

CARDNET MERCHANT SERVICES LIMITED

ANNUAL REPORT AND ACCOUNTS 2002



CARDNET MERCHANT SERVICES LIMITED
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Registered number: 735844

Registered office:

25 Gresham Street
London
EC2V 7HN

Directors:

D.R. Gagie (Chairman)
G.E.R. Hawkins
P.J.Martin
R.Schimenz

Company Secretary:

S.N. O'Connor

Member of Lloyds TSB Group

CARDNET MERCHANT SERVICES LIMITED

REPORT OF THE DIRECTORS

Principal activities

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

Results and dividends

The profit after taxation for the year ended 31 December 2002 amounted to £21,641,000 (2001: £23,285,000) as set out in the profit and loss account on page 4. An interim dividend of £10,403,000 was paid on 1st October 2002 (2001: £9,855,000) to the A & B shareholders. The directors recommend the payment of a further dividend of £11,238,000 (2001: £13,430,000) to the A & B shareholders.

Directors

The names of the directors of the company are shown on page 1.

The following changes in directors have taken place during the year:

	Appointment	Resignation
P.G.E. Aycliffe		29 April 2002
D. R. Gagie	29 April 2002	

Reference is made on page 8 in note 8 to the directors' interests in the capital of Lloyds TSB Group plc, the ultimate parent company, and its subsidiaries.

Policy and practice on payment of creditors

The company follows "The Better Payment Practice Code" published by the Department of Trade and Industry, regarding payments to suppliers. A copy of the code and information about it may be obtained from the Department of Trade and Industry, No. 1 Victoria Street, London, SW1H 0ET.

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.

The number of days to be shown on this report, to comply with the provisions of the Companies Act 1985, is 28 (2001: 31). This bears the same proportion to the number of days in the year as the aggregate of the amounts owed to trade creditors at 31 December 2002 bears to the aggregate of the amounts invoiced by suppliers during the year.

On behalf of the board



Peter Martin

Director

4 September
----- 2003

CARDNET MERCHANT SERVICES LIMITED

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

We have audited the financial statements which comprise the profit and loss account, the balance sheet, the cashflow statement and the related notes, which have been prepared under the historical cost convention and the accounting policies set out in Note 1.

Respective responsibilities of directors and auditors

The directors are responsible for preparing the annual report including, as described below, the financial statements. The United Kingdom Companies Act 1985 requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company as at the end of the year and of the profit or loss for that year. In preparing those financial statements the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed 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 accounting records which disclose with reasonable accuracy at any time the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985. 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.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or in to whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions is not disclosed.

We read the other information contained in the annual report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. The other information comprises only the directors' report.

Basis of audit opinion

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

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

Opinion

In our opinion the financial statements give a true and fair view of the state of the Company's affairs at 31 December 2002 and of its profit and cash flows for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

PricewaterhouseCoopers

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
Southampton

4 September 2003

CARDNET MERCHANT SERVICES LIMITED

PROFIT AND LOSS ACCOUNT

FOR THE YEAR ENDED 31 DECEMBER 2002

	Notes	2002 £'000	2001 £'000
Turnover	1	39,590	43,918
Administrative expenses		(11,018)	(13,676)
Operating profit		<u>28,572</u>	<u>30,242</u>
Interest receivable	3	2,343	3,023
Profit on ordinary activities before taxation	4	<u>30,915</u>	<u>33,265</u>
Taxation on profit on ordinary activities	7	(9,274)	(9,980)
Profit on ordinary activities after taxation		<u>21,641</u>	<u>23,285</u>
Dividends – paid		(10,403)	(9,855)
- proposed		(11,238)	(13,430)
Retained profits/(losses) transferred to profit and loss reserves		<u>-</u>	<u>-</u>

The company had no recognised gains or losses other than those disclosed in the profit and loss account, and therefore no separate statement of total recognised gains and losses has been presented.

All income and expenditure arose from continuing activities.

The company has no movement in shareholders' funds other than those included in the profit and loss account, and therefore no separate reconciliation of movement in shareholders' funds has been presented.

There are no differences between the profit on ordinary activities before taxation and the retained profit for the year stated above and their historical cost equivalents.

The notes on pages 7 to 11 form part of these accounts.

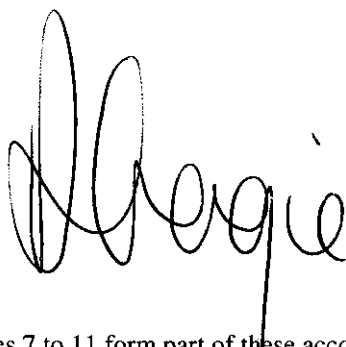
CARDNET MERCHANT SERVICES LIMITED

BALANCE SHEET

AS AT 31 DECEMBER 2002

	Notes	2002 £'000	2001 £'000
Fixed assets	9	57	77
Current assets			
Debtors	10	94,857	107,991
Cash at bank and in hand		203	2
		95,060	107,993
Creditors: amounts falling due within one year	11	(93,535)	(104,140)
Net current assets		1,525	3,853
Creditors: amounts falling due after more than one year	12	(201)	-
Provisions for liabilities and charges	13	(1,378)	(3,927)
Total Assets		3	3
Capital and reserves			
Called up share capital	14	3	3
Profit and loss account		-	-
Total shareholders' funds		3	3
Analysis of shareholders' funds			
Equity	14	2	2
Non-equity		1	1
		3	3

D.R. Gagie
Chairman



The notes on pages 7 to 11 form part of these accounts.

CARDNET MERCHANT SERVICES LIMITED

CASHFLOW STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2002

	2002 £'000	2001 £'000
Net cash inflow from operating activities	32,352	27,105
Dividend paid	(23,833)	(20,768)
Tax paid	(10,634)	(9,321)
Purchase of tangible fixed asset	(27)	(38)
Returns on investment and servicing of finance		
Interest received	2,343	3,023
Increase in cash	<u>201</u>	<u>1</u>

Reconciliation of operating profit to net cash inflow from operating activities

	2002 £'000	2001 £'000
Operating profit	28,572	30,242
Decrease/(Increase) in debtors	13,134	53,845
(Decrease)/Increase in creditors and provisions	(9,401)	(57,024)
Depreciation on fixed assets	47	42
Net cash inflow from continuing operating activities	<u>32,352</u>	<u>27,105</u>

Refer to Note 16 on page 11 for an explanation of the reconciliation of net cash flow to movement in net funds for the year ended 31 December 2002 and analysis of changes in net funds.

CARDNET MERCHANT SERVICES LIMITED

Notes to the accounts

1 Accounting Policies

The accounts are prepared in accordance with applicable accounting standards and under the historical cost convention using the following accounting policies. Certain prior period balance sheet amounts have been reclassified to conform with current year presentation.

a) Turnover

Turnover comprises merchant service charges and other fees receivable from merchants net of deductions for interchange payable to card issuers and costs of processing and settlement services.

b) Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes. No material timing differences existed in the current or prior years.

c) Provisions for bad and doubtful debts

Provisions for chargebacks are established when specific losses are identified with respect to merchants where recovery is at risk.

d) Other provisions and liabilities

Provisions in respect of obligations of the company are made in line with prudent estimates of the likely outcome.

e) Interest receivable

Interest income is recognised in the profit and loss accounts as it accrues.

f) Fixed assets

Equipment is depreciated by equal instalments over the estimated useful lives of the assets, which are 3-8 years.

g) Foreign Currency Translation

Assets, Liabilities and results in foreign currencies are expressed in sterling at the rates of exchange ruling on the date of the balance sheet. All exchange profits or losses, which arise from normal trading activities, are included in the profit and loss account.

2 Segmental analysis

In the opinion of the directors, the company has one class of business, the provision of services to merchants enabling the acceptance, authorisation and clearing of plastic card transactions. In addition, during the year it had no significant activities outside the United Kingdom. Accordingly, no segmental analysis by class of business or geographical location is provided.

3 Interest receivable

	2002 £'000	2001 £'000
Interest receivable from Lloyds TSB Bank plc	2,343	3,023

4 Profit on ordinary activities before taxation

	2002 £'000	2001 £'000
Profit on ordinary activities before taxation is stated after charging:		
Auditors remuneration – audit services	17	20
Depreciation	47	42

CARDNET MERCHANT SERVICES LIMITED

Notes to the accounts (continued)

5 Directors' emoluments

The aggregate of the emoluments of the directors directly attributable to services provided to Cardnet Merchant Services Limited was £133,055 (2001: £125,140). These comprise amounts paid by the parent undertaking to the directors for their services to this company, which relate to the management of the affairs of this company.

Retirement benefits are accruing to one director under a defined benefit pension scheme (2001: one).

These costs are recharged to the company and included within expenses recharged by Lloyds TSB Bank plc in Note 15 to the accounts.

One director exercised share options in the parent company during the year (2001: three).

6 Employee information

The company has no employees (2001: Nil). All activities of the company are carried out by the joint venture partners Lloyds TSB Bank plc and FDR Limited for which the company is recharged.

7 Taxation on profit on ordinary activities

	2002 £'000	2001 £'000
UK corporation tax on profit for the year	9,274	9,980

The charge for tax on the profit for the year is based on the average UK corporation tax rate of 30 per cent (2001: 30 per cent).

8 Directors' interests

The interests of the directors of the company at the end of the year in the capital of Lloyds TSB Group plc were:

Shares	At 31 December 2002	At 1 st January (or later date of appointment)
D.R. Gagie	1,079	1,079
G.E.R. Hawkins	119,845	124,790
P.J.Martin	21,080	18,516
R. Schimenz	-	-

Options to acquire shares	At 1 st January 2002 (or later Date of appointment)	During the year or since appointment date		At 31 December 2002
		Granted	Exercised	
D.R. Gagie	17,872	-	-	17,872
G.E.R. Hawkins	42,297	-	-	42,297
P.J.Martin	26,620	3,843	8,497	21,966
R. Schimenz	-	-	-	-

None of the directors had any other interest in the capital of Lloyds TSB Group plc or its subsidiaries.

CARDNET MERCHANT SERVICES LIMITED

Notes to the accounts (Continued)

9 Fixed assets

	Equipment £'000
Cost:	
At 1 January 2002	154
Additions	27
Disposals	-
At 31 December 2002	<u>181</u>
Depreciation:	
At 1 January 2002	77
Charge for the year	47
Disposals	-
At 31 December 2002	<u>124</u>
Balance Sheet amount at 31 December 2002	<u>57</u>
Balance Sheet amount at 31 December 2001	<u>77</u>

10 Debtors

	2002 £'000	2001 £'000
Accrued Income	11,829	10,533
Amount owed by Card Schemes	14,624	2,324
Amount owed by Lloyds TSB Bank plc	68,404	95,134
	<u>94,857</u>	<u>107,991</u>

Amounts owed by group undertakings are unsecured and have no fixed date of repayment.

11 Creditors: amounts falling due within one year

	2002 £'000	2001 £'000
Taxation	4,792	6,152
Accruals and other creditors	4,719	2,534
Proposed dividend	11,238	13,430
Liability to merchants	72,786	82,024
	<u>93,535</u>	<u>104,140</u>

CARDNET MERCHANT SERVICES LIMITED

Notes to the accounts (continued)

12 Creditors: amounts falling due after more than one year

	2002 £'000	2001 £'000
Deposits from merchants	201	-

13 Provisions for liabilities and charges

The movement in provisions is as follows:	2002 £'000	2001 £'000
Balance brought forward 1 January	3,927	556
Amounts written off	(3,743)	(627)
Additional provisions made	1,194	3,998
Balance carried forward 31 December	1,378	3,927

Under the rules of the card schemes that govern the card industry, card issuers can seek reimbursement from the company for any amounts they have refunded to cardholders for goods and services paid for but not received. In turn, the company normally recovers from the merchants the value of these chargebacks. Provisions for chargebacks are based on an appraisal of specific merchants where this recovery is at risk. Charges for the year are included within administrative expenses.

14 Called up share capital and non-equity shareholder funds

	2002 £'000	2001 £'000
Authorised issued and fully paid		
650 "A" ordinary shares of £1 each	650	650
651 "B" ordinary shares of £1 each	651	651
1,300 deferred shares of £1 each	1,300	1,300
	2,601	2,601

The ordinary shareholders (the holders of the 'A' ordinary shares and/or 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 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.

15 Related party disclosures

Financial Reporting Standard 8 required disclosure of material transactions with related parties. As shareholders, Lloyds TSB Bank plc and FDR Limited are related parties to the company.

Lloyds TSB Bank plc	2002 £'000	2001 £'000
- expenses recharged by Lloyds TSB Bank plc	8,710	8,976
- interest receivable from Lloyds TSB Bank plc	2,343	3,023
- amounts owed by Lloyds TSB Bank plc	68,404	95,134
- cash held with Lloyds TSB Bank plc	203	2

CARDNET MERCHANT SERVICES LIMITED

Notes to the accounts (continued)

Related party disclosures (continued)

Net income collected by Lloyds TSB Bank plc on behalf of the company amounted to £38.5m (2001: 40.0m). Turnover includes £1m (2001: £3.87m) from Lloyds TSB Bank plc relating to an adjustment for fees received and receivable for those cash disbursements to cardholders at counters of branches of Lloyds TSB Bank plc which are acquired by the company.

Certain management costs of the company are paid by Lloyds TSB Bank plc and recharged.

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 £9.75m at 31 December 2002 (2001: £15.2m).

	2002 £'000	2001 £'000
FDR Limited		
- expenses recharged by FDR Limited	1,267	1,064
- amounts owed to FDR Limited (included in Accruals and other creditors)	2,674	1,856
- fees charged by FDR Limited	7,843	5,471

Fees charged by FDR Limited include contractual credits received of £3.53m (2001: £7.15m).

For certain merchants, the risk of irrecoverable chargebacks is underwritten by FDR Limited. Underwriting fees paid to FDR Limited during the year ended 31 December 2002 amount to £1.1m (2001: £0.36m).

16 Cash flows

		2002 £'000	
a) Reconciliation of net cash flow to movement in net funds			
Net funds at 1 January		2	
Increase in cash in the year and change in net funds		201	
Net funds at 31 December		<u>203</u>	
	At 1 January 2002 £'000	Cashflows during 2002 £'000	At 31 December 2002 £'000
b) Analysis of changes in net funds			
Cash in hand and at bank	2	201	203

17 Ultimate parent company

The company regarded by the directors as the ultimate parent company is Lloyds TSB Group plc, which is also the parent undertaking of the largest group of undertakings for which group accounts are drawn up and of which the company is a member. Lloyds TSB Bank plc is the parent undertaking of the smallest such group of undertakings. Copies of the accounts of both companies may be obtained from the company secretary's office, Lloyds TSB Group plc, 25 Gresham Street, London EC2V 7HN.

18 Date of approval

The directors approved the accounts on 4 SEPTEMBER 2003.