

Cardnet Merchant Services Limited

Directors' report and financial statements For the year ended 31 December 2012

Registered office

25 Gresham Street
London
EC2V 7HN

Registered number

735844

Directors

S D Bonham
A R England
R C Neagle
M C Regnier

Company secretary

S N Slattery



Directors' report

For the year ended 31 December 2012

The directors present their report and the audited financial statements of Cardnet Merchant Services Limited ("the Company") for the year ended 31 December 2012

Business review

Principal activities

The Company is a limited company incorporated and domiciled in England and Wales (registered number 735844)

The Company is a joint venture between Lloyds TSB Bank plc, FDR Limited and Lloyds Bank Subsidiaries Limited and its principal activity during the year was the provision of services to merchants enabling the acceptance, authorisation and clearing of plastic card transactions

The Company's results for the year show a Profit before tax of £54,979,000 (2011 £53,841,000) and Net interest income of £10,611,000 (2011 £8,710,000). The directors aim to continue the development of the business by recruiting new merchants and leveraging Lloyds Banking Group plc corporate relationships with the existing customer base

Future outlook

The environment within which the Company operates remains competitive. The Company has written a satisfactory level of new business in the year and this is expected to continue in the foreseeable future. The directors are supporting a strategy designed to ensure that the Company's interest and other charges fully reflect the risks associated with its core products whilst maintaining competitiveness.

Principal risks and uncertainties

The directors consider that the principal areas of risk are counterparty credit risk, but there is also exposure to liquidity risk, interest rate risk, foreign exchange risk, geographical and sector concentrations of risk and business risk. The Company has counterparty credit risk management processes in place which are designed to prevent specific individual merchant loss.

The Company's financial risk management objectives and policies are given in notes 2 and 18 to the financial statements.

Key performance indicators ("KPIs")

The Company's two main KPIs are the number of transactions processed in comparison with the prior year and the aggregate value of those transactions processed in comparison with the prior year. This is monitored separately between the Sterling and Multicurrency platforms.

Sterling platform

During the year ended 31 December 2012 the Company processed 13.4% (2011 18.7%) more transactions by value and 13.7% (2011 26.1%) more transactions by volume than during the year ended 31 December 2011 on the Sterling platform.

Multicurrency platform

During the year ended 31 December 2012 the Company processed 17.5% (2011 23.8%) more transactions by value and 12.2% (2011 20.0%) more transactions by volume than during the year ended 31 December 2011 on the Multicurrency platform.

Policy and practice on payment of suppliers

The Company follows "The Prompt Payment Code" published by the Department for Business Innovation and Skills (BIS) regarding the making of payments to suppliers. Information about the "Prompt Payment Code" may be obtained by visiting www.promptpaymentcode.org.uk.

The Company's policy is to agree terms of payment with suppliers and these normally provide for settlement within 30 days after the date of the invoice, except where other arrangements have been negotiated.

It is the policy of the Company to abide by the agreed terms of payment, provided the supplier performs according to the terms of the contract.

In relation to amounts owed to trade creditors as at 31 December 2012, the number of days required to be shown in this report, to comply with the provisions of the Companies Act 2006, is 5 days (2011 5 days).

Dividends

A dividend of £40,838,000, representing a dividend of £31,389 per share was declared and paid during the year (2011 £37,210,000) to A and B shareholders.

Directors' report (continued)

For the year ended 31 December 2012

Going concern

The directors are satisfied that the Company has adequate resources to continue in business for the foreseeable future and consequently the going concern basis continues to be appropriate in preparing the financial statements

Directors

The names of the current directors are shown on the cover

The following changes have taken place during the year or since the year end

N R Leacock	(resigned 2 February 2012)
M C Regnier	(appointed 2 February 2012)
R M Dallas	(resigned 2 May 2012)
A R England	(appointed 2 May 2012)
S L Warner	(resigned 24 July 2012)
R C Neagle	(appointed 24 July 2012)

Statement of directors' responsibilities

The directors are responsible for preparing the Directors' report and the financial statements in accordance with applicable law and regulations

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Company will continue in business

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

Disclosure of information to auditors

Each director in office at the date of this report confirms that

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

This confirmation is given, and should be interpreted, in accordance with the provisions of section 418 of the Companies Act 2006

Independent auditors

PricewaterhouseCoopers LLP are deemed to be re-appointed as auditors under section 487(2) of the Companies Act 2006

On behalf of the board


M C Regnier
Director

19 June 2013

Independent auditors' report to the members of Cardnet Merchant Services Limited

We have audited the financial statements of Cardnet Merchant Services Limited for the year ended 31 December 2012 which comprise the Statement of comprehensive income, the Balance sheet, the Statement of changes in equity, the Cash flow statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the European Union.

Respective responsibilities of directors and auditors

As explained more fully in the Statement of directors' responsibilities set out on page 2, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Directors' report and financial statements to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2012 and of its profit and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

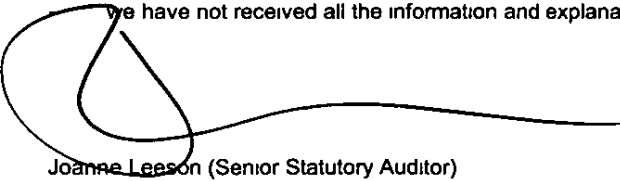
In our opinion the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

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

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

we have not received all the information and explanations we require for our audit



Joanne Leeson (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
31 Great George Street
Bristol
BS1 5QD

19 June 2013

Statement of comprehensive income

For the year ended 31 December 2012

	Note	2012 £'000	2011 £'000
Interest income		13,942	14,566
Interest expense		(3,331)	(5,856)
Net interest income	4	10,611	8,710
Fees and commission income		249,002	232,215
Fees and commission expense		(186,481)	(171,575)
Net fees and commission income	5	62,521	60,640
Other operating expenses	6	(18,153)	(15,509)
Profit before tax		54,979	53,841
Taxation	9	(13,488)	(14,265)
Profit for the year attributable to equity shareholders, being total comprehensive income		41,491	39,576

The notes on pages 8 to 19 are an integral part of these financial statements

Balance sheet

As at 31 December 2012

	Note	2012 £'000	2011 £'000
ASSETS			
Cash and cash equivalents		52,999	38,773
Other current assets	10	460,032	396,390
Property, plant and equipment	11	-	1
Deferred tax asset	12	18	150
<hr/>			
Total assets		513,049	435,314
<hr/>			
LIABILITIES			
Other current liabilities	13	454,861	391,453
Provision for liabilities and charges	14	3,848	3,530
Current tax liability		27,734	14,378
<hr/>			
Total liabilities		486,443	409,361
<hr/>			
EQUITY			
Share capital	15	3	3
Retained profits		26,603	25,950
<hr/>			
Total equity		26,606	25,953
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Total equity and liabilities		513,049	435,314

The notes on pages 8 to 19 are an integral part of these financial statements

The financial statements on pages 4 to 19 were approved by the board of directors and were signed on its behalf by


M C Regnier
Director

19 June 2013

Statement of changes in equity

For the year ended 31 December 2012

	Share capital £'000	Retained profits £'000	Total £'000
At 1 January 2011	3	23,584	23,587
Profit for the year being total comprehensive income	-	39,576	39,576
Dividend paid to equity shareholders of the Company	-	(37,210)	(37,210)
At 31 December 2011	3	25,950	25,953
Profit for the year being total comprehensive income	-	41,491	41,491
Dividend paid to equity shareholders of the Company	-	(40,838)	(40,838)
At 31 December 2012	3	26,603	26,606

The notes on pages 8 to 19 are an integral part of these financial statements

Cash flow statement

For the year ended 31 December 2012

	2012 £'000	2011 £'000
Cash flows generated from operating activities		
Profit before tax	54,979	53,841
Adjustments for		
- Interest income	(13,942)	(14,566)
- Interest expense	3,331	5,856
- Depreciation	1	-
- Increase/(decrease) in Provision for liabilities and charges	318	(178)
- Net increase in Other current assets	(63,642)	(80,534)
- Net increase in Other current liabilities	63,408	80,047
Cash generated from operations	44,453	44,466
Interest received	13,942	14,566
Interest paid	(3,331)	(5,856)
Taxes paid	-	(13,835)
Net cash generated from operating activities	55,064	39,341
Cash flows used in financing activities		
Dividends paid	(40,838)	(37,210)
Net cash used in financing activities	(40,838)	(37,210)
Net increase in Cash and cash equivalents	14,226	2,131
Cash and cash equivalents at beginning of year	38,773	36,642
Cash and cash equivalents at end of year	52,999	38,773
Cash and cash equivalents comprise		
Cash at bank	52,999	38,773
Cash and cash equivalents	52,999	38,773

The notes on pages 8 to 19 are an integral part of these financial statements

Notes to the financial statements

For the year ended 31 December 2012

1 Accounting policies

1.1 Basis of preparation

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to both years presented, unless otherwise stated.

These financial statements have been prepared in accordance with applicable IFRSs as adopted by the European Union and the Companies Act 2006 applicable to companies reporting under IFRSs. IFRSs comprise accounting standards prefixed IFRS issued by the International Accounting Standards Board ("IASB") and those prefixed IAS issued by the IASB's predecessor body as well as interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") and its predecessor body.

There are no new IFRS pronouncements relevant to the Company requiring adoption in these financial statements.

Details of those pronouncements which will be relevant to the Company but which were not effective at 31 December 2012 and which have not been applied in preparing these financial statements are given in note 22.

The financial statements have been prepared on a going concern basis as detailed in the Directors' report and under the historical cost convention.

1.2 Income and expenses recognition

Interest income and expense

Interest income and expenses are recognised in the Statement of comprehensive income for all interest bearing financial instruments, using the effective interest rate method. The effective interest rate method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense to a period of account. The effective interest rate is the rate that discounts the estimated future cash payments or receipts over the expected life of the instrument to the net carrying amount of the financial asset or financial liability.

Fees and commission income and expense

Fees and commissions are recognised on an accruals basis when the service has been provided. These services comprise initialisation and ongoing fees for services delivered to merchants. Revenue is recognised net of chargebacks and commission clawbacks.

Expenses directly attributable to merchant acquiring business are recognised through Fees and commission expense. All other expenses are recognised through Other operating expenses.

Valuation on foreign currency

The financial statements are presented in Sterling which is the Company's functional and presentation currency. Foreign currency transactions are translated into Sterling at the exchange rate prevailing at the date of the transaction.

Exchange gains and losses arising from the translation of monetary assets and liabilities at the exchange rate prevailing at the balance sheet date are recognised in the Statement of comprehensive income.

1.3 Financial assets and liabilities

Financial assets consist of Amounts owed by related undertakings, Amounts owed by card schemes, Amounts owed by merchants, Other trade receivables and Cash and cash equivalents. Financial liabilities consist of Amounts owed to merchants, Amounts owed to card schemes, Other creditors and Amounts owed to related undertakings. Financial assets and liabilities are recognised when the Company becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are derecognised when the rights to receive cash flows, or obligations to pay cash flows, have expired.

Interest bearing financial assets and liabilities are recognised and measured at amortised cost inclusive of transaction costs, using the effective interest rate method.

1.4 Property, plant and equipment

Property, plant and equipment is included at historical purchase cost less depreciation and any impairment allowance. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Depreciation is calculated using the straight line method to allocate the difference between the cost and expected residual value over their estimated useful lives. The useful life of all items of Property, plant and equipment is 3 to 8 years.

Notes to the financial statements (continued)

For the year ended 31 December 2012

1 Accounting policies (continued)

1.4 Property, plant and equipment (continued)

Future rates of depreciation are reassessed each year in light of changes to anticipated residual values, and are amended as required

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In the event that an asset's carrying amount is determined to be greater than its recoverable amount it is written down immediately.

1.5 Dividends

Dividends on ordinary shares are recognised through equity in the period in which they are paid.

1.6 Cash and cash equivalents

For the purposes of the Balance sheet and Cash flow statement, Cash and cash equivalents comprises balances with less than three months' maturity.

1.7 Taxation, including deferred income taxes

Current tax which is payable or receivable on taxable profits or losses is recognised as an expense or credit in the period in which the profits or losses arise.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates that have been enacted or substantively enacted by the balance sheet date that are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised. The tax effect of losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

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

1.8 Trade and other receivables

Trade and other receivables are measured at amortised cost, less provision for impairment.

1.9 Trade and other payables

Trade and other payables are measured at amortised cost.

1.10 Provision for liabilities and charges

Provisions are recognised in respect of present obligations arising from past events where it is probable that outflows of resources will be required to settle the obligations and they can be reliably estimated.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably.

2. Risk management policy

The Company's operations expose it to credit risk, liquidity risk, interest rate risk, foreign exchange risk, geographical and sector concentrations of risk and business risk, it is not exposed to any significant market risk.

The directors are responsible for establishing a framework for evaluating, measuring, monitoring and controlling risk. They are responsible for ensuring that the risks within the business are identified, assessed, monitored and controlled. These controls and procedures where relevant comply with Lloyds Banking Group policies and standards. All risk policies are reviewed and authorised by the Company's board of directors, which comprises directors appointed by Lloyds TSB Bank plc and FDR Limited.

Notes to the financial statements (continued)

For the year ended 31 December 2012

2. Risk management policies (continued)

2.1 Credit risk

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. Credit risk arises from extending credit in all forms, where there is a possibility that a counterparty may default. The Company is committed to a strong credit culture that recognises the need to ensure that risk assets are of high quality.

Credit risk mitigation

- The Company maintains and adheres to a credit policy document in compliance with policies established by the Group Risk Management Department within the Lloyds Banking Group.
- Credit principles and policy. Lloyds Banking Group Risk sets out the credit principles and policy according to which credit risk is managed, which in turn is the basis for the Company's credit policy. Principles and policy are reviewed regularly and any changes are subject to a review and approval process. Principles and policy includes lending guidelines, which define the responsibilities of lending officers and provide a disciplined and focused benchmark for credit decisions.
- Credit scoring. Every new merchant is subject to a detailed credit check which includes a review of financial information (for example, audited financial statements, management accounts, projections and business plans), a credit reference agency search, review of terms and conditions, associated websites and site visit reports (as necessary). Full Know Your Customer and Know Your Business checks are undertaken in line with the Company's anti-money laundering policies.
- The prime risk for the Company arises from the chargeback rules of the card schemes in which the Company operates, and if the financial strength of the merchant is weak, risk mitigation is considered. This includes taking guarantees (including from Lloyds TSB Bank plc), cash security and deferral of funds to the merchant. The Company also takes into account the availability of bonding by obtaining security through travel agents under ATOL/ABTA and insurance cover.
- The Company adopts a prudent approach to the identification, definition, and control of impaired debts, including chargebacks. An impairment provision is made where there is clear evidence that any merchant has financial difficulties, or debts are overdue, which may impact its ability to repay any amounts owing to the Company including future chargebacks.
- Stress testing and scenario analysis. The credit portfolio is also subjected to stress testing and scenario analysis, to simulate outcomes and calculate their associated impact.

2.2 Liquidity risk

Liquidity risk is the risk that the Company is unable to meet its obligations as they fall due. This is not considered to be a significant risk to the Company as collection from the scheme is completed before payment to the merchant. This is further supported by the Company being primarily funded by the shareholders (Lloyds TSB Bank plc and FDR Limited).

2.3 Interest rate risk

Interest rate risk is the risk of financial loss as a result of adverse movements in interest rates, and arises largely because of timing differences between the re-pricing of financial assets and liabilities.

Exposure to interest rate risk within the Company's activities is managed within the policies laid down by the Group Balance Sheet Management Department of Lloyds Banking Group. The Company's policy operates within guidelines set by the board of directors.

2.4 Foreign exchange risk

Foreign exchange risk is the risk of financial loss arising from fluctuations in foreign currency exchange rates. The foreign exchange risk that the Company faces arises from running multi-currency operations.

2.5 Geographical and sector concentrations of risk

The Company operates primarily within the UK. There is an exposure to particular sectors arising where there is a long period of time elapsing between payment and the provision of goods/services. The resulting risk is closely monitored and controlled with agreed parameters set by the Company's credit policy.

Notes to the financial statements (continued)

For the year ended 31 December 2012

2. Risk management policies (continued)

2.6 Business risk

Business risk is the risk that the Company's earnings are adversely impacted by a suboptimal business strategy or the suboptimal implementation of the strategy. In assessing business risk, consideration is given to internal and external factors such as products, funding, resource capability and economic, political and regulatory factors.

Through regular reports and oversight business risk is managed by corrective actions to plans and reductions in exposures where necessary.

3 Critical accounting estimates and judgements in applying accounting policies

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although those estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

Estimates, judgements and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. The most critical estimate and judgement made by the Company is in respect of Provision for liabilities and charges.

Provision for chargebacks and fraud

This provision relates to the risk that the Company may be liable for the chargebacks of transactions on merchants who are potentially unable to meet the chargeback demands themselves. The provision is against merchant and customer fraud which is inherent due to the nature of the business. The amount held is based on the value of related transactions and the likelihood of chargebacks.

Terminal commission clawback

This provision is for refunding commissions earned, where the contractual relationship with a merchant subsequently terminates. The provisioning rate is based on recent historical performance of refunds.

4. Net interest income

	2012 £'000	2011 £'000
Interest income	13,942	14,566
Interest expense	(3,331)	(5,856)
Net interest income	10,611	8,710
Representing		
Lloyds TSB Bank plc (see note 17)	10,603	8,705
Third parties	8	5
	10,611	8,710

5. Net fees and commission income

	2012 £'000	2011 £'000
Fees and commission income		
Service charges	227,518	214,383
Commission receivable	21,484	17,832
Total Fees and commission income	249,002	232,215
Fees and commission expense		
Other fees and commission payable	(186,481)	(171,575)
Net fees and commission income	62,521	60,640

Notes to the financial statements (continued)

For the year ended 31 December 2012

5. Net fees and commission income (continued)

Included within Other fees and commission payable is £12,218,000 (2011 £12,113,000) payable to the related undertaking, FDR Limited

6 Other operating expenses

	2012 £'000	2011 £'000
Recharges relating to salary and other related costs (see note 17)	11,714	10,454
Depreciation (see note 11)	1	-
Marketing	522	543
Change in provisions, operational losses and fraud (see note 3)	1,530	2,477
Communications	94	129
Charges payable to Lloyds TSB Bank plc (see note 17)	1,044	873
Other operating expenses	3,248	1,033
	18,153	15,509

Charges payable to Lloyds TSB Bank plc are comprised of expenses incurred by the Lloyds TSB Bank plc on behalf of the Company which are recharged to the Company. Fees payable to the Company's auditors for the audit of the financial statements of £29,000 (2011 £36,000) are included within Other operating expenses

7. Staff costs

The Company did not employ any persons during the year (2011 none). Staff who manage the affairs of the Company are employed by the shareholders, Lloyds TSB Bank plc and FDR Limited, who recharge the cost of these employees to the Company

8. Directors' emoluments

The amounts paid to the directors in respect of services to the Company were £1,000 (2011 £156,000). The amounts paid to the directors in respect of compromise agreements were £150,000 (2011 £nil). These relate to payments made to one director only and are comprised of both cash and defined benefit pension scheme contribution payments. One director accrued pensions under a defined benefit scheme operated by Lloyds TSB Bank plc (2011 1). One director received shares under long term incentive plans during the year (2011 1). None of the directors exercised share options (2011 none).

Full disclosure in respect of pensions in accordance with IAS 19 "Employee Benefits" and shares received under long term incentive plans can be found in the financial statements of Lloyds TSB Bank plc, one of the Company's shareholders

9. Taxation

	2012 £'000	2011 £'000
a) Analysis of charge for the year		
UK corporation tax		
- Current tax on taxable profit for the year	13,468	14,378
- Adjustments in respect of prior years	(112)	(9)
Current tax charge	13,356	14,369
UK deferred tax		
- Origination and reversal of timing differences	9	(113)
- Adjustments in respect of prior years	121	9
- Impact of deferred tax rate change	2	-
Deferred tax charge/(credit) (see note 12)	132	(104)
	13,488	14,265

Corporation tax is calculated at a rate of 24.5% (2011 26.5%) of the taxable profit for the year

Notes to the financial statements (continued)

For the year ended 31 December 2012

9 Taxation (continued)

b) Factors affecting the tax charge for the year

The tax on the Company's Profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the Company as follows

	2012 £'000	2011 £'000
Profit before tax	54,979	53,841
Tax charge thereon at UK corporation tax rate of 24.5% (2011: 26.5%)	13,470	14,268
Factors affecting charge		
- Non-allowable and non-taxable items	7	3
- Adjustments in respect of prior years	9	-
- Effect of reduction in tax rate	2	(6)
Tax on profit on ordinary activities	13,488	14,265
Effective rate	24.5%	26.5%

10. Other current assets

	2012 £'000	2011 £'000
Amounts owed by related undertakings (see note 17)	280,393	186,959
Amounts owed by card schemes	148,829	179,659
Amounts owed by merchants	10,089	8,648
Other trade receivables	1,464	1,925
Accrued income	19,257	19,199
	460,032	396,390

Amounts owed by related undertakings are interest bearing and the average rate of net interest earned during the year was 3.19% (2011: 3.99%). The fair value of Other current assets is equal to its carrying value. No provisions have been recognised in respect of these amounts.

11 Property, plant and equipment

	2012 £'000	2011 £'000
Cost		
At 1 January and 31 December	217	217
Accumulated depreciation		
At 1 January	216	216
Charge for the year	1	-
At 31 December	217	216
Balance sheet amount at 31 December	-	1

Notes to the financial statements (continued)

For the year ended 31 December 2012

12 Deferred tax asset

The movement in the Deferred tax asset is as follows

	2012 £'000	2011 £'000
Brought forward	150	46
(Charge)/credit for the year (see note 9)	(132)	104
	18	150

The deferred tax (charge)/credit in the Statement of comprehensive income comprises the following temporary differences

	2012 £'000	2011 £'000
Accelerated capital allowances	(8)	7
Other temporary differences	(124)	97
	(132)	104

	2012 £'000	2011 £'000
Deferred tax asset comprises		
Accelerated capital allowances	18	26
Other temporary differences	-	124
	18	150

On 21 March 2012, the Government announced a reduction in the rate of corporation tax to 24% with effect from 1 April 2012. This reduction was enacted under the Provisional Collection of Taxes Act 1968 on 26 March 2012. In addition, the Finance Act 2012, which passed into law on 3 July 2012, included legislation to reduce the main rate of corporation tax from 24% to 23% with effect from 1 April 2013. The change in the main rate of corporation tax from 25% to 23% has resulted in a reduction in the Company's Deferred tax asset at 31 December 2012 of £2,000 comprising a £2,000 charge included in the Statement of comprehensive income.

On 5 December 2012, the Government announced a further reduction in the main rate of corporation tax to 21% from 1 April 2014. In addition, on 20 March 2013 the Government announced a further reduction in the main rate of corporation tax to 20% from 1 April 2015. The effect of this further change upon the Company's deferred tax balances cannot be quantified at this stage.

13. Other current liabilities

	2012 £'000	2011 £'000
Amounts owed to merchants	448,814	385,446
Amounts owed to card schemes	2	105
Other creditors and accruals	2,717	3,376
Amounts owed to related undertakings (see note 17)	3,328	2,526
	454,861	391,453

Amounts owed to related undertakings are non interest bearing. The fair value of Other current liabilities owed is equal to their carrying value.

Notes to the financial statements (continued)

For the year ended 31 December 2012

14. Provision for liabilities and charges

	2012 £'000	2011 £'000
At 1 January	3,530	3,708
Provisions made during the year	1,796	3,631
Amounts utilised during the year	(1,478)	(3,809)
At 31 December	3,848	3,530
Provision for chargebacks and fraud	1,673	1,634
Terminal commission clawback	2,175	1,896
	3,848	3,530

Information on the nature of provisions is disclosed in note 3

15 Share capital

	2012 £'000	2011 £'000
Allotted, issued and fully paid		
650 'A' ordinary shares of £1 each	1	1
651 'B' ordinary shares of £1 each	1	1
1,300 deferred shares of £1 each	1	1
	3	3

At 31 December 2012, the authorised share capital of the Company was £2,601, divided into 650 'A' shares of £1 each, 651 'B' ordinary shares of £1 each and 1,300 deferred shares of £1 each

The ordinary shareholders (the holders of the 'A' ordinary shares and the 'B' ordinary shares) have priority over the deferred shareholders (the holders of the deferred shares) to receive dividends distributed up to the 'deferred share threshold' as defined in the Company's articles of association. Dividends above the threshold are to be distributed as follows: 99% amongst the ordinary shareholders and 1% amongst the deferred shareholders. On winding up, the deferred shareholders have priority over the ordinary shareholders to receive repayment of capital. The ordinary shareholders have equal voting rights and the deferred shareholders have no voting rights.

FDR Limited holds 650 'A' ordinary shares. Lloyds TSB Bank plc holds 637 'B' ordinary shares. Lloyds Bank Subsidiaries Limited holds 14 'B' ordinary shares. Lloyds Banking Group plc holds 1,300 deferred shares.

The terms of the contractual agreement between the shareholders is such that the Company is accounted for as a joint venture under the requirement of IAS 31 Interests in Joint Ventures and therefore does not have an ultimate parent undertaking.

16 Ordinary dividends

	2012 £'000	2012 £ per share	2011 £'000	2011 £ per share
Amounts paid in respect of preceding years				
Second interim dividend	25,941	19,939	23,575	18,121
Amounts paid in respect of current years				
First interim dividend	14,897	11,450	13,635	10,480
	40,838	31,389	37,210	28,601

Notes to the financial statements (continued)

For the year ended 31 December 2012

17. Related party transactions

A number of transactions are entered into with related parties in the normal course of business. These include fee transactions. A summary of the outstanding balances at the year end and the related income and expense for the year are set out below.

	2012 £'000	2011 £'000
Amounts owed by related undertakings		
Lloyds TSB Bank plc (see note 10)	280,393	186,959
Amounts owed to related undertakings		
FDR Limited (see note 13)	3,328	2,526
Cash and cash equivalents held with related undertakings		
Lloyds TSB Bank plc	35,289	24,445
Interest income		
Lloyds TSB Bank plc	13,934	14,561
Interest expense		
Lloyds TSB Bank plc	(3,331)	(5,856)
Net interest income (see note 4)	10,603	8,705
Fees and commission expense		
FDR Limited (see note 5)	12,218	12,113
Recharges relating to salary and other related costs		
Lloyds TSB Bank plc (see note 6)	11,714	10,454
Amounts charged by related undertakings		
Lloyds TSB Bank plc (see note 6)	1,044	873

The above balances are unsecured in nature and are expected to be settled in cash or by cash equivalents. Transactions in the year are those reflected through the Statement of comprehensive income.

For certain merchants, the risk of irrecoverable chargebacks is underwritten by Lloyds TSB Bank plc. The credit risk underwritten by Lloyds TSB Bank plc amounted to £92,882,000 (2011: £79,278,000).

Deposits with Lloyds TSB Bank plc are placed on normal commercial terms.

Key management personnel

Key management personnel are those persons having authority and responsibility for planning and controlling the activities of the Company. Key management personnel are employed by Lloyds TSB Bank plc or FDR Limited and consider that their services to the Company are incidental to their other activities within those organisations.

Directors' emoluments information is disclosed in note 8. There were no transactions between the Company and key management personnel during the current or preceding year.

UK Government

In January 2009, the UK Government through HM Treasury became a related party of Lloyds Banking Group plc, the ultimate parent company of Lloyds TSB Bank plc and Lloyds Bank Subsidiaries Limited, following its subscription for ordinary shares issued under a placing and open offer. As at 31 December 2012, HM Treasury held a 39.2 per cent (2011: 40.2 per cent) interest in Lloyds Banking Group plc's ordinary share capital and consequently HM Treasury remained a related party of the Company during the year ended 31 December 2012.

Notes to the financial statements (continued)

For the year ended 31 December 2012

18 Financial risk management

A description of the nature and mitigation of key risks facing the Company is provided in note 2. A description of the Company's financial assets/liabilities and associated accounting is provided in note 1.

18.1 Credit risk

The maximum credit exposure of the Company in the event of other parties failing to perform their obligations is detailed below:

	2012 £'000	2011 £'000
Cash and cash equivalents	52,999	38,773
Amounts owed by related undertakings	280,393	186,959
Trade and other receivables	160,382	190,232
Maximum credit risk exposure	493,774	415,964

An analysis of the credit quality of the Company's Trade and other receivables is presented below. The assessment of the risk level of trade and other receivables which are neither past due nor impaired is derived from information presented to the Company's management.

Trade and other receivables which are neither past due nor impaired

	2012 £'000	2011 £'000
High quality	150,715	181,922
Good quality	7,248	5,864
Satisfactory quality	-	-
Lower quality	-	-
Below standard, but not impaired	-	-
Total	157,963	187,786

High quality lending comprises those balances with a low probability to default rating assigned. Receivables of high quality are those amounts owed by card schemes, merchants and other receivables generated in the normal course of business. In general, good quality lending comprises those balances with a lower probability to default rating assigned and the rating progressively increases for each category exhibiting a progressively higher probability to default. Receivables of good quality are those under investigation by the Company.

Trade and other receivables which are past due but not impaired

	2012 £'000	2011 £'000
Past due up to 30 days	965	1,163
Past due from 30-60 days	1,221	420
Past due from 60-90 days	217	410
Past due from 90-180 days	601	1,205
Total	3,004	3,198

Past due is defined as failure to make a payment when it falls due.

Impaired trade and other receivables

	2012 £'000	2011 £'000
Impaired trade and other receivables assessed on an individual basis	272	216
Total	272	216

Notes to the financial statements (continued)

For the year ended 31 December 2012

18. Financial risk management (continued)

18.1 Credit risk (continued)

Total trade and other receivables gross of impairment allowances	161,239	191,200
Allowance for impairment losses	(857)	(968)
Total Trade and other receivables	160,382	190,232

18.2 Liquidity risk

The Company is entirely funded by the shareholders, Lloyds TSB Bank plc and FDR Limited. The table below sets out the undiscounted cash flows payable by the Company in respect of financial liabilities, according to contractual maturity into relevant maturity groupings based on the remaining period at the balance sheet date.

As at 31 December 2012

	Up to 1 month £	1-3 months £	3-12 months £	1-5 years £	Total £
Amounts owed to merchants	448,814	-	-	-	448,814
Amounts owed to card schemes	2	-	-	-	2
Other creditors and accruals	1,838	879	-	-	2,717
Amounts owed to related parties	1,892	1,436	-	-	3,328
Financial liabilities	452,546	2,315	-	-	454,861

As at 31 December 2011

	Up to 1 month £	1-3 months £	3-12 months £	1-5 years £	Total £
Amounts owed to merchants	381,910	2,704	479	353	385,446
Amounts owed to card schemes	103	2	-	-	105
Other creditors and accruals	3,171	195	9	1	3,376
Amounts owed to related parties	1,796	1,724	(994)	-	2,526
Financial liabilities	386,980	4,625	(506)	354	391,453

The Company has sufficient funding to meet liquidity needs as there is a current funding arrangement with Lloyds TSB Bank plc.

18.3 Interest rate risk

The Company is not subject to any significant interest rate risk.

18.4 Foreign currency risk

Generally the risk is minimised because the liability to merchants is funded from receipts from payment schemes in the same currency. In addition to this, the short term settlement period limits the exposure to liquidity risk to a few days.

19. Capital disclosures

The Company's objectives when managing capital are to safeguard the entity's ability to continue as a going concern, provide an adequate return to its shareholders through pricing products and services commensurately with the level of risk and, indirectly, to support the Group's regulatory capital requirements.

The Company's parent manages the Company's capital structure and advises the board of directors to consider making adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the board of directors may adjust the amount of dividends to be paid to shareholders, return capital to shareholders, issue new shares, or sell assets.

The Company's capital comprises all components of equity, movements in which appear in the Statement of changes in equity. The Company receives its funding requirements from its related undertakings and does not raise funding externally.

Notes to the financial statements (continued)

For the year ended 31 December 2012

20. Contingent liabilities and capital commitments

There were no contingent liabilities or contracted capital commitments at the balance sheet date (2011 £nil)

21. Post balance sheet events

There are no post balance sheet events requiring disclosure in these financial statements

22. Future developments

The following pronouncements will be relevant to the Company but were not effective at 31 December 2012 and have not been applied in preparing these financial statements

Pronouncement	Nature of change	Effective date
Improvements to IFRSs (issued May 2012)	Sets out minor amendments to IFRS standards as part of the annual improvements process. Most amendments clarified existing practice.	Annual periods beginning on or after 1 January 2013
Amendment to IFRS 7, 'Financial instruments: Disclosures' on Offsetting financial assets and financial liabilities	Amends the required disclosures to include information that will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with the entity's recognised financial assets and recognised financial liabilities, on the entity's financial position.	Annual periods beginning on or after 1 January 2013
IFRS 13 Fair value Measurement	Sets out a single IFRS framework for the measurement of fair value and the related disclosure requirements.	Annual periods beginning on or after 1 January 2013
Amendment to IAS 32 Financial instruments: Presentation on Offsetting financial assets and financial liabilities	Provides additional clarification regarding the concept of the 'legally enforceable right of set-off' for the purposes of offsetting financial assets and financial liabilities.	Annual periods beginning on or after 1 January 2014
IFRS 9 Financial Instruments Classification and Measurement ^{1 & 2}	Replaces those parts of IAS 39 Financial Instruments Recognition and Measurement relating to the classification, measurement and derecognition of financial assets and liabilities. Requires financial assets to be classified into two measurement categories, fair value and amortised cost, on the basis of the objectives of the entity's business model for managing its financial assets and the contractual cash flow characteristics of the instrument. The available-for-sale financial asset and held-to-maturity categories in the existing IAS 39 will be eliminated. The requirements for financial liabilities and derecognition are broadly unchanged from IAS 39.	Annual periods beginning on or after 1 January 2015

¹ At the date of this report, this pronouncement is awaiting EU endorsement.

² IFRS 9 is the initial stage of the project to replace IAS 39. Future stages are expected to result in amendments to IFRS 9 to deal with changes to the impairment of financial assets measured at amortised cost and hedge accounting. Until all stages of the replacement project are complete, it is not possible to determine the overall impact on the financial statements of the replacement of IAS 39.

The full impact of these pronouncements is being assessed by the Company. However, the initial view is that none of these pronouncements are expected to cause any material adjustments to the reported numbers in the financial statements.