

# Britannia Building Society

Annual Report & Accounts 2004



**Britannia**

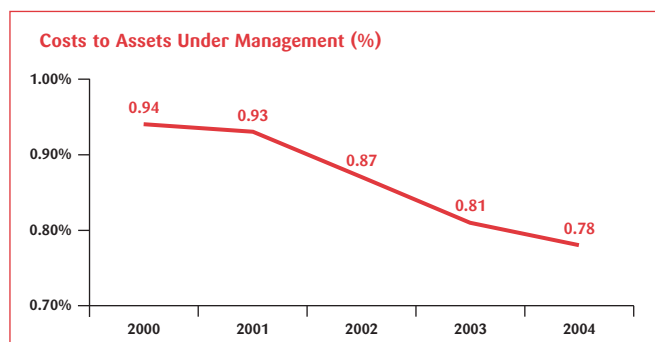
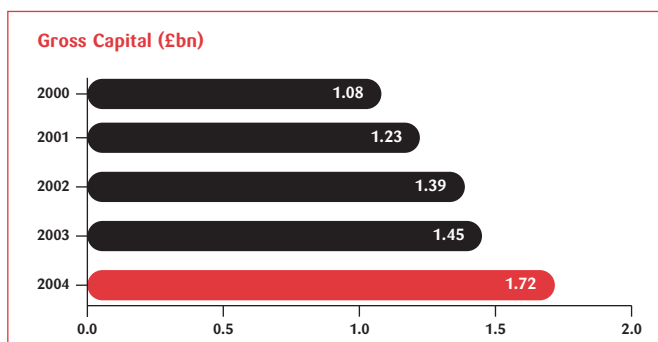
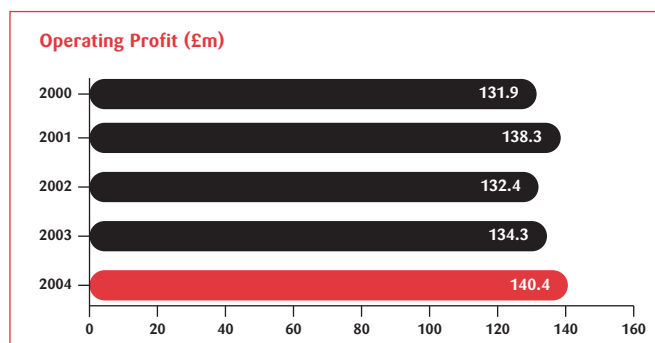
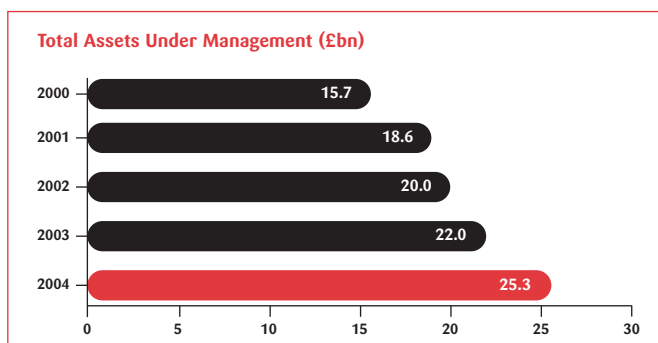
Where membership means a great deal

2004 has been a year of achievement for Britannia, winning over 30 awards and commendations, all for the benefit of our Members. Our mission remains to be known as Britain's best mutual – a great organisation to which our Members and our people are proud to belong.

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## Five Year Review



### Definitions:

**'Total assets under management'** represents the Group's total assets after adding back non-recourse finance.

**'Operating profit'** is measured before exceptional items and Britannia Membership Reward.

**'Gross capital'** represents the aggregate of general reserve, subordinated liabilities and subscribed capital.

**'Cost'** represents administrative expenses and depreciation, including costs allocated to securitisation vehicles and excludes amortisation of goodwill.

**'Assets under management'** represents the amount produced by halving the aggregate of the Group's total assets (after adding back non-recourse finance) at the beginning and end of the financial year.

## Chairman's Statement

2004 was a successful year for Britannia, as we continued on our mission to become known as Britain's best mutual. We achieved record results and the completion of a major new investment in systems which will enable us to boost customer service, against the backdrop of uncertainty in the housing market, record mortgage lending, intense competition for savings, and significant new regulatory changes to integrate into the business.



### Excellent products

We've been highly commended for many of our products. 'Your Mortgage' magazine voted Platform 'Best Adverse Credit Mortgage Lender'.

The first half of the year saw the housing market forging ahead, with house price inflation running at 20% per annum. The boom was fed, in part, by low interest rates and lenders competing keenly for business. Several Bank of England base rate hikes succeeded in dampening down the market to such a degree that many commentators in the latter part of the year expressed fears of a significant slowdown in the market.

The strength of the market in the first half of the year helped Britannia achieve record lending figures in 2004. Indeed, in June, the Membership business sold more mortgages than in any previous month in our history whilst at the same time maintaining our prudent approach to lending. Our intermediary lender, Platform, also went from strength to strength, posting record lending and profit figures.

Britannia continues to reap the benefits of its business model, running our Membership business separately from the Britannia Capital Investment Group (BCIG) subsidiaries. The Membership business, the traditional building society part of the Group, has an absolute focus on providing value and service to our savers and borrowers. BCIG is dedicated to delivering a return for our Members, shared through our unique Britannia Membership Reward. The strong performance of Platform and the other BCIG companies underlines the wisdom of investing in these businesses. The significant returns fund our Membership Reward, which has now shared more than £370 million with Members over the last nine years.

The savings and investment market remained highly competitive, with new market entrants offering high rates in the short-term on easy access internet and telephone accounts. This poses a challenge to traditional savings providers, who deliver the extra service by maintaining a retail network for customers who prefer to transact their business on a face to face basis. Britannia has responded positively with new accounts offering a choice of great rates and remains committed to the convenience of using our High Street branches.

We welcome the Financial Services Authority assuming responsibility for regulating mortgages - high standards in the market are good news for customers and, ultimately, good news to reputable businesses like Britannia. We will work with our regulators to ensure we meet the spirit, as well as the letter, of the law. However, I remain concerned about the weight of legislation and regulation that has been imposed on us in recent years, and question whether our customers benefit sufficiently from the ever increasing range of financial and business regulation, the cost of which will ultimately be borne by them.

Ensuring we comply with new regulations has required major investment in systems. This was incorporated into our unprecedented £60 million programme to replace all of our core systems. We have now completed this programme, and it is already having a real impact on the service we provide to our Members as part of our continuing drive to facilitate their borrowing and savings requirements.

Our success in delivering a project of such magnitude has been recognised with a number of awards, including the British Computer Society's flagship award for overall business achievement. IS services manager, Mark Jacot, also won the BCS IT Service Manager of the Year award.

Our challenge now is to use this investment to produce a real uplift in service to our Members. We know that we have not always met customers' expectations in recent months, particularly while the new systems were bedding in, and this will change. We are committed to providing a first class service to our Members and we believe that our new systems will enable us to achieve this aim.

This is my first annual report as Chairman of Britannia. My predecessor, Barrie Bernstein, retired after the 2004 Annual General Meeting having completed ten years service as a Director of Britannia, five as Chairman. Barrie was a major influence in preparing Britannia for the challenges of the modern financial services marketplace, and I would like to formally acknowledge his great contribution.

Following Barrie's retirement, we welcomed a new Non-executive Director on to the Board. Helen Keays is a former UK Board Director of Vodafone who has worked in senior marketing and retailing roles for Sears Retail, GE Capital and Thomson Holidays. With her customer management and marketing skills, Helen is a terrific addition to the team, reinforcing our commitment to always act in our Members' interests.

I would also like to take this opportunity to thank the Members' Council, some of whom retired during the year, for their invaluable contribution to the business. Attending four meetings a year and providing us with a Member's view on our strategy, products and services, gives us another insight into the views of the Membership.

I am grateful to all of my Board colleagues for their support and wise counsel over the last year - their knowledge and commitment to Britannia are key to maintaining our track record of delivering great results for our Members. I would also like to thank Group Chief Executive, Neville Richardson, his team and all of the 3,762 Britannia Group employees for their enthusiasm and dedication to our Members and customers. We are extremely fortunate in having such a highly motivated and talented team.

As we move into 2005, there is considerable uncertainty about whether the housing market, and therefore the mortgage market, faces a prolonged period of slow or no growth, or whether, as is far less likely, it will crash. We are well prepared for the future, and our record of innovation and prudent lending will stand us in good stead as we move forward with confidence.



**Ian Adam**  
Chairman  
8 February 2005



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#### Modern systems

We won the British Computer Society 'Project of the Year' award for our new £60m systems focused on providing excellent customer service.

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## Chief Executive's Report

2004 was a year of award-winning achievement for Britannia with record lending of £6.3 billion, taking us to assets under management of over £25 billion, record operating profit and £60 million worth of systems upgrades completed to facilitate significant customer service improvements going forward.



### First class service

We've won many awards for providing first class service. In 2004, 'Your Mortgage' magazine voted us 'Best Direct Mortgage Lender' for the second year running.

Our success was recognised with a raft of industry awards for lending, innovation and customer service during the year - underlining our mission to become known as Britain's best mutual. In the annual Your Mortgage magazine awards we were Best Direct Mortgage Lender and Best Adverse Credit Lender for the second year running.

Last year we set out clearly the values to which we subscribe as a business and as people working in that business. These values are putting customers first, being easy to do business with, being excellent at communications, taking personal responsibility and striving to be faster, cheaper, better in all that we do. We have started to make real progress towards ensuring that everyone in the business lives these values.

We have continued to invest heavily in the development, training and succession management of our people. This is supported by excellent communications to enable our people to understand the context in which we provide service to the Members of Britannia. These developments will be the key to our long-term sustained success.

In assessing our performance we set targets and review our performance against a balanced scorecard of measures, including financial, customer satisfaction and employee satisfaction. In this way we believe we are assessing all of the components which will lead to long-term sustained success.

### Financial Performance

Financial strength is one of the cornerstones of our strategy. Operating profit, before Britannia Membership Reward, was a record £140.4 million (2003 : £134.3 million). In 2004 we shared some £42 million (2003 : £42 million) with our Members through our unique Britannia Membership Reward. More than £370 million has now been returned to

Members in the nine years since the scheme was introduced. The average amount paid out in that time now totals £364, with potential maximum payouts totalling £4,500. In addition to Britannia's annual share of profits through its Membership Reward, we continued our policy of passing on to Members the benefits of operational efficiency and mutual status through competitive pricing. The total value of these benefits for Members was over £120 million.

Total lending for the year of £6.3 billion was up 28% on last year's total of £4.9 billion, with both the Membership business and Platform delivering record figures. The quality of lending remained high. Just 3.9% of Group residential lending was at more than 90% loan to value with the average mortgage loan to value at just 65%. Over 94% of lending was at multiples of 3.5 times salary or less, among the lowest in the industry and thus minimising the risk of bad debt. Group arrears over 12 months remained negligible, less than £1 million, and losses were insignificant. At 31 December 2004, Group arrears were nearly 5% lower than the industry average.

Britannia Capital Investment Group (BCIG) contributed £90.3 million of profits. Membership business profits were on target at £50.1 million - the planned reduction through mutual pricing of our products reflecting a commitment to Members to make only the profit necessary to remain financially strong.

Sales success meant an improvement in our cost to assets under management ratio to 0.78% (2003 : 0.81%). Overall expenses of £153.6 million (2003 : £143.1 million) reflected increased investment in the development of BCIG and the cost of meeting new rules designed to benefit customers, such as the new mortgage regulations.

Last year Britannia lent

# £6.3 billion

in mortgages to help people buy their homes - more than ever before.



Operating profit in 2004 was a record

# £140.4 million



## Chief Executive's Report contd.

### The Membership Business

These strong results show we are competing effectively in our target markets and delivering good performance for our Members in this low margin environment. We achieved record lending with a responsible approach and that means avoiding high risk lending which would increase the risk of problems in a market downturn.

Britannia's Membership business delivered its best-ever sales figures for mortgages, insurance and investment products. The Membership business sells direct to customers rather than paying fees to financial intermediaries.

The Membership business further developed its position as a leading provider of affinity accounts for Unison, Police Mutual and many major football clubs with increased savings balances and a 51% increase in mortgage sales to nearly £500 million.

Our new telephone-operated Direct Saver account, which was launched in August, attracted balances of over £500 million by the end of the year. Overall, highly competitive market pricing continued to make it difficult to attract new retail funds on a fair basis for the customer for the long-term and there was a modest increase in retail funds for the year up to £11.8 billion.

We regularly feature in the 'best-buy' tables and at the end of 2004 we reduced our headline standard variable mortgage rate by 0.4%, making it one of the lowest in the industry. Sales of life and investment products, general insurance and personal loans also grew during the year. This sales success was in part due to the completion of a new sales excellence training programme designed to ensure we meet customers' needs, and which was run throughout the contact centre and branch network.

Our new 50/50 Guaranteed Bond was an instant success, proving popular with our Members, and this contributed to a 62% increase in investment sales during the year.

In October we announced we had chosen AXA Sun Life to provide life, pension, protection and investment sales alongside Britannic Asset Management investments. This arrangement started in January 2005, when new FSA rules on the sale of regulated products came into effect, and means Britannia Members can buy AXA mortgage and life protection, investments, pensions, annuities, unit trusts and ISAs, in Britannia branches and via a dedicated telesales team.

We regularly ask our Members and customers for their opinions on our products and services. In 2004 they told us that we were maintaining our standards but this did not meet with our own ambition of improvement and it will be an area of focus for us in 2005.

The completion of our £60 million core systems replacement programme is already making us easier to do business with. For example, we now offer a 'one-touch' service - dealing with enquiries at first point of contact - to many more of our Members. As mentioned in the Chairman's Statement, success in delivering this programme was recognised with a number of awards. Britannia's website and customer magazine also won awards during the year.

### Britannia Capital Investment Group

BCIG had another highly successful year. Investing in these profitable companies enables Britannia to pay our unique Membership Reward over and above the benefits which our Members receive through our mutual pricing.



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### Quality publications

Our member magazine (M) was voted 'Customer Magazine of the Year'.

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### INVESTOR IN PEOPLE

#### Great place to work

Investors in People have again given us a glowing report, plus we've achieved a lot of recognition for our programme of activities to support diversity.

In the first full year of operation after we merged our Platform and Verso subsidiaries to offer a one-stop service to mortgage intermediaries, offering a full range of conforming and non-conforming mortgages, lending increased by 60% to £2.6 billion – ahead of expectations.

Western Mortgage Services maintained its excellent record of providing high quality, low cost servicing for Platform's loans, as well as growing mortgage processing business from third parties.

Britannia Commercial Lending loaned over £500 million, similar to last year, concentrating on lending where tenants are strong, well established organisations and Housing Associations, which generally provide accommodation to those unable to get on the ever more expensive housing ladder.

Britannia Treasury Services completed two securitisations, raising a total £1.7 billion of funding together with a number of acquisitions of mortgage portfolios.

The opening of our third Britannia International branch on the Isle of Man, at Port Erin, led to considerable new business, and we are confident that we can continue to build on our market-leading position with Manx residents. The continuous review of our product range, including a number of 'best-buy' bonds during the year, led to a significant increase in balances from expatriate customers.

#### Our People

From a solid base, we have invested significantly to improve service to those who matter most – our Members and customers. We can only achieve this by having the right, well trained and developed people in the right roles and by everyone understanding the context in which Britannia has to compete as a modern mutual to deliver benefits to those customers and our Members. A key development

in this area has been the introduction of values based recruitment. Everyone recruited or appointed to the organisation is assessed on their fit to our values – it is the first thing we look at.

Our commitment to making Britannia a great place to work, grow and develop is reflected in best ever results from our Viewpoint employee attitude survey. Excellent levels of people satisfaction resulting from our people understanding the context of the many changes which we are actioning put us among the best in British industry and ahead of many competitors in financial services.

#### Future Strategy

Britannia's unique business model meant a great deal for Members in 2004. It was a year of real achievement across the Britannia Group. We are putting in place the direction, values, systems, processes and the people to continue taking Britannia forward.

We will pursue our policy of offering long-term, sustainable value to our Members through competitively priced mortgages and great service. We will continue to make only the profit we need to fund future growth in our Membership business, whilst maximising returns from the BCIG companies.

We will enhance the value of the investments we have made in systems to improve customer service. In the coming years we will make the customer experience at Britannia one of which our Members and staff are proud. We will continue to look for innovative ways to reward Members' loyalty, ensuring they never come second to new customers. And we will further expand our BCIG activities to generate greater returns for our Members.

**Neville Richardson**

Group Chief Executive  
8 February 2005

Cost to assets under management ratio is a good way of measuring efficiency. This year the ratio fell to

**0.78%**

the lowest in recent years, meaning we're becoming more efficient.



## Board of Directors

The Board comprises eleven Directors, three of whom are full-time Executive Directors. The other Directors are Non-executives; they are all independent Directors as defined in the Combined Code of Best Practice on Corporate Governance and they do not receive any material additional remuneration from the Society for services provided.



### **1 Ian Adam, CA**

#### **Chairman**

Ian Adam, 61, a Chartered Accountant, joined the Board in 1998, becoming Chairman in April 2004. He is Chairman of the Nominations Committee and is a member of the Remuneration Committee. He is a member of the Scottish Higher Education Funding Council where he chairs the Audit Committee. He was formerly Finance Director at Christian Salvesen PLC and Deputy Chairman of Fishers Holdings Limited.

### **2 Neville Richardson, BA, FCA**

Neville Richardson, 47, is the Group Chief Executive. He joined the Board in 1998 as Group Finance Director after 21 years with PricewaterhouseCoopers, where he was a partner in the financial services practice. He was appointed to his current position in November 2002. He is a member of the Assets and Liabilities Committee, the Nominations Committee and the Group Credit Committee and is also a Trustee of the Britannia Building Society Foundation. Neville is a member of the BSA Council and Court of Lancaster University. He is also a Director of Mutuo (Communicate Mutuality Limited).

### **3 Bill Gordon, FCIB**

#### **Deputy Chairman and Senior Independent Director**

Bill Gordon, 65, joined the Board as a Non-executive Director in September 1999, becoming Deputy Chairman in April 2004. He is a member of the Assets and Liabilities Committee, the Audit Committee and the Nominations Committee and is a Director of Britannia Treasury Services Limited. He is the former Chief Executive of UK Banking Services at Barclays and he was Chairman of Barclays Pension Fund Trustees Limited until 31 December 2004.

### **4 Gerald Gregory, BA, MA**

Gerald Gregory, 49, joined the Board as Sales and Marketing Director in September 1999 and is now Managing Director of the Britannia Capital Investment Group. He is a Director of a number of subsidiary companies including Platform Home Loans Limited and Britannia Treasury Services Limited and he is a member of the Society's Assets and Liabilities Committee and the Group Credit Committee. He is also a Trustee of the Britannia Building Society Foundation. Gerald joined the Society in 1989 from Girobank PLC. He was formerly Treasurer, Head of Lending and then Director of Mutuality and Marketing at the Society.

### **5 Francis Gugen, FCA**

Francis Gugen, 55, joined the Board as a Non-executive Director in December 2003. He is also a member of the Audit Committee. He is a Chartered Accountant with wide-ranging interests in the energy and utility sectors. He is also a member of several CBI committees and was formerly CEO at Amerada Hess Corporation in Europe and before that Finance Director at Amerada Hess Corporation (UK). Before joining the oil industry, Francis worked as an accountant for 12 years, latterly with Arthur Andersen. He is Chairman of the Audit Committee of Petroleum-Geo Services ASA.



**6 Chris Jones, LLB**

Chris Jones, 52, joined the Board as a Non-executive Director in May 2003. He is also Chairman of the Remuneration Committee and a member of the Group Credit Committee. He is a solicitor and specialised in insolvency and banking law before becoming managing partner of Hammonds, a leading international law firm. He is a Non-executive Director of debt recovery specialists, Agenda Management Services Limited, trading as Drydens, a member of the Law Society and the Institute of Credit Management.

**7 Helen Keays, BA**

Helen Keays, 40, joined the Board as a Non-executive Director in October 2004. She is a management consultant with particular interest in marketing and customer management. She is a Non-executive Director of Chrysalis and formerly a Director of Vodafone UK Limited and Sears PLC. She is also a business mentor for the Prince's Trust.

**8 Phil Lee, BSc, CIPFA, CA**

Phil Lee, 49, joined the Board in September 2002 as Group Finance Director, with responsibility for Finance, Change Management, Group Risk Management and Information Systems. He is Chairman of the Assets and Liabilities Committee, a member of the Group Credit Committee, a Trustee of the Society's Pension Scheme and a Director of a number of subsidiary companies. Formerly he was Finance Director at West Bromwich Building Society and previously he has held senior roles at Bristol & West, Somerfield and Ernst & Young.

**9 Bridget Rosewell, MA, MPhil**

Professor Bridget Rosewell, 53, joined the Board as a Non-executive Director in July 1999. She also chairs the Audit Committee. She is an economist and is a founding Director and Executive Chairman of the economic and market analysis firm Volterra Consulting Limited. Bridget is consultant Chief Economist to the Greater London Authority and a visiting professor at City University Business School. She is also a Non-executive Director at the Department for Work and Pensions and is Chairman of its Audit Committee.

**10 Tom Sawyer**

Tom Sawyer, 61, Member of the House of Lords, joined the Board as a Non-executive Director in July 1999. He is a member of the Remuneration Committee, Chairman of the Trustees of the Society's Pension Scheme and Chairman of the Members' Council. He is former Chairman of Notting Hill Housing Trust and is a consultant to Touchstone Training. He is a visiting professor at Cranfield Business School and he chairs the Union Income Benefit Advisory Board. Tom was General Secretary of the Labour Party for four years, having previously been Deputy General Secretary of Unison.

**11 Elizabeth Walmsley, BSc, PhD, MBA**

Dr Elizabeth Walmsley, 52, joined the Board as a Non-executive Director in 2000. She is a Trustee of the Britannia Building Society Foundation and a Trustee of the Society's Pension Scheme. She is a Director of the Change Partnership, a subsidiary of Whitehead Mann, and has wide experience in the management of modern, complex businesses. She also chairs White Rose Technology Limited and is a former member of the Council of Sheffield University.

The Britannia Membership Reward is our annual share of profits rewarding members for their loyalty.

# £42 million

was shared this year among 800,000 people.



## Corporate Governance Report

The Board operates to promote the success of the Society by directing and supervising its affairs. The Board meets routinely eleven times a year and provides leadership of the Society within a framework of prudent and effective controls, which enable risk to be assessed and managed.

The Board sets the Society's strategic aims, ensures that the necessary financial, human and other resources are in place for the Society to meet its objectives and reviews management performance.

The Society has complied throughout the year with the Interim Prudential Sourcebook for Building Societies and the Integrated Prudential Sourcebook as applicable, implemented by the Financial Services Authority, which includes guidance for boards and management. The Society complies with all relevant aspects of the Combined Code of Best Practice on Corporate Governance, both main and supporting principles.

The Board has assessed all its Non-executive Directors as being independent in accordance with the criteria set out in the Code.

Where Executive Directors hold directorships in external companies, they do not personally receive any remuneration in respect of their appointments.

The Directors maintain a schedule of reserved matters, which are solely for the decision of the Board, for example the maintenance of the corporate plan and the approval of annual budgets and Treasury policy. Other matters are delegated to the Group Executive Board and senior management as appropriate, for example product and services development, staffing and marketing.

All Directors receive a regular supply of information about the Society so that they are equipped to play as full a part as possible in Board meetings. Papers for Board and Committee meetings are typically distributed one week prior to the relevant meeting. All Board members have access to the Society Secretary for any further information they require. Independent professional advice is available to Directors in appropriate circumstances, at the Society's expense and the Society has arranged appropriate insurance cover in respect of legal action against the Directors and Officers.

The Directors address necessary professional development through various means, for example, attendance at conferences and seminars, external briefing papers and specialist study. The Society also arranges presentations and supporting documentation on current topics, such as new legislation or regulation. In addition, the Secretary ensures that all Board members receive appropriate training as necessary.

Non-executive Directors are encouraged to visit the Society's branches and operations and to speak to Members and employees. All Directors are required to submit themselves for re-election every three years and new Directors are appointed to the Board on the recommendation of the Nominations Committee.

The Board undertakes an annual evaluation of the performance of the Board, its committees and individual Directors. This is done by means of a detailed assessment questionnaire, appraising a range of factors which contribute to an effective Board. The results are shared and discussed with all the Directors, with a view to continuous improvement.

Annually, through the Audit Committee, the Board conducts a rigorous assessment of the Group's systems of internal control, which are considered to remain satisfactory. The review encompasses all material controls, including financial, operational and compliance controls and risk management systems.

Several sub-committees act for the Board to ensure that Non-executive Directors have a direct role in Britannia's corporate governance.

The membership of the Assets and Liabilities Committee includes one Non-executive Director, Bill Gordon. The Committee reviews and recommends to the Board changes to the Society's wholesale funding, liquidity and balance sheet risk management policies and oversees compliance with these policies.

The Nominations Committee consisting of the Chairman, Deputy Chairman and Chief Executive, meets at least three times each year. It reviews and recommends on the composition of the Board and its sub-committees, including succession planning and new Board appointments. In recommending new Board appointments, the Nominations Committee has adopted the use of open advertisements and external search consultants. All potential candidates receive a thorough appraisal.

The Remuneration Committee comprises three Non-executive Directors. In line with best practice, the Board has prepared an Annual Report on Directors' Remuneration and the role of the Remuneration Committee; this report is on pages 16 to 17.

## Corporate Governance Report contd.

The Audit Committee comprises three Non-executive Directors. Bridget Rosewell chairs the Committee. The Committee oversees the Group's internal controls, accounting policies and financial reports, and monitors compliance with legal and regulatory requirements. It is also responsible for liaison with the Group's external auditors. The Committee meets at least four times a year. The Chairman and other members of the Committee maintain regular contact with key personnel involved with audit matters, including the Head of Group Risk, the Group Compliance Officer, the Group Money Laundering Reporting Officer, the Head of Group Finance and the internal auditors. The Group's external auditors undertake non-audit services, including the provision of advice on taxation matters. A policy has been introduced whereby audit and non-audit fees of external auditors are approved by the Audit Committee and auditor objectivity and independence is safeguarded by competitive tendering and regular appraisal.

The number of Board and Committee meetings attended by each Director during the year is shown in the table below:

	Board (11 in period)	Audit (4 in period)	Assets and Liabilities (11 in period)	Remuneration (4 in period)	Nominations (5 in period)
Ian Adam	11 <sup>c</sup>	2 <sup>1</sup>		4	5 <sup>c</sup>
Barrie Bernstein <sup>2</sup>	4			1	2
Bill Gordon	11	2 <sup>3</sup>	10		2 <sup>4</sup>
Gerald Gregory	11		9		
Francis Gugen	11	4			
Chris Jones	10			4 <sup>c</sup>	
Helen Keays <sup>5</sup>	2				
Phil Lee	11		11 <sup>c</sup>		
Neville Richardson	11		10		5
Bridget Rosewell	11	4 <sup>c</sup>			
Tom Sawyer	11			3	
Elizabeth Walmsley	11				

<sup>1</sup> Member until 28 April 2004

<sup>2</sup> Retired 2 April 2004

<sup>3</sup> Member from 28 April 2004

<sup>4</sup> Member from 2 April 2004

<sup>5</sup> Appointed 1 October 2004

<sup>c</sup> Chairperson

Copies of the Terms of Reference of the Audit, Nominations, Remuneration and Assets and Liabilities Committees are available on request. Copies are also available on the Society's website, [www.britannia.co.uk](http://www.britannia.co.uk).

Tom Sawyer is Chairman of the Pension Trustees, responsible for the Britannia Pension Schemes. Phil Lee and Elizabeth Walmsley are also Trustees. The Trustees meet routinely four times a year.

Certain Non-executive Directors occupy unpaid positions on the Boards of Britannia subsidiary companies as detailed on pages 59 to 63.



**Paul Mills**

Secretary

For the Board of Directors

8 February 2005

In total, we gave

# £500,000

last year, mostly through the Britannia Building Society Foundation, supporting charities working in the areas of homelessness, community safety and education.



#### Community support

Our 'Numbers Partners' initiative has received a 'Big Tick' award from 'Business in the Community'.



**Being owned by our Members, at Britannia we take our role in the community very seriously. We strive to be a good neighbour, supporting a wide range of charities, voluntary groups, schools and other good causes in our home communities.**

Britannia supports the Staffordshire Money Advice service provided through local Citizens Advice offices. The service offers counselling and guidance for people with budgeting or debt problems.

Visually impaired children across the UK will be able to enjoy a new set of Braille books, thanks to a £12,000 donation to the National Library for the Blind from the Britannia Building Society Foundation.

Britannia has helped three charities working in Sheffield and Staffordshire that provide second-hand furniture to families and other people on low incomes who are trying to set up their own homes.

Local children were invited to compose their own rap songs on the issue of racism as part of a Britannia - sponsored competition with Stoke City FC as part of the Kick Racism out of Football campaign.

## Annual Report on Directors' Remuneration

To succeed in our mission to be known as Britain's best mutual and to manage Members' assets of more than £25 billion, our Board must comprise high calibre Directors with extensive, relevant experience and expertise. This report explains how the Board decides the appropriate levels of pay and benefits to attract, retain and reward our Directors.

### Purpose and Composition of the Remuneration Committee

The Remuneration Committee consists of three Non-executive Directors. It agrees the terms and conditions of employment of all Directors and other senior managers. Committee members have no direct financial interest in decisions they make and do not take part in discussions regarding their own remuneration. The Committee normally meets at least four times a year, with special meetings when needed.

### During 2004 the Committee comprised the following

#### Non-executive Directors:

Ian Adam  
Barrie Bernstein Retired April 2004  
Chris Jones Chairman from April 2004  
Tom Sawyer

The Society's Secretary, Paul Mills, attends as Secretary to the Committee.

Meetings of the Committee are also attended, as necessary, by Neville Richardson (Group Chief Executive), Phil Lee (Group Finance Director) and other senior management as appropriate, including representation from Organisational Development.

During 2004 the Committee met four times to consider the remuneration of Directors and senior managers, the achievement of bonusable objectives in 2003, bonusable objectives for 2004 and the 2005 executive bonus scheme.

### Determination of Remuneration

The Committee bases its decisions on remuneration of the Executive Directors on three principal factors - level of responsibility, external market competitiveness and individual performance in the role. All decisions on Directors' remuneration are subject to rigorous challenge before agreement by the Remuneration Committee.

To help decide the right remuneration for a particular role, the Committee compares the responsibilities of Britannia's Directors and their salaries and benefits against those of comparable positions elsewhere. In addition, assessments of individual performance are undertaken each year. The Group Chief Executive conducts annual performance appraisals for all of the Executive Directors and is in turn appraised by the Chairman. All Non-executive Directors receive an annual appraisal conducted by the Chairman, who receives an appraisal conducted by the Deputy Chairman.

The Committee continues to take guidance from expert external advisors, including Watson Wyatt LLP.

### Base Pay

Britannia salaries are, on average, in line with the median salaries paid for comparable positions among similar financial services organisations. However, when deciding the appropriate level of base pay the performance of the Executive is also taken into account.

### Bonus Scheme

The design of all bonus schemes for Executive Directors are subject to Remuneration Committee review and agreement. Performance against objectives and the attendant bonus payments are also subject to independent external review.

To ensure alignment of Executive Director reward with the corporate balanced scorecard, all performance measures and targets that apply to the bonus are reviewed each year to ensure they support the key business drivers for the Group. All schemes are constructed around the achievement of target levels of performance, based on the Group's stretching budget figures. A threshold level of performance is set, below which no payment will be made. A maximum level is also set at which bonuses are capped.

Details of the 2004 bonus scheme for the Executive Directors were provided in the Report on Directors' Remuneration in 2003 and received strong support from Members. Under this scheme bonuses were aligned with the corporate strategy through links to Group profit, cost to income ratio, cost to assets under management ratio, customer satisfaction, employee satisfaction and the achievement of personal objectives.

In 2004 the on-target bonus continued to be 35% of salary, with a maximum of 70% available for exceptional performance in the measures other than Group profit. Achievement of objectives was subject to expert independent external scrutiny. Group profits in excess of target produced no additional payment as our goal is to return value to Members, not to maximise profits. The actual bonus reflects the strong performance of the Group during the year. Further details are shown in Note 7 of the Accounts. To ensure Executive focus remains on strategic objectives, and to aid retention, 3/7ths of the payment has been deferred for two years. Executive Directors will receive deferred amounts only if they remain employed by the Society at the end of the deferral period.

To recognise the importance of the contribution of the Britannia Capital Investment Group (BCIG) to overall Group results, an additional bonus of up to 30% relating to stretching financial and regulatory targets for BCIG was available to Gerald Gregory. The actual additional bonus reflects the very strong performance of BCIG during 2004. Further details are shown in Note 7 of the Accounts.

The payment for 2004 reflects the Group's strong performance against target. The Remuneration Committee approved the design of the Directors' bonus for the year ended 31 December 2005, which will be exactly the same as the 2004 scheme.

The Committee has set the target performance levels for all measures on which the 2005 bonuses will be paid, based on the Group's forecasts for 2005.

As a mutual the Society does not have share capital and therefore there is no share based remuneration available for Directors or employees.

### Benefits

Although it is more difficult to compare the monetary value of benefits between organisations than levels of base pay, the Group aims to benchmark its benefits and position them at the median level amongst a peer group of financial services organisations.

#### The main benefits provided for Executive Directors are:

- car of the Director's choice up to the monthly lease cost of a stipulated benchmark model;
- private mileage fuel;
- a Group Healthcare Scheme providing private medical insurance cover for the Directors and their families. (Non-executive Directors may obtain cover under the Scheme but must pay the annual subscription);
- a concessionary mortgage up to £35,000 borrowed at 3.8%;
- membership (after two years of employment) of an Income Protection Scheme which provides income in the event of being unable to continue working due to disability or prolonged illness; and
- membership of the contributory Britannia Building Society Pension and Life Assurance Scheme which includes an accrual rate of up to 1/30th of final pensionable salary per year of service to a maximum of 2/3rds of the average of the last three years' pensionable salary. A supplementary scheme provides pension benefits, where relevant, in respect of basic salary in excess of the Earnings Cap.

### Period of Notice

All Executive Director appointments have a rolling one-year contract of employment.

The Remuneration Committee has agreed that Executive Directors are entitled to receive a notice payment should their contract be terminated, plus an additional payment covering any amount due in relation to other contractual benefits.

### Analysis of Directors' Remuneration for the year ended 31 December 2004

The remuneration of each Director is analysed in Note 7 of the Annual Report and Accounts. Non-executive Directors are remunerated solely by fees and do not receive any salary, pension, benefits or the benefit of any bonus schemes. Pension information in respect of each Director is shown in Note 7.

### Request for Feedback from Members

The Board is committed to best practice in corporate governance. This includes publishing information on Directors' remuneration.

This report, together with the details in the Notes to the Accounts, has been prepared with the aim of giving Members an insight into how decisions around Directors' remuneration are taken and to disclose the remuneration of the Directors. We have again put forward a resolution at the Annual General Meeting inviting Members to vote on the 2004 Report on Directors' Remuneration. The vote is advisory, and the Board will consider what action is required.

The Committee would welcome any comments or suggestions as to whether the information contained in this report has been helpful and what additional information could be provided in future. These should be addressed to the Society's Secretary, Paul Mills.



#### Chris Jones

Chairman of the Remuneration Committee  
8 February 2005

## Directors' Report

The Directors are pleased to present the Annual Report and the Audited Accounts for the year ended 31 December 2004.

### Business Objectives and Activities

Britannia's mission is to be known as Britain's best mutual, a great organisation to which our Members and staff are proud to belong.

The reports of the Chairman and Chief Executive review the Group's existing business and prospects on pages 2 to 8 of this report. No activities of a different nature to those previously engaged in were carried out during 2004.

### Directors

The Directors of the Society during the year and at 31 December 2004 were:

Ian Adam \*  
Barrie Bernstein \* (retired 2 April 2004)  
Bill Gordon \*  
Gerald Gregory  
Francis Gugen \*  
Chris Jones \*  
Helen Keays \* (appointed 1 October 2004)  
Phil Lee  
Neville Richardson  
Bridget Rosewell \*  
Tom Sawyer \*  
Elizabeth Walmsley \*

\* Non-executive Director

Under the Building Societies Act 1986 and the Society's rules, Bill Gordon, Gerald Gregory and Phil Lee are due to retire by rotation at the Annual General Meeting in 2005. They are eligible and will stand for re-election. Helen Keays has been appointed since last year's Annual General Meeting and will therefore stand for election.

None of the Directors has any interest in the share capital of the Society's connected undertakings.

### Profit and Capital

The Group's operating profit, before Britannia Membership Reward of £42.1 million (2003 : £42.0 million), was ahead of target at £140.4 million (2003 : £134.3 million) and profit after tax amounted to £71.4 million (2003 : £65.3 million), which was added to reserves. At the end of the year, the gross capital ratio was 8.1% (2003 : 7.6%) and the free capital ratio was 7.5% (2003 : 6.9%) (see Annual Business Statement on page 58 for an explanation of these ratios).

### Fixed Assets

As part of its commitment to improve service to its customers, the Group continues to invest in its infrastructure. A key element of this is our £60 million core systems replacement programme which was completed this year.

The Directors consider the estimated market value of the Group's interest in land and buildings to be not less than its net book value at 31 December 2004.

### Liquid Assets

Liquid assets comprising cash, bank balances and other authorised investments totalled £6.7 billion (2003 : £6.0 billion), representing 31% (2003 : 31%) of the assets of Members. This includes asset backed and mortgage backed securities which are held for investment purposes. We believe a liquidity holding of this size ensures sufficient short-term funds are available. Our financial objective is to maximise returns from liquid asset investments while minimising the credit risk by placing funds with highly rated institutions spread widely across financial sectors and countries.

### Arrears

As a consequence of our proactive approach to arrears management, which includes co-operation with and support for independent debt counselling services, the number of accounts 12 months or more in arrears at 31 December 2004 was 86 (2003 : 126). The balances on these accounts totalled £4.2 million (2003 : £8.0 million).

The total arrears outstanding on these accounts was £0.6 million (2003 : £1.1 million), which represents approximately 0.01% (2003 : 0.01%) of total Group mortgage accounts and 0.01% (2003 : 0.01%) of total Society mortgage accounts. The Group remains committed to the effective and fair management of lending and arrears. Through careful control in this area we were able to restrict the charge for bad and doubtful debts to £7.3 million (2003 : £14.2 million).

### **Control of Derivatives**

A derivative is an off balance sheet treasury instrument that allows the Group to change the characteristics of a product, such as a fixed rate mortgage into a variable rate. The Group pays or receives the difference between the two rates to the derivative counterparty.

The off balance sheet nature of these instruments means that the nominal value of these transactions is not included in the balance sheet, however, the payments/receipts appear in the interest margin.

The Group has a formal structure for managing risk, including established risk limits, reporting lines, mandates and other controls. The Board reviews this structure regularly in line with new requirements from regulators. The Assets and Liabilities Committee monitors compliance and performance against the structure, and manages and controls the balance sheet exposures of the Group.

The Board has authorised the use of derivatives under Section 9A of the Building Societies Act 1986. The Financial Services Authority agrees an overall limit on the derivatives outstanding at any one time. The Board sets all other limits over the use of derivative products on the recommendation of the Assets and Liabilities Committee.

The Group has no substantial exposure to foreign exchange or net exposure to interest rate variations, as a result of the procedures described above.

### **Creditor Payment Policy**

The Society discharges a supplier's invoice for the complete provision of goods and services (unless there is an express provision for stage payments) when in full conformity with the terms and conditions of the purchase within agreed payment terms. The Group's policy is to agree the terms of payment at the start of trading with the supplier, ensure that suppliers are aware of the terms of payment and pay in accordance with its contractual and other legal obligations.

Creditor days at 31 December 2004 were 10 days (2003 : 10 days).

### **Going Concern**

The Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future and that it is, therefore, appropriate to adopt the going concern basis in preparing the Annual Report and Accounts.

### **Impact of the Euro**

The Board continues to consider the requirements, opportunities and threats that the United Kingdom's potential entry into the European Monetary System (EMS) could create for the Group.

### **International Accounting Standards (IAS)**

In common with other European Union listed institutions, Britannia will be required to prepare its Annual Accounts for 2005 under IAS.

The introduction of IAS will have implications for all businesses. The Society recognised the need to tackle this issue early and has been working to identify all implications and make necessary changes to processes and systems. The Group, which has a project overseen by the Audit Committee of the Board, has committed the necessary level of resources and funding to ensure that it will be compliant from 2005.

The impact of these standards (excluding IAS 39 'Financial Instruments : Recognition and Measurement') will not have a significant effect on the Group results. The changes required by IAS 39 will inevitably introduce volatility into the financial statements. Whilst we will ensure the volatility is carefully managed, we will continue to employ effective economic hedges to minimise risk.

In the third quarter of 2005, when we announce our interim results, we will present the impact of IAS on these results, together with a summary of our 2004 financial accounts on an IAS basis.

### **Post Balance Sheet Events**

The Directors consider that there has been no event since the year-end that has had a significant effect on the Society's position or that of any of its connected undertakings.

### **Donations**

During the year, the Society and its subsidiaries made donations to charities and other deserving causes totalling £500,000. Some £300,000 of this total was allocated through the Britannia Building Society Foundation. No contributions were made for political purposes.

### **Auditors' Independence**

The Society's Audit Committee, chaired by Non-executive Director Bridget Rosewell, reviews and monitors the auditors' independence. The Committee ensures that any work awarded to the auditors does not affect their objectivity and independence.

## Directors' Report contd.

### Statement of Directors' Responsibilities

#### In Respect of the Preparation of the Annual Accounts

The following statement, which should be read in conjunction with the statement of respective responsibilities of the Directors and Auditors on page 21, is made by the Directors to explain their responsibilities in relation to the preparation of the Annual Accounts, Annual Business Statement and Directors' Report.

The Directors are required by the Building Societies Act 1986 to prepare, for each financial year, Annual Accounts which give a true and fair view of the income and expenditure of the Society and the Group for the financial year, of the state of affairs of the Society and the Group as at the end of the financial year and of the cash flows of the Group for the financial year. In preparing those Annual Accounts, the Directors are required to:

- select appropriate accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the Annual Accounts; and
- prepare the Annual Accounts on the going concern basis, unless it is inappropriate to presume that the Group will continue in business.

In addition to the Annual Accounts, the Act requires the Directors to prepare, for each financial year, an Annual Business Statement and a Directors' Report, each containing prescribed information relating to the business of the Society and its connected undertakings.

#### Website

As well as our branch network and contact centre, Britannia can be contacted via our website, [www.britannia.co.uk](http://www.britannia.co.uk). The maintenance and integrity of the Britannia website is the sole responsibility of the Directors. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

### In Respect of Accounting Records and Internal Control

The Directors are responsible for ensuring that the Society and its connected undertakings:

- keep accounting records in accordance with the Building Societies Act 1986; and
- take reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Financial Services Authority under the Financial Services and Markets Act 2000.

The Directors have general responsibility for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

### Appointment of Auditors

It is a requirement that the Auditors be appointed by the Society at each Annual General Meeting and the effect of the resolution to be proposed at this year's Annual General Meeting, if passed, would be that PricewaterhouseCoopers LLP will be re-appointed until the conclusion of the next Annual General Meeting.



**Paul Mills**

Secretary

For the Board of Directors

8 February 2005

## Independent Auditors' Report to the Members of Britannia Building Society

We have audited the Annual Accounts which comprise the income and expenditure accounts, the balance sheets, the cash flow statement and the related notes which have been prepared under the historical cost convention and the accounting policies set out in the Statement of Accounting Policies. We have examined the Annual Business Statement (other than the details of Directors and Officers upon which we are not required to report) and the Directors' Report.

### Respective Responsibilities of Directors and Auditors

The Directors' responsibilities for the preparation of the Annual Report include responsibilities for the Annual Accounts, the Annual Business Statement and the Directors' Report and are set out in the Statement of Directors' Responsibilities. Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for, the Society's Members as a body in accordance with Section 78 of the Building Societies Act 1986 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or in to whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the Annual Accounts give a true and fair view and are properly prepared in accordance with the Building Societies Act 1986, on certain information included within the Annual Business Statement and on whether, in our opinion, the Directors' Report is consistent with the accounting records and the Annual Accounts. We also report to you if, in our opinion, we have not received all the information and explanations we require for our audit, or if the Annual Accounts are not in agreement with the accounting records.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent mis-statements or material inconsistencies with the Annual Accounts, the Annual Business Statement or the Directors' Report. The other information comprises only the Chairman's Statement, the Chief Executive's Report, the Annual Report on Directors' Remuneration, Corporate Governance Report and the Five Year Review.

### Basis of Audit Opinion

We conducted our audit in accordance with auditing standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Annual Accounts and the Annual Business Statement. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Annual Accounts, and of whether the accounting policies are appropriate to the Society's and Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Annual Accounts are free from material mis-statement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the Annual Accounts.

### Opinion

#### In our opinion:

- (a) the Annual Accounts give a true and fair view of the state of affairs of the Society and of the Group as at 31 December 2004 and of the income and expenditure of the Society and the income and expenditure and cash flows of the Group for the year then ended;
- (b) the information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given;
- (c) the information given in the Directors' Report is consistent with the accounting records and the Annual Accounts; and
- (d) the Annual Accounts, the Annual Business Statement and the Directors' Report have each been prepared in accordance with the applicable requirements of Part VIII of the Building Societies Act 1986 and regulations made under it.



#### PricewaterhouseCoopers LLP

Chartered Accountants and Registered Auditors

Manchester

8 February 2005

## Group Income and Expenditure Account

for the year ended 31 December 2004

	Notes	2004 £m	2003 £m
Interest receivable and similar income	1	996.8	794.9
Interest payable and similar charges	2	(789.5)	(577.1)
<b>Net interest receivable</b>		<b>207.3</b>	217.8
Share of operating profit in joint ventures	17	1.1	1.3
Fees and commissions receivable		81.4	71.7
Fees and commissions payable		(24.8)	(20.0)
Other operating income	4	68.4	49.4
<b>Total income</b>		<b>333.4</b>	320.2
Administrative expenses	5	(153.6)	(143.1)
Depreciation and amortisation		(32.1)	(28.6)
<b>Profit before provisions and Britannia Membership Reward</b>		<b>147.7</b>	148.5
Provisions for bad and doubtful debts	16	(7.3)	(14.2)
<b>Profit before Britannia Membership Reward</b>	6	<b>140.4</b>	134.3
Britannia Membership Reward	10	(42.1)	(42.0)
<b>Profit on ordinary activities before tax</b>		<b>98.3</b>	92.3
Tax on profit on ordinary activities	11	(26.9)	(27.0)
<b>Profit for the financial year</b>	30	<b>71.4</b>	65.3

There have been no recognised gains or losses other than the above profits.

The accounting policies and notes on pages 27 to 57 form part of these Accounts.

All the results in the current year shown above relate to continuing activities.

## Society Income and Expenditure Account

for the year ended 31 December 2004

	Notes	2004 £m	2003 £m
Interest receivable and similar income	1	970.8	773.5
Interest payable and similar charges	2	(805.9)	(588.1)
<b>Net interest receivable</b>		<b>164.9</b>	185.4
Income from investments	3	40.1	34.3
Fees and commissions receivable		32.8	37.8
Fees and commissions payable		(13.2)	(11.9)
Other operating income	4	1.3	1.4
<b>Total income</b>		<b>225.9</b>	247.0
Administrative expenses	5	(121.0)	(115.8)
Depreciation and amortisation		(27.6)	(25.1)
<b>Profit before provisions and Britannia Membership Reward</b>		<b>77.3</b>	106.1
Provisions for bad and doubtful debts	16	0.6	(6.5)
<b>Profit before Britannia Membership Reward</b>		<b>77.9</b>	99.6
Britannia Membership Reward	10	(42.1)	(42.0)
<b>Profit on ordinary activities before tax</b>		<b>35.8</b>	57.6
Tax on profit on ordinary activities	11	(1.3)	(9.6)
<b>Profit for the financial year</b>	30	<b>34.5</b>	48.0

There have been no recognised gains or losses other than the above profits.

The accounting policies and notes on pages 27 to 57 form part of these Accounts.

All the results in the current year shown above relate to continuing activities.

# Group Balance Sheet

at 31 December 2004

	Notes	2004 £m	2004 £m	2003 £m	2003 £m
<b>Assets</b>					
<b>Liquid Assets</b>					
Cash in hand and balances with the Bank of England			30.8		35.4
Loans and advances to credit institutions	12		1,153.0		1,018.8
Debt securities	13		5,483.7		4,905.5
			<b>6,667.5</b>		<b>5,959.7</b>
<b>Loans and advances to customers</b>					
Loans fully secured on residential property			14,785.1		12,993.1
Loans fully secured on residential property subject to non-recourse finance	15	2,043.9		1,098.7	
Non-recourse finance	15	(1,990.6)		(1,062.9)	
			<b>53.3</b>		<b>35.8</b>
			<b>14,838.4</b>		<b>13,028.9</b>
Other loans	14		1,371.9		1,588.0
	14		<b>16,210.3</b>		<b>14,616.9</b>
Investments in joint ventures	17				
Share of gross assets			43.7		44.8
Share of gross liabilities			(42.7)		(43.6)
			<b>1.0</b>		<b>1.2</b>
Intangible fixed assets	18		52.3		43.6
Tangible fixed assets	19		128.5		134.5
Other assets			55.5		41.6
Prepayments and accrued income	20		182.7		131.3
Total assets	6		<b>23,297.8</b>		<b>20,928.8</b>
<b>Liabilities</b>					
Shares	21		11,798.8		11,103.6
Amounts owed to credit institutions	22		1,228.9		766.1
Amounts owed to other customers	23		2,653.5		2,598.5
Debt securities in issue	24		5,565.6		4,708.3
Other liabilities	25		193.7		158.3
Accruals and deferred income	26		102.6		127.4
Provisions for liabilities and charges	27		30.4		13.9
Subordinated liabilities	28		447.7		247.5
			<b>22,021.2</b>		<b>19,723.6</b>
Subscribed capital	29		110.0		110.0
Share premium	30		3.1		3.1
General reserve	30		1,163.5		1,092.1
Total liabilities			<b>23,297.8</b>		<b>20,928.8</b>
<b>Memorandum Items</b>					
Commitments	31		454.6		507.8

The accounting policies and notes on pages 27 to 57 form part of these Accounts.

Approved by the Board of Directors on 8 February 2005.



**I C Adam**  
(Chairman)



**N B Richardson**  
(Group Chief Executive)



**P A Lee**  
(Group Finance Director)

# Society Balance Sheet

at 31 December 2004

	Notes	2004 £m	2003 £m
<b>Assets</b>			
<b>Liquid Assets</b>			
Cash in hand and balances with the Bank of England		30.7	35.4
Loans and advances to credit institutions	12	1,135.1	1,001.8
Debt securities	13	5,414.1	4,836.5
		<b>6,579.9</b>	<b>5,873.7</b>
<b>Loans and advances to customers</b>			
Loans fully secured on residential property	14	10,668.7	10,035.3
Other loans	14	1,288.2	1,338.5
		<b>11,956.9</b>	<b>11,373.8</b>
Investments	17	4,399.5	3,359.6
Tangible fixed assets	19	111.2	116.7
Other assets		14.0	16.4
Prepayments and accrued income	20	169.1	124.3
<b>Total assets</b>		<b>23,230.6</b>	<b>20,864.5</b>
<b>Liabilities</b>			
Shares	21	11,798.8	11,103.6
Amounts owed to credit institutions	22	1,217.6	753.5
Amounts owed to other customers	23	2,882.0	2,767.2
Debt securities in issue	24	5,565.6	4,708.3
Other liabilities	25	64.1	66.4
Accruals and deferred income	26	100.1	112.0
Provisions for liabilities and charges	27	28.2	14.0
Subordinated liabilities	28	447.7	247.5
		<b>22,104.1</b>	<b>19,772.5</b>
Subscribed capital	29	110.0	110.0
Share premium	30	3.1	3.1
General reserve	30	1,013.4	978.9
<b>Total liabilities</b>		<b>23,230.6</b>	<b>20,864.5</b>
<b>Memorandum Items</b>			
Commitments	31	370.0	411.1

The accounting policies and notes on pages 27 to 57 form part of these Accounts.

Approved by the Board of Directors on 8 February 2005.



**I C Adam**  
(Chairman)



**N B Richardson**  
(Group Chief Executive)



**P A Lee**  
(Group Finance Director)

## Consolidated Cash Flow Statement

for the year ended 31 December 2004

	Notes	2004 £m	2003 £m
Net cash inflow from operating activities	33	436.4	716.2
Returns on investments and servicing of finance			
Interest paid on subordinated liabilities		(23.0)	(12.7)
Interest paid on subscribed capital		(14.1)	(14.3)
Taxation		(9.7)	(12.8)
Capital expenditure and financial investment			
Purchase of investment securities		(19,910.8)	(26,505.0)
Sale and maturity of investment securities		19,340.0	25,834.1
Purchase of tangible fixed assets		(25.7)	(29.5)
Sale of tangible fixed assets		3.5	4.1
Financing			
Issue of subordinated liabilities		200.0	—
Decrease in cash	33	(3.4)	(19.9)

# Statement of Accounting Policies

## Accounting Convention

The Accounts are prepared under the historical cost convention.

## Basis of Preparation and Consolidation

The Accounts have been prepared in accordance with the Building Societies (Accounts and Related Provisions) Regulations 1998 ('the Regulations') and applicable Accounting Standards. The Group Accounts consolidate the state of affairs, cash flows and results of the Society and its subsidiary undertakings, and other companies which are considered by the Directors to be quasi-subsidiaries as defined in Financial Reporting Standard No. 5 (Reporting the substance of transactions), all of which have accounting periods ended 31 December.

The financial statements are prepared in accordance with relevant British Bankers Association Statements of Recommended Accounting Practice (SORP) in all material respects.

An analysis of the Group by business segment is shown in Note 6. A Group geographical segmental analysis is not disclosed as the Group's business is predominantly United Kingdom based.

## Advances Subject to Non-recourse Finance

Loans fully secured on residential properties subject to non-recourse finance meeting the conditions specified in Financial Reporting Standard No. 5 are included in the balance sheet using the linked presentation method. Such balances are stated at book value less provisions for impairment.

## Income Recognition

Interest is recognised in the income and expenditure account on an accruals basis. Mortgage arrangement fees are taken to fees and commissions receivable on a received basis except for commercial lending fees, where the amount of the fee can be increased in exchange for a discounted mortgage rate. These commercial fees are amortised over the period of the discounted interest rate.

The cost of mortgage cashbacks is amortised on a straight line basis over the early redemption fee period, and charged against interest receivable. The cost of discounts is charged as incurred against interest receivable.

## Goodwill and Premiums on Acquisitions

In accordance with Financial Reporting Standard No. 10 (Goodwill and intangible assets), amounts paid for businesses in excess of the fair value of the net tangible assets acquired are amortised on a straight line basis over their estimated useful economic lives up to a maximum of twenty years, subject to any adjustments arising from impairment reviews.

Premiums paid for mortgage book businesses in excess of the fair value of the net tangible assets acquired are included in intangible

fixed assets and amortised on a level yield basis over the lesser of five years and the redemption rate of the mortgages. Premium amortisation is included within interest receivable.

Premiums paid for mortgage book businesses before 1999 were deducted from reserves in the year of acquisition.

## Broker Fees

Broker fees are capitalised within other assets and written off against fees and commissions payable, on a straight line basis over the lower of five years and the redemption rate of the mortgages.

## Interests in Joint Ventures

A joint venture is one where the Group holds an interest on a long-term basis and which is jointly controlled by the Group and other third party entities. Group profit includes income from interests in joint ventures based on accounts made up to the same date. Interests in joint ventures are included in the consolidated balance sheet at the Group's share of the book value of the net tangible assets of the undertakings concerned.

## Pensions

The expected cost, including variations from the regular cost, of pensions in respect of the Group's defined benefit pension scheme and unfunded benefits scheme is charged to the income and expenditure account so as to spread the cost of pensions over the expected service lives of employees in the scheme. The pension cost is assessed in accordance with the advice of qualified actuaries. On a triennial basis, a formal actuarial valuation of the Group's pension scheme is undertaken.

The costs of pensions in respect of the Group's defined contribution scheme are charged to the income and expenditure account as incurred.

## Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is provided at current rates on a non-discounted basis, on all timing differences between the recognition of gains and losses in the accounts and their recognition in a tax computation.

## Liquid Assets

Debt securities intended for use on a continuing basis in the Group's activities are classified as financial fixed assets and are stated at cost less provision for any permanent diminution in value. Premiums and discounts arising on the purchase of financial fixed assets are amortised over the period to maturity. Any amounts so amortised are charged or credited to net interest receivable within the income and expenditure account.

## Statement of Accounting Policies contd

### Provisions for Bad and Doubtful Debts

Provisions are made to reduce the value of loans and advances to the amount which the Directors consider is likely to be recoverable.

Throughout the year, and at the year end, assessments are made of all loans and advances on properties which are in possession or in arrears. Specific provisions are made against those loans and advances when, in the opinion of the Directors, their circumstances make full recovery doubtful. Anticipated losses on these accounts are calculated as the difference between the achievable market value of the security, calculated by applying an industry recognised national house price index less a forced sale deduction to valuations, and the outstanding loan balance, after making appropriate allowance for costs of repossession and sale. A possession probability factor is then applied to the shortfall to determine the provision required. The probability factor reflects the Group's actual experience of the propensity of the different arrears categories to reach possession status. Allowance is made for loss insurance cover where appropriate. The Directors recognise that not all accounts in arrears will result in possession and apply a factor based on recent experience and other relevant risk considerations to reflect this probability when calculating the provision for accounts in arrears.

Once properties have been sold and any shortfall crystallised, individual cases are reviewed for potential insurance recovery. Provision is made for amounts not considered to be recoverable and written off when there is no realistic prospect of recovery.

A general provision is made to cover potential losses which, although not yet specifically identified, are known from experience to exist in the Group's loan portfolio. Such provisions are calculated with reference to actuarial assumptions, credit loss predictions and consistency with industry levels. These provisions are regularly reviewed against actual experience.

The charge to the income and expenditure account represents new or additional provisions made less any reduction in provisions or recoveries of amounts previously provided. Interest which is considered irrecoverable, where the property has been taken into possession or the normal lending relationship has ceased, is suspended. Interest up to that time is credited to income and provision made as appropriate.

### Shares, Deposits, Subordinated Liabilities and Subscribed Capital

In accordance with Financial Reporting Standard No. 4 (Capital instruments), issue costs are deducted from debt instruments on the balance sheet, or, in the case of permanent interest bearing shares, were deducted from the share premium account.

Premiums and discounts, together with commissions and other costs incurred in the issuing of fixed and floating rate notes and subordinated liabilities, are amortised on a straight line basis over the life of the instruments.

### Hedging Contracts and Instruments

The criteria required for an instrument to be classified as a hedge are that the transaction must be reasonably expected to match or eliminate a significant proportion of the risk inherent in the assets, liabilities, other positions or cash flows being hedged and which results from potential movements in interest rates, exchange rates and market indices. Adequate evidence of the intention to hedge and linkage with the underlying risk inherent in the assets, liabilities, other positions or cash flows being hedged, must be established at the outset of the transaction.

All interest, exchange rate and market price related instruments which are designated as hedges are accounted for on a consistent basis with the underlying assets, liabilities or positions. Where a hedge is terminated early because the underlying assets were redeemed, the realised gain or loss is immediately credited/expensed to the income and expenditure account. Amounts accrued on hedging contracts and instruments are included within prepayments and accruals.

### Tangible Fixed Assets and Depreciation

The directly attributable cost of additions and alterations to office premises, including borrowing costs incurred in the development of major premises, and additions to equipment, fixtures, fittings, development of computer software and vehicles is capitalised.

The cost of tangible fixed assets is written down to their residual value in equal annual instalments over their estimated expected useful lives, which are reviewed regularly in the light of technological developments, usage and other relevant factors:

#### Land and buildings

Freehold properties	50 years
Leasehold properties	Life of lease
Major alterations to existing properties	7 years

#### Vehicles

1 year

#### General equipment

3 - 7 years

#### Computer equipment and software

3 - 5 years.

### Leases

Assets acquired under finance leases are capitalised at fair value at the start of the lease, with the corresponding obligations being included in other liabilities. The finance lease costs charged to the income and expenditure account are based on a constant periodic rate as applied to the outstanding liabilities.

The rentals paid for assets acquired under operating leases are charged to the income and expenditure account in accordance with the terms of the individual lease.

### **Captive Insurance Fund**

The Society has established a wholly owned subsidiary, as a captive insurance company, for the purposes of insuring part of the risk upon secured lending and, in certain cases, charges a fee to the customer.

The subsidiary uses a fixed earnings pattern to estimate future claims and the amount of premium to be retained against future liabilities. Independent actuaries assess future liabilities to ensure adequacy of reserves.

Premiums charged to borrowers which have not yet been released to income are included in accruals and deferred income.

### **Britannia Membership Reward**

The payment to be made under the Britannia Membership Reward is shown as an additional line to the income and expenditure account. This reflects the special nature of the payment which was not envisaged when the Regulations were drawn up prescribing the standard income and expenditure account format.

### **Foreign Currency Transactions**

All non-sterling assets and liabilities are translated at the closing rate of exchange unless a currency exchange contract exists, when the contract rate is applied. All foreign exchange differences are taken to the income and expenditure account as they arise. Amounts due or receivable under foreign currency swap contracts are included within accruals or prepayments.

# Notes to the Accounts

for the year ended 31 December 2004

## 1. Interest Receivable and Similar Income

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
On loans fully secured on residential property	<b>621.1</b>	460.8	<b>435.6</b>	350.0
On other loans				
Connected undertakings	—	—	<b>175.8</b>	106.0
Other	<b>148.0</b>	135.9	<b>135.2</b>	122.9
On debt securities				
Interest and other income	<b>195.4</b>	152.9	<b>191.8</b>	149.1
Net gains arising on realisation	<b>0.8</b>	4.0	<b>0.8</b>	4.0
On loans and advances to credit institutions				
Interest and other income	<b>30.2</b>	24.8	<b>30.0</b>	24.7
Net income on financial instruments	<b>1.3</b>	16.5	<b>1.6</b>	16.8
	<b>996.8</b>	794.9	<b>970.8</b>	773.5

Interest receivable on other loans includes Group £16.3 million (2003 : £16.3 million), Society £5.8 million (2003 : £5.7 million), in respect of loans advanced prior to 1 October 1998, to corporate bodies, such as Housing Associations, which are fully secured on residential property. The classification adopted for such amounts is consistent with the balance sheet classification of the related loan in accordance with the Building Societies Act 1997 (see Note 14).

All of the Group's loan interest receivable arises from loans originated and advanced in the United Kingdom.

Mortgage incentives of Group £1.5 million (2003 : £1.7 million), Society £1.5 million (2003 : £1.7 million) have been charged against interest receivable.

Unamortised incentives of Group £1.0 million (2003 : £1.1 million), Society £1.0 million (2003 : £1.1 million) are included in other assets on the balance sheet.

Interest receivable, as shown above, has been reduced by £0.7 million (2003 : £0.8 million) representing interest suspended on non-performing loans in accordance with the Group's accounting policy. Movements in the suspended interest account are as follows:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Balance brought forward	<b>6.5</b>	6.4	<b>4.8</b>	4.7
Interest written off during the year	<b>(0.1)</b>	(0.7)	<b>(0.3)</b>	(0.7)
Interest suspended during the year	<b>0.7</b>	0.8	<b>0.7</b>	0.8
Balance carried forward (Note 16)	<b>7.1</b>	6.5	<b>5.2</b>	4.8

## 2. Interest Payable and Similar Charges

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
On shares held by individuals	<b>418.9</b>	329.5	<b>418.9</b>	329.5
On subscribed capital	<b>14.3</b>	14.3	<b>14.3</b>	14.3
On deposits and other borrowings				
Subordinated liabilities	<b>23.0</b>	12.9	<b>23.0</b>	12.9
Connected undertakings	—	—	<b>60.1</b>	48.8
Other	<b>333.3</b>	220.4	<b>289.6</b>	182.6
	<b>789.5</b>	577.1	<b>805.9</b>	588.1

### 3. Income from Investments

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Dividend income from shares in subsidiaries	—	—	40.1	34.3

### 4. Other Operating Income

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Other operating income includes:				
Rent	0.9	0.9	1.3	1.4
Profit before tax of securitised operations (Note 15)	44.8	41.2	—	—
Other	22.7	7.3	—	—
	<b>68.4</b>	49.4	<b>1.3</b>	1.4

### 5. Administrative Expenses

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Employee costs				
Wages and salaries	75.7	70.4	55.7	52.2
Social security costs	6.5	5.8	5.2	4.7
Other pension costs	5.6	8.3	5.0	7.7
	<b>87.8</b>	84.5	<b>65.9</b>	64.6
Other administrative expenses	<b>65.8</b>	58.6	<b>55.1</b>	51.2
	<b>153.6</b>	143.1	<b>121.0</b>	115.8

Other administrative expenses include operating lease rentals of Group £6.4 million (2003 : £6.2 million) and Society £6.0 million (2003 : £6.4 million).

#### Services provided by the Group's auditors

During the year the Group obtained the following services from the Group's auditors at costs as detailed below:

	2004 £m	2003 £m
Audit related services		
Statutory audit	0.4	0.3
Further assurance services	0.5	0.3
Tax services	0.1	0.1
Other services not covered above	<b>0.1</b>	0.1

# Notes to the Accounts

for the year ended 31 December 2004

## 6. Segmental Information

The Group reports through two principal business segments: Membership business and Britannia Capital Investment Group ('BCIG'). An analysis of the Group profit before Britannia Membership Reward and Group total and net assets is provided in the table below:

	Membership business 2004 £m	BCIG 2004 £m	Total Group 2004 £m	Membership business 2003 £m	BCIG 2003 £m	Total Group 2003 £m
Profit before Britannia Membership Reward	50.1	90.3	140.4	58.3	76.0	134.3
Net assets	1,157.8	118.9	1,276.7	1,109.4	95.8	1,205.2
Total assets	15,072.8	8,225.0	23,297.8	14,373.7	6,555.1	20,928.8
Non-recourse finance	—	1,990.6	1,990.6	—	1,062.9	1,062.9
Assets under management	15,072.8	10,215.6	25,288.4	14,373.7	7,618.0	21,991.7

In order to analyse net interest between the BCIG and Membership business segments it is necessary to apply a transfer price to the internal funding of the BCIG businesses.

Total and net assets represent the actual assets of the businesses within each of the segments after elimination of balances outstanding between these businesses.

Assets under management comprise total Group assets after adding back non-recourse finance.

## 7. Directors' Remuneration

Remuneration of the Society's Directors is detailed below:

	Salary/fee £000	Performance related bonus (payable March 2005) £000	Performance related bonus (deferred) £000	Benefits £000	Increase in accrued pension £000	Total £000
<b>2004</b>						
<b>Executive Directors</b>						
Neville Richardson	319	94	75	25	13	526
Gerald Gregory	206	101	76	19	9	411
Phil Lee	185	59	44	22	6	316
<b>Non-executive Directors</b>						
Ian Adam (Chairman from 2 April 2004)	85	—	—	—	—	85
Barrie Bernstein (Chairman until retirement on 2 April 2004)	24	—	—	—	—	24
Bill Gordon	52	—	—	—	—	52
Francis Gugen	35	—	—	—	—	35
Helen Keays (appointed 1 October 2004)	9	—	—	—	—	9
Chris Jones	35	—	—	—	—	35
Bridget Rosewell	39	—	—	—	—	39
Tom Sawyer	35	—	—	—	—	35
Elizabeth Walmsley	35	—	—	—	—	35
	1,059	254	195	66	28	1,602

## 7. Directors' Remuneration (continued)

	Salary/fee £000	Performance related bonus £000	Performance related bonus (deferred) £000	Benefits £000	*Other payments £000	Increase/ (decrease) in accrued pension £000	Total £000
<b>2003</b>							
<b>Executive Directors</b>							
Neville Richardson	297	80	60	25	—	19	481
Gerald Gregory	195	53	39	21	—	9	317
Phil Lee	180	49	36	60	—	6	331
Graham Stow (retired 31 May 2003)	121	57	—	12	—	(8)	182
John Suffolk (resigned 2 April 2003)	50	—	—	5	51	2	108
<b>Non-executive Directors</b>							
Barrie Bernstein (Chairman)	92	—	—	—	—	—	92
Ian Adam	54	—	—	—	—	—	54
Harry Coe (resigned 31 March 2003)	9	—	—	—	34	—	43
Bill Gordon	39	—	—	—	—	—	39
Francis Gugen (appointed 17 December 2003)	1	—	—	—	—	—	1
Chris Jones (appointed 7 May 2003)	22	—	—	—	—	—	22
Rhidian Jones (retired 24 September 2003)	26	—	—	—	—	—	26
Bridget Rosewell	34	—	—	—	—	—	34
Tom Sawyer	34	—	—	—	—	—	34
Elizabeth Walmsley	34	—	—	—	—	—	34
	1,188	239	135	123	85	28	1,798

\* includes £51,154 paid to John Suffolk by way of compensation for loss of office and £34,065 paid to Harry Coe in lieu of notice.

The following information shows the value of Directors' pension benefits. The increase in accrued pension represents the change in the annual pension to which each Director is entitled as the result of changes in pensionable earnings (excluding inflation), increases in pensionable service and investment return during the year. The transfer value equivalent represents the present capital value of the changes in Directors' accrued pension entitlements excluding employees' contributions for the year and has been calculated in accordance with Actuarial Guidance Note GN 11.

All the Executive Directors will receive benefits from the Society's approved UK pension arrangements. Certain Directors, who are subject to the earnings cap, will also receive benefits from an unfunded scheme which does not qualify for certain tax allowances under the Income and Corporation Taxes Act 1998.

	Increase in accrued pension for the year ended 31 December 2004 £000	Accrued pension entitlement at 31 December 2004 £000	Increase in transfer value of accrued benefits for the year ended 31 December 2004 £000	Transfer value of accrued benefits at 31 December 2004 £000	Employees' contributions for the year ended 31 December 2004 £000
<b>Executive Directors</b>					
Neville Richardson		13	64	244	15
Gerald Gregory		9	82	230	14
Phil Lee		6	14	97	12

## 8. Employees

The average number of persons employed during the year was:

	Group 2004 Full-time	Group 2004 Part-time	Group 2003 Full-time	Group 2003 Part-time	Society 2004 Full-time	Society 2004 Part-time	Society 2003 Full-time	Society 2003 Part-time
Head and administrative offices	1,388	289	1,294	250	1,388	289	1,294	250
Branch and subsidiary undertakings' offices	1,546	539	1,474	592	1,046	514	1,045	570
	2,934	828	2,768	842	2,434	803	2,339	820

# Notes to the Accounts

for the year ended 31 December 2004

## 9. Pensions

The Britannia Building Society Pension Scheme operates a funded defined benefit pension scheme for the employees of the Society (and for certain employees of subsidiary undertakings) who commenced employment prior to 1 September 2001. The costs have been assessed in accordance with the advice of a qualified actuary using the projected unit valuation method. A full actuarial assessment is undertaken every three years. The latest assessment was at 6 April 2002. The Society adopted this valuation in its financial statements with effect from 6 April 2002.

The assumptions that have the most significant effect on the results of the valuation are those relating to the long-term rates of yield on funds invested and of salary increases. These have been taken as 8.0% and 4.0% in respect of past service accrued and future service pension benefits. In addition, allowances have been made for the age related promotional salary scale and increases in post retirement benefits.

For those eligible employees who commenced employment after 1 September 2001, the Society operates a defined contribution section within the Britannia Building Society Pension Scheme. During 2004, the Society paid contributions of £0.5 million in respect of this section of the scheme (2003 : £0.3 million).

The Society has chosen not to adopt Financial Reporting Standard No.17 ('FRS 17') (Retirement benefits) early and has adopted its transitional arrangements. Accordingly it complies with the existing Statement of Standard Accounting Practice No. 24 ('SSAP 24') (Accounting for pension costs) and provides the disclosure in respect of the balance sheet, statement of total recognised gains and losses and the income and expenditure account which is required by FRS 17.

### Statement of Standard Accounting Practice No. 24

At the date of the latest valuation, the market value of the assets of the defined benefit section was £149.9 million. The actuarial value was sufficient to cover 83% of the accrued benefits that will be due to members, after allowing for future salary increases. The Minimum Funding Requirement funding level as at 6 April 2002 was 96% (1999 : 102%). Consequently, in 2003 the Society increased its salary related level of contributions to 16% which has been continued in the current year. During the year, the Society also contributed £30.0 million (2003 : £30.0 million) as one of a series of regular additional payments to be made to the scheme in order to meet the ongoing scheme requirements and satisfy the Minimum Funding Requirement. In addition, staff contributions were increased to 6% from 1 April 2003 and to 7% from 1 April 2004.

Prepayments and accrued income (Note 20) include £76.6 million (2003 : £44.0 million) in respect of prepayments into the defined benefit section of the scheme calculated in accordance with SSAP 24.

Included within accruals and deferred income is a provision for unfunded benefits for employees who are subject to the Inland Revenue earnings cap calculated in accordance with SSAP 24 of £2.6 million (2003 : £2.3 million).

### Financial Reporting Standard No. 17

The valuation used for FRS 17 disclosures has been based on the most recent actuarial valuation as at 6 April 2002, updated by Wm. M. Mercer to take account of the requirements of FRS 17 in order to assess the liabilities of the scheme at 31 December 2004. Scheme assets are stated at their market value at 31 December 2004.

The financial assumptions used in calculating the liabilities and expected rates of return on assets under the projected unit valuation method were:

	31 December 2004 %	31 December 2003 %	31 December 2002 %
Rate of increase in salaries	4.00	4.00	3.75
Rate of increase in pensions in payment	3.25	3.25	3.25
Discount rate	5.30	5.40	5.60
Inflation rate	2.80	2.80	2.50

## 9. Pensions (continued)

The assets in the scheme and the long-term expected rate of return were:

	Expected rate of return 31 December 2004 %	Fair value 31 December 2004 £m	Expected rate of return 31 December 2003 %	Fair value 31 December 2003 £m	Expected rate of return 31 December 2002 %	Fair value 31 December 2002 £m
Equities	7.3	166.5	7.4	132.1	7.4	96.2
Bonds	5.0	83.3	5.5	47.9	5.5	28.7
Cash	3.9	3.4	3.9	19.5	3.9	15.4
Total market value of assets		253.2		199.5		140.3
Present value of scheme liabilities		(269.0)		(246.9)		(217.1)
Deficit in the scheme		(15.8)		(47.4)		(76.8)
Related deferred tax asset		4.7		14.2		23.0
Net pension liability		(11.1)		(33.2)		(53.8)

If the above amounts had been recognised in the financial statements, the Group's general reserves would be as follows:

	31 December 2004 £m	31 December 2003 £m
General reserve excluding pension liability	1,163.5	1,092.1
SSAP 24 prepayment	(76.6)	(44.0)
Pension liability	(11.1)	(33.2)
General reserve including pension liability	1,075.8	1,014.9

Under FRS 17, there is no significant difference to the provision required in respect of the unfunded benefits.

No changes were made to benefits and the Group paid contributions of £36.0 million (2003 : £37.6 million) and the Society £35.9 million (2003 : £37.4 million).

The amounts recognised in the financial statements if FRS17 had been fully adopted would have been as follows:

### Analysis of the amount charged to operating profit

	31 December 2004 £m	31 December 2003 £m
Service cost	4.5	4.6
Past service cost	—	0.8
Total operating charge	4.5	5.4

### Analysis of net return on pension scheme assets

	31 December 2004 £m	31 December 2003 £m
Expected return on pension scheme assets	13.3	10.0
Interest on pension liabilities	(13.4)	(12.5)
Net interest cost	(0.1)	(2.5)

### Analysis of amount recognised in Statement of Total Recognised Gains and Losses

	31 December 2004 £m	31 December 2003 £m	31 December 2002 £m	31 December 2004 %	31 December 2003 %	31 December 2002 %	
Actual return less expected return on assets	5.9	15.6	(32.0)	2	8	(23)	% of scheme assets
Experience gains and losses on liabilities	—	—	3.8	—	—	2	% of scheme liabilities
Changes in assumptions	(5.7)	(15.9)	(21.1)				
Actuarial gain/(loss)	0.2	(0.3)	(49.3)	—	—	23	% of scheme liabilities

# Notes to the Accounts

for the year ended 31 December 2004

## 9. Pensions (continued)

### Movement in deficit in the year

	31 December 2004 £m	31 December 2003 £m
Deficit in the scheme at the beginning of the year	(47.4)	(76.8)
Movement in the year		
Current service cost	(4.5)	(4.6)
Contributions	36.0	37.6
Past service cost	—	(0.8)
Net interest cost	(0.1)	(2.5)
Actuarial gain/(loss)	0.2	(0.3)
Deficit in the scheme at the end of the year	(15.8)	(47.4)

### Under FRS 17, the disclosures in respect of the unfunded benefits scheme are as follows:

During the year ended 31 December 2004 £0.4 million (2003 : £0.3 million) would have been charged to operating profit, £0.3 million (2003 : £0.2 million) of which was in respect of service cost.

During the year ended 31 December 2004 a net loss of £0.3 million would have been recognised in the Statement of Total Recognised Gains and Losses, which was in respect of changes in assumptions (2003 : £0.1 million in respect of actual return less expected return on assets).

### Movement in unfunded benefit provision in the year

	31 December 2004 £m	31 December 2003 £m
Provision at the beginning of the year	(2.7)	(2.3)
Movement in the year		
Current service cost	(0.3)	(0.2)
Interest on pension liabilities	(0.1)	(0.1)
Actuarial loss	(0.3)	(0.1)
Provision at the end of the year	(3.4)	(2.7)

## 10. Britannia Membership Reward

	Group and Society 2004 £m	Group and Society 2003 £m
Payable to Members	42.1	42.0

The Britannia Membership Reward is designed to reward Members of the Society for the contribution they have made to the continued success of the Society, by distributing funds which are not required for the continued growth and stability of the Society.

The Directors have decided that the Reward Pool for 2004 is £42.1 million (2003 : £42.0 million), which has been distributed to registered Members in proportion to the number of Reward Points earned. Reward Points are calculated on the number and value of products held, and the length of Membership.

## 11. Tax on Profit on Ordinary Activities

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
UK tax at 30% (2003 : 30%)				
Corporation tax				
Current	17.5	18.5	(5.1)	1.5
Prior year items	(1.4)	(1.4)	(1.0)	(3.7)
Share of current tax of joint ventures	0.4	0.5	—	—
Total corporation tax	16.5	17.6	(6.1)	(2.2)
Deferred tax	10.4	9.4	7.4	11.8
	26.9	27.0	1.3	9.6

### Factors affecting tax charge for the year

The corporation tax assessed for the period is lower than the standard rate of corporation tax in the UK (30%). The differences are explained below:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Profit on ordinary activities before tax	98.3	92.3	35.8	57.6
Profit before tax multiplied by standard rate of tax	29.5	27.7	10.7	17.3
Effects of				
Movements in short term timing differences	(11.2)	(7.9)	(7.9)	(7.8)
Dividends from UK subsidiaries	—	—	(9.3)	(7.9)
Other	(1.8)	(2.2)	0.4	(3.8)
Corporation tax charge/(credit) for year	16.5	17.6	(6.1)	(2.2)

## 12. Loans and Advances to Credit Institutions

Loans and advances to credit institutions have remaining maturities as follows:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Accrued interest	3.9	2.1	3.9	2.1
Repayable on demand	18.6	17.4	0.7	0.4
Other loans and advances by residual maturity repayable				
In not more than three months	1,007.7	957.8	1,007.7	957.8
In more than three months but not more than one year	117.8	36.5	117.8	36.5
In more than one year but not more than five years	5.0	5.0	5.0	5.0
	1,153.0	1,018.8	1,135.1	1,001.8

## Notes to the Accounts

for the year ended 31 December 2004

### 13. Debt Securities

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Issued by public bodies	166.9	191.4	155.3	165.2
Issued by other borrowers	5,316.8	4,714.1	5,258.8	4,671.3
	<b>5,483.7</b>	4,905.5	<b>5,414.1</b>	4,836.5

Debt securities have remaining maturities as follows:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Accrued interest	34.3	26.9	33.6	26.2
In not more than one year	1,745.0	1,952.9	1,726.0	1,925.3
In more than one year	3,704.4	2,925.7	3,654.5	2,885.0
	<b>5,483.7</b>	4,905.5	<b>5,414.1</b>	4,836.5

Transferable debt securities comprise

Listed	3,763.6	3,041.8	3,736.3	2,994.9
Unlisted	1,720.1	1,863.7	1,677.8	1,841.6
	<b>5,483.7</b>	4,905.5	<b>5,414.1</b>	4,836.5

Market value of transferable debt securities

Government debt securities	166.8	187.1	152.5	160.8
Private sector debt securities	5,322.3	4,714.6	5,266.7	4,671.9
	<b>5,489.1</b>	4,901.7	<b>5,419.2</b>	4,832.7

The market value of bank and building society certificates of deposit included in the above was £1,079.1 million (2003 : £1,249.3 million).

Market value of listed transferable debt securities	3,769.0	3,038.2	3,741.4	2,991.3
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Included in debt securities are

Unamortised premiums	5.0	6.7	5.0	6.7
Unamortised discounts	1.0	1.3	1.0	1.3

The Directors of the Society consider that the primary purpose of holding securities is prudential. The securities are held as liquid assets with the intention of use on a continuing basis in the Group's activities and are therefore classified as financial fixed assets rather than current assets.

Listed debt securities include £1,394.6 million (2003 : £1,064.4 million) asset backed and mortgage backed securities which are held for investment purposes and are not treated as part of the Society's prudential liquidity.

Debt securities include £115.5 million (2003 : £169.8 million) in respect of sale and repurchase agreements.

Movements during the year of debt securities held as financial fixed assets are analysed as follows:

	Group £m	Society £m
Adjusted cost and net book value (excluding accrued interest)		
At 1 January 2004	4,878.6	4,810.3
Additions	19,910.8	19,823.6
Redemptions and disposals	(19,340.0)	(19,253.4)
<b>At 31 December 2004</b>	<b>5,449.4</b>	<b>5,380.5</b>

## 14. Loans and Advances to Customers

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Loans fully secured on residential property	14,838.4	13,028.9	10,668.7	10,035.3
Other loans				
Loans fully secured on land	1,300.7	1,553.0	1,223.9	1,315.0
Other loans	71.2	35.0	64.3	23.5
	<b>16,210.3</b>	14,616.9	<b>11,956.9</b>	11,373.8

Other loans fully secured on land include Group £135.1 million (2003 : £319.9 million), Society £90.4 million (2003 : £82.4 million) of loans which are fully secured on residential property and which were made to corporate bodies, such as Housing Associations, prior to 1 October 1998, the date the Society adopted the powers of the Building Societies Act 1997. The classification of these assets is not consistent with the treatment of similar loans made after 1 October 1998, which are included in 'loans fully secured on residential property' but is necessary to comply with the requirements of the Building Societies Act 1997.

### Maturity analysis

The remaining maturity of loans and advances to customers from the date of the balance sheet is as follows:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Repayable on demand	13.2	3.9	—	—
Other loans and advances by residual maturity repayable				
In not more than three months	56.5	59.5	14.5	12.4
In more than three months but not more than one year	178.4	163.4	31.3	34.8
In more than one year but not more than five years	1,139.3	1,323.4	322.6	530.7
In more than five years	16,882.7	14,192.7	11,616.9	10,825.3
	<b>18,270.1</b>	15,742.9	<b>11,985.3</b>	11,403.2
Less				
Provisions for bad and doubtful debts (Note 16)	(69.2)	(63.1)	(28.4)	(29.4)
Non-recourse finance	(1,990.6)	(1,062.9)	—	—
	<b>16,210.3</b>	14,616.9	<b>11,956.9</b>	11,373.8

The maturity analysis is produced on the basis that where a loan is repayable by instalments, each such instalment is treated as a separate repayment. Arrears are spread across the remaining term of the loan.

The actual experience of repayments may differ from the above since many loans and advances are repaid early.

## 15. Loans Fully Secured on Residential Property Subject to Non-recourse Finance

Quasi-subsiaries of the Society, Leek Finance Number Three PLC (L3), Leek Finance Number Seven PLC (L7), Leek Finance Number Ten PLC (L10), Leek Finance Number Eleven PLC (L11), Leek Finance Number Twelve PLC (L12) and Leek Finance Number Fourteen PLC (L14) have advances secured on residential property subject to non-recourse finance funding. The Society and its subsidiaries are not obliged to support any losses in respect of these mortgages subject to the non-recourse finance other than to the extent of its subordinated funding, nor do they intend to do so. This is clearly stated in agreements with the providers of the funding. Repayment of the non-recourse finance facilities and the deferred consideration will be made solely from the cash flows generated by the underlying mortgage portfolios.

The Society and its subsidiary, Mortgage Agency Services Number Two Limited, have rights to the residual income from the portfolio of mortgages amounting to £145.0 million in L3, L11 and L12. The Society and its subsidiary, Mortgage Agency Services Number Six Limited, have rights to the residual income from the portfolio of mortgages amounting to £93.7 million in L14. The Society and its subsidiaries within the Platform Group Holdings Limited group of companies, have rights to the residual income from the portfolio of mortgages amounting to £1,801.0 million in L7, L10, L11, L12 and L14.

## Notes to the Accounts

for the year ended 31 December 2004

### 15. Loans Fully Secured on Residential Property Subject to Non-recourse Finance (continued)

The quasi-subsiidiaries were originally funded as follows:

Company	Original maximum funding £m	Funded by Group £m	Funded during year
Leek Finance Number Three PLC	94.7	4.3	1999
	115.9	—	2000
	<u>312.3</u>	—	2002
	522.9		
Leek Finance Number Seven PLC	389.1	6.0	2002
Leek Finance Number Ten PLC	375.2	10.5	2003
Leek Finance Number Eleven PLC	373.2	5.3	2003
Leek Finance Number Twelve PLC	703.7	9.4	2004
Leek Finance Number Fourteen PLC	1,045.7	17.8	2004
	<u>3,409.8</u>	<u>53.3</u>	

The rights of the Society are subordinated to all other creditors of L3, L7, L10, L11, L12 and L14.

The non-Group providers of finance have no recourse other than to the assets of the respective quasi-subsiidiary.

The results of the quasi-subsiidiary companies (shown in Note 17) have been incorporated using the linked presentation method. Their aggregated summarised financial statements at 31 December 2004 are:

	2004 £m	2003 £m
<b>Income and expenditure account</b>		
Interest receivable and similar income	133.0	101.5
Interest payable and similar charges	(78.2)	(57.2)
Net interest receivable	54.8	44.3
Other income and charges	(5.5)	(3.1)
Administrative expenses	(0.6)	(2.0)
Provisions for bad and doubtful debts	(3.9)	2.0
Profit on ordinary activities before tax (Note 4)	44.8	41.2
Tax on profit on ordinary activities	(13.4)	(12.4)
Profit for the financial year	31.4	28.8
<b>Assets</b>		
Advances secured on residential property subject to non-recourse finance	2,043.9	1,098.7
Cash at bank and in hand	4.4	10.6
Other debtors	155.1	101.7
Unamortised premium on acquisition of mortgage books	34.5	20.1
Total assets	2,237.9	1,231.1
<b>Capital and liabilities</b>		
Non-recourse finance	2,093.1	1,135.5
Deferred consideration	66.9	44.6
Subordinated funding from Britannia Building Society	53.3	35.8
Other creditors	24.6	14.8
Capital and reserves	—	0.4
Total liabilities	2,237.9	1,231.1

Non-recourse finance includes £102.5 million (2003 : £72.6 million) included within other liabilities in the Group balance sheet.

## 15. Loans Fully Secured on Residential Property Subject to Non-recourse Finance (continued)

	2004 £m	2003 £m
<b>Cash flow statement</b>		
Net cash inflow from operating activities	29.2	122.0
Net (increase)/decrease in mortgage balances	(949.8)	256.2
Net increase/(decrease) in non-recourse finance	957.6	(325.4)
Net increase/(decrease) in subordinated funding	17.5	(13.8)
Payment of deferred purchase consideration	(60.3)	(59.1)
Taxation	(0.4)	—
Decrease in cash	(6.2)	(20.1)

## 16. Provisions for Bad and Doubtful Debts

	Loans fully secured on residential property Specific £m	Loans fully secured on residential property General £m	Other loans fully secured on land Specific £m	Other loans fully secured on land General £m	Total £m
<b>Group</b>					
At 1 January 2004	0.8	45.1	—	10.7	56.6
Amounts written off	(1.8)	—	—	—	(1.8)
Charge/(credit) for the year	3.4	(1.8)	0.6	5.1	7.3
<b>At 31 December 2004</b>	<b>2.4</b>	<b>43.3</b>	<b>0.6</b>	<b>15.8</b>	<b>62.1</b>
Included within suspended interest account (Note 1)					7.1
					<b>69.2</b>

Provisions against non-performing loans at 31 December 2004 were £2.6 million (2003 : £1.5 million). The total of non-performing loans at 31 December 2004 was £347.6 million (2003 : £321.2 million).

During the year the Group recovered £0.8 million (2003 : £1.2 million) against amounts previously written off.

	Loans fully secured on residential property Specific £m	Loans fully secured on residential property General £m	Other loans fully secured on land Specific £m	Other loans fully secured on land General £m	Total £m
<b>Society</b>					
At 1 January 2004	0.1	13.8	—	10.7	24.6
Amounts written off	(0.8)	—	—	—	(0.8)
Charge/(credit) for the year	0.8	(3.1)	0.6	1.1	(0.6)
<b>At 31 December 2004</b>	<b>0.1</b>	<b>10.7</b>	<b>0.6</b>	<b>11.8</b>	<b>23.2</b>
Included within suspended interest account (Note 1)					5.2
					<b>28.4</b>

Provisions against non-performing loans at 31 December 2004 were £0.6 million (2003 : £0.6 million). The total of non-performing loans at 31 December 2004 was £118.6 million (2003 : £183.2 million).

During the year the Society recovered £0.8 million (2003 : £1.2 million) against amounts previously written off.

# Notes to the Accounts

for the year ended 31 December 2004

## 17. Investments

Investments in equity shares of subsidiary and associated undertakings are financial fixed assets.

Investments in subsidiary and associated undertakings:

	Shares £m	Loans £m	Total £m
<b>Society</b>			
Movements during the year are analysed as follows:			
At 1 January 2004	65.2	3,294.4	3,359.6
Additions	—	5,254.2	5,254.2
Repayments	—	(4,214.3)	(4,214.3)
<b>At 31 December 2004</b>	<b>65.2</b>	<b>4,334.3</b>	<b>4,399.5</b>

### Subsidiary undertakings

The Society has a direct interest in the ordinary share capital of the following principal subsidiary undertakings trading in the businesses indicated. All subsidiary undertakings are included in the consolidation.

Principal subsidiary undertakings which are wholly owned, registered in England and operating in the United Kingdom:

<b>Britannia Treasury Services Limited</b>	Mortgage and syndicated lending
<b>Britannia Development and Management Company Limited</b>	Property investment

Britannia Treasury Services Limited has the following wholly owned subsidiary undertakings, registered in England, operating in the United Kingdom, trading in the businesses indicated:

<b>Mortgage Agency Services Number One Limited</b>	Mortgage and syndicated lending
<b>Mortgage Agency Services Number Two Limited</b>	Mortgage lending
<b>Mortgage Agency Services Number Three Limited</b>	Bank account custodian
<b>Mortgage Agency Services Number Four Limited</b>	Mortgage lending
<b>Mortgage Agency Services Number Five Limited</b>	Mortgage lending
<b>Mortgage Agency Services Number Six Limited</b>	Mortgage lending
<b>Mortgage Agency Services Number Seven Limited</b>	Mortgage lending
<b>Western Mortgage Services Limited</b>	Mortgage book administration
<b>Platform Group Holdings Limited</b>	Holding company

Platform Group Holdings Limited has the following wholly owned subsidiary undertakings, registered in England, operating in the United Kingdom, trading in the businesses indicated:

<b>Platform Consumer Services Limited</b>	Mortgage lending
<b>Platform Funding Limited</b>	Mortgage origination
<b>Platform Funding No. 2 Limited</b>	Finance company
<b>Platform Funding No. 3 Limited</b>	Finance company
<b>Platform Funding No. 4 Limited</b>	Mortgage origination
<b>Platform Funding No. 5 Limited</b>	Mortgage origination
<b>Platform Funding No. 6 Limited</b>	Finance company
<b>Platform Home Loans Limited</b>	Mortgage origination and servicing
<b>Plum Sterling No. 1 PLC</b>	Mortgage lending

Platform Consumer Services Limited is the only direct subsidiary of Platform Group Holdings Limited.

Registered in the Isle of Man and operating overseas:

<b>Britannia International Limited</b>	Deposit taking
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Registered in Guernsey and operating overseas:

<b>Britsafe Insurance Services (Guernsey) Limited</b>	Mortgage insurance company
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Registered in Scotland and operating in the United Kingdom:

<b>Britannia Life Direct Limited</b>	Direct sales of financial services
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## 17. Investments (continued)

Subsidiary undertaking, registered in Scotland and operating in the United Kingdom, where the Society owns half the share capital represented by its holding of all the 'A' class ordinary shares and the majority of voting rights:

**Britannia New Homes (Scotland) Limited** Property development

### Joint ventures

The Society owns 49% of the shares in Britannia Personal Lending Limited and 50% of the shares in MutualPlus Limited, which are registered in England, operating in the United Kingdom, trading in the businesses indicated:

**Britannia Personal Lending Limited** Unsecured personal lending  
**MutualPlus Limited** Provision of branch sharing services

The total income of Britannia Personal Lending Limited for the year was £6.4 million (2003 : £6.5 million). The total income of MutualPlus Limited for the year was £0.2 million (2003 : £nil). The Society has 50% of the voting rights in the above joint ventures.

### Other directly held associated bodies

The Society has membership rights in Link Interchange Network Limited (LINK), a private limited company registered in England and Funds Transfer Sharing Limited (FTS), a private company registered in England limited by guarantee. LINK provides the Society and others with automated teller machine facilities operating throughout the United Kingdom. Both FTS and LINK are directly held associated bodies of the Society. Their results have been excluded from the accounts as, in the opinion of the Directors, they are not material.

### Quasi-subidiaries

The companies considered by the Directors to be quasi-subidiaries as defined in Financial Reporting Standard No. 5 (Reporting the substance of transactions) are set out below:

<b>Leek Finance Holdings Limited</b>	Holding company
<b>Leek Finance Number One PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Two Limited</b>	Holding company
<b>Leek Finance Number Two PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Three Limited</b>	Holding company
<b>Leek Finance Number Three PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Four Limited</b>	Holding company
<b>Leek Finance Number Four Limited</b>	Securitisation company
<b>Leek Finance Holdings Number Five Limited</b>	Holding company
<b>Leek Finance Number Five Limited</b>	Securitisation company
<b>Leek Finance Holdings Number Six Limited</b>	Holding company
<b>Leek Finance Number Six Limited</b>	Securitisation company
<b>Leek Finance Holdings Number Seven Limited</b>	Holding company
<b>Leek Finance Number Seven PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Eight Limited</b>	Holding company
<b>Leek Finance Number Eight Limited</b>	Securitisation company
<b>Leek Finance Holdings Number Nine Limited</b>	Holding company
<b>Leek Finance Number Nine Limited</b>	Securitisation company
<b>Leek Finance Holdings Number Ten Limited</b>	Holding company
<b>Leek Finance Number Ten PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Eleven Limited</b>	Holding company
<b>Leek Finance Number Eleven PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Twelve Limited</b>	Holding company
<b>Leek Finance Number Twelve PLC</b>	Securitisation company
<b>Leek Finance Holdings Number Fourteen Limited</b>	Holding company
<b>Leek Finance Number Fourteen PLC</b>	Securitisation company
<b>Meerbrook Finance Holdings Number One Limited</b>	Holding company
<b>Meerbrook Finance Number One Limited</b>	Securitisation company
<b>Meerbrook Finance Holdings Number Two Limited</b>	Holding company
<b>Meerbrook Finance Number Two Limited</b>	Securitisation company
<b>Rudyard Finance Holdings Number One Limited</b>	Holding company
<b>Rudyard Finance Number One PLC</b>	Securitisation company

The Society holds one non-voting share in Leek Finance Holdings Limited, representing 12.5% of the issued share capital.

## Notes to the Accounts

for the year ended 31 December 2004

### 17. Investments (continued)

In addition, the Directors consider the following companies to be quasi-subsiidiaries through its wholly owned subsidiary Platform Group Holdings Limited:

<b>Platform Home Loans Holdings Limited</b>	Holding company
<b>Platform Home Loans No. 1 PLC</b>	Securitisation company
<b>Platform Home Loans Holdings No. 2 Limited</b>	Holding company
<b>Platform Home Loans No. 2 PLC</b>	Securitisation company

The Society has no shareholding in any of the quasi-subsiidiaries listed above, other than its shareholding in Leek Finance Holdings Limited as disclosed above.

All quasi-subsiidiaries are registered in England and operate in the United Kingdom.

In addition to the above, the Society has interests in a number of minor subsidiary undertakings.

### 18. Intangible Fixed Assets

	Goodwill £m
<b>Group</b>	
Cost:	
At 1 January 2004	60.6
Acquired during the year	15.3
Disposal during the year	(0.1)
<b>At 31 December 2004</b>	<b>75.8</b>
Amortisation:	
At 1 January 2004	17.0
Charge for the year	
included in depreciation and amortisation	2.2
included in interest receivable and similar income	4.3
<b>At 31 December 2004</b>	<b>23.5</b>
Net book amount:	
<b>At 31 December 2004</b>	<b>52.3</b>
At 31 December 2003	43.6

A number of mortgage portfolios were acquired during the year for a cash consideration of £958.7 million and a provisional fair value (equal to book value) of £943.7 million.

Included in the amount acquired is £0.3 million of costs not included in the fair value.

During the year mortgages of £10.0 million acquired from Southern Pacific Mortgages Limited on 30 November 2003, were returned to the vendor for the cash consideration paid on acquisition.

## 19. Tangible Fixed Assets

	Land and buildings £m	Equipment, fixtures, fittings, computer equipment, software and vehicles £m	Total £m
<b>Group</b>			
Cost:			
At 1 January 2004	112.1	252.2	364.3
Additions during the year	3.7	22.9	26.6
Disposals during the year	(1.6)	(3.3)	(4.9)
<b>At 31 December 2004</b>	<b>114.2</b>	<b>271.8</b>	<b>386.0</b>
Depreciation:			
At 1 January 2004	57.3	172.5	229.8
Charge for the year	4.3	25.6	29.9
Disposals during the year	(0.3)	(1.9)	(2.2)
<b>At 31 December 2004</b>	<b>61.3</b>	<b>196.2</b>	<b>257.5</b>
Net book amount:			
<b>At 31 December 2004</b>	<b>52.9</b>	<b>75.6</b>	<b>128.5</b>
At 31 December 2003	54.8	79.7	134.5

The net book amount of land and buildings occupied by the Group for its own activities is £47.9 million (2003 : £51.2 million).

	Land and buildings £m	Equipment, fixtures, fittings, computer equipment, software and vehicles £m	Total £m
<b>Society</b>			
Cost:			
At 1 January 2004	95.5	244.5	340.0
Additions during the year	3.7	20.9	24.6
Disposals during the year	(1.5)	(3.0)	(4.5)
<b>At 31 December 2004</b>	<b>97.7</b>	<b>262.4</b>	<b>360.1</b>
Depreciation:			
At 1 January 2004	55.9	167.4	223.3
Charge for the year	4.1	23.5	27.6
Disposals during the year	(0.3)	(1.7)	(2.0)
<b>At 31 December 2004</b>	<b>59.7</b>	<b>189.2</b>	<b>248.9</b>
Net book amount:			
<b>At 31 December 2004</b>	<b>38.0</b>	<b>73.2</b>	<b>111.2</b>
At 31 December 2003	39.6	77.1	116.7

The net book amount of land and buildings occupied by the Society for its own activities is £33.3 million (2003 : £34.3 million).

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Net book amount of land and buildings is represented by:				
Freehold	49.5	50.3	34.9	35.5
Long leasehold	2.6	3.5	2.3	3.2
Short leasehold	0.8	1.0	0.8	0.9
	<b>52.9</b>	54.8	<b>38.0</b>	39.6

## Notes to the Accounts

for the year ended 31 December 2004

### 20. Prepayments and Accrued Income

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Accrued interest relating to off balance sheet instruments	82.5	74.5	78.1	72.3
Prepayment to defined benefit pension scheme (in accordance with Statement of Standard Accounting Practice No. 24) (see Note 9)	76.6	44.0	76.6	44.0
Other	23.6	12.8	14.4	8.0
	<b>182.7</b>	<b>131.3</b>	<b>169.1</b>	<b>124.3</b>

### 21. Shares

	Group and Society 2004 £m	Group and Society 2003 £m
Held by individuals	11,798.8	11,103.6

Shares are repayable from the balance sheet date in the ordinary course of business as follows:

	Group and Society 2004 £m	Group and Society 2003 £m
Accrued interest	292.8	255.0
Repayable on demand	9,314.2	9,589.4
Other shares by residual maturity repayable		
In not more than three months	353.5	143.9
In more than three months but not more than one year	820.3	837.4
In more than one year but not more than five years	1,018.0	277.9
	<b>11,798.8</b>	<b>11,103.6</b>

### 22. Amounts Owed to Credit Institutions

Amounts owed to credit institutions are repayable from the balance sheet date in the ordinary course of business as follows:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Accrued interest	17.1	14.6	17.0	14.2
Repayable on demand	29.5	42.5	28.0	36.8
Other amounts owed to credit institutions by residual maturity repayable				
In not more than three months	1,059.3	616.5	1,059.2	615.5
In more than three months but not more than one year	43.7	16.0	43.4	15.5
In more than one year but not more than five years	71.5	70.1	70.0	67.0
In more than five years	7.8	6.4	—	4.5
	<b>1,228.9</b>	<b>766.1</b>	<b>1,217.6</b>	<b>753.5</b>

Amounts owed to credit institutions include £264.2 million (2003 : £76.9 million) in respect of sale and repurchase agreements.

### 23. Amounts Owed to Other Customers

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Amounts owed to subsidiary undertakings	—	—	<b>1,353.9</b>	1,182.2
Other	<b>2,653.5</b>	2,598.5	<b>1,528.1</b>	1,585.0
	<b>2,653.5</b>	2,598.5	<b>2,882.0</b>	2,767.2

Amounts owed to other customers are repayable from the balance sheet date in the ordinary course of business as follows:

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Accrued interest	<b>42.4</b>	36.1	<b>9.6</b>	6.1
Repayable on demand	<b>367.7</b>	396.6	<b>1,400.8</b>	1,239.5
Other amounts owed to other customers by residual maturity repayable				
In not more than three months	<b>1,729.9</b>	1,861.6	<b>1,177.5</b>	1,309.3
In more than three months but not more than one year	<b>363.3</b>	192.7	<b>232.6</b>	185.3
In more than one year but not more than five years	<b>141.5</b>	108.6	<b>61.5</b>	27.0
In more than five years	<b>8.7</b>	2.9	—	—
	<b>2,653.5</b>	2,598.5	<b>2,882.0</b>	2,767.2

### 24. Debt Securities in Issue

	Group and Society 2004 £m	Group and Society 2003 £m
Certificates of deposit	<b>1,137.9</b>	817.9
Fixed and floating rate notes	<b>1,963.1</b>	1,752.9
Other debt securities	<b>2,464.6</b>	2,137.5
	<b>5,565.6</b>	4,708.3

Debt securities in issue are repayable from the balance sheet date in the ordinary course of business as follows:

	Group and Society 2004 £m	Group and Society 2003 £m
Accrued interest	<b>34.7</b>	24.2
Debt securities in issue by residual maturity repayable		
In not more than one year	<b>3,725.5</b>	3,043.3
In more than one year but not more than five years	<b>1,763.8</b>	1,640.8
In more than five years	<b>41.6</b>	—
	<b>5,565.6</b>	4,708.3

## Notes to the Accounts

for the year ended 31 December 2004

### 25. Other Liabilities

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Amounts falling due within one year				
Income tax	2.5	1.0	2.4	0.8
Corporation tax	25.0	18.2	—	—
Other creditors	67.4	74.5	61.7	65.6
	<b>94.9</b>	93.7	<b>64.1</b>	66.4
Amounts falling due in more than one year				
Other creditors	98.8	64.6	—	—
	<b>193.7</b>	158.3	<b>64.1</b>	66.4

Other creditors for the Group and Society include £42.1 million (2003 : £42.0 million) in respect of the Britannia Membership Reward for the year.

### 26. Accruals and Deferred Income

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Accruals relating to off balance sheet instruments	50.0	68.7	50.0	68.7
Interest accrued on subordinated liabilities	5.5	4.5	5.5	4.5
Interest accrued on subscribed capital	6.0	6.0	6.0	6.0
Other	41.1	48.2	38.6	32.8
	<b>102.6</b>	127.4	<b>100.1</b>	112.0

Other accruals for the Group include £1.0 million (2003 : £13.9 million) in respect of high loan to value advance premiums received. Following an actuarial review in 2004, the Group accelerated the release to profit of these premiums and £9.7 million (2003 : £3.0 million) was released to other operating income.

### 27. Provisions for Liabilities and Charges

	Deferred taxation £m	Other £m	Total £m
<b>Group</b>			
At 1 January 2004	2.6	11.3	13.9
Amounts provided during the year	10.4	10.5	20.9
Amounts paid/utilised during the year	—	(4.4)	(4.4)
<b>At 31 December 2004</b>	<b>13.0</b>	<b>17.4</b>	<b>30.4</b>
<b>Society</b>			
At 1 January 2004	5.1	8.9	14.0
Amounts provided during the year	7.4	10.9	18.3
Amounts paid/utilised during the year	—	(4.1)	(4.1)
<b>At 31 December 2004</b>	<b>12.5</b>	<b>15.7</b>	<b>28.2</b>

Other provisions for liabilities and charges consist primarily of a provision against various potential claims on endowment policies. The amount provided during the year was charged to fees and commissions receivable.

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
The amount provided for deferred tax, which represents a full potential deferred tax liability, comprises:				
Accelerated capital allowances	2.5	3.3	1.1	1.6
Other timing differences	10.5	(0.7)	11.4	3.5
	<b>13.0</b>	2.6	<b>12.5</b>	5.1

## 28. Subordinated Liabilities

	Group and Society 2004 £m	Group and Society 2003 £m
Fixed rate subordinated notes 2011	99.8	99.7
Fixed rate subordinated notes 2024	200.0	—
Fixed rate subordinated notes 2033	147.9	147.8
	<b>447.7</b>	<b>247.5</b>

On a winding up, the claims of the noteholders are subordinated in right of payment to depositors and other creditors, and those holding shares where the Society remains a building society. Interest is payable on the 2011 fixed notes at 8.875%, on the 2024 fixed notes at 5.75% and on the 2033 fixed notes at 5.875%. The fixed rate notes are repayable at the Society's option and with the prior consent of the Financial Services Authority, on any interest date within five years of the maturity date.

## 29. Subscribed Capital

	Group and Society 2004 £m	Group and Society 2003 £m
Permanent interest bearing shares	110.0	110.0

Interest is paid in arrears at the rate of 13% pa in half yearly instalments. The shares are repayable only in the event of a winding up of the Society or otherwise with the consent of the Financial Services Authority. Interest may not be paid or credited under certain circumstances. In a winding up or dissolution of the Society the claims of the holders of permanent interest bearing shares would rank behind all other creditors of the Society and the claims of Members holding shares as to principal and interest. The holders of permanent interest bearing shares are not entitled to any share in any final surplus upon a winding up or final dissolution of the Society.

The non-equity interest of the Group and Society comprises permanent interest bearing shares of £110.0 million (2003 : £110.0 million) and the share premium thereon of £3.1 million (2003 : £3.1 million).

## 30. Reserves

	Share premium £m	General reserve £m
<b>Group</b>		
At 1 January 2004	3.1	1,092.1
Profit for the financial year	—	71.4
<b>At 31 December 2004</b>	<b>3.1</b>	<b>1,163.5</b>
<b>Society</b>		
At 1 January 2004	3.1	978.9
Profit for the financial year	—	34.5
<b>At 31 December 2004</b>	<b>3.1</b>	<b>1,013.4</b>

The cumulative amount of goodwill, resulting from acquisitions, after making deductions for disposals, which has been written off to Group general reserve is £59.5 million (2003 : £59.5 million), Society £nil (2003 : £nil).

# Notes to the Accounts

for the year ended 31 December 2004

## 31. Memorandum Items

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Commitments				
Irrevocable undrawn loan facilities	405.8	464.5	321.2	367.8
Undrawn formal standby facilities, credit lines and other commitments to lend greater than one year	48.8	43.3	48.8	43.3
	<b>454.6</b>	<b>507.8</b>	<b>370.0</b>	<b>411.1</b>
Credit risk weighted amount	<b>125.8</b>	<b>137.8</b>	<b>104.7</b>	<b>113.6</b>

## 32. Financial Commitments

### Contingent liabilities

In common with other financial institutions, the Society has a contingent liability in respect of contributions to the Financial Services Compensation Scheme. The Society has not been notified of any claims against the Scheme.

### Capital commitments for which no provision has been made in the accounts

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Capital expenditure contracted for but not provided in the accounts	0.9	1.9	0.8	1.9

### Commitments under operating leases

At the balance sheet date, annual commitments under operating leases relating to land and buildings, and equipment were as follows:

	Land and buildings 2004 £m	Land and buildings 2003 £m	Equipment 2004 £m	Equipment 2003 £m
<b>Group</b>				
Leases which expire				
In not more than one year	0.1	0.2	0.2	0.1
In more than one year but not more than five years	1.6	2.1	0.5	0.3
In more than five years	5.6	5.3	—	—
	<b>7.3</b>	<b>7.6</b>	<b>0.7</b>	<b>0.4</b>
<b>Society</b>				
Leases which expire				
In not more than one year	0.1	0.1	0.1	0.1
In more than one year but not more than five years	1.0	0.8	0.2	0.3
In more than five years	4.6	4.5	—	—
	<b>5.7</b>	<b>5.4</b>	<b>0.3</b>	<b>0.4</b>

### 33. Consolidated Cash Flow Statement

#### Reconciliation of operating profit to net cash inflow from operating activities

	2004 £m	2003 £m
Operating profit after provisions and Britannia Membership Reward	98.3	92.3
Increase in prepayments and accrued income	(60.6)	(32.0)
Increase in accruals and deferred income	31.4	23.4
Provisions for bad and doubtful debts	6.1	11.4
Transfer of free mortgage indemnity guarantee insurance to provisions for bad and doubtful debts	1.2	2.8
Loans and advances written off, net of recoveries	(1.8)	(0.5)
Amortisation	6.5	4.3
Depreciation	29.9	26.4
Interest on subscribed capital	14.3	14.3
Interest on subordinated liabilities	23.0	12.9
Profit on sale of tangible fixed assets	(0.8)	(1.1)
Increase in provisions for liabilities and charges	6.1	2.5
<b>Net cash inflow from trading activities</b>	<b>153.6</b>	<b>156.7</b>
Net increase in loans and advances to customers	(1,598.9)	(1,395.1)
Net increase in shares	657.4	709.4
Net increase in amounts owed to credit institutions and other customers	509.0	65.7
Net increase in debt securities in issue	846.8	1,482.0
Net increase in loans and advances to credit institutions	(131.2)	(204.2)
Net decrease in value of joint ventures	0.2	—
Net (increase)/decrease in other assets	(13.9)	0.8
Net increase in intangible fixed assets	(15.2)	(4.4)
Net increase/(decrease) in other liabilities	28.6	(94.7)
<b>Net cash inflow from operating activities</b>	<b>436.4</b>	<b>716.2</b>

#### Analysis of changes in financing during the year

	Subscribed capital £m	Subordinated liabilities £m
At 1 January 2004	110.0	247.5
Issue of subordinated liabilities	—	200.0
Amortisation of deferred issue costs	—	0.2
<b>At 31 December 2004</b>	<b>110.0</b>	<b>447.7</b>

#### Analysis of the balances of cash as shown in the balance sheet

	2003 £m	Flows £m	2004 £m
Cash in hand and balances with the Bank of England	35.4	(4.6)	30.8
Loans and advances to credit institutions repayable on demand	17.4	1.2	18.6
	52.8	(3.4)	49.4

# Notes to the Accounts

for the year ended 31 December 2004

## 34. Financial Instruments

A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability of another entity. Britannia is a retailer of financial instruments, mainly in the form of mortgages, savings and insurance products. The Group uses wholesale financial instruments to invest liquid asset balances and raise wholesale funding, and to manage the risks arising from its operations.

The Group has a formal structure for managing risk, including established risk limits, reporting lines, mandates and other control procedures. This structure is reviewed regularly by the Assets and Liabilities Committee (ALCO), which is charged with the responsibility for managing and controlling the balance sheet exposures of the Group. A report of all ALCO meetings is made to the Board.

Instruments used for risk management purposes include derivative financial instruments (derivatives), which are contracts or agreements whose value is derived from one or more underlying price, rate or index inherent in the contract or agreement, such as interest rates, exchange rates or stock market indices.

Derivatives are only used by the Group in accordance with the Building Societies Act 1986, to limit the extent to which the Group will be affected by changes in interest rates, exchange rates or other factors specified in the legislation.

Derivatives are not used in trading activity or for speculative purposes.

### Types of derivatives

The principal derivatives used in balance sheet risk management are interest rate swaps, interest rate options, cross currency interest rate swaps and foreign exchange contracts, which are used to hedge Group balance sheet exposures arising from fixed rate mortgage lending and savings products, funding and investment activities.

The following table describes the significant activities undertaken by the Group, the related risks associated with such activities and the types of derivatives which are typically used in managing such risks. Such risks may alternatively be managed using on balance sheet instruments as part of an integrated approach to risk management.

Activity	Risk	Type of hedge
Management of the investment of reserves and other net non-interest bearing liabilities	Sensitivity to changes in interest rates	Interest rate swaps
Fixed rate savings products and fixed rate funding	Sensitivity to falls in interest rates	Receive fixed interest rate swaps
Fixed rate mortgage lending and fixed rate investments	Sensitivity to increases in interest rates	Pay fixed interest rate swaps
Investment and funding in foreign currencies	Sensitivity to changes in foreign exchange rates	Cross currency interest rate swaps and foreign exchange contracts
Equity linked investment products	Sensitivity to changes in equity indices	Equity linked futures and interest rate swaps

Derivative products which are combinations of more basic derivatives are used only in circumstances where the underlying position being hedged contains the same risk features. For example, guaranteed equity bonds issued by the Group may be hedged with a single contract incorporating both the interest rate and equity index risk incurred. In such cases the derivatives used will be designed to match exactly the risks of the underlying asset or liability. Exposure to market risk on such contracts is therefore fully hedged.

### Control of derivatives

The Board has authorised the use of derivatives in accordance with the Building Societies Act 1986 and sets a prudential limit for the Group on the amount of derivatives outstanding at any one time. All other limits over the use of derivative products are the responsibility of ALCO with the exception of the monitoring and review of lending exposures arising in all aspects of the Group's operations which is the responsibility of the Credit Committee, which works within Board approved Group credit policies.

All exchange-traded instruments are subject to cash requirements under the standard margin arrangements applied by the individual exchanges. Other derivatives contracts are not subject to the cash requirements. The accounting policies for derivatives are described in the Statement of Accounting Policies on pages 27 to 29.

### 34. Financial Instruments (continued)

The table below analyses the derivatives by type of contract and maturity and shows the nominal principal amounts, credit risk weighted amount and replacement costs of contracts. Nominal principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The replacement cost represents the cost of replacing contracts with positive values, calculated at market rates current at the balance sheet date reflecting the Group's exposure should the counterparties default. The credit risk weighted amount, which is calculated according to rules specified by the Financial Services Authority, is based on the replacement cost, but also takes into account measures of the extent of potential future exposure and the nature of the counterparty.

	Nominal principal amount 2004 £m	Credit risk weighted amount 2004 £m	Replacement cost 2004 £m	Nominal principal amount 2003 £m	Credit risk weighted amount 2003 £m	Replacement cost 2003 £m
<b>Group and Society</b>						
Exchange rate contracts						
Cross currency interest rate swaps	1,089.1	2.9	3.7	904.9	2.8	4.7
Forward foreign exchange	323.7	6.9	18.5	438.7	8.6	21.0
	<b>1,412.8</b>	<b>9.8</b>	<b>22.2</b>	<b>1,343.6</b>	<b>11.4</b>	<b>25.7</b>
Under one year	1,089.1	2.9	3.7	904.9	2.8	4.7
Between one and five years	323.7	6.9	18.5	438.7	8.6	21.0
	<b>1,412.8</b>	<b>9.8</b>	<b>22.2</b>	<b>1,343.6</b>	<b>11.4</b>	<b>25.7</b>
Interest rate contracts						
Interest rate swaps	11,330.1	32.4	104.6	11,278.3	32.9	111.5
Forward rate agreements	230.0	0.2	0.2	400.0	0.2	—
Futures (exchange traded)	—	—	—	200.0	—	—
Caps, collars and floors	100.3	0.2	0.3	298.0	0.2	0.5
	<b>11,660.4</b>	<b>32.8</b>	<b>105.1</b>	<b>12,176.3</b>	<b>33.3</b>	<b>112.0</b>
Under one year	3,919.8	5.8	29.0	4,074.7	4.8	23.9
Between one and five years	5,729.7	18.2	62.5	6,678.3	22.2	77.7
Over five years	2,010.9	8.8	13.6	1,423.3	6.3	10.4
	<b>11,660.4</b>	<b>32.8</b>	<b>105.1</b>	<b>12,176.3</b>	<b>33.3</b>	<b>112.0</b>
Equity contracts						
Under one year	3.2	—	—	89.1	1.1	—
Between one and five years	263.6	7.4	15.8	207.5	5.1	9.1
Over five years	25.7	0.5	—	2.9	0.1	—
	<b>292.5</b>	<b>7.9</b>	<b>15.8</b>	<b>299.5</b>	<b>6.3</b>	<b>9.1</b>

All of the Group's derivatives activity is contracted with OECD financial institutions.

The material financial risks faced by the Group include credit risk, liquidity risk, interest rate risk and currency rate risk.

#### Credit risk

Credit risk is the risk that counterparties will not be able to meet their obligations as they fall due. The Credit Committee is responsible for approving and monitoring the Group's credit exposures for lending which it does through reviewing and approving the Group's lending policy and credit scoring systems and through setting limits on credit exposures to individual counterparties and industrial sectors. The ALCO is responsible for approving limits on Treasury counterparties and country exposures.

#### Liquidity risk

The Group's liquidity policy is to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding, to retain full public confidence in the solvency of the Group and to enable the Group to meet its financial obligations. This is achieved through maintaining a prudent level of liquid assets, through wholesale funding facilities and through management control of the growth of the business.

# Notes to the Accounts

for the year ended 31 December 2004

## 34. Financial Instruments (continued)

### Interest rate risk

The Group is exposed to movements in interest rates, and manages this exposure on a continuous basis, within limits set by the Board, using a combination of on and off balance sheet instruments. The Group monitors risk daily using a Risk Management system and operates within limits set down by ALCO. The Group adopts a prudent approach to risk management, monitored by the Financial Services Authority and uses a varied amount of on and off balance sheet instruments to limit the Group's exposure to market risk. After taking into account the various derivatives entered into by the Group, the interest rate sensitivity exposure of the Group was:

	Not more than three months £m	More than three months but not more than six months £m	More than six months but not more than one year £m	More than one year but not more than five years £m	More than five years £m	Non-interest bearing £m	Total £m
<b>At 31 December 2004</b>							
<b>Assets</b>							
Liquid assets	6,121.8	148.7	164.7	191.6	2.5	38.2	6,667.5
Loans fully secured on residential property and other loans	9,689.8	477.3	1,370.7	2,812.9	1,854.1	5.5	16,210.3
Tangible and intangible fixed assets	—	—	—	—	—	180.8	180.8
Other assets	—	—	—	—	—	239.2	239.2
<b>Total assets</b>	<b>15,811.6</b>	<b>626.0</b>	<b>1,535.4</b>	<b>3,004.5</b>	<b>1,856.6</b>	<b>463.7</b>	<b>23,297.8</b>
<b>Liabilities</b>							
Shares	10,361.5	216.7	282.0	642.9	2.9	292.8	11,798.8
Amounts owed to credit institutions, other customers and debt securities in issue	7,902.0	458.1	272.2	704.6	3.3	107.8	9,448.0
Other liabilities	—	—	—	—	—	326.7	326.7
Subordinated liabilities and subscribed capital	—	—	—	99.8	457.9	—	557.7
Reserves	—	—	—	—	—	1,166.6	1,166.6
<b>Total liabilities</b>	<b>18,263.5</b>	<b>674.8</b>	<b>554.2</b>	<b>1,447.3</b>	<b>464.1</b>	<b>1,893.9</b>	<b>23,297.8</b>
Off balance sheet items	1,260.3	466.3	(330.8)	(77.9)	(1,317.9)	—	—
<b>Interest rate sensitivity gap</b>	<b>(1,191.6)</b>	<b>417.5</b>	<b>650.4</b>	<b>1,479.3</b>	<b>74.6</b>	<b>(1,430.2)</b>	<b>—</b>
<b>At 31 December 2003</b>							
<b>Assets</b>							
Liquid assets	5,408.9	73.8	183.9	225.4	2.8	64.9	5,959.7
Loans fully secured on residential property and other loans	9,752.5	292.3	514.7	3,036.5	1,015.5	5.4	14,616.9
Tangible and intangible fixed assets	—	—	—	—	—	178.1	178.1
Other assets	—	—	—	—	—	174.1	174.1
<b>Total assets</b>	<b>15,161.4</b>	<b>366.1</b>	<b>698.6</b>	<b>3,261.9</b>	<b>1,018.3</b>	<b>422.5</b>	<b>20,928.8</b>
<b>Liabilities</b>							
Shares	9,704.1	216.7	282.0	642.9	2.9	255.0	11,103.6
Amounts owed to credit institutions, other customers and debt securities in issue	7,313.0	90.9	210.0	407.1	7.4	44.5	8,072.9
Other liabilities	—	—	—	—	—	299.6	299.6
Subordinated liabilities and subscribed capital	—	—	—	99.7	257.8	—	357.5
Reserves	—	—	—	—	—	1,095.2	1,095.2
<b>Total liabilities</b>	<b>17,017.1</b>	<b>307.6</b>	<b>492.0</b>	<b>1,149.7</b>	<b>268.1</b>	<b>1,694.3</b>	<b>20,928.8</b>
Off balance sheet items	(846.3)	1,055.9	1,744.7	(520.1)	(1,434.2)	—	—
<b>Interest rate sensitivity gap</b>	<b>(2,702.0)</b>	<b>1,114.4</b>	<b>1,951.3</b>	<b>1,592.1</b>	<b>(684.0)</b>	<b>(1,271.8)</b>	<b>—</b>

Liquid assets comprise cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.

Other assets comprise investments, other assets and prepayments and accrued income.

Other liabilities comprise other liabilities, accruals and deferred income and provisions for liabilities and charges.

### 34. Financial Instruments (continued)

#### Currency rate risk

The Group has no significant net exposure to foreign exchange rate fluctuations or changes in foreign currency interest rates.

#### Hedges of transactions

The Society will hedge fixed rate savings products and fixed rate mortgage products based on the impact of these products on the overall balance sheet position and net interest margin. Products relating to specific markets such as equity linked growth bonds are hedged specifically based on the expected sales levels. Foreign currency transactions are hedged at the time of the transaction which removes the Group's foreign currency exposure.

#### Fair values of financial instruments

Set out below is a comparison of book and fair values of some of the Group's financial instruments by category as at 31 December 2004. Where available, market values have been used to determine fair values. Where market values are not available, fair values have been calculated for options by using option-pricing models and for other financial instruments by discounting cash flows at prevailing interest and exchange rates.

The table excludes certain financial assets and liabilities which are not listed or publicly traded, or for which a liquid and active market does not exist. It therefore excludes mortgages, retail savings accounts and other balance sheet items. Book and fair values of those items would differ at 31 December 2004.

	Book value 2004 £m	Fair value 2004 £m	Book value 2003 £m	Fair value 2003 £m
<b>Assets/(liabilities)</b>				
On balance sheet instruments				
Liquid assets	6,667.5	6,671.3	5,959.7	5,979.8
Wholesale liabilities	(9,448.0)	(9,474.4)	(8,072.9)	(8,120.2)
Subordinated liabilities	(447.7)	(475.7)	(247.5)	(269.7)
Subscribed capital	(110.0)	(230.6)	(110.0)	(202.2)
Off balance sheet and similar instruments	27.3	(45.0)	5.4	(118.7)

Liquid assets comprise cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.

Wholesale liabilities comprise certain financial liabilities reported within amounts owed to credit institutions, amounts owed to other customers and debt securities in issue for which an active and liquid market exists.

Off balance sheet and similar instruments comprise derivative instruments used to hedge liquid assets and wholesale liabilities.

Gains and losses on hedges carried forward in the balance sheet as at 31 December 2004 are as follows:

	Gains £m	Losses £m	Net gain/ (loss) £m
Gains/(losses) carried forward in the balance sheet at 31 December 2003	—	(0.4)	(0.4)
Gains/(losses) arising in the year to 31 December 2004	—	(0.4)	(0.4)
<b>Gains/(losses) carried forward in the balance sheet at 31 December 2004</b>	<b>—</b>	<b>(0.8)</b>	<b>(0.8)</b>
Of which expected to be recognised in the year to 31 December 2005	—	(0.2)	(0.2)

The Group pays/receives a premium relating to certain types of derivatives which are amortised in line with the underlying assets/liabilities. The cost/income from these derivatives is fully reflected in the pricing of the Group's products.

# Notes to the Accounts

for the year ended 31 December 2004

## 34. Financial Instruments (continued)

Unrecognised gains and losses on hedges are as follows:

	Gains £m	Losses £m	Net gain/ (loss) £m
Unrecognised gains/(losses) on hedges at 31 December 2003	92.8	(216.9)	(124.1)
Of which recognised in the year to 31 December 2004	10.9	(41.1)	(30.2)
Gains/(losses) before 31 December 2003 that were not recognised in the year to 31 December 2004	81.9	(175.8)	(93.9)
Gains/(losses) arising in the year to 31 December 2004 that were not recognised in that year	6.0	(55.1)	(49.1)
<b>Unrecognised gains/(losses) on hedges at 31 December 2004</b>	<b>87.9</b>	<b>(230.9)</b>	<b>(143.0)</b>
Of which expected to be recognised in the year to 31 December 2005	13.0	(45.9)	(33.0)

The Group enters into derivative contracts to reduce the Group's overall exposure to interest rate/currency risk. The gains/(losses) on derivatives shown within this note are generally matched by equal and opposite unrecognised gains/(losses) from on balance sheet positions.

Gains/(losses) recognised within the year to 31 December 2004, consist of maturing contracts and a reduction in gain/(loss) on those contracts during 2004 to a maximum of that reported as at 31 December 2003.

Gains/(losses) arising during the year consist of new deals and any increase in the gain/(loss) for the year from that reported as at 31 December 2003.

The amount to be recognised in the year to 31 December 2005 relates to maturing contracts.

## 35. Non-sterling Assets and Liabilities

The aggregate amount of assets and liabilities included in the balance sheet denominated in a currency other than sterling was as follows:

	Group and Society 2004 £m	Group and Society 2003 £m
Assets	<b>1,778.5</b>	1,689.0
Liabilities	<b>3,053.8</b>	2,632.0

The Group's non-sterling assets and liabilities are hedged on balance sheet or by using derivatives to eliminate material currency exposures.

## 36. Directors' Loans and Related Party Transactions

	Society 2004 £000	Society 2003 £000
Investments and deposits held by 11 Directors (2003 : 10 Directors)	<b>909</b>	1,262
Loans outstanding to 5 Directors (2003 : 5 Directors)	<b>1,188</b>	1,214

A register is maintained by the Society containing details of loans, transactions and arrangements made between the Society or its subsidiary companies and Directors of the Society or persons connected with Directors of the Society.

The register will be available for inspection by Members at the Annual General Meeting and during normal office hours at the Society's Principal Office (Britannia House, Leek, Staffordshire) during the period of 15 days prior to the meeting.

The Society has taken advantage of the exemption in Financial Reporting Standard No. 8 (Related party disclosures) and does not therefore disclose transactions with wholly owned subsidiaries.

The Directors consider the following companies to be related parties of the Society and therefore under Financial Reporting Standard No. 8 (Related party disclosures) transactions between the Society and these companies require disclosure.

### **36. Directors' Loans and Related Party Transactions (continued)**

#### **Britannic plc and its subsidiaries**

A Society subsidiary, Britannia Life Direct Limited is an agent of the Britannic Marketing Group and received commissions of £4.8 million during the year (2003 : £6.3 million) in relation to sales of unit trusts, PEPs and ISAs. At 31 December 2004, Britannic plc owed £0.8 million to Britannia Life Direct Limited (2003 : £0.7 million).

#### **Liverpool Victoria**

During 2004, a Society subsidiary, Britannia Life Direct Limited, was an agent of Liverpool Victoria. In the year to 31 December 2004, Britannia Life Direct Limited received commissions of £3.3 million in relation to the sales of personal life and health insurance (2003 : £2.0 million). At 31 December 2004, Liverpool Victoria owed £1.4 million to Britannia Life Direct Limited (2003 : £1.1 million).

#### **Britannia Personal Lending Limited (BPL)**

BPL is a joint venture company and paid commissions to the Society of £0.1 million during the year (2003 : £0.2 million). There were no material balances outstanding between the parties at the year end.

#### **MutualPlus Limited**

MutualPlus Limited is a joint venture company created in 2002. At 31 December 2004 it owed £0.1 million to the Society (2003 : £0.1 million).

# Annual Business Statement

## 1. Statutory Percentages

	2004 %	Statutory Limit %
Proportion of business assets not in the form of loans fully secured on residential property (the 'lending limit')	<b>10.0</b>	<b>25.0</b>
Proportion of shares and borrowings not in the form of shares held by individuals (the 'funding limit')	<b>44.5</b>	<b>50.0</b>

The above percentages have been calculated in accordance with, and the statutory limits are those prescribed by, Sections 6 and 7 of the Building Societies Act 1986 as amended by the Building Societies Act 1997.

- Business assets are the total assets of the Group as shown in the balance sheet, **plus** provisions for bad and doubtful debts, **less** fixed assets and liquid assets.
- Loans fully secured on residential property are the amount of principal owing by borrowers and interest accrued not yet payable. This is the amount shown in the balance sheet, **plus** provisions for bad debts, **less** unamortised premiums on the acquisition of loans.
- Shares and borrowings represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue.

## 2. Other Percentages

	2004 %	2003 %
As a percentage of shares and borrowings:		
Gross capital	<b>8.1</b>	7.6
Free capital	<b>7.5</b>	6.9
Liquid assets	<b>31.4</b>	31.1
Profit after taxation as a percentage of mean total assets	<b>0.32</b>	0.33
Management expenses as a percentage of mean total assets	<b>0.84</b>	0.87

The above percentages have been prepared from the Society's consolidated accounts and in particular:

- 'Gross capital' represents the aggregate of general reserve, subordinated liabilities and subscribed capital;
- 'Free capital' represents the aggregate of gross capital and general loss provisions for bad and doubtful debts less tangible and intangible fixed assets;
- 'Liquid assets' represent the total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities;
- 'Mean total assets' represent the amount produced by halving the aggregate of total assets at the beginning and end of the financial year;
- 'Management expenses' represent the aggregate of administrative expenses, depreciation and amortisation.

### 3. Directors' Responsibilities

#### DIRECTORS

Name and Date of Birth	Business Occupation and Other Directorships	Date of Appointment as a Director of the Society
<b>I C Adam, CA</b> 2.9.1943	Company Director  Member of the Scottish Higher Education Funding Council	22.6.1998
<b>W J Gordon, FCIB</b> 24.4.1939	Company Director  Britannia Treasury Services Limited	22.9.1999
<b>F R Gugen, FCA</b> 26.2.1949	Company Director  CH4 Energy Limited CH4 Limited CH4 Pipelines Limited Echo Petroleum Limited Gugen Consulting Limited Island Gas Limited PermaGas Limited Petroleum Geo-Services ASA StrataGas PLC StrataGas CBM Limited	17.12.2003
<b>G A Gregory, BA, MA</b> 26.4.1955	Building Society Executive Director  Britannia Building Society Land and Development Company (Midlands) Limited Britannia Development and Management Limited Britannia Independent Limited Britannia International Limited Britannia Lending Company Limited Britannia New Homes Limited Britannia Treasury Services Limited Britannia Asset Management Limited Mortgage Agency Services Number One Limited Mortgage Agency Services Number Two Limited Mortgage Agency Services Number Three Limited Mortgage Agency Services Number Four Limited Mortgage Agency Services Number Five Limited Mortgage Agency Services Number Six Limited Mortgage Agency Services Number Seven Limited PCSL Services No. 1 Limited PCSL Services No. 2 Limited Platform Consumer Services Limited Platform Group Holdings Limited Platform Funding Limited Platform Funding No. 2 Limited Platform Funding No. 3 Limited Platform Funding No. 4 Limited Platform Funding No. 5 Limited Platform Funding No. 6 Limited Platform Home Loans Limited Verso Limited Western Mortgage Services Limited School Governor - St Peter and St Paul Trust	22.9.1999

## Annual Business Statement contd.

### 3. Directors' Responsibilities (continued)

#### DIRECTORS

Name and Date of Birth	Business Occupation and Other Directorships	Date of Appointment as a Director of the Society
<b>C Jones, LLB</b> 23.2.1953	Solicitor and Company Director  Agenda Management Services Limited	7.5.2003
<b>H M Keays, BA</b> 26.3.1964	Company Director  Chrysalis Group PLC	1.10.2004
<b>P A Lee, BSc, CIPFA, CA</b> 25.5.1955	Building Society Executive Director  Britannia Asset Management Limited Britannia Building Society Estate Agents Limited Britannia Building Society Land and Development Company (Midlands) Limited Britannia Conveyancing Services Limited Britannia Development and Management Limited Britannia Estate Agents Limited Britannia Estate Agents (London) Limited Britannia Independent Limited Britannia (Isle of Man) Limited Britannia LAS Direct Limited Britannia Lending Company Limited Britannia Life Direct Limited Britannia Motor Insurances Limited Britannia New Homes Limited Britannia Overseas Limited Britannia Pension Investment Limited Britannia Shield Conveyancing Services Limited Britannia Shield Financial Services Limited Britannia Shield Property Services Limited Britannia Treasury Services Limited Findprior Limited Mornington Information Technology Services Limited Mortgage Agency Services Number One Limited Mortgage Agency Services Number Two Limited Mortgage Agency Services Number Four Limited Mortgage Agency Services Number Five Limited Mortgage Agency Services Number Six Limited Mortgage Agency Services Number Seven Limited PCSL Services No. 1 Limited PCSL Services No. 2 Limited Platform Consumer Services Limited Platform Funding Limited Platform Funding No. 2 Limited Platform Funding No. 3 Limited Platform Funding No. 4 Limited Platform Funding No. 5 Limited Platform Funding No. 6 Limited Platform Group Holdings Limited Platform Home Loans Limited Plum Sterling Number 1 PLC The Mortgage Agency PLC Verso Limited Western Mortgage Services Limited	1.9.2002

### 3. Directors' Responsibilities (continued)

#### DIRECTORS

Name and Date of Birth	Business Occupation and Other Directorships	Date of Appointment as a Director of the Society
<b>N B Richardson, BA, FCA</b> 2.6.1957	Building Society Executive Director  Britannia Treasury Services Limited Communicate Mutuality Limited	28.9.1998
<b>B C Rosewell, MA, MPhil</b> 19.9.1951	Economist  Department for Work and Pensions The Environment Business Limited Volterra Consulting Limited	28.7.1999
<b>L Sawyer</b> 12.5.1943	Member of the House of Lords Management and Training Consultant  Investors in People UK	28.7.1999
<b>E Walmsley, BSc, PhD, MBA</b> 28.2.1953	Company Director  Change Partnership Sheffield University Enterprises Limited White Rose Technology Limited	13.3.2000

Documents may be served on the above named Directors at the following address: Howsons, 50 Broad Street, Leek, Staffordshire Moorlands, ST13 5NS.

#### OFFICERS

	Business Occupation and Directorships
<b>P M Buckley, BSc</b>	Head of Direct Channels and Affinity  Britannia Personal Lending Limited
<b>I M Dale, ACA</b>	Head of Group Finance  Britsafe Insurance Services (Guernsey) Limited Verso Limited
<b>M A Ellison, BA, MA</b>	Head of Information Systems
<b>D Facci</b>	Acting Head of Marketing
<b>T A Franklin, ACIB</b>	Managing Director of Member Business  MutualPlus Limited
<b>P Garlick, ACIB, BA</b>	Head of Membership Services
<b>S A Goldstraw</b>	Managing Director, Britannia Commercial Lending  Britannia New Homes (Scotland) Limited
<b>S Jones, MA (Oxon), ACIB, FiSMM</b>	Head of Retail Operations  Britannia Personal Lending Limited

## Annual Business Statement contd.

### 3. Directors' Responsibilities (continued)

#### OFFICERS

#### Business Occupation and Directorships

<b>J Katovsky, BA, MA</b>	Managing Director, Britannia Treasury Services Limited  Western Mortgage Services Limited
<b>G C Leftwich, BSc, MA</b>	Head of Corporate Communications
<b>M Lewis</b>	Managing Director, Western Mortgage Services Limited
<b>P Mansfield, BA, MA, FCIPD</b>	Managing Director, Britannia International Limited  The Derbyshire (Isle of Man) Limited
<b>D McCready</b>	Group Money Laundering Reporting Officer
<b>I G McKilligan, CA</b>	Head of Group Risk
<b>P A Mills, BSc, ACA</b>	Group Secretary  Britannia Asset Management Limited Britannia Building Society Land and Development Company (Midlands) Limited Britannia International Limited Britannia (Isle of Man) Limited Britannia Motor Insurance Services Limited Britannia New Homes Limited Britsafe Insurance Services (Guernsey) Limited Mornington Information Technology Services Limited Mortgage Agency Services Number Four Limited Mortgage Agency Services Number Five Limited PCSL Services No.1 Limited PCSL Services No.2 Limited Platform Consumer Services Limited Platform Funding Limited Platform Funding No.2 Limited Platform Funding No.3 Limited Platform Funding No.6 Limited Platform Group Holdings Limited Platform Home Loans Limited
<b>K Moir, BA</b>	Director of Organisational Development  Governor of Staffordshire University
<b>S Nichols, ACIB, MCT, ACIS</b>	Head of Treasury
<b>N Noakes</b>	Group Compliance Officer

### 3. Directors' Responsibilities (continued)

#### OFFICERS

#### Business Occupation and Directorships

<b>A J Thompson</b>	Head of Change Management
<b>D Tweedy, BA, MBA</b>	Managing Director, Platform Home Loans Limited  Platform Funding Limited Platform Consumer Services Limited PCSL Services No. 1 Limited PCSL Services No. 2 Limited Western Mortgage Services Limited
<b>D P Waddingham, MBA, FCIB, MCIM, MCMI, C.Dir</b>	Head of Strategic Relationships  MutualPlus Limited

### 4. Directors' Service Contracts

The following Directors have service contracts with the Society, entered into on the dates stated below:

N B Richardson	1 November 2001
G A Gregory	22 September 1999
P A Lee	1 September 2002

All Executive Director appointments (including promotions) have a rolling one-year contract of employment.





Britannia Building Society is authorised and regulated by the Financial Services Authority. All loans are subject to status, valuation and Rules of the Society, copies of which are available on request. Britannia undertakes to comply with The Banking Code. Copies of this Codes are available on request. Calls may be recorded and/or monitored.

**YOUR HOME MAY BE REPOSSESSED IF YOU DO NOT KEEP UP REPAYMENTS ON YOUR MORTGAGE.**

**Britannia Building Society**  
**Britannia House, Leek, Staffordshire Moorlands, ST13 5RG**  
**[www.britannia.co.uk](http://www.britannia.co.uk)**

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**Where membership means a great deal**