisition date on a retrospective basis. Except for deferred tax assets arising, other adjustments after 12 months are accounted for as an error in prior periods, adjusting the acquisition goodwill.

### Acquired intangible assets

Acquired intangible assets are capitalised if they can be separately identified from Goodwill. Their useful lives are based on the period for which they are expected to generate economic benefits. If there are any signs of a decrease in value the asset will be subject to impairment testing. If there is no foreseeable limit on this period, their life is deemed to be indefinite and the asset tested annually for impairment.

### Internally generated intangible assets

Costs associated with maintaining computer software programmes and websites are recognised as a charge to profit as incurred. Costs that are directly associated with the production of identifiable software products, controlled by the Group, and which will generate future economic benefits, are recognised as intangible assets. These assets are amortised on a straight line basis over their useful economic lives, which are limited to a maximum of 5 years.

### Indefinite life assets

The Group currently has no intangible assets with an indefinite life, other than Goodwill.

## **Income and interest expense \***

Interest is recognised on an accruals basis using the effective yield method, which allocates the interest income or expense over the relevant period. When calculating the effective yield, the Group estimates cash flows considering all contractual terms of the financial instrument. The calculation includes all amounts receivable or payable by the Group that are an integral part of the overall return, including origination fees, mortgage incentives, estimated early repayment charges and all other premiums and discounts. It also includes direct incremental transaction costs related to the acquisition or issue of the financial instrument. The calculation does not consider future credit losses.

When a financial asset has been written down as a result of impairment or loss, the interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

## **Fees and commissions**

Fee and commission income other than that directly related to loans is recognised over the period for which service has been provided or on completion of an act to which the fee relates.

## **Taxation**

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their accounting carrying amounts. It is calculated using current tax rates and the liability method.

Deferred tax assets are recognised for all temporary differences to the extent that it is probable that taxable profit will be available against which the reversal of the temporary difference can be utilised.

Deferred and current assets and liabilities are only offset when they arise in the same reporting tax group and where there is both a legal right of offset and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

## **Cash and cash equivalents**

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than 3 months maturity from the date of acquisition; including cash and balances with central banks, treasury bills and other eligible bills, amounts due from other banks and short term liquid investments.

## **Property, plant, equipment and depreciation**

All property, plant and equipment is stated at cost less accumulated depreciation less any provision for impairment. Cost includes expenditure that is directly attributable to the acquisition of the item. Depreciation is calculated on a straight line method to write down the cost of such assets to their residual values over their estimated useful lives as follows:

Freehold and long-leasehold properties	50 years
Short leasehold properties	Lease term
Major improvements to properties	4 – 7 years
Equipment	3 – 7 years

Property, plant and equipment are reviewed annually for indication of impairment.

Gains and losses on disposal of assets are calculated with reference to the carrying value of the asset and the net disposal proceeds. Repairs and renewals are charged to the income statement when the expenditure is incurred.

## **Financial assets \***

The Group classifies its financial assets in the following categories:

### Loans and receivables

Loans and advances to customers are classified as loans and receivables and are carried at amortised cost using the effective interest method with all movements being recognised in the income and expenditure account.

### Financial assets at fair value through profit or loss

A financial asset is classified in this category if it is so designated by management on initial recognition and permitted by IAS 39. Derivatives are held at fair value through the income and expenditure account. The assets are initially measured at fair value, with transaction costs taken directly to the income statement. Subsequent measurement is at fair value, with changes recognised directly in the income and expenditure account.

## Available for sale

Available for sale assets are non-derivative financial assets intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates. They are initially measured at fair value with subsequent movements recognised directly in equity. On derecognition or where there is objective evidence that the asset is impaired, the cumulative gains or losses recognised in equity are removed from equity and recycled through the income and expenditure account.

## Held to maturity assets

Held to maturity financial assets are non-derivative financial assets with fixed or determinable payments that the Group has the ability and intention to hold to maturity. They are initially measured at cost including direct and incremental transaction costs. Subsequent measurement is at amortised cost using the effective interest method, with differences being recognised in the income and expenditure account.

## Asset impairment

### Tangible and intangible assets

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication of an impairment loss. For impaired assets, the recoverable amount of the asset is estimated in order to determine the extent of loss. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the Cash-Generating Unit (CGU) to which the asset belongs.

The recoverable amount is the greater of net selling price and value in use. For assessing value in use the estimated future cash flows are discounted to their present value using a pre-tax discount rate (reflecting the time value of money and the risks specific to the asset). If the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount.

Where the recoverable amount of an impaired asset increases, the carrying amount of the asset is increased to the revised estimate of its recoverable amount. This is capped at the carrying amount that would have been determined had no impairment loss been recognised.

Impairment losses are recognised as an expense immediately. A reversal of an impairment loss is recognised in the income and expenditure account immediately unless the relevant asset is carried at a revalued amount, when it is treated as a revaluation increase.

Intangible assets not yet in use and Goodwill are subject to annual impairment reviews even if no indication of impairment is noted.

### Loans and advances to customers \*

The Group assesses its financial assets or groups of financial assets for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event (or events) that has occurred after initial recognition and before the balance sheet date and has a reliably measurable impact on the estimated future cash flows of the financial assets or groups of financial assets.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the Group about the following loss events:

1. Significant financial difficulty of the issuer or obligor;
2. A breach of contract, such as a default or delinquency in interest or principal payments;
3. The lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
4. It becomes probable that the borrower will enter bankruptcy or other financial reorganisation;
5. The restrictions on an active market for that financial asset because of financial difficulties; or
6. Observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
  - Adverse changes in the payment status of borrowers in the portfolio;
  - National or local economic conditions that correlate with defaults on the assets in the portfolio.

If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an impairment allowance and the amount of the loss is recognised in the income and expenditure account. In future periods the unwind of the discount is recognised within interest income.

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

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the customer's credit rating), the previously recognised impairment loss is reversed by adjusting the impairment allowance. The amount of the reversal is recognised in the income and expenditure account.

Available for sale financial assets \*

The Group assesses whether there is objective evidence of impairment as the difference between the assets' carrying value and the present value of estimated cash flows. The rate used to discount the cash flows is the original effective rate on the asset. The amount of impairment loss is recognised in the income and expenditure account. This includes cumulative gains and losses previously recognised in reserves which are recycled from reserves to the income and expenditure account.

## **Leases**

The Group enters into finance leases for buildings and into operating leases for land and buildings and other assets. Where the land element of a property cannot be reliably separated from the building, the entire lease is treated as a finance lease. Finance lease assets are recorded at fair value with an equal liability recorded in other liabilities. Interest is allocated to the lease payments so as to record a constant rate of charge on the outstanding liability for each accounting period.

Operating lease payments are charged to the income statement on a straight line basis over the term of the lease.

The Group policy is to provide for the minimum future lease payments on buildings that it does not currently use. The provision is not released against future lease payments until the building can be sub-let or is brought back into use.

## **Foreign currency transactions**

Foreign currency is recorded at the rate of exchange on the transaction date. Foreign currency monetary assets and liabilities are re-translated at the closing rate with differences recognised in the income statement for that period.

## **Financial liabilities \***

Financial liabilities are recognised initially at fair value, being the issue proceeds received net of transaction costs incurred. Financial liabilities are subsequently stated at amortised cost. Differences between the amortised cost and the initial valuation are recognised in the income and expenditure account, over the period of the borrowing, using the effective interest rate.

### **Guaranteed Capital Equity Bond (GCEB)**

A financial liability is classified in this category by management on initial recognition. The liability is measured at fair value and changes are recognised directly in the income statement. This treatment is applied to prevent an accounting mismatch that would otherwise arise from measuring GCEB deposits and derivatives used to hedge these products on different bases.

## **Pensions**

The Group operates both a defined benefit and a defined contribution pension scheme.

A defined benefit plan defines the amount of benefit that an employee will receive on retirement. In a defined contribution plan the employer pays fixed contributions and is under no obligation to pay further contributions on retirement.

The defined benefit scheme liability recognised in the balance sheet is the present value of the obligations less the fair value of plan assets. Every third year the scheme obligations are valued by qualified external actuaries. The method used is the projected unit method, which is discounted using the current rate of return on a high quality sterling bond of comparable term to the related pension liability.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited each year to equity and shown in the statement of recognised income and expense.

The income and expenditure account includes the current service cost of providing pension benefits, the interest cost on the scheme's liabilities less expected return on the scheme's assets.

Obligations for contributions to the defined contribution scheme are recognised as an expense in the income and expenditure account as incurred.

## **Hedging policy \***

The Group undertakes transactions in derivative financial instruments to hedge its exposure to foreign exchange and interest rate risk arising from its activities. The Group does not hold or issue derivative financial instruments for trading purposes.

Derivative financial instruments are held at fair value in the balance sheet with changes in their fair value going through the income and expenditure account. Changes in the fair value of derivatives used to hedge particular risks can either be offset in the income and expenditure account or deferred to equity where the hedges qualify for hedge accounting.

There are three types of hedge accounting strategies that the Group undertakes and these are summarised below:

### **Fair value hedges**

Where a derivative financial instrument hedges the changes in fair value of a recognised asset or liability or an unrecognised firm commitment, any gain or loss on the hedging instrument is recognised in the income and expenditure account. To the extent that there is an effective hedge relationship, the associated hedged items (e.g. mortgage assets) are stated at fair value in respect of the hedged risk, with any gain or loss also recognised in the income and expenditure account. As a result the hedging instrument and hedged items offset each other and reduce profit volatility.

### **Cash flow hedges**

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. Any ineffective portion of the gain or loss on the hedging instrument is recognised immediately in the income and expenditure account. If the forecast transaction is no longer expected to occur, the cumulative unrealised gain or loss recognised in equity is also recognised immediately in the income and expenditure account.

### **Fair value hedge accounting for a portfolio hedge of interest rate risk**

As part of its risk management process the Group identifies a portfolio of items whose interest rate risk it wishes to hedge. The portfolio may comprise only assets, only liabilities or both assets and liabilities.

The Group analyses the portfolio into repricing time periods based on expected, rather than contractual, repricing dates by scheduling cash flows into the periods in which they are expected to occur. On the basis of this analysis, the Group decides the amount it wishes to hedge and designates as the hedged item an amount of assets or liabilities (but not a net amount) from the identified portfolio equal to the amount it wishes to designate as being hedged.

Periodically, the Group measures the change in fair value of the hedged item that is attributable to the hedged risk, on the basis of the expected repricing date. Provided that the hedge is determined to have been highly effective when assessed using the Group's documented method of assessing effectiveness, the Group recognises the change in fair value of the hedged item as a gain or loss in profit or loss and in one of two line items in the balance sheet (single separate line item for those repricing time periods in which the hedged item is an asset and similarly for when the hedged item is a liability in a single separate liability line item). The change in fair value is not allocated to individual assets or liabilities as under normal fair value hedge accounting.

The Group measures the change in fair value of the hedging instrument and recognises it as a gain or loss in profit or loss. The fair value of the hedging instrument is recognised as an asset or liability in the balance sheet. Any ineffectiveness will be recognised in profit or loss as the difference between the change in fair value of the hedged item and the change in fair value of the hedging instrument.

Any adjustment to the separate balance sheet item is amortised to profit or loss. Amortisation may begin as soon as an adjustment exists and no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged. The adjustment is amortised using a straight line method, which ensures the adjustment is amortised by the expiry of the relevant repricing period.

Derivatives that do not qualify for hedge accounting are held at fair value with changes in fair value recognised in the income and expenditure account.

#### Embedded derivatives

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risk of the host instrument, and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivative recognised in the income and expenditure account.

Depending on the classification of the host instrument, the host is then measured in accordance with the relevant IFRS standard.

#### **Britannia Membership Reward**

A liability for the Britannia Membership Reward is recognised when a payment has been approved by the Board. It is disclosed separately in the income and expenditure account in view of its size and importance with the liability included within other liabilities.

## UK GAAP to IFRS Reconciliations

### Income and Expenditure Account to 30 June 2004 : Reconciliation between UK GAAP and IFRS

	UK GAAP 6 months ended 30 June 2004	Securitisation vehicles adjustment Note 1	Effect of Transition to IFRS (excl. IAS 32 and IAS 39)	IFRS 6 months ended 30 June 2004
	£m	£m	£m	£m
Interest income	456.9	57.3	1.1 (Note 2)	515.3
Interest expense	(351.9)	(31.2)	-	(383.1)
<b>Net interest income</b>	<b>105.0</b>	<b>26.1</b>	<b>1.1</b>	<b>132.2</b>
Fees and commissions income	42.9	-	0.2 (Note 3)	43.1
Fees and commissions expense	(13.4)	(2.2)	-	(15.6)
<b>Net fees and commissions income</b>	<b>29.5</b>	<b>(2.2)</b>	<b>0.2</b>	<b>27.5</b>
Gains less losses from derivative financial instruments	-	-	(1.4) (Note 4)	(1.4)
Gains less losses from investment securities	-	-	0.3 (Note 5)	0.3
Other operating income	28.8	(23.9)	-	4.9
<b>Operating income</b>	<b>28.8</b>	<b>(23.9)</b>	<b>(1.1)</b>	<b>3.8</b>
Impairment losses on loans and advances	(1.9)	0.9	-	(1.0)
Administrative expenses	(93.8)	(0.9)	0.9 (Note 6)	(93.8)
<b>Operating profit</b>	<b>67.6</b>	<b>-</b>	<b>1.1</b>	<b>68.7</b>
Share of results of joint ventures	0.3	-	-	0.3
<b>Profit before tax and Britannia Membership Reward</b>	<b>67.9</b>	<b>-</b>	<b>1.1</b>	<b>69.0</b>
Britannia Membership Reward	-	-	-	-
<b>Profit before tax</b>	<b>67.9</b>	<b>-</b>	<b>1.1</b>	<b>69.0</b>
Tax	(20.8)	-	-	(20.8)
<b>Profit after tax</b>	<b>47.1</b>	<b>-</b>	<b>1.1</b>	<b>48.2</b>

#### Notes to the reconciliation:

1. Reversal of the UK GAAP (Financial Reporting Standard No. 5 : Reporting the substance of transactions) (FRS5) treatment for the net income of special purpose vehicles. Under IFRS the results are reported on a line by line basis as opposed to being reported within other operating income under UK GAAP.
2. Reclassification of derivative close out costs less profits on sale of investment securities.
3. Reversal of UK GAAP increase in insurance captive equalisation reserves. Under IFRS equalisation reserves are not permitted.
4. Reclassification of derivative close out costs.
5. Reclassification of profits on sales of investment securities.
6. Includes the write back of goodwill amortisation of £1.1 million (under IFRS goodwill is not amortised but is tested for impairment on an annual basis) less an increase in pension charge of £0.2 million.

## Income and Expenditure Account to 31 December 2004 : Reconciliation between UK GAAP and IFRS

	UK GAAP year ended 31 December 2004	Securitisation vehicles adjustment Note 1	Effect of Transition to IFRS (excl. IAS 32 and IAS 39)	IFRS year ended 31 December 2004
	£m	£m	£m	£m
Interest income	996.8	132.4	1.1 (Note 2)	1,130.3
Interest expense	(789.5)	(78.0)	-	(867.5)
<b>Net interest income</b>	<b>207.3</b>	<b>54.4</b>	<b>1.1</b>	<b>262.8</b>
Fees and commissions income	81.4	-	0.5 (Note 3)	81.9
Fees and commissions expense	(24.8)	(5.3)	-	(30.1)
<b>Net fees and commissions income</b>	<b>56.6</b>	<b>(5.3)</b>	<b>0.5</b>	<b>51.8</b>
Gains less losses from derivative financial instruments	-	-	(1.4) (Note 4)	(1.4)
Gains less losses from investment securities	-	-	0.3 (Note 5)	0.3
Other operating income	68.5	(44.8)	(3.4)	20.3
<b>Operating income</b>	<b>68.5</b>	<b>(44.8)</b>	<b>(4.5)</b>	<b>19.2</b>
Impairment losses on loans and advances	(7.3)	(3.9)	-	(11.2)
Administrative expenses	(185.7)	(0.4)	1.6 (Note 6)	(184.5)
<b>Operating profit</b>	<b>139.4</b>	<b>-</b>	<b>(1.3)</b>	<b>138.1</b>
Share of results of joint ventures	1.0	-	-	1.0
<b>Profit before tax and Britannia Membership Reward</b>	<b>140.4</b>	<b>-</b>	<b>(1.3)</b>	<b>139.1</b>
Britannia Membership Reward	(42.1)	-	-	(42.1)
<b>Profit before tax</b>	<b>98.3</b>	<b>-</b>	<b>(1.3)</b>	<b>97.0</b>
Tax	(26.9)	-	0.1	(26.8)
<b>Profit after tax</b>	<b>71.4</b>	<b>-</b>	<b>(1.2)</b>	<b>70.2</b>

### Notes to the reconciliation:

1. Reversal of the UK GAAP (FRS5) treatment for the income of special purpose vehicles. Under IFRS the results are reported on a line by line basis as opposed to being reported within other operating income under UK GAAP.
2. Reclassification of derivative close out costs less profits on sale of investment securities.
3. Reversal of UK GAAP increase in insurance captive equalisation reserves. Under IFRS equalisation reserves are not permitted.
4. Reclassification of derivative close out costs.
5. Reclassification of profits on sales of investment securities.
6. Includes the write back of goodwill amortisation of £2.2 million (under IFRS goodwill is not amortised but is tested for impairment on an annual basis) less an increase in pension charge of £0.6 million.

**Balance Sheet as at 31 December 2003 and 1 January 2004 : Reconciliation between UK GAAP and IFRS**

	Note	UK GAAP 31 December 2003	Balance sheet re- classification	Other effects of IFRS	IFRS 1 January 2004
		£m	£m	£m	£m
<b>ASSETS</b>					
<b>Liquid assets</b>					
Cash and balances with the Bank of England		35.4	-	-	35.4
Due from banks		1,018.8	-	-	1,018.8
Debt/investment securities		4,905.5	-	-	4,905.5
Loans and advances to customers	1	14,616.9	6.7	1,062.9	15,686.5
Investments in joint ventures		1.2	-	-	1.2
Intangible fixed assets	2	43.6	18.3	-	61.9
Goodwill	3	-	36.9	-	36.9
Property, plant and equipment	4	134.5	(61.7)	(1.5)	71.3
Other assets	5	172.9	1.6	(22.7)	151.8
<b>Total assets</b>		<b>20,928.8</b>	<b>1.8</b>	<b>1,038.7</b>	<b>21,969.3</b>
<b>LIABILITIES</b>					
Due to customers – shares		11,103.6	-	-	11,103.6
Deposits and debt securities	6	8,072.9	(7.1)	1,137.6	9,203.4
Other borrowed funds		357.6	-	-	357.6
Other liabilities	7	299.5	(71.1)	(5.5)	222.9
Retirement benefit obligations	8	-	-	51.1	51.1
<b>Total liabilities</b>		<b>19,833.6</b>	<b>(78.2)</b>	<b>1,183.2</b>	<b>20,938.6</b>
Share premium		3.1	-	-	3.1
Retained earnings	9	1,092.1	-	(64.5)	1,027.6
<b>Total equity and liabilities</b>		<b>20,928.8</b>	<b>(78.2)</b>	<b>1,118.7</b>	<b>21,969.3</b>

**Balance Sheet as at 30 June 2004 : Reconciliation between UK GAAP and IFRS**

	Note	UK 30 June 2004	Balance sheet re- classification	Other effects of IFRS	IFRS 30 June 2004
		£m	£m	£m	£m
<b>ASSETS</b>					
<b>Liquid assets</b>					
Cash and balances with the Bank of England		51.8	-	-	51.8
Due from banks		667.4	-	-	667.4
Debt/investment securities		5,302.5	-	-	5,302.5
Loans and advances to customers	1	15,441.0	10.5	1,368.8	16,820.3
Investments in joint ventures		0.5	-	-	0.5
Intangible fixed assets	2	44.5	17.4	-	61.9
Goodwill	3	-	36.9	-	36.9
Property, plant and equipment	4	130.8	(62.3)	(1.1)	67.4
Other assets	5	229.2	(1.3)	(24.0)	203.9
<b>Total assets</b>		<b>21,867.7</b>	<b>1.2</b>	<b>1,343.7</b>	<b>23,212.6</b>
<b>LIABILITIES</b>					
Due to customers – shares		11,152.6	-	-	11,152.6
Deposits and debt securities	6	8,678.9	8.4	1,455.7	10,143.0
Other borrowed funds		557.7	-	-	557.7
Other liabilities	7	336.2	(103.6)	(3.3)	229.3
Retirement benefit obligations	8	-	-	51.1	51.1
<b>Total liabilities</b>		<b>20,725.4</b>	<b>(95.2)</b>	<b>1,503.5</b>	<b>22,133.7</b>
Share premium		3.1	-	-	3.1
Retained earnings	9	1,139.2	-	(63.4)	1,075.8
<b>Total equity and liabilities</b>		<b>21,867.7</b>	<b>(95.2)</b>	<b>1,440.1</b>	<b>23,212.6</b>

**Balance Sheet as at 31 December 2004 : Reconciliation between UK GAAP and IFRS**

	Note	UK 31 December 2004	Balance sheet re- classification	Other effects of IFRS	IFRS 31 December 2004
		£m	£m	£m	£m
<b>ASSETS</b>					
<b>Liquid assets</b>					
Cash and balances with the Bank of England		30.8	-	-	30.8
Due from banks		1,153.0	-	-	1,153.0
Debt/investment securities		5,483.7	-	-	5,483.7
Loans and advances to customers	1	16,210.3	17.6	1,990.6	18,218.5
Investments in joint ventures		1.0	-	-	1.0
Intangible fixed assets	2	52.3	7.9	-	60.2
Goodwill	3	-	36.9	-	36.9
Property, plant and equipment	4	128.5	(60.2)	(1.1)	67.2
Other assets	5	238.2	1.5	(64.8)	174.9
<b>Total assets</b>		<b>23,297.8</b>	<b>3.7</b>	<b>1,924.7</b>	<b>25,226.2</b>
<b>LIABILITIES</b>					
Due to customers – shares		11,798.8	-	-	11,798.8
Deposits and debt securities	6	9,448.0	(5.2)	2,088.9	11,531.7
Other borrowed funds		557.7	-	-	557.7
Other liabilities	7	326.7	(93.1)	(15.9)	217.7
Retirement benefit obligations	8	-	-	20.4	20.4
<b>Total liabilities</b>		<b>22,131.2</b>	<b>(98.3)</b>	<b>2,093.4</b>	<b>24,126.3</b>
Share premium		3.1	-	-	3.1
Retained earnings	9	1,163.5	-	(66.7)	1,096.8
<b>Total equity and liabilities</b>		<b>23,297.8</b>	<b>(98.3)</b>	<b>2,026.7</b>	<b>25,226.2</b>

## Notes to the balance sheet reconciliations between UK GAAP and IFRS

1. Reclassification of mortgage book premiums (from intangible assets) and full consolidation of securitisation vehicles previously reported under linked presentation (FRS 5).
2. Reclassification of mortgage book premiums (note 1 above), software development costs previously reported as tangible fixed assets (note 4 below) and goodwill on an acquisition of subsidiary company (note 3 below).
3. Goodwill on acquisition of a subsidiary company previously disclosed as an intangible asset.
4. Reclassification of software costs to intangible assets and changes in treatment of leased assets.
5. Release of the prepayment to the pension fund, reclassification of fixed assets and minor adjustments to carrying values and recognition of deferred tax on retirement benefit obligations.
6. IFRS numbers include securitisation vehicles non-recourse funding previously reported under linked presentation (FRS 5).
7. Reclassification comprises excess securitisation vehicle non-recourse funding not reported as part of linked presentation under FRS 5. The other effect of IFRS is the release of captive insurance equalisation reserves not permitted under IFRS.
8. Recognition of retirement benefit obligations under IAS 19.
9. Comprises:
  - a) recognition of retirement benefit obligations including the write off of prepayments to the scheme and adjustments to associated deferred tax
  - b) differences in profit between IFRS and UK GAAP

Balance Sheet as at 31 December 2004 and 1 January 2005 : Reconciliation between UK GAAP and IFRS

	Note	IFRS 31 December 2004 (excl. IAS 32 and IAS 39)	Other effects of IAS 32 and IAS 39	IFRS 1 January 2005
		£m	£m	£m
<b>ASSETS</b>				
<b>Liquid assets</b>				
Cash and balances with the Bank of England		30.8	-	30.8
Due from banks		1,153.0	-	1,153.0
Debt/investment securities	1	5,483.7	3.1	5,486.8
Derivative financial instruments	2	-	155.1	155.1
Loans and advances to customers	3	18,218.5	135.4	18,353.9
Investments in joint ventures		1.0	-	1.0
Intangible fixed assets		60.2	-	60.2
Goodwill		36.9	-	36.9
Property, plant and equipment		67.2	-	67.2
Other assets	4	174.9	(138.9)	36.0
<b>Total assets</b>		<b>25,226.2</b>	<b>154.7</b>	<b>25,380.9</b>
<b>LIABILITIES</b>				
Due to customers – shares	5	11,797.8	15.7	11,813.5
Derivative financial instruments	2	-	270.2	270.2
Deposits and debt securities	6	11,532.7	(45.6)	11,487.1
Other borrowed funds	6	557.7	18.4	576.1
Other liabilities	7	217.7	(75.1)	142.6
Retirement benefit obligations		20.4	-	20.4
<b>Total liabilities</b>		<b>24,126.3</b>	<b>183.6</b>	<b>24,309.9</b>
Share premium	8	3.1	(3.1)	-
Retained earnings		1,096.8	(28.0)	1,068.8
Other reserves	9	-	2.2	2.2
<b>Total equity and liabilities</b>		<b>25,226.2</b>	<b>154.7</b>	<b>25,380.9</b>

## Notes to the balance sheet reconciliation at 1 January 2005:

1. Under IFRS, debt securities are recognised on the balance sheet at fair value as opposed to cost under UK GAAP. Movements in fair value are posted to other reserves and shown in the Statement of Recognised Income and Expense.
2. Derivative financial instruments used to hedge exchange and interest rate risk are recognised on the balance sheet at fair value. Under UK GAAP derivatives were not recognised on the balance sheet.
3. The IFRS adjustment comprises:
  - a) fair value hedging adjustment representing the movement in market value of those mortgages for which there is an effective hedging relationship with a derivative instrument
  - b) the difference between the IFRS amortised cost and the UK GAAP historical cost – amortised cost includes capitalised fees and costs of origination, plus accrued early repayment charges which are capitalised and recognised over the expected life of the mortgages
  - c) adjustment of loans and advances – impairment provisions
4. Under IFRS broker fees deferred are included within the amortised cost of the mortgages (see note 3 above). These were previously shown under other assets under UK GAAP. Under IFRS derivative accrued interest is included within the fair value amounts recorded under ‘derivative financial instruments’. Hence the UK GAAP accrued interest included within other assets has been removed.
5. The IFRS adjustment comprises:
  - a) the fair value of the hedged item arising from the application of fair value accounting to certain financial instruments
  - b) the reinstatement of derecognised liabilities
6. The IFRS adjustment comprises:
  - a) the fair value of the hedged item arising from the application of fair value hedge accounting to certain deposits and debt securities
  - b) reclassification of share premium (note 8 below)
7. Under IFRS derivative accrued interest is included within the fair value amounts recorded under ‘derivative financial instruments’. Hence the UK GAAP accrued interest included within other liabilities has been removed. Deferred income reserves held with the Group’s captive insurance company have been released and replaced with an amortised cost adjustment to the carrying value of mortgages (note 3 above).
8. Under IAS 39 the share premium is recorded as part of the issued debt.
9. Fair value adjustments on available for sale assets.

## Proforma Information

In order to aid comparability of the 2005 results with those of 2004, 2005 results have also been prepared on a proforma basis, which excludes the impact of International Accounting Standard 39 (Financial instruments : recognition and measurement).

### Pro-forma Group Income and Expenditure Account

	<b>6 months to 30 June 2005</b>	<b>6 months to 30 June 2004</b>	<b>12 months to 31 December 2004</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Interest income	650.3	515.3	1,130.3
Interest expense	(520.9)	(383.1)	(867.5)
<b>Net interest income</b>	<b>129.4</b>	<b>132.2</b>	<b>262.8</b>
Fees and commissions income	42.8	43.1	81.9
Fees and commissions expense	(15.5)	(15.6)	(30.1)
<b>Net fees and commissions income</b>	<b>27.3</b>	<b>27.5</b>	<b>51.8</b>
Gains less losses from derivative financial instruments	1.4	(1.4)	(1.4)
Gains less losses from investment securities	0.3	0.3	0.3
Other operating income	10.4	4.9	20.3
<b>Operating income</b>	<b>12.1</b>	<b>3.8</b>	<b>19.2</b>
Impairment losses on loans and advances	(1.2)	(1.0)	(11.2)
Administrative expenses	(96.2)	(93.8)	(184.5)
<b>Operating profit</b>	<b>71.4</b>	<b>68.7</b>	<b>138.1</b>
Share of results of joint ventures	1.1	0.3	1.0
<b>Profit before tax and Britannia Membership Reward</b>	<b>72.5</b>	<b>69.0</b>	<b>139.1</b>
Britannia Membership Reward	-	-	(42.1)
<b>Profit before tax</b>	<b>72.5</b>	<b>69.0</b>	<b>97.0</b>
Tax	(22.5)	(20.8)	(26.8)
<b>Profit after tax</b>	<b>50.0</b>	<b>48.2</b>	<b>70.2</b>

## Pro-forma Group Balance Sheet

	As at 30 June 2005	As at 30 June 2004	As at 31 December 2004
	£m	£m	£m
<b>ASSETS</b>			
<b>Liquid assets</b>			
Cash and balances with the Bank of England	28.2	51.8	30.8
Treasury bills and other eligible instruments	-	-	-
Due from banks	1,352.0	667.4	1,153.0
Debt/investment securities	5,070.5	5,302.5	5,483.7
Derivative financial instruments	-	-	-
Loans and advances to customers	18,865.0	16,820.3	18,218.5
Investments in joint ventures	1.0	0.5	1.0
Intangible fixed assets	54.8	61.9	60.2
Goodwill	36.9	36.9	36.9
Property, plant and equipment	60.4	67.4	67.2
Other assets	185.0	203.9	174.9
<b>Total assets</b>	<b>25,653.8</b>	<b>23,212.6</b>	<b>25,226.2</b>
<b>LIABILITIES</b>			
Due to customers – shares	12,379.6	11,152.6	11,798.8
Deposits and debt securities	11,321.2	10,143.0	11,531.7
Other borrowed funds/(subordinated liabilities)	557.8	557.7	557.7
Other liabilities	221.9	229.4	217.7
Retirement benefit obligations	20.4	51.1	20.4
<b>Total liabilities</b>	<b>24,500.9</b>	<b>22,133.8</b>	<b>24,126.3</b>
Share premium	3.1	3.1	3.1
Retained earnings	1,149.8	1,075.7	1,096.8
<b>Total equity and liabilities</b>	<b>25,653.8</b>	<b>23,212.6</b>	<b>25,226.2</b>