The Co-operative Bank plc

Building a better society

Financial Statements 2010

"Focused on future growth."

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good with money

Part of The **co-operative** financial services

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Chair's statement

This is my first report as Chair of The Co-operative Bank. I have been lucky enough to take the helm at one of the most exciting points in our history, one that will establish us in the world of financial services as a 'compelling, co-operative alternative'.

Many businesses talk about putting customers first and reducing their impact on the environment, but at The Co-operative Bank we have been 'walking the walk' since long before social responsibility was fashionable. As part of the UK's most diversified financial services mutual, we pride ourselves on being member owned, sharing the fruits of our business with our members and customers, rather than with external shareholders.

For many years some commentators have seen this as a limitation, given that it denies us one of the more common sources of generating capital; but we believe it allows us to focus more sharply on the interests of our members, our customers and the communities within which we operate. As the last of the demutualisers disappear into government or plc ownership, we are proud of the alternative we offer the increasingly beleaguered UK consumer.

That alternative is partly based on our well known ethical approach to our business. That ethical stance sees us continue to decline investment opportunities in businesses or governments that do not meet our customers' ethical expectations, but it also manifests itself in our positive engagement as investors ourselves, and as members of the wider co-operative movement.

That engagement encompasses support for the British credit union movement through pioneering initiatives such as the Credit Union Current Account and The Co-operative Enterprise Hub. It also manifests itself in support for local communities, with both financial support and over 47,000 hours of colleagues' own time invested in projects from conserving woodland to redecorating community centres. We are also actively inspiring young people to change their world, through schemes such as Fit4Finance, Number Partners and Enterprise4Education. This year saw the opening of the Co-operative Academy, while a planned Co-operative Apprenticeship Academy will deliver some 2,000 new apprenticeships by 2013. (You can learn more about these programmes in our Sustainability report on page 9.)

But the compelling, co-operative alternative is not just a matter of ethical leadership; it is firmly grounded in sound, commercial sense. In a mortgage market marked by retrenchment we have increased our lending portfolio, while focusing on lending to customers only what they can actually afford to repay. More generally, as a business moving from post merger stabilisation into ambitious transformation, we have taken great care to minimise the impact on our customers while maximising the benefits.

This year we were recognised by the Financial Times as the 'World's Most Sustainable Bank' ahead of an international field. The term 'sustainable' refers both to our determination to enrich rather than exploit our environment, and to the long term, commercial sustainability of our business model. Financial prudence and customer focus may sound like rather traditional ideas, but as the award demonstrates they are the hallmark of a business with its eye on the future.

Another hallmark of our forward looking approach is our increasingly close relationship with The Co-operative Group. The power of a shared brand has already enabled us to increase our profile with people who are not yet customers, and I note with pride that both The Co-operative Group and The Co-operative Bank featured in the top ten most influential brands in this year's survey of industry leaders and commentators. Not only had we risen to our highest ever position, but we were respectively the top placed retailer and financial services company in the survey.

Beyond the power of brand lies commercial opportunity, particularly the cross selling opportunities offered by the Group's diverse customer base. This year we have been working closely with the Co-operative Food business to pilot a number of in-store banking facilities. The pilot has provided some invaluable learning on what customers do and don't want, and we are planning to increase the number of in-store outlets in the coming year.

As active members of a unified, profitable 'superbrand' The Co-operative Bank can now look forward to even closer co-operation in the coming years, signalled by the appointment of our Chief Executive Neville Richardson, as one of two Deputy Group Chief Executives. Brought together already by our shared tradition and values, the next step in our evolution will be to focus on developing a truly joined up customer service proposition.

For the Bank in particular, this involves the replacement of our entire banking systems platform. We are the first UK bank to undertake such an ambitious programme, and we believe it will put us in an outstanding position to offer our customers the service they truly deserve, while attracting those who don't yet have a relationship with us through the advocacy of those who have.

As we look forward to the next chapter in our evolution I would like to express my thanks to the outgoing Chair, Bob Burlton. In his six year term Bob guided our business safely through both the credit crunch and our successful merger with Britannia Building Society. He can justly look back on his time as a period of successful change grounded in stability and a strong ethical compass.

I would also like to thank departing director John Reizenstein for shaping our corporate banking operations into a respected, competitive force.

Keith Alderson has joined the executive with responsibility for corporate and business banking. Keith has a wealth of corporate banking experience and has played a leading role in improving our corporate customer experience. I would like to congratulate him on a well deserved promotion.

At the end of my first few months in post, I feel a great sense of pride and excitement. Pride in the continued success and increasing recognition of The Co-operative Bank as a viable alternative to a discredited financial services model; and excitement at the journey ahead of us and the opportunities it offers. I would like to invite you to share that journey, whether as a member, an investor or a customer. As a group we have targeted a membership of 20 million by 2020; it is an ambitious figure but one that we believe we can achieve. As a new era dawns for the financial services market, we believe we offer something unique, democratic, forward thinking and on the verge of greatness. Come and join us, and be part of the *real* 'Big Society'.

Paul Flowers, Chair

Chief Executive's overview

Welcome to The Co-operative Bank's report and accounts for 2010. As I write, continued uncertainty hovers over the UK and wider economy, with the Government's austerity measures occupying the front pages and a 'double dip' recession still a possibility. Money remains in short supply, customer confidence is fragile, caution reigns and with the Bank of England base rate at an all time low, margins remain very tight.

Others (in Spain, Portugal and Ireland for instance) have been even less fortunate – and in a global market we share their pain. Economies that have been 'surfing the wave' of global expansion and cheap credit are now obliged to get themselves out of deep water. And as governments attempt to balance the books, the public inevitably gets the bill.

Customers are beset by financial woes for which by and large they bear little or no responsibility. Long held faith in the strength and trustworthiness of the banking sector has all but vanished, and as money becomes harder and more expensive to access, this distrust is fuelled by a real sense of anger and helplessness.

A compelling, co-operative alternative

In this climate, The Co-operative Bank is uniquely placed to deliver a compelling, co-operative alternative. Our business model is not driven by the needs of shareholders but by a long held belief in putting our customers' interests first. We have maintained a prudent approach, driven by our vision and values, trading within our means and focusing on sustainable customer service.

As a result we have not had to take government handouts to recapitalise or recover our commercial viability. Indeed, while many competitors retrench we have embarked on a pioneering transformation programme that will deliver an even better customer experience within the next three years. Moreover we are doing so without jeopardising either short term service levels or long term stability, which means that at no point will our customers be expected to underwrite our ambition at the expense of their financial security.

A year of stability and success

Our 2009 merger with Britannia Building Society launched us on a journey to become the UK's most admired financial services business. Eighteen months into that journey our financial results demonstrate the prudence that has made us an increasingly popular alternative to shareholder owned providers. In a year of low interest rates, cautious customer behaviour and tighter regulatory oversight we have maintained our profitability with an underlying operating result, excluding the cost of reinvesting in strategic change, of £170.5m (34.3% higher than in 2009).

Recognising the importance of overheads in the current financial climate, we have continued to manage our 'business as usual' operating cost closely, while the diversity of our business model enables us to offset limitations in one sector with opportunities in another.

The relationship of trust we enjoy with our customers has continued to yield dividends through excellent retention of funds (including a 97% retention of maturing cash ISA balances) while our willingness in a cautious mortgage market to lend to homebuyers within their means, has seen our mortgage book hold its value while those of many competitors are shrinking.

Our corporate sector continues to offer the same personal service to a wide range of business and corporate customers. In a difficult year for the industry, our operating result of £69.9m (an increase of £14.5m on 2009) reflects sustained demand, which has enabled our corporate banking team to be selective in its new business opportunities while significantly growing our term deposit base.

A key priority this year has been to grow our numbers of primary account holders – customers who are proud to say, "I bank with the Co-operative". Our focus on relationship banking is aimed at building a lasting, mutually rewarding relationship that will allow us to offer more and more customers both our own comprehensive range of products, and those of our parent company The Co-operative Financial Services (CFS). The high levels of service that underpin these products will help to strengthen the core relationship and make our customers powerful advocates for The Co-operative Bank in the wider community.

One key outcome of this strategic focus was a 79% increase in customers switching current accounts to us in 2010. This is testimony to the strength of our brand and reputation, particularly when one considers that the UK continues to have one of the lowest switching rates for primary bank accounts in the EU.

Current accounts play a key role in retail banking and yet are a major barrier to greater competition in the sector. We want to find a solution that makes switching a current account as easy as changing your utility provider or porting your mobile phone number. Our submission to the Treasury Select Committee on competition and choice in retail banking includes the recommendation that a dedicated working group be set up to consider how to make switching easier.

Meanwhile our balance sheet continues to reflect our underlying strength. We have maintained a robust capital position without resorting to the defensive recapitalisation seen elsewhere, itself the result of high risk strategies to which we did not expose ourselves. Our core tier 1 capitalisation reflects the requirements of our business model, but as a forward looking, competitive business we are actively exploring capitalisation options that will allow us to grow without impairing the mutual status that is so fundamental to our ethos.

Our liquidity remains stable – a fact highlighted by the strong customer funding profile underpinning our retail lending. We also benefit from a strong risk management strategy, with potential threats to the business understood and robust mitigants in place.

Our unique position as a prudent, trusted provider in a credibility challenged market has been underscored by a range of industry and customer voted accolades, and we were named the 'World's Most Sustainable Bank' by the Financial Times, ahead of an international field.

Chief Executive's overview continued

Transformation with the customer at its core
Sustainability is not merely a question of prudence or trust. To maintain and strengthen our place in the market we recognise that we must continue to offer our customers the best experience possible – we are aiming not just for satisfied customers but for customer advocates.

Last year the CFS Board agreed an investment of over £700m in the next three years to enable a business wide transformation into a truly compelling, co-operative alternative. A significant proportion of that investment is funding the replacement of The Co-operative Bank's core systems platform; we are the first UK bank to undertake such an ambitious project and we believe it will move us significantly closer to our vision of being the UK's most admired financial services provider.

Our corporate customers have already benefited from the launch of two new business banking platforms and over the next three years retail customers will also reap the benefits, as we develop a holistic view of customer holdings, faster and more efficient processing of customer transactions and the ability to bring new, customer focused products to market in days rather than months.

The journey continues
In 2009 with the creation of the UK's most diversified financial services mutual, The Co-operative Bank embarked on a new chapter in its history. Eighteen months on we have already laid the foundations with a unified leadership, organisational structure, vision and business strategy. Over the next year we will take further significant strides towards our vision of becoming the UK's most admired financial services business.

We have moved from stabilisation to transformation without disturbing our excellent customer relationships, and in many cases without customers noticing anything had changed (although we are confident they will as our transformation yields increasing customer benefits).

We have been able to achieve this, primarily through the dedication and engagement of colleagues throughout the business. 2010 has been a year of uncertainty in our markets and extensive change within the business itself; I would like to express my thanks to all my colleagues for remaining committed to the transformation process while refusing to compromise on our customer promise or our core values. This commitment, more than any other single factor, defines the 'compelling co-operative alternative'.

During 2011, in common with our colleagues within CFS, we intend to build on these firm foundations, with an ambitious strategy focusing on:

- active management of risk in accordance with our risk appetite, to deliver targeted rewards;
- implementation of a single employee terms and conditions package;
- embedding our target leadership model and culture across the business;
- support by all areas of the business for our game changing, banking transformation programme;
- consistent understanding of and delivery against our customer promise;
- maintenance of a dynamic balance between profit, capital and liquidity; and
- embedding a culture of cost control and efficiency.

Our target outcomes for 2012 reflect the same ambition grounded on firm foundations. Here is our vision of CFS in 2012:

We are clearly seen as the financial services arm of The Co-operative Group and customers repeatedly choose us for their primary financial services relationship and recommend us to others.

Our people are proud to work for us and advocate CFS as an employer and service provider, reflected in UK leading employee advocacy scores.

We operate within a clearly defined risk appetite. We are seen as a highly efficient business and we are recognised as a source of financial strength.

We stand at the threshold of a new era in financial services. We are uniquely placed to make it an 'era of co-operation'. The journey continues.

Neville Richardson

Neville Richardson, Chief Executive

Business and financial review

Overview

As the UK financial services market continues to suffer from the current, unprecedented, global economic challenges, The Co-operative Bank (the Bank), as part of The Co-operative Financial Services (CFS), has continued to offer a member owned, customer led and ethically guided alternative business model; one that has been endorsed this year, with the naming of the CFS as 'The World's Most Sustainable Bank'. As the award implies, CFS is forging a business model focused on long term, sustainable success. CFS was also named a 'recommended provider' by Which? Magazine and was the highest placed high street bank in the influential JD Power survey.

The Bank has maintained and enhanced its financial strength, while delivering benefits for customers and members. The operating result of £144.5m for 2010 was 25.4% higher than 2009. Excluding the costs of reinvesting in strategic change, the underlying operating result was up 34.3% to £170.5m. The excellent levels of customer funding in the Bank of 107% at December 2010, and the continued reduction in arrears (with a 22% reduction in late mortgage arrears during 2010) attest to our principle of being financially prudent and strong.

Meanwhile, the Bank's values based approach to all aspects of the business seeks to balance financial strength with the needs of our customers and our people. Our continuing focus on an easy, fair, personal and responsible service, during a time of deep uncertainty for many of our customers, remains a key distinguishing factor.

CFS customer advocacy figures remain 7.5 percentage points ahead of our competitors, while the business has also continued to deliver industry leading levels of employee engagement, with 89% of our people proud to work for us.

CFS saw a 79% increase in current account switchers in 2010. While this is testimony to the strength of, and trust in, our brand, the fact remains that the UK continues to have one of the lowest switching rates for primary bank accounts in the EU. Current accounts play a cornerstone role in retail banking and yet are a major barrier to greater competition in the sector. We want to find a solution that enables consumers to switch their current accounts and retain their current account number as easily as they can switch mobile phone providers whilst retaining their mobile phone number. In our submission to the Treasury Select Committee on competition and choice in retail banking, we recommended that a dedicated working group was set up to find a way to make switching easier. One issue it should consider is the introduction, longer term, of a portable bank account and sort code for personal customers.

By combining a unique business model, ongoing financial stability and strong customer advocacy, CFS and the Bank continue to offer the financial services customer a compelling, co-operative alternative.

Over the last 18 months, since the merger with Britannia Building Society, CFS has continued to make excellent progress, completing the integration of two complementary operations. The fundamental transformation of the combined business is now well underway, with its focus on delivering an enhanced customer experience. As the first release of our Banking Transformation Programme (the replacement of our core banking systems), Business Online Banking is now offered to our Small and Medium Enterprise customers and FD Online to our corporate customers. Both services offer enhanced functionality, improved security and have a more durable and responsive systems infrastructure. Co-operative current accounts are now available in all Britannia branches, and the core product range is aligned across Co-operative and Britannia channels.

The integration programme in relation to the merger with Britannia has built on the strengths of both heritage businesses and has so far delivered significant annual cost synergies within CFS of £48m, which predominantly relate to the Bank, and are ahead of expectations. Meanwhile, a comprehensive organisation design process has been completed, giving colleagues the focus, support structures and 'line of sight' to deliver the CFS customer promise.

Looking to the longer term, significant further investment is planned to extend the Banking Transformation Programme to all customers over the next three years. This will further transform the customer experience, through easier account opening processes, integrated product offerings and improved multi-channel capability. The business is also forging greater ties more widely across The Co-operative Group, which will enable the Bank to achieve its commitment to be part of the UK's most admired financial services business.

Business and financial review continued

Highlights

The Co-operative Bank operating result and profit before taxation	2010 £m	2009 £m	Change £m	Change %
Income	**821.8**	652.9	168.9	25.9
Operating costs – steady state	**(555.5)**	(413.8)	(141.7)	(34.2)
Operating costs – strategic initiatives	**(26.0)**	(11.8)	(14.2)	(120.3)
Impairment losses	**(95.8)**	(112.1)	16.3	14.5
Operating result	**144.5**	115.2	29.3	25.4
Significant items	**(55.5)**	(38.1)	(17.4)	(45.7)
Payment Protection Insurance (PPI) provision	**(4.3)**	–	(4.3)	–
Share of post tax profits/(losses) from joint ventures	**0.7**	(0.1)	0.8	800.0
Financial Services Compensation Scheme (FSCS) levies	**(11.5)**	(3.7)	(7.8)	(210.8)
Profit before taxation, distributions and fair value amortisation	**73.9**	73.3	0.6	0.8
Fair value amortisation	**(14.2)**	99.1	(113.3)	(114.3)
Profit before taxation and distributions	**59.7**	172.4	(112.7)	(65.4)
Membership dividend	**(10.8)**	(7.8)	(3.0)	(38.5)
Profit before taxation	**48.9**	164.6	(115.7)	(70.3)

Profit before taxation of £48.9m was lower than in 2009. This was predominantly due to amortisation of fair values created at the time of the merger; the apparent volatility of these initial adjustments is evident in the swing from a substantial benefit of £99.1m in 2009 to a charge of £14.2m in 2010. However, it should be noted that these adjustments are designed to unwind over future periods, are broadly profit neutral over time and have no cashflow impact.

Profit before taxation, distributions and fair value amortisation was 1% higher than 2009, at £73.9m. Higher significant items were incurred as a result of investment in the Banking Transformation Programme and a provision for pension mis-selling arising within the independent financial advisory business. In addition, the FSCS levy was £7.8m higher than 2009, and a £4.3m provision for Payment Protection Insurance (PPI) was incurred.

The operating result of £144.5m was 25.4% higher than 2009, reflecting both the increased scale of the combined business (with the result for 2009 including the Britannia business from August 2009) and notable organic growth in developing business areas. The operating profit reported within the consolidated income statement of £118.8m is stated after the deduction of the FSCS levy of £11.5m and the impact of fair value amortisation of £14.2m.

The operating result is stated after the significant costs of reinvesting in strategic change initiatives; these amounted to £26.0m in 2010 (2009: £11.8m). Excluding these change costs, the underlying operating result was up 34.3% to £170.5m, despite the challenges of the current economic environment and the ongoing weakness in the financial services sector in particular. On a like for like basis (including the pre-merger performance of Britannia for 2009), the underlying result excluding change costs was up by 10.8%.

Like for like income remained resilient (although down slightly in 2010 against 2009), a great achievement when taking into account the pressures on margin from low interest rates.

A policy of tight control and governance of the underlying cost base has continued in 2010 and is a key focus for the business going forward. Like for like costs fell by 2% in 2010, once the impact of inflation is excluded. Cost synergies of £41m, ahead of target, have helped to offset inflationary increases in costs.

Like for like impairment charges are significantly reduced from prior year levels, at 38.0% lower. This reflects a combination of improved arrears collection processes, the continued tightening of credit risk in the unsecured lending business and the cautious approach taken by both heritage businesses.

In 2010 a distribution of profit of £10.8m has been made to individual members of The Co-operative Group based on their account holdings with the Bank.

While total shareholder assets reduced slightly, from £46.1bn to £45.6bn, customer lending and deposits both grew, by 2.7% and 4.6% respectively.

Despite a difficult mortgage market, the Bank has increased its lending, with gross advances of £4.7bn, which illustrates the business's continued support to families and small businesses during these difficult times. The Bank is also sensitive to the depressed nature of the savings market and is doing what it can to balance savers' interests with those of borrowers.

While the credit risk on the residential mortgage portfolio is substantially mitigated by the fair value adjustments made at merger for any latent default risk in the Britannia assets, it is extremely pleasing to note the considerable reduction in arrears during 2010 (with a 22% reduction in late mortgage arrears during 2010), resulting from the tight credit control and focus on debt management.

The underlying strength of the business is evident in its stable capital and liquidity profile. The Bank core tier 1 ratio was 9.6% (2009: 8.7%), while the capital ratio was 14.0% (2009: 13.5%), and the tier 1 ratio, 9.9% (2009: 9.0%). These ratios reflect the strong capital base of the business, yet it is notable that the Bank has not taken, or needed, government capital support. This capital position has been more than sufficient to fund ambitious transformation projects while delivering outstanding service to our customers.

The Bank has maintained an excellent liquidity position, attracting and retaining high levels of customer funding. The customer funding ratio (excluding securitised assets) remains robust, at 107% (2009: 104%).

Our businesses

The Bank consists of two main segments – Retail, and Corporate and Markets (CAM).

The Co-operative Bank operating result	2010 £m	2009 £m	Change £m	Change %
Retail	**(3.2)**	(13.8)	10.6	76.8
CAM	**147.7**	123.7	24.0	19.4
Other	**–**	5.3	(5.3)	–
Operating result	**144.5**	115.2	29.3	25.4

The Retail business offers a range of financial products and services to individuals, households and small businesses throughout the UK, trading as The Co-operative Bank, Britannia and Smile.

Corporate and Markets (CAM) comprises a range of business to business services including corporate banking, treasury, intermediary mortgage lending and a number of fee for service businesses such as customer foreign exchange.

The other area of the Bank includes Unity Trust Bank, the result for which has decreased year on year.

Retail

Retail operating result	2010 £m	2009 £m	Change £m	Change %
Net interest income	**351.8**	262.2	89.6	34.2
Non-interest income	**149.7**	134.5	15.2	11.3
Net income	**501.5**	396.7	104.8	26.4
Operating costs – steady state	**(421.0)**	(318.6)	(102.4)	(32.1)
Operating costs – strategic initiatives	**(19.9)**	(9.2)	(10.7)	(116.3)
Impairment losses	**(63.8)**	(82.7)	18.9	22.9
Operating result	**(3.2)**	(13.8)	10.6	76.8

There was a significant improvement in the performance of the Retail Bank, reflecting stronger underlying profitability, despite the challenges of continuing low interest rates and uncertainty in the general economic environment. Underlying profitability, which excludes the cost of strategic change initiatives, was substantially improved at a profit of £16.7m (2009: loss of £4.6m). The strength of the CFS franchise, evidenced by continued growth in both current account balances and customer lending, combined with tight cost control and lower impairment charges have been at the heart of a strong 2010 performance. This places CFS in a great position for the future.

The improvement in profitability is complemented by high customer advocacy, 8.8% ahead of the 'top 5' in CFS's peer group.

The number of primary current accounts held by customers has increased by 17% in 2010; primary current accounts reflect those which a customer treats as their main bank account. In addition, the number of customers switching current account has increased by 79% during 2010.

Customer lending has increased, such that loans and advances now stand at £17.3bn (up 3.4%), reflecting the Bank's commitment to its retail customers, with gross advances of £3.1bn in 2010, at a time when many competitors were reducing their lending. The quality of the mortgage book remains high with a combined average loan to value of 41.8%. The growth in lending has been successfully self funded through the increase in customer deposits to £28.6bn and has contributed strongly to the Bank's overall customer funding ratio at 107%, reducing its dependency on funding from the wholesale markets.

Retail impairment of £63.8m was 22.9% better than 2009 reflecting a combination of improved arrears collection processes, strong quality of the mortgage book, declining credit card exposures and the continued tightening of credit risk scorecards in the unsecured lending business. These figures represent a considerable improvement given the current economic climate.

The strength of the retail customer proposition has again been recognised by a range of awards. CFS was named a 'recommended provider' by Which? Magazine, and won multiple categories at the Moneywise Customer Service awards. The Bank achieved the highest rating in the Forrester UK bank website benchmarking survey (beating NatWest, Santander, Barclays, Lloyds TSB and Halifax), and was the highest placed high street bank in the influential JD Power survey.

Business and financial review continued

Corporate and Markets (CAM)

CAM operating result	2010 £m	2009 £m	Change £m	Change %
Net interest income	**271.3**	199.4	71.9	36.1
Non-interest income	**38.2**	42.9	(4.7)	(11.0)
Net income	**309.5**	242.3	67.2	27.7
Operating costs – steady state	**(128.2)**	(87.7)	(40.5)	(46.2)
Operating costs – strategic initiatives	**(6.1)**	(2.6)	(3.5)	(134.6)
Impairment losses	**(27.5)**	(28.3)	0.8	2.8
Operating result	**147.7**	123.7	24.0	19.4

The CAM operating result for 2010 of £147.7m was 19.4% up on 2009.

Corporate banking
Corporate banking has delivered an operating result of £69.9m during 2010, an increase of £14.5m on 2009. This demonstrates a sustained performance in another difficult year for the industry, driven by measured growth on the corporate banking asset book through selected high quality new business, combined with significant liability growth through term deposits (54% growth in corporate deposits during 2010, evidencing the appeal of our proposition to the market). The increase in operating result is largely a result of a £13.0m increase in net interest income, due to the increased size of the newly combined business. Impairment losses have remained under control, falling from £32.3m to £30.4m.

Corporate will seek to drive further balance sheet growth through a dedicated customer deposits team and the roll out of a further two corporate banking centres during 2011, taking the total number to 22.

Platform
The Platform intermediary mortgage business, refocused on the prime mortgage market, has continued to grow its presence in this marketplace throughout 2010. The focus for Platform has been on good quality, prudent lending; advances of £0.6bn have been extended during 2010 with strong margins being achieved, and minimal arrears (0.71% of accounts in late arrears at the end of 2010).

Optimum
In 2010 the Optimum portfolio, a closed book of intermediary and acquired mortgage book assets, reduced in size, as planned, by 5% to £8.1bn, with the book performing strongly and in line with expectations.

Throughout the year, the business has delivered major improvements in the arrears management process with a focus on both existing arrears cases and pre-arrears cases. As a result, arrears in Optimum have improved steadily during the year. The merger related fair value provisions against the portfolio continue to provide a high degree of cover against credit losses.

Treasury
Treasury has delivered effectively on its core responsibilities of ensuring a strong and stable liquidity base, providing diverse sources of wholesale funding to the Bank, managing market risk within risk appetite and delivering a strong financial performance on the investment portfolio. The Treasury result was impacted by a challenging funding environment, with margins continuing to be under pressure during the year. Net interest income was negatively impacted due to increased investment in highly liquid, low risk assets in order to further strengthen our liquidity position as well as the reduction in higher risk, higher earning investment assets.

The Bank has been able to fund competitively in the wholesale markets, completing a £2.5bn prime mortgage securitisation transaction early in the year. This was followed towards the end of 2010 with an unsecured issuance of £400m, evidencing a considerable vote of confidence in the business from the market.

Summary and outlook
Notwithstanding the considerable challenges of the current economic environment and the integration of two businesses, the Bank has delivered a resilient performance for the year. Underlying profitability remains robust, supported by strong cost control and the complementary nature of the two heritage businesses. The Bank remains the compelling co-operative provider of a wide range of financial services, including our commitment to making switching current accounts an easier process, thanks to a strong balance sheet, responsible strategy and financial prudence, as evidenced by our strong capital and liquidity profile.

The excellent progress made in integrating the two businesses leaves the Bank, and its parent, CFS, well positioned to deliver market leading customer service. The benefits already provided to corporate customers through the Banking Transformation Programme will be extended to all customers over the next three years. We recognise the challenges ahead but are confident that our unique position within the industry, and the support of our people and customers, mean that we are favourably placed to achieve our vision.

Sustainability report

Sustainability is a key element of The Co-operative Financial Services' business strategy. The 'compelling co-operative alternative' means measuring our success, not just in financial terms but in how we impact on our community. It is one of the CFS 'givens' that we will champion co-operative values, principles and ethics. In furtherance of this we commit ourselves to taking personal and social responsibility. The following pages outline how we set out to honour these commitments.

2010 proved to be much more than a year of consolidation for The Co-operative Financial Services (CFS), following our merger with Britannia. With ethical and environmental considerations remaining key to our strategy, it was extremely pleasing to see our work recognised by the public and opinion leaders alike. From over 100 entrants in the global financial services industry, we became the Financial Times 'World's Most Sustainable Bank'. This award recognises our ethical and environmental leadership and the hard work of our colleagues. Together with our sector leading performance in the Sunday Times Best Green Companies List and our number one sector ranking amongst the general public for our social responsibility performance, the accolade attests to the absolute embeddedness of sustainability in our business.

We believe our future aspirations should surpass our previous accomplishments. That's why, in 2011, to consolidate its position as the most responsible UK business, The Co-operative has launched its boldest ethical campaign to date – Project Revolution – calling on millions of customers and members to help build a fairer world.

Strategy, materiality and governance

CFS' approach focuses on the issues of greatest relevance to our core business activities and stakeholders: the provision of ethical financial products and services; community investment and inclusion; and responsible environmental management.

As a co-operative business, our values and principles remain as relevant today as when they were conceived in the nineteenth century. Such values are reflected in The Co-operative's unique democratic structure, and in the ethical policies that underpin all banking and investments activity. This approach ensures that The Co-operative is held accountable via a Values and Principles Committee, drawn from the membership that own the business, and enables it to mobilise members and customers in innovative campaigning activity.

Leadership in social responsibility is taken into consideration in the remuneration of the CFS Executive Team, and performance is transparently reported in the award winning annual Sustainability Report of The Co-operative. 2011 sees a new milestone in our pursuit of sustainability, in the form of a three year Ethical Operating Plan, which sets ambitious new targets across our family of businesses.

Performance overview

Ethical finance

Our Co-operative Bank Ethical Policy acknowledges that the most significant sustainability impact we have is in who we lend money to – a principle that many of our competitors are slow to recognise. We have declined over £1bn of finance to businesses, in line with our customers' ethical concerns, whilst continuing to grow our commercial lending overall – its value is now 16 times that of 1992, when the policy was launched. We have extended our ethical screening approach to the £1bn of investments that underpin our insurance products, whilst continuing to ensure that we remain an active and responsible institutional investor. Our Ethical Engagement Policy, a world first, sets out a commitment to use our power as an institutional investor to push for improvements in the ethical and environmental performance of investee companies. In support of this policy, in 2010, we voted on over 4,000 UK shareholder resolutions, taking a stand against management in 10% of instances. This included challenging oil companies, such as BP and Shell, to be more transparent about tar sands developments, which risk dangerous levels of climate change and local ecological disaster.

Last year saw the launch of our Social Banking Unit, which ensures that businesses and organisations with a distinctly ethical or social purpose – such as charities or co-operatives – benefit from the services of a dedicated expert team. One early success story of this new service is the £1.2m loan provided for a wind turbine on the island of Tiree in the Inner Hebrides, where the majority of adults are Co-operative members. Moving forward, our commitment to fund energy efficiency and renewable solutions will increase to £1bn. During 2010, we also promoted awareness of ethical banking and investment amongst the general public, through our continued support for National Ethical Investment Week.

We continue to make finance accessible to all and not the few. Our provision of basic bank accounts is up nearly 30% from 2009, and we maintain our support to the pioneering bank accounts for prisoners project, through which over 5,000 prisoners have now been provided with an account – and, therein, a better opportunity to secure housing and employment; factors considered key to reducing reoffending.

Keeping communities thriving

In 2010, The Co-operative family of businesses invested £12.4m in the community. CFS colleagues contributed to the total of over 90,000 hours volunteered by Co-operative colleagues, taking part in community team challenges, which ranged from conserving woodland to redecorating community centres. Next year, we will encourage our colleagues, customers and members to help raise £5m for Mencap, our 2011 Charity of the Year, to enable their fantastic work improving the lives of young people with learning disabilities.

Our new Ethical Operating Plan has set an ambitious new target for our community investment – by 2013, 10% of The Co-operative's profits available for distribution will be invested in the community, with at least £5m being targeted at tackling poverty in the neighbourhoods around Co-operative branches and stores.

Sustainability report continued

Supporting co-operatives

We hold a strong belief in the principle of 'co-operation amongst co-operatives', and The Co-operative was proud to support the very first 'Co-operatives Fortnight' – a series of events aiming to raise the profile of co-operatives in the UK. We continue to be the largest provider of banking to the British Credit Union movement and support the Co-operative sector's further development through pioneering initiatives, such as the Credit Union Current Account.

The Co-operative Enterprise Hub, which is funded by The Co-operative, is committing some £7.5m over the next three years to provide the advice, training and finance needed to ensure that the sector continues to thrive. This further enhances CFS' support for renewable energy projects. For example, the Hub has provided funding to Energy4All Ltd, a development company born of the UK's first community owned wind farm, Baywind Energy Co-operative. Baywind was partly financed by The Co-operative Bank when it was established in 1996, and recent Hub funding has led to the creation of further co-operatives around the UK. The creation of an additional £20m International Co-operative Development Loan Fund promises to ensure that our investment in the co-operative sector can have similarly positive impacts in developing communities overseas.

Inspiring young people

The initiatives undertaken by The Co-operative with the aim of 'Inspiring Young People' are helping over 250,000 young people change their world. Our Skills4Schools programme, delivered by colleague volunteers, promotes three initiatives – Fit4Finance, Number Partners and Enterprise4Education – which aim to improve the financial literacy, numeracy and employability of schoolchildren. In 2010, 6,800 hours of Company time and expertise were invested in the programme. We are the main sponsor of The Co-operative Academy in Manchester, which was launched in 2010. Specialising in business and finance, this school benefits from our business expertise and receives funding for community work. Furthermore, work is currently underway on the creation of The Co-operative Apprenticeship Academy, which, by 2013, will have created 2,000 new apprenticeships.

Tackling global poverty

The Co-operative continues to strive for a fairer world, where basic human needs are met and rights are respected. At CFS, we have supported microfinance institutions in 27 countries across the globe, through a $50m fund to provide small loans to people in the world's poorest countries. To date, a staggering £6m has been raised by charity credit card customers for organisations that tackle global poverty or protect human rights, such as Oxfam or Amnesty International.

The Co-operative also continues to work directly with communities in the developing world – with significant water, sanitation and green energy solutions being funded and delivered in 2010. Our conviction that we can and should be doing more to tackle global poverty will see us launch, in 2011, a renewed third world debt campaign – 'Unfinished Business'.

Protecting the environment

CFS continues to offset all CO_2 emissions, together with an additional 10% to compensate for our carbon legacy. Most ambitiously, The Co-operative is now seeking to reduce, by 35%, operational greenhouse gas emissions across the family of businesses by 2017; a stretching target for a business that has already made considerable headway in addressing this impact.

Last year, CFS completed the roll out of our environmental management systems across the Britannia estate and were extremely proud to achieve recertification to the ISO14001 standard. We remain the only financial services organisation in the world to achieve this leading standard across all business activities and products.

Our pioneering 'Think' credit card not only rewards ethical consumerism, but has helped save over 2,000 acres of Indonesian rainforest through donations made by CFS on our customers' behalf. We've also worked to shape the wider debate on ecological sustainability. As part of our Toxic Fuels campaign, The Co-operative has called for a ban on UK shale gas developments until related human and environmental risks have been assessed.

The conviction that a profitable business must also be a principled one has remained integral to our business throughout a period of considerable change. 2011 promises to be another exciting year, as the launch of The Co-operative's new Ethical Operating Plan will not only bolster our own performance, but also challenge others in the UK financial services industry to raise their game in the pursuit of sustainable development.

The Board
The Co-operative Bank plc

Non-executive directors:

Paul Flowers (BA (Hons))
Age 60. Joined the Board in 2009 and appointed Chair in 2010. Deputy Chair of The Co-operative Group Limited. Superintendent Methodist Minister/ Bradford city councillor. Member of The Co-operative Group North Regional Board. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Rodney Baker-Bates (MA, FCA, AIMC, FCIB)
Age 66. Joined the Board in 2009 and appointed Deputy Chair in 2010. Directorships also held at Assura Group plc, AtlasFram Group Limited, Bedlam Asset Management plc, Dolphin Square Trust Limited, EG Solutions plc, G's Group Holding Limited and Stobart Group plc. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Duncan Bowdler (BSc (Hons) Biochemistry)
Age 52. Joined the Board in 2009. Trade liaison manager. Member of The Co-operative Group North West and North Midlands Regional Board. Non-executive director of The Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

David Davies (BSc (Econ), FIA)
Age 63. Joined the Board in 2003, appointed Deputy Chair in 2010 and is the senior independent director. Chair of Sun Life Assurance Company of Canada (UK) and Nortel Networks Pension Scheme in the UK, and non-executive director of Interglobal Insurance Company Limited. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Peter Harvey (ACIB, Dip FS)
Age 55. Joined the Board in 2009. Consultant to Berwin Leighton Paisner LLP. Also non-executive director at Marshalls Holdings Limited and a member of the Supervisory Board and Audit Committee of Surrey Cricket Club Limited. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Paul Hewitt (MA, ACA, Dip German (Open))
Age 55. Joined the Board in 2003. Non-executive director of Kiln Group and Collins Stewart plc. Chair of Four Times Enterprises Limited, The Good Care Group Limited and R.J. Kiln & Co Limited. Industrial partner with Lyceum Capital, a mid market private equity firm and trustee of NEST (the National Employment Savings Trust). Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Chris Jones (LLB)
Age 58. Joined the Board in 2009. Member of the Institute of Credit Management, the Law Society and a Fellow of the Royal Society of Arts and of the Association of Business Recovery Professionals. Runs Tourmalet Consulting, specialising in business turnaround. Non-executive director of Agenda Management Services Limited, Armitage Jones LLP, Montpelier Business Reorganisation Limited, Trango Ltd and The Business Desk. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited. Chair of Illius Properties Limited.

Stephen Kingsley (BSc (Hons), FCA)
Age 58. Joined the Board in 2009. Over 35 years' experience in financial services primarily auditing and consulting. Has held senior positions at Arthur Andersen and AON Corporation. Currently a senior Managing Director at FTI Consulting Limited, the global expert services firm. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Peter Marks
Age 61. Joined the Board in 2009. Chief Executive of The Co-operative Group Limited. Entire working life spent within the co-operative movement. Instrumental in bringing about a number of major co-operative mergers over the past decade. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Bob Newton (BSc, FIA, CDir)
Age 61. Joined the Board in 2007. Forty years' experience in the financial services industry; now has a portfolio of business and pro bono interests. Holds non-executive directorships with UIA (Insurance) Limited, and AI Claims Solutions plc. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited, CIS General Insurance Limited and Reclaim Fund Ltd.

Ben Reid (OBE, FCCA)
Age 56. Joined the Board in 2009. Chief Executive of The Midcounties Co-operative. Chair of Walsall Hospitals NHS Trust. Non-executive director of The Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

The Board continued

Len Wardle (BA)
Age 66. Joined the Board in 2006. Chair of The Co-operative Group Limited and member of the South East Regional Board. Held management positions in local government and latterly was a Fellow at the University of Surrey in the School of Management. Director of Communicate Mutuality Limited. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Martyn Wates (ACA, ATII, BA (Hons))
Age 44. Joined the Board in 2007. Chief Executive, Specialist Businesses and Deputy Chief Executive of The Co-operative Group Limited. Has held various senior finance positions within the co-operative movement. Director of various internal subsidiaries and non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Steve Watts (MA (Cantab), MA (Econ), BA (Hons))
Age 59. Joined the Board in 2006. Member of the Central & Eastern Regional Board. Retired pricing, research, and information officer within the Directorate of Employment and Skills at Cambridge Regional College. Non-executive director of Unity Trust Bank plc. Deputy Chair of The Co-operative Group Limited, non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Piers Williamson (BA (Hons), ACIB, MCT)
Age 49. Joined the Board in 2005. Over 25 years' experience of the UK, US and European financial markets. Holds non-executive directorships with various Industrial and Provident Societies and funding vehicles associated with the Housing Finance Corporation, where he is Chief Executive, also a sustainable development commissioner for the Greater London Authority. Non-executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Executive directors:

Neville Richardson (BA (Hons), FCA)
Age 53. Joined the Board in 2009. Chief Executive. Deputy Chief Executive of The Co-operative Group Limited. Director of Communicate Mutuality Limited. Member of the Court of the University of Lancaster and of the Building Societies Association Council. Also Chief Executive of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Rod Bulmer (BA (Hons), MSc)
Age 41. Joined the Board in 2009. Managing Director, Retail. Joined Co-operative Financial Services in October 2007 and became Sales Director in July 2008. Executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Tim Franklin (ACIB)
Age 49. Joined the Board in 2009. Chief Operating Officer. Non-executive director of Reclaim Fund Ltd. Executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Phil Lee (BSc, CA)
Age 55. Joined the Board in 2009. Executive director, Integration and Change. Executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Barry Tootell (BA (Hons), FCA)
Age 49. Joined the Board in 2008. Chief Financial Officer. Qualified accountant with over 20 years of finance and control experience. Chair of CFS Management Services Limited. Executive director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited.

Report of the Board of Directors

The directors submit their report, together with the audited financial statements, for the period to 31 December 2010. The full financial statements 2010 contain the corporate governance statement on pages 17 to 22 and the risk management section on pages 45 to 77, which are deemed to form part of the report of the Board of Directors. As set out more fully in the Basis of preparation and accounting policies, these financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. All financial information given in this report is taken solely from the statutory results prepared on this basis. Unaudited, like for like results which allow business segment comparison between 2010 and 2009 are given in the business and financial review on pages 5 to 8.

Principal activities

The Co-operative Bank plc (the Bank) and its subsidiary undertakings provide an extensive range of banking and financial services in the UK.

Business review

A review of the development and performance of the Bank and its operating subsidiaries during the financial year and any significant events since the year end are set out in the business and financial review on pages 5 to 8. The principal risks and uncertainties facing the Bank are set out in the risk management section on pages 45 to 77. Note 36 of the financial statements provides details of the Bank's principal subsidiaries and the nature of each organisation's business.

The Bank changed its accounting reference date in 2009 to 31 December. Where these financial statements refer to 'year ended 31 December 2010' this represents the 52 week period for 1 January 2010 to 31 December 2010. The 2009 comparatives are stated for the 51 week period from 11 January 2009 to 31 December 2009.

On 15 December 2010 the Bank allotted £180m of share capital to its parent company, Co-operative Financial Services Limited (CFS), to reinforce its capital strength.

Key performance indicators

The CFS Group has introduced a balanced scorecard that reflects its goals as a business over its three year corporate plan.

How do we measure our success?

The CFS business strategy measures success in four key areas: financial, customer, people and process. This 'balanced scorecard' approach is a key reflection of our co-operative difference. The balanced scorecard helps us ensure that, in all decisions we make as a business, we focus on the financial, customer, people and process implications of the decision. It also helps us to take a broad view of our progress towards our strategic vision.

How do we measure our success?

Financial

Financial measures focus on profitability and underlying financial strength:

- **Profit**
  This is our measure of operating profit for the business as a whole and includes operating profit (adjusted for significant items) before tax. The measure also incorporates a new business profit measure for our life business.

  CFS Shareholder profit before tax: £209.7m

  Progress: ●

- **Liquidity**
  Our liquidity measure sets a minimum liquidity limit for the year in line with the Financial Plan.

  Minimum liquidity level: 107%

  Progress: ●

- **Surplus capital**
  Similarly our surplus capital measure sets a minimum amount of capital for each year, below which the business should not operate. This minimum is set in line with the Financial Plan with due regard for our regulatory requirements.

  Amount of surplus capital: On target

  Progress: ●

Customer

Customer measures address the key relationships through which we sustain and grow our business:

- **Customer advocacy**
  We use an external survey to monitor advocacy of customers across the Retail businesses relative to appropriate peers. This gives us our customer advocacy measure.

  Customer advocacy: +7.5%

  Progress: ●

- **Primary current account customers**
  Primary current account customers are defined as those who:

  – hold one of our standard current accounts.
  – credit their account with at least £800 per month.

  Primary account customers: 552,000

  Progress: ●

- **Products held per primary current account customer**
  This measure monitors how well we are meeting the needs of our relationship customers (as defined above) by calculating the average number of active products they hold with us.

  Products per primary account holder: 2.59

  Progress: ●

To be the UK's most admired Financial Services Business

People

People measures reflect the importance of internal, as well as customer advocacy:

- **Colleague engagement**
  Our colleague engagement assessment is derived from our twice yearly internal colleague survey.

  Colleague engagement: 78.5%

  Progress: ●

Process

Process measures focus on the efficiency of our business in delivering services to our customers:

- **Cost**
  This measure focuses on our cost base. The target for this measure reflects the current combined business position and the outputs from the Financial Plan over a three year period.

  CFS efficiency ratio: 38.2%

  Progress: ●

- **Compliance with risk appetite**
  We track this measure using key risk criteria across the business. Success means no material breaches against any of these criteria.

  Compliance with risk appetite: 100%

  Progress: ●

● On target
○ Good progress
○ Below target

Report of the Board of Directors continued

Financial measures specific to the Bank are discussed in the business and financial review, on pages 5 to 8.

Results and dividends

Profit before taxation and significant items was £108.7m. Profit attributable to the ordinary shareholders amounted to £36.4m (2009: £110.3m). No dividends were paid during 2010. The directors recommend that no final dividend is paid in respect of 2010.

Changes to the Board

The names of the present members of the Board and their biographies and details of length of service are set out on pages 11 and 12.

The directors of the Bank during the financial year are listed below. They were appointed for the full period unless otherwise indicated:

Non-executive directors:

Paul Flowers (Chair)
Rodney Baker-Bates
Duncan Bowdler
Bob Burlton (resigned 15 April 2010)
David Davies
Peter Harvey
Paul Hewitt
Chris Jones
Stephen Kingsley
Peter Marks
Bob Newton
Ben Reid
Len Wardle
Martyn Wates
Steve Watts
Piers Williamson

Executive directors:

Neville Richardson (Chief Executive)
Rod Bulmer
Tim Franklin
Phil Lee
John Reizenstein (resigned 7 December 2010)
Barry Tootell

Reappointment of directors

Under the Articles of Association, one third of the Board are required to retire by rotation at the conclusion of the Annual General Meeting (AGM). In accordance with the Articles of Association, therefore, Len Wardle, Martyn Wates and Steve Watts retire by rotation and all offer themselves for re-election at the 2011 AGM. No directors have been appointed since the conclusion of the last AGM on 12 May 2010 which would make them eligible for re-appointment at the 2011 AGM. The notice of the AGM can be found on page 125. All directors up for re-election continue to demonstrate commitment to their roles (see schedule of attendance on page 20).

On 15 April 2010, Bob Burlton, Chair, retired from the Bank Board, and Paul Flowers was appointed Chair in his place. Paul Flowers has served on the Board since 2009 and on the Board of The Co-operative Group since 2008. Rodney Baker-Bates and David Davies were appointed Deputy Chairs on 21 April 2010. Rodney Baker-Bates had previously served on the Board of Britannia Building Society since 2006. David Davies joined the Board in 2003 and was appointed senior independent director in 2005. John Reizenstein, Managing Director Corporate and Markets, left the Bank Board on 7 December 2010.

Directors' and officers' liability insurance and indemnity

The Bank maintains appropriate directors' and officers' liability insurance cover, through the ultimate parent organisation, in respect of legal action against its directors and officers. This constitutes a 'qualifying third party indemnity provision' for the purposes of the Companies Act 2006 and applied to all of the Bank's directors serving during the financial year. The insurance cover was reviewed and renewed in 2010. A 'qualifying pension scheme indemnity provision' was also in place for one or more of the directors who served during the financial year.

Directors and their interests

No director had a material interest at any time during the year in any contract of significance, other than a service contract, with the Bank or any of its subsidiary undertakings.

No director had a beneficial interest in any shares in the Bank or in The Co-operative Group Limited, which is the ultimate holding organisation, or in any other entity controlled by The Co-operative Group Limited.

Going concern

The financial statements are prepared on a going concern basis as the directors are satisfied that the Group and parent company have the resources to continue in business for the foreseeable future. In making this assessment, the directors have considered a wide range of information relating to present and future conditions including future projections of profitability, cash flows and capital resources. Further information relevant to the assessment is provided within the basis of preparation of the financial statements on page 38.

Corporate governance

The Bank is committed to high standards of corporate governance. The Bank believes it has, with the exception of the level of independent Board representation, fully complied throughout the year with the principles and provisions of the Combined Code on Corporate Governance appropriate to the structure of the Bank and its parent organisation, Co-operative Financial Services Limited (CFS) and The Co-operative Group Limited (The Co-operative Group). Further information is provided within the corporate governance report on pages 17 to 22.

Information and communication

Communication takes place with all key stakeholders through a variety of media including the sustainability report produced by The Co-operative Group. Employees receive and provide information on strategy and objectives through their reporting lines and a formal performance measurement process. Newsletters, bulletins and electronic media communicate other information.

Employees

The Bank and its subsidiary undertakings employed 8,583 persons at 31 December 2010 (2009: 8,705). The weekly average number of people was 8,746 (2009: 5,993) and their aggregate remuneration, before significant items, for the year was £221.1m (2009: £151.0m). The Bank, as part of CFS operates learning and development initiatives across the organisation as part of a continuous improvement programme, supporting its approach to performance management, personal development, talent and succession planning.

CFS, in Bank orientated activities, continues to consult and communicate with colleagues on customer, organisation and business performance issues, using colleague publications, surveys, conferences, videos and both informal and formal consultations with Unite and other unions, which continue to be fully involved where organisational change and other issues affect colleagues.

Diversity
The Bank, as part of CFS, welcomes diversity and actively promotes a policy and practice of equality of opportunity in employment for all colleagues, regardless of age, disability, ethnicity, gender, religion or belief, or sexual orientation.

The Bank, as part of CFS, is a member of the following diversity advisory bodies:

- Employers Forum on Disability
- Employers Forum on Age
- Race for Opportunity
- Opportunity Now
- Stonewall

Employees with disabilities
CFS is a holder of the 'Positive about Disabled People' symbol, a recognition given by Jobcentre Plus to employers who have agreed to meet five commitments regarding the recruitment, employment, retention and career development of disabled people. CFS has policies and processes in place to support disabled colleagues in the workplace.

Further guidance and information for colleagues on disability issues is available through human resources and on the colleagues' intranet. CFS recognises its responsibility for making reasonable adjustments for new colleagues with disabilities and for those individuals who develop disabilities whilst in employment.

Employees' wellbeing
The Bank, as part of CFS, recognises that health and wellbeing at work play a vital part in delivering its core values. Wellbeing services include an occupational health scheme, physiotherapy services and seasonal wellbeing initiatives such as discounted allergy testing and flu jabs.

In addition to this, colleagues and their immediate families have access to an external employee assistance programme, providing free expert advice on a wide range of medical, legal and family issues.

Corporate responsibility
The Bank's corporate responsibility activities are outlined on pages 17 to 22. In addition, The Co-operative Group Sustainability Report, which will be published in the first half of 2011, describes how The Co-operative Group Limited, CFS, the Bank, Co-operative Insurance Society Limited and CIS General Insurance Limited manage their social, ethical and environmental impacts.

Political and charitable donations
During the year, CFS Management Services Limited, a fellow subsidiary of CFS, made donations (which exclude affinity card payments) of £0.4m to charitable organisations on behalf of the Bank (2009: £0.4m). A further £0.5m of donations were made directly by the Bank with £0.4m allocated through the Britannia Foundation. Additional costs associated with the Bank's community involvement are provided within The Co-operative Group Sustainability Report. It is the Bank's policy that no donations are made for political purposes.

Outlets
At 31 December 2010 the Bank had 370 outlets (2009: 368 outlets).

Market value of land and buildings
Freehold and leasehold land and buildings held by the Bank are held on the balance sheet at historic cost and have not been revalued. Based on valuations carried out by The Co-operative Group's internal property valuers, their market value at the balance sheet date is £75.2m which is £8.0m higher than carrying value.

Supplier payment policy and practice
With the exception of the Britannia business area detailed below, the Bank does not pay suppliers directly as all supplies and services are sourced through CFS Management Services Limited, a fellow subsidiary of CFS. A management charge is payable to cover the cost of these services.

Suppliers are paid directly by the former Britannia business where the 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 obligations. Creditor days at 31 December were 16 (2009: 11 days).

Report of the Board of Directors continued

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 Bank's position or that of any of its connected undertakings.

Significant contracts
The Bank maintains a number of significant contracts with IT providers, cash handling entities and mailing service companies as well as with a CFS Group company, CFS Management Services Limited which provides facilities and services for all CFS Group companies.

Financial statements
So far as the directors are aware, there is no relevant audit information of which the Bank's auditors are unaware, and the directors have taken all steps that they ought to have taken as directors in order to make themselves aware of any relevant audit information and to establish that the Bank's auditors are aware of that information.

Statement of directors' responsibilities in respect of the report of the Board of Directors and the financial statements
The directors are responsible for preparing the financial statements and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare Group and parent company financial statements for each financial year. Under that law they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent company and of their profit or loss for that period. In preparing each of the Group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a remuneration report, a directors' report and a corporate governance report that comply with that law and those regulations.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Auditors
In accordance with Section 489 of the Companies Act 2006, resolutions for the appointment and remuneration of the auditors are proposed at the next AGM and set out on page 125. Further detail in relation to the appointment of the auditors is set out on page 22.

By Order of the Board
Moira Lees, Secretary

29 March 2011

Corporate governance report

UK Combined Code on Corporate Governance

For the period ended 31 December 2010, The Co-operative Bank plc (the Bank) believes it has, with the exception of the level of independent representation on the Board and CFS Audit and Regulatory Compliance Committee (which is commented upon later), fully complied with the principles and provisions of the Combined Code on Corporate Governance (the Code) appropriate to the structure of the Bank and its parent organisation, Co-operative Financial Services Limited (CFS) and The Co-operative Group Limited (The Co-operative Group).

The Bank will, for the period ended 31 December 2011, report against the new UK Corporate Governance Code. A gap analysis has been completed and work is underway to ensure compliance with the UK Corporate Governance Code.

Board composition and independence

The Board currently comprises 15 non-executive directors and five executive directors.

The Code requires at least half of the Board, excluding the Chair, to be independent non-executive directors. In accordance with the Code, it is for the Board to consider whether a director is independent in character and judgment and whether there are any relationships or circumstances which are likely to affect, or could appear to affect, the director's judgment. The size and composition of the Board is currently under review and increasing the proportion of independent directors on the Board will be considered as part of this review.

The Board has concluded that, looking across the wider Co-operative Group, the individual members elected by and from The Co-operative Group's seven regions to stand as directors (unless employees within the last five years) should be defined as independent, while those appointed directors representing independent society members of The Co-operative Group could not be so categorised in the co-operative context. This is because the latter represent significant shareholders with material business relationships.

Included within the Board members are seven independent professional non-executive directors, Rodney Baker-Bates, David Davies, Peter Harvey, Chris Jones, Bob Newton, Stephen Kingsley and Piers Williamson. David Davies is the senior independent director. In addition, there are two independent non-executive directors elected by and from the members of The Co-operative Group that the Board have determined to be independent as described above. These are Len Wardle and Steve Watts.

Ben Reid represents independent society members of The Co-operative Group. Peter Marks and Martyn Wates hold executive appointments in The Co-operative Group (Peter Marks is the Chief Executive and Martyn Wates is a Deputy Chief Executive). Duncan Bowdler is an employee of The Co-operative Group. Paul Hewitt was, until 28 July 2007, Deputy Chief Executive of The Co-operative Group. These directors cannot therefore be considered to be independent.

The Board believes it has sufficient independent representation having nine independent non-executive directors (excluding the Chair). The Board believes that all the non-executives have considerable experience and make valuable contributions to the operation of the Bank.

The non-executive directors constructively challenge and help develop proposals on strategy and bring strong, independent judgment, knowledge and experience to the Board's deliberations. The non-executive directors are of sufficient calibre and number that their views carry significant weight in the Board's decision making.

The directors that serve on the CFS Board (the Bank's parent) also sit on the Bank Board to provide a common understanding of objectives. Appointments to the CFS Board are made by The Co-operative Group Board. Under the CFS rules, each non-executive director is appointed for a term of three years commencing on the day following the Annual General Meeting for the year in which the director is appointed.

All non-executive directors are eligible for re-appointment at the end of each term of office. The Co-operative Group Board, being party to agreements with the independent professional non-executive directors for services to CFS and its subsidiaries, including the Bank, may resolve to re-appoint at or before the date their contracts expire for a further three year term. It is the normal policy of the Board not to allow an independent professional non-executive director to serve for more than nine years in aggregate.

For the recruitment of non-executive directors, external recruitment consultants are retained.

Roles and responsibilities of the Bank Board

The directors are committed to leading and controlling the Bank effectively. The Board is responsible for the success of the Bank within a framework of controls, which enables risk to be assessed and managed. It is responsible for setting strategy, maintaining the policy and decision making framework in which this strategy is implemented, ensuring that the necessary financial and human resources are in place to meet strategic aims, monitoring performance against key financial and non-financial indicators, overseeing the system of risk management and for setting values and standards in governance matters.

The responsibility of the Board is to direct the business of the Bank and in particular to:

- ensure that the Bank's affairs are conducted and managed in accordance with its Articles of Association and the best interests of its stakeholders and in accordance with co-operative values and principles;
- agree objectives, policies and strategies, and monitor the performance of executive management;
- approve the annual budget and business plan;
- approve the reported financial statements and dividends;
- monitor, through various committees, the key significant risks facing the Bank;
- establish Board committees and agree their terms of reference; and
- approve the delegated financial authorities.

Corporate governance report continued

The Board manages these matters at its regular Board and strategy meetings and details of attendance at Board meetings are noted on page 20. The Board meets on a monthly basis and it met 12 times in 2010. There were also two strategy meetings, attended by senior executives, devoted to consideration of performance and longer term planning. The Board is scheduled to meet for 11 Board meetings and to hold two strategy meetings in 2011.

Board procedures

Board and committee papers are distributed at least one week in advance of meetings. This provides the opportunity for directors to prepare fully for meetings. The minutes of all meetings are circulated to all directors. As well as circulating papers as hard copies, the Board has access to its own secure website where papers are available together with additional supporting material (and which acts as a library of papers for directors).

There is regular communication between the directors, the Chair, the Deputy Chairs and the Secretary between meetings.

When a director is unable to attend Board or committee meetings, issues can be raised with the Chair or the Deputy Chairs. Written questions for management on papers are encouraged from directors between meetings. A rolling schedule of matters arising from Board and committee meetings is followed through.

The roles of the Chair, Deputy Chairs and Chief Executive

The division of responsibilities between the Chair of the Board and the Chief Executive is clearly defined and has been approved by the Board.

The Bank Chair is a non-executive director. He leads the Board in the determination of its strategy and in the achievement of its objectives. The Chair is responsible for organising the business of the Board, ensuring its effectiveness and setting its agenda. He has no involvement in the running of the day to day business of the Bank. The Chair facilitates the effective contribution of directors and constructive relations between the executive and non-executive directors, and ensures directors receive accurate, timely and clear information and ensures that there is effective communication with members. During 2010 the Chair undertook one to one discussions with all directors regarding the performance of the Board. On 21 April 2010 two Deputy Chairs were appointed to support the Chair.

Details of the Chair's and Deputy Chairs' professional commitments are included in the biographies on page 11. The Board is satisfied that these responsibilities do not interfere with the performance of the Chair or Deputy Chairs' duties for the Bank.

The Chief Executive, appointed by The Co-operative Group Board, has direct charge of the Bank on a day to day basis and is accountable to the Board for the financial and operational performance of the Bank.

Board committees

With the agreement of the Financial Services Authority (FSA), the Board has delegated certain responsibilities to the following committees, all of which have written terms of reference covering the authority delegated to it by the Board. Each of these committees has a role in ensuring the effectiveness of the Bank and its subsidiaries. A provision of the Code is that the terms of reference for the Remuneration and Appointments Committee and the Audit and Regulatory Compliance Committee are available on the Bank's website, and the Bank complies with this.

Remuneration and Appointments Committee

The CFS Remuneration and Appointments Committee meets as a joint committee for CFS, Co-operative Insurance Society Limited (CIS), CIS General Insurance Limited (CISGIL) and the Bank. Information on the Remuneration and Appointments Committee is found on page 23.

CFS Audit and Regulatory Compliance Committee

The CFS Audit and Regulatory Compliance Committee meets as a joint committee for CFS, CIS, CISGIL and the Bank. The committee comprises five members and is chaired by Paul Hewitt. During the year the committee comprised:

Paul Hewitt	(Chair)
Paul Flowers	(resigned 12 May 2010)
Chris Jones	
Bob Newton	
Ben Reid	
Martyn Wates	

Paul Hewitt, Ben Reid and Martyn Wates bring recent and relevant financial experience and in addition Ben Reid is the Chair of The Co-operative Group's Audit and Risk Committee. Paul Flowers stood down from the committee following his appointment as Chair of the Board. Chris Jones and Bob Newton are considered to be independent members of the committee. The committee's terms of reference and constitution are currently under review. Please see page 20 for further detail.

The committee met four times during the financial year. The main responsibilities of the committee are to:

- review and discuss with management and auditors the preliminary results, interim information and annual financial statements of the Bank before submission to the Board;
- review, prior to its consideration by the Board, the external auditor's reports to the directors and management's response;
- receive reports on activities and note the minutes of the CFS Risk Management Committee;
- consider any necessary disclosure implications from the process that has been applied by the Board to deal with material internal control aspects of any significant problems disclosed in the financial statements;
- obtain assurance that the Bank is compliant with relevant regulation;
- review and discuss issues identified as a result of compliance work and how management is addressing these issues;
- monitor regulatory relationships, in particular, with the FSA;
- assess the qualification, expertise, resources, effectiveness and independence of the external auditors and approve the terms of engagement and remuneration paid to the external auditors in respect of the audit services provided;
- review co-ordination between the internal and external auditors and, where relevant, the risk management functions;
- review and discuss with the relevant business leaders any issues identified as a result of internal audit work and how management is addressing these issues as well as reviewing reports on management response to audit recommendations;
- monitor and assess the role and effectiveness of the internal audit function; and
- approve policies and review the adequacy of risk management activities in relation to operational risk.

CFS Risk Management Committee

The CFS Risk Management Committee meets as a joint committee for CFS, CIS, CISGIL and the Bank. The committee comprises six members and is chaired by Piers Williamson. During the year the committee comprised:

Piers Williamson (Chair)
David Davies
Mike Fairbairn (Director of Risk) (who is not a Board director)
Paul Flowers (resigned 7 July 2010)
Paul Hewitt
Stephen Kingsley
Barry Tootell

Paul Flowers stood down from the committee following his appointment as Chair of the Board although he may attend any committee meeting as an observer at his discretion. The committee's terms of reference and constitution are currently under review. Please see page 46 for further detail.

The committee met six times during the financial year. The main responsibilities of the committee are to:

- review and challenge the impact assessment of the strategic plan on the risk and capital profile of the Bank;
- review and challenge the risk appetite process with a focus on the overall organisational view of risk appetite;
- monitor compliance with Board approved risk appetite;
- approve mandates and portfolio limits in line with risk appetite, and monitor and review any breaches thereof;
- assess the robustness of Individual Capital Adequacy Assessment Processes (ICAAP);
- review and challenge the executive's recommendations on level of capital held in relation to how adequately it reflects the Bank's risk profile;
- review and challenge the adequacy of risk management activities across the Bank managed by the executive, including risk mitigation;
- review and challenge the adequacy of the risk management process and systems in operation;
- set standards for risk management processes and techniques, and benchmark against industry best practice on a regular basis; and
- monitor the credit risk performance of new and existing portfolios against limits, and ensure any appropriate risk mitigation action or review of risk policies or limits is taken.

CFS Exposures Committee

The CFS Exposures Committee meets as a joint committee for CFS, CIS, CISGIL and the Bank. The committee comprises five members and is chaired by Peter Harvey. During the year the committee comprised:

Peter Harvey (Chair)
Kevin Blake (Business Leader, Banking Risk) (who is not a Board director)
Bob Burlton (resigned 15 April 2010)
Neville Richardson
Steve Watts
Piers Williamson

The Bank Chair may attend any committee meeting as an observer at his discretion.

The committee met 11 times during the financial year. The main responsibilities of the committee are to:

- approve all Bank advances in excess of the delegated lending authority of the Chief Executive;
- review all decisions taken within the delegated authority of the Chief Executive or any individual executive by way of Noting Returns;
- review and approve management actions on excess positions on lending exposures which exceed the Chief Executive's discretion;
- review and approve management actions on excess positions on investment exposures which exceed the Chief Executive's discretion;
- review and approve management actions on individual counterparty positions on the corporate banking credit risk watchlist, the Bank's market credit risk watchlist, and The Co-operative Asset Management credit risk watchlist;
- review and approve management actions on any other positions which the Credit Committee or the Business Leader, Actuarial Risk, determine should be brought to its attention; and
- review minutes of the Risk Management Committee and note any actions to be taken as relevant to the remit of the committee.

During the year the committee reviewed its own effectiveness.

Corporate governance report continued

CFS Banking Transformation Programme Sub-Committee

In addition to the main Board committees detailed above, the CFS Banking Transformation Programme Sub-Committee was constituted by the CFS Board at its meeting on 17 February 2010. The sub-committee's purpose is to provide oversight of CFS's Banking Transformation Programme in order to give assurance to the Board on the progress of the work in the programme. The work of the Banking Transformation Programme includes replacing the existing retail and corporate banking systems with new technology systems, redesigning processes and interaction with customers.

Attendance

The table below sets out the frequency of, and attendance at, the Board and Board committee meetings for the period under review by directors.

The number in brackets indicates the total number of meetings the director was eligible to attend during the year. In the case of a director being unable to attend a meeting, the Chair has received a satisfactory reason for their absence.

Provision of advice to directors

A number of external consultants provide professional advice to the Boards of the constituent parts of the wider Co-operative Group. There is an agreed procedure by which directors may take independent professional advice at the Bank's expense in furtherance of their duties.

Training and professional development

In 2010, a new Board Learning and Development Policy was introduced to support all non-executive directors.

Following meetings with non-executive directors to review individual and collective training and development, thematic learning and development sessions for the whole Board have taken place each month.

Specific training has been organised for Board committees including the CFS Remuneration and Appointments Committee, the CFS Audit and Regulatory Compliance Committee and the Risk Management Committee. In addition, one to one support has been provided to a number of directors.

The directors' website has been used as a resource bank to enable directors to access, revisit and review copies of presentations and materials from the development sessions.

At the end of 2010 individual learning and development records were issued to all non-executive directors summarising activity through the year and individual learning plans were being progressed with a view to constructing the framework for individual and collective learning and development going forwards.

Performance evaluation

The Code requires the Board to undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.

During the year an external evaluation of the CFS Board, also sitting as the Bank Board, was completed in order to provide independent and informed advice on the effectiveness and impact of the Board and its committees. The review included observation of Board and committee meetings, review of constitutional documents and one to one confidential interviews with directors. The findings of the review were reported back to the Board at a strategy meeting in November 2010. A small number of recommendations were made and these are being implemented during 2011.

In addition to the Board review, an external review of the Bank risk management framework was conducted during 2010 which included a review of the responsibilities and terms of reference for the CFS Audit and Regulatory Compliance Committee and the CFS Risk Management Committee. The results of the review, which were reported to the Board, confirmed that the Bank risk management framework was coherent. The review made a number of recommendations in light of new regulations and evolving best practice and these are to be considered during 2011 alongside a detailed review of the terms of reference and composition of both the CFS Audit and Regulatory Compliance Committee and the CFS Risk Management Committee.

Due to the extent of the external reviews which took place in 2010, with the exception of CFS Exposures Committee, internal Board and committee evaluations were not required. The internal evaluation process will recommence in 2011.

Directors	Bank Board	CFS Remuneration and Appointments Committee	CFS Audit and Regulatory Compliance Committee	CFS Risk Management Committee	CFS Exposures Committee
Number of meetings held	**12**	**6**	**4**	**6**	**11**
Paul Flowers	11 (12)	5 (6)	1 (1)	1 (3)	
Rodney Baker-Bates	11 (12)	5 (6)			
Duncan Bowdler	11 (12)				
Rod Bulmer	11 (12)				
Bob Burlton	4 (4)	4 (4)			3 (4)
David Davies	10 (12)	6 (6)		6 (6)	
Tim Franklin	11 (12)				
Peter Harvey	11 (12)				11 (11)
Paul Hewitt	11 (12)		4 (4)	4 (6)	
Chris Jones	12 (12)		4 (4)		
Stephen Kingsley	12 (12)			6 (6)	
Phil Lee	12 (12)				
Peter Marks	10 (12)	5 (6)			
Bob Newton	12 (12)		4 (4)		
Ben Reid	9 (12)		3 (4)		
John Reizenstein	10 (11)				
Neville Richardson	12 (12)				11 (11)
Barry Tootell	12 (12)			6 (6)	
Len Wardle	12 (12)	5 (6)			
Martyn Wates	12 (12)		4 (4)		
Steve Watts	12 (12)				11 (11)
Piers Williamson	12 (12)			6 (6)	11 (11)

The Secretary to the Board
The Secretary is professionally qualified and is responsible for advising the Board through the Chair on all governance matters. The directors have access to the advice and services of the Secretary. The Articles of Association and the schedule of matters reserved to the Board for decision provide that the appointment and removal of the Secretary is a matter for the full Board.

The executive
It is the responsibility of the executive to implement the strategic objectives as agreed by the Board. The executive, under the leadership of the Chief Executive is responsible for the day to day management of the Bank.

Effective from 1 January 2011 the Chief Executive reports directly to the Chief Executive of The Co-operative Group in order for CFS and its subsidiaries, including the Bank, to become more closely integrated into The Co-operative Group.

Relations with members
The Bank has two equity shareholders. The majority of the shares are held by CFS, which is a wholly owned subsidiary of The Co-operative Group. The remainder of the shares are held directly by The Co-operative Group.

The Bank has approximately 2,500 preference shareholders. The preference shares are fixed-interest shares and are non-cumulative and irredeemable. The preference shareholders are entitled to attend the Annual General Meetings, but the shares only hold speaking or voting rights if and when the dividend has been in arrears for six months or more, or if a resolution is to be proposed at general meeting abrogating or varying any of their respective rights or privileges, or for the winding up of the Bank or other return of capital and then only on such resolution.

Risk management
The Board and executive management have the primary responsibility for identifying the key business risks facing the organisation. The CFS risk management framework, which is approved and reviewed by the Bank Board, outlines the approach taken to ensure a robust risk management process is in place throughout the organisation and is regularly reviewed. The framework includes an ongoing process for identifying, evaluating and managing significant risks and has been in place for the year under review and up to the date of the approval of the annual financial statements.

An independent review of the Bank risk management framework has recently been completed.
The objective of the review was to consider whether the current framework is capable of enabling good risk governance and to make recommendations for improvement. The review considered the current framework to be suitable for an organisation of the Bank's size and complexity.

The Board accepts that there are risks which could impact on the achievement of the Bank's business objectives, but endeavours through positive risk management strategies as outlined in the risk management framework, to manage these in a manner that optimises returns within the confines of the business' risk appetite, whilst protecting members' interests and reserves.

For further information on the Bank's approach to risk management see pages 45 to 77.

Internal control
Internal controls are the activities undertaken by management, the Board and other parties to enhance risk management and increase the probability that established objectives and goals will be achieved. The Board has overall responsibility for the Bank's system of internal controls which aim to ensure effective and efficient operations, quality of internal and external reporting, safeguarding of the Bank's assets and compliance with laws and regulations. Whilst recognising that the system is designed to manage rather than eliminate risk of failure to achieve business objectives, it can only provide reasonable and not absolute assurance against material misstatement or loss.

Corporate governance report continued

The Bank's internal control framework is designed to create an attitude of taking acceptable business risk within clearly defined limits. The control environment includes:

- an organisational governance structure with clear lines of responsibility, delegation of authority and reporting requirements;
- checks and balances to ensure that business processes operate efficiently reducing the risk posed to the organisation whilst adhering to organisational values;
- comprehensive systems of financial reporting. The annual budget and long term plan of the Bank and of each division are reviewed and approved by the Board;
- a code of business conduct covering relations with customers, shareholders, colleagues, suppliers, community and competitors;
- a whistleblowing policy and procedure which provides for any employee to report, in confidence, suspected serious malpractice;
- internal audit, risk and compliance functions that review the system of internal control; and
- a control self assessment process designed to fully support the annual review of the effectiveness of the system of internal control and enable continual monitoring and improvement of the internal control environment.

External audit

One of the duties of the CFS Audit and Regulatory Compliance Committee is to make recommendations to The Co-operative Group Audit and Risk Committee in relation to the appointment of the external auditors. In 2003 The Co-operative Group Board approved the re-appointment of KPMG Audit plc as the external auditor following a competitive tender exercise. A repeat tender exercise is currently underway and it is intended that a resolution to appoint the external auditor be put to the next Annual General Meeting of The Co-operative Group on 21 May 2011. It is proposed that KPMG Audit plc remain as external auditors of the Bank until this date. A resolution to re-appoint KPMG Audit plc as external auditor at the Bank's next Annual General Meeting on 12 May 2011 is contained in the Notice of the Annual General Meeting on page 125.

The CFS Audit and Regulatory Compliance Committee has put in place safeguards to ensure that the independence of the audit is not compromised including a policy on the conduct of non-audit services from the external auditors. The external auditors are permitted to provide some non-audit services that are not, and are not perceived to be, in conflict with their independence. The Co-operative Group Audit and Risk Committee receives at each meeting a report providing details of assignments (and related financial fees) carried out by the external auditor of the Bank in addition to their statutory audit work. The pre-approval of the committee is required for services above certain thresholds determined by the committee.

In addition, the following assignments are prohibited from being performed by the external auditors:

- bookkeeping or other services related to the accounting records or financial statements;
- financial information systems design and implementation;
- actuarial services;
- internal audit outsourcing services;
- management functions or human resources; and
- any other services that the CFS Audit and Regulatory Compliance Committee may determine.

The performance of the external auditors is regularly monitored to ensure it meets the needs of the Bank and the results are reported to the committee.

Internal audit

The internal audit function is an independent function, which reports to the CFS Audit and Regulatory Compliance Committee. Its primary role is to provide assurance over the adequacy and effectiveness of the internal control framework including risk management practices.

Internal audit seeks to discharge the responsibilities set down in its charter by completing a risk based internal audit plan, reviewing the processes which ensure that the key business risks are effectively managed by key controls.

Internal audit also acts as a source of constructive advice and best practice, assisting senior management with its responsibility to improve the processes by which business risks are identified and managed.

Internal audit reports are submitted to, and significant issues discussed at, the CFS Audit and Regulatory Compliance Committee. Full details of the operation of this committee can be found on page 18.

By Order of the Board
Moira Lees, Secretary

29 March 2011

Remuneration report

The Co-operative Bank (the Bank) uses, as a guideline for its disclosure in relation to remuneration, the requirements applicable to Listed Companies, as set out in schedule 8 of the Large and Medium sized Companies and Groups (Accounts and Reports) Regulations 2008 (incorporated into the Companies Act 2006) and will be subject to an advisory vote of shareholders of the Company at its Annual General Meeting to be held on 12 May 2011.

This report provides details of the remuneration of both the executive directors and the non-executive directors. The details, also shown in the report of Co-operative Financial Services (CFS), do not represent additional payments.

The key issues this year are:

- extensive dialogue with the Financial Services Authority (FSA) in connection with our current and future remuneration practices. All remuneration arrangements and practices in place are compliant with the FSA Code of Practice;
- compliance with the new disclosure requirements of the FSA in respect of those colleagues who are designated as code staff but who are not executives. The relevant information in respect of those colleagues is to be found in section 9 of this report;
- the introduction of a new annual incentive plan with effect from 1 January 2010; and
- the introduction of a new long term incentive plan with effect from 1 January 2010.

These issues are covered in detail in the body of the report.

Introduction

The remuneration report is presented by the Board and contains the following information:

- a description of the role of the CFS Remuneration and Appointments Committee (the committee), in respect of the Bank;
- a summary of the Bank's remuneration policy, including a statement of policy on executive directors and non-executive directors; and
- details of the terms of the service contracts and the remuneration of the executive directors and non-executive directors for the 2010 financial year.

The CFS Remuneration and Appointments Committee meets as a combined committee for CFS and the Bank. Its role is described below.

Role of the Remuneration and Appointments Committee

The committee's terms of reference were last revised and approved by the CFS Board on 12 May 2010.

The committee's principal terms of reference are to:

- determine the policy on remuneration and other main terms and conditions of employment in respect of Bank executives;
- oversee contractual arrangements for the executives and approve the principal terms and conditions of employment of such executives;
- review remuneration using comparisons against the agreed market policy for the executive;
- make recommendations on executive appointments and the terms and conditions relating to these;
- review and agree the remuneration policy and outcomes in respect of all code staff;
- approve any relevant incentive schemes, ensure that they are in line with current market practice and the FSA Code of Practice, and authorise payments under any incentive schemes in line with their rules; and
- receive, review and decide on issues raised in relation to the Co-operative Group Pension (Average Career Earnings) Scheme and any other retirement benefit scheme within the Group and advise the Board on them as appropriate.

The Co-operative Group Remuneration and Appointments Committee oversees these arrangements in respect of the CFS Chief Executive.

The terms of reference for the committee are available on the CFS website.

Members of the committee during 2010 were Rodney Baker-Bates (Deputy Chair CFS) as Chair, together with Len Wardle (Group Chair), Peter Marks (Co-operative Group Chief Executive), Paul Flowers (Bank Chair) and David Davies (Deputy Chair, CFS). Bob Burlton sat on the committee until his retirement from the Board on 15 April 2010. The Board believes that all members of the committee are independent for the purpose of reviewing remuneration matters.

The CFS Chief Executive and the Director of Organisational Development also attended the meetings of the committee during the year except when their own remuneration was being discussed. The Chief Risk Officer provided an annual report to the committee and attended and provided advice on specific risk adjustments in relation to remuneration issues as required by the FSA. Other individuals were invited to attend for specific agenda items when necessary. The committee worked with the Co-operative Group Remuneration and Appointments Committee in ensuring consistency, where appropriate, across the wider Co-operative Group.

The committee members are all non-executive directors. They have no personal financial interests in the committee's decisions, and they have no involvement in the day to day management of the Bank.

The committee met six times in the year to 31 December 2010.

To ensure that it receives independent advice on remuneration matters, the committee retained Hewitt New Bridge Street (a trading name of Aon Hewitt Limited, part of the Aon Corporation) as its advisers during 2010 to provide advice solely on remuneration matters. Hewitt New Bridge Street has supplied survey data and advised on market trends and other general remuneration issues. Other than specialist advice in relation to remuneration matters, Hewitt New Bridge Street does not provide other services to CFS. Addleshaw Goddard was also retained to provide legal advice to the committee with respect to executives' service contracts.

Policy on directors' remuneration

Executive directors

In determining the remuneration policy for executive directors, the committee consider a number of factors including:

- the importance of attracting, retaining and motivating senior executives of the appropriate calibre to further the success of the Bank;
- the linking of reward to business and individual performance and the strengthening of co-operative values which include a strong belief in stewardship of all the Bank's resources and, therefore, ensures that executives are not rewarded for the assumption of undue risk;
- ensuring that the interests and pay practices of the executive directors are aligned across the Bank, taking into account also the pay levels and employment conditions of colleagues within the business;
- in conjunction with the Group Remuneration and Appointments Committee ensuring that pay practices are coherent with those in the Society as a whole; and
- ensuring appropriate compliance with the FSA Code of Practice.

Remuneration report continued

The current policy is to pay executive directors, who also sit on the CFS Board, basic salaries around the market median, when compared with other organisations of comparable size and complexity, and also organisations in the same business sector. The committee supports the principle of performance related pay and operates an annual incentive plan and a long term incentive plan which, together, mean that over 50% of the remuneration package is performance related. The committee does not consider it appropriate to follow the quantum available in some publicly traded companies. Accordingly, the amounts payable under these plans are lower than in comparable publicly traded companies. Together, the annual incentive plan and long term incentive plan represent total variable remuneration, with awards under the long term incentive plan comprising the deferred element of variable remuneration as required by the FSA.

The committee considers that a successful remuneration policy needs to be sufficiently flexible to take account of future changes in the Bank's business environment, and in comparative remuneration practice. Accordingly, the committee continuously keeps the Bank's remuneration policy under review.

Whilst the business climate in financial services remains challenging, the Bank has remained resilient through the period, having a robust model based on sound co-operative principles (which avoid undue risk taking or reliance on a single business stream). In particular, the absence of highly leveraged incentive plans (when compared with some practices in the quoted sector) has ensured that executives have not been encouraged to accept undue risk as a means of securing personal reward.

The committee notes that the remuneration practices already adopted at the Bank, in addition to being right for the business, have been endorsed by the FSA through its Code of Practice on remuneration policies. However, the committee continues to strive for further improvements in its executive remuneration arrangements as best practice evolves.

The main components of executive directors' remuneration are:

1. Basic salary

It is the committee's policy to ensure that the basic salary for each executive director is appropriate and competitive for the responsibilities involved. Basic salaries for executive directors are reviewed by the committee, normally annually, having regard to competitive market practice (in particular, salary levels for similar positions in comparable companies), and business and individual performance during the financial year. The normal month for salary review is January. Basic salary is the only element of remuneration that is pensionable. Salaries received by executive directors in respect of 2010 are set out in table 1.

2. Annual incentive plan

Each executive director is eligible to participate in an annual performance related incentive plan. The committee reviews and sets incentive targets and levels of eligibility annually.

The design and terms of the 2010 plan are as follows:

- target payment levels for all of the executive team are 35% of base salary with a maximum opportunity of 60%; and
- all measures used in the plan are derived from the corporate balanced scorecard.

Such an approach, in addition to being right for the business, represents best practice as set out in the FSA Code of Practice.

The measures and weightings in the balanced scorecard are as set out below:

- financial (30%): shareholder profit before tax;
- process (30%): cost v budget;
- customer (20%): customer advocacy; and
- people (20%): colleague engagement score.

In addition to achieving performance against the balanced scorecard measures and weightings, four further underpins must be achieved before any payment is made. These are as follows:

1. The budget profit must be achieved before any element becomes payable.
2. CFS must stay within its required liquidity range as agreed by the CFS Board.
3. CFS must stay within its required minimum capital level as agreed by the CFS Board.
4. There should be no material breaches of risk in accordance with the risk appetite as agreed by the CFS Board. The Chief Risk Officer is required to provide an annual report to the committee before bonus payments are signed off.

Additionally in accordance with the FSA Code of Practice, deferral provisions, clawback facility and malus adjustment (bonus reduction facility) are built into the plan.

3. Long term incentive plan

A new long term incentive plan (LTIP), compliant with the FSA Code of Practice and representing deferred remuneration, was introduced with effect from 1 January 2010. The plan is designed to focus and align the leadership team with the long term strategy of the business. The plan measures performance over a three year period. The first three year period is 2010 to 2012 with potential payment in 2013. It is intended that awards will be made annually thereafter.

The level of award under the LTIP is 75% of base salary for executives and 100% of base salary for the Chief Executive. These awards represent the maximum amount payable in respect of each three year performance period. The actual amount of award vesting is subject to the achievement of the performance measures.

The performance measures are based on the performance of the business over a three year period as set out in the balanced scorecard, the measures being designed to ensure delivery of CFS's strategic targets. The specific measures for 2010 to 2012 are shareholder profit, cost management, customer satisfaction, and colleague engagement. Additionally, the underpins applicable to the annual incentive plans also apply to the LTIP. Any breach thereof will result in the committee considering a reduction in any payment that may otherwise be calculated as due. These underpins are to provide appropriate risk adjustment and to be compliant with the FSA Code of Practice.

4. Service agreements

It is the Bank's policy for the notice period in executive directors' service contracts not to exceed one year. Executive directors have consistent contracts that are terminable by up to one year's notice by the organisation and six months' notice by the individual. In the event of termination, any payments due to an executive director would be based on this. The committee may make a discretionary award of bonus earned up to the date of termination of employment. Any such award would be subject to deferral in accordance with the FSA code of practice.

All the Bank executive directors had similar contracts during 2010. The dates of existing contracts or dates of appointment are shown in table 1.

In normal circumstances, it is the committee's policy to apply service contracts for any newly recruited executive directors in a similar form to the model that has been developed for existing executive directors.

5. Share options

As a co-operative, CFS does not operate a share or share option plan.

6. Non-executive directorships

The committee has determined that, subject to the committee's approval, executive directors may accept one non-executive directorship, or similar, with an external organisation believing that this represents an important opportunity for professional development. Any fees received from such a role will normally be paid to the Bank, CFS or The Co-operative Group.

At this time, with the exception of Neville Richardson who is a director of Communicate Mutuality Limited, none of the executives hold any non-executive directorships with companies outside of The Co-operative Group.

7. Pensions

The financial services businesses participate in the Co-operative Group Pension (Average Career Earnings) Scheme (the PACE Scheme). However, following the merger with Britannia Building Society on 1 August 2009, colleagues who at that date were members of the Britannia Pension Scheme (the Britannia Scheme) continue in membership of the Britannia Scheme. From 1 August 2009, for the interim, only the defined contribution section of the Britannia Scheme is available to new colleagues of the financial services businesses.

The PACE Scheme, which is a registered occupational pension scheme, provides defined benefit pensions based on 1⁄60th of average pensionable earnings, re-valued for inflation for each year of pensionable service from 6 April 2006 (the date the PACE Scheme was implemented). Benefits accrued as at 5 April 2006, in respect of membership of the scheme preceding the PACE Scheme, continue to be linked to final pensionable salary at a member's date of leaving or retirement, whichever is earlier. Pensions are also payable to dependants on death and a lump sum is payable if death occurs in service.

The Britannia Scheme, which is also a registered occupational pension scheme, provides benefits under two sections:

- a defined benefit (DB) section (closed to new colleagues), which provides pensions based on an accrual of 1⁄80th, 1⁄60th or up to 1⁄30th for executives, of final pensionable salary for each year of pensionable service; and
- a defined contribution (DC) section (open to new colleagues) with an employer contribution rate of 4%, 6% or 8% depending on the level of member contribution.

Under both sections pensions are also payable to dependants on death and a lump sum is payable if death occurs in service.

Members of the PACE Scheme currently contribute 6% of their pensionable salary whilst members of the Britannia Scheme contribute either 6% or 8% of their pensionable salary if they are in the DB section. The employer pays the balance of cost of providing DB benefits. Members of the Britannia Scheme DC section pay 2%, 3% or 4% of their pensionable salary. All members have the choice of making pension contributions by salary sacrifice.

Prior to the merger on 1 August 2009, Neville Richardson, Tim Franklin and Phil Lee had contractual arrangements under which they accrued pension benefits in an unfunded employer financed retirement scheme (EFRBS).

Remuneration report continued

These contractual arrangements were revised from 1 August 2009 and the rate of benefit aligned more closely to Group executive pension policy. The EFRBS is in place to provide pension benefits that exceed the lifetime allowance. Benefits up to the lifetime allowance will be provided from the Britannia Scheme. The revised pension arrangements are subject to further review in 2011.

Executives have the facility of opting out of future pension accrual under the relevant registered scheme when the value of their accrued pension benefits reaches the lifetime allowance under the tax rules in favour of a pension allowance of 16% of basic salary in lieu of pension provision. John Reizenstein had previously opted out of the PACE Scheme on this basis and is entitled to a deferred pension. He received a pension allowance of 16% of basic salary.

Supplementary life cover is provided to executives in order to provide total life cover of four times salary when aggregated with benefits from the PACE Scheme or Britannia Scheme, as appropriate.

Additional details are available in table 2.

Non-executive directors
All the non-executive directors are appointed, and their directors' fees are determined and paid, by The Co-operative Group.

The basic fee for a non-executive director elected to sit on The Co-operative Group Board who is also appointed to serve on the CFS Board and its principal subsidiaries (including the Bank) is £15,555 per annum, and these same non-executive directors receive additional fees for serving on the various CFS Board committees (which also have responsibility for Bank business). The Chair's fee is £107,848 per annum.

During the year under review, Hewitt New Bridge Street conducted a benchmarking exercise of fee levels for the independent professional non-executive directors serving on the CFS Board and its committees, and, as a result, recommendations from the CFS Remuneration and Appointments Committee were approved by the Board of The Co-operative Group in September 2010.

Following this benchmarking exercise the seven independent professional non-executive directors and the professional non-executive director receive a fee of £57,002 per annum. Directors serving on the various committees also receive additional fees, as do the Deputy Chairs, to reflect their additional responsibilities.

Fees are increased in line with RPI every year. The increase in fees in 2010 was 3.7%, effective from 1 June 2010.

The independent professional non-executive directors and the professional non-executive director are party to agreements with The Co-operative Group governing the terms on which their services are made available to the Bank. These service agreements all expire on 31 July 2012, with the exception of Bob Newton, Piers Williamson and Paul Hewitt whose service agreements expire on 31 July 2011.

The Co-operative Group Board may resolve to re-appoint any of the independent professional non-executive directors at or before the date their service agreements expire for a further three year term. It is the normal policy of the Board not to allow an independent professional non-executive director to serve for more than nine years in aggregate.

The non-executive directors' service agreements contain no specific provision for liquidated damages on early termination of an agreement.

None of the independent professional non-executive directors are directors of The Co-operative Group or members of any Co-operative Group pension scheme or incentive plan.

Details of the directors' year of appointment and fees are shown in table 3.

Code staff remuneration
Code staff is defined by the FSA as staff having a material impact on a firm's risk profile, including a person who performs a significant influence function for a firm, a senior manager and risk takers. The information provided within this section is supplementary to the qualitative and quantitative information provided herein with respect to the executive and non-executive directors, all of whom are code staff.

Remuneration policy and outcomes for code staff are determined by the committee. The design of the component parts of remuneration is as set out for the executives. However, the overall remuneration levels and incentive opportunities are lower than for executives. For all code staff, performance related pay is risk adjusted through the use of the underpins to the incentive plans together with the application of deferrals, clawback and malus adjustments in accordance with the FSA Code of Practice.

Details of the aggregate remuneration information required by the FSA are shown in table 4 and are in respect of all CFS code staff. The amounts shown in respect of executive and non-executive directors do not represent additional remuneration.

By Order of the Board
Rodney Baker-Bates, Chair
CFS Remuneration and Appointments Committee

29 March 2011

Table 1 – Emoluments of executive directors for the year ending 31 December 2010

	Date of service contract or appointment	Basic salary £000	Other supplements[1] £000	Performance related pay annual[2] £000	Benefits in kind £000	Total related to 2010 £000	Performance related pay medium/long term[3] £000	2010 Total emoluments £000	2009 Total emoluments[9] £000
Neville Richardson[4] [8]	1 August 2009	664	9	349	12	1,034	162	1,196	443
Rod Bulmer[7] [8]	1 June 2008	351	150	184	–	685	69	754	203
Tim Franklin[4] [8]	1 August 2009	385	18	203	1	607	94	701	262
Phil Lee[4] [8]	1 August 2009	385	9	203	9	606	94	700	262
John Reizenstein[5] [6]	6 January 2005	351	74	–	–	425	–	425	728
Barry Tootell[8]	4 April 2008	385	25	203	–	613	78	691	566
Total		2,521	285	1,142	22	3,970	497	4,467	2,464
Former directors who served the Bank in 2009									1,014
Compensation for loss of office[10]									1,750
									5,228

The table above represents total emoluments for executive directors in relation to their services for the CFS Group.

(1) Other supplements include car allowance, pension (in lieu), and medical insurance (in lieu). These elements are non-pensionable.
(2) Performance related pay (annual) refers to amounts earned in respect of 2010.
(3) Performance related pay (medium/long term) refers to compensatory amounts paid in respect of the lost opportunity as a result of the early vesting of the 2008–2010 plan.
(4) Benefits in kind for Neville Richardson and Phil Lee are in respect of company car and medical insurance and for Tim Franklin in respect of medical insurance only. These benefits were provided under the terms of their contract with Britannia.
(5) The other supplements figure for John Reizenstein includes a salary supplement in lieu of pension provision.
(6) John Reizenstein resigned as executive director on 7 December 2010.
(7) The other supplements figure for Rod Bulmer includes a compensatory payment in respect of a lost long term incentive opportunity arising from his previous employment.
(8) In accordance with the FSA Code of Practice, payment of 60% of 2010 variable pay is deferred over a three year period. Variable pay comprises annual bonus in respect of 2010 plan plus long term incentive awarded in 2011 in respect of the 2010 year.
(9) 2009 total emoluments were in respect of a part year only for Neville Richardson, Tim Franklin and Phil Lee.
(10) Compensation for loss of office in 2009 was in respect of David Anderson £1,022,000 and Dick Parkhouse £728,000.

Table 2 – Pension details of executive directors

	Years of service[1]	Total accrued pension at 31 December 2010[1] £000	Increase in accrued pension during the year £000	Increase in accrued pension during the year (net of inflation) £000	Transfer value of previous column at 31 December 2010 net of members' contributions[3] £000	Transfer value of total accrued pension at 31 December 2009[3] £000	Transfer value of total accrued pension at 31 December 2010[3] £000	Increase in transfer values net of members' contributions[3] £000
Neville Richardson	12	140	18	13	174	2,423	2,903	433
Rod Bulmer[2]	3	13	6	6	20	53	99	25
Tim Franklin	10	87	11	7	77	1,310	1,536	199
Phil Lee	8	78	11	8	125	1,409	1,717	280
John Reizenstein[4]	7	5	–	–	–	89	99	10
Barry Tootell[2]	2	17	7	6	37	97	166	45

(1) Years of service include, where appropriate, pre-merger service with Britannia. The total accrued pension is that which would be paid annually on retirement at normal retirement age based on service to 31 December 2010 and includes any transferred-in benefits as appropriate.
(2) Members have the option of paying additional voluntary contributions to their respective pension scheme. Neither these contributions nor the benefits arising from them are shown in the above table.
(3) All transfer values have been calculated in accordance with the current transfer value method and basis in force for the scheme applicable to the executive director. This is set by the Trustee(s), after taking actuarial advice, to be consistent with the requirements of legislation and the rules of the scheme.
(4) John Reizenstein opted out of joining the PACE Scheme on 6 April 2006 and became entitled to a deferred pension. He is paid a pension allowance of 16% of basic salary in lieu of pension provision. Deferred pensions are revalued under the PACE Scheme rules but no account has been taken of this in the above table. He resigned as an executive director on 7 December 2010. The details on the table are calculated at that date.

Remuneration report continued

Table 3 – Non-executive directors' remuneration

Non-executive directors	Date appointed	2010 fees £000[1]	2009 fees £000
Duncan Bowdler[5]	2009	16	8
Paul Flowers[3]	2009	83	11
Peter Marks[4]	2009	–	–
Ben Reid[5] [6]	2009	19	10
Len Wardle[5]	2006	16	13
Martyn Wates[4]	2007	–	–
Stephen Watts[5] [7]	2006	18	15
Bob Burlton[2]	2004	48	102
Independent professional non-executive directors (IPNEDs)			
Rodney Baker-Bates[8] [9]	2009	66	20
David Davies[8] [9]	2003	68	58
Peter Harvey[8] [10]	2009	57	24
Chris Jones[8] [14]	2009	72	28
Stephen Kingsley[8] [11]	2009	58	24
Bob Newton[8]	2007	56	53
Piers Williamson[8] [12]	2005	58	53
Professional non-executive director (PNED)			
Paul Hewitt[8] [13]	2003	66	62

(1) Fees for the year are based on 52 weeks compared to 51 weeks in 2009.
(2) Bob Burlton resigned with effect from 15 April 2010.
(3) Paul Flowers was appointed Chair with effect from 15 April 2010. His annual fee is £107,848.
(4) Peter Marks, Chief Executive of The Co-operative Group and Martyn Wates, Chief Executive of Food and Specialist Businesses are both employees and remunerated by The Co-operative Group and do not receive fees for serving on the CFS Board.
(5) The non-executive directors that also serve on the Group Board receive a fee of £15,555 per annum for serving on the CFS Board.
(6) Ben Reid, as a non-executive director who is a member of the CFS Audit and Regulatory Compliance Committee and who is not an IPNED, receives an additional £3,111 per annum.
(7) Stephen Watts, as a non-executive director who is a member of the CFS Exposures Committee and who is not an IPNED, receives an additional £2,074 per annum.
(8) Under their service contracts, the IPNEDs receive a fee of £57,002 per annum.
(9) The Deputy Chairs receive an additional fee of £15,000 per annum.
(10) The Chair of the CFS Exposures Committee receives an additional £5,000 per annum.
(11) The Chair of the CFS Banking Transformation Programme sub-committee receives an additional £7,000 per annum.
(12) The Chair of the CFS Risk Management Committee receives an additional £10,500 per annum.
(13) The Chair of the CFS Audit and Regulatory Compliance Committee receives an additional £10,500 per annum.
(14) The Chair of Illius Properties Limited receives a fee of £15,000 per annum.

Table 4 – Aggregate information in respect of code staff

Number of code staff	Total remuneration[1] £000	Total fixed remuneration[2] £000	Total variable remuneration[3] £000	Annual incentive plan[4] £000	Long term incentive plan[5] £000	Outstanding deferred remuneration[6] £000	Deferred reduced and paid £000	Sign on and severance payments £000	Severance payments made in year £000
Senior Management									
25[7]	8,306	4,395	3,911	1,482	2,429	5	–	–	–
Other code staff									
40	12,550	7,510	5,040	2,529	2,511	194	–	–	–

The table above represents the emoluments of code staff in relation to their services for the CFS Group.

(1) Total remuneration consists of base salary as at 31 December 2010, allowances, employer pension contributions and incentive payments relating to the 2010 financial year together with future earnings opportunity comprised in the 2011–13 long term incentive awards.
(2) Total fixed remuneration is base salary as at 31 December 2010 plus allowances and employer pension contributions.
(3) Total variable remuneration is the sum of the annual incentive plan payments in respect of the 2010 financial year and the awards made under the 2011–13 long term incentive plan. The awards under the 2011–13 long term plan are performance related and, to the extent achieved will be payable in 2014. All payments as and when due are made in cash.
(4) Payments made under the annual incentive plan are in respect of the 2010 financial year.
(5) Awards made under the 2011–13 long term incentive plan are all unvested and represent deferred remuneration in respect of the 2010 financial year, in accordance with the FSA code.
(6) The outstanding deferred remuneration is deferred cash where no long term incentive award is made or the award is insufficient to satisfy the deferral percentage required by the FSA.
(7) Senior management consists of executive directors, members of the executive committee and non-executive directors.

Independent auditor's report

We have audited the financial statements of The Co-operative Bank plc for the year ended 31 December 2010 set out on pages 30 to 75 and pages 78 to 123. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and reporting on corporate governance, on terms that have been agreed. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and reporting on corporate governance, those matters that we have agreed to state to them in our report, and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the directors' responsibilities statement set out on page 16, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www.frc.org.uk/apb/scope/private.cfm.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2010 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU;
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion:

- the information given in the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the information given in the corporate governance statement set out on pages 17 to 22 with respect to internal control and risk management systems in relation to financial reporting processes and about share capital structures is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

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

Under the Listing Rules we are required to review the directors' statement, set out on page 15, in relation to going concern.

In addition to our audit of the financial statements, the directors have engaged us to review their corporate governance statement as if the company were required to comply with the Listing Rules and the Disclosure Rules and Transparency Rules of the Financial Services Authority in relation to those matters. Under the terms of our engagement, we are required to review the part of the corporate governance statement on pages 17 and 18 relating to the company's compliance with the nine provisions of the June 2008 Combined Code specified for our review.

Andrew Walker, Senior Statutory Auditor
for and on behalf of KPMG Audit Plc,
Statutory Auditor
Chartered Accountants
St James Square
Manchester
M2 6DS

29 March 2011

Consolidated income statement

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

	Notes	**Before significant items 2010**	**Significant items 2010**	**After significant items 2010**	Before significant items 2009	Significant items 2009	After significant items 2009
Interest receivable and similar income	4	**1,713.3**	**–**	**1,713.3**	1,061.6	–	1,061.6
Interest expense and similar charges	4	**(1,104.9)**	**–**	**(1,104.9)**	(481.9)	–	(481.9)
Net interest income		**608.4**	**–**	**608.4**	579.7	–	579.7
Fee and commission income	5	**237.2**	**(13.1)**	**224.1**	210.8	–	210.8
Fee and commission expense	5	**(60.3)**	**–**	**(60.3)**	(47.2)	–	(47.2)
Net fee and commission income		**176.9**	**(13.1)**	**163.8**	163.6	–	163.6
Net trading income	6	**4.6**	**–**	**4.6**	5.2	–	5.2
Other operating income	7	**8.1**	**–**	**8.1**	6.9	–	6.9
Operating income		**798.0**	**(13.1)**	**784.9**	755.4	–	755.4
Operating expenses	8	**(571.9)**	**(46.7)**	**(618.6)**	(429.0)	(38.1)	(467.1)
Financial Services Compensation Scheme levies	32	**(11.5)**	**–**	**(11.5)**	(3.7)	–	(3.7)
Operating profit before impairment losses		**214.6**	**(59.8)**	**154.8**	322.7	(38.1)	284.6
Impairment losses on loans and advances	15	**(97.3)**	**–**	**(97.3)**	(116.1)	–	(116.1)
Impairment gains on investments	16	**1.5**	**–**	**1.5**	4.0	–	4.0
Operating profit		**118.8**	**(59.8)**	**59.0**	210.6	(38.1)	172.5
Share of post tax profits/(losses) from joint ventures	36	**0.7**	**–**	**0.7**	(0.1)	–	(0.1)
Profit before taxation and profit based payments		**119.5**	**(59.8)**	**59.7**	210.5	(38.1)	172.4
Profit based payments to members of The Co-operative Group		**(10.8)**	**–**	**(10.8)**	(7.8)	–	(7.8)
Profit before taxation		**108.7**	**(59.8)**	**48.9**	202.7	(38.1)	164.6
Income tax	10	**(29.8)**	**16.7**	**(13.1)**	(62.1)	10.7	(51.4)
Profit for the financial year		**78.9**	**(43.1)**	**35.8**	140.6	(27.4)	113.2
Attributable to:							
Equity shareholders	12	**79.5**	**(43.1)**	**36.4**	137.7	(27.4)	110.3
Minority interests		**(0.6)**	**–**	**(0.6)**	2.9	–	2.9
		78.9	**(43.1)**	**35.8**	140.6	(27.4)	113.2
Earnings per share (basic and diluted)	12	**1.67p**	**(0.90)p**	**0.77p**	3.60p	(0.72)p	2.88p

Results relating to the transfer of engagements of Britannia Building Society are included with effect from the date of completion on 31 July 2009.

The significant items in 2010 relate to a programme of investment and integration and to provisions made for customer redress (see note 8 and note 32).
The significant items in 2009 relate to a programme of investment and integration.

Consolidated statement of comprehensive income

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

	Group	
	2010	2009
Profit for the year – equity shareholders	**36.4**	110.3
(Loss)/profit for the year – minority interests	**(0.6)**	2.9
Profit for the financial year	**35.8**	113.2
Other comprehensive expense:		
Changes in cashflow hedges		
Net changes in fair value recognised directly in equity	**(3.5)**	(29.5)
Income tax	**1.5**	8.2
Net losses transferred from equity to income or expense	**(0.1)**	–
Changes in available for sale assets		
Net changes in fair value recognised directly in equity	**(25.4)**	28.6
Income tax	**6.2**	(7.4)
Net losses transferred from equity to income or expense	**4.8**	–
Income tax	**(1.3)**	–
Revaluation of equity shares	**–**	(3.2)
Income tax	**–**	0.9
Transferred to other operating income on disposal of equity shares	**–**	(0.7)
Income tax	**–**	0.2
Defined benefit plan actuarial losses	**(0.3)**	(0.3)
Income tax	**0.1**	0.1
Other comprehensive expense for the financial year, net of income tax	**(18.0)**	(3.1)
Total comprehensive income for the financial year	**17.8**	110.1
Attributable to:		
Equity shareholders	**19.0**	108.5
Minority interests	**(1.2)**	1.6
Total comprehensive income for the financial year	**17.8**	110.1

The accounting policies and notes on pages 37 to 123 form part of these financial statements.

Consolidated balance sheet

At 31 December 2010

All amounts are stated in £m unless otherwise indicated

	Notes	2010	2009 restated
Assets			
Cash and balances at central banks	13	**1,735.6**	1,706.8
Loans and advances to banks	14	**2,394.1**	1,781.5
Loans and advances to customers	15	**34,977.3**	34,073.7
Fair value adjustments for hedged risk	15	**166.8**	66.1
Investment securities – loans and receivables	16	**1,917.3**	2,486.2
Investment securities – available for sale	16	**2,985.8**	4,457.3
Derivative financial instruments	17	**931.9**	1,023.0
Equity shares	18	**7.2**	7.2
Investments in joint ventures	36	**2.5**	1.8
Goodwill	19	**0.6**	0.6
Intangible fixed assets	20	**45.1**	46.1
Investment properties	21	**162.3**	137.7
Property, plant and equipment	22	**98.5**	121.5
Amounts owed by other Co-operative Group undertakings	37	**0.6**	91.0
Other assets	23	**52.5**	22.1
Prepayments and accrued income	24	**16.2**	30.1
Deferred tax assets	33	**87.0**	86.1
Total assets		**45,581.3**	46,138.8
Liabilities			
Deposits by banks	25	**2,938.6**	6,082.4
Customer accounts	26	**32,320.0**	30,828.2
Customer accounts – capital bonds	27	**1,794.7**	1,647.1
Debt securities in issue	28	**4,212.2**	3,334.3
Derivative financial instruments	17	**702.4**	591.3
Other borrowed funds	29	**975.4**	946.5
Amounts owed to other Co-operative Group undertakings	37	**188.5**	329.2
Other liabilities	30	**146.8**	221.9
Accruals and deferred income	31	**131.3**	158.0
Provisions for liabilities and charges	32	**55.8**	52.8
Current tax liabilities		**42.5**	71.0
Total liabilities		**43,508.2**	44,262.7
Capital and reserves attributable to the Bank's equity holders			
Ordinary share capital	38	**410.0**	230.0
Share premium account	38	**8.8**	8.8
Retained earnings		**1,598.9**	1,562.8
Available for sale reserve		**(13.1)**	2.5
Cashflow hedging reserve		**36.9**	38.4
		2,041.5	1,842.5
Minority interests		**31.6**	33.6
Total equity		**2,073.1**	1,876.1
Total liabilities and equity		**45,581.3**	46,138.8

Approved by the Board on 29 March 2011 and signed on its behalf by:

Paul Flowers, Chair
Neville Richardson, Chief Executive
Moira Lees, Secretary

The accounting policies and notes on pages 37 to 123 form part of these financial statements.
Restated items are shown in notes 15, 32 and 33.

Registered number 990937

Bank balance sheet

At 31 December 2010

All amounts are stated in £m unless otherwise indicated

	Notes	2010	2009 restated
Assets			
Cash and balances at central banks	13	**1,735.6**	1,706.8
Loans and advances to banks	14	**1,728.6**	1,220.1
Loans and advances to customers	15	**23,844.9**	23,050.8
Fair value adjustments for hedged risk	15	**164.6**	60.6
Investment securities – loans and receivables	16	**1,986.8**	2,555.6
Investment securities – available for sale	16	**2,650.1**	4,060.6
Derivative financial instruments	17	**661.0**	660.8
Equity shares	18	**7.2**	7.2
Investments in Group undertakings	36	**1,458.9**	1,572.4
Goodwill	19	**0.6**	0.6
Intangible fixed assets	20	**43.8**	44.9
Property, plant and equipment	22	**79.1**	101.6
Amounts owed by other Co-operative Group undertakings		**14,233.7**	11,861.6
Other assets	23	**51.5**	45.8
Prepayments and accrued income	24	**14.5**	27.4
Deferred tax assets	33	**154.0**	210.3
Total assets		**48,814.9**	47,187.1
Liabilities			
Deposits by banks	25	**2,870.8**	5,613.0
Customer accounts	26	**29,912.0**	28,660.0
Customer accounts – capital bonds	27	**1,744.0**	1,581.7
Debt securities in issue	28	**1,856.8**	1,739.3
Derivative financial instruments	17	**697.4**	567.2
Other borrowed funds	29	**975.4**	946.5
Amounts owed to other Co-operative Group undertakings		**8,340.9**	5,765.0
Other liabilities	30	**140.5**	210.8
Accruals and deferred income	31	**117.0**	134.3
Provisions for liabilities and charges	32	**39.3**	45.0
Current tax liabilities		**17.3**	56.8
Total liabilities		**46,711.4**	45,319.6
Capital and reserves attributable to the Bank's equity holders			
Ordinary share capital	38	**410.0**	230.0
Share premium account	38	**8.8**	8.8
Retained earnings		**1,661.4**	1,588.5
Available for sale reserve		**(13.1)**	2.5
Cashflow hedging reserve		**36.4**	37.7
Total equity		**2,103.5**	1,867.5
Total liabilities and equity		**48,814.9**	47,187.1

Approved by the Board on 29 March 2011 and signed on its behalf by:

Paul Flowers, Chair
Neville Richardson, Chief Executive
Moira Lees, Secretary

The accounting policies and notes on pages 37 to 123 form part of these financial statements.
Restated items are shown in notes 32 and 36.

Registered number 990937

Consolidated statement of cash flows

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

	2010	2009
Cash flows from operating activities		
Profit before taxation	**48.9**	164.6
Adjustments for:		
Decrease in prepayments and accrued income	**16.0**	105.1
Decrease in accruals and deferred income	**(81.9)**	(67.2)
Interest payable in respect of subordinated liabilities	**45.5**	17.1
Effect of exchange rate movements	**(2.8)**	(96.0)
Effect of non-cash pension costs	**–**	0.2
Impairment losses on loans and advances	**97.3**	116.1
Movements on investment impairments	**(1.5)**	(4.0)
Depreciation and amortisation	**26.3**	22.4
Interest amortisation	**(6.3)**	(12.6)
Amortisation of investments	**(40.6)**	(0.8)
Loss on disposal of fixed assets	**0.8**	1.4
Unwind of fair value adjustments arising on transfer of engagements	**14.2**	(99.1)
Preference dividend	**5.6**	5.6
	121.5	152.8
Decrease in deposits by banks	**(3,143.8)**	(1,108.5)
Increase in customer accounts and capital bonds	**1,639.1**	872.0
Increase/(decrease) in debt securities in issue	**471.6**	(1,035.5)
Decrease/(increase) in loans and advances to banks	**401.5**	(1,037.5)
Increase in loans and advances to customers	**(850.6)**	(996.2)
Decrease in amounts owed by other Co-operative Group undertakings	**90.4**	46.9
(Decrease)/increase in amounts owed to other Co-operative Group undertakings	**(140.7)**	103.7
Net movement of other assets and other liabilities	**112.4**	82.1
Income tax paid	**(34.9)**	(23.4)
Net cash flows from operating activities	**(1,333.5)**	(2,943.6)
Cash flows from investing activities		
Cash and cash equivalents acquired on transfer of engagements	**–**	1,535.6
Purchase of tangible and intangible fixed assets	**(30.9)**	(15.1)
Proceeds from sale of investment properties	**0.5**	–
Purchase of investment securities	**(1,506.2)**	(1,814.8)
Proceeds from sale and maturity of investment securities	**3,757.2**	3,162.4
Net cash flows from investing activities	**2,220.6**	2,868.1
Cash flows from financing activities		
Interest paid on subordinated liabilities	**(44.8)**	(29.7)
Proceeds of issued shares	**180.0**	175.0
Preference share dividends paid	**(5.6)**	(5.6)
Dividends paid to minority shareholders in subsidiary undertaking	**(0.8)**	(0.9)
Net cash flows from financing activities	**128.8**	138.8
Increase in cash and cash equivalents	**1,015.9**	63.3
Cash and cash equivalents at the beginning of the financial year	**2,387.3**	2,324.0
Cash and cash equivalents at the end of the financial year	**3,403.2**	2,387.3
Cash and balances with central banks (note 13)	**1,699.5**	1,672.8
Loans and advances to banks (note 14)	**1,478.7**	462.5
Short term investments (note 16)	**225.0**	252.0
	3,403.2	2,387.3

The cash flows cannot be directly reconciled to the Group balance sheet movements as these movements include the non-cash unwinds of the fair value adjustments arising on the transfer of engagements of Britannia Building Society.

The accounting policies and notes on pages 37 to 123 form part of these financial statements.

Bank statement of cash flows

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

	2010	2009
Cash flows from operating activities		
Profit before taxation	**101.9**	201.8
Adjustments for:		
Decrease in prepayments and accrued income	**14.1**	119.4
Decrease in accruals and deferred income	**(67.2)**	(131.3)
Interest payable in respect of subordinated liabilities	**45.5**	17.1
Effect of exchange rate movements	**(2.8)**	(96.0)
Effect of non-cash pension costs	**–**	0.2
Impairment losses on loans and advances	**94.5**	114.9
Movements on investment impairments	**(1.5)**	(4.0)
Depreciation and amortisation	**26.5**	21.4
Interest amortisation	**(6.3)**	(12.6)
Amortisation of investments	**(82.6)**	(4.4)
Loss on disposal of fixed assets	**0.8**	1.5
Unwind of fair value adjustments arising on transfer of engagements	**(234.3)**	(99.1)
Dividends from subsidiary undertakings	**–**	0.2
Preference dividends	**5.6**	5.6
	(105.8)	134.7
Decrease in deposits by banks	**(2,742.2)**	(1,089.6)
Increase in customer accounts and capital bonds	**1,398.6**	486.7
Increase/(decrease) in debt securities in issue	**98.4**	(798.4)
Decrease/(increase) in loans and advances to banks	**517.1**	(499.8)
Increase in loans and advances to customers	**(812.3)**	(1,059.4)
(Increase)/decrease in amounts owed by other Co-operative Group undertakings	**(2,372.1)**	11.4
Increase in amounts owed to other Co-operative Group undertakings	**2,575.9**	38.2
Net movement of other assets and other liabilities	**151.0**	160.5
Income tax paid	**(10.6)**	(3.1)
Net cash flows from operating activities	**(1,302.0)**	(2,618.8)
Cash flows from investing activities		
Cash and cash equivalents acquired on transfer of engagements	**–**	889.6
Purchase of tangible and intangible fixed assets	**(4.3)**	(3.7)
Movements in investments in Group undertakings	**–**	310.4
Purchase of investment securities	**(126.2)**	(624.9)
Proceeds from sale and maturity of investment securities	**2,330.3**	1,947.5
Net cash flows from investing activities	**2,199.8**	2,518.9
Cash flows from financing activities		
Interest paid on subordinated liabilities	**(44.8)**	(29.7)
Proceeds of issued shares	**180.0**	175.0
Preference share dividends paid	**(5.6)**	(5.6)
Net cash flows from financing activities	**129.6**	139.7
Increase in cash and cash equivalents	**1,027.4**	39.8
Cash and cash equivalents at the beginning of the financial year	**2,363.6**	2,323.8
Cash and cash equivalents at the end of the financial year	**3,391.0**	2,363.6
Cash and balances with central banks (note 13)	**1,699.5**	1,672.8
Loans and advances to banks (note 14)	**1,466.5**	438.8
Short term investments (note 16)	**225.0**	252.0
	3,391.0	2,363.6

The cash flows cannot be directly reconciled to the Bank balance sheet movements as these movements include the non-cash unwinds of the fair value adjustments arising on the transfer of engagements of Britannia Building Society.

Consolidated and Bank statements of changes in equity

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

	Attributable to equity holders of the Company							
	Share capital	Share premium	Available for sale reserve	Cashflow hedging reserve	Retained earnings	Total	Minority interest	Total equity
Group								
2010								
Balance at the beginning of the year	**230.0**	**8.8**	**2.5**	**38.4**	**1,562.8**	**1,842.5**	**33.6**	**1,876.1**
Total comprehensive income for the financial year	**–**	**–**	**(15.6)**	**(1.5)**	**36.1**	**19.0**	**(1.2)**	**17.8**
Transactions with owners recorded directly in equity:								
Increase in share capital	**180.0**	**–**	**–**	**–**	**–**	**180.0**	**–**	**180.0**
Dividend	**–**	**–**	**–**	**–**	**–**	**–**	**(0.8)**	**(0.8)**
Balance at the end of the year	**410.0**	**8.8**	**(13.1)**	**36.9**	**1,598.9**	**2,041.5**	**31.6**	**2,073.1**
Group								
2009								
Balance at the beginning of the year	55.0	8.8	(16.6)	59.1	641.5	747.8	32.9	780.7
Amounts arising on transfer of engagements	–	–	–	–	811.2	811.2	–	811.2
Total comprehensive income for the financial year	–	–	19.1	(20.7)	110.1	108.5	1.6	110.1
Transactions with owners recorded directly in equity:								
Increase in share capital	175.0	–	–	–	–	175.0	–	175.0
Dividend	–	–	–	–	–	–	(0.9)	(0.9)
Balance at the end of the year	230.0	8.8	2.5	38.4	1,562.8	1,842.5	33.6	1,876.1

	Attributable to equity holders of the Company					
	Share capital	Share premium	Available for sale reserve	Cashflow hedging reserve	Retained earnings	Total equity
Bank						
2010						
Balance at the beginning of the year	**230.0**	**8.8**	**2.5**	**37.7**	**1,588.5**	**1,867.5**
Total comprehensive income for the financial year	**–**	**–**	**(15.6)**	**(1.3)**	**72.9**	**56.0**
Transactions with owners recorded directly in equity:						
Increase in share capital	**180.0**	**–**	**–**	**–**	**–**	**180.0**
Balance at the end of the year	**410.0**	**8.8**	**(13.1)**	**36.4**	**1,661.4**	**2,103.5**
Bank						
2009						
Balance at the beginning of the year	55.0	8.8	(16.8)	58.2	610.7	715.9
Amounts arising on transfer of engagements	–	–	–	–	811.2	811.2
Total comprehensive income for the financial year	–	–	19.3	(20.5)	166.6	165.4
Transactions with owners recorded directly in equity:						
Increase in share capital	175.0	–	–	–	–	175.0
Balance at the end of the year	230.0	8.8	2.5	37.7	1,588.5	1,867.5

The accounting policies and notes on pages 37 to 123 form part of these financial statements.

Basis of preparation and significant accounting policies

For the year ended 31 December 2010

The Co-operative Bank plc is registered in England and Wales under the Companies Act 2006.

Basis of preparation

Both the parent company financial statements and the Group financial statements have been prepared and approved by the directors in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), and IFRS Interpretations Committee (IFRIC) guidance as adopted by the European Union (EU). On including the parent company financial statements here together with the Group financial statements, the Company is taking advantage of the exemption in s408 of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these approved financial statements. Information in respect of the Company alone is labelled throughout as 'Bank'.

The financial information has been prepared on the basis of recognition and measurement requirements of IFRS in issue that are endorsed by the EU and are effective for accounting periods beginning on or after 1 January 2010.

Standards and interpretations issued and effective

In preparing these consolidated financial statements, the Bank has adopted the following pronouncements during the year that are new or revised but have no material impact on the financial statements:

- Revised IFRS 3 Business Combinations (2008)

  This standard incorporates the following changes which will be applied prospectively:

  - The definition of a business has been broadened, which may result in more acquisitions being treated as business combinations.
  - Contingent consideration will be measured at fair value, with subsequent changes in fair value recognised in profit or loss.
  - Transaction costs, other than share and debt issue costs, will be expensed as incurred.
  - Any pre-existing interest in an acquiree will be measured at fair value, with the related gain or loss recognised in profit or loss.
  - Any non-controlling (minority) interest will be measured at either fair value, or at its proportionate interest in the identifiable assets and liabilities of an acquiree, on a transaction by transaction basis.

- Amended IAS 27 Consolidated and Separate Financial Statements (2008)

  This standard requires accounting for changes in ownership interests in a subsidiary that occur without loss of control, to be recognised as an equity transaction. When the Bank loses control of a subsidiary, any interest retained in the former subsidiary will be measured at fair value with the gain or loss recognised in profit or loss.

- Amended IAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items (2008)

  The standard was amended to clarify how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations.

- IFRIC 17 Distributions of Non-cash Assets to Owners

  This interpretation was issued to address when an entity should recognise, measure and account for any differences arising on dividends payable from non-cash assets.

Standards and interpretations issued but not yet effective

- IFRS 9 Financial Instruments: Classification and Measurement

  This new standard's objective is to gradually phase out IAS 39 Financial Instruments: Recognition and Measurement. Phase one of this process specifically requires financial assets to be classified as at amortised cost or at fair value. Consequently, the available for sale (AFS) category currently used by the Bank will become void.

  Early adoption is permitted, once endorsed by the EU. The impact of IFRS 9 is likely to be material to the Bank once it becomes effective as of 1 January 2013.

- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments

  This interpretation addresses the accounting by an entity when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor of the entity to extinguish all or part of the financial liability. It does not address the accounting by the creditor.

  The impact of this interpretation is considered to be immaterial to the Bank.

- Revised IAS 24 *Related Party Disclosures*

  IAS 24 requires entities to disclose in their financial statements information about transactions with related parties. In broad terms, two parties are related to each other if one party controls, or significantly influences, the other party.

  The standard simplifies the disclosure requirements for government related entities and clarifies the definition of a related party. The revised standard is effective for annual periods beginning on or after 1 January 2011, with earlier application permitted.

  The impact of this revision is considered to be immaterial to the Bank.

  Other standards and interpretations have been issued but these are not considered to be relevant to the Bank's operations.

Basis of preparation and significant accounting policies continued
For the year ended 31 December 2010

Basis of preparation continued

Going concern

The Group's business activities together with its financial position, and the factors likely to affect its future development and performance are set out in the business and financial review on pages 5 to 8. In addition, the risk management section on pages 45 to 77 includes the Group's objectives, policies and processes for managing its liquidity risk, details of financial instruments and hedging activities, and its exposure to credit risk and liquidity risk. The capital management section provides information on the Bank's capital policies and capital resources.

In common with many financial institutions, the Group meets its day to day liquidity requirements through managing both its retail and wholesale funding sources, and is required to maintain a sufficient buffer over regulatory capital requirements in order to continue to be authorised to carry on its business. The Group's forecasts and objectives, taking into account a number of potential changes in trading performance and funding retention, show that the Group should be able to operate at adequate levels of both liquidity and capital, for the foreseeable future. The Group has also considered a number of stress tests on capital and liquidity and these provide assurance that the Bank is sufficiently capitalised and adequately positioned in excess of liquidity stress tests.

Consequently, after making enquiries, the directors are satisfied that the Group has sufficient resources to continue in business for the foreseeable future and have therefore continued to adopt the going concern basis in preparing the financial statements.

Use of estimates and judgments

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

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

Information about significant areas of estimation, uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements are described within the risk management section on pages 45 to 77 and the critical judgments section on pages 79 to 81.

Prior year restatements

In accordance with IFRS 3, the Bank has 12 months from the date of the merger with Britannia in which to complete the initial accounting for the merger. The Bank has reassessed the carrying values of the Britannia assets and liabilities acquired and made the following adjustments:

The carrying value of loans and advances to customers has been increased following a review of the probabilities of default of assets that were neither past due nor impaired at the merger date. Based on further information that has become available, the Bank has reassessed the fair value of provisions for liabilities and charges.

The impact of this adjustment is not material to the overall level of adjustments to the carrying values of Britannia assets and liabilities that were made on merger and there is no change to the amount of goodwill arising.

Change in accounting reference date

Following the transfer of engagements of Britannia Building Society, the Bank changed its accounting reference date to 31 December. Where these financial statements refer to 'year ended 31 December 2009' this represents the 51 week period from 11 January to 31 December 2009.

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

(a) Business combinations

On 1 August 2009 The Co-operative Bank plc merged with Britannia Building Society, with Britannia transferring their engagements to the Company.

This business combination has been accounted for applying the requirements of IFRS 3: Business Combinations (2004).

The consideration transferred was valued by reference to the members' interests acquired. Financial assets and liabilities which, following the Group's accounting policies, would be carried at amortised cost, were brought on to the balance sheet at their fair value at acquisition and were subsequently carried at amortised cost using the effective interest rate method. The income statement includes the results of the engagements transferred from Britannia since the date of acquisition. Details of the combination are given in note 39.

(b) Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled by the Bank. Control exists when the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The financial statements have been prepared using uniform accounting policies and are based on the same accounting period as the Bank.

Intra-group balances and transactions, and any unrealised gains and losses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

Special purpose entities

Special purpose entities (SPEs) are entities that are created to accomplish a narrow and well defined objective, for the Bank this includes:

- various securitisation transactions in which mortgages were sold to SPEs. The equity of these SPEs is not owned by the Bank.
- Covered Bond Limited Liability Partnerships created in order to act as a guarantor for the issue of covered bonds (refer to note 36 for further information).

An SPE is consolidated if, based on an evaluation of the substance of its relationship with the Bank and the SPE's risks and rewards, the Bank concludes that it controls the SPE.

Significant accounting policies continued

The following circumstances may indicate a relationship in which, in substance, the Bank controls and consequently consolidates an SPE:

- the activities of the SPE are being conducted on behalf of the Bank according to its specific business needs so that the Bank obtains benefits from the SPE's operation.
- the Bank has the decision making powers to obtain the majority of the benefits of the activities of the SPE.
- the Bank has the rights to obtain the majority of the benefits of the SPE and therefore may be exposed to the risks incidental to the activities of the SPE.
- the Bank retains the majority of the residual or ownership risks related to the SPE or its assets in order to obtain benefits from its activities.

The assessment of whether the Bank has control over an SPE is carried out at inception. No further assessment of control is carried out unless changes in the structure or terms of the SPE or additional transactions between the Bank and the SPE occur.

Interests in joint ventures

The Bank's interests in joint ventures are accounted for using the equity method. The consolidated financial statements include the Bank's share of the income and expenses and equity movements of equity accounted investees, after adjustments to align the accounting policies with those of the Bank.

(c) Revenue recognition

Interest income and expense

Interest income and expense is recognised on an effective interest rate (EIR) basis, inclusive of directly attributable incremental transaction costs and fees including arrangement and broker fees, valuation and solicitor costs, discounts and premiums where appropriate and loan closure based transactions ie early redemption and late notice fees.

The EIR basis spreads the interest income and expense over the expected life of each instrument. The EIR is the rate that, at the inception of the instrument, exactly discounts expected future cash payments and receipts through the expected life of the instrument back to the initial carrying amount. When calculating the EIR, the Group estimates cash flows considering all contractual terms of the instrument (for example, prepayment options) but does not consider assets' future credit losses except for assets acquired at a deep discount.

For assets acquired at a value significantly below the carrying value in the acquiree's financial statements because they have incurred loss, expectations of future loss are higher than at origination, and interest spreads have widened because of deteriorating market conditions, the calculation of EIR is the same as shown above with the exception that the estimates of future cash flows include anticipated credit losses.

Fees and commissions

Fee and commission income is predominantly made up of arrangement and other fees relating to loans and advances to customers that are included in the effective interest calculation. Commitment fees received are deferred and included in the effective interest calculation upon completion or taken in full at the date the commitment period expires and completion does not occur.

Fees and commissions payable to introducers in respect of obtaining lending business, where these are direct and incremental costs related to the issue of a financial instrument, are included in interest income as part of the effective interest rate. Other fees are taken to the income statement.

All other fee and commission income that is not included in the effective interest calculation is recognised on an accruals basis as the service is provided.

(d) Significant items

Items which are material by both size and nature (ie outside of the normal operating activities of the Bank) are treated as significant items and disclosed separately on the face of the income statement.

The separate reporting of significant items helps provide an indication of the Bank's underlying business performance. Events which may give rise to the classification of items as significant include individually significant restructuring costs.

(e) Financial instruments (excluding derivatives)

Recognition

The Group initially recognises loans and advances, deposits, debt securities issued and other borrowed funds on the date at which they are originated.

Regular way purchases and sales of financial assets are recognised on the trade date at which the Group commits to purchase or sell the asset. All other financial assets and liabilities are initially recognised on the trade date at which the Group becomes a party to the contractual provisions of the instrument.

Financial assets

The Bank classifies its financial assets (excluding derivatives) as either:

- Loans and receivables;
- Available for sale; or
- Financial assets at fair value through income statement.

i) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and the Group does not intend to sell immediately or in the near term. These are initially measured at fair value plus transaction costs that are directly attributable to the financial asset. Subsequently, these are measured at amortised cost using the effective interest method. The amortised cost is the amount advanced less principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the amount advanced and the maturity amount less impairment provisions for incurred losses.

Loans and receivables mainly comprise loans and advances to banks and customers (except where the Group has elected to carry the loans and advances to customers at fair value through income or expense as described in accounting policy (e) iii) below) and assets reclassified from available for sale (see below).

Basis of preparation and significant accounting policies continued
For the year ended 31 December 2010

Significant accounting policies continued

ii) Available for sale

Available for sale financial assets are debt securities that are not held for trading and are intended to be held for an indefinite period of time. These are measured at fair value based on current bid prices where quoted in an active market. Where the securities are unlisted the fair values are based on valuation techniques including discounted cashflow analysis, with reference to relevant market rates, and other commonly used valuation techniques. Movements in fair value are recorded in equity as they occur. On disposal, gains and losses recognised previously in equity are transferred to the income statement. In exceptional circumstances, for instance where the market in the securities has become inactive, the Group has reclassified such assets as loans and receivables.

Any transfer back from loans and receivables, upon reclassification, would be measured at fair value based on current bid prices where quoted in an active market. Where there is no active market or the securities are unlisted the fair values are based on valuation techniques including discounted cashflow analysis, with reference to relevant market rates, and other commonly used valuation techniques.

iii) Financial assets at fair value through income or expense

These are either:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term;
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short term profit taking; or
- upon initial recognition designated at fair value through income or expense to eliminate or significantly reduce a measurement and recognition inconsistency or where management specifically manages an asset or liability on that basis ie capital bonds.

These are measured at fair value based on current bid prices where quoted in an active market. Where there is no active market or the securities are unlisted the fair values are based on valuation techniques including discounted cashflow analysis, with reference to relevant market rates, and other commonly used valuation techniques. Gains and losses arising from changes in the fair value are brought into the income statement within trading income as they arise.

iv) Impairment provision

At the balance sheet date, the Bank assesses its financial assets not at fair value through income or expense for objective evidence that an impairment loss has been incurred.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of a loan or advance on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, or the disappearance of an active market for a security.

The Group considers evidence for impairment for loans and advances at both a specific asset and collective level. All individually significant loans and advances are assessed specifically for impairment. Loans and advances not individually significant are collectively assessed for impairment by grouping together loans and advances by similar risk characteristics.

In assessing collective impairment the Group uses statistical modelling of historical trends of probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

The amount of the loss is the difference between:

- the asset's carrying amount; and
- the present value of estimated future cash flows (discounted at the asset's original or variable effective interest rate for amortised cost assets and at the current market rate for available for sale assets).

Impairment of financial assets carried at amortised cost

The amount of the impairment loss on assets carried at amortised cost is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised through the use of an allowance account.

A write off is made when all or part of a claim is deemed uncollectible or forgiven after all the possible collection procedures have been completed and the amount of loss has been determined. Write offs are charged against previously established provisions for impairment or directly to the income statement. Any additional recoveries from borrowers, counterparties or other third parties made in future periods are offset against the write off charge in the income statement once they are received.

Provisions are released at the point when it is deemed that following a subsequent event the risk of loss has reduced to the extent that a provision is no longer required.

Impairment of financial assets classified as available for sale

Available for sale assets are assessed at each balance sheet date to see whether there is objective evidence of impairment. In such cases, any impairment losses are recognised by transferring the cumulative loss that has been recognised directly in equity to income or expense.

When a subsequent event causes the amount of impaired loss on available for sale investment securities to decrease and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the income statement. However any further recovery in fair value of an impaired available for sale equity security is recognised directly in equity.

Significant accounting policies continued

v) Derecognition of financial assets

Financial assets are derecognised when:

- the rights to receive cash flows from the asset have ceased; or
- the Bank has transferred substantially all the risks and rewards of ownership of the assets.

When available for sale financial assets are derecognised the cumulative gain or loss, including that previously recognised in reserves, is recognised in the income statement.

vi) Financial liabilities

Financial liabilities are contractual obligations to deliver cash or another financial asset. Financial liabilities are recognised initially at fair value, net of directly attributable transaction costs.

Financial liabilities, other than derivatives and capital bonds, are subsequently measured at amortised cost.

Certain non-derivative financial liabilities included within customer accounts (capital bonds) have been designated at fair value upon initial recognition in the balance sheet. Changes in fair value are recognised through the income statement. The capital bonds are economically matched using equity linked derivatives, which do not meet the requirements for hedge accounting. Recording changes in fair value of both the derivatives and the related liabilities through the income statement most closely reflects the economic reality of the transactions. In doing so this accounting treatment eliminates a measurement inconsistency that would otherwise arise from valuing the capital bonds at amortised cost and the derivatives at fair value.

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

Borrowed funds

Borrowings are recognised initially at issue proceeds net of transaction costs incurred, equating to their fair value. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments. The Bank's preference shares are classified as financial liabilities as they carry the right to a fixed non-cumulative preferential dividend (further information is provided in note 29) and are subsequently presented in other borrowed funds. The dividends on these preference shares are recognised in the income statement as interest expense on an amortised cost basis using the effective interest method.

Subscribed capital

Subscribed capital is carried at the nominal value plus any share premium and a fair value adjustment for hedged risk where items are designated as part of a fair value hedge relationship.

Interest payable on perpetual subordinated bonds recognised in the income statement using the EIR method.

(f) Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(g) Sale and repurchase agreements

Securities sold subject to repurchase agreements (repos) are reclassified on the balance sheet as pledged assets when the transferee has the right by contract or custom to sell or repledge the assets. The liability to the transferee is also included on the balance sheet, in deposits from banks, other deposits or shares, as appropriate. The difference between sale and repurchase price is accrued over the life of the agreements using the EIR method.

Securities purchased under agreements to re-sell (reverse repos) are classified as loans and advances to banks on the balance sheet, as appropriate.

Securities lent to counterparties are retained on the balance sheet.

Securities borrowed are not recognised on the balance sheet, unless they are sold to third parties, in which case the purchase and sale are recorded. The obligation to return them is recorded at fair value as a trading liability.

(h) Derivative financial instruments and hedge accounting

Derivatives used for asset and liability management purposes

Derivatives are used to hedge interest and exchange rate exposures related to non-trading positions. Instruments used for hedging purposes include swaps, forward rate agreements, futures, options and combinations of these instruments. The Bank also uses equity derivatives to hedge the equity risks within its capital bonds.

Derivative financial instruments are stated at fair value based on quoted market prices in active markets, and where these are not available, using valuation techniques such as discounted cashflow models. Further information is provided on page 74. All derivatives are carried as assets when the fair value is positive and liabilities when the fair value is negative. The gain or loss on re-measurement to fair value is recognised immediately in the income statement except where derivatives qualify for cashflow hedge accounting.

On initial designation of derivatives and qualifying hedged items as a hedge, the Bank formally documents the relationship between the hedging instrument(s) and hedged item(s) including the risk management objective and strategy in undertaking the hedge transaction together with the method used to assess effectiveness of the hedging relationship.

The Bank makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, whether the hedging instruments are expected to be 'highly effective' on offsetting the changes in fair value or cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80%–125%.

Basis of preparation and significant accounting policies continued
For the year ended 31 December 2010

Significant accounting policies continued

Cashflow hedges

Where derivatives are designated as hedges of the exposure to variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the portion of the fair value gain or loss on the derivative that is determined to be an effective hedge is recognised directly in equity. The ineffective part of any gain or loss is recognised in the income statement immediately.

Cumulative amounts recognised through equity are recycled to the income statement in the period in which the underlying hedged item matures and its associated gain or loss affects the income statement. When a hedging relationship is designated, or the hedge becomes ineffective, hedge accounting is discontinued. The cumulative unrealised gain or loss remaining in equity continues to be held in equity, and is transferred to the income statement when the forecast transaction is recognised.

Where the gain or loss in equity relates to a forecast transaction is no longer expected to occur, the cumulative unrealised gain or loss remaining in equity is amortised to the income statement over the remaining life of the asset or liability as part of the item's effective interest rate, or all transferred to the income statement when a forecast transaction is recognised.

Fair value hedges

Where a derivative is designated as the hedging instrument to hedge the change in fair value of a recognised asset or liability or a firm commitment that could affect income or expense, changes in the value of the derivative are recognised immediately in the income statement together with changes in the fair value of the hedged item that are attributable to the hedged risk.

Fair values are based on quoted market prices in active markets, and where these are not available, using valuation techniques such as discounted cashflow models.

If the derivative expires or is sold, terminated, or exercised, or no longer meets the criteria for fair value hedge accounting, or the designation is revoked, then hedge accounting is prospectively discontinued. Any adjustment up to that point, to a hedged item for which the effective interest method is used, is amortised to income or expense as part of the recalculated effective interest rate of the item over its remaining life.

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

As part of its risk management process the Bank identifies portfolios whose interest rate risk it wishes to hedge. The portfolios may comprise only assets, only liabilities or both assets and liabilities. The Bank analyses each portfolio into repricing time periods based on expected repricing dates, by scheduling cash flows into the periods in which they are expected to occur. Using this analysis, the Bank decides the amount it wishes to hedge and designates as the hedged item an amount of assets or liabilities from each portfolio equal to this.

The Bank measures monthly the change in fair value of the portfolio relating to the risk that is being hedged. Provided that the hedge has been highly effective the Bank recognises the change in fair value of each hedged item in the income statement with the cumulative movement in its value being shown on the balance sheet as a separate item, fair value adjustment for hedged risk, either within assets or liabilities as appropriate. If the hedge no longer meets the criteria for hedge accounting, this amount is amortised to the income statement over the remaining average useful life of the hedge relationship.

The Bank measures the fair value of each hedging instrument monthly. The value is included in derivative financial instruments in either assets or liabilities as appropriate, with the change in value recorded in the income statement.

Any hedge ineffectiveness is recognised in the income statement as the difference between the change in fair value of the hedged item and the change in fair value of the hedging instrument.

Embedded derivatives

A derivative may be embedded in another instrument, known as the host contract. Where the economic characteristics and risks of an embedded derivative are not closely related to those of the host contract (and the host contract is not carried at fair value through income or expense), the embedded derivative is separated from the host and held on balance sheet at fair value.

Movements in fair value are posted to the income statement, whilst the host contract is accounted for according to the relevant accounting policy for that particular asset or liability.

Derivatives used for trading purposes

Derivatives entered into for trading purposes include swaps, forward rate agreements, futures, options and combinations of these instruments. Derivatives used for trading purposes are measured at fair value and any gains or losses are included in the income statement. The use of derivatives and their sale to customers as risk management products is an integral part of the Bank's trading activities.

Mortgage commitments

The Bank enters into derivative contracts to reduce the exposure to risk on mortgage commitments made (for example, where the Bank has made an irrevocable offer of a loan to a customer). Mortgage commitments are designated at fair value through income or expense, the corresponding derivative contracts are recorded at fair value and movements are recognised in the income statement.

Financial guarantee contracts

Other financial guarantees, in respect of intra group funding and the pension deficit in respect of the former Britannia Pension Scheme, between the Bank and its subsidiaries are treated as insurance contracts in accordance with IFRS 4. In accordance with the standard the recognised insurance liability is assessed based on the current estimate of forecast future cash flows. If this highlights that the liability is inadequate the liability is increased and the corresponding charge taken through income statement.

Significant accounting policies continued

(i) Property, plant and equipment

Items of property, plant and equipment are stated at cost less any accumulated depreciation and impairment losses. Depreciation is provided on a straight line basis at the following rates, which are estimated to write down the assets to realisable values at the end of their useful lives.

Freehold and long leasehold buildings	2% to 2.5% per annum
Short leasehold buildings	life of lease
Equipment	10% to 33.3% per annum
Vehicles	25% per annum

All items of property, plant and equipment are reviewed for indications of impairment on a regular basis and at each balance sheet date. Any impairment identified would be charged to the income statement.

(j) Intangible assets

Computer software

Computer software is stated at cost less cumulative amortisation and impairment. All costs directly attributable in the development of computer software for internal use are capitalised and classified as intangible assets where they are not an integral part of the related hardware and amortised over their useful life up to a maximum of seven years. For core systems, a review of the asset's useful life is carried out and a maximum useful life of up to ten years may be applied.

Goodwill

All business combinations are accounted for by applying the purchase method. Goodwill represents amounts arising on acquisition of subsidiaries, associates and joint ventures and represents the difference between the cost of the acquisition and the fair value of the identifiable assets, liabilities and contingent liabilities acquired.

If a business combination is achieved without transfer of consideration, the amount of goodwill is calculated by reference to the fair value of the Group's interest in the aquiree using a valuation technique. The technique involves assessing the future net profit of the acquiree and then discounting using a rate that reflects current market assessment of the time value of money and risks specific to the acquiree.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is not amortised but is tested for impairment on an annual basis. Where impairment is required the amount is recognised in the income statement and cannot be written back.

(k) Assets leased to customers

Finance leases

Income from assets leased to customers is credited to the income statement based on a pattern reflecting a constant periodic rate of return on the net investment in the lease.

(l) Assets leased from third parties

The Bank enters into leases for land and buildings and operating leases for vehicles.

Leases for land and buildings are split between leases for the land and leases for the buildings for accounting purposes only. The leases are separately assessed as to whether they are finance or operating leases.

Finance lease assets are initially recorded at the lower of fair value and the present value of the minimum lease payments, and subsequently in accordance with the relevant policy for the underlying asset. An equal liability is recorded in other liabilities. Interest is allocated to the lease payments so as to record a constant periodic rate of charge on the outstanding liability.

Operating lease payments are charged to the income statement on a straight line basis over the term of the lease and the asset is not recognised on the balance sheet.

The Bank policy is to provide for the minimum future lease payments on buildings that it does not currently use.

(m) Investment property

Property held for long term rental yields that is not occupied by the Bank or property held for capital appreciation is classified as investment property.

Investment property comprises freehold land and buildings. It is carried at fair value. Fair value is based on discounted expected future cashflows and is representative of current prices in an active market for similar properties in the same location and condition. No depreciation is provided on these properties. Any gain or loss arising from a change in fair value is recognised in the income statement.

If the Bank takes occupancy of an investment property it is reclassified as property, plant and equipment and its fair value at the date of reclassification becomes its cost for subsequent accounting purposes. Similarly, transfers to the investment property portfolio are made when occupancy by the Bank ceases and the property meets the criteria of an investment property under IAS 40. Prior to such a transfer the property is measured at fair value with any gain or loss recognised in the income statement.

(n) Cash and cash equivalents

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

Basis of preparation and significant accounting policies continued
For the year ended 31 December 2010

Significant accounting policies continued

(o) Income tax

Tax on the income statement for the year comprises current and deferred tax, which is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in the statement of comprehensive income.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided for is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(p) Pension costs

Defined contribution basis

With effect from 6 April 2006, the Bank, along with other businesses within The Co-operative Group, has participated in the Co-operative Group Pension (Average Career Earnings) Scheme (the PACE scheme). This scheme is a defined benefit scheme, the assets of which are held in a separate fund administered by trustees. As a group wide pension scheme, the PACE scheme exposes the participating businesses to actuarial risks associated with the current and former employees of other group companies, with the result that there is no consistent and reliable basis for allocating liabilities, assets and costs to individual companies participating in the scheme. Therefore pension costs in respect of the scheme are accounted for on a defined contribution basis and recognised as an expense in the income statement as incurred.

Former Britannia Building Society pension scheme

Following the transfer of engagements of Britannia Building Society (note 39), the Britannia defined benefit pension scheme transferred to The Co-operative Financial Services Management Services Limited (CFSMS), a fellow subsidiary undertaking of Co-operative Financial Services Limited. As this pension fund is not maintained by the Bank, pension costs in respect of the scheme are accounted for on a defined contribution basis and recognised as an expense in the income statement as incurred.

(q) Foreign currency

The functional and presentational currency for the Bank is sterling. Transactions in foreign currencies are translated at the foreign exchange rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to sterling at the foreign exchange rate ruling at that date. Foreign currency differences arising on retranslation are recognised in the income statement, except for foreign currency differences arising on retranslation of available for sale equity instruments or a qualifying cashflow hedge, which are recognised directly in the statement of comprehensive income. Foreign exchange differences arising on translation are recognised in the income statement. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair values are translated to sterling at the exchange rates prevailing at the dates the values were determined.

(r) Investments in group undertakings

Investments in subsidiaries are initially measured at fair value which equates to cost and subsequently valued at cost less impairment.

(s) Provisions for liabilities and charges

A provision is recognised in the balance sheet if the Bank has a legal or constructive obligation as a result of a past event and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(t) Profit based payments to members of The Co-operative Group

Members of The Co-operative Group receive a dividend based on their transactions with the Group and its subsidiaries including the Bank. The profit based payments to members of The Co-operative Group represent a recharge of the proportion of the dividend payable to the ultimate parent company, Co-operative Group Limited, where the underlying transaction is a Bank product. The recharge is recognised when the profit based payments are approved by The Co-operative Group Limited.

Risk management
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

The CFS group of companies including The Co-operative Financial Services Limited, Co-operative Insurance Society Limited (Life & Savings business), CIS General Insurance Limited, and The Co-operative Bank plc have a common Board composition.

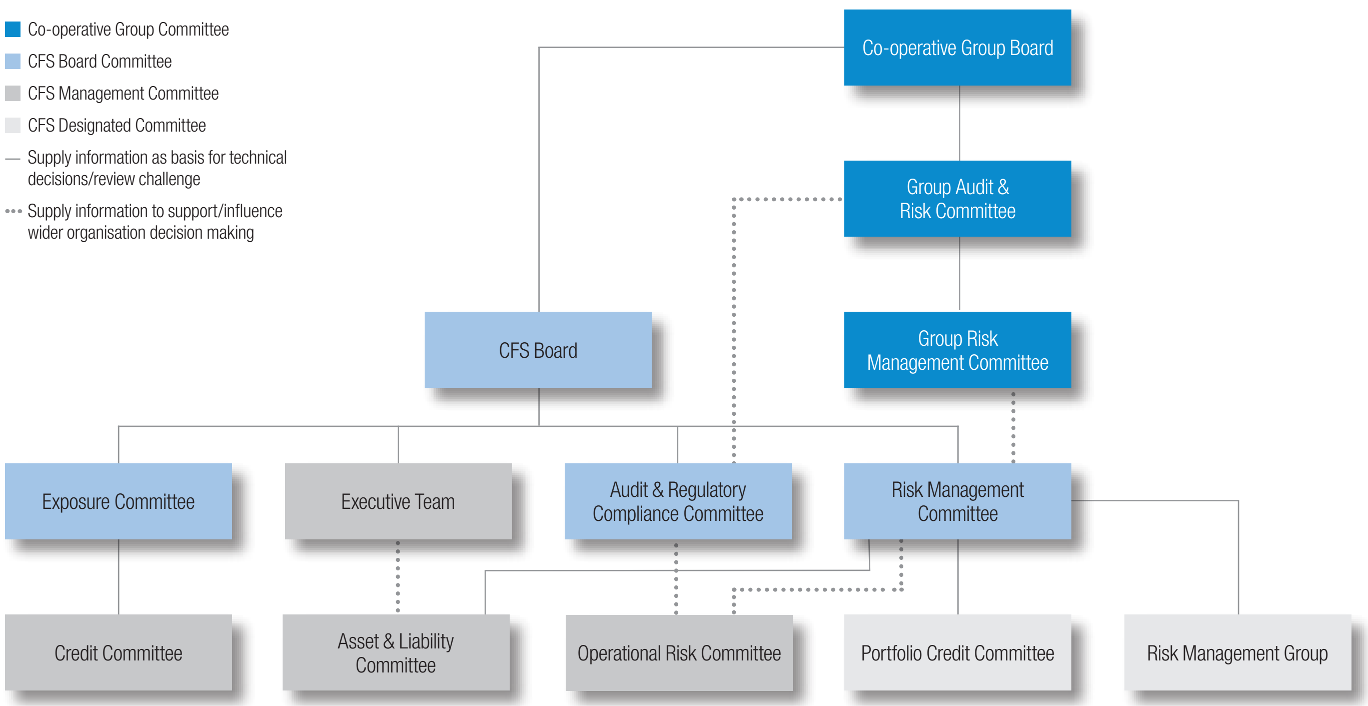
CFS has developed and implemented a common governance and organisation structure, with the same committee structure supporting each Board within the CFS Group.

The Board is responsible for approving the CFS strategy, its principal markets and the level of acceptable risks articulated through its statement of risk appetite. It is also responsible for overall corporate governance which includes ensuring that there is an adequate system of risk management and that the level of capital and liquidity held is consistent with the risk profile of the business.

The Board has established Board committees and senior management committees to administer, oversee and challenge the risk management process, identifying the key risks facing the business and assessing the effectiveness of planned management actions.

Specific Board authority has been delegated to Board committees and the Chief Executive who may, in turn, delegate elements of his discretions to appropriate executive directors and their senior line managers.

Risk management structure



The CFS Board delegates authority to the CFS Risk Management Committee (RMC) for monitoring compliance with the Board approved risk appetite statements. This includes:

- setting limits for individual types of risk; and
- approving (at least annually) and monitoring compliance with risk policies and delegated levels of authority.

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Risk management structure continued
CFS Risk Management Committee (RMC): this committee is responsible for the review and challenge of the adequacy of capital for all risks (including operational risk), and for technical risk management activities (including liiquidity) and portfolio exposures across CFS including:

- operation of mandates and limits and any breaches thereof;
- technical risk management policy approval;
- risk management information reporting and integrity of relevant data;
- risks adequately identified and measured;
- risk and portfolio exposure management strategy;
- adequacy of the risk mitigation process;
- review and discussion of technical risk issues identified as a result of internal audit work; and
- review and challenge the impact assessment of the strategic plan on the risk and capital profile of CFS.

CFS Audit & Regulatory Compliance Committee (ARCC): this committee provides oversight in relation to financial reporting, internal control, regulatory compliance, external and internal audit. It is responsible for approval of policies and review of adequacy of risk management activities in relation to operational risk.

CFS Exposures Committee: this committee ensures that non-executive directors are actively involved in major credit decisions (including sanctioning large counterparty transactions), monitors large exposures and problem loans and reviews the adequacy of individual credit provisions.

CFS Executive Team: the Executive Team manage the business in line with the Board risk appetite statement. It also maintains oversight of risk management processes and management information.

CFS risk and capital management sub committees
CFS Portfolio Credit Committee (PCC): this committee is a designated committee reporting to RMC and chaired by the Business Leader Banking Risk. It is responsible for defining Bank Group credit risk appetite; providing oversight and timely action in relation to credit risk management; monitoring, challenging and approving changes to Basel rating systems; and reviewing lending and arrears policies.

CFS Asset & Liability Committees (ALCO): these committees are management committees of the Board which are chaired by the Chief Financial Officer. They are primarily responsible for overseeing the management of interest rate, market, liquidity and funding risks and to advise on capital utilisation, in addition to, the composition and sourcing of adequate capital.

CFS Risk Management Group (RMG): this committee is a designated committee reporting to RMC and chaired by the Chief Risk Officer. Its purpose is to provide a mechanism to ensure that CFS wide technical risk management requirements, developments and processes are reviewed, challenged and approved (with escalation to RMC where required) and embedded within and across CFS. The committee also monitors all significant and emerging technical risks, and oversees the development and implementation of stress testing and risk appetite across CFS.

CFS Credit Committee: this committee is chaired by the Business Leader Banking Risk. The chair has delegated authority for approving credit facilities within approved strategies and delegated authorities.

CFS Operational Risk Committee (ORC): this committee interfaces with both the Executive Team and ARCC and is chaired by the Business Leader Regulatory Compliance and Operational Risk. It monitors significant operational risks and controls as well as the management actions taken to mitigate them to an acceptable level and/or transfer them. This includes business continuity arrangements and insurance cover to protect the CFS business. Capital requirements in relation to operational risk are monitored by the RMC.

There is also a framework of sector specific management committees supporting risk and capital management, implementing changes in business strategy, optimising performance, adherence to and setting of policy, and development of management information and training.

Bank significant risks
The Bank's significant risks arise in four broad categories:

- credit risk;
- market risk;
- liquidity risk; and
- operational risk.

Credit risk
Credit risk is the current or prospective risk to earnings and capital arising from a borrower's failure to meet the terms of any contract with the Bank or its failure to perform as agreed.

Credit risk is an integral part of many of our business activities and is inherent in traditional banking products (loans, commitments to lend and contingent liabilities, such as letters of credit) and in 'traded products' (derivative contracts such as forwards, swaps, options, repurchase agreements and securities borrowing and lending transactions).

The credit risk policies are approved by RMC (delegated authority from the Board) annually and are the responsibility of the Business Leader Banking Risk. The policies determine the criteria for the management of retail, corporate and wholesale risk, including securitisation, market exposures and credit management standards, country, sector and counterparty limits, along with risk appetites and delegated authorities.

All authority to take credit risk derives from the CFS Board. This is delegated through authorities to individuals or committees via the Chief Executive. The level of credit risk authority delegated depends on seniority and experience, varying according to the quality of the counterparty or any associated security or collateral held.

Credit risk continued

The Bank's retail secured and unsecured credit policy is to establish credit criteria which determine the optimum balance between volume growth (generating higher income) and higher bad debts, so as to maximise overall profitability within the Bank's risk appetite. The majority of retail credit risk related decisions are based on well founded and robust decision mechanisms designed to segregate customers into risk categories. There is a suite of bespoke, externally and internally developed application and behavioural scorecards derived from sound historic data. It is the responsibility of the Credit Risk Control Unit to design, select, implement, maintain and monitor these systems. The PCC and RMC receive regular reports on the performance of the portfolios.

The Bank's corporate sector policy is to maintain a broad sectoral spread of exposures which reflect the Bank's areas of expertise. Credit exposures to corporate and business banking customers are assessed individually. The quality of the overall portfolio is monitored using a credit grading system calibrated to expected loss. All aspects of credit management are controlled centrally. The PCC and RMC receive regular reports on the performance of the portfolio. The Exposures Committee receives regular reports on new facilities, bad debt provisions and the management of problem loans.

The Bank's wholesale market credit risk framework takes a holistic approach to risk management with, at its centre, a credit risk policy which governs the types of exposure the business can take and sets concentration parameters. To complement this, individual authority is delegated in terms of Internal Rating Grade (IRG) and associated Probability of Default (PD) to approve limits to individual counterparties within the parameters established by the credit risk policy. The PCC and RMC receive regular reports on the performance of the portfolio. The exposures committee receives regular reports on changes in exposure limits, watchlist and problem counterparty information.

Cash and balances at central banks are considered to be risk free and have been excluded from the following analysis of credit exposure.

Credit exposure

Group	Notes	**Gross balance 2010**	**Credit commitments 2010**	**Credit risk exposure 2010**	Gross balance 2009	Credit commitments 2009	Credit risk exposure 2009
Loans and receivables							
Loans and advances to banks	14	**2,394.1**	**176.0**	**2,570.1**	1,781.5	113.8	1,895.3
Loans and advances to customers	15	**35,199.9**	**4,717.7**	**39,917.6**	34,267.7	5,021.3	39,289.0
Investment securities	16	**1,930.3**	**–**	**1,930.3**	2,500.7	–	2,500.7
Available for sale financial assets							
Investment securities	16	**3,058.1**	**–**	**3,058.1**	4,529.2	–	4,529.2
Derivative financial instruments	17	**931.9**	**–**	**931.9**	1,023.0	–	1,023.0
		43,514.3	**4,893.7**	**48,408.0**	44,102.1	5,135.1	49,237.2
Allowance for impairment losses on loans and advances	15			**(222.6)**			(194.0)
Impairment losses on investments	16			**(85.3)**			(86.4)
Total carrying amount				**48,100.1**			48,956.8
Bank							
Loans and receivables							
Loans and advances to banks	14	**1,728.6**	**176.0**	**1,904.6**	1,220.1	113.8	1,333.9
Loans and advances to customers	15	**24,055.4**	**4,576.3**	**28,631.7**	23,242.8	4,763.6	28,006.4
Investment securities	16	**1,999.8**	**–**	**1,999.8**	2,570.1	–	2,570.1
Available for sale financial assets							
Investment securities	16	**2,722.4**	**–**	**2,722.4**	4,132.5	–	4,132.5
Derivative financial instruments	17	**661.0**	**–**	**661.0**	660.8	–	660.8
		31,167.2	**4,752.3**	**35,919.5**	31,826.3	4,877.4	36,703.7
Allowance for impairment losses on loans and advances	15			**(210.5)**			(192.0)
Impairment losses on investments	16			**(85.3)**			(86.4)
Total carrying amount				**35,623.7**			36,425.3

Credit commitments include revocable commitments which are unused credit card limits in Group and Bank of £2,344.9m (2009: £2,621.9m).

Notes 15 and 16 provide further analysis on concentration of credit risk.

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Credit risk continued
Credit risk analysis

2010 Group	**Loans and advances to banks**	**Loans and advances to customers**	**Investment securities loans and receivables**	**Investment securities available for sale**	**Derivative financial instruments**	**Total**
Individually impaired						
90 days past due or evidence of impairment	**–**	**1,715.4**	**25.0**	**72.3**	**–**	**1,812.7**
Impairment recognised	**–**	**(64.4)**	**(8.5)**	**(72.3)**	**–**	**(145.2)**
Carrying amount	**–**	**1,651.0**	**16.5**	**–**	**–**	**1,667.5**
Collectively impaired						
Less than 90 days past due	**–**	**243.7**	**119.2**	**–**	**–**	**362.9**
90–179 days past due	**–**	**18.4**	**–**	**–**	**–**	**18.4**
180 days plus past due	**4.6**	**143.4**	**–**	**–**	**–**	**148.0**
Impairment recognised	**–**	**(158.2)**	**(4.5)**	**–**	**–**	**(162.7)**
Carrying amount	**4.6**	**247.3**	**114.7**	**–**	**–**	**366.6**
Past due but not impaired						
0–29 days past due	**–**	**253.7**	**–**	**–**	**–**	**253.7**
30–59 days past due	**–**	**125.3**	**–**	**–**	**–**	**125.3**
60–89 days past due	**–**	**123.6**	**–**	**–**	**–**	**123.6**
Carrying amount	**–**	**502.6**	**–**	**–**	**–**	**502.6**
Neither past due nor impaired						
Low to medium risk	**2,565.5**	**32,134.9**	**1,786.1**	**2,974.9**	**931.9**	**40,393.3**
Medium to high risk	**–**	**5,159.2**	**–**	**10.9**	**–**	**5,170.1**
Carrying amount	**2,565.5**	**37,294.1**	**1,786.1**	**2,985.8**	**931.9**	**45,563.4**
Total carrying amount	**2,570.1**	**39,695.0**	**1,917.3**	**2,985.8**	**931.9**	**48,100.1**

2009 Group	Loans and advances to banks	Loans and advances to customers	Investment securities loans and receivables	Investment securities available for sale	Derivative financial instruments	Total
Individually impaired						
90 days past due or evidence of impairment	–	2,100.3	25.0	71.9	–	2,197.2
Impairment recognised	–	(53.6)	(8.5)	(71.9)	–	(134.0)
Carrying amount	–	2,046.7	16.5	–	–	2,063.2
Collectively impaired						
Less than 90 days past due	–	212.1	124.3	–	–	336.4
90–179 days past due	–	22.6	–	–	–	22.6
180 days plus past due	4.6	143.0	–	–	–	147.6
Impairment recognised	–	(140.4)	(6.0)	–	–	(146.4)
Carrying amount	4.6	237.3	118.3	–	–	360.2
Past due but not impaired						
0–29 days past due	–	281.0	–	–	–	281.0
30–59 days past due	–	125.0	–	–	–	125.0
60–89 days past due	–	52.1	–	–	–	52.1
Carrying amount	–	458.1	–	–	–	458.1
Neither past due nor impaired						
Low to medium risk	1,890.7	28,723.1	2,351.4	4,457.3	1,023.0	38,445.5
Medium to high risk	–	7,629.8	–	–	–	7,629.8
Carrying amount	1,890.7	36,352.9	2,351.4	4,457.3	1,023.0	46,075.3
Total carrying amount	1,895.3	39,095.0	2,486.2	4,457.3	1,023.0	48,956.8

Credit risk continued

2010 Bank	**Loans and advances to banks**	**Loans and advances to customers**	**Investment securities loans and receivables**	**Investment securities available for sale**	**Derivative financial instruments**	**Total**
Individually impaired						
90 days past due or evidence of impairment	**–**	**245.2**	**25.0**	**72.3**	**–**	**342.5**
Impairment recognised	**–**	**(52.3)**	**(8.5)**	**(72.3)**	**–**	**(133.1)**
Carrying amount	**–**	**192.9**	**16.5**	**–**	**–**	**209.4**
Collectively impaired						
Less than 90 days past due	**–**	**55.2**	**119.2**	**–**	**–**	**174.4**
90–179 days past due	**–**	**18.4**	**–**	**–**	**–**	**18.4**
180 days plus past due	**4.6**	**143.4**	**–**	**–**	**–**	**148.0**
Impairment recognised	**–**	**(158.2)**	**(4.5)**	**–**	**–**	**(162.7)**
Carrying amount	**4.6**	**58.8**	**114.7**	**–**	**–**	**178.1**
Past due but not impaired						
0–29 days past due	**–**	**52.0**	**–**	**–**	**–**	**52.0**
30–59 days past due	**–**	**39.3**	**–**	**–**	**–**	**39.3**
60–89 days past due	**–**	**29.6**	**–**	**–**	**–**	**29.6**
Carrying amount	**–**	**120.9**	**–**	**–**	**–**	**120.9**
Neither past due nor impaired						
Low to medium risk	**1,900.0**	**25,607.7**	**1,855.6**	**2,639.2**	**661.0**	**32,663.5**
Medium to high risk	**–**	**2,440.9**	**–**	**10.9**	**–**	**2,451.8**
Carrying amount	**1,900.0**	**28,048.6**	**1,855.6**	**2,650.1**	**661.0**	**35,115.3**
Total carrying amount	**1,904.6**	**28,421.2**	**1,986.8**	**2,650.1**	**661.0**	**35,623.7**

2009 Bank	Loans and advances to banks	Loans and advances to customers	Investment securities loans and receivables	Investment securities available for sale	Derivative financial instruments	Total
Individually impaired						
90 days past due or evidence of impairment	–	258.0	25.0	71.9	–	354.9
Impairment recognised	–	(51.6)	(8.5)	(71.9)	–	(132.0)
Carrying amount	–	206.4	16.5	–	–	222.9
Collectively impaired						
Less than 90 days past due	–	67.9	124.3	–	–	192.2
90–179 days past due	–	22.6	–	–	–	22.6
180 days plus past due	4.6	136.7	–	–	–	141.3
Impairment recognised	–	(140.4)	(6.0)	–	–	(146.4)
Carrying amount	4.6	86.8	118.3	–	–	209.7
Past due but not impaired						
0–29 days past due	–	52.2	–	–	–	52.2
30–59 days past due	–	29.6	–	–	–	29.6
60–89 days past due	–	15.0	–	–	–	15.0
Carrying amount	–	96.8	–	–	–	96.8
Neither past due nor impaired						
Low to medium risk	1,329.3	25,013.2	2,420.8	4,060.6	660.8	33,484.7
Medium to high risk	–	2,411.2	–	–	–	2,411.2
Carrying amount	1,329.3	27,424.4	2,420.8	4,060.6	660.8	35,895.9
Total carrying amount	1,333.9	27,814.4	2,555.6	4,060.6	660.8	36,425.3

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Credit risk continued

Analysis of impaired assets and associated collateral
Impaired assets
Loans and securities are considered impaired where it is determined that the Bank will be unable to collect all principal and interest outstanding, according to the contractual terms of the agreements.

The loan portfolios are reviewed on a periodic basis, usually once a month, to assess impairment. A loan will be deemed to be impaired where there is objective evidence that a loss event has occurred after recognition of an asset and prior to the balance sheet date.

Objective evidence of impairment on the loan portfolios includes:

Portfolio	**Impairment definition**
Corporate	• an instalment on a loan account is overdue, or has been in excess of its limit (or is overdrawn without an agreed limit) for 90 days or more;
	• if, as a result of lending being (either now or previously) at risk in distress, the Bank has agreed to a material postponement or forgiveness of interest and/or 'soft' rates or to a waiver and/or reduction of normal fees and charges, the accounts must be considered impaired while such favourable terms are being applied;
	• there has been a full or partial write off of debt, following which the account must remain impaired for at least six months;
	• there has been an event likely to result in insolvency which may involve bankruptcy, or the appointment of an administrative receiver, liquidator or administrator; or
	• if the Bank considers that at some point (normally taken as within the next 12 months) actions such as an issue of formal demand will be required in order to achieve full repayment.
Mortgages	• arrears outstanding are equivalent to three or more monthly instalments; or
	• we have commenced litigation against the borrower for repossession of the property against which the loan is secured.
Unsecured	• loans with any amount of arrears are treated as impaired.

For all portfolios the actual provision will depend on the expected roll rate to charge off or anticipated cash flow, and the estimated value of any supporting collateral.

Once a loan is defined as impaired the provision will be calculated as the difference between the current carrying value of the asset and the expected future recovery, discounted at the loan's effective interest rate, taking into account the expected charge-off rate and any supporting collateral. The table below shows the impairment rates of the various portfolios, shown by customer balance outstanding:

	2010				2009			
	Customer balance	**%**	**Impaired**	**%**	Customer balance	%	Impaired	%
Corporate	**10,456.0**	**28.1**	**664.0**	**6.4**	10,188.0	28.1	648.0	6.4
Mortgages	**25,222.0**	**68.0**	**1,838.8**	**7.3**	24,571.0	67.7	1,976.2	8.0
Unsecured:								
Credit cards	**606.0**	**1.6**	**96.2**	**15.9**	661.0	1.8	99.8	15.1
Loans	**810.0**	**2.2**	**43.0**	**5.3**	783.0	2.2	37.3	4.8
Overdrafts	**52.0**	**0.1**	**13.1**	**25.2**	56.0	0.2	14.5	25.9
	37,146.0	**100.0**	**2,655.1**	**7.1**	36,259.0	100.0	2,775.8	7.7

At the balance sheet date, the Bank assesses its debt securities for objective evidence that an impairment loss has occurred. For a debt security this may be the disappearance of an active market. For available for sale debt securities particular consideration is given to evidence of any significant difficulty of the issuer or measurable decrease in the estimated cash flows from the investments.

Renegotiation of retail lending
The Bank is committed to supporting borrowers who are in financial difficulties and will consider a range of treatments to help a borrower meet their loan commitments and clear any outstanding arrears. On secured lending, repossession of the property is always considered a last resort.

Alternative treatments for borrowers include arrangements to repay arrears over an extended period, or temporary concessions where arrears are allowed to increase for a temporary period. Such arrangements may be negotiated directly with the borrower or via a third party. Where such arrangement is made the loan will continue to be treated as impaired until such time as the arrears have been cleared in full.

In certain circumstances, as defined in the Bank's policy, we may agree to renegotiate a loan to repay outstanding arrears over the remaining term of the loan.

- On mortgages where such a renegotiation takes place, known as capitalisation, the loan will be classified as neither past due nor impaired, for so long as the mortgagors comply with the terms of their renegotiated contracts. During 2010, 541 secured loans (2009: 534) in the Group were renegotiated, including 86 (2009: eight) in the Bank. The balance of these loans as at 31 December 2010 in the Group was £63.2m (2009: £95.2m), including £5.8m (2009: £28.1m) in the Bank.
- On unsecured lending renegotiated loans, known as re-aged loans, will continue to be treated as impaired for a period of 12 months, or until three payments have been missed on the re-aged loan. The expected charge off rate will be based on the performance of other re-aged loans. At the end of 2010 there were £23.9m of re-aged loans.

Credit risk continued

Past due but not impaired

Loans and securities are considered past due where the contractual interest or principal payment are in arrears, however there are certain mitigating circumstances that may deem it necessary not to raise a provision for past due accounts (eg amount/days past due are immaterial). Provisions can be raised where accounts are not past due, this could be the stage of collection of amounts owed to the Bank or a specific event such as bankruptcy.

In the table past due but not impaired represents the outstanding balances on mortgages and unsecured retail lending where borrowers have failed to make payments when contractually due and the Bank expects that all contractual payments will be collected. This includes credit card exposures less than 30 days and 45 days for other retail unsecured lending. For mortgages, accounts up to 90 days in arrears but with no provision are classed as past due but not impaired.

Within the credit risk analysis table, low to medium risk has been defined as exposures where the PD is 1% or below over a one year time horizon for exposures on IRB approach under Basel II and slotting category strong/good/satisfactory for specialised lending exposures under the slotting approach. Medium to high risk has been defined as a PD of greater than 1% over a one year time horizon for exposure on IRB approach under Basel II and slotting category weak for specialised lending exposures under the slotting approach.

Within the treasury debt security portfolio 82% (2009: 82%) of exposures have an external credit rating equivalent to Fitch A or above.

The factors considered in determining if financial assets are individually impaired are stated above and within critical judgments on pages 79 to 81.

Fair value adjustments and provisions held against impaired exposures

When Britannia merged with The Co-operative Bank, the Britannia lending portfolios were carried into the newly merged entity at their fair value, taking account of future lifetime expected loss on the lending portfolios at 31 July 2009. The lifetime expected loss adjustment is offset against the Britannia gross lending balances in the combined entity's financial statements. The utilisation and allocation of the fair value adjustment is reviewed on a regular basis.

Description of collateral

The Bank uses collateral and guarantees to mitigate credit risk. Collateral is regularly revalued and guarantees reviewed to ensure continuing effectiveness. The majority of collateral held is not eligible financial collateral, it is residential real estate collateral for retail mortgages or either residential or commercial real estate collateral held against corporate lending.

When calculating the value of collateral for regulatory capital risk mitigation purposes, the appropriate valuation criteria contained within BIPRU is applied. When assessing the collateral valuations for corporate lending policy purposes, a more conservative written down value is used, stepped according to the risk level of the asset.

Where exposures are agreed on a secured basis, security cover is taken into account only where:

- the security is legally enforceable and is of a tangible nature and type;
- an appropriate, recent and reliable valuation is held; and
- a prudent margin is applied to the valuation, for the type of security involved.

Eligible financial collateral includes gilts held as part of reverse repo agreements, and cash as part of collateralised swaps or against corporate lending. The guarantees include parental guarantees held against subsidiary exposures.

At the reporting date the value of collateral held as security against financial assets was as follows:

	2010	2009
Fair value of collateral on financial assets which are past due but not impaired	**895.4**	966.9
Fair value of collateral on individually impaired financial assets	**1,956.1**	2,037.3
Carrying value of assets obtained by taking possession of collateral or calling on guarantees	**186.6**	229.0

Eurozone risk

All Eurozone exposures continue to be closely monitored especially those to financial institutions in Portugal, Ireland, Italy, Spain and Belgium. The Bank has no exposure to Greece.

Underlying term assets are deemed to be in run off, with associated counterparty and country limits reducing as assets mature and there is no new term exposure. All of the residual direct wholesale term exposure to these countries matures by mid 2012.

The Bank's exposure to these Eurozone countries (as valued for credit risk purposes) represented 2.4% of total Bank exposures.

Market risk

Market risk arises from the effect of changes in market prices of financial instruments, on income derived from the structure of the balance sheet, execution of customer and interbank business and proprietary trading. The majority of the risk arises from changes in interest rates.

Interest rate risk

Interest rate risk policy statements, approved by the RMC on behalf of the Board, specify the scope of the Bank's wholesale market activity, market risk limits and delegated authorities. The policy is managed by the Bank's ALCO which meets monthly and its prime task is to assess the interest rate risk inherent in the maturity and repricing characteristics of the Bank's assets and liabilities. It sets limits within which treasury and balance sheet management manage the effect of interest rate changes on the Bank's overall net interest income. Treasury is responsible for interest rate risk management for the Bank. The principal analytical techniques involve assessing the impact of different interest rate scenarios and changes in balances over various time periods.

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Market risk continued

The Board receives reports on the management of balance sheet risk and, each month, ALCO reviews the balance sheet risk position and the utilisation of wholesale market risk limits.

Non-treasury interest rate risk

The Bank (excluding wholesale) uses a gap report and earnings approach to managing interest rate risk, focusing in detail on the sensitivity of assumed changes in interest rates on net interest income for one year. Higher level analysis is performed for subsequent years.

ALCO monitors the non-trading interest rate risk which is split between certain wholesale portfolios, banking and investment books, and the rest of the Bank's balance sheet. The following describes the Bank non-trading portfolios excluding these certain wholesale portfolios. These positions are managed by treasury. All interest rate risk is centralised into treasury using appropriate transfer pricing rates.

Gap reports are based on defined time periods. ALCO set guidance limits around the gap, principally that the sum of positions maturing in greater than 12 months and non-sensitive balances (includes non-maturity deposits) is no more than a set limit.

Risk limits are formally calculated at each month end. Interest rate risk and effectiveness of hedging is monitored daily using gap positions, incorporating new business requirements. Draw down risk, in particular for fixed rate mortgages, is managed through weekly balance sheet meetings. Treasury undertake hedges for interest rate risk using derivative instruments and investment securities which are executed via the dealing room to wholesale markets, and loans and deposits which are executed internally with treasury.

The table below illustrates the sensitivity analysis relating to the 'core' Bank, a primary measure in the approach to managing interest rate risk.

The table illustrates the Present Value (PV) change based on a 1% shock in interest rates at the end of the year across the yield curve on the Bank's balances excluding wholesale treasury and customer currency balances (subject to a 0% floor), which are managed within the treasury risk framework. The shock results are driven by product pricing and product mix. The extent of rate movements and low rate environment have impacted the repricing of liability products resulting in larger exposure to rate shocks.

	100bp increase	**100bp decrease**
2010		
At the year end	**(9.0)**	**10.7**
Average for the period	**(12.8)**	**13.5**
Maximum sensitivity for the period	**(35.3)**	**37.3**
Minimum sensitivity for the period	**(0.2)**	**0.4**
2009		
At the year end	(0.2)	1.9
Average for the period	(4.4)	5.7
Maximum sensitivity for the period	(23.3)	25.6
Minimum sensitivity for the period	3.4	(3.7)

Treasury interest rate risk

Treasury executes short term funding and hedging transactions with the wholesale markets on behalf of the Bank and its customers. It also generates incremental income from proprietary trading within strict risk limits. There are two prime measures of risk supplemented by additional controls such as maturity and stop loss limits. Risk units express the various repricing and maturity mismatches as a common unit of measurement. Value at Risk (VaR) measures the daily maximum potential gain or loss due to market volatility within a statistical confidence level of 95% and a one day holding period. Simulation is being developed to provide VaR calculations to cover the combined core banking book positions. The VaR methodology has inherent limitations in that market volatility in the past, may not be a reliable predictor of the future, and may not reflect the time required to hedge or dispose of the position, hence VaR is not used as the sole measure of risk.

PV100

This illustrates the change in valuation on a fixed income portfolio experienced given a 1% increase and decrease in interest rates for treasury, representing treasury banking book and trading book combined. PV100 is the effect on the net present value (NPV) of the treasury portfolio to a parallel shift of 100 basis points upon the base yield curve. The effects of a 1% increase in interest rates are (£11.0m) (2009: £0.4m) and a 1% decrease £9.1m (2009: (£0.2m)).

Currency risk

The Bank's treasury foreign exchange activities are primarily:

- providing a service in meeting the foreign exchange requirements of customers;
- maintaining liquidity in euros and US dollars by raising funds and investing these to generate a return; and
- performing limited intraday trading and overnight positioning in major currencies to generate incremental income.

The table below provides an analysis of the Group's and Bank's assets and liabilities by currency.

Group	£ 2010	$ 2010	€ 2010	Other 2010	Total 2010	£ 2009	$ 2009	€ 2009	Other 2009	Total 2009
Assets										
Cash and balances at central banks	**1,735.6**	**–**	**–**	**–**	**1,735.6**	1,706.8	–	–	–	1,706.8
Loans and advances to banks	**1,879.9**	**35.4**	**475.3**	**3.5**	**2,394.1**	1,377.9	101.5	293.8	8.3	1,781.5
Loans and advances to customers	**34,683.2**	**61.6**	**217.4**	**15.1**	**34,977.3**	33,724.9	72.2	261.0	15.6	34,073.7
Fair value adjustments for hedged risk	**166.8**	**–**	**–**	**–**	**166.8**	66.1	–	–	–	66.1
Investment securities – loans and receivables	**1,500.0**	**68.1**	**294.0**	**55.2**	**1,917.3**	1,862.7	137.3	426.6	59.6	2,486.2
Investment securities – available for sale	**1,900.4**	**379.8**	**444.9**	**260.7**	**2,985.8**	2,441.0	613.3	1,042.4	360.6	4,457.3
Derivative financial instruments	**931.5**	**0.1**	**0.3**	**–**	**931.9**	1,022.7	–	0.3	–	1,023.0
Equity shares	**7.2**	**–**	**–**	**–**	**7.2**	7.2	–	–	–	7.2
Investments in joint ventures	**2.5**	**–**	**–**	**–**	**2.5**	1.8	–	–	–	1.8
Goodwill	**0.6**	**–**	**–**	**–**	**0.6**	0.6	–	–	–	0.6
Intangible fixed assets	**45.1**	**–**	**–**	**–**	**45.1**	46.1	–	–	–	46.1
Investment properties	**162.3**	**–**	**–**	**–**	**162.3**	137.7	–	–	–	137.7
Property, plant and equipment	**98.5**	**–**	**–**	**–**	**98.5**	121.5	–	–	–	121.5
Amounts owed by other Co-operative Group undertakings	**0.6**	**–**	**–**	**–**	**0.6**	91.0	–	–	–	91.0
Other assets	**47.2**	**0.7**	**2.9**	**1.7**	**52.5**	20.9	0.3	0.8	0.1	22.1
Prepayments and accrued income	**16.2**	**–**	**–**	**–**	**16.2**	30.1	–	–	–	30.1
Deferred tax assets	**87.0**	**–**	**–**	**–**	**87.0**	86.1	–	–	–	86.1
Total assets	**43,264.6**	**545.7**	**1,434.8**	**336.2**	**45,581.3**	42,745.1	924.6	2,024.9	444.2	46,138.8

Group	£ 2010	$ 2010	€ 2010	Other 2010	Total 2010	£ 2009	$ 2009	€ 2009	Other 2009	Total 2009
Liabilities										
Deposits by banks	**1,480.8**	**473.0**	**840.4**	**144.4**	**2,938.6**	4,056.5	488.0	1,397.5	140.4	6,082.4
Customer accounts	**32,205.8**	**23.6**	**88.9**	**1.7**	**32,320.0**	30,755.6	22.4	46.3	3.9	30,828.2
Customer accounts – capital bonds	**1,794.7**	**–**	**–**	**–**	**1,794.7**	1,647.1	–	–	–	1,647.1
Debt securities in issue	**4,007.4**	**–**	**204.8**	**–**	**4,212.2**	3,201.0	123.8	9.5	–	3,334.3
Derivative financial instruments	**689.2**	**5.2**	**6.8**	**1.2**	**702.4**	580.3	4.2	6.8	–	591.3
Other borrowed funds	**975.4**	**–**	**–**	**–**	**975.4**	946.5	–	–	–	946.5
Amounts owed to other Co-operative Group undertakings	**188.5**	**–**	**–**	**–**	**188.5**	329.2	–	–	–	329.2
Other liabilities	**141.3**	**1.5**	**2.8**	**1.2**	**146.8**	220.2	0.9	0.8	–	221.9
Accruals and deferred income	**131.3**	**–**	**–**	**–**	**131.3**	158.0	–	–	–	158.0
Provisions for liabilities and charges	**55.8**	**–**	**–**	**–**	**55.8**	52.8	–	–	–	52.8
Current tax liabilities	**42.5**	**–**	**–**	**–**	**42.5**	71.0	–	–	–	71.0
Total liabilities	**41,712.7**	**503.3**	**1,143.7**	**148.5**	**43,508.2**	42,018.2	639.3	1,460.9	144.3	44,262.7
Net on balance sheet position	**1,551.9**	**42.4**	**291.1**	**187.7**	**2,073.1**	726.9	285.3	564.0	299.9	1,876.1

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Currency risk continued

Bank	£ 2010	$ 2010	€ 2010	Other 2010	Total 2010	£ 2009	$ 2009	€ 2009	Other 2009	Total 2009
Assets										
Cash and balances at central banks	**1,735.6**	**–**	**–**	**–**	**1,735.6**	1,706.8	–	–	–	1,706.8
Loans and advances to banks	**1,214.4**	**35.4**	**475.3**	**3.5**	**1,728.6**	816.5	101.5	293.8	8.3	1,220.1
Loans and advances to customers	**23,665.1**	**50.3**	**114.4**	**15.1**	**23,844.9**	22,816.3	60.9	158.0	15.6	23,050.8
Fair value adjustments for hedged risk	**164.6**	**–**	**–**	**–**	**164.6**	60.6	–	–	–	60.6
Investment securities – loans and receivables	**1,569.5**	**68.1**	**294.0**	**55.2**	**1,986.8**	1,932.1	137.3	426.6	59.6	2,555.6
Investment securities – available for sale	**1,564.7**	**379.8**	**444.9**	**260.7**	**2,650.1**	2,044.3	613.3	1,042.4	360.6	4,060.6
Derivative financial instruments	**660.6**	**0.1**	**0.3**	**–**	**661.0**	660.5	–	0.3	–	660.8
Equity shares	**7.2**	**–**	**–**	**–**	**7.2**	7.2	–	–	–	7.2
Investments in Group undertakings	**1,458.9**	**–**	**–**	**–**	**1,458.9**	1,572.4	–	–	–	1,572.4
Goodwill	**0.6**	**–**	**–**	**–**	**0.6**	0.6	–	–	–	0.6
Intangible fixed assets	**43.8**	**–**	**–**	**–**	**43.8**	44.9	–	–	–	44.9
Property, plant and equipment	**79.1**	**–**	**–**	**–**	**79.1**	101.6	–	–	–	101.6
Amounts owed by other Co-operative Group undertakings	**14,168.8**	**–**	**64.9**	**–**	**14,233.7**	11,751.7	10.7	99.2	–	11,861.6
Other assets	**46.2**	**0.7**	**2.9**	**1.7**	**51.5**	44.6	0.3	0.8	0.1	45.8
Prepayments and accrued income	**14.5**	**–**	**–**	**–**	**14.5**	27.4	–	–	–	27.4
Deferred tax assets	**154.0**	**–**	**–**	**–**	**154.0**	210.3	–	–	–	210.3
Total assets	**46,547.6**	**534.4**	**1,396.7**	**336.2**	**48,814.9**	43,797.8	924.0	2,021.1	444.2	47,187.1

Bank	£ 2010	$ 2010	€ 2010	Other 2010	Total 2010	£ 2009	$ 2009	€ 2009	Other 2009	Total 2009
Liabilities										
Deposits by banks	**1,413.0**	**473.0**	**840.4**	**144.4**	**2,870.8**	3,587.1	488.0	1,397.5	140.4	5,613.0
Customer accounts	**29,797.8**	**23.6**	**88.9**	**1.7**	**29,912.0**	28,587.4	22.4	46.3	3.9	28,660.0
Customer accounts – capital bonds	**1,744.0**	**–**	**–**	**–**	**1,744.0**	1,581.7	–	–	–	1,581.7
Debt securities in issue	**1,652.0**	**–**	**204.8**	**–**	**1,856.8**	1,606.0	123.8	9.5	–	1,739.3
Derivative financial instruments	**684.2**	**5.2**	**6.8**	**1.2**	**697.4**	556.2	4.2	6.8	–	567.2
Other borrowed funds	**975.4**	**–**	**–**	**–**	**975.4**	946.5	–	–	–	946.5
Amounts owed to other Co-operative Group undertakings	**8,340.9**	**–**	**–**	**–**	**8,340.9**	5,765.0	–	–	–	5,765.0
Other liabilities	**135.0**	**1.5**	**2.8**	**1.2**	**140.5**	209.1	0.9	0.8	–	210.8
Accruals and deferred income	**117.0**	**–**	**–**	**–**	**117.0**	134.3	–	–	–	134.3
Provisions for liabilities and charges	**39.3**	**–**	**–**	**–**	**39.3**	45.0	–	–	–	45.0
Current tax liabilities	**17.3**	**–**	**–**	**–**	**17.3**	56.8	–	–	–	56.8
Total liabilities	**44,915.9**	**503.3**	**1,143.7**	**148.5**	**46,711.4**	43,075.1	639.3	1,460.9	144.3	45,319.6
Net on balance sheet position	**1,631.7**	**31.1**	**253.0**	**187.7**	**2,103.5**	722.7	284.7	560.2	299.9	1,867.5

At 31 December 2010 the Group and Bank's open position was £0.4m (2009: £0.7m) representing a potential loss of £nil given a 3% depreciation in sterling (2009: £nil). The open position is monitored against limits in addition to limits in place on individual currencies. All figures are in £ sterling equivalent.

Liquidity risk

Liquidity risk arises from the timing of cash flows generated from the Group's assets and liabilities (including derivatives). The Group's liquidity management policies are reviewed and approved annually by the RMC and compliance reviewed monthly by ALCO.

Liquidity risk arising from the structure of the balance sheet (structural liquidity) is managed to policies developed by ALCO. Liquidity risk is defined as the Board approved survival period under stress scenarios. The Bank undertakes various stress tests on a weekly basis.

The Bank has enhanced its liquidity management by introducing a liquidity risk framework which has a number of strategic and tactical measures that feed into an overall liquidity status score. The Bank's liquidity management framework is designed in line with FSA BIPRU regulations and industry guidelines, including Institute of International Finance and Bank for International Settlements recommendations.

The Bank manages liquidity risk by applying:

- a systematic control process embedded in the Bank's operations; and
- controlled end to end liquidity management with:
  - net outflows monitored to ensure they are within FSA limits;
  - maintenance of a well diversified deposit base;
  - management of stocks: high quality primary liquidity including cash, and secondary liquidity including certificates of deposit;
  - target strategic ratios; and
  - stress testing.

The strategic measures set by ALCO and monitored monthly are:

- wholesale borrowing ratio – the amount of wholesale borrowing compared to total liabilities;
- liquid asset ratio – amount of total assets that are liquid assets; and
- customer loan/deposit ratio – amount of customer loans funded by customer deposits.

Day to day cash flow (tactical liquidity) is managed by treasury within guidelines laid down by ALCO and in accordance with the standards established for all banks by the FSA.

The Bank has a high proportion of retail assets funded by retail deposits, ensuring there is no over reliance on wholesale funding. There are customer funding and wholesale funding ratios as described above which are set in line with the Board approved strategic plan. The Group's structural liquidity risk management is therefore retail based and is dependent on behavioural analysis of both customer demand and deposit and loan drawdown profiles by product category based on experience over the last ten years. The behaviour of retail products is reviewed by ALCO and in addition the Group has maturity mismatch limits to control the exposure to longer term mismatches.

The Bank's liquidity position is monitored on a daily basis and reported to ALCO each month. Treasury holds a pool of liquid assets on behalf of the Bank, and management actions are in place to provide additional liquidity when required. These sources of liquidity are held in order to be available to meet unexpected liquidity requirements.

Marketable assets are maintained as a liquidity pool against potential retail outflows; the liquidity pool is the highest quality debt and consists of high quality government issued debt, and cash at the Bank of England.

The Bank has access to a variety of medium term wholesale funding sources: securitisation, covered bond and Euro Medium Term Notes. The Bank will issue from the programmes as funding requirements and market conditions permit.

ALCO meets monthly and discusses the actual liquidity position and projected position incorporating business plans. As required a more regular meeting is held, this is typically when the markets have a heightened period of stress or liquidity shortage. The meetings ensure that the business plans are accurate and can be flexed as required.

Liquidity gap

The following table analyses assets and liabilities into relevant maturity groupings based on the remaining period of the balance sheet date to the contractual maturity date.

The Bank manages liquidity on a behavioural rather than contractual basis, reflecting where actual behaviour differs from contractual maturity:

- retail and corporate deposit bases are very stable, with deposits being attracted to the Bank by good customer service and its ethical policy. As a result, the deposit base remains stable whereas the contractual maturity is immediate for instant access deposits; and
- personal loan and visa balances are repaid earlier than their contractual maturity date.

These behavioural adjustments are based on historical experience of customer behaviour over a period of up to ten years.

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Liquidity risk continued

Gross contractual cash flow maturity analysis

Gross contractual cash flows include interest and other revenue cash flows. The following is an analysis of gross contractual cash flows of financial liabilities held at the balance sheet date:

2010 Group	Carrying value	Gross nominal outflow	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Non-derivative liabilities							
Deposits by banks	**2,938.6**	**2,931.0**	**776.3**	**415.8**	**774.4**	**964.5**	**–**
Customer accounts	**32,320.0**	**32,588.8**	**20,347.0**	**1,856.8**	**6,811.5**	**3,573.5**	**–**
Customer accounts – capital bonds	**1,794.7**	**1,749.4**	**11.4**	**64.1**	**254.8**	**1,362.6**	**56.5**
Debt securities in issue	**4,212.2**	**5,006.4**	**303.9**	**695.6**	**397.4**	**1,172.4**	**2,437.1**
Other borrowed funds	**975.4**	**1,799.6**	**45.8**	**4.7**	**58.0**	**420.8**	**1,270.3**
Amounts owed to other Co-operative Group undertakings	**188.5**	**188.5**	**188.5**	**–**	**–**	**–**	**–**
	42,429.4	**44,263.7**	**21,672.9**	**3,037.0**	**8,296.1**	**7,493.8**	**3,763.9**
Derivative liabilities							
Net outflow	**702.4**	**794.2**	**139.5**	**37.5**	**121.6**	**295.5**	**200.1**
	43,131.8	**45,057.9**	**21,812.4**	**3,074.5**	**8,417.7**	**7,789.3**	**3,964.0**
Other liabilities	**376.4**	**–**	**–**	**–**	**–**	**–**	**–**
Total recognised liabilities	**43,508.2**	**45,057.9**	**21,812.4**	**3,074.5**	**8,417.7**	**7,789.3**	**3,964.0**
Unrecognised loan commitments	**4,759.5**	**4,759.5**	**4,499.3**	**62.5**	**188.2**	**9.5**	**–**
Total liabilities	**48,267.7**	**49,817.4**	**26,311.7**	**3,137.0**	**8,605.9**	**7,798.8**	**3,964.0**

2009 Group	Carrying value	Gross nominal outflow	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Non-derivative liabilities							
Deposits by banks	6,082.4	6,092.8	531.4	4,309.4	710.3	540.5	1.2
Customer accounts	30,828.2	30,894.6	21,020.5	1,173.6	6,330.9	2,369.6	–
Customer accounts – capital bonds	1,647.1	1,594.3	11.6	42.8	343.8	1,139.9	56.2
Debt securities in issue	3,334.3	4,256.5	570.0	232.6	898.0	2,515.7	40.2
Other borrowed funds	946.5	2,119.8	115.4	64.2	82.0	438.1	1,420.1
Amounts owed to other Co-operative Group undertakings	329.2	329.2	92.6	236.6	–	–	–
	43,167.7	45,287.2	22,341.5	6,059.2	8,365.0	7,003.8	1,517.7
Derivative liabilities							
Net outflow	591.3	773.1	89.1	34.8	217.7	377.6	53.9
	43,759.0	46,060.3	22,430.6	6,094.0	8,582.7	7,381.4	1,571.6
Other liabilities	503.7	–	–	–	–	–	–
Total recognised liabilities	44,262.7	46,060.3	22,430.6	6,094.0	8,582.7	7,381.4	1,571.6
Unrecognised loan commitments	4,642.3	4,642.3	4,517.8	60.7	–	63.8	–
Total liabilities	48,905.0	50,702.6	26,948.4	6,154.7	8,582.7	7,445.2	1,571.6

Liquidity risk continued

2010 Bank	**Carrying value**	**Gross nominal outflow**	**Less than 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**
Non-derivative liabilities							
Deposits by banks	**2,870.8**	**2,931.0**	**776.3**	**415.8**	**774.4**	**964.5**	**–**
Customer accounts	**29,912.0**	**30,129.8**	**18,708.1**	**1,633.5**	**6,328.4**	**3,459.8**	**–**
Customer accounts – capital bonds	**1,744.0**	**1,652.8**	**9.3**	**58.0**	**232.1**	**1,296.9**	**56.5**
Debt securities in issue	**1,856.8**	**1,951.6**	**291.6**	**672.5**	**297.0**	**249.5**	**441.0**
Other borrowed funds	**975.4**	**1,799.6**	**45.8**	**4.7**	**58.0**	**420.8**	**1,270.3**
Amounts owed to other Co-operative Group undertakings	**8,340.9**	**8,340.9**	**8,340.9**	**–**	**–**	**–**	**–**
	45,699.9	**46,805.7**	**28,172.0**	**2,784.5**	**7,689.9**	**6,391.5**	**1,767.8**
Derivative liabilities							
Net outflow	**697.4**	**774.6**	**142.9**	**34.7**	**119.0**	**291.6**	**186.4**
	46,397.3	**47,580.3**	**28,314.9**	**2,819.2**	**7,808.9**	**6,683.1**	**1,954.2**
Other liabilities	**314.1**	**–**	**–**	**–**	**–**	**–**	**–**
Total recognised liabilities	**46,711.4**	**47,580.3**	**28,314.9**	**2,819.2**	**7,808.9**	**6,683.1**	**1,954.2**
Unrecognised loan commitments	**4,619.5**	**4,619.5**	**4,359.3**	**62.5**	**188.2**	**9.5**	**–**
Total liabilities	**51,330.9**	**52,199.8**	**32,674.2**	**2,881.7**	**7,997.1**	**6,692.6**	**1,954.2**

2009 Bank	Carrying value	Gross nominal outflow	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Non-derivative liabilities							
Deposits by banks	5,613.0	5,623.3	530.5	3,915.9	709.7	467.2	–
Customer accounts	28,660.0	28,736.8	19,694.8	910.6	5,798.4	2,324.0	9.0
Customer accounts – capital bonds	1,581.7	1,531.8	7.5	41.5	329.4	1,097.4	56.0
Debt securities in issue	1,739.3	1,592.0	568.4	189.9	93.6	700.0	40.1
Other borrowed funds	946.5	1,828.1	113.7	60.9	65.6	318.5	1,269.4
Amounts owed to other Co-operative Group undertakings	5,765.0	5,765.0	5,528.4	236.6	–	–	–
	44,305.5	45,077.0	26,443.3	5,355.4	6,996.7	4,907.1	1,374.5
Derivative liabilities							
Net outflow	567.2	567.2	92.8	12.3	43.1	320.2	98.8
	44,872.7	45,644.2	26,536.1	5,367.7	7,039.8	5,227.3	1,473.3
Other liabilities	446.9	–	–	–	–	–	–
Total recognised liabilities	45,319.6	45,644.2	26,536.1	5,367.7	7,039.8	5,227.3	1,473.3
Unrecognised loan commitments	4,604.3	4,604.3	4,479.8	60.7	–	63.8	–
Total liabilities	49,923.9	50,248.5	31,015.9	5,428.4	7,039.8	5,291.1	1,473.3

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Liquidity risk continued

Gross expected cashflow maturity analysis – behavioural

The following is an analysis of gross expected cash flow maturity. Liquidity cash flows are managed on a behavioural basis reflecting the actual behaviour of customers based on historic cash flow profiles over a period of ten years.

2010 Group	**Carrying value**	**Gross nominal outflow**	**Less than 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**
Non-derivative liabilities							
Deposits by banks	**2,938.6**	**2,931.0**	**776.3**	**415.8**	**774.4**	**964.5**	**–**
Customer accounts	**32,320.0**	**32,588.7**	**2,187.8**	**2,091.0**	**4,213.8**	**24,096.1**	**–**
Customer accounts – capital bonds	**1,794.7**	**1,749.4**	**11.4**	**64.1**	**254.8**	**1,362.6**	**56.5**
Debt securities in issue	**4,212.2**	**4,980.8**	**303.9**	**670.0**	**397.4**	**1,172.4**	**2,437.1**
Other borrowed funds	**975.4**	**1,799.6**	**45.8**	**4.7**	**58.0**	**420.8**	**1,270.3**
Amounts owed to other Co-operative Group undertakings	**188.5**	**188.5**	**188.5**	**–**	**–**	**–**	**–**
	42,429.4	**44,238.0**	**3,513.7**	**3,245.6**	**5,698.4**	**28,016.4**	**3,763.9**
Derivative liabilities							
Net outflow	**702.4**	**794.2**	**139.5**	**37.5**	**121.6**	**295.5**	**200.1**
	43,131.8	**45,032.2**	**3,653.2**	**3,283.1**	**5,820.0**	**28,311.9**	**3,964.0**
Other liabilities	**376.4**	**–**	**–**	**–**	**–**	**–**	**–**
Total recognised liabilities	**43,508.2**	**45,032.2**	**3,653.2**	**3,283.1**	**5,820.0**	**28,311.9**	**3,964.0**
Unrecognised loan commitments	**4,759.5**	**4,759.5**	**4,499.3**	**62.5**	**188.2**	**9.5**	**–**
Total liabilities	**48,267.7**	**49,791.7**	**8,152.5**	**3,345.6**	**6,008.2**	**28,321.4**	**3,964.0**

2009 Group	Carrying value	Gross nominal outflow	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Non-derivative liabilities							
Deposits by banks	6,082.4	6,092.7	531.4	4,309.3	710.3	540.5	1.2
Customer accounts	30,828.2	30,880.9	1,954.3	2,339.6	4,638.9	21,948.1	–
Customer accounts – capital bonds	1,647.1	1,594.3	11.6	42.8	343.8	1,139.9	56.2
Debt securities in issue	3,334.3	4,256.5	570.0	232.6	898.0	2,515.7	40.2
Other borrowed funds	946.5	2,119.8	115.4	64.2	82.0	438.1	1,420.1
Amounts owed to other Co-operative Group undertakings	329.2	329.2	92.6	236.6	–	–	–
	43,167.7	45,273.4	3,275.3	7,225.1	6,673.0	26,582.3	1,517.7
Derivative liabilities							
Net outflow	591.3	773.1	89.1	34.8	217.7	377.6	53.9
	43,759.0	46,046.5	3,364.4	7,259.9	6,890.7	26,959.9	1,571.6
Other liabilities	503.7	–	–	–	–	–	–
Total recognised liabilities	44,262.7	46,046.5	3,364.4	7,259.9	6,890.7	26,959.9	1,571.6
Unrecognised loan commitments	5,016.2	5,016.2	4,891.7	60.7	–	63.8	–
Total liabilities	49,278.9	51,062.7	8,256.1	7,320.6	6,890.7	27,023.7	1,571.6

Liquidity risk continued

2010 Bank	**Carrying value**	**Gross nominal outflow**	**Less than 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**
Non-derivative liabilities							
Deposits by banks	**2,870.8**	**2,931.0**	**776.3**	**415.8**	**774.4**	**964.5**	**–**
Customer accounts	**29,912.0**	**30,129.8**	**1,871.3**	**1,622.6**	**3,730.7**	**22,905.2**	**–**
Customer accounts – capital bonds	**1,744.0**	**1,637.4**	**9.3**	**58.0**	**231.7**	**1,283.6**	**54.8**
Debt securities in issue	**1,856.8**	**1,951.6**	**291.6**	**672.5**	**297.0**	**249.5**	**441.0**
Other borrowed funds	**975.4**	**1,799.6**	**45.8**	**4.7**	**58.0**	**420.8**	**1,270.3**
Amounts owed to other Co-operative Group undertakings	**8,340.9**	**8,340.9**	**8,340.9**	**–**	**–**	**–**	**–**
	45,699.9	**46,790.3**	**11,335.2**	**2,773.6**	**5,091.8**	**25,823.6**	**1,766.1**
Derivative liabilities							
Net outflow	**697.4**	**774.6**	**142.9**	**34.7**	**119.0**	**291.6**	**186.4**
	46,397.3	**47,564.9**	**11,478.1**	**2,808.3**	**5,210.8**	**26,115.2**	**1,952.5**
Other liabilities	**314.1**	**–**	**–**	**–**	**–**	**–**	**–**
Total recognised liabilities	**46,711.4**	**47,564.9**	**11,478.1**	**2,808.3**	**5,210.8**	**26,115.2**	**1,952.5**
Unrecognised loan commitments	**4,619.5**	**4,619.5**	**4,359.3**	**62.5**	**188.2**	**9.5**	**–**
Total liabilities	**51,330.9**	**52,184.4**	**15,837.4**	**2,870.8**	**5,399.0**	**26,124.7**	**1,952.5**

2009 Bank	Carrying value	Gross nominal outflow	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Non-derivative liabilities							
Deposits by banks	5,613.0	5,623.3	530.5	3,915.9	709.7	467.2	–
Customer accounts	28,660.0	28,715.9	1,498.4	1,207.2	4,106.5	21,903.8	–
Customer accounts – capital bonds	1,581.7	1,531.8	7.5	41.5	329.4	1,097.4	56.0
Debt securities in issue	1,739.3	1,592.0	568.4	189.9	93.6	700.0	40.1
Other borrowed funds	946.5	1,828.1	113.7	60.9	65.6	318.5	1,269.4
Amounts owed to other Co-operative Group undertakings	5,765.0	5,765.0	5,528.4	236.6	–	–	–
	44,305.5	45,056.1	8,246.9	5,652.0	5,304.8	24,486.9	1,365.5
Derivative liabilities							
Net outflow	567.2	567.2	92.8	12.3	43.1	320.2	98.8
	44,872.7	45,623.3	8,339.7	5,664.3	5,347.9	24,807.1	1,464.3
Other liabilities	446.9	–	–	–	–	–	–
Total recognised liabilities	45,319.6	45,623.3	8,339.7	5,664.3	5,347.9	24,807.1	1,464.3
Unrecognised loan commitments	4,760.6	4,760.6	4,636.1	60.7	–	63.8	–
Total liabilities	50,080.2	50,383.9	12,975.8	5,725.0	5,347.9	24,870.9	1,464.3

Demand deposits are shown as less than one month in the analysis above.

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities
The table below sets out a summary of the carrying and fair values of those financial assets and liabilities not presented on the Group and Bank balance sheets at fair value unless there is no significant difference between carrying and fair values.

		Group		Bank	
Category (as defined by IAS 39)	**Class (as determined by the Group)**	**Carrying Value**	**Fair Value**	**Carrying Value**	**Fair Value**
2010					
Financial assets					
Loans and receivables					
	Loans and advances to banks	**2,394.1**	**2,391.8**	**1,728.6**	**1,726.3**
	Loans and advances to customers	**35,144.1**	**35,771.0**	**24,009.5**	**24,510.1**
	Investment securities	**1,917.3**	**2,036.4**	**1,986.8**	**2,119.6**
Financial liabilities					
Financial liabilities at amortised cost					
	Deposits by banks	**2,938.6**	**2,971.1**	**2,870.8**	**2,903.3**
	Customer accounts	**32,320.0**	**32,400.8**	**29,912.0**	**29,985.7**
	Debt securities in issue	**4,212.2**	**4,831.7**	**1,856.8**	**1,898.6**
	Other borrowed funds	**975.4**	**1,107.4**	**975.4**	**1,107.4**

		Group		Bank	
		Carrying Value	Fair Value	Carrying Value	Fair Value
2009					
Financial assets					
Loans and receivables					
	Loans and advances to banks	1,781.5	1,780.5	1,220.1	1,219.1
	Loans and advances to customers	34,139.8	34,758.0	23,111.4	23,463.8
	Investment securities	2,486.2	2,489.4	2,555.6	2,558.8
Financial liabilities					
Financial liabilities at amortised cost					
	Deposits by banks	6,082.4	6,084.7	5,613.0	5,615.3
	Customer accounts	30,828.2	30,919.6	28,660.0	28,747.0
	Debt securities in issue	3,334.3	2,475.2	1,739.3	1,739.8
	Other borrowed funds	946.5	787.0	946.5	787.0

Key considerations in the calculation of fair values are as follows:

(a) Loans and advances to banks/deposits by banks

Loans and advances to banks include interbank placements and items in the course of collection.

The fair value of floating rate placements and overnight deposits is their carrying amount. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money market interest rates for debts with similar credit risk and remaining maturity. A credit loss adjustment has been applied based on expected loss amounts derived from the Bank's regulatory capital calculations.

(b) Loans and advances to customers

Fixed rate loans and advances to customers are revalued to fair value based on future interest cash flows (at funding rates) and principal cash flows discounted using the zero coupon rate. Forecast principal repayments are based on redemption at the earlier of maturity or repricing date with some overlay for historic behavioural experience where relevant. The eventual timing of future cash flows may be different from the forecast due to unpredictable customer behaviour. It is assumed there is no fair value adjustment required in respect of interest rate movement on variable rate assets. A credit loss adjustment has been applied based on expected loss amounts derived from the Bank's regulatory capital calculations.

(c) Customer accounts

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without quoted market price is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

(d) Customer accounts – capital bonds

The estimated fair value of customer accounts - capital bonds is based on independent third party valuations using forecast future movements in the appropriate indices.

Fair values of financial assets and liabilities continued

(e) Debt securities in issue and other borrowed funds

The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, a discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

(f) Investment securities

Fair value is based on market prices. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

(g) Derivatives

Futures and options are marked to market using listed market prices. For interest rate swaps, the estimated fair value is based on discounted cash flows using prevailing money market interest rates for instruments with similar remaining maturity.

Use of financial instruments

The use of financial instruments is essential to the Bank's business activities and financial instruments constitute a significant proportion of the Bank's assets and liabilities. Risk management procedures are described earlier in this report, and analysis of the financial instruments is provided in the notes to the financial statements.

The table below analyses financial instruments by measurement basis as defined by IAS 39.

Balance sheet categories	Held for Trading	Designated at fair value	Loans and receivables	Available for sale	Other amortised cost	Cash flow hedges	Total
2010							
Group							
Assets							
Cash and balances at central banks	–	–	1,735.6	–	–	–	1,735.6
Loans and advances to banks	–	–	2,394.1	–	–	–	2,394.1
Loans and advances to customers	–	74.1	35,070.0	–	–	–	35,144.1
Investment securities	–	28.7	1,917.3	2,957.1	–	–	4,903.1
Derivative financial instruments	67.0	646.1	–	–	–	218.8	931.9
Equity shares	–	–	–	7.2	–	–	7.2
Amounts owed by other Co-operative Group undertakings	–	–	0.6	–	–	–	0.6
Total financial assets	67.0	748.9	41,117.6	2,964.3	–	218.8	45,116.6
Non-financial assets							464.7
Total assets							45,581.3
Liabilities							
Deposits by banks	–	–	–	–	2,938.6	–	2,938.6
Customer accounts	–	–	–	–	32,320.0	–	32,320.0
Customer accounts – capital bonds	–	1,794.7	–	–	–	–	1,794.7
Debt securities in issue	–	–	–	–	4,212.2	–	4,212.2
Derivative financial instruments	52.9	487.6	–	–	–	161.9	702.4
Other borrowed funds	–	–	–	–	975.4	–	975.4
Amounts owed to other Co-operative Group undertakings	–	–	–	–	188.5	–	188.5
Total financial liabilities	52.9	2,282.3	–	–	40,634.7	161.9	43,131.8
Non-financial liabilities							376.4
Total liabilities							43,508.2
Capital and reserves							2,073.1
Total liabilities and equity							45,581.3

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued
Use of financial instruments

Balance sheet categories	Held for Trading	Designated at fair value	Loans and receivables	Available for sale	Other amortised cost	Cash flow hedges	Total
2009							
Group							
Assets							
Cash and balances at central banks	–	–	1,706.8	–	–	–	1,706.8
Loans and advances to banks	–	–	1,781.5	–	–	–	1,781.5
Loans and advances to customers	–	48.2	34,091.6	–	–	–	34,139.8
Investment securities	–	–	2,486.2	4,457.3	–	–	6,943.5
Derivative financial instruments	48.9	855.5	–	–	–	118.6	1,023.0
Equity shares	–	–	–	7.2	–	–	7.2
Amounts owed by other Co-operative Group undertakings	–	–	91.0	–	–	–	91.0
Total financial assets	48.9	903.7	40,157.1	4,464.5	–	118.6	45,692.8
Non-financial assets							446.0
Total assets							46,138.8
Liabilities							
Deposits by banks	–	103.8	–	–	5,978.6	–	6,082.4
Customer accounts	–	–	–	–	30,828.2	–	30,828.2
Customer accounts – capital bonds	–	1,647.1	–	–	–	–	1,647.1
Debt securities in issue	–	–	–	–	3,334.3	–	3,334.3
Derivative financial instruments	40.2	480.6	–	–	–	70.5	591.3
Other borrowed funds	–	–	–	–	946.5	–	946.5
Amounts owed to other Co-operative Group undertakings	–	–	–	–	329.2	–	329.2
Total financial liabilities	40.2	2,231.5	–	–	41,416.8	70.5	43,759.0
Non-financial liabilities							503.7
Total liabilities							44,262.7
Capital and reserves							1,876.1
Total liabilities and equity							46,138.8

Fair values of financial assets and liabilities continued

Use of financial instruments

Balance sheet categories	Held for Trading	Designated at fair value	Loans and receivables	Available for sale	Other amortised cost	Cash flow hedges	Total
2010							
Bank							
Assets							
Cash and balances at central banks	–	–	1,735.6	–	–	–	1,735.6
Loans and advances to banks	–	–	1,728.6	–	–	–	1,728.6
Loans and advances to customers	–	74.1	23,935.4	–	–	–	24,009.5
Investment securities	–	28.7	1,986.8	2,621.4	–	–	4,636.9
Derivative financial instruments	70.4	371.8	–	–	–	218.8	661.0
Equity shares	–	–	–	7.2	–	–	7.2
Amounts owed by other Co-operative Group undertakings	–	–	14,233.7	–	–	–	14,233.7
Total financial assets	70.4	474.6	43,620.1	2,628.6	–	218.8	47,012.5
Non-financial assets							1,802.4
Total assets							48,814.9
Liabilities							
Deposits by banks	–	–	–	–	2,870.8	–	2,870.8
Customer accounts	–	–	–	–	29,912.0	–	29,912.0
Customer accounts – capital bonds	–	1,744.0	–	–	–	–	1,744.0
Debt securities in issue	–	–	–	–	1,856.8	–	1,856.8
Derivative financial instruments	56.3	479.2	–	–	–	161.9	697.4
Other borrowed funds	–	–	–	–	975.4	–	975.4
Amounts owed to other Co-operative Group undertakings	–	5,848.7	–	–	2,492.2	–	8,340.9
Total financial liabilities	56.3	8,071.9	–	–	38,107.2	161.9	46,397.3
Non-financial liabilities							314.1
Total liabilities							46,711.4
Capital and reserves							2,103.5
Total liabilities and equity							48,814.9

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued
Use of financial instruments

Balance sheet categories	Held for Trading	Designated at fair value	Loans and receivables	Available for sale	Other amortised cost	Cash flow hedges	Total
2009							
Bank							
Assets							
Cash and balances at central banks	–	–	1,706.8	–	–	–	1,706.8
Loans and advances to banks	–	–	1,220.1	–	–	–	1,220.1
Loans and advances to customers	–	48.2	23,063.2	–	–	–	23,111.4
Investment securities	–	–	2,555.6	4,060.6	–	–	6,616.2
Derivative financial instruments	52.7	489.5	–	–	–	118.6	660.8
Equity shares	–	–	–	7.2	–	–	7.2
Amounts owed by other Co-operative Group undertakings	–	–	11,861.6	–	–	–	11,861.6
Total financial assets	52.7	537.7	40,407.3	4,067.8	–	118.6	45,184.1
Non-financial assets							2,003.0
Total assets							47,187.1
Liabilities							
Deposits by banks	–	103.8	–	–	5,509.2	–	5,613.0
Customer accounts	–	–	–	–	28,660.0	–	28,660.0
Customer accounts – capital bonds	–	1,581.7	–	–	–	–	1,581.7
Debt securities in issue	–	–	–	–	1,739.3	–	1,739.3
Derivative financial instruments	43.8	452.9	–	–	–	70.5	567.2
Other borrowed funds	–	–	–	–	946.5	–	946.5
Amounts owed to other Co-operative Group undertakings	–	3,397.6	–	–	2,367.4	–	5,765.0
Total financial liabilities	43.8	5,536.0	–	–	39,222.4	70.5	44,872.7
Non-financial liabilities							446.9
Total liabilities							45,319.6
Capital and reserves							1,867.5
Total liabilities and equity							47,187.1

Fair values of financial assets and liabilities continued

Valuation of financial instruments

The following table analyses financial assets and liabilities at fair value by the three level fair value hierarchy as defined within IFRS 7.

Group 2010		**Fair value measurement at end of the reporting period using:**			
Category (as defined by IAS 39)	**Class (as determined by the Group)**	**Quoted market prices in active markets Level 1**	**Valuation techniques using observable inputs Level 2**	**Valuation techniques using unobservable inputs Level 3**	**Total**
Financial assets					
Loans and receivables designated at fair value					
	Loans and advances to customers	**–**	**62.3**	**11.8**	**74.1**
	Total loans and receivables designated at fair value	**–**	**62.3**	**11.8**	**74.1**
Available for sale financial assets					
	Investment securities – available for sale	**902.9**	**2,054.2**	**–**	**2,957.1**
	Investment securities – designated at fair value	**–**	**28.7**	**–**	**28.7**
	Equity shares	**–**	**–**	**7.2**	**7.2**
	Total available for sale financial assets	**902.9**	**2,082.9**	**7.2**	**2,993.0**
Derivative financial instruments					
	Interest rate swaps				
	– designated as fair value hedges	**–**	**75.0**	**–**	**75.0**
	– designated as cash flow hedges	**–**	**218.8**	**–**	**218.8**
	– at fair value through income and expense	**–**	**90.1**	**–**	**90.1**
	Other	**–**	**548.0**	**–**	**548.0**
	Total derivative financial instruments	**–**	**931.9**	**–**	**931.9**
Total assets carried at fair value		**902.9**	**3,077.1**	**19.0**	**3,999.0**

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued
Valuation of financial instruments

Group 2010		Fair value measurement at end of the reporting period using:			
Category (as defined by IAS 39)	**Class (as determined by the Group)**	**Quoted market prices in active markets Level 1**	**Valuation techniques using observable inputs Level 2**	**Valuation techniques using unobservable inputs Level 3**	**Total**
Financial liabilities					
Financial liabilities designated at fair value					
	Capital bonds	**–**	**1,794.7**	**–**	**1,794.7**
	Total financial liabilities designated at fair value	**–**	**1,794.7**	**–**	**1,794.7**
Derivative financial instruments					
	Interest rate swaps				
	– designated as fair value hedges	**–**	**411.0**	**–**	**411.0**
	– designated as cash flow hedges	**–**	**161.9**	**–**	**161.9**
	– at fair value through income and expense	**–**	**86.6**	**–**	**86.6**
	Cross currency interest rate swaps				
	– designated as fair value hedges	**–**	**1.2**	**–**	**1.2**
	Other	**–**	**41.7**	**–**	**41.7**
	Total derivative financial instruments	**–**	**702.4**	**–**	**702.4**
Total liabilities carried at fair value		**–**	**2,497.1**	**–**	**2,497.1**

Fair values of financial assets and liabilities continued

Valuation of financial instruments

Group
2009

Fair value measurement at end of the reporting period using:

Category (as defined by IAS 39)	**Class (as determined by the Group)**	Quoted market prices in active markets Level 1	Valuation techniques using observable inputs Level 2	Valuation techniques using unobservable inputs Level 3	Total
Financial assets					
Loans and receivables designated at fair value					
	Loans and advances to customers	–	36.4	11.8	48.2
	Total loans and receivables designated at fair value	–	36.4	11.8	48.2
Available for sale financial assets					
	Investment securities – available for sale	942.7	3,514.6	–	4,457.3
	Equity shares	–	–	7.2	7.2
	Total available for sale financial assets	942.7	3,514.6	7.2	4,464.5
Derivative financial instruments					
	Interest rate swaps				
	– designated as fair value hedges	–	0.5	–	0.5
	– designated as cash flow hedges	–	118.1	–	118.1
	– at fair value through income and expense	–	170.1	–	170.1
	Cross currency interest rate swaps				
	– designated as fair value hedges	–	635.5	–	635.5
	Other	–	98.8	–	98.8
	Total derivative financial instruments	–	1,023.0	–	1,023.0
Total assets carried at fair value		942.7	4,574.0	19.0	5,535.7

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued
Valuation of financial instruments

Group
2009

Fair value measurement at end of the reporting period using:

Category (as defined by IAS 39)	**Class (as determined by the Group)**	Quoted market prices in active markets Level 1	Valuation techniques using observable inputs Level 2	Valuation techniques using unobservable inputs Level 3	Total
Financial liabilities					
Financial liabilities designated at fair value					
	Deposits from banks	–	103.8	–	103.8
	Capital bonds	–	1,647.1	–	1,647.1
	Total financial liabilities designated at fair value	–	1,750.9	–	1,750.9
Derivative financial instruments					
	Interest rate swaps				
	– designated as cash flow hedges	–	70.5	–	70.5
	– at fair value through income and expense	–	479.1	–	479.1
	Other	–	41.7	–	41.7
	Total derivative financial instruments	–	591.3	–	591.3
Total liabilities carried at fair value		–	2,342.2	–	2,342.2

The floating rate notes within available for sale assets have been restated from level 1 to level 2 in 2009 in line with emerging industry practice.

Fair values of financial assets and liabilities continued

Valuation of financial instruments

Bank
2010

Category (as defined by IAS 39)	Class (as determined by the Group)	Fair value measurement at end of the reporting period using: Quoted market prices in active markets Level 1	Valuation techniques using observable inputs Level 2	Valuation techniques using unobservable inputs Level 3	Total
Financial assets					
Loans and receivables designated at fair value					
	Loans and advances to customers	–	**62.3**	**11.8**	**74.1**
	Total loans and receivables designated at fair value	–	**62.3**	**11.8**	**74.1**
Available for sale financial assets					
	Investment securities – available for sale	**902.9**	**1,718.5**	–	**2,621.4**
	Investment securities – designated at fair value	–	**28.7**	–	**28.7**
	Equity shares	–	–	**7.2**	**7.2**
	Total available for sale financial assets	**902.9**	**1,747.2**	**7.2**	**2,657.3**
Derivative financial instruments					
	Interest rate swaps				
	– designated as fair value hedges	–	**75.0**	–	**75.0**
	– designated as cash flow hedges	–	**218.8**	–	**218.8**
	– at fair value through income and expense	–	**74.1**	**34.0**	**108.1**
	Other	–	**259.1**	–	**259.1**
	Total derivative financial instruments	–	**627.0**	**34.0**	**661.0**
Total assets carried at fair value		**902.9**	**2,436.5**	**53.0**	**3,392.4**

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued
Valuation of financial instruments

Bank
2010

Category (as defined by IAS 39)	Class (as determined by the Group)	Quoted market prices in active markets Level 1	Valuation techniques using observable inputs Level 2	Valuation techniques using unobservable inputs Level 3	Total
		Fair value measurement at end of the reporting period using:			
Financial liabilities					
Financial liabilities designated at fair value					
	Capital bonds	–	1,744.0	–	1,744.0
	Amounts owed to other Co-operative Group undertakings	–	–	5,848.7	5,848.7
	Total financial liabilities designated at fair value	–	1,744.0	5,848.7	7,592.7
Derivative financial instruments					
	Interest rate swaps				
	– designated as fair value hedges	–	403.8	–	403.8
	– designated as cash flow hedges	–	161.9	–	161.9
	– at fair value through income and expense	–	67.5	21.3	88.8
	Cross currency interest rate swaps				
	– designated as fair value hedges	–	1.2	–	1.2
	Other	–	41.7	–	41.7
	Total derivative financial instruments	–	676.1	21.3	697.4
Total liabilities carried at fair value		–	2,420.1	5,870.0	8,290.1

Fair values of financial assets and liabilities continued

Valuation of financial instruments

Bank
2009

Fair value measurement at end of the reporting period using:

Category (as defined by IAS 39)	**Class (as determined by the Group)**	Quoted market prices in active markets Level 1	Valuation techniques using observable inputs Level 2	Valuation techniques using unobservable inputs Level 3	Total
Financial assets					
Loans and receivables designated at fair value					
	Loans and advances to customers	–	36.4	11.8	48.2
	Total loans and receivables designated at fair value	–	36.4	11.8	48.2
Available for sale financial assets					
	Investment securities – available for sale	942.7	3,117.9	–	4,060.6
	Equity shares	–	–	7.2	7.2
	Total available for sale financial assets	942.7	3,117.9	7.2	4,067.8
Derivative financial instruments					
	Interest rate swaps				
	– designated as fair value hedges	–	0.5	–	0.5
	– designated as cash flow hedges	–	118.1	–	118.1
	– at fair value through income and expense	–	170.1	39.2	209.3
	Cross currency interest rate swaps				
	– designated as fair value hedges	–	233.1	–	233.1
	Other	–	99.8	–	99.8
	Total derivative financial instruments	–	621.6	39.2	660.8
Total assets carried at fair value		942.7	3,775.9	58.2	4,776.8

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued
Valuation of financial instruments

Bank
2009

Category (as defined by IAS 39)	Class (as determined by the Group)	Fair value measurement at end of the reporting period using: Quoted market prices in active markets Level 1	Valuation techniques using observable inputs Level 2	Valuation techniques using unobservable inputs Level 3	Total
Financial liabilities					
Financial liabilities designated at fair value					
	Deposits from banks	–	103.8	–	103.8
	Capital bonds	–	1,581.7	–	1,581.7
	Amounts owed to other Co-operative Group undertakings	–	–	3,397.6	3,397.6
	Total financial liabilities designated at fair value	–	1,685.5	3,397.6	5,083.1
Derivative financial instruments					
	Interest rate swaps				
	– designated as cash flow hedges	–	70.5	–	70.5
	– at fair value through income and expense	–	444.7	–	444.7
	Cross currency interest rate swaps				
	– designated as fair value hedges	–	11.9	–	11.9
	Other	–	40.1	–	40.1
	Total derivative financial instruments	–	567.2	–	567.2
Total liabilities carried at fair value		–	2,252.7	3,397.6	5,650.3

The floating rate notes within available for sale assets have been restated from level 1 to level 2 in 2009 in line with emerging industry practice.

Fair values of financial assets and liabilities continued

Movements in fair values of instruments with significant unobservable inputs were:

2010	Fair value at the beginning of the year	Purchases	Sales	Transfer of engagements	Profit or loss including impairment	Fair value at the end of the year
Group						
Loans and advances to customers	**11.8**	**–**	**–**	**–**	**–**	**11.8**
Equity shares	**7.2**	**–**	**–**	**–**	**–**	**7.2**
	19.0	**–**	**–**	**–**	**–**	**19.0**
Bank						
Loans and advances to customers	**11.8**	**–**	**–**	**–**	**–**	**11.8**
Derivative assets	**39.2**	**–**	**–**	**–**	**(5.2)**	**34.0**
Equity shares	**7.2**	**–**	**–**	**–**	**–**	**7.2**
Derivative liabilities	**–**	**–**	**–**	**–**	**(21.3)**	**(21.3)**
Amounts owed to other Co-operative Group undertakings	**(3,397.6)**	**(3,076.2)**	**625.1**	**–**	**–**	**(5,848.7)**
	(3,339.4)	**(3,076.2)**	**625.1**	**–**	**(26.5)**	**(5,817.0)**

2009	Fair value at the beginning of the year	Purchases	Sales	Transfer of engagements	Profit or loss including impairment	Fair value at the end of the year
Group						
Loans and advances to customers	13.8	(0.5)	–	–	(1.5)	11.8
Equity shares	8.8	–	–	1.5	(3.1)	7.2
	22.6	(0.5)	–	1.5	(4.6)	19.0
Bank						
Loans and advances to customers	13.8	(0.5)	–	–	(1.5)	11.8
Derivatives	29.9	–	–	–	9.3	39.2
Equity shares	8.8	–	–	1.5	(3.1)	7.2
Amounts owed to other Co-operative Group undertakings	(1,996.3)	(250.7)	648.9	(1,799.5)	–	(3,397.6)
	(1,943.8)	(251.2)	648.9	(1,798.0)	4.7	(3,339.4)

Valuation techniques

Fair values are determined according to the following hierarchy:

(a) Level 1 – Quoted market prices in active markets

Financial instruments with quoted prices for identical instruments in active markets. The best evidence of fair value is a quoted market price in an actively traded market.

(b) Level 2 – Valuation techniques using observable inputs

Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

The valuation techniques used to value these instruments employ only observable market data and relate to the following assets and liabilities:

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Fair values of financial assets and liabilities continued

Loans and advances to customers
Loans and advances to customers include corporate loans of £62.3m (2009: £36.4m) which are fair valued through income or expense using observable inputs. Loans held at fair value are valued at the sum of all future expected cash flows, discounted using a yield curve based on observable market inputs.

Investment securities – available for sale
Debt securities classified under valuation techniques using observable inputs are described in the critical judgments section on page 79.

Derivative financial instruments
OTC (ie non-exchange traded) derivatives are valued using valuation models which are based on observable market data. Valuation models calculate the present value of expected future cash flows, based upon 'no arbitrage' principles. The Bank enters into vanilla foreign exchange and interest rate swap derivatives, for which modelling techniques are standard across the industry. Examples of inputs that are generally observable include foreign exchange spot and forward rates, and benchmark interest rate curves.

(c) Level 3 – Valuation techniques using unobservable inputs
This is used for financial instruments valued using models where one or more significant inputs are not observable.

The small proportion of financial assets valued based on significant unobservable inputs are analysed as follows:

Loans and advances to customers
Loans and advances to customers include 25 year fixed rate mortgages £11.8m (2009: £11.8m) which are fair valued through income or expense using unobservable inputs. 25 year fixed rate mortgages are valued using future interest cash flows at the fixed customer rate and estimated schedule of customer repayments. Cash flows are discounted at a credit adjusted discount rate; the credit adjustment is based on the average margin of new long dated (5 years or greater) fixed rate business written in the last six months, and subject to quarterly review. The eventual timing of future cash flows may be different from that forecast due to unpredictable customer behaviour, particularly on a 25 year product. The valuation methodology takes account of credit risk and has decreased the valuation by £0.1m in 2010 (2009: increase of £0.2m). A reasonable change in the assumptions would not result in any material change in the valuation.

Equity shares
Primarily, equity shares relate to investments held in Vocalink Limited which are unquoted shares. The valuation of such shares is based on our percentage shareholding of the most recent public information valuation issued by the company.

Derivative financial instruments
Derivative financial instruments including internal interest rate swaps have been entered into during the year between the Bank and The Covered Bond LLP (LLP) and the Bank and Silk Road Finance Number One (Silk Rd 1).

The purpose of the swap is to convert the fixed and base rate linked revenue receipts of the pool of mortgage assets to the same LIBOR linked basis as the intercompany loan. Under this swap arrangement the LLP or Silk Rd 1 pays to the swap counterparty, the monthly mortgage revenue receipts of the pool of assets and receives from the swap counterparty LIBOR plus a contractual spread on the same notional balance; the spread being sufficient to cover the intercompany loan and any expenses.

The swap is valued based on an assumed amortisation profile of the pool of assets to the bond maturity date (assuming some annual prepayment), an assumed profile of customer receipts over this period, and LIBOR prediction using forward rates. Swap cash flows are discounted to present value using mid-yield curve zero coupon rates, ie no adjustment is made for credit losses, nor for transaction or any other costs.

The fair value of the swap is based on a valuation model that reflects the mortgage cash flows over a three year period using a discount rate based on LIBOR spreads. This derivative eliminates on consolidation.

Amounts owed to other Co-operative Group undertakings
Deposits from customers includes deposits by the LLP and Silk Rd 1 subsidiaries relating to the legal transfer of loans and advances on issue of the Bank's covered bonds and securitisation. The deposit is fair valued to eliminate an accounting mismatch of the swap derivative as discussed above.

Revaluation of the £5.9bn (2009: £3.4bn) mortgage pool from carrying to fair value is based on assumed timing of future mortgage capital and revenue receipts, discounted to present value using a credit adjusted discount rate.

The amortisation profile is as per the swaps valuation methodology, assuming some annual prepayment, but is extended beyond any bond maturity, until all the mortgages themselves mature, which is circa 25 years. Similarly, the revenue receipts are calculated as per the swap valuation methodology, but extended until all the mortgages mature. For fixed rate mortgages, revenue receipts are based on fixed customer rates within the assumed amortisation profile. For tracker, SVR and discount products, revenue receipts are assumed to be based on forward LIBOR rates plus the product margins. Fixed and tracker mortgages are assumed to revert to SVR at the end of any offer period. All mortgages in the covered bond pool were originated pre 31 December 2007.

The fair value of the swap is based on a valuation model that reflects the mortgage cash flows over a three year period using a discount rate based on LIBOR spreads. This derivative eliminates on consolidation.

Primary financial instruments used by the Bank

The main financial instruments used by the Bank, and the purposes for which they are held, are outlined below:

Customer loans and deposits

The provision of banking facilities to customers is the prime activity of the Bank and customer loans and deposits are major constituents of the balance sheet. Customer loans include retail mortgages, corporate loans, credit cards, unsecured retail lending and overdrafts. Customer deposits include retail and corporate current and saving accounts. The Bank has detailed policies and procedures to manage risks. In addition to mortgage lending, much of the lending to corporate and business banking customers is secured.

Debt securities, wholesale market loans and deposits

Debt securities include structured investments and credit trading vehicles. Further details are provided in critical judgments on page 79. Debt securities also underpin the Bank's liquidity requirements and generate incremental net interest and trading income.

The Bank issues medium term notes within an established euro medium term note programme and also issues certificates of deposit and commercial paper as part of its normal treasury activities. These sources of funds alongside wholesale market loans are invested in marketable, investment grade debt securities, short term wholesale market placements and used to fund customer loans.

Capital funds – subordinated note issues and preference shares

The Bank has a policy of maintaining prudent capital ratios and utilises a broad spread of capital funds. In addition to ordinary share capital and retained earnings, the Bank has issued £60m preference shares and, when appropriate, also issues perpetual and fixed term subordinated notes.

Foreign exchange

The Bank undertakes foreign exchange dealing to facilitate customer requirements and to generate incremental income from short term trading in the major currencies. Structured risk and trading related risk are managed formally within position limits approved by the Board.

Derivatives

A derivative is a financial instrument that derives its value from an underlying rate or price such as interest rates, exchange rates and other market prices. Derivatives are an efficient means of managing market risk and limiting counterparty exposure. The Bank uses them mainly for hedging purposes and to meet the needs of customers.

The most frequently used derivative contracts are interest rate swaps, exchange traded futures and options, caps and floors, forward rate agreements, currency swaps and forward currency transactions. Terms and conditions are determined by using standard industry documentation. Derivatives are subject to the same market and credit risk control procedures as are applied to other wholesale market instruments and are aggregated with other exposures to monitor total counterparty exposure which is managed within approved limits for each counterparty.

Risk management continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Unaudited risk management disclosures
The following risk management disclosure, operational risk and additional risks do not form part of the audited accounts and are not audited.

Operational risk
Operational risk is defined within CFS as the risk of loss resulting from inadequate or failed internal processes, people and systems or external events. This encompasses the effectiveness of risk management techniques and controls to minimise these losses.

Examples of such include internal and external fraud, loss or theft of confidential customer information, loss of key personnel, system capacity issues or program failure, process failures affecting payment settlement and external events over which CFS has limited controls such as terrorist attack, floods and contagious disease.

Operational risks are identified, managed and mitigated through ongoing risk management practices including risk assessments, formal control procedures, training, segregation of duties, delegated authorities and contingency planning. Operational risks are formally reviewed on a regular basis. Significant operational risks are regularly reported to executive directors, a management operational risk committee, and the ARCC (a formal Board sub-committee). These meet regularly to monitor the suitability of the risk management framework and management of significant risks within CFS. Capital requirements in relation to operational risk are monitored by the RMC.

Business continuity is managed from within the operational risk team and sets out to take appropriate steps to minimise the risk of disruption in the event of a sudden, unplanned occurrence that could seriously disrupt customer service, or pose a risk to employees, business operations and/or reputation. This includes developing and exercising crisis and incident management teams to maintain appropriate preparedness in the event of a major operational disruption. 2010 has seen a continued focus on developing our capability to respond to these threats.

CFS also has a corporate insurance programme to transfer specific risks to insurers as part of its risk management approach.

During 2009–2012 CFS has a significant change agenda to integrate and transform the combined business. Delivery and implementation of this change agenda is robustly planned and closely managed to ensure delivery is within clearly defined time, cost and quality criteria. As part of this the impact on the CFS operational risk profile (especially in terms of impact on our people, processes and systems) is assessed and managed (both in terms of reduction of risks through implementation of enhanced systems, and through close management of implementation of change).

Additional risks
In addition to the significant risks covered above, the following risks are also reported and managed in the CFS risk management framework:

- group wide risks, to include pensions, reputational and contagion risk;
- business risk; and
- securitisation risk.

Group wide risks

Pensions risk: the risk of the Group being unable to meet pension scheme commitments. Risks are identified at The Co-operative Group level, with the impact of any potential changes to contribution assessed under the Bank risk management framework.

The combined entity is exposed to two distinct areas of pension risk:

- PACE – CFS Management Services Ltd (CFSMS) and the Bank are participating members of The Co-operative Group Pension (Average Career Earnings) – defined benefit scheme; and
- Britannia Pension Scheme – the Bank is a participating member of the Britannia Pension Scheme – defined benefit and contribution sections (defined benefit section closed to new members since 2001).

The Co-operative Group, alongside the scheme trustees, are responsible for the risk management arrangements for PACE, agreeing suitable contribution rates, investment strategies and for taking professional advice as appropriate.

CFSMS, alongside the scheme trustee, are responsible for the risk management arrangements for the Britannia Pension Scheme, agreeing suitable contribution rates, investment strategies and for taking professional advice as appropriate.

The Bank is therefore exposed to potential future increases in required contributions.

Reputational risk: failure to proactively develop, protect and optimise the value of the brands of the CFS group of companies through inappropriate strategic decisions, poor business performance, or operational failure. Reputational risks are identified at the Bank entity level. As part of the assessment of this risk, we consider the impact of other CFS entities and Co-operative Group entities to the Bank.

Contagion risk: risks originating from elsewhere in the Group impacting upon the Bank.

Business risk

Business risk arises from changes to the Bank's business, specifically the risk of not being able to carry out the Bank's business plan and desired strategy.

Securitisation risk

Securitisation is the process by which a group of assets, usually loans, are aggregated into a pool, which is used to back the issuance of new securities. This allows the credit quality of the assets to be separated from the credit rating of the original company and transfers risk to external investors. The Bank has established securitisation structures as part of its funding and capital management activities. These securitisation structures use retail mortgages as the asset pool.

Asset based securitisation is assessed using the ratings based approach, under foundation IRB, where risk weight percentages are applied to each deal depending on the external rating, seniority and granularity of the instrument.

Securitisation risk is the residual credit risk arising from retaining an interest in the Bank's securitisation companies through the provision of subordinated debt and/or start up expense loans where applicable. The Bank has historically entered into securitisation transactions in which it sells mortgages to special purpose entities (SPEs). These SPEs are included as subsidiaries in the consolidated financial statements. The Bank continues to recognise these securitised assets as loans and advances to customers on the balance sheet and income from the securitised assets continues to be recognised as income. Securitisations provide a committed and linked source of funding for higher risk mortgage lending.

The Bank has 14 years' experience of issuing securitisations under various programmes, and has built up a depth of knowledge, processes and management information to deal effectively with these funding vehicles. Securitisation has historically been used as part of a balanced portfolio management approach whilst helping to increase the diversification of funding sources available whilst managing maturity mismatch risk and also assisting overall credit risk management.

The appetite for securitisation risk is cautious, and the Bank has only acted as mortgage originator and servicing agent. The Bank does not provide liquidity facilities, bridging loans or repackaging, nor does it act as underwriter or dealer in the securitisations. All transactions have relevant accounting and legal advice to ensure compliance with applicable regulatory/statutory rules and are also approved at Board level.

The Bank entered into one securitisation transaction in February 2010, Silk Rd 1, which was not subject to significant risk transfer rules under BIPRU 9.
The transaction, rated by Fitch and Moody's re-established the Bank's presence in debt capital markets following the merger with Britannia Building Society in August 2009. Silk Rd 1 generated £2.5bn of Class A1 notes – £375m were publicly placed with third party investors, £1.0bn was pre-placed with a JPMorgan affiliate and £1.125bn was retained by the Bank.

Capital management

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

Capital resources

The Group's policy is to maintain a strong base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Group's policy is to be more prudent than industry norms by having a higher proportion of core tier one as the Group is not able to raise equity externally. However, the Group still recognises the need to maintain a balance between the potential higher returns that might be achieved with greater gearing, and the advantages and security afforded by a sound capital position.

On 15 December 2010, the Bank issued £180.0m of share capital to its immediate parent company the Co-operative Financial Services Limited. The transaction was to ensure that the Bank was in a position of strength in preparation for the implementation of new Basel III minimum equity ratio requirements.

Our submissions to the FSA in the year have shown that the Group and its individually regulated operations have complied with all externally imposed capital requirements throughout the period.

There have been no material changes in the Group's management of capital during the year.

	2010	2009
Core tier one capital		
Permanent share capital	**410.0**	230.0
Retained earnings	**1,562.8**	1,454.2
Minority interest	**31.6**	29.5
Interim profits	**16.1**	15.9
Share premium account	**8.8**	8.8
Total core tier one capital	**2,029.3**	1,738.4
Perpetual non-cumulative preference shares	**60.0**	60.0
Total tier one capital before regulatory deductions	**2,089.3**	1,798.4
Tier two capital		
Revaluation reserves	**2.9**	2.9
Long term subordinated debt	**884.6**	870.5
Total tier two capital before deductions	**887.5**	873.4

The Group's regulatory capital is analysed with two tiers:

Tier one capital

Tier one capital includes share capital, retained earnings, and perpetual non cumulative preference shares. The preference shares carry the right to fixed non cumulative preferential dividend at a rate of 9.25%, payable 31 May and 30 November. Retained earnings exclude gains or losses on cash flow hedges and available for sale assets.

Tier two capital

Revaluation reserves relating to net gains on equity held in the available for sale financial assets category are included in tier two capital.

The tier two capital includes five subordinated debt issues. The rights of payment to the holders of subordinated debt are subordinated to the claims of depositors and other creditors of the Bank. More information on these can be found in note 29.

Upon transfer of engagements, the Britannia permanent interest bearing shares were converted into perpetual subordinated debt of CFS (Perpetual Subordinated Bonds). This debt also ranks as tier two capital.

The capital ratios reported in the business and financial review are based on the Pillar I capital requirement.

Capital allocation

The allocation of capital between specific operations and activities is driven by optimisation of the return achieved on the capital allocated, and is based upon the regulatory capital. Capital allocation is undertaken independently of those responsible for capital management and is reviewed by ALCO.

Critical judgments and estimates

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

The Bank makes critical judgments and estimates that affect the reported assets, liabilities and profits. Estimates are calculated using various assumptions. Critical judgments and the assumptions used in calculating estimates are continually assessed and reviewed, and are based on historical experience and reasonable expectations of future events.

Financial asset and liability classification

The Bank's accounting policies provide scope for assets and liabilities designated at inception into different accounting categories in certain circumstances as outlined on pages 37 to 44 and defined as follows:

- in classifying financial assets and liabilities as 'trading', the Bank has determined that it meets the description of trading assets for those assets and liabilities it acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short term profit or position taking as set out in accounting policy (e) iii);
- in designating financial assets or liabilities at fair value through income or expense, the Bank has determined that it has met one of the criteria for this designation as set out in accounting policy (e) iii); and
- in classifying assets as loans and receivables at amortised cost, the Bank has determined it meets the description as set out in accounting policy (e) i).

Qualifying hedge relationships

In designating a financial instrument as part of a qualifying hedge relationship, the Bank has determined that the hedge is expected to be highly effective over the life of the hedging instrument. In accounting for a derivative as a cash flow hedge, the Bank has determined that the hedged cash flow exposure relates to highly probable future cash flows.

Valuation of financial instruments

Background

Investment securities

The Bank's investment portfolio primarily comprises bank and building society certificates of deposit (CDs), floating rate notes (FRNs), asset backed securities, mortgage backed securities and government issued securities. Additionally, the Bank has a small portfolio of three structured investments vehicles (SIVs) and one credit trading vehicle (CTV) investment.

Loans and advances

Some financial instruments that were originally recognised as investment securities were subsequently reclassified as loans and receivables due to the loss of an active market caused by the 'credit crunch' restricting the availability of traded prices for these assets.

Valuation approach

Investment securities

The accounting treatment for these assets is primarily available for sale which means that they are fair valued in the balance sheet with movements passing through reserves, unless the assets are deemed to be impaired which results in movements being recognised in the income statement.

Loans and advances

As explained in note 16, the assets that have been reclassified as loans and receivables, are held on the balance sheet at amortised cost less any associated impairment.

Except for those assets reclassified to loans and receivables the Bank's CDs, FRNs and government issued securities are valued daily based upon an observable market price feed data, with all non-moving valuations validated against an alternative price source. No significant assumptions are required.

Impairment of financial instruments

Investment securities

Impairment has been assessed by:

- whether there is evidence that a loss event has occurred; and
- whether the loss event has a negative impact on future cash flows.

Each of the Bank's SIVs and its CTV do not meet these criteria in 2010 and therefore no impairment provision has been made. These assessments have particularly given consideration to evidence of any significant financial difficulty of the issuer or measurable decrease in the estimated cash flows from the investments.

During the year there have been no further impairments of investment securities.

Further information on the Bank's accounting policy for impairment is given on page 40.

Critical judgments and estimates continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

Loans and advances
The loan portfolios are reviewed on a continuous basis to assess impairment. In determining whether an impairment provision should be recorded, judgments are made as to whether there is objective evidence that a financial asset or portfolio of financial assets is impaired as a result of loss events that occurred after recognition of the asset and prior to the balance sheet date.

Collective provisions
Personal advances are identified as impaired by taking account of the age of the debt's delinquency, by product type.

The provision is calculated by applying a percentage rate to different categories and ages of impairment debt.

The provision rates reflect the likelihood that the debt in that category/age will be written off or charged off at some point in the future. The rates are based on historical experience and current trends, incorporate the effects of discounting at the customer interest rate and are subject to regular review. The provision is the product of the rate and the spot balance for the relevant arrears bucket.

Individual provisions
Mortgage accounts are identified as impaired by taking account of the age of the debt's delinquency on a case by case basis based on arrears data held within the mortgages system.

Individual provisions are raised on a case by case basis for each mortgage account in arrears.

Each corporate account is assessed and allocated a 'risk grade' to enable the Bank to monitor the overall quality of its lending assets. Those of lesser quality, where the lending is potentially at risk and provisions for future loss may be required, are centrally monitored with specific management actions taken at each stage within laid down procedures and specific provisioning criteria. Provisions represent the likely net loss after realisation of any security.

For further information on credit risk and impairment see 'Risk management' pages 45 to 77.

Effective interest rate
IAS 39 requires interest income to be recognised on an effective interest rate (EIR) basis, inclusive of directly attributable incremental transaction costs and fees, and discounts and premiums where appropriate.

The EIR basis spreads the interest income over the expected life of the instrument. The expected life of an instrument is the period from its inception up to its redemption or maturity date, ie for the mortgage portfolio it would be its redemption date, whilst the non-mortgage portfolio would be its maturity date.

On applying this approach to the mortgage portfolio, judgments are made in relation to estimating the average life of that portfolio. These judgments are made based on specific factors including product terms and historical repayment data. The estimates are updated in each reporting period to reflect actual performance. A key judgment area is the average life of the mortgage portfolio. A change in the average life by one year would have an impact of 0.2% to gross interest income.

For non-mortgage portfolios, see 'Fair values' below.

Corporation taxes
The Bank is subject to corporation taxes in three jurisdictions. Significant estimates are required in determining the provision for corporation taxes. There are certain significant transactions and calculations for which the ultimate tax determination is uncertain at the balance sheet date. In the opinion of the directors, the judgments made are appropriate and the level of provision is adequate to cover the likely liability.

Financial Services Compensation Scheme levy

The Financial Services Compensation Scheme (FSCS) provides compensation to customers of financial institutions in the event that an institution is unlikely, or is likely to be unable, to pay claims against it. As a result of a number of institutions' failures during 2008, the FSCS has borrowed £19.7bn on an interest only basis until March 2012 from HM Treasury in order to meet its obligations to the depositors. These borrowings are anticipated to be repaid wholly or substantially from the realisation of the assets of the failed institutions. The FSCS raises annual levies from the banking industry in order to meet its management expenses and compensation costs. The annual levies are based upon the individual institutions proportion of protected deposits of the total market protected deposits at 31 December of each year. The Group has provided £20.9m for its share of levies that will be raised by the FSCS including the interest on the loan from HM Treasury in respect of the levy years to 31 March 2012. The provision includes estimates for the interest that the FSCS will pay on the loan and of the Group's market participation in the relevant periods.

At the date of these financial statements, it is not possible to estimate whether there will be ultimately additional levies on the industry, the level of the Group's market participation or other factors that may affect amounts or the timing of amounts that may ultimately become payable, nor the effect that such levies may have upon operating results in any particular periods.

Provisions

Provisions are carried in respect of certain known or forecast future expenditure, as described in note 32.

Transfer of engagements of Britannia Building Society

The transfer of engagements of Britannia Building Society did not involve any cash consideration, other than the maintenance of Britannia Membership Reward (BMR) payments and the payment of joining fees for Britannia members to become members of Co-operative Financial Services.

Goodwill

This is based on a discounted cash flow of further BMR payments which would have been paid to Britannia members in perpetuity. The judgments and estimates in this calculation are set out in note 19. The principal judgments and estimates are forecasted profit, the discount rate and the proportion of profit after tax that would have been paid out in the form of BMR.

In the event that consideration was 5% higher or lower, goodwill on acquisition would be higher or lower by £58m.

Fair values

The fair value adjustment to loans and advances to customers comprises:

- an interest rate adjustment on a discounted cash flow basis to reflect the value inherent in fixed rate, base and tracker products compared to current market pricing;
- the inclusion of a credit risk adjustment to reflect future lifetime expected credit losses; and
- the write off of existing EIR balances and fair value adjustment for hedged risk.

The initial fair value adjustments fully unwind over their associated financial instruments' future expected lives or such shorter period as deemed reasonable. This judgment of future expected lives is therefore a critical judgment and estimate.

It has been assumed that debt securities will be redeemed in full at five years after their interest step up date. This has the impact of decreasing profit by £6m in 2010.

During 2010, as part of the Bank's regular review of its critical judgments and estimates, the rate of mortgage redemptions was considered in the light of current experience. As a result, the Optimum mortgages expected lives were extended up to 2023 and the expected lives of the debt securities, that only redeem as and when the underlying mortgages repay, were also extended.

The impact of increasing the mortgage redemptions by 10% per annum on the mortgage interest fair value adjustment is not material; however on the debt securities in issue fair value adjustment the impact is to decrease profits by a total of £17m in the years up to 2013 and to increase profits by the same amount in the following years up to 2017.

Another critical judgment and estimate is the release of the credit risk fair value adjustment. On the transfer of engagements with Britannia Building Society, £5.3bn of loans and advances to customers were acquired at a deep discount due to incurred credit losses. For these loans, the effective interest rate does not include estimated future credit losses. This credit risk fair value adjustment is utilised instead on the actual redemptions of the associated mortgages.

Notes to the financial statements

For the year ended 31 December 2010

All amounts are stated in £m unless otherwise indicated

1. Segmental information

At the highest level, the Group's internal reporting structure is split between Retail, Corporate and Markets (CAM) and Other, based on differences in products and services. CAM has been split further into Corporate, Treasury, Optimum and Platform, and Other. This level of information is regularly presented to the Board. Revenues are attributed to the segment in which they are generated. Transactions between the reportable segments are on normal commercial terms. Internal charges and transfer pricing adjustments have been reflected in each segment.

The Group is comprised of the following main reportable segments:

- **Retail** – customer focused products and services for individuals, sole traders and small partnerships. This includes mortgages, credit cards, consumer loans, current accounts and savings products;
- **Corporate** – customer focused products and services for businesses. This includes large corporate and commercial entities and small to medium entities. It includes loans, asset finance, current accounts and savings products;
- **Treasury** – this is the asset and liability management across the Bank's balance sheet, including trading activities;
- **Optimum and Platform** – this is the specialist mortgage team dealing with intermediary lending;
- **Other CAM** – the business services part of the CAM segment; and
- **Other** – includes Unity Trust, a subsidiary bank operating in the corporate banking and social economy sectors on behalf of trade unions.

	Retail	Corporate	Treasury	Optimum and Platform	Other CAM	Sub total CAM	Other	Total
2010								
Interest margin	**351.8**	**121.9**	**22.3**	**125.7**	**1.4**	**271.3**	**9.2**	**632.3**
Non-interest income	**149.7**	**37.2**	**(25.4)**	**9.4**	**17.0**	**38.2**	**1.6**	**189.5**
Segment operating income	**501.5**	**159.1**	**(3.1)**	**135.1**	**18.4**	**309.5**	**10.8**	**821.8**
Operating expenses	**(440.9)**	**(58.8)**	**(21.2)**	**(42.5)**	**(11.8)**	**(134.3)**	**(6.3)**	**(581.5)**
Impairment losses on loans and advances	**(63.8)**	**(30.4)**	**–**	**1.4**	**–**	**(29.0)**	**(4.5)**	**(97.3)**
Impairment gains on investments	**–**	**–**	**1.5**	**–**	**–**	**1.5**	**–**	**1.5**
Segment operating profit	**(3.2)**	**69.9**	**(22.8)**	**94.0**	**6.6**	**147.7**	**–**	**144.5**
Fair value amortisation								**(14.2)**
Financial Services Compensation Scheme levies								**(11.5)**
Share of post tax profits from joint ventures								**0.7**
Profit based payments to members of The Co-operative Group								**(10.8)**
Significant items								**(59.8)**
Profit before taxation								**48.9**
Income tax								**(13.1)**
Profit for the financial year								**35.8**

The Board relies primarily on net interest revenue to assess the performance of each segment. As a result interest margin is reported on a net basis to the Board.

	Retail	Corporate	Treasury	Optimum and Platform	Other CAM	Sub total CAM	Other	Total
Other segment information 2010								
Segment assets	**17,316.0**	**8,172.0**	**8,312.0**	**9,284.7**	**4.7**	**25,773.4**	**–**	**43,089.4**
Unallocated assets								**1,680.7**
Total assets	**17,316.0**	**8,172.0**	**8,312.0**	**9,284.7**	**4.7**	**25,773.4**	**–**	**44,770.1**
Segment liabilities	**28,591.7**	**4,449.3**	**8,647.1**	**–**	**38.1**	**13,134.5**	**–**	**41,726.2**
Unallocated liabilities								**1,013.4**
Total liabilities	**28,591.7**	**4,449.3**	**8,647.1**	**–**	**38.1**	**13,134.5**	**–**	**42,739.6**
Amount of investment in associate/ joint ventures	**2.5**	**–**	**–**	**–**	**–**	**–**	**–**	**2.5**
Depreciation	**21.4**	**1.3**	**0.1**	**0.8**	**–**	**2.2**	**0.3**	**23.9**
Amortisation	**11.0**	**0.5**	**–**	**–**	**–**	**0.5**	**0.1**	**11.6**

The Group's activities are in the UK.

1. Segmental information continued

Reconciliation to statutory income statement	2010
Interest margin	
Total interest margin for reportable segments	632.3
Reclassification of gains less losses on derivatives	(1.6)
Interest fair value unwind	(22.3)
Net interest income	608.4
Non-interest income	
Total non-interest income for reportable segments	189.5
Reclassification of gains less losses on derivatives	1.6
Interest fair value unwind	(1.5)
Non-interest income	189.6
Operating expenses	
Total operating expenses for reportable segments	(581.5)
Operating expenses fair value unwind	9.6
Operating expenses	(571.9)
Fair value amortisation	
Total interest fair value unwind for reportable segments	(14.2)
Interest margin unwind	22.3
Non-interest income unwind	1.5
Operating expenses unwind	(9.6)
	–

Reconciliation of other segment information	
Assets	
Total assets for reportable segments	44,770.1
Statutory reclassifications	811.2
Consolidated total assets	45,581.3
Liabilities	
Total liabilities for reportable segments	42,739.6
Statutory reclassifications	768.6
Consolidated total liabilities	43,508.2

Notes to the financial statements continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

1. Segmental information continued

	Retail	Corporate	Treasury	Optimum and Platform	Other CAM	Sub total CAM	Other	Total
2009								
Interest margin	262.2	108.8	33.5	56.8	0.3	199.4	12.4	474.0
Non-interest income	134.5	37.4	(8.6)	6.0	8.1	42.9	1.5	178.9
Segment operating income	396.7	146.2	24.9	62.8	8.4	242.3	13.9	652.9
Operating expenses	(327.8)	(58.5)	(11.4)	(16.1)	(4.3)	(90.3)	(7.5)	(425.6)
Impairment losses on loans and advances	(82.7)	(32.3)	–	–	–	(32.3)	(1.1)	(116.1)
Impairment gains on investments	–	–	4.0	–	–	4.0	–	4.0
Segment operating profit	(13.8)	55.4	17.5	46.7	4.1	123.7	5.3	115.2
Fair value amortisation								99.1
Financial Services Compensation Scheme levies								(3.7)
Share of post tax profits from joint ventures								(0.1)
Profit based payments to members of The Co-operative Group								(7.8)
Significant items								(38.1)
Profit before taxation								164.6
Income tax								(51.4)
Profit for the financial year								113.2
Other segment information 2009								
Segment assets	16,722.6	7,900.5	9,531.1	9,276.4	–	26,708.0	–	43,430.6
Unallocated assets								1,703.0
Total assets	16,722.6	7,900.5	9,531.1	9,276.4	–	26,708.0	–	45,133.6
Segment liabilities	28,324.0	3,148.0	10,863.8	–	–	14,011.8	–	42,335.8
Unallocated liabilities								860.3
Total liabilities	28,324.0	3,148.0	10,863.8	–	–	14,011.8	–	43,196.1
Amount of investment in associate/ joint ventures	1.8	–	–	–	–	–	–	1.8
Depreciation	17.7	1.6	0.5	0.5	–	2.6	0.3	20.6
Amortisation	6.5	0.6	–	0.1	–	0.7	0.1	7.3

1. Segmental information continued

Reconciliation to statutory income statement	2009
Interest margin	
Total interest margin for reportable segments	474.0
Reclassification of gains less losses on derivatives	(3.6)
Interest fair value unwind	109.3
Net interest income	579.7
Non-interest income	
Total non-interest income for reportable segments	178.9
Reclassification of gains less losses on derivatives	3.6
Non-interest fair value unwind	(6.8)
Non-interest income	175.7
Operating expenses	
Total operating expenses for reportable segments	(425.6)
Operating expenses fair value unwind	(3.4)
Operating expenses	(429.0)
Fair value amortisation	
Total interest fair value unwind for reportable segments	99.1
Interest margin unwind	(109.3)
Non-interest income unwind	6.8
Operating expenses unwind	3.4
Fair value amortisation	–

Reconciliation of other segment information	
Assets	
Total assets for reportable segments	45,133.6
Statutory reclassifications	1,005.2
Consolidated total assets	46,138.8
Liabilities	
Total liabilities for reportable segments	43,196.1
Statutory reclassifications	1,066.6
Consolidated total liabilities	44,262.7

Notes to the financial statements continued
For the year ended 31 December 2010
All amounts are stated in £m unless otherwise indicated

2. Profit before taxation

	2010 £'000	2009 £'000
Profit before taxation is stated after:		
Audit of these financial statements	**457**	604
Amounts receivable by auditors and their associates in respect of:		
Audit of financial statements of subsidiaries pursuant to legislation	**392**	389
Other services pursuant to such legislation	**87**	16
Other services relating to taxation	**7**	21
Services relating to litigation	**2**	2
Services relating to information technology	**92**	56
Services relating to corporate finance transactions	**15**	77
All other services	**822**	377
	1,874	1,542

Amounts paid to the Bank's auditor in respect of services to the Bank, other than the audit of the Bank's financial statements, have not been disclosed as the information is required instead to be disclosed on a consolidated basis. Amounts capitalised are not disclosed above.

3. Directors' emoluments

	2010 £'000	2009 £'000
Executive directors	**4,002**	1,945
Compensation for loss of office	**–**	805
	4,002	2,750

Retirement benefits are accruing to five directors (2009: five) under defined benefit schemes.

All non-executive directors are appointed and their directors' fees are determined and paid by The Co-operative Group and therefore no amounts are shown above (2009: £nil). Further details of directors' emoluments are included in the remuneration report on pages 23 to 28. The remuneration report is unaudited.

4. Net interest income

	2010	2009
Interest receivable and similar income		
On financial assets not at fair value through income or expense:		
On loans and advances to customers	**1,605.0**	1,047.1
On loans and advances to banks	**9.3**	17.8
On investment securities	**277.5**	163.8
	1,891.8	1,228.7
On financial assets at fair value through income or expense:		
Net expense on financial instruments hedging assets	**(168.9)**	(167.5)
Net interest (expense)/income on financial instruments not in a hedging relationship	**(9.6)**	0.4
	1,713.3	1,061.6

Interest income accrued on impaired financial assets during the year was £90.5m (2009: £62.7m). Interest due to unwinding of discount on impairment provisions relating to impaired financial assets amounted to £2.2m (2009: £3.8m).

	2010	2009
Interest expense and similar charges		
On financial liabilities not at fair value through income or expense:		
On customer accounts	**471.9**	262.4
On bank and other deposits	**515.5**	197.2
On subordinated liabilities	**43.9**	31.1
On perpetual secured debt	**17.2**	11.7
	1,048.5	502.4
On financial liabilities at fair value through income or expense:		
Net income/(expense) on financial instruments hedging liabilities	**56.4**	(20.5)
	1,104.9	481.9

5. Net fee and commission income

	Before significant items 2010	Significant items 2010	After significant items 2010	Before and after significant items 2009
Fee and commission income				
On items not at fair value through income or expense	**235.9**	**(13.1)**	**222.8**	209.3
On trust or fiduciary activities that result from holding or investing in assets on behalf of others	**1.3**	**–**	**1.3**	1.5
	237.2	**(13.1)**	**224.1**	210.8
Fee and commission expense				
On items not at fair value through income or expense	**52.2**	**–**	**52.2**	47.1
On items at fair value through income or expense	**8.1**	**–**	**8.1**	0.1
	60.3	**–**	**60.3**	47.2

The significant items in 2010 relate to provisions made for customer redress as detailed in note 32.

6. Net trading income

	2010	2009
Foreign exchange	**6.5**	5.5
Other interest rate instruments	**(1.9)**	(0.3)
	4.6	5.2

Foreign exchange net trading income includes gains less losses from spot forward and forward contracts, options, futures and translated foreign currency assets and liabilities.

Other interest rate instruments include the result of transacting in government securities, money market instruments, interest rate and currency swaps, options and other derivatives.

7. Other operating income

	2010	2009
Rent receivable from investment properties (note 21)	**6.5**	2.1
Other rent receivable	**1.7**	0.8
Proceeds from equity shares	**–**	0.5
Change in fair value of investment properties (note 21)	**(0.1)**	3.5
	8.1	6.9

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8. Operating expenses

	Before significant items 2010	**Significant items 2010**	**After significant items 2010**	Before significant items 2009	Significant items 2009	After significant items 2009
Staff costs (note 9)	**292.6**	**29.6**	**322.2**	200.5	26.4	226.9
Administrative expenses	**224.9**	**17.1**	**242.0**	173.7	11.7	185.4
Depreciation of property, plant and equipment (note 22)	**24.8**	**–**	**24.8**	21.0	–	21.0
Amortisation of intangible fixed assets (note 20)	**4.1**	**–**	**4.1**	5.1	–	5.1
Loss on sale of property, plant and equipment	**0.8**	**–**	**0.8**	1.4	–	1.4
Operating lease rentals	**27.7**	**–**	**27.7**	22.0	–	22.0
Property provisions for liabilities and charges provided in the year (note 32)	**3.4**	**–**	**3.4**	0.9	–	0.9
Property provisions for liabilities and charges released during the year (note 32)	**(0.3)**	**–**	**(0.3)**	(2.2)	–	(2.2)
Regulatory provisions for liabilities and charges provided in the year (note 32)	**3.5**	**–**	**3.5**	5.5	–	5.5
Regulatory provisions for liabilities and charges released during the year (note 32)	**(12.3)**	**–**	**(12.3)**	(0.1)	–	(0.1)
Direct expenses from investment properties that generated rental income in the year	**2.6**	**–**	**2.6**	1.1	–	1.1
Direct expenses from investment properties that did not generate rental income in the year	**0.1**	**–**	**0.1**	0.1	–	0.1
	571.9	**46.7**	**618.6**	429.0	38.1	467.1

The significant items in 2010 and 2009 relate to a programme of investment and integration.

9. Staff costs

	Before significant items 2010	**Significant items 2010**	**After significant items 2010**	Before significant items 2009	Significant items 2009	After significant items 2009
Wages and salaries	**221.1**	**16.5**	**237.6**	151.0	9.4	160.4
Social security costs	**20.6**	**0.3**	**20.9**	13.0	0.7	13.7
Bank payroll tax	**(0.1)**	**–**	**(0.1)**	0.3	–	0.3
Pension costs						
Defined benefit plans (note 34)	**0.2**	**–**	**0.2**	0.2	–	0.2
Defined contribution plans (note 34)	**28.2**	**0.5**	**28.7**	17.9	0.7	18.6
Other staff costs	**22.6**	**12.3**	**34.9**	18.1	15.6	33.7
	292.6	**29.6**	**322.2**	200.5	26.4	226.9

The Bank staff costs included above are £265.2m before significant items and £294.8m after significant items (2009: £186.7m before significant items, £213.1m after significant items).

In 2009, £0.3m was accrued for the estimated tax payable in respect of the bank payroll tax announced in the Finance Bill 2010. During the year, tax of £0.2m was paid and £0.1m was released to the income statement.

Average number of employees

The average number of persons working for the Group and the Bank during the year was made up as follows:

	Group		**Bank**	
	No. of employees 2010	No. of employees 2009	**No. of employees 2010**	No. of employees 2009
Full time	**6,499**	4,479	**5,843**	4,146
Part time	**2,247**	1,514	**2,117**	1,453
	8,746	5,993	**7,960**	5,599

Employee activities are undertaken across the Co-operative Financial Services Group and the figures above reflect the Bank's share of these services. Employee numbers include 4,724 staff who transferred on the transfer of engagements of Britannia Building Society on 1 August 2009.

10. Income tax

	Before significant items 2010	**Significant items 2010**	**After significant items 2010**	Before significant items 2009	Significant items 2009	After significant items 2009
Current tax – current year	**28.6**	**(16.7)**	**11.9**	42.2	(10.7)	31.5
Current tax – prior year	**0.8**	**–**	**0.8**	(0.7)	–	(0.7)
Deferred tax – current year (note 33)	**2.5**	**–**	**2.5**	20.9	–	20.9
Deferred tax – prior year (note 33)	**(2.1)**	**–**	**(2.1)**	(0.3)	–	(0.3)
	29.8	**(16.7)**	**13.1**	62.1	(10.7)	51.4

Further information about deferred income tax is presented in note 33. The tax on the Group's profit before taxation differs from the theoretical amount that would arise using the corporation tax rate in the UK as follows:

	2010	2009
Profit before tax	**48.9**	164.6
Tax calculated at a rate of 28% (2009: 28%)	**13.7**	46.1
Effects of:		
Preference share interest not deductible for tax purposes	**1.6**	1.6
Expenses not deductible for tax purposes	**(2.3)**	2.4
Depreciation of expenditure not qualifying for capital allowances	**2.2**	0.4
(Profits)/losses taxed at lower rates	**(3.7)**	2.0
Non-taxable income	**(1.2)**	(0.1)
Adjustments to tax charge in respect of prior periods	**(1.3)**	(1.0)
Change in rate of deferred tax (note 33)	**4.3**	–
Other differences	**(0.2)**	–
	13.1	51.4

11. Group profit attributable to equity shareholders dealt with in the accounts of The Co-operative Bank plc

	Before significant items 2010	**Significant items 2010**	**After significant items 2010**	Before significant items 2009	Significant items 2009	After significant items 2009
Net profit attributable to equity shareholders of the Bank	**108.1**	**(35.0)**	**73.1**	194.0	(27.4)	166.6

As permitted by Section 408 of the Companies Act 2006, the income statement of The Co-operative Bank plc has not been presented separately.

12. Earnings per share

Basic earnings per share is calculated by dividing the net profit attributable to equity shareholders of the Bank by the weighted average number of ordinary shares in issue during the year.

	Before significant items 2010	**Significant items 2010**	**After significant items 2010**	Before significant items 2009	Significant items 2009	After significant items 2009
Profit attributable to equity shareholders of the Bank	**79.5**	**(43.1)**	**36.4**	137.7	(27.4)	110.3
Ordinary shares in issue (millions)						
At beginning of year	**4,600**	**4,600**	**4,600**	1,100	1,100	1,100
Issued in the year (note 38)	**3,600**	**3,600**	**3,600**	3,500	3,500	3,500
At end of year	**8,200**	**8,200**	**8,200**	4,600	4,600	4,600
Weighted average number of ordinary shares in issue (millions)	**4,767.7**	**4,767.7**	**4,767.7**	3,827.7	3,827.7	3,827.7
Basic earnings per share (expressed in pence per share)	**1.67**	**(0.90)**	**0.77**	3.60	(0.72)	2.88

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13. Cash and balances at central banks

	Group		Bank	
	2010	2009	**2010**	2009
Cash in hand	**255.8**	259.6	**255.8**	259.6
Balances with the Bank of England other than mandatory reserve deposits	**1,443.7**	1,413.2	**1,443.7**	1,413.2
Included in cash and cash equivalents	**1,699.5**	1,672.8	**1,699.5**	1,672.8
Mandatory reserve deposits with the Bank of England (note 35)	**36.1**	34.0	**36.1**	34.0
	1,735.6	1,706.8	**1,735.6**	1,706.8

Mandatory reserve deposits are not available for use in the Group and Bank's day to day operations, are non-interest bearing and are not included in cash and cash equivalents.

14. Loans and advances to banks

	Group		Bank	
	2010	2009	**2010**	2009
Items in course of collection from other banks	**139.9**	149.0	**139.7**	148.8
Placements with other banks	**1,338.8**	313.5	**1,326.8**	290.0
Included in cash and cash equivalents	**1,478.7**	462.5	**1,466.5**	438.8
Other loans and advances to banks	**915.4**	1,319.0	**262.1**	781.3
	2,394.1	1,781.5	**1,728.6**	1,220.1

15. Loans and advances to customers

	Group		Bank	
	2010	2009 restated	**2010**	2009
Gross loans and advances	**35,199.9**	34,267.7	**24,055.4**	23,242.8
Less: allowance for losses on loans and advances to customers	**(222.6)**	(194.0)	**(210.5)**	(192.0)
	34,977.3	34,073.7	**23,844.9**	23,050.8

Group and Bank loans and advances to customers include £74.1m (2009: £48.2m) of financial assets at fair value through income or expense designated at initial recognition to eliminate or significantly reduce a measurement or recognition inconsistency. Of these, £20.0m (2009: £21.0m) are secured by real estate collateral.

Loans and advances to customers includes £11,215.9m (2009: £9,492.7m) securitised under the Group's securitisation and covered bond programmes. The Group remains exposed to substantially all of the risks and rewards of ownership of these assets. Included within Group deposits by banks (note 25) are £67.2m (2009: £466.7m) of loans from external third parties and within Group debt securities in issue (note 28) are £1,898.1m (2009: £2,683.7m) of floating rate notes, all secured on these mortgage assets. Included within the Bank amounts owed by other Co-operative Group undertakings are £3,995.8m (2009: £2,969.0m) of floating rate notes issued to the Bank and £2,400.9m (2009: £2,400.4m) of other loans, secured on these mortgage assets.

Concentration of exposure
The Group's exposure is virtually all within the UK. The following industry concentrations of gross advances before provisions are considered significant:

	Group		Bank	
	2010	2009 restated	**2010**	2009
Property and construction	**4,544.6**	4,498.1	**2,606.9**	2,481.6
Retail distribution and services	**500.1**	446.9	**357.0**	313.9
Business and other services	**3,808.1**	3,658.2	**3,683.5**	3,525.0
Personal – unsecured	**1,613.1**	1,625.6	**1,613.1**	1,625.6
Personal – secured	**24,734.0**	24,038.9	**15,794.9**	15,296.7
	35,199.9	34,267.7	**24,055.4**	23,242.8

15. Loans and advances to customers continued

Allowance for losses on loans and advances

2010	Individual mortgage	Individual corporate	Collective	Total
Group				
At the beginning of the year	**2.3**	**51.3**	**140.4**	**194.0**
Charge against profits	**7.2**	**35.5**	**63.9**	**106.6**
Amounts written off	**(0.9)**	**(30.5)**	**(44.9)**	**(76.3)**
Unwind of discount allowance	**–**	**(1.0)**	**(1.2)**	**(2.2)**
Interest charged on impaired loans	**–**	**0.5**	**–**	**0.5**
At the end of the year	**8.6**	**55.8**	**158.2**	**222.6**
Bank				
At the beginning of the year	**2.3**	**49.3**	**140.4**	**192.0**
Charge against profits	**0.9**	**31.0**	**63.9**	**95.8**
Amounts written off	**(0.3)**	**(30.4)**	**(44.9)**	**(75.6)**
Unwind of discount allowance	**–**	**(1.0)**	**(1.2)**	**(2.2)**
Interest charged on impaired loans	**–**	**0.5**	**–**	**0.5**
At the end of the year	**2.9**	**49.4**	**158.2**	**210.5**

Allowance for losses on loans and advances

2009	Individual mortgage	Individual corporate	Collective	Total
Group				
At the beginning of the year	1.5	45.6	140.8	187.9
Charge against profits	1.5	33.3	81.2	116.0
Amounts written off	(0.7)	(26.5)	(79.2)	(106.4)
Unwind of discount allowance	–	(1.4)	(2.4)	(3.8)
Interest charged on impaired loans	–	0.3	–	0.3
At the end of the year	2.3	51.3	140.4	194.0
Bank				
At the beginning of the year	1.5	44.7	140.8	187.0
Charge against profits	1.5	32.2	81.2	114.9
Amounts written off	(0.7)	(26.5)	(79.2)	(106.4)
Unwind of discount allowance	–	(1.4)	(2.4)	(3.8)
Interest charged on impaired loans	–	0.3	–	0.3
At the end of the year	2.3	49.3	140.4	192.0

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15. Loans and advances to customers continued
The net impairment charge in the Group income statement is £97.3m (2009: £116.1m). This includes amounts recovered by the Group of £9.3m (2009: charge of £0.1m) against amounts previously written off. The recoveries have been made from the mortgagors and from other parties involved in the origination or acquisition of the mortgages.

Loans and advances to customers include finance lease receivables.

	Group		Bank	
	2010	2009	**2010**	2009
Gross investment in finance leases may be analysed as follows:				
No later than one year	**28.4**	32.8	**22.4**	28.9
Later than one year and no later than five years	**66.2**	75.9	**44.8**	53.9
Later than five years	**78.7**	73.3	**56.5**	45.6
	173.3	182.0	**123.7**	128.4
Unearned future finance income on finance leases	**(44.2)**	(40.6)	**(29.1)**	(22.6)
Net investment in finance leases	**129.1**	141.4	**94.6**	105.8
The net investment in finance leases may be analysed as follows:				
No later than one year	**21.2**	25.4	**18.0**	24.4
Later than one year and no later than five years	**44.9**	54.5	**32.0**	42.0
Later than five years	**63.0**	61.5	**44.6**	39.4
	129.1	141.4	**94.6**	105.8

There are no unguaranteed residual values for any of the finance leases.

The Group enters into finance lease and hire purchase arrangements with customers in a wide range of sectors including transport, retail and utilities. The accumulated allowance for uncollectible minimum lease payments receivable is £0.8m (2009: £1.7m).

Fair value adjustments for hedged risk
The Group has entered into interest rate swaps that protect it from changes in interest rates on the floating rate liabilities that fund its portfolio of fixed rate mortgages. Changes in the fair values of these swaps are offset by changes in the fair values of the fixed rate mortgages. The changes in fair value of fixed rate mortgages are disclosed on the balance sheet as fair value adjustments for hedged risk immediately below the loans and advances to customers.

Fair value adjustments to loans and advances to customers attributable to portfolio hedged risk in the Group are £166.8m (2009: £66.1m) and in the Bank are £164.6m (2009: £60.6m).

16. Investment securities
Loans and receivables

	Group		Bank	
	2010	2009	**2010**	2009
Loans and receivables				
Listed	**164.6**	124.3	**164.6**	124.3
Unlisted	**1,765.7**	2,376.4	**1,835.2**	2,445.8
	1,930.3	2,500.7	**1,999.8**	2,570.1
Less: allowance for losses	**(13.0)**	(14.5)	**(13.0)**	(14.5)
	1,917.3	2,486.2	**1,986.8**	2,555.6
Included in cash and cash equivalents	**–**	–	**–**	–
The movement in investment securities – loans and receivables excluding interest amounts may be summarised as follows:				
At the beginning of the year	**2,483.5**	123.4	**2,552.8**	123.4
Arising on transfer of engagements	**–**	2,440.4	**–**	2,506.1
Disposals and maturities	**(735.8)**	(201.3)	**(748.9)**	(201.3)
Exchange adjustments	**0.4**	0.1	**0.4**	0.1
Fair value movements through equity	**(1.5)**	86.1	**(1.5)**	86.1
Fair value movements through income and expense	**–**	–	**11.7**	–
Amortisation	**166.6**	26.8	**168.2**	30.4
Impairment losses	**1.5**	8.0	**1.5**	8.0
At the end of the year	**1,914.7**	2,483.5	**1,984.2**	2,552.8

16. Investment securities continued

Impairment analysis of loans and receivables

	Group		Bank	
	2010	2009	**2010**	2009
At the beginning of the year	**14.5**	22.5	**14.5**	22.5
Release for the year	**(1.5)**	(8.0)	**(1.5)**	(8.0)
At the end of the year	**13.0**	14.5	**13.0**	14.5

Available for sale

	Group		Bank	
	2010	2009	**2010**	2009
Available for sale				
Listed	**2,417.7**	1,470.4	**2,417.7**	1,470.4
Unlisted	**640.4**	3,058.8	**304.7**	2,662.1
	3,058.1	4,529.2	**2,722.4**	4,132.5
Less: allowance for losses	**(72.3)**	(71.9)	**(72.3)**	(71.9)
	2,985.8	4,457.3	**2,650.1**	4,060.6
Included in cash and cash equivalents	**225.0**	252.0	**225.0**	252.0

Included within the listed available for sale investments for both Group and Bank is £28.7m of financial assets at fair value through income or expense designated at initial recognition to eliminate or significantly reduce a measurement or recognition inconsistency.

The movement in investment securities – available for sale excluding interest amounts may be summarised as follows:

	Group		Bank	
	2010	2009	**2010**	2009
At the beginning of the year	**4,444.1**	2,108.3	**4,049.0**	1,686.8
Arising on transfer of engagements	**–**	3,680.8	**–**	3,680.8
Acquisitions	**9,895.2**	15,820.7	**8,515.2**	14,630.8
Disposals and maturities	**(11,437.4)**	(17,293.6)	**(9,997.4)**	(16,078.6)
Exchange adjustments	**20.2**	92.4	**20.2**	92.4
Fair value movements through equity	**(19.8)**	64.6	**(19.8)**	65.9
Fair value movements through income and expense	**43.9**	(1.9)	**43.9**	(1.9)
Amortisation	**28.4**	(23.2)	**28.4**	(23.2)
Impairment losses	**–**	(4.0)	**–**	(4.0)
At the end of the year	**2,974.6**	4,444.1	**2,639.5**	4,049.0

Impairment analysis of investment securities – available for sale

	Group		Bank	
	2010	2009	**2010**	2009
At the beginning of the year	**71.9**	69.8	**71.9**	69.8
Impairment losses recycled through equity reserves	**–**	4.0	**–**	4.0
Charge for the year	**–**	4.0	**–**	4.0
Exchange adjustments	**0.4**	(1.9)	**0.4**	(1.9)
At the end of the year	**72.3**	71.9	**72.3**	71.9

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16. Investment securities continued
Reclassification of available for sale assets

Pursuant to the amendments to IAS 39 and IFRS 7, during 2008 the Bank reclassified specific available for sale investment securities to loans and receivables at amortised cost. The Bank identified particular assets that would have met the definition of loans and receivables (if they had not been designated as available for sale) for which at 27 July 2008 it considered it had the intention and ability to hold them for the foreseeable future or until maturity, due to the market in such instruments being considered to be inactive.

As per the amendment to IAS 39, the reclassifications were made with effect from 27 July 2008 at fair value at that date. The table below sets out the carrying values and fair values for both the Group and Bank at the balance sheet date:

		2010		2009	
	Amounts reclassified in 2008	**Carrying value**	**Fair value**	Carrying value	Fair value
Available for sale financial assets transferred to loans and receivables	127.0	**131.2**	**134.1**	134.8	138.0

The amounts reclassified in 2008 are stated net of disposals of £4.9m in the period.

At the date of transfer fair value equated to carrying value. As at 31 December 2010 and 2009 fair value is based on quoted market prices, being the only indicator of fair value that is available.

The table below sets out the amounts actually recognised during the year in respect of the financial assets reclassified out of available for sale securities for both the Group and Bank:

	Income or expense 2010	**Other comprehensive income 2010**	Income or expense 2009	Other comprehensive income 2009
Period after reclassification				
Available for sale investments reclassified to loans and receivables:				
Interest income	**0.2**	**–**	3.1	–
Net impairment release/(charge)	**1.5**	**(1.5)**	8.0	(1.4)
Net change in fair value	**–**	**5.2**	–	4.7
	1.7	**3.7**	11.1	3.3

The table below sets out the amounts that would have been recognised for both the Group and Bank in 2010 and in 2009, if the reclassification in 2008 had not been made:

	Income or expense 2010	**Other comprehensive income 2010**	Income or expense 2009	Other comprehensive income 2009
Available for sale investments reclassified to loans and receivables:				
Interest income	**0.2**	**–**	3.1	–
Net impairment release/(charge)	**1.5**	**–**	8.0	(4.0)
Net change in fair value	**–**	**4.9**	–	25.6
	1.7	**4.9**	11.1	21.6

16. Investment securities continued

At 27 July 2008, the effective interest rates on available for sale assets reclassified to loans and receivables at amortised cost ranged from 8% to 12% with expected recoverable cash flows as at 31 December 2010 of £135.8m (2009: £144.2m).

Gains and losses from investment securities, included within interest income, comprise:

	2010	2009
Derecognition of available for sale assets	**(5.1)**	7.1

Analysis of investment securities by issuer

	Group		**Bank**	
	2010	2009	**2010**	2009
Investment securities issued by public bodies:				
Government securities	**903.0**	942.7	**903.0**	942.7
Other public sector securities	**57.3**	9.1	**57.3**	9.1
	960.3	951.8	**960.3**	951.8
Investment securities issued by other issuers:				
Bank and building society certificates of deposits	**560.8**	849.2	**225.1**	452.5
Other debt securities:				
Credit trading funds	**16.5**	16.5	**16.5**	16.5
Structured investment vehicles	**–**	–	**–**	–
Other floating rate notes	**1,624.9**	2,774.6	**1,624.9**	2,774.6
Mortgage backed securities	**1,740.6**	2,351.4	**1,810.1**	2,420.8
	3,382.0	5,142.5	**3,451.5**	5,211.9
	4,903.1	6,943.5	**4,636.9**	6,616.2

Other floating rate notes (FRNs) relate to sterling, euro, US dollar, Canadian dollar and Australian dollar denominated FRNs with maturities ranging from one month to three years from the balance sheet date.

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17. Derivative financial instruments
The Bank has entered, as principal, into various derivatives either as a trading activity, which includes proprietary transactions and customer facilitation, or as a hedging activity for the management of interest rate risk, equity risk and foreign exchange rate risk. Positive and negative fair values have not been netted as the Group does not have a legal right of offset.

Derivatives held for trading purposes
The trading transactions are wholly interest rate related contracts including swaps, caps and floors, forward rate agreements and exchange traded futures. Trading transactions include derivatives where the Bank enters into a transaction to accommodate a customer together with the corresponding hedge transaction.

Non-trading derivatives
Non-trading transactions comprise derivatives held for hedging purposes to manage the asset and liability positions of the Group. Derivatives used to manage interest rate related positions include swaps, caps and floors, forward rate agreements and exchange traded futures. The foreign exchange rate positions are managed using forward currency transactions and swaps. Equity risk is managed using equity swaps.

	Group			Bank		
	Contractual/ notional amount	Fair value Assets	Fair value Liabilities	Contractual/ notional amount	Fair value Assets	Fair value Liabilities
2010						
Derivatives held for trading purposes						
Interest rate derivatives:						
Interest rate swaps	**3,035.9**	**65.1**	**(51.0)**	**3,215.9**	**68.5**	**(54.4)**
Over The Counter (OTC) interest rate options	**241.8**	**1.9**	**(1.9)**	**241.8**	**1.9**	**(1.9)**
Exchange traded interest rate futures	**189.0**	**–**	**–**	**189.0**	**–**	**–**
Total derivative assets/(liabilities) held for trading purposes	**3,466.7**	**67.0**	**(52.9)**	**3,646.7**	**70.4**	**(56.3)**
Derivatives held for non-trading purposes						
Derivatives designated as cashflow hedges:						
Interest rate swaps	**14,006.9**	**218.8**	**(161.9)**	**14,006.9**	**218.8**	**(161.9)**
Derivatives designated as fair value hedges:						
Interest rate swaps	**9,245.2**	**75.0**	**(411.0)**	**7,211.5**	**75.0**	**(403.8)**
Cross currency interest rate swaps	**11.3**	**–**	**(1.2)**	**11.3**	**–**	**(1.2)**
Derivatives held for non-trading purposes for which hedge accounting has not been applied:						
Interest rate swaps	**9,803.4**	**23.1**	**(32.5)**	**5,844.6**	**37.7**	**(31.3)**
Embedded derivatives – options	**1,344.5**	**19.3**	**(17.8)**	**1,344.5**	**19.3**	**(17.8)**
Forward currency transactions	**3,282.1**	**431.4**	**(23.6)**	**1,741.7**	**147.4**	**(23.6)**
OTC interest rate options	**213.0**	**–**	**(1.2)**	**213.0**	**–**	**(1.2)**
Equity swaps	**1,137.1**	**97.3**	**(0.3)**	**1,090.9**	**92.4**	**(0.3)**
Credit default swaps	**–**	**–**	**–**	**79.4**	**–**	**–**
Total derivative assets/(liabilities) held for non-trading purposes	**39,043.5**	**864.9**	**(649.5)**	**31,543.8**	**590.6**	**(641.1)**
Total recognised derivative assets/(liabilities)	**42,510.2**	**931.9**	**(702.4)**	**35,190.5**	**661.0**	**(697.4)**

17. Derivative financial instruments continued

	Group			Bank		
	Contractual/ notional amount	Fair value Assets	Fair value Liabilities	Contractual/ notional amount	Fair value Assets	Fair value Liabilities
2009						
Derivatives held for trading purposes						
Interest rate derivatives:						
Interest rate swaps	2,938.1	45.0	(34.8)	3,108.2	48.8	(38.4)
Over The Counter (OTC) interest rate options	323.3	3.7	(3.7)	323.3	3.7	(3.7)
Exchange traded interest rate futures	1,000.0	–	–	1,000.0	–	–
Total derivative assets/(liabilities) held for trading purposes	4,261.4	48.7	(38.5)	4,431.5	52.5	(42.1)
Derivatives held for non-trading purposes						
Derivatives designated as cashflow hedges:						
Interest rate swaps	5,986.1	117.1	(69.6)	5,986.1	117.1	(69.6)
Derivatives designated as fair value hedges:						
Interest rate swaps	14,853.2	114.5	(433.0)	11,472.7	114.5	(405.9)
Cross currency interest rate swaps	192.4	6.5	(1.3)	192.4	6.5	(1.3)
Derivatives held for non-trading purposes for which hedge accounting has not been applied:						
Interest rate swaps	4,307.9	11.8	(14.4)	5,766.2	47.2	(13.8)
Embedded derivatives – options	268.3	5.4	(4.0)	268.3	5.4	(4.0)
Forward currency transactions	5,033.0	657.7	(23.4)	2,929.1	255.3	(23.4)
OTC interest rate options	25.0	–	(0.3)	25.0	–	(0.3)
Equity swaps	1,638.6	61.3	(6.8)	1,575.0	58.2	(6.8)
Credit default swaps	–	–	–	79.4	4.1	–
Total derivative assets/(liabilities) held for non-trading purposes	32,304.5	974.3	(552.8)	28,294.2	608.3	(525.1)
Total recognised derivative assets/(liabilities)	36,565.9	1,023.0	(591.3)	32,725.7	660.8	(567.2)

The derivatives designated as cashflow hedges are interest rate swaps used to hedge interest rate risk in the Bank's retail lending operations. Cash flows are hedged by quarterly time periods for durations up to ten years. During the year there were no forecast transactions for which hedge accounting had previously been used but are no longer expected to occur.

During the year the Bank has entered into fair value hedges to mitigate price movements due to interest rate sensitivities.

The number of non-margin exchange traded contracts held by the Bank as at 31 December 2010 was nil (2009: nil).

The Bank is aware that other financial institutions are moving to using overnight indexed swap (OIS) curves in the valuation of derivatives. The Bank is currently assessing the impact of what such a change would mean to the valuation of its own derivatives with a view to making any changes in 2011.

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18. Equity shares

	Group and Bank	
	2010	2009
Investment securities – unlisted	**7.2**	7.2
Included above are the following trade investments:		
Vocalink Limited – 4,416,165 ordinary shares of £1 each (2009: 4,416,165)	**7.1**	7.1

Equity shares are classified as available for sale.

19. Goodwill

	Group and Bank	
	2010	2009
Net book amount		
At the beginning of the year	**0.6**	–
Amounts arising on transfer of engagements	**–**	0.6
At the end of the year	**0.6**	0.6

The Bank's goodwill recognised in 2009 relates to the transfer of engagements of Britannia Building Society. Further detail is provided in note 39.

In accordance with IAS 38 the goodwill has been assessed as having an indefinite useful life. In assessing the recoverable amount of the goodwill the Group allocates the goodwill to the lowest cash generating unit (CGU) within the Group that is expected to benefit from the synergies of the business combination. A CGU is the smallest identifiable group of assets that generates cash inflows which are largely independent of the cash inflows from other assets of the Group.

The CGUs to which the goodwill has been allocated are the Retail, Corporate, Wholesale and Optimum and Platform reportable segments of the Bank. The recoverable amounts have been calculated by considering their value in use to the Bank. The key assumptions used in the calculation are shown below. These have been determined using past experience, understanding of the business and its industry, the expected lives of the assets and liabilities and recognition of current market events with respect to retail deposit taking business:

- modest growth in assets of 2.5% per annum from 2014 onward;
- net interest margin of 1.39% by 2014 thereafter growing by 1.5bps per annum until 2024;
- other income of 0.14% of average total assets by 2014, thereafter growing by 0.2bps per annum until 2024;
- management expenses of 0.72% of average total assets in 2014 reducing gradually to 0.57% by 2024;
- loss provisions of 0.10% of total average assets each year from 2014 onward;
- additional payments that would have been made to the members of Britannia Building Society had the transfer of engagements not occurred of 35% of profit before taxation in 2014, growing by 2.5% per annum to 40% in 2016 and remaining at 40% thereafter; and
- a discount rate of 11% has been applied to the additional payments that would have been made to the members of Britannia Building Society.

The calculations have been flexed to assess the sensitivities to reasonable changes in the already conservative assumptions. This sensitivity analysis did not indicate any likely impairment of the goodwill.

20. Intangible fixed assets

	Group 2010 Internally generated intangible assets	Group 2010 Other intangible assets	Group 2010 Total	Group 2009 Internally generated intangible assets	Group 2009 Other intangible assets	Group 2009 Total
Cost						
At the beginning of the year	**18.9**	**46.0**	**64.9**	19.5	–	19.5
Amounts arising on transfer of engagements	**–**	**–**	**–**	–	46.0	46.0
Additions	**3.1**	**–**	**3.1**	2.9	–	2.9
Disposals	**(8.1)**	**–**	**(8.1)**	(3.5)	–	(3.5)
At the end of the year	**13.9**	**46.0**	**59.9**	18.9	46.0	64.9
Accumulated amortisation						
At the beginning of the year	**15.1**	**3.7**	**18.8**	17.2	–	17.2
Charge for the year	**1.5**	**2.6**	**4.1**	1.4	3.7	5.1
Disposals	**(8.1)**	**–**	**(8.1)**	(3.5)	–	(3.5)
At the end of the year	**8.5**	**6.3**	**14.8**	15.1	3.7	18.8
Net book value						
At the end of the year	**5.4**	**39.7**	**45.1**	3.8	42.3	46.1
At the beginning of the year	3.8	42.3	46.1	2.3	–	2.3

	Bank 2010 Internally generated intangible assets	Bank 2010 Other intangible assets	Bank 2010 Total	Bank 2009 Internally generated intangible assets	Bank 2009 Other intangible assets	Bank 2009 Total
Cost						
At the beginning of the year	**17.3**	**46.0**	**63.3**	18.4	–	18.4
Amounts arising on transfer of engagements	**–**	**–**	**–**	–	46.0	46.0
Additions	**2.7**	**–**	**2.7**	2.4	–	2.4
Disposals	**(6.9)**	**–**	**(6.9)**	(3.5)	–	(3.5)
At the end of the year	**13.1**	**46.0**	**59.1**	17.3	46.0	63.3
Accumulated amortisation						
At the beginning of the year	**14.7**	**3.7**	**18.4**	16.9	–	16.9
Charge for the year	**1.2**	**2.6**	**3.8**	1.3	3.7	5.0
Disposals	**(6.9)**	**–**	**(6.9)**	(3.5)	–	(3.5)
At the end of the year	**9.0**	**6.3**	**15.3**	14.7	3.7	18.4
Net book value						
At the end of the year	**4.1**	**39.7**	**43.8**	2.6	42.3	44.9
At the beginning of the year	2.6	42.3	44.9	1.5	–	1.5

Internally generated intangible assets consist of software development costs.

Other intangible assets consist of a core deposit intangible of £44m and a brand intangible of £2m. The brand intangible has an indefinite useful life and is not amortised but is subject to an annual impairment review, using the same assumptions as those used for goodwill (refer to note 19). On the basis of this review the brand is considered to be unimpaired.

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21. Investment properties

	Group	
	2010	2009
Fair value		
At the beginning of the year	**137.7**	–
Amounts arising on transfer of engagements	**–**	123.7
Additions – acquisitions	**21.6**	8.9
Additions – subsequent expenditure	**3.6**	1.6
Disposals	**(0.5)**	–
Changes in fair value (note 7)	**(0.1)**	3.5
At the end of the year	**162.3**	137.7

All investment properties are held to generate rental income until such time that the Group considers it appropriate to realise its investment. Investment properties are carried at fair value.

The range of yields applied to the net annual rental income to determine the fair value of property is 3% to 8%.

The Group lets investment properties on Assured Shorthold Tenancy agreements, most of which are for contract periods of no more than 12 months. The future minimum lease receipts under non-cancellable operating leases are £2.4m (2009: £1.8m). The Group has not recognised any contingent rent in the year (2009: £nil). None of the lease agreements are individually significant.

Included in Group other operating income for the year is £6.5m (2009: £2.1m) of rental income relating to investment properties (note 7).

22. Property, plant and equipment

2010 Group	**Land and buildings**	**Leasehold improvements**	**Computers and other equipment**	**Total**
Cost				
At the beginning of the year	**55.7**	**24.9**	**134.6**	**215.2**
Additions	**–**	**–**	**2.6**	**2.6**
Disposals	**–**	**–**	**(12.1)**	**(12.1)**
At the end of the year	**55.7**	**24.9**	**125.1**	**205.7**
Accumulated depreciation				
At the beginning of the year	**4.1**	**2.8**	**86.8**	**93.7**
Charge for the year	**1.3**	**5.2**	**18.3**	**24.8**
Disposals	**–**	**–**	**(11.3)**	**(11.3)**
At the end of the year	**5.4**	**8.0**	**93.8**	**107.2**
Net book value				
At the end of the year	**50.3**	**16.9**	**31.3**	**98.5**
At the beginning of the year	51.6	22.1	47.8	121.5

2010 Bank	**Land and buildings**	**Leasehold improvements**	**Computers and other equipment**	**Total**
Cost				
At the beginning of the year	**34.8**	**24.8**	**130.9**	**190.5**
Additions	**–**	**–**	**1.6**	**1.6**
Disposals	**–**	**–**	**(11.5)**	**(11.5)**
At the end of the year	**34.8**	**24.8**	**121.0**	**180.6**
Accumulated depreciation				
At the beginning of the year	**1.4**	**2.8**	**84.7**	**88.9**
Charge for the year	**0.8**	**5.1**	**17.4**	**23.3**
Disposals	**–**	**–**	**(10.7)**	**(10.7)**
At the end of the year	**2.2**	**7.9**	**91.4**	**101.5**
Net book value				
At the end of the year	**32.6**	**16.9**	**29.6**	**79.1**
At the beginning of the year	33.4	22.0	46.2	101.6

22. Property, plant and equipment continued

2009 Group	Land and buildings	Leasehold improvements	Computers and other equipment	Total
Cost				
At the beginning of the year	10.1	–	144.2	154.3
Amounts arising on transfer of engagements	45.6	24.8	12.2	82.6
Additions	–	0.1	1.6	1.7
Disposals	–	–	(23.4)	(23.4)
At the end of the year	55.7	24.9	134.6	215.2
Accumulated depreciation				
At the beginning of the year	3.5	–	91.2	94.7
Charge for the year	0.6	2.8	17.6	21.0
Disposals	–	–	(22.0)	(22.0)
At the end of the year	4.1	2.8	86.8	93.7
Net book value				
At the end of the year	51.6	22.1	47.8	121.5
At the beginning of the year	6.6	–	53.0	59.6

2009 Bank	Land and buildings	Leasehold improvements	Computers and other equipment	Total
Cost				
At the beginning of the year	2.6	–	141.9	144.5
Amounts arising on transfer of engagements	32.2	24.7	11.1	68.0
Additions	–	0.1	1.2	1.3
Disposals	–	–	(23.3)	(23.3)
At the end of the year	34.8	24.8	130.9	190.5
Accumulated depreciation				
At the beginning of the year	1.0	–	89.6	90.6
Charge for the year	0.4	2.8	16.9	20.1
Disposals	–	–	(21.8)	(21.8)
At the end of the year	1.4	2.8	84.7	88.9
Net book value				
At the end of the year	33.4	22.0	46.2	101.6
At the beginning of the year	1.6	–	52.3	53.9

	Group		Bank	
	2010	2009	**2010**	2009
The net book value of land and buildings comprises:				
Freehold	**49.7**	51.0	**31.8**	32.8
Leasehold	**0.6**	0.6	**0.6**	0.6
	50.3	51.6	**32.4**	33.4

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23. Other assets

	Group		Bank	
	2010	2009	**2010**	2009
Amounts recoverable within one year:				
Trade debtors	**1.4**	1.7	**1.3**	1.7
Current tax assets	**–**	–	**–**	21.2
Other assets	**51.1**	20.4	**50.2**	22.9
	52.5	22.1	**51.5**	45.8

24. Prepayments and accrued income

	Group		Bank	
	2010	2009	**2010**	2009
Amounts recoverable within one year:				
Other	**16.2**	30.1	**14.5**	27.4

25. Deposits by banks

	Group		Bank	
	2010	2009	**2010**	2009
Items in course of collection	**45.3**	53.9	**45.3**	53.9
Deposits from other banks	**2,893.3**	6,028.5	**2,825.5**	5,559.1
	2,938.6	6,082.4	**2,870.8**	5,613.0

Included within deposits from other banks are liabilities of £1,349.1m (2009: £2,998.8m) secured on investment securities with a carrying value of £1,550.9m (2009: £3,697.0m) which have been sold under sale and repurchase agreements (note 35).

26. Customer accounts

	Group		Bank	
	2010	2009	**2010**	2009
Retail	**26,846.6**	26,700.1	**26,081.7**	26,041.5
Corporate and Markets	**4,900.1**	3,577.1	**3,830.3**	2,618.5
Other	**573.3**	551.0	**–**	–
	32,320.0	30,828.2	**29,912.0**	28,660.0

The Group has entered into interest rate swaps that protect it from changes in interest rates on the floating rate assets that are funded by its fixed rate customer accounts. Changes in the fair values of these swaps are offset by changes in the fair values of the fixed rate customer accounts. Included within customer accounts are ‘fair value hedged’ fixed rate accounts with a total nominal value of £84.7m (2009: £3,359.3m) against which there are fair value adjustments for hedged risk of £0.2m (2009: £9.7m), giving a total carrying value of £84.9m (2009: £3,369.0m).

27. Customer accounts – capital bonds

	Group		Bank	
	2010	2009	**2010**	2009
Retail	**1,794.7**	1,647.1	**1,744.0**	1,581.7

The capital bonds are fixed term customer accounts with returns based on the movement in an index (eg FTSE100) over the term of the bond.

The capital bonds have been designated on initial recognition at fair value through income and expense and are carried at their fair value.

The fair values for the capital bonds are obtained on a monthly basis from the third parties that issue these products. These external valuations are reviewed independently using valuation software to ensure the fair values are priced on a consistent basis.

None of the change in the fair value of the capital bonds is attributable to changes in the liability's credit risk.

The maximum amount the Group would contractually be required to pay at maturity for all the capital bonds is £1,756.0m (2009: £1,653.2m).

The Group uses swaps to create economic hedges against all of its capital bonds. The gain on capital bonds in the income statement for the year is £28.5m (2009: £41.8m). However, taking into account changes in fair value of the associated swaps, the net impact to the income statement for the year is a loss of £0.3m (2009: loss of £0.2m).

28. Debt securities in issue

	Group		Bank	
	2010	2009	**2010**	2009
Certificates of deposit	**638.8**	294.9	**638.8**	294.9
Commercial paper	**20.1**	71.5	**20.1**	71.5
Fixed and floating rate notes	**3,553.3**	2,967.9	**1,197.9**	1,372.9
	4,212.2	3,334.3	**1,856.8**	1,739.3

The Group has entered into cross currency interest rate swaps that protect it from changes in exchange rates and interest rates on its debt securities in issue. Changes in the fair values of these swaps are largely offset by changes in the sterling equivalent carrying value of the debt securities in issue.

Debt securities in issue include fixed and floating rate notes, the majority of which are secured on portfolios of variable and fixed rate mortgages. The notes are redeemable in part from time to time, such redemptions being limited to the net capital received from mortgagors in respect of the underlying assets. There is no requirement for the Group to make good any shortfall out of general funds. The maturity date of the notes matches the maturity date of the underlying assets.

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29. Other borrowed funds

	Group		Bank	
	2010	2009 restated	2010	2009 restated
£150,000,000 Step up callable subordinated notes 2019	**150.0**	150.0	**150.0**	150.0
60,000,000 9.25% non-cumulative irredeemable preference shares of £1 each	**60.0**	60.0	**60.0**	60.0
Floating rate subordinated notes 2016	**104.1**	102.8	**104.1**	102.8
Subordinated notes 2021	**150.0**	150.0	**150.0**	150.0
Fixed rate subordinated notes 2024	**144.0**	130.6	**144.0**	130.6
Fixed rate subordinated notes 2033	**99.1**	91.9	**99.1**	91.9
Perpetual subordinated bonds	**253.2**	246.6	**253.2**	246.6
Issue costs, discounts and accrued interest	**15.0**	14.6	**15.0**	14.6
	975.4	946.5	**975.4**	946.5

The 2009 restatement relates to a reclassification of accrued interest.

Step up callable subordinated notes 2019
The notes were issued on 1 April 2004 at a discount of 0.946%.

The notes are an unsecured obligation of the Bank and in the event of the winding up of the Bank, the claims of noteholders will be subordinated in right of payment to the claims of depositors and other creditors of the Bank.

The notes carry an interest rate of 5.875% per annum to (but excluding) 2 April 2014, and thereafter the interest rate will be determined by reference to the gross redemption yield on the five year benchmark gilt, and a margin of 2.25%. Interest is payable annually in arrears on 2 April.

The Bank may redeem all, but not less than all, of the notes at their principal amount on 2 April 2014.

60,000,000 9.25% non-cumulative irredeemable preference shares of £1 each
The preference shares carry the right to a fixed non-cumulative preferential dividend on the capital for the time being paid up, at the rate of 9.25% per annum exclusive of any associated tax credit. The dividends are payable on 31 May and 30 November each year and take priority over dividends to any other class of share in the capital of the Bank.

On a return of capital on winding up, the assets of the Bank shall be applied in repaying the preference share capital in priority to any payments to the holders of any other class of shares in the capital of the Bank. The amount receivable by the holders of the preference shares shall be the greater of the capital paid up or the average quoted price during the three months immediately preceding the date of the notice convening the meeting to consider the resolution to wind up.

The holders of the preference shares shall have the right to vote at a general meeting of the Bank only if and when, at the date of the notice convening the meeting, the dividend due to them has been in arrears for six months or more or if a resolution is to be proposed at the meeting abrogating or varying their rights or privileges or for the winding up of the Bank or other return of capital and then only on that resolution.

Floating rate subordinated notes 2016
The notes were issued on 18 May 2006 at a discount of 0.14%.

The notes are an unsecured obligation of the Bank and in the event of the winding up of the Bank, the claims of noteholders will be subordinated in right of payment to the claims of depositors and other creditors of the Bank.

The notes are denominated in euros and interest is calculated at three months EURIBOR plus a margin of 0.28%. The first interest coupon was paid in August 2006.

The notes are hedged with a cross currency swap converting the exposure into sterling which pays floating rate at three months LIBOR with a margin on interest coupon of 0.34125% and receives floating rate of three months EURIBOR plus a margin on interest coupon of 0.28%. The cross currency swap matures on 18 May 2011.

The Bank may redeem all, but not less than all, of the notes at the principal amount on 18 May 2011, and on any quarterly interest payment date thereafter.

Subordinated notes 2021
The notes were issued on 16 November 2006 at a discount of 0.189%.

The notes are an unsecured obligation of the Bank and in the event of the winding up of the Bank, the claims of noteholders will be subordinated in right of payment to the claims of depositors and other creditors of the Bank.

The notes carry an annual interest rate of 5.625% up to and including the interest payment date on 16 November 2016, when the interest basis changes to floating rate. During the fixed rate period, interest is payable semi-annually in arrears on 16 May and 16 November.

From 17 November 2016, the notes carry a floating interest rate of three months LIBOR plus a margin of 1.75%. Interest is payable quarterly in arrears on 16 February, 16 May, 16 August and 16 November, commencing on the interest payment date falling in February 2017 up to and including the maturity date.

The Bank may redeem all, but not less than all, of the notes at the principal amount on 16 November 2016, and on any quarterly interest payment date thereafter.

29. Other borrowed funds continued

Fixed rate subordinated notes 2024

The notes were issued on 17 March 2004 at a discount rate of 1.148%.

The notes are an unsecured obligation of the Bank and in the event of the winding up of the Bank, the claims of noteholders will be subordinated in right of payment to the claims of depositors and other creditors of the Bank.

The notes carry an annual interest rate of 5.75% to maturity. The notes are hedged with interest rate swaps that convert the interest rate payable into floating rates at six months LIBOR plus a margin of 0.72%. The fixed receipt leg of the swap is received annually to match the payment to the noteholders. The floating payment leg of the swap is payable semi-annually in June and December. The interest rate swaps mature on 2 December 2019.

The Bank may redeem all, but not less than all, of the notes at the principal amount on 2 December 2019, and on any quarterly interest payment date thereafter.

Fixed rate subordinated notes 2033

The notes were issued on 28 March 2002 at a discount rate of 0.93%.

The notes are an unsecured obligation of the Bank and in the event of the winding up of the Bank, the claims of noteholders will be subordinated in right of payment to the claims of depositors and other creditors of the Bank.

The notes carry an annual interest rate of 5.875% to maturity. Interest is payable semi-annually in March and September.

Of the notes, £100m are hedged with interest rate swaps that have a floating payment leg at six months LIBOR payable in March and September. The fixed interest rate receivable legs on the swaps are £25m at 5.405% and £75m at 5.225%. The annual interest receivable leg on the swap is matched to the dates on the notes.

Perpetual subordinated bonds

Following the transfer of engagements of Britannia Building Society, the Britannia permanent interest bearing shares (PIBS) were converted into perpetual subordinated debt of the Co-operative Financial Services (perpetual subordinated bonds).

From 1 August 2009, the Bank assumed a liability to each PIBS holder for a subordinated deposit equal to the principal amount of their PIBS. These deposits have automatically been applied in subscription to either perpetual subordinated bonds having an annual interest rate of 13% in respect of the 'first perpetual subordinated bonds' or perpetual subordinated bonds having an annual interest rate of 5.5555% in respect of the 'second perpetual subordinated bonds' for an amount corresponding to the principal amount of that holder's PIBS.

The trustee for the holders of the perpetual subordinated bonds is The Law Debenture Trust Corporation plc whose registered office is Fifth Floor, 100 Wood Street, London, EC2V 7EX.

The FSA must give prior written consent to the early repayment, including the purchase of the notes or stock by the Group, for cancellation of any subordinated bond.

30. Other liabilities

	Group		Bank	
	2010	2009	**2010**	2009
Amounts falling due within one year:				
Other creditors	**142.8**	217.7	**136.7**	206.7
Amounts falling due after one year:				
Other creditors	**4.0**	4.2	**3.8**	4.1
	146.8	221.9	**140.5**	210.8

Other creditors for the Group and Bank include finance lease obligations as follows:

	Present value of lease payments		Future minimum lease payments	
	2010	2009	**2010**	2009
Due within one year	**–**	–	**–**	–
Due between one year and five years	**0.1**	0.1	**0.1**	0.1
Due after five years	**1.3**	1.2	**1.7**	1.8
	1.4	1.3	**1.8**	1.9

The future minimum lease payments have been discounted at LIBOR over the term of the lease to give the present value of these payments.

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31. Accruals and deferred income

	Group		Bank	
	2010	2009	**2010**	2009
Amounts falling due within one year:				
Other	**85.3**	148.1	**71.1**	124.5
Amounts falling due after one year:				
Other	**46.0**	9.9	**45.9**	9.8
	131.3	158.0	**117.0**	134.3

32. Provisions for liabilities and charges

2010 Group	**Property**	**FSCS levies**	**Regulatory/ other**	**Total**
At the beginning of the year	**7.1**	**20.6**	**25.1**	**52.8**
Income statement movements:				
Provided in the year – operating expense (note 8)	**3.4**	**11.5**	**3.5**	**18.4**
Provided in the year – operating income (note 5)	**–**	**–**	**13.1**	**13.1**
Released during the year (note 8)	**(0.3)**	**–**	**(12.3)**	**(12.6)**
Utilised during the year	**(1.4)**	**(11.2)**	**(3.3)**	**(15.9)**
At the end of the year	**8.8**	**20.9**	**26.1**	**55.8**
Provisions were analysed as follows:				
Amounts falling due within one year	**1.2**	**10.6**	**24.1**	**35.9**
Amounts falling due after one year	**7.6**	**10.3**	**2.0**	**19.9**
	8.8	**20.9**	**26.1**	**55.8**

2010 Bank	**Property**	**FSCS levies**	**Regulatory/ other**	**Total**
At the beginning of the year	**5.4**	**20.1**	**19.5**	**45.0**
Income statement movements:				
Provided in the year – operating expense	**3.2**	**11.0**	**–**	**14.2**
Provided in the year – operating income	**–**	**–**	**4.3**	**4.3**
Released during the year	**(0.2)**	**–**	**(12.2)**	**(12.4)**
Utilised during the year	**(1.0)**	**(10.8)**	**–**	**(11.8)**
At the end of the year	**7.4**	**20.3**	**11.6**	**39.3**
Provisions were analysed as follows:				
Amounts falling due within one year	**1.0**	**9.7**	**11.6**	**22.3**
Amounts falling due after one year	**6.4**	**10.6**	**–**	**17.0**
	7.4	**20.3**	**11.6**	**39.3**

32. Provisions for liabilities and charges continued

2009 restated **Group**	Property	FSCS levies	Regulatory/ other	Total
At the beginning of the year	5.1	10.5	0.2	15.8
Arising on transfer of engagements	4.0	10.1	19.5	33.6
Income statement movements:				
Provided in the year – operating expense (note 8)	0.9	10.1	5.5	16.5
Released during the year (note 8)	(2.2)	(6.4)	(0.1)	(8.7)
Utilised during the year	(0.7)	(3.7)	–	(4.4)
At the end of the year	7.1	20.6	25.1	52.8
Provisions were analysed as follows:				
Amounts falling due within one year	1.6	11.6	21.4	34.6
Amounts falling due after one year	5.5	9.0	3.7	18.2
	7.1	20.6	25.1	52.8

2009 restated **Bank**	Property	FSCS levies	Regulatory/ other	Total
At the beginning of the year	4.5	10.2	–	14.7
Arising on transfer of engagements	2.7	10.1	19.5	32.3
Income statement movements:				
Provided in the year	0.9	9.7	–	10.6
Released during the year	(2.0)	(6.3)	–	(8.3)
Utilised during the year	(0.7)	(3.6)	–	(4.3)
At the end of the year	5.4	20.1	19.5	45.0
Provisions were analysed as follows:				
Amounts falling due within one year	0.9	11.2	19.5	31.6
Amounts falling due after one year	4.5	8.9	–	13.4
	5.4	20.1	19.5	45.0

Property

The Group has a number of leasehold properties available for rent. Provisions are made when either the sub-lease income does not cover the rental expense or the property is vacant. The provision is based on the expected outflows during the remaining periods of the leases using the discount rate applied in the goodwill calculations of 11%.

FSCS levies

In common with other financial institutions authorised by the FSA, the Group contributes to the Financial Services Compensation Scheme (FSCS). The FSCS covers financial institutions authorised to do business in the UK. When an institution is unlikely, or likely to be unable, to pay claims against it, its customers may be able to claim compensation from the FSCS. The FSCS raises funds to meet the known compensation claims through levies on other FSA authorised institutions.

As a result of a number of institutions failing during 2008, the FSCS received funds from HM Treasury in order to meet its obligations to depositors. These borrowings are anticipated to be repaid wholly or substantially from the realisation of the assets of the failed institutions.

The FSCS raises annual levies from the banking industry in order to meet its management expenses and compensation costs. The annual levies are based upon each individual institution's proportion of protected deposits of the total market protected deposits at 31 December each year.

The Group has provided £20.9m (2009: £20.6m) for its share of the levies that will be raised by the FSCS including the interest on the loan from the HM Treasury in respect of the levy years 31 March 2011 to 31 March 2012 respectively. The provision includes estimates for the interest the FSCS will pay on the loan and of the Group's market participation in the relevant years.

At the date of these financial statements, it is not possible to estimate whether there will ultimately be additional levies on the industry, the level of the Group's market participation or other factors that may affect amounts or the timing of amounts that may ultimately become payable, nor the effect that such levies may have upon operating results in any particular year.

The Financial Services Commission in the Isle of Man operates a similar scheme. Britannia International Limited has provided £0.3m (2009: £0.3m) for the year ended 31 December 2010 in respect of this scheme.

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32. Provisions for liabilities and charges continued
Regulatory/other

Provisions have been made in respect of various potential customer compensation claims. Claims are investigated on an individual basis and, where appropriate, compensation payments are made.

The release of regulatory/other provision relates to a disputed claim which was resolved during the year.

33. Deferred tax
Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 27% (2009: 28%).

The movements on the deferred tax accounts are as follows:

	Group		Bank	
	2010	2009 restated	**2010**	2009
Net deferred tax at the beginning of the year	**86.1**	(27.0)	**210.3**	(22.5)
Amounts arising on transfer of engagements	**–**	124.6	**–**	233.0
Income statement charge	**(2.5)**	(20.9)	**(57.8)**	(9.3)
Prior year adjustments	**2.1**	0.3	**0.2**	–
Charged to equity:				
Unrealised appreciation on investments	**–**	1.1	**–**	1.1
Pension fund deficit	**0.1**	0.1	**0.1**	0.1
Cashflow hedges	**1.2**	7.9	**1.2**	7.9
Net deferred tax at the end of the year	**87.0**	86.1	**154.0**	210.3
Net deferred tax comprises:				
Deferred tax asset	**203.3**	285.2	**154.0**	230.9
Deferred tax liability	**(116.3)**	(199.1)	**–**	(20.6)
	87.0	86.1	**154.0**	210.3
Deferred tax				
Cashflow hedges	**(13.4)**	(11.1)	**(13.4)**	(11.1)
Unrealised appreciation on investments	**(1.1)**	(2.9)	**(1.1)**	(2.8)
Capital allowances on fixed assets	**32.6**	(3.1)	**33.6**	(2.0)
Capital allowances on assets leased to customers	**(3.5)**	(4.0)	**0.2**	–
Pensions and other post-retirement benefits	**1.0**	1.0	**1.0**	1.0
Fair value adjustments	**34.5**	26.3	**129.0**	198.4
Other temporary differences	**36.9**	74.9	**4.7**	21.8
Tax losses carried forward	**–**	5.0	**–**	5.0
	87.0	86.1	**154.0**	210.3

Other temporary differences for the Group of £36.9m (2009: £74.9m) include deferred tax assets/liabilities as a result of interest deductible when paid, loss provisions on mortgage assets held by Special Purpose Entities (SPEs), taxation of SPEs under the securitisation regime and spreading of the tax effect of IFRS transitional adjustments.

The deferred tax charge in the income statement comprises the following temporary differences:

	Group		Bank	
	2010	2009	**2010**	2009
Cashflow hedges	**–**	0.2	**–**	0.2
Capital allowances on fixed assets	**4.2**	(1.4)	**4.3**	(1.6)
Capital allowances on assets leased to customers	**(0.5)**	(0.3)	**(0.2)**	(0.2)
Fair value adjustments	**(44.3)**	46.8	**33.4**	13.1
Other temporary differences	**41.0**	(37.6)	**20.1**	(14.0)
Tax losses carried forward	**–**	12.9	**–**	11.8
	0.4	20.6	**57.6**	9.3

The Budget on 23 March 2011 announced that the UK corporation tax rate will reduce from 28% to 23% over a period of four years from 2011. The first reduction in the UK corporation tax rate from 28% to 27% was substantively enacted on 20 July 2010 and would have been effective from 1 April 2011. The budget on 23 March now proposes that a UK corporation tax rate of 26% will be effective from 1 April 2011. This will reduce the Group's future current tax charge accordingly. The tax disclosures for the period reflect the deferred tax at the 27% substantively enacted rate. It has not yet been possible to quantify the full anticipated effect of the further rate reductions, although this will further reduce the Group's future tax charge and reduce the Group's deferred tax assets/liabilities accordingly.

34. Pensions

Defined contribution basis

With effect from 6 April 2006 the Bank Group, along with other businesses within The Co-operative Group has participated in the Co-operative Group Pension (Average Career Earnings) Scheme (the PACE scheme). This scheme is a defined benefit scheme, the assets of which are held in a separate fund administered by trustees. As a group wide pension scheme, the PACE scheme exposes the participating businesses to actuarial risks associated with the current and former employees of other Group companies, with the result that there is no consistent and reliable basis for allocating liabilities, assets and costs to individual companies participating in the scheme. Therefore the pension cost shown in these accounts in respect of the PACE scheme for the period after 6 April 2006 is the actual contributions paid by the Bank.

Key assumptions of the Group pension scheme

The key aspects of The Co-operative Group's PACE scheme are as follows:

	2010	2009
The principal assumptions used to determine the liabilities of the PACE scheme are:		
Discount rate	**5.20%**	5.60%
Rate of increase in salaries	**5.20%**	5.30%
Future pension increases where capped at 5.0% per annum	**3.70%**	3.80%
Future pension increases where capped at 2.5% per annum	**2.50%**	2.50%
Assumptions used to determine net pension cost for the PACE scheme are:		
Discount rate	**5.60%**	5.70%
Expected long term return on scheme assets	**6.50%**	6.40%
Rate of increase in salaries	**5.30%**	4.75%

The average life expectancy (in years) for mortality tables used to determine scheme liabilities for the PACE scheme at the 2010 year end is:

	Male	**Female**
Life expectancy:		
Member currently aged 65 (current life expectancy)	**21.7**	**23.3**
Member currently aged 45 (life expectancy at age 65)	**23.2**	**24.9**

The amounts recognised in the balance sheet of The Co-operative Group are as follows:

	2010	2009
Present value of funded obligations	**(5,794.2)**	(5,509.0)
Present value of unfunded obligations	**(4.1)**	(3.8)
Fair value of plan assets	**6,071.3**	5,514.4
	273.0	1.6

The weighted average asset allocations at the year end were as follows:

	2010	2009
Equities	**31%**	35%
Liability driven investments	**54%**	54%
Alternative growth	**9%**	6%
Property	**4%**	4%
Cash	**2%**	1%

To develop the expected long term rate of return on assets assumption, the Group considered the current level of expected returns on risk free investments (primarily government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each asset class. The expected return for each asset class was then weighted based on the target asset allocation to develop the expected long term rate of return on assets assumption for the portfolio. This resulted in the selection of the 6.5% assumption for the year ended 31 December 2010.

Former Britannia Building Society pension scheme

Following the transfer of engagements of Britannia Building Society, the Britannia pension scheme transferred to the Co-operative Financial Services Management Services Limited (CFSMS). The pension cost shown in these accounts in respect of the Britannia defined benefit scheme for the period after 31 July 2009 is the actual contribution paid by the Bank.

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34. Pensions continued
The key aspects of the Britannia defined benefit scheme are as follows:

	2010	2009
The principal assumptions used to determine the liabilities of the Britannia defined benefit scheme are:		
Discount rate	**5.20%**	5.60%
Rate of increase in salaries	**5.20%**	5.30%
Future pension increases where capped at 5.0% per annum	**3.70%**	3.80%
Future pension increases where capped at 2.5% per annum	**2.50%**	2.50%
Assumptions used to determine net pension cost for the Britannia defined benefit scheme are:		
Discount rate	**5.60%**	6.30%
Expected long term return on scheme assets	**6.20%**	6.40%
Rate of increase in salaries	**5.30%**	5.30%

The average life expectancy (in years) for mortality tables used to determine defined benefit scheme liabilities for the former Britannia Building Society scheme at the 2010 year end is:

	Male	**Female**
Life expectancy:		
Member currently aged 65 (current life expectancy)	**23.4**	**25.7**
Member currently aged 40 (life expectancy at age 60)	**24.9**	**27.3**

	2010	2009
Present value of funded obligations	**(549.4)**	(478.1)
Present value of unfunded obligations	**(5.6)**	(4.7)
Fair value of plan assets	**509.2**	449.6
	(45.8)	(33.2)

	2010	2009
The weighted average asset allocations at the year end were as follows:		
Equities	**28%**	26%
Diversified growth	**17%**	20%
Liability driven investments	**54%**	54%
Property	**1%**	–

Bank (unfunded) pension scheme
The Bank also operates a small unfunded pension scheme.

	2010	2009	2008	2007	2006
Expected return on scheme assets	**N/A**	N/A	N/A	N/A	N/A
Rate of increase of pensions in payment	**3.7%**	3.8%	3.3%	3.4%	2.9%
Rate of increase in salaries	**5.2%**	5.3%	4.8%	4.9%	4.4%
Discount rate	**5.2%**	5.6%	5.7%	5.7%	4.9%

The assumptions used by the actuary were the best estimates chosen from a range of possible actuarial assumptions which, due to the timescales covered, may not necessarily be borne out in practice.

The values of the assets and liabilities of the unfunded pension scheme were:

	Group		**Bank**	
	2010	2009	**2010**	2009
Present value of unfunded obligations	**(3.8)**	(3.5)	**(3.8)**	(3.5)
Deficit in scheme	**(3.8)**	(3.5)	**(3.8)**	(3.5)
Related deferred tax asset	**1.0**	1.0	**1.0**	1.0
Net pension liability	**(2.8)**	(2.5)	**(2.8)**	(2.5)
Analysis of amount charged to income statement:				
Current service cost	**–**	–	**–**	–
Interest on pension scheme liabilities	**0.2**	0.2	**0.2**	0.2
	0.2	0.2	**0.2**	0.2

34. Pensions continued

Changes in the present value of the scheme liabilities are as follows:

	Group		Bank	
	2010	2009	**2010**	2009
Opening defined benefit liabilities	**3.5**	3.2	**3.5**	3.2
Current service cost	**–**	–	**–**	–
Interest on liabilities	**0.2**	0.1	**0.2**	0.1
Actuarial losses	**0.3**	0.3	**0.3**	0.3
Benefits paid	**(0.2)**	(0.1)	**(0.2)**	(0.1)
Closing defined benefit liabilities	**3.8**	3.5	**3.8**	3.5

Amounts recognised in the statement of comprehensive income:

	Group		Bank	
	2010	2009	**2010**	2009
Actuarial losses on scheme liabilities during the year	**(0.3)**	(0.3)	**(0.3)**	(0.3)
Actuarial gains on scheme assets during the year	**–**	–	**–**	–
Total scheme losses during the year	**(0.3)**	(0.3)	**(0.3)**	(0.3)

The amounts for the current year are as follows:

	Group		Bank	
	2010	2009	**2010**	2009
Defined benefit obligation	**(3.8)**	(3.5)	**(3.8)**	(3.5)
Scheme assets	**–**	–	**–**	–
Deficit in scheme	**(3.8)**	(3.5)	**(3.8)**	(3.5)
Experience adjustment on scheme liabilities	**–**	–	**–**	–
Experience adjustment on scheme assets	**–**	–	**–**	–

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35. Contingent liabilities and commitments
The tables below give, for the Group and Bank, the nominal principal amounts, credit equivalent amounts and risk weighted amounts of contingent liabilities and commitments. The nominal principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The credit equivalent and risk weighted amounts have been calculated in accordance with the FSA guidelines implementing the Capital Requirements Directive (CRD).

The contingent liabilities of the Group and the Bank as detailed below arise in the normal course of banking business and it is not practical to quantify their future financial effect.

	Contract amount 2010	Credit equivalent amount[i] 2010	Average risk weight 2010	Risk weighted amount 2010	Contract amount 2009	Risk weighted amount 2009
Group						
Contingent liabilities:						
Guarantees and irrevocable letters of credit	**134.2**	**108.9**	**91.0%**	**99.1**	118.9	89.5
Bank						
Contingent liabilities:						
Guarantees and irrevocable letters of credit	**132.8**	**108.2**	**90.9%**	**98.4**	116.8	88.5
Group						
Other commitments:						
Documentary credits and short term trade related transactions	**2.8**	**0.6**	**83.3%**	**0.5**	2.1	0.4
Forward asset purchases and forward deposits placed	**165.8**	**165.8**	**8.8%**	**14.6**	164.5	78.2
Undrawn formal standby facilities, credit lines and other commitments to lend (includes revocable and irrevocable commitments)[ii]	**4,590.9**	**2,782.0**	**39.2%**	**1,089.3**	4,822.9	1,032.9
	4,759.5	**2,948.4**	**37.5%**	**1,104.4**	4,989.5	1,111.5
Bank						
Other commitments:						
Documentary credits and short term trade related transactions	**2.8**	**0.6**	**83.3%**	**0.5**	2.1	0.4
Forward asset purchases and forward deposits placed	**165.8**	**165.8**	**8.8%**	**14.6**	164.5	78.2
Undrawn formal standby facilities, credit lines and other commitments to lend (includes revocable and irrevocable commitments)[ii]	**4,450.9**	**2,705.1**	**40.0%**	**1,081.5**	4,656.4	995.8
	4,619.5	**2,871.5**	**38.2%**	**1,096.6**	4,823.0	1,074.4

Notes
(i) Under the CRD credit conversion factors are applied to exposures subject to the Standard and Foundation IRB approach, primarily Corporate and Wholesale exposures as defined by BIPRU. Under the retail IRB approach the Credit Equivalent amount is defined as Exposure at Default.
(ii) Undrawn loan commitments include revocable commitments which are unused credit card limits of £2,344.9m (2009: £2,621.9m).

Assets pledged
Assets are pledged as collateral under repurchase agreements with other banks. These deposits are not available to finance the Group's day to day operations. Mandatory reserve deposits are also held with the Bank of England in accordance with statutory requirements.

At 31 December 2010, the mandatory reserve deposits held with the Bank of England were £36.1m (2009: £34.0m) (see note 13).

Investment securities with a carrying value of £1,550.9m (2009: £3,697.0m) have been sold under sale and repurchase agreements. These assets have not been derecognised as the Group and Bank has retained substantially all the risks and rewards of ownership. Included within deposits by banks are the related liabilities of £1,349.1m (2009: £2,998.8m). Also £988.6m (2009: £nil) of amounts owed by other Co-operative Group undertakings, held by the Bank, have been sold under sale and repurchase agreements, included within deposits by banks are the related liabilities of £778.6m (2009: £nil).

The Group and Bank have loans and advances to banks of £70.0m (2009: £nil) under reverse sale and repurchase agreements and against which it holds gilts with a fair value of £70.0m (2009: £nil). These transactions are conducted under terms that are usual and customary to standard stock lending, securities borrowing and reverse purchase agreements. The Group is permitted to sell or repledge the assets received as collateral in the absence of their default. The Group is obliged to return equivalent securities. At 31 December 2010 the fair value of collateral repledged amounted to £70.0m (2009: £nil). The Group and Bank do not adjust for the fair value of securities received under reverse sale and repurchase agreements.

35. Contingent liabilities and commitments continued

Commitments under operating leases

The Group leases various properties and equipment under non-cancellable operating lease arrangements. The leases have various terms, ranging from six months to 999 years. None of these leases are individually material and none have any material clauses. The table below discloses the minimum operating lease payments the Group and the Bank will be required to make over the remaining lives of the leases.

	Land and buildings 2010	**Equipment 2010**	Land and buildings 2009	Equipment 2009
Group				
Falling due:				
Within one year	**24.4**	**0.4**	22.2	0.8
Between one and five years	**78.6**	**0.4**	74.8	0.7
In five years or more	**103.5**	**–**	110.5	0.1
	206.5	**0.8**	207.5	1.6
Bank				
Falling due:				
Within one year	**24.0**	**0.4**	22.0	0.8
Between one and five years	**75.9**	**0.4**	70.5	0.7
In five years or more	**84.5**	**–**	94.0	0.1
	184.4	**0.8**	186.5	1.6

The Group leases a number of branch and office premises under operating leases. The leases typically run for a period of up to 25 years, with an option to renew the lease after that period. Lease payments are generally reviewed every three to five years to reflect market rentals.

The total value of future minimum sub-lease payments expected to be received under non-cancellable sub-leases for the Group was £13.4m (2009: £13.3m) and for the Bank was £12.2m (2009: £12.2m).

Former Britannia Building Society pension scheme guarantee

Following the transfer of engagements of Britannia Building Society, the Britannia pension scheme transferred to CFSMS. Under the terms of this transfer the Bank entered into a deed of guarantee to provide assurance to the trustees of the pension scheme to support CFSMS in meeting its funding obligations to the scheme should CFSMS be unable to pay its obligations as they fall due.

Intra-group guarantee

The Bank has an indemnification agreement, accounted for as an intra-group guarantee under IFRS 4, with CFSMS in which the Bank has agreed to indemnify CFSMS against all and any liability, loss, damage, costs and expense arising from the agreement.

Payment protection insurance (PPI)

The Financial Services Authority (FSA) set out its requirements for this industry wide issue in a policy statement published on 10 August 2010. This amended the 'Disputes Resolution: Complaints' section of the FSA Handbook which sets out the rules for handling such complaints. Firms were initially required to comply with these new rules by 1 December 2010. However, in October 2010, the British Bankers Association (BBA) launched a judicial review on the basis that the FSA's policy statement applies incorrect standards for the management of complaints relating to PPI sales and also that it retrospectively applied rules with higher standards than those in place at the time of sale. Pending the outcome of this review, the implementation of the FSA's policy statement is on hold and therefore it is not practicable to make a reliable estimate of the amount of any provision that may be required.

The Bank stopped selling PPI at the beginning of 2009.

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36. Investments in Group undertakings
Investments in equity shares and loans of subsidiary undertakings are financial assets.

	2010			2009 restated		
	Ordinary shares	**Capital contributions**	**Total**	Ordinary shares	Capital contributions	Total
At the beginning of the year	**576.4**	**996.0**	**1,572.4**	2.7	966.6	969.3
Arising on transfer of engagements	**–**	**–**	**–**	542.3	424.2	966.5
Additions	**11.5**	**386.0**	**397.5**	31.4	59.2	90.6
Impairment of investment in Co-operative Bank Financial Advisers Limited	**(18.9)**	**–**	**(18.9)**	–	–	–
Repayments	**–**	**(492.1)**	**(492.1)**	–	(454.0)	(454.0)
At the end of the year	**569.0**	**889.9**	**1,458.9**	576.4	996.0	1,572.4

Subsidiary undertakings
The Bank has, except in the case of Unity Trust Bank plc, 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 consolidated Group results.

Principal subsidiary undertakings which are registered in England and operating in the UK:

		Group interest 2010	Group interest 2009
Unity Trust Bank plc (held through subsidiary undertaking)	Banking	**27%**	27%
Co-operative Commercial Limited	Investment company	**100%**	100%
Roodhill Leasing Limited	Leasing	**100%**	100%
First Roodhill Leasing Limited	Leasing	**100%**	100%
Second Roodhill Leasing Limited	Leasing	**100%**	100%
Third Roodhill Leasing Limited	Leasing	**100%**	100%
Fourth Roodhill Leasing Limited	Leasing	**100%**	100%
Co-operative Bank Financial Advisers Limited	Financial advisers	**100%**	100%
The Covered Bond LLP	Mortgage acquisition and guarantor of covered bonds	**100%**	100%
Britannia Treasury Services Limited*	Holding company	**100%**	100%
Britannia Development and Management Company Limited*	Property investment	**100%**	100%
Britannia Asset Management Limited*	Holding company	**100%**	100%
Illius Properties Limited*	Property investment	**100%**	100%
Moorland Covered Bonds LLP* (formerly Britannia Covered Bonds LLP)	Mortgage acquisition and guarantor of covered bonds	**100%**	100%
Britannia Estate Agents Limited*	Former estate agents	**100%**	100%
Phoenix Credit Services Limited	In house debt recovery agents	**100%**	100%

During 2008, The Covered Bond LLP was established as a result of a £1.0bn covered bond issued by the Bank. Loans and advances to customers of £2.3bn were transferred to the LLP. The transfer was funded by a loan of £1.0bn and capital contribution of £1.3bn.

On the transfer of engagements of Britannia Building Society, the Bank obtained an interest in Moorland Covered Bonds LLP, which was established as a result of a £1.4bn covered bond issuance. Loans and advances to customers of £1.9bn were transferred to Moorland Covered Bonds LLP. The transfer was funded by a loan of £1.4bn and capital contribution of £0.5bn.

The loans issued by the Bank to fund the transfer of the loans and advances to customers are included within amounts owed by other Co-operative Group undertakings. The associated capital contribution invested by the Bank in both covered bond issuances is included within investments in Group undertakings. The covered bonds were immediately repurchased by the Bank and therefore no liability is recognised on the balance sheet.

The Covered Bond LLP and Moorland Covered Bonds LLP do not have ordinary share capital. The Bank's interest in The Covered Bond LLP and Moorland Covered Bonds LLP is in substance no different than a wholly owned subsidiary and consequently they are fully consolidated in the Group accounts.

The accounting policy for Special Purpose Entities (SPEs) is disclosed on pages 38 and 39.

Unity Trust Bank plc is considered to be a subsidiary undertaking of The Co-operative Bank plc as The Co-operative Bank plc elects a majority of the directors and appoints the chair and managing director. This provides the power to control.

Investments in equity shares and loans with subsidiary undertakings are shown net of impairments.

36. Investments in Group undertakings continued

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

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

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

Platform Consumer Services Limited*	Mortgage lending
Platform Funding Limited*	Mortgage origination
Platform Funding No. 2 Limited*	Finance company
Platform Funding No. 3 Limited*	Finance company
Platform Funding No. 4 Limited*	Finance company
Platform Funding No. 5 Limited*	Finance company
Platform Funding No. 6 Limited*	Finance company
Platform Home Loans Limited*	Mortgage origination and servicing

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

Registered in the Isle of Man and operating overseas:

Britannia International Limited*	Deposit taking

Registered in Scotland and operating in the UK:

Britannia Life Direct Limited*	Direct sales of financial services

Subsidiary undertaking, registered in Scotland and operating in the UK, where the Bank 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

Securitisation vehicles

The results of the following securitisation vehicles are consolidated into the results of the Group under IAS 27:

Leek Finance Holdings Limited*	Holding company
Leek Finance Number One plc*	Securitisation company
Leek Finance Holdings Number Two Limited*	Holding company
Leek Finance Number Two plc*	Securitisation company
Leek Finance Holdings Number Three Limited*	Holding company
Leek Finance Number Three plc*	Securitisation company
Leek Finance Holdings Number Four Limited*	Holding company
Leek Finance Number Four Limited*	Securitisation company
Leek Finance Holdings Number Five Limited*	Holding company
Leek Finance Number Five Limited*	Securitisation company
Leek Finance Holdings Number Six Limited*	Holding company
Leek Finance Number Six Limited*	Securitisation company
Leek Finance Holdings Number Seven Limited*	Holding company
Leek Finance Number Seven plc*	Securitisation company
Leek Finance Holdings Number Eight Limited*	Holding company
Leek Finance Number Eight Limited*	Securitisation company
Leek Finance Holdings Number Nine Limited*	Holding company
Leek Finance Number Nine Limited*	Securitisation company
Leek Finance Holdings Number Ten Limited*	Holding company
Leek Finance Number Ten plc*	Securitisation company
Leek Finance Holdings Number Eleven Limited*	Holding company
Leek Finance Number Eleven plc*	Securitisation company
Leek Finance Holdings Number Twelve Limited*	Holding company
Leek Finance Number Twelve plc*	Securitisation company
Leek Finance Holdings Number Fourteen Limited*	Holding company

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36. Investments in Group undertakings continued

Leek Finance Number Fourteen plc*	Securitisation company
Leek Finance Holdings Number Fifteen Limited*	Holding company
Leek Finance Number Fifteen plc*	Securitisation company
Leek Finance Holdings Number Sixteen Limited*	Holding company
Leek Finance Number Sixteen plc*	Securitisation company
Leek Finance Holdings Number Seventeen Limited*	Holding company
Leek Finance Number Seventeen plc*	Securitisation company
Leek Finance Holdings Number Eighteen Limited*	Holding company
Leek Finance Number Eighteen plc*	Securitisation company
Leek Finance Holdings Number Nineteen Limited*	Holding company
Leek Finance Number Nineteen plc*	Securitisation company
Leek Finance Holdings Number Twenty Limited*	Holding company
Leek Finance Number Twenty plc*	Securitisation company
Leek Finance Holdings Number Twenty One Limited*	Holding company
Leek Finance Number Twenty One plc*	Securitisation company
Leek Finance Holdings Number Twenty Two Limited*	Holding company
Leek Finance Number Twenty Two plc*	Securitisation company
Meerbrook Finance Holdings Number One Limited*	Holding company
Meerbrook Finance Number One Limited*	Securitisation company
Meerbrook Finance Holdings Number Two Limited*	Holding company
Meerbrook Finance Number Two Limited*	Securitisation company
Meerbrook Finance Holdings Number Three Limited*	Holding company
Meerbrook Finance Number Three Limited*	Securitisation company
Meerbrook Finance Holdings Number Four Limited*	Holding company
Meerbrook Finance Number Four Limited*	Securitisation company
Meerbrook Finance Holdings Number Five Limited*	Holding company
Meerbrook Finance Number Five Limited*	Securitisation company
Meerbrook Finance Holdings Number Six Limited*	Holding company
Meerbrook Finance Number Six Limited*	Securitisation company
Rudyard Finance Holdings Number One Limited*	Holding company
Rudyard Finance Number One plc*	Securitisation company
Dovedale Finance Number One plc*	Securitisation company
Silk Road Finance Number One plc	Securitisation company
Silk Road Holdco Limited	Holding company
Prescot Finance Holdings Number One Limited	Holding company
Prescot Finance Number One plc	Securitisation company
Platform Home Loans Holdings Limited*	Holding company
Platform Home Loans Number One plc*	Securitisation company
Platform Home Loans Holdings Number Two Limited*	Holding company
Platform Home Loans Number Two plc*	Securitisation company
Plum Sterling Number One plc*	Securitisation company

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

All securitisation vehicles are registered in England and operate in the UK, with the exception of Dovedale Finance Number One plc, which is registered and operates in the Republic of Ireland.

All of the above companies are related parties to the Group. See note 37 for the related party disclosures.

Joint ventures*
The Group's investment in joint ventures is £2.5m (2009: £1.8m).

The Bank owns 49% of the ordinary shares in Britannia Personal Lending Limited, a company registered in England and operating in the UK. The company trades in the business indicated:

Britannia Personal Lending Limited	Unsecured personal lending

* These subsidiary undertakings, securitisation vehicles and joint ventures were acquired following the transfer of engagements of Britannia Building Society (note 39).

36. Investments in Group undertakings continued

The Group's interest in Britannia Personal Lending Limited is as follows:

	2010	2009
Current assets	**21.7**	24.0
Long term assets	**22.6**	38.8
	44.3	62.8
Current liabilities	**27.3**	34.4
Long term liabilities	**17.0**	28.4
	44.3	62.8
Income	**2.5**	1.5
Expenses	**(1.5)**	(1.7)
Profit/(loss) before tax	**1.0**	(0.2)
Taxation	**(0.3)**	0.1
Profit/(loss) after tax	**0.7**	(0.1)

Joint ventures are accounted for using the equity method.

37. Related party transactions

Parent, subsidiary and ultimate controlling party

The Co-operative Financial Services Limited owns 100% of the issued ordinary share capital of the Bank and is the Bank's immediate holding company. The Co-operative Financial Services Limited is incorporated in England and is registered under the Industrial and Provident Societies Acts. The ultimate holding organisation is The Co-operative Group Limited (formerly known as Co-operative Group (CWS) Limited), which is incorporated in England and registered under the Industrial and Provident Societies Acts. The financial statements of the immediate and ultimate holding organisations are available from New Century House, Manchester, M60 4ES.

Further details of subsidiary undertakings and joint ventures are disclosed in note 36.

A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits. Key management (as defined by IAS 24) are considered to be Board and executive members of the Group, and Board and executive members of the Group's immediate and ultimate holding organisations. The volume of related party transactions, outstanding balances at the year end, and related income and expense for the year are as follows:

Directors, key management personnel and close family members

	Group and Bank	
	2010	2009
Loans outstanding at the beginning of the year	**3.1**	1.3
Arising on transfer of engagements	**–**	0.8
Net movement	**(0.8)**	1.0
Loans outstanding at the end of the year	**2.3**	3.1
Deposits and investments at the beginning of the year	**2.0**	2.0
Arising on transfer of engagements	**–**	0.6
Net movement	**–**	(0.6)
Deposits and investments at the end of the year	**2.0**	2.0

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37. Related party transactions continued
Directors' loans

	2010 Mortgages	2010 Credit cards
Number of directors with loan type	**8**	**11**
Total value of directors' loans	**2.2**	**–**

	2009 Mortgages	2009 Credit cards
Number of directors with loan type	6	7
Total value of directors' loans	2. 6	–

The Bank undertook the following transactions with Group companies during the year:

	Interest paid to Bank	Interest received from Bank	Staff recharges paid to Bank	Rent received from Bank	Administration recharge paid to Bank
2010					
First Roodhill Leasing Limited	**–**	**0.1**	**–**	**–**	**–**
Second Roodhill Leasing Limited	**0.2**	**–**	**–**	**–**	**–**
Third Roodhill Leasing Limited	**0.3**	**–**	**–**	**–**	**–**
Fourth Roodhill Leasing Limited	**0.1**	**–**	**–**	**–**	**–**
Co-operative Bank Financial Advisers Limited	**–**	**0.5**	**–**	**–**	**7.6**
The Covered Bond LLP	**11.9**	**12.0**	**–**	**–**	**–**
Britannia Treasury Services Limited	**0.3**	**–**	**–**	**–**	**–**
Britannia Development and Management Company Limited	**–**	**–**	**–**	**0.6**	**–**
Britannia Asset Management Limited	**–**	**0.3**	**–**	**–**	**–**
Mortgage Agency Services Number One Limited	**17.8**	**–**	**0.1**	**–**	**–**
Mortgage Agency Services Number Two Limited	**0.4**	**–**	**–**	**–**	**–**
Mortgage Agency Services Number Four Limited	**1.3**	**–**	**0.1**	**–**	**–**
Mortgage Agency Services Number Five Limited	**3.0**	**–**	**1.1**	**–**	**–**
Mortgage Agency Services Number Six Limited	**0.1**	**–**	**–**	**–**	**–**
Platform Group Holdings Limited	**44.2**	**–**	**–**	**–**	**–**
Britannia International Limited	**–**	**39.5**	**–**	**–**	**–**
Britannia Life Direct Limited	**–**	**0.7**	**–**	**–**	**–**
Illius Properties Limited	**3.5**	**–**	**1.0**	**–**	**–**
Moorland Covered Bonds LLP	**17.0**	**53.7**	**–**	**–**	**–**

37. Related party transactions continued

	Interest paid to Bank	Interest received from Bank	Staff recharges paid to Bank	Rent received from Bank	Administration recharge paid to Bank
2009					
Co-operative Commercial Limited	0.1	–	–	–	–
First Roodhill Leasing Limited	–	0.1	–	–	–
Second Roodhill Leasing Limited	0.2	–	–	–	–
Third Roodhill Leasing Limited	0.4	–	–	–	–
Fourth Roodhill Leasing Limited	0.1	–	–	–	–
Co-operative Bank Financial Advisers Limited	–	0.2	–	–	12.2
The Covered Bond LLP	20.9	21.2	–	–	–
Britannia Treasury Services Limited	0.2	–	–	–	–
Britannia Development and Management Company Limited	–	–	–	0.3	–
Britannia Asset Management Limited	–	0.1	–	–	–
Mortgage Agency Services Number One Limited	6.7	–	–	–	–
Mortgage Agency Services Number Two Limited	0.2	–	–	–	–
Mortgage Agency Services Number Four Limited	0.6	–	0.1	–	–
Mortgage Agency Services Number Five Limited	1.4	–	0.5	–	–
Platform Group Holdings Limited	23.3	–	–	–	–
Britannia International Limited	–	12.1	–	–	–
Britannia Life Direct Limited	–	0.3	–	–	–
Illius Properties Limited	0.4	–	0.4	–	–
Moorland Covered Bonds LLP	8.4	17.8	–	–	–

Interest accrues on outstanding balances at a transfer price rate agreed between the Bank and its subsidiaries.

	Interest and fees received from other Co-operative Group undertakings 2010	**Interest and fees paid to other Co-operative Group undertakings 2010**	Interest and fees received from other Co-operative Group undertakings 2009	Interest and fees paid to other Co-operative Group undertakings 2009
Parent undertakings	**5.7**	**0.5**	3.0	0.6
Fellow subsidiary undertakings	**2.1**	**–**	3.3	–
	7.8	**0.5**	6.3	0.6

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37. Related party transactions continued
At the year end the following unsecured balances were outstanding:

	Loans owed to Bank 2010	**Loans owed by Bank 2010**	Loans owed to Bank 2009	Loans owed by Bank 2009
Co-operative Commercial Limited	**1.0**	**–**	1.4	–
Roodhill Leasing Limited	**–**	**0.9**	–	0.8
First Roodhill Leasing Limited	**–**	**3.1**	–	2.1
Second Roodhill Leasing Limited	**3.5**	**–**	4.2	–
Third Roodhill Leasing Limited	**5.4**	**–**	7.2	–
Fourth Roodhill Leasing Limited	**0.7**	**–**	2.1	–
Co-operative Bank Financial Advisers Limited	**–**	**10.3**	–	7.5
The Covered Bond LLP	**1,000.0**	**1,432.6**	1,000.0	1,537.5
Unity Trust Bank plc	**–**	**78.1**	–	0.5
Britannia Treasury Services Limited	**34.4**	**–**	48.6	–
Britannia Development and Management Company Limited	**–**	**2.3**	–	1.9
Britannia Asset Management Limited	**–**	**39.9**	–	40.2
Mortgage Agency Services Number One Limited	**2,169.3**	**–**	2,345.1	–
Mortgage Agency Services Number Two Limited	**55.9**	**–**	65.1	–
Mortgage Agency Services Number Four Limited	**165.7**	**–**	184.4	–
Mortgage Agency Services Number Five Limited	**365.6**	**–**	431.1	–
Mortgage Agency Services Number Six Limited	**33.4**	**–**	18.1	–
Mortgage Agency Services Number Seven Limited	**–**	**0.3**	–	0.3
Platform Group Holdings Limited	**2,929.6**	**–**	1,899.3	–
Britannia International Limited	**–**	**1,931.3**	–	1,733.4
Britannia Life Direct Limited	**–**	**95.5**	–	89.2
Britannia New Homes Limited	**–**	**0.1**	–	0.1
Britannia Independent Limited	**–**	**0.7**	–	0.9
The Mortgage Agency plc	**–**	**0.1**	–	0.1
Verso Limited	**2.5**	**–**	–	0.2
Britannia Shield Property Services Limited	**0.2**	**–**	0.2	–
Britannia Estate Agents Limited	**0.1**	**–**	0.2	–
Western Mortgage Services Limited	**0.7**	**–**	0.2	–
Illius Properties Limited	**144.1**	**–**	120.5	–
Moorland Covered Bonds LLP	**1,422.5**	**1,827.8**	1,417.4	1,843.5
First Co-operative Finance Limited	**0.8**	**–**	0.9	–
Cleveland Guaranty Limited	**1.0**	**–**	1.0	–
Cleveland Finance Limited	**0.6**	**–**	0.6	–
Second Pioneers Leasing Limited	**0.4**	**–**	0.4	–
Phoenix Credit Services Limited	**–**	**0.1**	–	0.1

	Loans owed by other Co-operative Group undertakings 2010	**Loans owed to other Co-operative Group undertakings 2010**	Loans owed by other Co-operative Group undertakings 2009	Loans owed to other Co-operative Group undertakings 2009
Parent undertakings	**–**	**110.5**	89.5	27.2
Fellow subsidiary undertakings	**0.6**	**78.0**	1.5	302.0
	0.6	**188.5**	91.0	329.2

There are no formal repayment terms with subsidiary companies.

37. Related party transactions continued

Transactions with SPEs

The Bank undertook the following transactions with SPEs during the year:

	Interest paid to Bank 2010	**Interest received from Bank 2010**	Interest paid to Bank 2009	Interest received from Bank 2009
Leek Finance Number Fourteen plc	**–**	**–**	0.3	–
Leek Finance Number Fifteen plc	**0.4**	**–**	0.4	–
Leek Finance Number Sixteen plc	**0.7**	**–**	0.3	–
Leek Finance Number Seventeen plc	**1.3**	**–**	0.6	–
Leek Finance Number Eighteen plc	**1.2**	**–**	0.5	–
Leek Finance Number Nineteen plc	**1.1**	**–**	0.7	–
Leek Finance Number Twenty plc	**26.4**	**–**	12.4	–
Leek Finance Number Twenty One plc	**17.7**	**–**	8.4	–
Leek Finance Number Twenty Two plc	**7.4**	**–**	3.5	–
Meerbrook Finance Number One Limited	**0.6**	**–**	0.3	–
Meerbrook Finance Number Three Limited	**0.3**	**–**	0.1	–
Meerbrook Finance Number Four Limited	**6.9**	**0.5**	2.1	0.3
Meerbrook Finance Number Six Limited	**0.1**	**–**	0.1	–
Silk Road Finance Number One plc	**24.4**	**–**	–	–

	Fees paid to Bank 2010	**Fees received from Bank 2010**	Fees paid to Bank 2009	Fees received from Bank 2009
Silk Road Holdco Limited	**2.0**	**–**	–	–
Silk Road Finance Number One plc	**–**	**2.1**	–	–
Meerbrook Finance Number Five Limited	**–**	**0.1**	–	–

At the year end the following balances were outstanding with SPEs:

	Loans owed to Bank 2010	**Loans owed by Bank 2010**	Loans owed to Bank 2009	Loans owed by Bank 2009
Leek Finance Number One plc	**–**	**0.1**	–	0.1
Leek Finance Number Four plc	**–**	**–**	–	0.1
Leek Finance Number Five Limited	**–**	**0.1**	–	0.1
Leek Finance Number Six Limited	**–**	**0.1**	–	0.1
Leek Finance Number Seven plc	**–**	**0.1**	–	0.1
Leek Finance Number Ten plc	**–**	**0.1**	–	0.1
Leek Finance Number Twelve plc	**–**	**0.1**	–	0.1
Leek Finance Number Fourteen plc	**–**	**0.2**	–	0.4
Leek Finance Number Fifteen plc	**–**	**0.1**	19.0	1.4
Leek Finance Number Sixteen plc	**–**	**0.1**	14.9	2.3
Leek Finance Number Seventeen plc	**35.0**	**2.1**	41.2	1.8
Leek Finance Number Eighteen plc	**31.6**	**0.3**	38.2	2.3
Leek Finance Number Nineteen plc	**56.7**	**0.3**	73.2	2.2
Leek Finance Number Twenty plc	**1,757.1**	**2.5**	1,863.2	2.8
Leek Finance Number Twenty One plc	**1,200.0**	**2.6**	1,271.8	2.9
Leek Finance Number Twenty Two plc	**487.1**	**1.6**	514.5	1.8
Meerbrook Finance Number One Limited	**41.5**	**27.8**	41.5	29.4
Meerbrook Finance Number Two Limited	**–**	**0.1**	1.3	0.4
Meerbrook Finance Number Three Limited	**10.1**	**2.8**	10.3	3.3
Meerbrook Finance Number Four Limited	**727.1**	**109.1**	391.7	120.7
Meerbrook Finance Number Five Limited	**–**	**–**	1.7	–
Meerbrook Finance Number Six Limited	**15.8**	**4.5**	15.9	4.8
Silk Road Finance Number One plc	**1,586.4**	**2,574.4**	–	–
Dovedale Finance Number One plc	**–**	**0.4**	–	0.2

The loans owed to the SPEs comprise cash balances deposited with the Bank.

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37. Related party transactions continued
Key management compensation

	Group and Bank	
	2010	2009
Salaries and short term benefits	**5.4**	4.5
Termination benefits	**–**	1.8
	5.4	6.3

Directors' remuneration
A listing of the members of the Board of directors is shown on pages 11 and 12. The total remuneration of directors was £4.5m (2009: £5.2m).

Further details of directors' remuneration are provided in the remuneration report on pages 23 to 28.

Recharges from CFSMS
During the year, operating costs of £433.5m (2009: £342.8m) incurred on its behalf were charged at cost to the Bank by CFSMS, a fellow subsidiary of Co-operative Financial Services Limited. At 31 December 2010, the Bank owed £4.4m (2009: £3.0m) to CFSMS.

38. Share capital

	Group and Bank	
	2010	2009
Authorised capital		
At the beginning of the year 4,600,000,000 ordinary shares of 5p each	**230.0**	55.0
Issued in the year 3,600,000,000 ordinary shares of 5p each	**180.0**	175.0
At the end of the year 8,200,000,000 ordinary shares of 5p each	**410.0**	230.0
Allotted called up and fully paid		
At the beginning of the year 4,600,000,000 ordinary shares of 5p each	**230.0**	55.0
Issued in the year 3,600,000,000 ordinary shares of 5p each	**180.0**	175.0
At the end of the year 8,200,000,000 ordinary shares of 5p each	**410.0**	230.0
Share premium account at the beginning and end of the year	**8.8**	8.8

On 15 December 2010, the Bank issued 3,600,000,000 ordinary shares of 5p each at a cost of £180.0m. These were issued to its immediate parent company, Co-operative Financial Services Limited.

The shareholders have one vote for every share held.

39. Transfer of engagements of Britannia Building Society

The initial accounting for Britannia was determined provisionally in the 2009 Financial Statements. In accordance with IFRS 3, adjustments to the initial provisional accounting for Britannia disclosed in the 2009 Financial Statements have been recognised as if the final accounting had been completed at the acquisition date. The impact of these adjustments is not material to the overall level of adjustments to the carrying values of Britannia assets and liabilities that were made on merger and there is no change to the amount of goodwill arising. Comparative information for the year ended 31 December 2009 has been adjusted; there was no material impact on the reported profit for 2009.

The revised fair values of the assets and liabilities of Britannia on merger are set out below:

		Final merger fair values	Provisional merger fair values
Cash and balances at central banks		**591.8**	**591.8**
Loans and advances to banks		**956.1**	**956.1**
Loans and advances to customers	(a)	**22,912.5**	**22,885.5**
Investment securities		**6,144.2**	**6,144.2**
Derivative financial instruments		**1,086.6**	**1,086.6**
Investments in joint ventures		**2.1**	**2.1**
Intangible fixed assets		**46.0**	**46.0**
Investment properties		**123.7**	**123.7**
Property, plant and equipment		**82.6**	**82.6**
Other assets		**9.4**	**9.4**
Prepayments and accrued income		**122.2**	**122.2**
Deferred tax assets		**132.2**	**132.2**
Total assets		**32,209.4**	**32,182.4**
Deposits by banks		**(6,117.6)**	**(6,117.6)**
Customer accounts		**(18,304.7)**	**(18,304.7)**
Capital bonds		**(1,593.2)**	**(1,593.2)**
Debt securities in issue		**(3,667.3)**	**(3,667.3)**
Derivative financial instruments		**(721.1)**	**(721.1)**
Other liabilities		**(54.0)**	**(54.0)**
Accruals and deferred income		**(242.4)**	**(242.4)**
Provisions for liabilities and charges	(b)	**(33.6)**	**(14.2)**
Current tax liabilities	(c)	**(53.5)**	**(45.9)**
Subordinated liabilities		**(309.5)**	**(309.5)**
Subscribed capital		**(240.0)**	**(240.0)**
Total liabilities and reserves		**(31,336.9)**	**(31,309.9)**
Net identifiable assets		**872.5**	**872.5**
Deferred consideration		**49.6**	**49.6**
Imputed consideration		**811.2**	**811.2**
Business combination costs		**12.3**	**12.3**
Goodwill recognised on business combination		**0.6**	**0.6**

Explanation of material changes to fair value adjustments:

(a) The carrying value of loans and advances to customers has been increased following a review of the probabilities of default of assets that were neither past due nor impaired at the merger date.

(b) Based on further information that became available, the Bank has reassessed the fair value of provisions for liabilities and charges.

(c) The above adjustments to fair values increase the expected level of the Bank's tax liabilities.

Responsibility statement

For the year ended 31 December 2010

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the directors' report includes a fair review of the development and performance of the business and the position of the issuer and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

By Order of the Board
Neville Richardson, Chief Executive

29 March 2011

Notice of Annual General Meeting 2011

NOTICE IS HEREBY GIVEN that the Annual General Meeting of The Co-operative Bank plc will be held on the 24th Floor, CIS Building, Miller Street, Manchester M60 0AL at 9am on Thursday, 12 May 2011 for the following purposes:

Ordinary Business:

1. To receive the notice convening the meeting.
2. To receive the annual reports and adopt the financial statements for the year ended 31 December 2010, together with the auditor's report.
3. To approve the remuneration report for the year ended 31 December 2010.
4. To accept the following recommendations of the Board in respect of the non-cumulative irredeemable preference shares:
   (i) that the payment of the dividend of 4.625p per £1 share on 30 November 2010 be confirmed.
   (ii) that a dividend of 4.625p per £1 share be declared and paid on 31 May 2011 to the registered holders as at 3 May 2011 providing a dividend rate of 9.25 per cent per annum and making a total distribution of £5,550,000.
5. To re-elect the following directors who retire by rotation, in accordance with the provisions of Article 105 and 105A:
   (i) Leonard Adrian Wardle, non-executive director
   (ii) Martyn James Wates, non-executive director
   (iii) Stephen Watts, non-executive director
6. To:
   (i) re-appoint KPMG Audit Plc as auditor of the Company, to hold office from the conclusion of this meeting until the conclusion of the Annual General Meeting of the Company's ultimate parent, The Co-operative Group Limited, on 21 May 2011, at a remuneration to be fixed by the directors; and
   (ii) give the directors the authority to appoint as the auditor of the Company, the auditor agreed by The Co-operative Group Limited at its Annual General Meeting on 21 May 2011, at a remuneration to be fixed by the directors, until the conclusion of the next General Meeting at which accounts are laid before the Company.

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Tel: 0870 702 0003

Registrar
Computershare Investor Services PLC
P.O. Box 82
The Pavilions
Bridgwater Road
Bristol BS99 7NH

By Order of the Board
Moira Lees, Secretary

29 March 2011

A member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and vote on his/her behalf. A proxy need not also be a member. Further information on Preference Shareholders' voting rights is given below.

Members should note that to attend the meeting their shareholding must be registered on the register of the Company not later than 9am on 10 May 2011. This applies to shares held in uncertified forms in CREST and to shares held in certified form.

Notes:

1. **Director Information**
   The biographies of the directors up for re-election and re-appointment at the Annual General Meeting can be found on pages 11 and 12 of the Financial Statements.
2. **Preference Shareholders – Extract from Articles of Association 4 (B)(c)**
   Voting and General Meetings
   (i) The holders of the Preference Shares shall be entitled to receive notice of and attend (either in person or by proxy) all General Meetings of the Company. The holders of the Preference Shares shall have a right to speak and vote at a General Meeting of the Company only if and when, at the date of the notice convening such meeting, the fixed preferential dividend payable to them respectively has been in arrears for six months or more after any date fixed for payment thereof, or if a resolution is to be proposed at such meeting abrogating or varying any of the respective rights or privileges attaching to their shareholding or for the winding up of the Company or other return of capital and then on such resolution only.
   (ii) Whenever the holders of the Preference Shares are entitled to vote at a General Meeting of the Company upon any resolution proposed at such meeting, on a show of hands every holder who (being an individual) is present in person or (being a corporation) is present by a representative or by proxy shall have one vote and, on a poll, shall have one vote in respect of each Preference Share registered in the name of such holder.

Glossary
For the year ended 31 December 2010

The following glossary defines terminology used within the Bank's Financial Statements to assist the reader and to facilitate comparison with publications by other financial institutions:

Terminology	**Definition**
Arrears	Customers are said to be in arrears when they are behind in fulfilling their obligations with the result that an outstanding loan is unpaid or overdue. Corporate customers may also be considered non-performing prior to being behind in fulfilling their obligations. This can happen when a significant restructuring exercise begins.
Bank for International Settlements (BIS)	An international organisation which fosters international monetary and financial co-operation and serves as a bank for central banks. Based in Basel, Switzerland.
Basel II	A statement of best practice issued by the Basel Committee, on Banking Supervision, that defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. Basel II became law in the EU Capital Requirements Directive, and was implemented in the UK via the FSA Handbook.
Basis points (bps)	One hundredth of a per cent (0.01%), so 100 basis points is 1%. Used in quoting movements in interest rates or yields on securities.
BIPRU	The prudential sourcebook for banks, building societies and investment firms which sets out the FSA's capital requirements.
Britannia membership reward (BMR)	This was designed to reward customers for the contribution they made to the continued success of Britannia's business. After an initial qualifying period, certain customers of Britannia were able to earn points each year. Each year, the Board decided the amount to be paid out as the reward pool, and distributed this to the customers in proportion to the number of points earned.
Business risk	Business risk arises from changes to the Bank's business, specifically the risk of not being able to carry out the Bank's business plan and desired strategy.
Capital bonds	Fixed term customer accounts with returns based on the movement in an index (eg FTSE100) over the term of the bond.
Capital ratio	Total of tier one capital plus tier two capital, all divided by risk weighted assets.
Capital Requirements Directive (CRD)	The common framework for the implementation of Basel II in the EU.
Carrying value	The value of an asset or liability as it appears in the balance sheet. For each asset or liability, the value is based on either of the amortised cost or fair value principles.
Certificates of deposits (CDs)	Debt issued by banks, savings and loan associations to individual investors with terms ranging from a few months to several years. Longer term CDs tend to bear a higher interest rate. At the expiration of the term, investors may (subject to penalties) withdraw both the principal and the accrued interest.
Commercial Paper	An unsecured promissory note issued to finance short term credit needs. It specifies the face amount paid to investors on the maturity date.
Commercial real estate	Includes office buildings, industrial property, medical centres, hotels, retail stores, shopping centres, blocks of residential flats, housing buildings, warehouses and garages.
Contagion risk	An international financial market term which describes a corrupting or harmful influence, spreading effects of shocks from one counterparty to another.
Corporate segment	The segment that comprises customer focused products and services for businesses. This includes large corporate and commercial entities and small to medium entities. It includes loans, asset finance, current accounts and savings products.
Cost income ratio	Operating expenses compared to operating income.
Counterparty	In any financial contract, the person or institution entering the contract on the opposite side of the transaction is called a counterparty.
Covered bonds	Debt securities backed by a portfolio of mortgages that are segregated from the issuer's other assets solely for the benefit of the holders of the covered bonds. The Bank issues covered bonds as part of its funding activities.
Credit conversion factors	The portion of an off balance sheet commitment drawn in the event of a future default. The conversion factor is expressed as a percentage. The conversion factor is used to calculate the exposure at default (EAD).

Terminology	Definition
Credit default swap	An arrangement whereby the credit risk of an asset (the reference asset) is transferred from the buyer to the seller of protection. A credit default swap is a contract where the protection seller receives premium or interest related payments in return for contracting to make payments to the protection buyer upon a defined credit event. Credit events normally include bankruptcy, payment default on a reference asset or assets, or downgrades by a rating agency.
Credit risk	Credit risk is the current or prospective risk to earnings and capital arising from a borrower's failure to meet the terms of any contract with the Bank or its failure to perform as agreed.
Credit trading vehicle (CTV)	An investment vehicle similar to a SIV (see SIVs).
Customer deposits	Money deposited by all individuals and companies that are not credit institutions. Such funds are recorded as liabilities in the Bank's balance sheet under Customer accounts or Financial liabilities designated at fair value.
Delinquency	A customer in arrears is also said to be in a state of delinquency. When a customer is in arrears, his entire outstanding balance is said to be delinquent, meaning that delinquent balances are the total outstanding loans on which payments are overdue (see 'Arrears').
Derivative	A financial instrument that has a value, based on the expected future price movements of the instrument to which it is linked, such as a share or a currency.
Effective interest rate method (EIR)	The method used to measure the carrying value of a financial asset or a liability and to allocate associated interest income or expense over the relevant period.
Expected loss	A measure of anticipated loss for exposures captured under an internal ratings based credit risk approach. The expected loss amount is the exposure from a potential default of a counterparty or dilution over a one year period to the amount outstanding at default.
Exposure at Default (EAD)	A Basel II parameter used in internal ratings based approaches to estimate the amount outstanding at the time of default.
External audit	The independent review of the financial statements of the company, by an external firm.
External credit rating	A financial indicator of risk, assigned by credit rating agencies, to potential investors in the Bank.
Financial instruments	Any document with monetary value. Examples include cash and cash equivalents, but also securities such as bonds and stocks which have value and may be traded in exchange for money.
Financial Services Authority (FSA)	An independent non-governmental body, given statutory powers by the Financial Services and Markets Act 2000, which regulates the financial services industry in the best interests of its stakeholders. It is a company limited by guarantee and financed by the financial services industry.
Financial Services Compensation Scheme (FSCS)	The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the FSA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.
Floating Rate Notes (FRNs)	Investments with a variable interest rate. The adjustments to the interest rate are usually made every six months and are tied (or 'float') to a certain money market index.
Hedging	Hedging is a technique used by the Bank to offset risks on one instrument by purchasing a second instrument that is expected to perform in the opposite way.
Impaired loans	Loans where the Bank does not expect to collect all the contractual cash flows or expects to collect them later than they are contractually due.
Individually/collectively assessed for impairment	Impairment is measured individually for assets that are individually significant with risk, and collectively where a portfolio comprises assets with a homogenous risk and where appropriate statistical techniques are available.
Institute of International Finance (IIF)	A global association of financial institutions which provides industry guidelines on areas such as liquidity management.
Internal audit	The examination of the company's records and reports by its employees. Internal audits are usually intended to prevent fraud and to ensure compliance with board directives and management policies.
Internal Capital Adequacy Assessment Process (ICAAP)	The Bank's own assessment, as part of Basel II requirements, of the levels of capital that it needs to hold in respect of its regulatory capital requirements (for credit, market and operational risks) and for other risks including stress events.
Internal rating grade (IRG)	The grading of credit risk resulting from the internal ratings based approach (IRB).

Glossary continued
For the year ended 31 December 2010

Terminology	Definition
Investment grade	A debt security, treasury bill or similar instrument with a credit rating measured by external agencies of AAA to BBB.
IRB (Internal ratings based approach)	A Basel II approach for measuring exposure to credit risks. IRB approaches are more sophisticated and risk sensitive than the Standardised Approach and may be Foundation or Advanced. IRB approaches may only be used with FSA permission.
LIBOR (London Interbank Offer Rate)	The interest rate participating banks offer to other banks for loans on the London market.
Lifetime expected loss	The losses that the Bank expects to incur over the lifetime of portfolios of mortgage assets which were acquired on merger with Britannia Building Society. This is different from expected loss (see definition above) which is based on assets expected to default in the next 12 months.
Limited Liability Partnership (LLP)	An LLP provides each of its individual partners protection against personal liability for certain partnership liabilities.
Liquidity risk	Liquidity risk arises from the timing of cash flows generated from the Bank's assets and liabilities. It is defined as the Board approved survival period under stress scenarios. The Bank undertakes various stress tests on a weekly basis.
Loan to value (LTV)	A ratio which expresses the amount of a mortgage as a percentage of the value of the property. The Bank calculates residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index (HPI)).
Loss provisions	Provisions held against assets on the balance sheet as a result of the raising of a charge against profit for the incurred loss inherent in the lending book. The allowance represents management's best estimate of losses incurred in the loan portfolio at the balance sheet date.
Malus	A facility whereby the Remuneration Committee may reduce the amount of any deferred bonus payable in the event that any of the underpins to the incentive plans are not met or where business and/or individual performance otherwise requires.
Mandatory reserve deposits	Mandatory reserve deposits are deposited with the Bank of England and are not available for use in the Bank's day to day operations. They are non-interest bearing and are not included in cash and cash equivalents.
Medium term notes (MTN)	Flexible medium term corporate debt instruments, continuously offered by the Bank, to investors, through a dealer. Investors can choose from differing maturities, ranging from nine months to 30 years.
Member	A person who has a share investment or a mortgage loan with the Bank.
Merger	Any combination of two or more business enterprises into a single enterprise. In the Bank, this specifically refers to the merger of the Bank with Britannia Building Society on 1 August 2009. See Transfer of engagements definition below.
Mortgage backed securities	Securities that represent interests in a group of mortgages. Investors in these securities have the right to cash received from future interest and/or principal mortgage payments.
Net interest income	The difference between interest received on assets and interest paid on liabilities after taking into account the effect of derivatives.
Net present value (NPV)	The present value of the expected future cash in and out flows on an asset or liability.
Off balance sheet	An FSA term that describes the regulatory treatment of certain of the Bank's SPEs.
Operational risk	The risk of loss resulting from inadequate or failed internal processes, people and systems or external events. This encompasses the effectiveness of risk management techniques and controls to minimise these losses.
Optimum & Platform segment	This is the specialist mortgage team dealing with intermediary lending.
Over the counter (OTC)	Contracts that are traded (and privately negotiated) directly between two parties, without going through an exchange or other intermediary. They offer flexibility because, unlike standardised exchange traded products, they can be tailored to fit specific needs.
Past due	When a counterparty has failed to make a payment when contractually due.
Preference shares	Preferred shares of the Bank that have first claim to a fixed non-cumulative preferential dividend on the capital for the time being paid up. The dividends take priority over dividends to any other class of share in the capital of the Bank.
Prime	Prime mortgages are mainstream residential loans, which typically have a higher credit quality and fit standard underwriting processes. As such, they are likely to have a good credit history, and pass a standard affordability assessment at the point of origination.

Terminology	Definition
Probability of default (PD)	The likelihood that a loan will not be repaid and will fall into default. PD may be calculated for each customer who has a loan (normally applicable to wholesale customers) or for a portfolio of customers with similar attributes (normally applicable to retail customers). To calculate PD, the Bank assesses the credit quality of borrowers and other counterparties and assigns them an internal risk rating.
Renegotiated loans	A permanent change to the terms and conditions of the customer's mortgage contract.
Repo/Reverse repo	A repurchase agreement that allows a borrower to use a financial security as collateral for a cash loan at a fixed rate of interest. In a repo, the borrower agrees to sell a security to the lender subject to a commitment to repurchase the asset at a specified price on a given date. For the party selling the security (and agreeing to repurchase it in the future) it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future) it is a reverse repurchase agreement or reverse repo.
Retail	The segment that comprises customer focused products and services for individuals, sole traders and small partnerships. This includes mortgages, credit cards, consumer loans, current accounts and savings products.
Risk management committee (RMC)	This committee is responsible for review and challenge of the adequacy of capital for all risks (including operational risk), and for technical risk management activities and portfolio exposures across CFS.
Risk weighted amount	Risk weightings are established in accordance with Basel II as implemented by the FSA. Risk weighted amounts are the carrying value of the Bank's assets, adjusted by the risk weightings, to reflect the degrees of risk they represent.
Secured lending	Lending in which the borrower pledges retail or commercial property as collateral for the loan, which then becomes a secured debt owed to the Bank. In the event that the borrower defaults, the Bank may take possession of the asset used as collateral and may sell it to regain some or the entire amount originally lent to the borrower.
Securitisation	A process by which a portfolio of retail mortgages is used to back the issuance of new securities by an SPE. The Bank has established securitisation structures as part of its funding and capital management activities.
Significant items	Items which are material by both size and nature (ie outside of the normal operating activities of the Bank) are treated as significant items and disclosed separately on the face of the income statement.
Special purpose entities (SPEs)	Entities that are created to accomplish a narrow and well defined objective. For the Bank this includes: – various securitisation transactions in which mortgages were sold to SPEs. The equity of these SPEs is not owned by the Bank – Covered Bond Limited Liability Partnerships created in order to act as guarantors for issues of covered bonds.
Specialised lending	Lending in which the primary source of repayment of the obligation is the income generated by the assets being financed, rather than the independent capacity of a broader commercial enterprise.
Standard Variable Rate (SVR)	A variable and basic rate of interest charged on a mortgage. This may change in reaction to market conditions resulting in monthly repayments going up or down.
Structured investments (SIVs)	Special purpose entities which invest in diversified portfolios of interest earning assets, generally funded through issues of commercial paper, medium term notes and other senior debt to take advantage of the spread differentials between the assets in the SIV and the funding cost.
Subordinated debt/liabilities	Liabilities which, in the event of insolvency or liquidation of the Bank, are subordinated to the claims of depositors and other creditors of the Bank.
Swaps	An agreement between the Bank and a counterparty in which one stream of future interest payments is exchanged for another stream, based on a specified principal amount. For example, interest rate swaps often involve exchanging a fixed receipt for a floating receipt, which is linked to an interest rate (most often LIBOR).
the Bank	The Co-operative Bank as a stand alone entity.
the Board	The Board of Directors. They manage the Bank's business performance in line with its purpose, givens, vision and values.
The Co-operative Group	The ultimate holding company.
the Group	The Co-operative Bank consolidated with its subsidiaries.

Glossary continued
For the year ended 31 December 2010

Terminology	**Definition**
Tier one	A regulatory measure of financial (capital) strength. Tier one is divided into core tier one and other tier one capital. Core tier one capital comprises general reserves from retained profits. The book values of goodwill and intangible assets are deducted from core tier one capital and other regulatory adjustments may be made for the purposes of capital adequacy. Qualifying capital instruments such as perpetual subordinated bonds are included in other tier one capital.
Tier one ratio	Tier one capital divided by risk weighted assets.
Tier two	Tier two capital comprises the Bank's property valuation reserve, qualifying subordinated notes and collective impairment allowance (for exposures treated on a Basel II standardised basis). Certain regulatory deductions may be made for the purposes of assessing capital adequacy.
Transfer of engagements	On 1 August 2009, Britannia Building Society merged with The Co-operative Bank plc by a transfer of engagements between the building society and the bank under the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007. See Merger definition above.
Treasury	The treasury department's responsibilities usually include capital management, risk management, strategic planning and investor relations.
Unsecured lending	Lending for which there is no collateral for the loan.
Value at risk (VaR)	An estimate of the potential loss which might arise from market movements under normal market conditions, if the current positions were to be held unchanged for one business day, measured to a defined confidence level. The Bank uses a confidence level of 95%.
Wholesale segment	The segment that carries out asset and liability management across the Bank's balance sheet including trading activities.
Write down	After an advance has been identified as impaired and is subject to an impairment allowance, the stage may be reached whereby it is concluded that there is no realistic prospect of further recovery. Write downs will occur when, and to the extent that, the whole or part of a debt is considered irrecoverable.

Notes

Notes

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