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The **co-operative** bank
good with money

financial statements 2007

co-operation
innovation
transformation

07

Changing our business
for the better

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

82
5-9-08

Contents:

inform,
involve,
inspire.

Vision, values, performance

growing, pionee

Our business

purpose

To be a growing, pioneering financial services business delivering benefits to customers, members and communities through commitment to value, fairness and social responsibility

Our CFS

vision

To be the UK's most admired financial services business

Our values

As a Co-operative business, we believe in:

social responsibility

We are committed to leading the way on ethical, environmental and community issues

openness and honesty

We work hard to earn credibility and trust from our customers and each other

being successful

We work together to make sure that CFS is admired, profitable and sustainable

being customer focused

We always aim to satisfy our customers and exceed their expectations where we can

making work fun

We are proud of CFS and know we can contribute to making it a great place to work

A **first class performance** across products and services has been rewarded by a range of awards and accolades for these achievements.

and achievements:

ring, achieving.

Performance

Improved profit before investment write downs, tax and significant items of £82 2m compared to £76 3m in 2006

Profit before tax was £11 1m (2006 £184 3m)

Average customer deposits grew by £0 7bn (9%) to £8 3bn and average customer lending balances grew by £0 3m (3%) to £8 0bn reflecting growth in Corporate balances

Achievements

- **smile** won 'Best of the Best' for current account products in the Which? Awards
- **smile** won one of the UK's Top 100 'Cool Brands' for 2006/07
- Best Direct Mortgage Lender 2006/2007 in 'Your Money Awards'
- **smile** won the 2007 PETA Europe Proggy Award
- Best Online Banking Provider in 'Your Money Awards'
- Best Student Account in 'Your Money Awards'
- Best 100% Mortgage Provider – 'Moneyfacts Awards'
- Named 'most impressive bank' in the Times Consumer poll
- Investment of £250m into the business to support growth in areas such as Retail and Corporate Banking
- Outsourcing partnerships in place to boost Information Services and our print and mail functions
- 15th Anniversary of our famous banking ethical policy
- Our work on green energy was recognised by British Renewable Energy Awards
- Delivery of our People Programme to create a high performance culture to underpin investment plans
- Launch of innovative **think** credit card aimed and ethical consumers
- Increased support for Microfinance initiatives through a special $50m fund, supporting businesses in some of the world's poorest countries
- Four new Corporate Banking Centres opened as part of our programme to double representation by mid-2009
- Continued improvement in customer satisfaction with a December 2007 score of 79 4% – the 11th monthly improvement since January 2007

Chair's statement:

The Co-operative Bank has been through a challenging period in 2007 However, we have not only risen to the challenge but demonstrated real progress The Bank reported a profit of £82 2m before write downs in 2007 compared to £76 3m in 2006 Although profitability was affected by a credit crunch experienced across the whole of the banking industry, we also saw the beginning of positive returns from significant investment in changes to the way we operate

The growth of The Co-operative Retail and Corporate Banking is being fertilized by an agreed investment of £250m by the CFS Board Plans include development of vital new technology and systems while doubling the number of Corporate Banking Centres This investment goes hand in hand with essential cost savings and our Operational Effectiveness Programme launched in January delivered £30m of savings by the end of the year through 62 initiatives across the wider CFS business

In last year's Financial Statements I mentioned the introduction of our new 'common identity' with The Co-operative Group's business In 2007 we have begun to use our new 'good with money' brand to bring banking even closer to the insurance and investment arms of CFS, reinforcing the bond to bring us increased recognition and further commercial success ATMs and Bank branches are being rebranded as part of a phased roll out due to be completed by the close of 2008

In 2007 we opened four new Corporate Banking Centres in Bristol, Oxford, Derby and Preston as part of our programme to double the representation by mid-2009 A further five new centres will open in 2008, taking the number of Corporate Banking Centres to 19 from a start point of ten in late 2006

Our productivity levels have continued to improve, as we seek to maximise our operational effectiveness by making the most of our **natural resources.**

One of our major achievements for the year was reaching the 15th anniversary of the launch of our famous ethical policy We believe that our ethical positioning is a positive driver for business with a total corporate loan book that has grown by 250% since 1992 and research showing that many customers join purely for ethical reasons The Bank's ethical policy clearly states who we will or will not do business with and in the last 15 years we have declined loans totalling more than £700m for ethical and ecological reasons

One of the key features of the Bank as a co-operative organisation is a commitment to return a share of profits to our members The strategy sets us apart from other plc competition in the marketplace and offers significant opportunities to the customer in terms of maximising value and increasing customer participation In 2007 the membership scheme has boosted our ability to develop loyal and extended relations with a single customer base We plan to take further advantage of The Co-operative Group membership base in 2008 to cross sell our banking products

As you will see from the awards listed on the previous pages of this report, the Bank continues to lead in its marketplace, winning 'best of the best' in the Which? Awards for current account products, being named 'most impressive bank' in The Times consumer poll and winning 'Best Online Banking Provider', 'Best Direct Mortgage Lender' and 'Best Student Account' in the Your Money Awards

The overall story for 2007 is one of a difficult economic backdrop for the Bank but also a journey of successful investment and change, setting us on the right path to reap the rewards in 2008

I would like to take this opportunity to thank Craig Shannon, Executive Director of Business Management, who left the Board in August 2007 and Independent Professional Board Director, Tony Lancaster, who has retired to be replaced by Bob Newton, who brings with him valuable experience and expertise I would also like to record my thanks to Martin Beaumont who retired in July as Group Chief Executive, Deputy Chair of the Bank Board and CFS Board Member The Group made tremendous progress under Martin's leadership – including closer working between the Group and the Bank Finally, we welcome Martyn Wates, who joined the CFS Board in November reflecting his role as Chief Financial Officer for The Co-operative Group

Graham Bennett
Chair

Chief Executive's overview: **adaptable, achievable, commendable.**

While The Co-operative Bank has faced both internal and external challenges in 2007, we have measured up well in terms of overall performance and continued to make satisfactory progress against our five key goals profit generation to create a sustainable business, market leading customer satisfaction, market leading colleague satisfaction, market leading social responsibility approach and membership growth

The Bank's well-balanced approach to growth has maintained the strength of our balance sheet in the current environment Our funding is overwhelmingly from retail and corporate deposits, rather than from the financial markets and our reliance on wholesale funding is lower than most other banks The quality of our mortgage book remains high and we have continued to reduce our exposure to unsecured assets Our capital position remains substantially higher than regulatory requirements laid down by the Financial Services Authority (FSA)

Before tax and write downs, the Bank recorded an improved profit of £82 2m in 2007, compared to £76 3m in 2006 However, profitability was impacted by £31 8m worth of write downs as a result of the banking industry's 'credit crunch', leading to an operating profit of £50 4m in 2007 compared with £76 3m in 2006 In turn we have seen bad debt levels reduced by £3 3m and we performed well in areas such as average loan values and current accounts and we exceeded our targets and produced a record performance in sales of our new mortgage two year tracker product

The Co-operative Bank has played a key role in CFS's journey of change and investment in 2007 Our commitment to strip out £100m of expenditure in the business by June 2008 meant facing the challenge head on and taking tough decisions to put us in a better place to succeed One of the toughest decisions we made was to lose 1,000 CFS roles under a major change programme, 'Transformation 07', reducing duplication and improving the structure of the organisation to improve efficiency and effectiveness The programme was a difficult time for many CFS colleagues but people in customer-facing roles, including advisers within Bank branches, have

Against a background of different challenges, our creative approach to dealing with change has lead to **resourceful solutions**, from simple, yet sound, business principles.

been unaffected by these changes and indeed numbers of customer facing roles have increased The transformation process realigned structures and systems in the wider organisation, properly integrating the Bank into CFS and making us more robust and ready for the journey to the top

Cost savings were a much needed part of the bigger picture and were linked to a £250m investment agreed by the Board in July this year to grow our business As well as developing and implementing vital new technology and processes, part of the growth plan for Retail and Corporate Banking includes doubling the number of Corporate Banking Centres, taking the number of Centres to 19 by the end of 2008

One of our key new products at the Bank in 2007 was our innovative **think** credit card, the first in the world aimed at ethical shoppers The card offers conscience consumers better rates of interest when making ethical purchases from an approved list of partner providers and at the same time the Bank helps save the rainforest by purchasing half an acre in the customer's name

This year we celebrated 15 years of our Bank's ethical policy and we are still proud to be a market-leader among socially responsible organisations As part of our commitment to the environment and to communities, we launched a £400m fund to support projects in the renewable energy sector and a $50m investment fund aimed specifically at further developing our presence in the growing Microfinance sector, providing finance to small enterprises in the developing world Colleagues at the Bank as part of CFS, together with colleagues at The Co-operative Group showed the co-operative spirit by raising over £2m for our Charity of the Year, The Children's Society, in 2007 The Bank also provides funding for NHS Local Investment Trusts, working on projects in the community to bring the latest in integrated health care to local people The introduction of two new Local Authorities customers took our market share to approximately 33% of the Local Authorities in England and Wales

The Bank is still maintaining a better rate of customer satisfaction than key competitors in our peer group and our customer satisfaction rate continued to improve month on month, reaching an impressive 79 4% by December

We have successfully introduced the Office of Fair Trading's new 'customer promise' which gives customers more clarity about the cheque clearing process and allows them to benefit from a more efficient service We are constantly looking at ways to improve our customer experience – investing in new, more efficient ways of corresponding and handling queries with our customers is an important part of this

Another key measure of our success is colleague satisfaction and much of the efforts of our Human Resources Division in 2007 have been focussed on our People Programme Central to the success of our overall change programme is the need to develop a high performing culture – put simply, having the right people in the right place within the business, doing the right things in the right way Our People Programme concentrated on six key areas leadership, management capability, performance development, recognition, people communication and measurement

The 'university for all' was established in October to bring together a structure for a new Centre of Excellence and Learning and Development for colleagues Through 2008, the university's curriculum will develop further as we raise the capability of colleagues and look for a greater return on our training investment

The Bank has collected a string of awards and accolades in 2007, recognising us as an excellent ethical and customer focused business Awards include the 'Best mortgage Lender 2006/2007', 'Best Online Banking provider' and 'Best Student Account' awarded by Your Money **smile** was awarded 'Best of the Best' by Which? for its current account and was named one of the UK's top 100 'Cool Brands' for 2006/07

Last year was characterised by new ways of thinking and change has been properly embraced at the Bank This commitment to investment and development, combined with our fundamental purpose of value, fairness and social responsibility puts us in a very good position to make positive headway in 2008

David Anderson
Chief Executive

Business and financial review:

Financial highlights

Results summary	**2007 £m**	**2006 £m**	**Change £m**	**Change %**
Net interest income	**334 8**	320 3	14 5	4 5
Non-interest income	**188 7**	201 2	(12 5)	(6 2)
Operating costs	**(339 3)**	(339 9)	0 6	(0 2)
Impairment losses	**(102.0)**	(105 3)	3 3	3 1
Operating profit before tax, significant items and investment write downs	**82.2**	76 3	5 9	7 7
Structured investment write downs	**(31.8)**	-	(31 8)	
Operating profit before tax and significant items	**50.4**	**76.3**	**(25 9)**	**(33 9)**
Profit based payments to members of the Co-operative Group	**(1 3)**	**(1 2)**	(0 1)	(8 3)
Profit before tax and significant items	**49 1**	75 1	**(26.0)**	(34 6)
Significant items	**(38.0)**	109 2	(147 2)	(134 8)
Profit before tax	**11.1**	184 3	**(173 2)**	(94 0)

The banking business recorded a reduced operating profit before tax and significant items of £50 4m compared to £76 3m in 2006 due largely to £31 8m of structured investment write downs Profit before Structured Investment write downs improved by £5 9m (7 7%) and reflects higher net interest income, lower costs and bad debts offset by lower non-interest income Balance sheet growth was achieved in both lending and deposit balances, particularly in the corporate sector

Net interest income growth of £14 5m arose principally from balance sheet growth as net interest margins were stable Non-interest income declined by £12 5m primarily due to industry-wide pressures on Payment Protection Insurance (PPI) and bank overdraft fee refunds as a result of publicity generated by the OFT market study

The Bank has maintained tight cost control in the period which has resulted in business-as-usual operating costs reducing by £0 6m

The impairment charge in the retail sector has seen a reduction from the levels reported last year as a direct result of a programme of focused activities particularly in the unsecured retail portfolios The Corporate impairment charge tends to be more volatile due to the nature and timing of one-off charges Overall the impairment charge is 3 1% lower than 2006

Results summary	2007 £m	2006 £m	Change £m	Change %
Operating profit before tax and significant items is analysed by segment				
• Retail	**47.1**	34 2	12 9	37 7
• Corporate	**57 5**	55 1	2 4	4 4
• Wholesale	**(43.1)**	3 9	(47 0)	(1,205 1)
• Central costs	**(11.1)**	(16 9)	5 8	34 3
Operating profit before significant items	**50 4**	76 3	(25 9)	(33 9)
Cost/Income ratio before significant items	**64 8%**	65 2%		(0 4)

In 2007, retail sector profitability has improved by £12 9m despite lower non-interest income as interest income increased, bad debts were reduced and costs were lowered

Corporate sector operating contribution increased by £2 4m due to significantly higher interest from balance sheet growth being offset by a specific bad debt

Wholesale sector operating contribution declined by £47 0m Wholesale margins have been impacted by the increased pressure in the interest rate environment, further compounded by the effects of the credit crisis The Structured Investment book has suffered from the volatility in the credit market, resulting in investment write downs of £31 8m The Bank exposure to these type of higher risk investments is now limited to £31m of Structured Investments which together with £50m of Credit Trading Fund Investments comprises a small part of the Bank's Wholesale portfolio, the rest of which is prime quality

2007 started the year with interest rates in the UK at 5%, a strong and growing economy with annual GDP running at an above trend 2 9% and double digit house price inflation Money market rates predicted interest rates to rise above 6 25% by the end of the 2007 Inflationary concerns and strong consumer data led to the MPC raising rates throughout the first half of the year to 5 75% in July

The second half of the year was dominated by the US sub-prime housing market problems and subsequent credit issues in the wholesale markets causing a run on a major UK bank Expectations changed to a recession in the US, and a severe slowdown in economic growth in the UK and Europe Liquidity problems continued in the cash markets with LIBOR reaching 110 basis points over base rate and the Bank of England cutting rates in December

Economic commentators now believe that the UK economy will grow below trend, with a deteriorating housing market, consumer weakness and interest rates falling to below 4 5%

For our customers who shop with their conscience, our new **think** card **actively reflects** and rewards their choices.

Balance sheet

Average customer deposits grew by £0 7bn (9%) to £8 3bn and average customer lending balances grew by £0 3m (3%) to £8 0bn reflecting growth in Corporate balances

The Bank has maintained a strong balance sheet with consistent robust liquidity and capital ratios The Basel I risk asset ratio was 13 5% with a Tier 1 ratio of 8 8%, substantially higher than the regulatory requirements laid down under Basel I by the Financial Services Authority (FSA) The Basel 2 solvency ratio was 143 0% The Bank has a very strong retail deposit base with customer deposits higher than customer lending such that its reliance on wholesale funding is lower than most other banks

Lending

Retail sector average customer lending balances fell by £239m (5%) compared to the previous year as the Bank has continued its strategy to reduce its exposure to new-to-Bank unsecured loan and credit card customers, where aggressive acquisition pricing and bad debts continue to constrain value There remains a focus on relationship customers such as those with Privilege packaged accounts with efforts also placed on cross sales to strengthen the relationship

The Bank's customer and marketing strategies are driven by a focus on customers who share our belief in the co-operative difference, developing strong loyal relationships based on the total CFS product range, recruiting and retaining relationship customers and a customer promise that sets our commitment

November 1 saw the launch of our new **think** credit card The **think** card offers consumers who shop with their conscience a lower rate of interest for designated ethical purchases and a package of other benefits, while at the same time also helping to save the rainforest, enabling customers to choose to do the right thing

The Bank and **smile** have seen continued recognition for the quality of service provided to our customers, including the 'Best Direct Mortgage Lender 2006/2007', 'Best Online Banking Provider' and 'Best Student Account' awarded by Your Money and 'Highly Commended Direct Mortgage Lender 2007/2008' by Your Mortgage Magazine

The Bank came out on top in the 'Best 100% Mortgage Provider' category at the Moneyfacts awards Moneyfacts also highly commended the Bank in the category for 'Best Credit Card Provider – Standard Rate' for its Clear credit card

Average Corporate lending balances increased by £509m (21%) The promising growth in Corporate lending balances included increased support for our expanding customer base as well as selected involvement in the syndicated lending sector and participation in PFI transactions We are also planning to increase significantly our lending commitment to the renewable energy sector where we will be focusing both on large scale project finance transactions and also smaller community based schemes The Bank also remains recognised as one of the UK market leaders in provision of finance for NHS Local Investment Trusts

The Bank is also increasing its support for Microfinance initiatives through a special $50m fund This money will be used to support the development of small businesses in some of the world's poorest countries

Deposits

Average customer deposits grew by £685m (9%) reflecting growth across both the Retail and Corporate sectors Average Retail sector balances of £5,756m are £477m (9%) higher than last year, with particularly strong growth in the Smartsaver and the Privilege Premier products

smile has also been awarded 'Best of the Best' by Which? for its current account products and also continues to be recognised as a desirable brand as it was named one of the UK's Top 100 'Cool Brands' for 2006/07

Corporate sector deposits increased by £208m (9%) We have opened four new Corporate Banking Centres (Bristol, Oxford, Derby and Preston) as part of our programme to double our representation by mid-2009

Our strategies are driven by a focus on customers who share our belief in the Co-operative difference, **developing strong, loyal relationships**.

The Bank has continued its improvement in customer satisfaction with a December 2007 score of 79 4% – the eleventh monthly improvement since January 2007 In a recent survey on BBC's Watchdog programme, we were rated number one on the high street for customer satisfaction

Partnerships

The Bank's links with the wider Co-operative Movement have continued as the Bank manages and operates ATMs located in retail stores The total number of ATMs in the Bank's network is approximately 2,300, all of which are free to use for LINK card holders

A number of new partnerships have been launched allowing us to sell products to the customers of third party companies These include the sale of mortgages through Places for People

Operating income

Operating income at £523 5m was £2 0m higher than 2006 reflecting a £14 5m increase in net interest income and a decrease of £12 5m in non-interest income Higher interest income from balance sheet growth was offset by lower wholesale income

Average balances and interest margins	2007 £m	2006 £m	Change £m
Net interest income	**334 8**	320 3	14 5
Average balances			
Interest-earning assets	**12,193**	11,827	366
Interest-bearing liabilities	**10,319**	10,072	247
Interest-free liabilities	**1,874**	1,755	119
Average rates	**%**	%	%
Gross yield on interest-earning assets	**6.5**	6 0	0 5
Cost of interest-earning liabilities	**4 5**	3 8	0 7
Interest spread	**2.0**	2 2	(0 2)
Contribution of interest-free liabilities	**0.7**	0 5	0 2
Net interest margin	**2.7**	2 7	–

Net interest income from the Bank's Retail and Corporate sectors increased, reflecting higher customer balances and stable overall net interest margin Growth was particularly strong in Corporate lending and deposits reflecting our expansion in this area and retail deposits from market leading products such as Smartsaver

Non-interest income	2007 £m	2006 £m	Change £m
Fees and commission receivable	**187 6**	193 6	(6 0)
Insurance commission income	**29.2**	38 8	(9 6)
Fees and commission payable	**(33 3)**	(33 8)	0 5
Other income, including dealing profit/losses	**5.2**	2 6	2 6
Total	**188.7**	201 2	**(12 5)**

Net interest income from wholesale activities was lower than last year mainly driven by higher funding costs

Non-interest income at £188 7m was £12 5m lower than the same period last year This was principally driven by reduced insurance commission generated from Payment Protection Insurance and bank overdraft fee refunds as a result of publicity generated by the OFT market study

Commission and fees receivable decreased by £6 0m (3%) due to bank overdraft fee refunds and reduced credit card default charges Increased income from LINK transaction fees from the Bank's ATM network is offset by increased costs of the ATM network, which are shown within operating costs

Other income, including dealing profits/losses improved by £2 6m despite difficult market and trading conditions, including further improved foreign exchange performance

Operating costs

Operating costs analysis – before significant items	**2007 £m**	**2006 £m**	**Change £m**
Staff costs	**145 3**	142 3	3 0
Other administrative expenses	**171.3**	173 2	(1 9)
Depreciation and amortisation	**22.7**	24 4	(1 7)
Total operating costs	**339.3**	339 9	(0 6)
Cost/income ratio before significant items	**64.8%**	65 2%	(0 4)%

The Bank has maintained tight cost control in the period which has resulted in business-as-usual operating costs reducing by £0 6m (2%)

Staff costs were £3 0m (2%) higher than the same period last year mainly due to the inflationary impact from the annual pay award offset by close management over recruitment of non-customer facing staff

Four new Corporate Banking Centres have been opened as part of our programme to **double our representation** by mid 2009.

Credit quality and impairment losses

Impairment losses	2007 £m	2006 £m	Change £m
Profit and loss charge			
Retail sector	**87 9**	99 4	(11 5)
Corporate sector	**14 1**	5 9	8 2
Total	**102 0**	105 3	(3 3)
Charge as a percentage of loans and advances to customers	**1.13%**	1 29%	(0 16%)

The impairment charge of £102 0m was £3 3m lower than 2006 reflecting lower charges for the Retail sector partly offset by higher Corporate charges

The impairment charge in the retail sector has seen a reduction from the levels reported last year as a direct result of a programme of focused activities particularly in the unsecured retail portfolios These actions have continued through into 2008 as the backdrop of personal insolvency and high consumer indebtedness has combined with a weaker economic environment The secured mortgage book continues to enjoy extremely low levels of default and subsequent impairment which reflects the relatively low average loan to value ratio and the affordability tests applied within our credit assessments Retail sector impairment losses were £11 5m lower than last year representing 1 7% expressed as percentage of average retail lending, 0 2% lower than last year

Against an industry backdrop of significantly increasing card fraud losses, particularly through the telephone and Internet channels, a variety of measures have been successfully implemented to enable the Bank to out-perform industry benchmarks These controls have been implemented with the customer experience at the heart of their development, but at the same time maintaining a consistent and committed approach to the prevention of financial crime

The Corporate impairment charge tends to be more volatile due to the nature and timing of one off charges In the last year we have continued to address issues arising from the higher risk sectors and the increase in the charge compared to last year reflects these actions

Investment in the future

On 20 July, CFS announced plans to improve its operational business performance for the benefit of its 6 million customers This next stage of development will see investment of £250 million being made in the business to support planned growth across the business The investment plans include enhanced relationship products, a new web offering for general insurance, new technology for CFS financial advisers, a doubling in the number of corporate banking centres, significant new Partnership arrangements, people development, and further investment in our Brand, which will be a key priority Our proposed 2008 campaign will bring 'good with money' to life at the heart of our brand Progress made in 2007 as part of this programme is set out below

In order to improve the return on this investment and to ensure it serves customers in the most cost effective way, CFS announced in July 2007 its plans to reduce annualised operational costs by £100m by the end of June 2008 and to reduce the workforce by approximately 1,000 during 2007 We have worked constructively with our Trade Unions to manage this change without impacting business performance and achieved the targeted reduction in roles through a combination of voluntary and compulsory redundancies, as well as the removal of a number of vacancies throughout the organisation

The Bank is increasing its support for microfinance initiatives through a special $50m fund. This money will be used to **support the development of small business** in some of the world's poorest countries.

People in our customer-facing roles, specifically those who service or sell to our customers by telephone, financial advisers and customer-facing advisers within Bank branches, have been unaffected by these changes The benefits of the reduced cost base will be shared between CFS's operating entities

The extensive restructuring and modernisation of the business has necessitated substantial investment resulting in significant items of £38 0m in 2007

The 2006 significant items include gains from April 2006, on implementation of the new Co-operative Group Pension (Average Career Earnings) scheme, as the Bank has adopted defined contribution accounting for pensions The pension assets and liabilities have been transferred from the Bank balance sheet, with P&L charges based solely on contributions made As at 5 April 2006, the Bank had total scheme deficits of £109 2m which were transferred to The Co-operative Group for no consideration and the resultant gain has been recognised in the income statement in accordance with IAS 19

Basel and other regulatory developments

The Bank's Basel Programme has culminated in the FSA's approval of its waiver application to operate under the Internal Ratings Based approach with effect from January 2008 This successful development means that for our retail book we are operating at the most advanced level whilst the corporate and wholesale assets will be risk assessed at the Foundation level initially, with the intention of moving to Advanced in the near future

Significant elements of achieving this objective have included the implementation of a revised governance structure, new modelling approaches and processes for Credit Risk Management, improved data quality and data governance and enhanced management information

The Bank also completed its first Internal Capital Adequacy Assessment Process (ICAAP) which was subject to the FSA's Supervisory Review Evaluation Process (SREP) during December

The Bank has also successfully introduced the Office of Fair Trading's (OFT) new 'customer promise' which gives customers more clarity about the cheque clearing process and allows them to benefit from a more efficient service

Summary and outlook

The Bank, as a significant element of CFS, has seen in 2007 the early impact on our performance of the change programme, including more web sales, enhanced ATM service availability and better targeted marketing In 2007, CFS showed its determination to tackle its cost base The underlying outcome of what was a year of change and market upheaval is that our business is now showing clear signs of progress towards our vision of becoming the UK's most admired financial services business

We **aim** to have the UK's most satisfied colleagues and customers.

Key performance indicators: **targeted, measured, defined.**

The Group's Key Performance Indicators are derived from the success measures on our journey towards our aspirational vision 'to be the UK's most admired financial services business' and the performance criteria in staff and executive incentive schemes.

1 Profit generation to create a sustainable model
The key financial performance measure is profitability Additional supplementary measures are cost/income ratio and net interest margin

Profitability is defined as operating profit before significant items and is the key financial performance measure in the Group

The Bank's contribution to CFS results was below targets primarily because of investment write downs

Cost/income ratio is calculated as operating expenses before significant items divided by operating income before significant items This was marginally better than 2006 due to tight cost control

Net interest margin is net interest income divided by interest-earning assets This was consistent with 2006

2 Market leading colleague satisfaction

We measure Colleague Satisfaction using a core set of questions via our annual survey of all colleagues, called the ECHO survey (Every Colleague Has Opinions)

These questions measure three key elements of colleague opinion

- Emotional attachment to the organisation
- Willingness to stay with the organisation
- Discretionary effort – how much colleagues are motivated to go beyond their normal duties to help the organisation achieve its aims

Sometimes known as 'Say, Stay and Strive', these are standard measures used across many businesses and organisations to measure engagement They have two clear advantages as key people measures Firstly, because they are used generally across many other organisations, we can easily benchmark our organisation's performance in engaging colleagues against others Secondly, they measure outcomes within an organisational culture, such as pride and advocacy They are, therefore, very difficult to influence by specific or short-term activities – for example, if response rates were used, this could be incentivised in some areas, skewing the figures

The score for Colleague Engagement is determined by reviewing the responses to the engagement questions asked in the ECHO survey The average proportion of favourable responses (eg 'Agree' or 'Strongly Agree') across the whole of the organisation provides our Engagement Index, which was 52% in 2007 Our strategic target is to improve this figure year on year until we reach the High Performance Norm level of 73% by 2010/11

3. Market leading customer satisfaction

Our current measurement of overall customer satisfaction is derived from GFK NOP's syndicated Financial Research Survey (FRS) The FRS is the largest survey in the marketplace (with 60,000 Financial Services customers interviewed each year)

Customers register their satisfaction levels with their providers at product level on a seven point scale – extremely, very, fairly, neither\nor, fairly dissatisfied, very dissatisfied, extremely dissatisfied Product level scores (based on Extremely and Very Satisfied responses) are then weighted by customer numbers to produce Business Unit level scores and an overall measure for CFS To ensure a statistically robust sample per CFS product area and to even out any seasonal variations in scores a rolling 12 month's worth of data is used

The trend of improvement in the overall CFS satisfaction score has been reflected in the retail bank which maintain a gap ahead of the market (Top Five by Market Share) with a score for extremely or very satisfied of 79 4% compared to the market of 65 3%

Our ultimate aim is to have the UK's most satisfied customers

4 Market leading social responsibility approach

In 2007, CFS measured its progress towards its goal of a market leading social responsibility approach using the following three indicators Two of the three targets set for attainment in 2007 have been achieved, and one has been partially achieved

The first indicator looks at unprompted public awareness of the Bank as a financial services business that takes social responsibility into account This measure derives from an independent survey of 1,000 members of the general public, which, in 2007, was undertaken in February Targets set for 2007 sought a number one ranking for the Bank Against these, the Bank retained the number one ranking, with a score of 11% (2006 12%) In 2008, the Bank is seeking to maintain its position

The second and third indicators look at performance in Business in the Community's Corporate Responsibility Index and Environment Index The indexes are voluntary self-assessment surveys that benchmark Corporate Responsibility and Environmental strategy (and their integration), management, reporting and performance across a range of issues The 2007 targets were to seek a Platinum (leading group) ranking for The Co-operative Financial Services by achieving a score of 95% or more in both indexes In the Corporate Responsibility Index 2006, which was published in May 2007, The Co-operative Financial Services achieved a Platinum Group ranking, attaining a score of 98% and emerging as a sector leader In the Environment Index, The Co-operative Financial Services achieved a Platinum ranking, attaining a score of 99 79% In 2008, CFS will be seeking to maintain its Platinum rankings in both indexes by achieving a score of 95% or above

5 Membership growth

The Bank, as part of The Co-operative Group, is ultimately jointly owned and democratically controlled by its members Members of The Co-operative enjoy a share in the profits and can exercise their democratic control, with equal rights and benefits The importance of growing a strong and committed membership base is integral to our vision and beliefs and is an integral part of our Brand Growing engagement with our customers via Membership is a key element in delivering Competitive Advantage and Social Goals

Whilst we are committed to growing our membership base, we recognise the importance of ensuring that our members are engaged with The Co-operative True engagement will be reflected in both transactional and democratic participation The focus for 2008 is therefore to drive active engagement from our members This will be demonstrated by increasing participation rates across the diverse range of businesses offered by The Co operative Group, so that individual members transact with multiple businesses Inevitably, this type of activity will also attract new members

Executive committee

David Anderson Cathy Wilcher Mike Fairbairn Gerry Pennell John Reizenstein

Stephan Pater Dick Parkhouse

Corporate responsibility: bigger, brighter,

Sustainable development
At The Co-operative Bank, we have a proud history of corporate responsibility, central to which is managing and developing the business in a sustainable manner, as spelled out in The Co-operative Financial Services' Sustainable Development Policy

We are guided by the views and expectations of members, customers and other stakeholders, and have committed to delivering value to partners in a socially responsible and ecologically sustainable manner Our employees have identified social responsibility as one of the five values which provide direction to The Co-operative Financial Services, and therefore contribute to success The co-operative movement's values of self-help, self-responsibility, democracy, equality, equity and solidarity are also key to the Bank's way of doing business

While other companies are beginning to tackle their contribution to climate change, CFS' operations have already gone 'beyond carbon neutral' – offsetting 110% of the business' remaining carbon dioxide emissions CFS also remains the only major financial services provider in the world to secure total business certification to the ISO 14001 environmental management standard across all activities, products and services

It is this kind of leadership that has seen CFS ranked, once again, in the Platinum Group of leading companies in three separate Business in the Community indices Corporate Responsibility, Environment, and Community, with scores of 98% and above The Bank's approach to ethical finance also contributed to The Co-operative Group being recognised, in 2007, with a Queen's Award for Enterprise in the Sustainability Development category This award was first attained by the Bank in 2002, and CFS is the only financial services provider ever to have received it

Management
Situated within the Group's Corporate Affairs and Social Goals Department, the ethics and sustainability, and community and campaigns teams are responsible for the day-to-day management of our sustainability agenda

Our sustainability performance is measured against a wide range of economic, social and environmental indicators, and reported in the Group's Sustainability Report This annual report is considered by the Values and Principles (V&P) committee (a sub-committee of the Board), which oversees sustainability strategy, performance and management

Social responsibility
Ethical finance
Over the years, The Co-operative Bank has been a pioneer in the area of ethical finance, and is still the only bank to have a customer-led ethical policy Launched in 1992, the policy seeks to ensure that personal customers' money is invested in line with their values

Potential corporate and business banking customers are screened to ensure that their business practices pose no conflicts with our ethical policy If they do, finance is declined In 2007, of the 348 finance opportunities assessed by our Ethical Policy Unit, 32 were found to be in conflict and therefore turned away

As reported in our latest Ethical Consumerism Report, UK consumers are increasingly taking ethical and environmental considerations into account when choosing who to spend their money with To better reward ethical purchasing, we launched **think**, a credit card that offers a lower rate of interest for purchases from designated ethical partners, alongside a package of additional reforestation features

greener.

2007 saw us extending our commitment to microfinance – the means by which low-value loans are offered to some of world's working poor We have pledged £25 million to support the development of small businesses in some of the world's poorest countries

Concern for the community
As one of the seven co-operative principles, 'concern for the community' is at the core of CFS' approach As part of The Co-operative Group, our work in this field is far-reaching, covering five key areas climate change, social inclusion, tackling crime, food ethics and modern co-operation

CFS measures its support for the community using the London Benchmarking Group (LBG) model, which quantifies both cash and in-kind donations In 2007, CFS contributed a total of £3 4m to charitable causes (2006 £3 7m), the equivalent of 2 2% of pre-tax profit

As part of this, we provided £44,000 to help community groups across the country, via the Bank's unique Customer Donation Fund This fund enables regular donations to be made to customers of our Community Directplus account – a dedicated bank account for community organisations, charities and social groups

49 local organisations benefited in 2007, including an organisation that promotes art by children with autism, and a volunteer run scheme that restores old hand-tools, before forwarding them worldwide Since the scheme was launched in 2003, it has provided over £140,000 to 170 groups

Our pioneering work with prisoners continued throughout 2007 The pilot project with Forest Bank prison provides soon-to-be-released prisoners with basic bank accounts, an often vital requirement of holding down a job or securing accommodation – factors seen as key to the reduction of re-offending

In addition, we are also working with the charity Credit Action to provide financial education to prisoners By the close of 2007, Newcastle College had successfully delivered the pilot course to six prisons Following positive feedback, the course is now being developed further and it is planned to roll it out to other prisons in 2008

CFS has partnered with Liverpool John Moores University on a new academic programme, aimed at deepening participants' understanding of poverty, over indebtedness and financial exclusion The Certificate of Professional Development in Promoting Financial Inclusion in Low Income Communities will offer a staff development opportunity for youth and community workers, health visitors and others who work with young people and adults in low income communities The module will cover a range of initiatives within the Government, community and voluntary sectors and financial services industry

We continue to be the largest provider of banking services to the credit union sector, providing facilities to over 60% of the British movement Following our work with the Association of British Credit Unions, a number of credit unions are now able to offer banking services (including a debit card, ATM withdrawals, direct debits and standing orders) to their members, the Bank providing behind the scenes service and administration Development of the credit union current account was seen as a step change in credit unions' ability to address financial inclusion and an average of 120 of these accounts were being opened every week by the close of 2007

Ethics drives our businessat
a **grass roots** level.

Our commitment to the community has always extended beyond financial support Employees are encouraged to take advantage of various volunteering opportunities, whether it be a team challenge, such as creating a community garden, or an individual one, such as mentoring a young person In 2007, 610 CFS employees registered that they had taken part in volunteering activities in work time, altogether contributing a total of 5,681 hours

Environment

The responsible management of energy, waste, transport, chemicals and biodiversity impacts are key to the Bank's vision of a more sustainable future Climate change is clearly a driving imperative and our work to tackle this has focused on energy saving, carbon offsetting, the provision of finance and renewable energy consumption and generation

CFS led the switch to green energy back in 1998, and currently sources virtually all of the business' electricity from good quality renewable sources, such as wind and water CFS is also involved with directly creating renewable energy, having developed the UK's largest solar project at The Co-operative Insurance's head office As a result, our greenhouse gas emissions have dropped by more than 70% against a 2002 baseline

Where we have unavoidable greenhouse gas emissions, CFS uses Climate Care to offset them through the delivery of renewable energy, energy efficiency and rainforest projects in the developing world As of 2007, an additional 10% is also offset, in order to account for legacy issues The Bank has been pioneering carbon offset schemes since 2000, and has already donated almost £1 5m to combat climate change on behalf of our mortgage customers

Throughout 2006 and 2007, we joined forces with Friends of the Earth to campaign on the theme of climate change, as part of the Customers Who Care campaign This call to action saw more than 22,000 customers lobby their MP on the Climate Change Bill, and monies totalling £290,000 distributed to nine climate change charities

CFS' commitment to combating climate change was one of the contributory factors that saw The Co-operative Group being declared outright winner at the Renewable Energy Association's 2007 Awards This Pioneer Award is presented to the UK organisation from outside the renewable industry that is most judged to have embraced the use of renewables and contributed most to the industry's development The Co-operative Group was also awarded top prize at Business Commitment to the Environment's Environmental Leadership Awards 2007, with the Bank praised by judges for the incorporation of carbon offset features into mortgage products

Further details of how the Bank is progressing in regard to corporate responsibility issues can be found in the Group's annual Sustainability Report

Wellbeing (health and safety)

CFS wants to 'make work a better place to be' for all our colleagues and in 2007 responsibility for occupational health and safety management became a part of our Wellbeing function within the Human Resources Division We believe that achieving excellent standards of colleague health and safety goes beyond just legal compliance and that our co-operative ethics clearly require us to protect everyone affected by our operations from harm

Our new wellbeing-led and people-focused approach to occupational health and safety will be innovative and effective, aimed at engaging all colleagues across all our business areas to meet their responsibilities to work safely and allowing CFS to gain full benefit from the commercial advantages that this will create

We continue to develop and maintain our occupational health and safety policies and protocols, in liaison with our Trade Union colleagues Where synergies exist, we are working with colleagues in the wider co-operative businesses to ensure we take full advantage of economies of scale and use resources wisely to both procure services and equipment and develop joint initiatives

Together with the more specific occupational health and safety inputs above, our Wellbeing activities include bringing a variety of new initiatives and events into CFS workplaces, which are aimed at health promotion and lifestyle enhancement Our in house gym and wellbeing suite is available to all colleagues, and locations away from the Manchester hub are benefiting from increasing access to both physiotherapy and alternative therapies All CFS colleagues have 24/7 access to a third-party Employee Assistance Programme We will continue to develop and improve our Wellbeing provision through 2008 and beyond

Business continuity

As part of our wider risk management process, effective business continuity planning ensures that the interests of customers, employees and other stakeholders are protected by minimising the risk of disruption to critical business operations caused by unplanned events Business continuity management continues to ensure that the risks of such incidents are reduced through appropriate resilience measures and, should the worst happen, that we have procedures in place to minimise unwanted impacts and to direct our response

The Bank is covered by the CFS Business Continuity Policy and in 2007 this Policy was revised in line with best practice and organisational changes The Executive approved an extended pool of senior managers to join the CFS Crisis Management Team Members attended training sessions culminating in the team undertaking a scenario exercise to test our preparedness in the event of a major operational disruption The Incident Response teams located at the major occupancies were also tested and continued to show an improvement in their capability A revised Business Impact Analysis – the method to confirm CFS' key processes during a major incident and their related systems – was completed by the business

In 2008 the data collated from the Business Impact Analysis will be used to ensure our capacity requirements are met A working group of cross-CFS business areas are reviewing our Pandemic *Influenza* contingency plans Building on the scenario exercises in 2007 Incident Response teams and the Crisis Management Team will undertake more stretching exercises and we will continue to assess our plans and arrangements against industry best practice

The Board

Bob Burlton Simon Butler Paul Hewitt Terry Morton

Graham Bennett David Davies Robert Newton Kathryn Smith

Graham Stow

Len Wardle

Martyn Wates

Stephan Pater

Stephen Watts

Piers Williamson

David Anderson

John Reizenstein

The Co-operative Bank Board

Non-Executive Directors

Graham Bennett Age 57 Chair of The Co-operative Bank p l c Occupation – Chief Executive Officer and Secretary, Southern Co-operatives Non-Executive Director of Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 1989

Bob Burlton Age 59 Occupation – Strategic Projects Executive, The Midcounties Co-operative Chair of Co-operative Financial Services Limited Non-Executive Director of Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2004

Simon Butler Age 53 Occupation – Photographer Member of the Co-operative Group Central & Eastern Regional Board Chair of Co-operative Insurance Society Limited and CIS General Insurance Limited Non-Executive Director of Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2003

David Davies Age 60 Senior Independent Director Occupation – Independent Professional Non-Executive Director Holds this position on the Boards of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited He is Chairman of Sun Life Assurance Company of Canada (UK) Limited and Hermes Fund Managers Limited First appointed to the Bank Board in 2003

Paul Hewitt Age 52 Occupation – Professional Non-Executive Director Holds this position on the Boards of Co-operative Financial Services Limited, Co-operative Insurance Society Limited, CIS General Insurance Limited and a number of organisations not connected with the Co-operative Group Previously deputy Chief Executive of Co-operative Group Limited First appointed to the Bank Board in 2003

Terry Morton Age 62 Occupation – Managing Secretary, Durham Alliance for Community Care Chair of Co-operative Group North Eastern & Cumbrian Regional Board Non-Executive Director of Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2006

Robert Newton Age 58 Occupation – Independent Professional Non-Executive Director Holds this position on the Board of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2007

Kathryn Smith Age 48 Occupation – Public Relations Consultant Member of the Co-operative Group South East Regional Board Non-Executive Director of Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2001

Graham Stow Age 63 Occupation – Independent Professional Non-Executive Director Holds this position on the Boards of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited Chair of the Audit & Regulatory Compliance Committee and a member of the Co-operative Group Food Retail Board Previously Group Chief Executive of Britannia Building Society from 1999 until 2003 First appointed to the Bank Board in 2003

Len Wardle Age 63 Occupation – University Fellow Member of the Co-operative Group South East Regional Board Chair of Co-operative Group Limited Non-Executive Director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2006

Martyn Wates Age 41 Occupation – Chief Financial Officer, Co-operative Group Non-Executive Director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2007

Stephen Watts Age 56 Occupation – Business Studies Lecturer Member of the Co-operative Group Central & Eastern Regional Board Non-Executive Director of Co-operative Group Limited, Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2006

Piers Williamson Age 46 Occupation – Chief Executive, The Housing Finance Corporation Independent Professional Non-Executive Director Holds this position on the Boards of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2005

Executive Directors

David Anderson Age 52 Chief Executive Also Chief Executive of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2005

Stephan Pater Age 56 Executive Director, CFS Chief Operating Officer Also Executive Director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2006

John Reizenstein Age 51 Chief Financial Officer during the year Also Executive Director of Co-operative Financial Services Limited, Co-operative Insurance Society Limited and CIS General Insurance Limited First appointed to the Bank Board in 2004

The Directors submit their report, together with the audited financial statements, for the year ended 12 January 2008

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 on pages 8 to 14 The principal risks and uncertainties facing the Bank are set out in the risk management section on pages 50 to 68 The Bank's key financial and non-financial performance indicators are described on pages 15 to 16 Note 32 of the financial statements provides details of the Bank's principal subsidiaries and the nature of each organisation's business

Principal activities
The Bank and its subsidiary undertakings provide an extensive range of banking and financial services in the United Kingdom

Outlets
At 12 January 2008 the Bank had 121 outlets (2006 116 outlets)

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 page 24 Robert Newton was appointed to the Board with effect from 1 August 2007 and Martyn Wates was appointed on 21 November 2007 Tony Lancaster resigned from the Board on 13 June 2007, Martin Beaumont resigned on 31 July 2007 and Craig Shannon resigned on 20 August 2007

Re-appointment of Directors
In accordance with the Articles of Association, Terry Morton, Len Wardle and Stephen Watts retire by rotation and, being eligible, offer themselves for re election None of the Directors offering themselves for re-election have service contracts with the Bank or any of its subsidiary undertakings which has a duration of more than one year All Directors up for re-appointment continue to demonstrate commitment to their roles (see schedule of attendance on page 30) The Notice for the Annual General Meeting at which the re-election of Directors will be proposed can be found on page 93

Results and dividends
The profit before taxation and significant items was **£49.1 million** (2006 £75 1 million), a decrease of £26 million on 2006 The profit attributable to the ordinary shareholders amounted to **£3.2 million** A dividend of £9 0 million was paid on 31 May 2007 No interim dividend was declared during 2007 The Directors recommend that there will not be a final dividend payment on 30 May 2008

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 group or in Co-operative Group Limited (formerly Co-operative Group (CWS) Limited), which is the ultimate holding organisation, or in any other entity controlled by the Co-operative Group

There have been no changes in the Directors' shareholdings between the end of the financial year and 3 April 2008

Employees
The Bank and its subsidiary undertakings employed 4,071 persons at 12 January 2008 (2006 4,163) The weekly average number of persons was 4,281 (2006 4,234) and their aggregate remuneration, before significant items, for the year was **£111.1 million** (2006 £109 6 million) 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 staff on customer, organisation and business performance issues, using staff publications, surveys, conferences, videos and both informal and formal consultations with Amicus, which continues to be fully involved where organisational change and other issues affect staff The Bank has been acknowledged as an 'Investor in People' company in the UK

Diversity
The Bank, as part of Co-operative Financial Services, welcomes diversity and actively promotes a policy and practice of equality of opportunity in employment for all employees, regardless of sex, gender reassignment, marital status, sexual orientation, colour, race and nationality, national or ethnic origin, religion or creed, disability, responsibility for dependants, age, membership or non membership of a trade union or political affiliation

Employees with disabilities
The Bank is a member of the Employers' Forum on Disability, which provides advice and guidance on the employment of people with disabilities The Bank 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 The Bank has an Equal Opportunities Policy, which includes provisions to consider employment applications from people with disabilities and to match vacancies with an individual's particular aptitudes and abilities Further guidance and

information for employees on disability issues is available through Human Resources and on the employees intranet The Bank recognises its responsibility for making 'reasonable adjustments' for new employees with disabilities and for those individuals who develop disabilities whilst in employment

Corporate responsibility and the environment
The Bank's corporate responsibility activities are outlined on pages 18 to 20 In addition, the CFS Sustainability Report, which will be published towards the latter half of the 2008 financial year, describes how CFS, Co-operative Insurance and the Bank manage their social, ethical and environmental impacts

Political and charitable donations
During the year, the Bank and its subsidiaries made donations (which excludes affinity card payments) of **£0.3 million** (2006 £0 5 million) to United Kingdom charitable organisations In addition payments of **£0.2 million** were charged by Co-operative Group but funded by CFS on behalf of Bank customers, as part of the Bank's Customers Who Care campaigns In 2006 similar donations were made directly by the bank and are included in the £0 5 million as stated above Additional costs associated with the Bank's community involvement are provided within the CFS Sustainability Report It is the Bank's policy that no donations are made for political purposes

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

Supplier payment policy and practice
During the year the Bank ceased to pay suppliers directly as all supplies and services are now sourced through CFS Management Services Limited, a fellow subsidiary of the CFS Group A management charge is payable to cover the cost of these services Consequently at 12 January 2008 the Bank had no purchases outstanding (2006 16 days), based on the average daily amount invoiced by suppliers during the financial year

Statement of Directors' responsibilities in respect of the Directors' Report and the financial statements
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 they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU

The financial statements are required by law to present fairly the financial position and the performance of the Bank and the Group, the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation

In preparing these 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 they have been prepared in accordance with IFRSs as adopted by the EU, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company and the Group will continue in business The Directors statement with respect to going concern is included on page 33

Under applicable law, the Directors are also responsible for preparing a Directors' Report and a Corporate Governance Statement, that comply with the law and those regulations

The Directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Bank and the Group and enable them to ensure that their financial statements comply with the Companies Act 1985 They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Bank and the Group and to prevent and detect fraud and other irregularities

Under applicable law and regulations, the Directors are also responsible for preparing a Directors Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and these 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

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

Auditor
In accordance with Section 385 of the Companies Act 1985, a resolution for the re-appointment of KPMG Audit Plc as auditor of the Bank and a resolution to authorise the Directors to fix their remuneration are to be proposed at the next Annual General Meeting

By Order of the Board
Moira Lees, Secretary
3 April 2008

UK Combined Code on Corporate Governance
For the year ended 12 January 2008 the Bank complied 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 Co-operative Group Limited (the Co-operative Group), with the exception of the areas noted throughout the Corporate Governance Report

Responsibility of the Bank Board
The Directors are committed to leading and controlling the Company effectively The Board is responsible for the success of the Company 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 Bank Board is to direct the business of the Company, and in particular to
- ensure that the Company's affairs are conducted and managed in accordance with its Memorandum and Articles, and the best interests of its stakeholders within the ethics and values of co-operative principles,
- agree objectives, policies and strategies and monitor executive management,
- determine the vision and strategy of the Company in consultation with the Chief Executive and the Executive,
- approve the annual budget and business plan,
- approve the reported financial statements and dividends,
- monitor, through various Committees, the key significant risks facing the Company,
- establish Board Committees, and
- approve the delegated financial authorities

The Board manages these matters at its regular Board and strategy meetings and details of attendance are noted on page 30 It has met eleven times in 2007 The Board is scheduled to meet for eleven Board meetings and two strategy meetings in 2008

Board balance and independence
The Board currently comprises thirteen Non-Executive Directors and three Executive Directors

The Board has appointed four Independent Professional Non-Executive Directors as defined under the Combined Code David Davies, Robert Newton, Piers Williamson and Graham Stow On 23 February 2005, the Board appointed David Davies to be the Senior Independent Director

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 judgement and whether there are any relationships or circumstances which are likely to affect, or could appear to affect, the Director's judgement The Board has concluded that, looking across the wider Co-operative Group, Co-operative Group Regional Directors (unless employees within the last five years) should be defined as independent while those representing corporate members of the Co-operative Group could not be so categorised in the Co-operative context This was because the latter represented significant 'shareholders' with material business relationships Throughout the year the Bank Board met those code requirements on the independence of Directors

With the exception of Graham Bennett and Bob Burlton, who represent corporate members of the Co-operative Group, Martin Beaumont who, until his resignation from the Board on 31 July 2007, was Chief Executive of the Co-operative Group Martyn Wates, appointed on 13 November 2007 and who holds an executive appointment in the Co-operative Group, and Paul Hewitt who was until 28 July 2007, Deputy Chief Executive of the Co-operative Group, the Board has determined the remaining five Non-Executive Directors Simon Butler, Terry Morton, Kathryn Smith, Len Wardle and Stephen Watts, being Regional Directors of the Co-operative Group, to be independent Together with the Independent Professional Non-Executive Directors, the balance of the Board meets with the Code's requirements The Board believes that all the Non-Executive Directors have considerable experience and make valuable contributions to the operation of the Bank

The Board Non-Executive Directors constructively challenge and help develop proposals on strategy and bring strong, independent judgement, 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 composition of the Boards of CFS, the Bank, CIS and CISGIL (which collectively operate the financial services business of the Co-operative Group) have been organised so that there is common membership of each CFS does not comply with the Combined Code principle that all directors should be submitted for re-election at regular intervals and that no non-executive director should serve a term of greater than nine years This is in part due to the method of appointing directors by the Co-operative Group However, Board composition, and the process for refreshing it, is under review currently

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

There is regular communication between the Directors, the Chair and the Secretary between meetings

When a Director is unable to attend Board or Committee meetings, issues can be relayed in advance to the relevant Chair Written questions for management on papers are encouraged from Directors between meetings A rolling schedule of matters arising from Board and Committee meetings are followed through

The Roles of the Chair 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 Bank Board

The 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, ensures Directors receive accurate, timely and clear information and facilitates effective communication with shareholders

Details of the Chair's professional commitments are included in the Chair's biography on page 24 The Board is satisfied that these responsibilities do not interfere with the performance of the Chair's duties for the Company

The Chief Executive 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, copies of which are available from the Secretary on request Each of these Committees has a role in overseeing the Company and its subsidiaries A provision of the Code is that the terms of reference for the remuneration committee and the audit committee are available on the Company's website

Remuneration and Appointments Committee
The CFS Remuneration and Appointments Committee meets as a joint Committee for CFS, CIS and the Bank The Committee currently comprises seven members and is chaired by the CFS Chair, Bob Burlton During the year the Committee also comprised Martin Beaumont (who resigned from the Board on 31 July 2007), Graham Bennett, Simon Butler, Terry Morton, Kathryn Smith, ~~and~~ Graham Stow and Len Wardle,

The Committee's role in respect of the Executive and Executive Directors, is to determine remuneration and employment policy, oversee contractual arrangements, review salaries, approve incentive schemes and any payments made under such schemes and recommend appointments to the Board In respect of Directors, the Committee makes recommendations to shareholders in a General Meeting for decision The Committee is supported by the Co-operative Group Remuneration and Appointments Committee in ensuring consistency, where appropriate, across the wider Group The Committee is responsible for overseeing succession planning It uses external consultants for the appointment of the Executive and Independent Professional Non-Executive Directors Directors are appointed by the Co-operative Group The Committee met eight times during 2007 and its report can be found on pages 34 to 38

The Combined Code provides that all members of the remuneration committee should be independent non-executive directors and that a majority of members of the nomination committee should be independent non-executive directors The CFS Remuneration and Appointments Committee fulfils the role of both these committees The code also provides that the Chair of the Board may be a member of the remuneration committee but not chair it unless he is considered independent on appointment as Chairman Bob Burlton is not considered independent The arrangements for chairing the Remuneration and Appointments Committee are being reviewed in 2008 as part of a wider review of board effectiveness

The Committee members are all Non-Executive Directors, one of whom is an Independent Professional Non-Executive Director They have no personal financial interests in the Committee's decisions, and they have no involvement in the day-to-day business of the Bank or its subsidiaries Bob Burlton and Graham Bennett are not considered 'independent' based on the statement agreed by the Board Whilst the independence criteria provision, of the Code, for a remuneration committee is not met, a majority of the members of the Remuneration and Appointments Committee are independent and it is felt that the Committee has a sufficient level of independence to discharge its duties

Board Standing Committee
The Board Standing Committee allows the consideration of urgent Bank business between meetings of the Bank Board The Committee meets on an ad hoc basis and did not meet in 2007 The Committee comprises the Chair, the Chief Executive, together with four Non-Executive Directors, to include the Chairs of CIS and CFS, and the Senior Independent Director

CFS Exposures Committee
The Committee comprises seven members and is chaired by the Bank Chair, Graham Bennett During the year the Committee comprised of Kathryn Smith, Stephen Watts, Piers Williamson, David Anderson, Kevin Blake (who is not a Board Director), Bryan Portman (who resigned from the Committee on 5 September 2007 and was not a Board Director), and Martyn Wates (who was appointed by the Board on 21 November) Keith Alderson (Director of Corporate Banking) usually attends the meetings by invitation

The Committee met ten 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 High Risk Exposures Return, where Credit Committee determines that these should be escalated,
- review and approve management actions on any other positions which the Credit Committee or the Heads of Risk and Capital Management determine should be brought to its attention, and
- review and approve any reports required to be scheduled as part of Board policies

CFS Audit & Regulatory Compliance Committee
The CFS Audit & Regulatory Compliance Committee meets as a joint committee for CFS, CIS, CISGIL and the Bank The Chair of the Committee is Graham Stow, an Independent Non-Executive Director The other members of the Committee are Tony Lancaster (who retired from the Board on 13 June 2007), Terry Morton, Kathryn Smith, Len Wardle (who retired from the Committee on 7 November 2007), Robert Newton (who was appointed to the Committee on 5 September 2007), and Paul Hewitt Paul Hewitt brings recent and relevant financial experience

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 and its subsidiaries 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 of the process that has been applied by the Boards to deal with material internal control aspects of any significant problems disclosed in the Financial Statements,
- obtain assurance that the Bank and its subsidiaries are compliant with relevant regulation,
- review and discuss, with the CFS Director of Compliance, the issues identified as a result of compliance work and how management is addressing these issues,
- monitor regulatory relationships, in particular, with the Financial Services Authority,
- review co-ordination between the internal and external auditors and, where relevant, the risk management functions,
- monitor and assess the role and effectiveness of the Internal Audit function, and
- review the annual statements on internal control of the Bank and its subsidiaries and their compliance with the Combined Code or subsequent corporate governance guidance (as applicable) prior to consideration by the Board, and in particular where requested by the Board

During the year, the Committee has reviewed its own effectiveness

CFS Risk Management Committee
The CFS Risk Management Committee meets as a joint committee for CFS, CIS, CISGIL, and the Bank The Chair of CIS, Simon Butler, chairs the Committee The other members of the Committee are David Davies, Mike Fairbairn (who is not a Board Director), Paul Hewitt, John Reizenstein, Piers Williamson and Craig Shannon (who was appointed to the Committee on 4 March 2007 and resigned from the Board on 20 August 2007) The Committee met seven 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 and its constituent elements,
- to review and challenge the risk appetite process with a focus on the overall organisational view of risk appetite,
- to monitor compliance with board approved risk appetite,
- to approve mandates and portfolio limits in line with risk appetite, and monitor and review any breaches thereof,
- to assess the robustness of ICAAP / ICAS processes,
- to review and challenge the Bank Executive's recommendations on level of capital held in relation to how adequately it reflects the Bank's risk profile,
- to review and challenge the adequacy of risk management activities across the Bank managed by the Bank's Executive, including risk mitigation,
- to review and challenge the adequacy of the risk management process and systems in operation,
- to set standards for risk management processes and techniques, and benchmark against industry best practice on a regular basis,
- 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

Attendance

The following table sets out the frequency of, and attendance at, the Board and Board Committee meetings for the period under review by Directors

Directors	**Main Board**	**CFS Remuneration and Appointments Committee**	**CFS Exposures Committee**
Number of meetings held	11	8	10
Graham Bennett	11(11)	7(8)	10(10)
Martin Beaumont	7(7)	2(3)	–
Bob Burlton	10(11)	8(8)	–
Simon Butler	11(11)	7(8)	–
David Davies	11(11)	–	–
Paul Hewitt	10(11)	–	–
Tony Lancaster	4(5)	–	–
Terry Morton*	11(11)	7(8)	–
Robert Newton	3(4)	–	–
Kathryn Smith	9(11)	6(8)	7(10)
Graham Stow*	11(11)	8(8)	–
Len Wardle	10(11)	2(2)	–
Martyn Wates	2(2)	–	0(0)
Stephen Watts	10(11)	–	8(10)
Piers Williamson	10(11)	–	9(10)
David Anderson	11(11)	–	10(10)
Stephan Pater	10(11)	–	–
John Reizenstein	9(11)	–	–
Craig Shannon	7(7)	–	–

Directors	**CFS Audit & Regulatory Compliance Committee**	**CFS Risk Management Committee**
Number of meetings held	4	7
Graham Bennett	–	–
Martin Beaumont	–	–
Bob Burlton	–	–
Simon Butler	–	7(7)
David Davies	–	5(7)
Paul Hewitt	4(4)	6(7)
Tony Lancaster	3(4)	–
Terry Morton*	4(4)	–
Robert Newton	1(1)	–
Kathryn Smith	3(4)	–
Graham Stow*	4(4)	–
Len Wardle	4(4)	–
Martyn Wates	–	–
Stephen Watts	–	–
Piers Williamson	–	6(7)
David Anderson	–	–
Stephan Pater	–	–
John Reizenstein	–	7(7)
Craig Shannon	–	1(2)

* Also members of the Co-operative Group Audit and Risk Committee

The Board Standing Committee did not meet in 2007

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 Company's expense in furtherance of their duties

Directors and Officers' Indemnity Insurance
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 The arrangements for this were reviewed during the year

Professional development
On appointment, Directors undertake an induction programme designed to develop their knowledge and understanding of the Group The induction is appropriately tailored to their experience and background and includes an overview of the Bank and the wider Group, together with the role of the Board and the matters reserved for its decision Directors also receive information on the principal Board and management committees, and the powers delegated to those committees, the Bank's corporate governance practices and procedures, including the powers reserved to the Executive, and the latest financial information Briefing sessions on the strategy and performance of the Bank's core business areas are also held with key members of the Executive

A Board training programme exists which ensures that Directors are regularly updated on the Bank's business, the competitive and regulatory environments in which it operates, corporate social responsibility matters and other changes affecting the Bank and the industries in which it operates

Performance evaluation
The Combined Code requires the Board to undertake a formal and rigorous annual evaluation of its own performance and that of its Committees and individual Directors At the present time the Board collectively evaluates its performance, effectiveness, and commitment The most recent process of annual evaluation started on 21 November and the analysis was reported to the Board in February 2008

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 Bank's 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 Company

From 15 January 2006, the Executive of the financial services Boards of CFS, CIS, CISGIL and the Bank were organised under a single Executive Management framework

Relations with shareholders
The Bank has two equity shareholders The majority of shares are held by CFS, which is a wholly owned subsidiary of the Co-operative Group The remainder of the shares are held by the Co-operative Group With effect from 15 January 2006, all the Directors of the CFS Board were appointed to the Bank Board ensuring a common understanding of objectives

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 Meeting but the shares only carry 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 the Annual 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

Internal control
The Board has overall responsibility for the Bank's system of internal controls which aim to safeguard the Company's assets, ensure that proper accounting records are maintained and that the financial information used within the business and for publication is accurate, reliable and fairly presents the financial position of the Bank and the results of its business operations The Board is also responsible for reviewing the effectiveness of the system of internal controls This has been in place for the year under review and up to the date of the approval of these financial statements and is regularly reviewed by the Board The system is designed to provide reasonable assurance of effective operations and compliance with laws and regulations, although any system of internal controls can only provide reasonable, not absolute, assurance against material mis-statement or loss, and can only mitigate rather that eliminate the risk of failure to achieve business objectives

Since the publication in September 1999 by the Institute of Chartered Accountants in England and Wales of the Turnbull Report, 'Internal Control Guidance for Directors on the Combined Code' (revised by the Financial Reporting Council in October 2005), the Directors have continued to review the effectiveness of the Bank's system of financial and non-financial controls, including operational and compliance controls, risk management and the Bank's high level internal control arrangements The Bank has adopted an internal control framework that contains the following key elements

Control environment

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

- an organisational structure with clear lines of responsibility, delegation of authority and reporting requirements,
- clearly defined policies for capital and revenue expenditure Larger capital and revenue expenditure requires Board authorisation,
- 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 Results are reported against budget and prior year The relevant Executives consider any significant changes and variances and remedial action is taken where appropriate,
- a Code of Business Conduct covering relations with customers, shareholders, employees, suppliers, community and competitors,
- a whistleblowing policy and procedure which provides for any employee to report, in confidence, suspected serious malpractice, and
- Internal Audit and Compliance functions that review the system of internal control

Risk assessment

The Board and Executive management have the primary responsibility for identifying the key business risks facing the Company The Board has established Board Committees and Executive Committees to administer a risk management process which identifies the key risks facing the business and reviews reports submitted to those Committees on how those risks are being managed

Management has responsibility for identifying and evaluating significant risks and for designing and operating suitable controls

Risks are documented in a risk register Each risk is assigned to an appropriate manager who is responsible for ensuring that it is managed in accordance with the Bank's risk management process, which is kept under review to ensure that it accords with best practice and the evolving requirements of the FSA Risk assessments are updated on a quarterly basis Significant risks are reported to the appropriate Risk Management Committee and CFS Audit & Regulatory Compliance Committee

Control procedures

The Bank's control procedures are designed to ensure complete and accurate accounting for financial transactions and to limit the potential exposure to loss of assets or fraud

In a commitment to the robustness of its internal control environment, in 2007 the Board established Process Management Operational Rigour to focus on improving processes and controls

Key accounting policies and procedures are documented Up to date manuals are maintained that cover the Bank's insurance procedures, employee policies and procedures, Code of Business Conduct and information technology standards These manuals are issued to appropriate management who are trained in the procedures

Information and communication

Communication takes place with all key stakeholders through a variety of media including the CFS Sustainability Report 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

Monitoring

The operation of the system of internal control is the responsibility of line management It is subject to independent review by Internal Audit and, where appropriate, by the Bank's external auditor and external regulators

The CFS Audit & Regulatory Compliance Committee on behalf of the Board reviews the reports of the Bank on internal control Full details of the operation of the Committee can be found on page 29

A key part of the work of the Committee is an annual 'letter of assurance' process by which responsible managers confirm the adequacy of their systems of internal financial and non-financial controls, their compliance with the Bank's policies (including those relating to safety, health and the environment), local laws and regulations (including the industry's regulatory requirements) and report any control improvements required

The Directors review the system of internal controls and believe it complies with the Turnbull Report guidance

External Audit

One of the duties of the CFS Audit & Regulatory Compliance Committee is to make recommendations to the Co-operative Group Audit and Risk Committee in relation to the appointment of the external auditor In 2003 the Co-operative Group Board approved the re-appointment of KPMG Audit Plc as the external auditor following a competitive tender exercise

Details of the amounts paid to the external auditors during the year for audit and other services are set out in note 2 on page 72

The 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 auditor The external auditor is 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 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 auditor

- 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 Audit & Regulatory Compliance Committee may determine

The performance of the external auditor 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 appraisal function, which derives its authority from the Board through the CFS Audit & Regulatory Compliance Committee Its primary role is to provide reasonable and objective assurance about the adequacy and effectiveness of the internal control framework and risk management practises

Internal Audit seeks to discharge the responsibilities set down in its charter by reviewing the processes which ensure that business risks are effectively managed, reviewing the financial and operational controls which help to ensure that the Bank's assets are properly safeguarded from losses, including fraud, reviewing the controls which help to ensure compliance with corporate objectives, policies and procedures and external legislation and regulation, and on an ad hoc basis, reviewing that value for money is obtained

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 and to report and advise on the proper and effective use of resources

Internal Audit reports are submitted to the CFS Audit & Regulatory Compliance Committee and significant issues are reported from that Committee to the Co-operative Group Audit and Risk Committee

Statement on Going Concern

After making all appropriate enquiries, the Directors have a reasonable expectation that the Bank has adequate resources to continue in operational existence for the foreseeable future For this reason, they continue to adopt the going concern basis in preparing the Bank's financial statements

Remuneration report

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 the Directors' Remuneration Report Regulations 2002 (incorporated into the Companies Act 1985)

The Bank Board comprises Non-Executive Directors including Independent Professional Non-Executive Directors, a Professional Non-Executive Director and Executive Directors appointed by the Co-operative Group Board

This report provides details of the remuneration of both the Executive Directors and Non-Executive Directors

This report will be put to an advisory vote of shareholders of the company at its Annual General Meeting, which will be held on 16 May 2008

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,
- details of the terms of the Service Contracts and the remuneration of the Executive Directors and Non-Executive Directors for the 2007 financial year

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

Role of the Remuneration & Appointments Committee
The Committee's principal terms of reference are to

- determine policy on remuneration and other main terms and conditions of employment,
- 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,
- approve any relevant incentive schemes, and ensure that they are in line with current market practice, and authorise payments under any incentive schemes in line with their rules

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

+ and Len Wardle

At the end of 2007, the Committee comprised ~~six~~ seven members The members are Bob Burlton as Chair, together with Graham Bennett, Simon Butler, Terry Morton, Kathryn Smith ~~and~~ Graham Stow During the year, Martin Beaumont (Deputy Chair of CFS) served as a member until his retirement from the Board on 31 July 2007 The Board believes that all members of the Committee are independent for the purposes of reviewing remuneration matters The CFS Chief Executive and the Human Resources Director also attended the meetings of the Committee, except when their own remuneration was being considered Other individuals are invited to attend for specific agenda items when necessary The Committee works with the Co-operative Group Remuneration & Appointments Committee in ensuring consistency, where appropriate, across the wider Group

The Committee members are all Non-Executive Directors, one of whom is an Independent Professional Non-Executive Director They have no personal financial interests in the Committee's decisions, and they have no involvement in the day-to-day business of the Bank The Committee met eight times in the period under review

To ensure that it receives independent advice on remuneration matters, the Committee retained New Bridge Street Consultants LLP as its advisers during 2007 to provide advice solely on remuneration matters New Bridge Street has supplied advice on remuneration survey data, market trends and pensions matters, including incentive schemes Other than specialist advice in relation to remuneration matters, New Bridge Street does not provide other services to the Bank Solicitors Addleshaw Goddard were also retained to provide legal advice to the Committee with respect to Executive Directors' service contracts

Policy on Directors' remuneration

Executive Directors
In determining the remuneration policy for Executive Directors, the Committee has considered a number of factors including

- the importance of attracting, retaining and motivating senior management 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, and
- ensuring that the interests of the Executive Directors are aligned with those of the Bank

The current policy is to pay Executive Directors, who also sit on the CFS Board, base 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 but does not consider it appropriate to follow the quantum available in PLCs Accordingly, the amounts payable under these plans are lower than in comparable PLCs

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 keeps the Bank's remuneration policy under review

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), business and individual performance during the financial year The normal salary review date for Executive Directors is at the start of each financial year in January Basic salary is the only element of remuneration that is pensionable Salaries received by Executive Directors during the financial year are set out in Table 1 on page 37

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 target level under the plan for the 2007 financial year was 35% of base salary for Executive Directors, including the Chief Executive Under the incentive plan the maximum potential for Directors (including the Chief Executive) is 60% of base salary for substantially exceeding targets These percentages remain unchanged for the 2008 plan

For Executive Directors, targets in the bonus year 2007 (paid 2008), are constructed so that 75% of any payout relates to financial measures, these being Total Shareholder Result, Life & Savings New Business Profit ('NBP') and Life & Savings Maintenance Expenses, with the remaining 25% being based on colleague and customer satisfaction

For the CFS Chief Executive, the ratio was 90% against CFS performance, and 10% based on wider Co-operative Group initiatives for the whole of 2007 For the Chief Information Officer for CFS and Co-operative Group, two thirds of the payment was weighted towards CFS performance, with the remaining third relating to Group performance, up to the merger of Co-operative Group and United Co-operatives on 28 July 2007 Following the merger, the Chief Information Officer's annual incentive plan is based only on CFS performance

For 2008, the same arrangements will apply for the CFS Chief Executive's bonus, however, the Chief Information Officer's bonus will be based 100% on CFS performance

The payments for the annual incentive plan in respect of the year 2007 are reflected in Table 1 within 'Performance Related Pay'

3) Long Term Incentive Plan

A medium term incentive plan was initially introduced in 2003 for Executive Directors of the Bank in order to align their objectives with the longer-term interests of the business The plan sets targets across a three-year period Performance against these targets is reviewed by the Committee on an annual basis Annual profit performance must be at or above 'Threshold' level for payment to be made The third three-year period of operation of the plan was 2005-2007 with potential payment in 2008 The target annualised payment level under the plan for Executive Directors, including the Chief Executive, for that three-year period (and subsequent years) is 28% of basic salary with a stretch level of 42% of basic salary for substantially out-performing targets

Following a review of incentives, this medium term incentive plan is being phased out with the plans that have started, ie 2006-2008 and 2007-2009, continuing for their three-year term being replaced by a new long term incentive plan from the start of 2008

The review of incentives, led by New Bridge Street, resulted in a new long term incentive plan for 2008 and beyond being approved The plan will be measured on the achievement of Financial Performance targets together with a Balanced Scorecard, ie customer satisfaction, growing colleague engagement, membership and corporate reputation, over a fixed three-year period starting 2008-2010 with potential payment in 2011 For Executive Directors, the threshold payment level, subject to performance conditions being met, is 16 7% of basic salary, with a maximum payment of up to 50% of salary for substantially exceeding targets It is envisaged that equivalent awards will be made annually thereafter

The payments for the Medium Term Incentive Plan are reflected in Table 1 within 'Performance Related Pay'

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 Remuneration & Appointments Committee may make a discretionary award of outstanding bonus payments earned up to the date of termination of employment

All the Bank Executive Directors had similar contracts during 2007 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
Senior executives of most companies get a payout under an executive share option scheme Because of the co-operative nature of the business it is not appropriate to operate a share option scheme

6) Non-Executive Directorships
The Committee has determined that 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 Co-operative Group

At this time, 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), which is a defined benefit pension scheme available to all employees The PACE Scheme, which is a registered occupational pension scheme, provides pensions based on 1/60th of average pensionable earnings, re-valued for inflation for each year of pensionable service from 6 April 2006 Accrued benefits as at 5 April 2006 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

Members of the PACE Scheme currently contribute 6% of their pensionable salary towards the cost of providing pension benefits with the employer paying the balance

Executive Directors have the facility of opting out of future pension accrual under the PACE Scheme when the value of their accrued pension benefits reaches the lifetime allowance under the tax rules in favour of a non-pensionable salary supplement 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 receives a salary supplement of 16% of basic salary

David Anderson and Stephan Pater have previously elected not to join the PACE Scheme and were each paid a salary supplement of 16% of basic salary Craig Shannon contributed to the PACE Scheme until he left the Scheme on 28 July 2007 when he became entitled to a deferred pension

Supplementary life cover is provided to Executive Directors in order to provide total life cover of 4 x salary when aggregated with benefits from the PACE Scheme

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 Co-operative Group In October 2007, Co-operative Group approved a fee of £100,000 per annum for the CFS Chair (Bob Burlton) with effect from October 2007 and an additional payment of £10,000 per annum to the Chair of the CFS Audit & Risk Committee (Graham Stow) with effect from November 2007 Details of the Directors' fees are shown in Table 3

Paul Hewitt became a Professional Non-Executive Director on 29 July 2007 having previously been an Executive Director by virtue of his former position as Deputy Chief Executive of Co-operative Group

The Bank Board includes four Independent Professional Non-Executive Directors, who are

- David Davies was appointed to the Board on 3 June 2003 In addition, he was appointed as Senior Independent Non-Executive Director on 23 February 2005, for which he receives an additional fee,
- Robert Newton was appointed to the Board on 1 August 2007,
- Graham Stow was appointed to the Board on 4 March 2003,
- Piers Williamson was appointed as to the Board on 1 July 2005

Tony Lancaster retired on 13 June 2007

Details of their remuneration are also shown in Table 3

Of the Non-Executive Directors the Independent Professional Non-Executive Directors and the Professional Non-Executive Director are party to agreements with Co-operative Group governing the terms on which their services are made available to the Bank

- Graham Stow holds an agreement effective up to 31 May 2009 with approval of the Co-operative Group Board in September 2007,
- David Davies holds an agreement effective up to 31 May 2010 with approval of the Co-operative Group Board following his appointment as Senior Independent Director, with effect from 23 February 2005,
- Robert Newton holds a three-year agreement, effective up to 31 July 2010,

- Piers Williamson holds a three-year agreement, effective up to 31 May 2008
- Paul Hewitt holds a three-year agreement, effective up to 28 July 2010

The Co-operative Group Board may resolve to reappoint any of the Independent Professional Non-Executive Directors at or before the date their contracts expire for a further three-year term It is normal policy of the Board not to allow an Independent Professional Non-Executive Director to serve for more than 9 year in aggregate

The agreements contain no specific provision for liquidated damages on early termination of a contract

None of the above Independent Professional Non-Executive Directors are Directors of Co-operative Group or members of any Group pension scheme or incentive plan

Table 1 – Executive Directors' Emoluments

	Date of service contract or appointment £'000	Basic Salary £'000	Other Supplements £'000	Performance Related Pay Annual £'000	Performance Related Pay Medium Term	Benefits in Kind £'000	2007 Total Emoluments £'000	2006 Total Emoluments £'000
David Anderson (1) (2) (4)	1 June 2005	570	94	216	385	13	1,278	844
Stephan Pater (2) (3) (4)	1 March 2005	321	54	98	78	23	574	599
John Reizenstein (2) (3) (4)	6 January 2005	336	57	123	87	16	619	556
Craig Shannon (2) (5) (8)	11 February 2005	194	6	–	–	13	213	499
		1,421	**211**	**437**	**550**	**65**	**2,684**	**2,498**
Former Directors who served the Bank in 2005 and 2006 (6) (7)		–	–	70		–	70	164
Compensation for loss of office (5)		–	–	–		–	405	–
Amounts attributable to fellow subsidiaries		(814)	(121)	(595)		(36)	(1,797)	(2,117)
		607	90	462		29	1,362	545

Notes

Note 1 Emoluments paid by the Society's ultimate parent organisation – Co-operative Group

Note 2 The emoluments in the table represent total basic pay, benefits in kind and performance related pay in respect of services for each individual as a Director of the Bank, CFS, CIS and CISGIL Of these emoluments, the following have been recharged to fellow group companies in respect of services as a Director or Senior Manager of CIS, CFS and CISGIL

David Anderson 57%
Stephan Pater 57%
John Reizenstein 58%
Craig Shannon 57%

Note 3 Benefits in kind includes a car allowance, which is paid with base salary, but is not pensionable
Note 4 The other supplements figures for David Anderson, Stephan Pater and John Reizenstein include a salary supplement in lieu of pension provision
Note 5 Compensation paid for loss of office was in respect of Craig Shannon for 2007
Note 6 John Marper was paid in full the remaining amount due for the Medium Term Incentive Scheme 2005-2007 of £36k
Note 7 Sheila Macdonald was paid in full the remaining amount due for the Medium Term Incentive Scheme 2005-2007of £34k
Note 8 Craig Shannon resigned as an Executive Director on 20 August 2008

Table 2 - Pension details of the Executive Directors

	Years of service	Total accrued pension at 12 January 2008 (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 12 January 2008 net of members' contributions £'000	Transfer value of total accrued pension at 13 January 2007 (3) £'000	Transfer value of total accrued pension at 12 January 2008 (3) £'000	Increase in transfer values net of members' contributions £'000
David Anderson (4)	2	–	–	–	–	–	–	–
Stephan Pater (4)	2	–	–	–	–	–	–	–
John Reizenstein (5)	4	5	–	–	–	59	62	3
Craig Shannon (2) (6)	4	45	24	23	146	178	350	161

Notes

Note 1 The total accrued pension is that which would be paid annually on retirement at normal retirement age based on service to 12 January 2008 and includes any transferred-in benefits as appropriate Under the terms of their contracts, existing Executive Directors at 17 January 2007 may take these benefits from age 60 and new Executive Directors after 17 January 2007 may take these benefits from age 65 The transfer values in the table above have been calculated on this basis

Note 2 Members of the PACE Pension Scheme have the option of paying additional voluntary contributions within the tax rules Neither these contributions nor the benefits arising from them are shown in the above Table

Note 3 All transfer values have been calculated in accordance with Actuarial Guidance Note GN11

Note 4 David Anderson and Stephan Pater were each paid a non-pensionable salary supplement of 16% of basic salary in lieu of pension provision

Note 5 John Reizenstein opted out of the occupational pension scheme in the previous year when he became entitled to a deferred pension under the PACE Scheme rules He was paid a non-pensionable salary supplement 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 figures

Note 6 Craig Shannon resigned as a Director on 20 August 2007 He became entitled to a deferred pension under the PACE Scheme rules when he left the Scheme on 28 July 2007 The deferred pension was augmented by payment of a contribution of £128,476 by the employer to the PACE Scheme in lieu of termination monies which would otherwise have been payable

Table 3 – Non-Executive Directors' Remuneration

Non Executive Directors	Date Appointed	Fee £'000 2007	Fee £'000 2006
Graham Bennett	1989	17	15
Simon Butler	2003	17	15
Terry Morton	2006	9	8
Kathryn Smith	2001	9	8
Len Wardle	2006	9	8
Martyn Wates (6)	2007	0	0
Stephen Watts	2006	9	8
Bob Burlton(1)	2004	21	0
Professional Non-Executive Directors			
Graham Stow	2003	51	46
David Davies	2003	55	51
Paul Hewitt (3)	2003	21	0
Tony Lancaster (4)	2004	18	46
Robert Newton (5)	2007	22	0
Piers Williamson	2005	48	46

Notes

(1) Up to 27 October 2007, Bob Burlton's fee was paid as a combined fee in respect of his position as Chair of Co-operative Group and was paid to his nominating Society – The Midcounties Co-operative With effect from 28 October 2007, he is remunerated by CFS for his position as CFS

(2) Martin Beaumont, Chief Executive of Co-operative Group served as Non-Executive Director of CFS and The Co-operative Bank being remunerated by Co-operative Group in respect of this appointment until his retirement on 31 July 2007

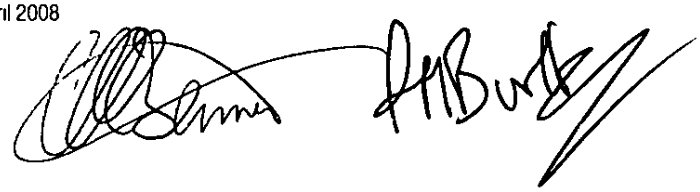
(3) Paul Hewitt was Deputy Chief Executive of Co-operative Group until 28 July 2007 and was remunerated by Co-operative Group in respect of his Non-Executive Director appointment With effect from 29 July 2007, he became a Professional Non-Executive Director and is remunerated by CFS

(4) Tony Lancaster retired on 13 June 2007

(5) Robert Newton was appointed as Non-Executive Director on 1 August 2007

(6) Martyn Wates, Chief Financial Officer of Co-operative Group was appointed as a Non-Executive Director of CFS on 13 November 2007 and is paid by Co-operative Group in respect of this appointment

By Order of the Board
Bob Burlton, Chair, CFS Remuneration & Appointments Committee
Graham Bennett, Chair, The Co-operative Bank
3 April 2008



Independent Auditor's report to the members of The Co-operative Bank p.l.c.

We have audited the Consolidated and Bank financial statements (the 'financial statements') of The Co-operative Bank p l c for the year ended 12 January 2008 which comprise the Consolidated Income Statement, the Consolidated and Bank Company Balance Sheets, the Consolidated and Bank Cash Flow Statements, the Consolidated and Bank Statements of Recognised Income and Expense and the related notes These financial statements have been prepared under the accounting policies set out therein

This report is made solely to the company's members, as a body, in accordance with section 235 of the Companies Act 1985 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 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

The directors' responsibilities for preparing the Annual Report and the financial statements in accordance with applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU, are set out in the Statement of Directors' Responsibilities on page 26

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland)

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985 and, as regards the Consolidated financial statements, Article 4 of the IAS Regulation We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements The information given in the Directors' Report includes that specific information presented in the Business and Financial Review that is cross referred from the Business Review section of the Directors' Report

In addition we report to you if, in our opinion, the Bank 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 other transactions is not disclosed

We review whether the Corporate Governance Statement reflects the Bank's compliance with the nine provisions of the 2006 Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the group's corporate governance procedures or its risk and control procedures

We read the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements Our responsibilities do not extend to any other information

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) 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 judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's and Bank'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

Auditors' report

Opinion

In our opinion

- the consolidated financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of the group's affairs as at 12 January 2008 and of its profit for the year then ended,
- the Bank financial statements give a true and fair view, in accordance with IFRSs as adopted by the EU, as applied in accordance with the provisions of the Companies Act 1985, of the state of the Bank's affairs as at 12 January 2008,
- the financial statements have been properly prepared in accordance with the Companies Act 1985 and, as regards the consolidated financial statements Article 4 of the IAS Regulation, and
- the information given in the Directors' Report is consistent with the financial statements

KPMG Audit Plc

KPMG Audit Plc
Chartered Accountants
Registered Auditor
St James Square
Manchester
M2 6DS
3 April 2008

	Notes	**Before significant items 2007**	**Significant items 2007**	**After significant items 2007**	Before significant items 2006	Significant items 2006	After significant items 2006
Interest and similar income		**800.0**	**–**	**800.0**	708 8	–	708 8
Interest expense and similar charges		**(465.2)**	**–**	**(465.2)**	(388 5)	–	(388 5)
Net interest income	4	**334 8**	**–**	**334 8**	320 3	–	320 3
Fee and commission income		**216.5**	**–**	**216.5**	232 1	–	232 1
Fee and commission expense		**(33 3)**	**–**	**(33.3)**	(33 8)	–	(33 8)
Net fee and commission income	5	**183.2**	**–**	**183 2**	198 3	–	198 3
Dividend income		**–**	**–**	**–**	0 1	–	0 1
Net trading income	6	**5.5**	**–**	**5 5**	2 8	–	2 8
Operating income		**523.5**	**–**	**523 5**	521 5	–	521 5
Operating expenses	7	**(339.3)**	**(38.0)**	**(377.3)**	(339 9)	109 2	(230 7)
Profit before impairment losses		**184.2**	**(38.0)**	**146 2**	181 6	109 2	290 8
Impairment losses on loans and advances	13	**(102.0)**	**–**	**(102.0)**	(105 3)	–	(105 3)
Impairment losses on structured investments	14	**(31 8)**	**–**	**(31.8)**	–	–	–
Operating profit		**50.4**	**(38.0)**	**12.4**	76 3	109 2	185 5
Profit based payments to members of the Co-operative Group		**(1.3)**	**–**	**(1.3)**	(1 2)	–	(1 2)
Profit before taxation		**49.1**	**(38 0)**	**11.1**	75 1	109 2	184 3
Income tax expense	9	**(16.6)**	**11 4**	**(5.2)**	(24 6)	(32 8)	(57 4)
Profit for the year		**32.5**	**(26.6)**	**5.9**	50 5	76 4	126 9
Attributable to							
Equity shareholders	10	**29.8**	**(26.6)**	**3.2**	48 3	75 1	123 4
Minority interests		**2 7**	**–**	**2.7**	2 2	1 3	3 5
		32.5	**(26 6)**	**5.9**	50 5	76 4	126 9
Earnings per share	11	**2.71p**	**(2.42)p**	**0.29p**	4 39p	6 83p	11 22p

2007 significant items relate to non-recurring expenditure associated with a Group programme of restructuring

2006 significant items relate to gains on implementation of PACE

Consolidated balance sheet

	Notes	2007	2006
Assets			
Cash and balances at central banks		**172.9**	186 9
Loans and advances to banks	12	**1,204.0**	1,367 0
Loans and advances to customers	13	**9,009 0**	8,147 6
Debt securities	14	**2,430 9**	2,753 1
Derivative financial instruments	15	**88.2**	84 4
Equity shares	16	**8 8**	1 7
Intangible fixed assets	17	**5.2**	7 2
Property, plant and equipment	18	**79.8**	93 8
Deferred tax assets	26	**-**	1 9
Other assets	19	**16.5**	44 1
Prepayments & accrued income		**71.6**	91 5
Total assets		**13,086 9**	12,779 2
Liabilities			
Deposits by banks	20	**661.3**	700 6
Customer accounts	21	**10,559.5**	9,544 3
Debt securities in issue	22	**535.8**	1,113 3
Derivative financial instruments	15	**92.3**	117 7
Other borrowed funds	23	**358.1**	387 8
Other liabilities	24	**103.8**	108 1
Accruals and deferred income		**37.5**	82 8
Provision for liabilities	25	**9 4**	6 8
Current tax liabilities		**6.1**	18 6
Deferred tax liabilities	26	**6.2**	-
Total liabilities		**12,370 0**	12,080 0
Capital and reserves attributable to the Bank's equity holders			
Ordinary share capital	28	**55 0**	55 0
Share premium account	28	**8.8**	8 8
Retained earnings	29	**627.6**	633 7
Other reserves	29	**(1 4)**	(22 7)
		690.0	674 8
Minority interests		**26.9**	24 4
Total equity		**716.9**	699 2
Total liabilities and equity		**13,086.9**	12,779 2

Approved by the Board on 3 April 2008 and signed on its behalf by

Graham Bennett, Chair
David Anderson, Chief Executive
Moira Lees, Secretary

The notes on pages 71 to 90 form part of these financial statements

	Notes	2007	2006
Assets			
Cash and balances at central banks		**172.9**	186 9
Loans and advances to banks	12	**1,211 2**	1,369 4
Loans and advances to customers	13	**8,914.4**	8,051 8
Debt securities	14	**1,985.7**	2,369 6
Derivative financial instruments	15	**88.5**	85 5
Equity shares	16	**8 8**	1 7
Shares in group undertakings	32	**2.7**	2 7
Intangible fixed assets	17	**4.3**	6 3
Property, plant and equipment	18	**74.0**	87 8
Deferred tax assets	26	**–**	8 3
Other assets	19	**16.4**	43 9
Prepayments & accrued income		**44.9**	79 3
Total assets		**12,523.8**	12,293 2
Liabilities			
Deposits by banks	20	**661.3**	700 6
Customer accounts	21	**10,068.1**	9,119 3
Debt securities in issue	22	**535 8**	1,113 3
Derivative financial instruments	15	**92.8**	118 0
Other borrowed funds	23	**358.1**	387 8
Other liabilities	24	**102 5**	106 9
Accruals and deferred income		**32.5**	75 3
Provision for liabilities	25	**8 8**	5 9
Current tax liabilities		**2.9**	16 5
Deferred tax liabilities	26	**0 7**	–
Total liabilities		**11,863 5**	11,643 6
Capital and reserves attributable to the Bank's equity holders			
Ordinary share capital	28	**55.0**	55 0
Share premium account	28	**8 8**	8 8
Retained earnings	29	**597 9**	608 3
Other reserves	29	**(1.4)**	(22 5)
Total equity		**660.3**	649 6
Total liabilities and equity		**12,523.8**	12,293 2

Approved by the Board on 3 April 2008 and signed on its behalf by

Graham Bennett, Chair
David Anderson, Chief Executive
Moira Lees, Secretary

The notes on pages 71 to 90 form part of these financial statements

Statement of recognised income and expense

	Group 2007	Group 2006	Bank 2007	Bank 2006
Effective portion of cash flow hedges transferred to equity	**20.3**	(29 1)	**19.7**	(28 2)
Cash flow hedges transferred to profit or loss	**(0.5)**	(0 1)	**(0.5)**	(0 1)
Available for sale investments				
Valuation gains/losses taken to equity	**2.4**	(7 0)	**2.1**	(6 7)
Valuation gains/losses transferred to profit or loss on sale	**(0.2)**	0 6	**(0.2)**	0 6
Net movement in pension fund deficit due to actuarial gains and losses	**(0.3)**	(13 6)	**(0.3)**	(13 3)
Net income and expense recognised directly in equity	**21.7**	**(49.2)**	**20 8**	**(47.7)**
Net profit/(loss) – equity shareholders	**3.2**	123 4	**(1 1)**	119 0
Net profit – minority interests	**2.7**	3 5	–	–
Total recognised income and expense for the year	**27.6**	**77 7**	**19 7**	**71.3**
Total recognised income and expense for the year is attributable to				
Equity shareholders	**24.2**	75 3	**19.7**	71 3
Minority interests	**3.4**	2 4	–	–
	27 6	**77.7**	**19.7**	**71.3**

Amounts shown above are net of tax

The notes on pages 71 to 90 form part of these financial statements

Consolidated cash flow statement

	2007	2006
Cash flows from operating activities		
Profit before taxation	**11.1**	184 3
Adjustments for		
– Decrease/(Increase) in prepayments and accrued income	**19.9**	(15 9)
– Decrease in accruals and deferred income	**(37.4)**	(1 8)
– Interest payable in respect of subordinated liabilities	**19.5**	18 4
– Effect of exchange rate movements	**(5.2)**	(5 0)
– Effect of non-cash pension costs	**0.1**	(108 5)
– Impairment losses on loans and advances	**102.0**	105 4
– Impairment losses on structured investments	**31.8**	–
– Depreciation and amortisation	**22.7**	24 4
– Interest amortisation	**(4.6)**	(0 2)
– Amortisation of investments	**(1.0)**	0 1
– Loss on sale of investments	**0.3**	0 8
– Loss on disposal of fixed assets	**7.4**	1 8
– Preference dividend	**5.6**	5 6
	172.2	**209.4**
(Decrease)/Increase in deposits by banks	**(53 7)**	146 1
Increase in customer accounts	**1,015.2**	725 5
(Decrease)/Increase in debt securities in issue	**(577 5)**	63 1
Decrease in loans and advances to banks	**145.0**	80 0
Increase in loans and advances to customers	**(958 9)**	(328 9)
Net movement of other assets and other liabilities	**26.2**	(27 3)
Income tax paid	**(19.1)**	(22 9)
Net cash flows from operating activities	**(250.6)**	**845.0**
Cash flows from investing activities		
Purchase of property, equipment and software	**(19.0)**	(41 3)
Proceeds from sale of property and equipment	**0.6**	8 1
Purchase of debt securities	**(10,304.5)**	(7,265 5)
Proceeds from sale and maturity of debt securities	**11,108.6**	6,791 3
Net cash flows from investing activities	**785.7**	**(507.4)**
Cash flows from financing activities		
Interest paid in respect of subordinated loanstock	**(19.3)**	(17 9)
Repayment of subordinated loanstock	**(30.0)**	(100 0)
Issue of subordinated loanstock	**-**	150 0
Ordinary share dividends paid	**(9.0)**	(4 2)
Preference dividends paid	**(5.6)**	(5 6)
Dividends paid to minority shareholders in subsidiary undertaking	**(0.9)**	(0 9)
Net cash flows from financing activities	**(64 8)**	**21 4**
Increase in cash and cash equivalents	**470.3**	**359.0**
Cash and cash equivalents at the beginning of the year	**1,599.9**	1,240 9
Cash and cash equivalents at the end of year	**2,070.2**	1,599 9
Cash and balances with central banks	**172.9**	186 9
Loans and advances to banks (note 12)	**1,204.0**	1,222 0
Short term investments (note 14)	**693.3**	191 0
	2,070 2	**1,599.9**

The notes on pages 71 to 90 form part of these financial statements

Bank cash flow statement

	2007	2006
Cash flows from operating activities		
Profit before taxation	**1.0**	172 5
Adjustments for		
– Decrease/(Increase) in prepayments and accrued income	**34.4**	(15 3)
– (Decrease)/Increase in accruals and deferred income	**(35.6)**	2 2
– Interest payable in respect of subordinated liabilities	**19 5**	18 4
– Effect of exchange rate movements	**(5 2)**	(5 0)
– Effect of non-cash pension costs	**0.1**	(105 9)
– Impairment losses on loans and advances	**102.0**	105 5
– Impairment losses on structured investments	**31 8**	–
– Depreciation and amortisation	**22 0**	24 0
– Interest amortisation	**(4 5)**	(0 1)
– Amortisation of investments	**(1.0)**	0 1
– Loss on sale of investments	**0 3**	0 8
– Loss on disposal of fixed assets	**7.4**	1 8
– Preference dividend	**5.6**	5 6
	177.8	**204.6**
(Decrease)/Increase in deposits by banks	**(53 7)**	139 5
Increase in customer accounts	**948 8**	727 8
(Decrease)/Increase in debt securities in issue	**(577.5)**	63 1
Decrease in loans and advances to banks	**145 0**	80 0
Increase in loans and advances to customers	**(960.0)**	(349 4)
Net movement of other assets and other liabilities	**26.9**	(28 3)
Income tax paid	**(16.0)**	(19 7)
Net cash flows from operating activities	**(308.7)**	**817.6**
Cash flows from investing activities		
Purchase of property, equipment and software	**(18.5)**	(40 2)
Proceeds from sale of property and equipment	**0.6**	8 1
Purchase of debt securities	**(9,387.4)**	(6,530 5)
Proceeds from sale and maturity of debt securities	**10,252.7**	6,083 8
Net cash flows from investing activities	**847 4**	**(478.8)**
Cash flows from financing activities		
Interest paid in respect of subordinated loanstock	**(19.3)**	(17 9)
Repayment of subordinated loanstock	**(30 0)**	(100 0)
Issue of subordinated loanstock	**–**	150 0
Ordinary share dividends paid	**(9.0)**	(4 2)
Preference dividends paid	**(5.6)**	(5 6)
Dividends from associated undertakings	**0.3**	0 3
Net cash flows from financing activities	**(63.6)**	**22.6**
Increase in cash and cash equivalents	**475.1**	**361.4**
Cash and cash equivalents at the beginning of the year	**1,602 3**	1,240 9
Cash and cash equivalents at the end of year	**2,077.4**	1,602 3
Cash and balances with central banks	**172.9**	186 9
Loans and advances to banks (note 12)	**1,211 2**	1,224 4
Short term investments (note 14)	**693.3**	191 0
	2,077.4	**1,602.3**

The notes on pages 71 to 90 form part of these financial statements

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 IFRS as adopted by the EU ('Adopted IFRS') On including the parent company financial statements here together with the group financial statements, the company is taking advantage of the exemption in S230 of the Companies Act 1985 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 effective at 12 January 2008

In preparing these consolidated financial statements, the Bank has adopted IFRS 7 *Financial Instruments Disclosure* and IAS 1 *Presentation of Financial Statements – Capital Disclosures* The adoption of IFRS 7 and the amendment to IAS 1 impacted the type and amount of disclosures made in these financial statements, but had no impact on the reported profits or financial position of the Group In accordance with the transitional requirements of the standards, the Bank has provided full comparative information

Standards and interpretations issued but not yet effective
The Group has not adopted the following standard

- IFRS 8 *Operating Segments*

This standard introduces the 'management approach' to segment reporting IFRS 8 will require the disclosure of segment information based on the internal reports regularly reviewed by the Group's Chief Operating Decision Maker in order to assess each segment's performance and to allocate resources to them

The Group is not expecting the standard to have an impact on the segmental information reported in the financial statements

The amendments are effective for accounting periods on or after 1 January 2009

Accounting date
The financial statements of the Bank and the Group relate to the 52 weeks to 12 January 2008 Since the Bank and Group accounting date is virtually coterminous with the calendar year 2007, figures in respect of the financial year are headed 2007 and the corresponding amounts for the 52 weeks to 13 January 2007 are headed 2006

Accounting policies
(a) Revenue recognition
Interest income
Interest income is 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 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 future credit losses
Fees and commissions
Unless included in the effective interest calculation, fees and commissions are recognised on an accruals basis as the service is provided
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

(b) Financial instruments (excluding derivatives)
The Bank classifies its financial assets (excluding derivatives) as either
- Loans and receivables,
- Available for sale, or
- Financial assets at fair value through profit or loss

No assets are classified as held-to-maturity On the application of IFRS7, Financial Instruments Disclosures the Bank has not reclassified between valuation methodologies during the year
The Group measures all of its financial liabilities at amortised cost, other than those within the wholesale trading portfolio which are measured at fair value through profit or loss

i) Loans and receivables
Loans and advances to customers and banks (except for specific assets designated at fair value through profit or loss – see below), are measured at amortised cost, being the amount advanced plus any unpaid interest, commissions and fees charged to the customer less amounts repaid or written off, less impairment provisions for incurred losses and adjusted for the cumulative amortisation arising from effective interest rate adjustments Effective interest rate adjustments arise when future cash flows are discounted through the expected life of the financial instrument

ii) Available for sale
Available for sale financial assets are non-traded investment securities, intended to be held for an indefinite period of time These are measured at fair value with movements in the carrying value brought into equity as they arise, except for changes in value arising from impairment and foreign exchange

gains and losses on monetary items which are recognised in the income statement On disposal, gains and losses recognised previously in equity are transferred to the income statement

iii) Financial assets at fair value through profit or loss

These are either

- Acquired or incurred principally for the purpose of selling or repurchasing in the near term, or
- 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 profit or loss to eliminate or significantly reduce a measurement or recognition inconsistency

These are measured at fair value with movements in the carrying value brought into the income statement within interest income as they arise

Impairment provision

At the balance sheet date, the Bank assesses its financial assets (including loans and advances to customers) for objective evidence that an impairment loss has been incurred

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)

The amount of the impairment loss 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

The written down value of the impaired financial assets is compounded back to the net realisable balance over time using the original effective interest rate This is reported through interest and similar income within the income statement and represents the unwind of the discount

A write-off is made when all or part of a claim is deemed uncollectible or forgiven Write-offs are charged against previously established provisions for impairment or directly to the income statement

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

Impairment losses on available for sale assets are recognised by transferring the difference between the amortised cost and current fair value out of equity to profit or loss When a subsequent event causes the amount of impairment loss on an available-for-sale debt security to decrease, the impairment loss is reversed through profit or loss

(c) 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

(d) 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

Derivative financial instruments are stated at fair value The gain or loss on remeasurement to fair value is recognised immediately in the income statement except where derivatives qualify for cash flow hedge accounting

Embedded derivatives A derivative may be embedded in another financial 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, 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 policy for that class of financial instrument

Cash flow 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 broken or the hedge becomes ineffective, the cumulative unrealised gain or loss remaining in equity continues to be held in equity, and is transferred to the income statement only when the forecast transaction is recognised

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

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

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

(e) Property, plant and equipment

Items of property, plant and equipment are stated at cost less any accumulated depreciation

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 5 per cent per annum

Short leasehold buildings	life of lease
Equipment	10 to 33 3 per cent per annum
Vehicles	25 per cent per annum

All items of property, plant and equipment are regularly reviewed for indications of impairment Any impairment identified would be charged to the income statement

(f) Intangible assets – *Computer software*

Costs incurred 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, which is generally 3 years

(g) Assets leased to customers – *Finance leases*

Assets leased to customers are included within 'loans and advances to customers' and valued at an amount equal to the net investment in the lease, less any provisions for impairment

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

(h) Cash and cash equivalents

Cash and cash equivalents comprises cash balances and balances with an original maturity of three months or less which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value

(i) Income tax expense

Income tax expense comprises current and deferred tax Income tax expense 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 equity

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

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

(j) Pension costs

Defined benefit basis

Prior to 5 April 2006, the Group operated a defined benefit pension scheme

The group net obligation in respect of defined benefit pension plans is calculated by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods The benefit is discounted to determine its present value and the fair value of any plan assets is deducted

The discount rate used is the market yield on high quality corporate bonds at the balance sheet date that have maturity dates approximating to the terms of the Group's obligation The calculation is performed by a qualified actuary using the projected unit credit method

The Group recognises actuarial gains and losses through equity

The charge to the income statement includes current service costs, past service cost, the interest cost of the scheme liabilities and the expected return on scheme assets

Defined contribution basis

Subsequent to 5 April 2006, the Group has accounted for pension costs on a defined contribution basis Obligations for contributions are recognised as an expense in the income statement as incurred

(k) Exchange rates

Balances in foreign currencies are expressed in £ sterling at the rate ruling at the balance sheet date All exchange differences are dealt with in the income statement

(l) Borrowed funds

Borrowings are recognised initially at issue proceeds net of transaction costs incurred

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's preference shares are classified as financial liabilities and are 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

(m) Insurance contracts

All financial guarantees in respect of intra-group funding between the Bank and its subsidiaries are treated as insurance contracts in accordance with IFRS 4

Risk management

Risk management framework

The CFS group of companies including Co-operative Financial Services Limited, Co-operative Insurance Society Limited, CIS General Insurance Limited and Co-operative Bank p l c have a common Board composition

The Board sub-committees also work on a CFS-wide basis, with the same committee structure supporting each Board within the CFS group

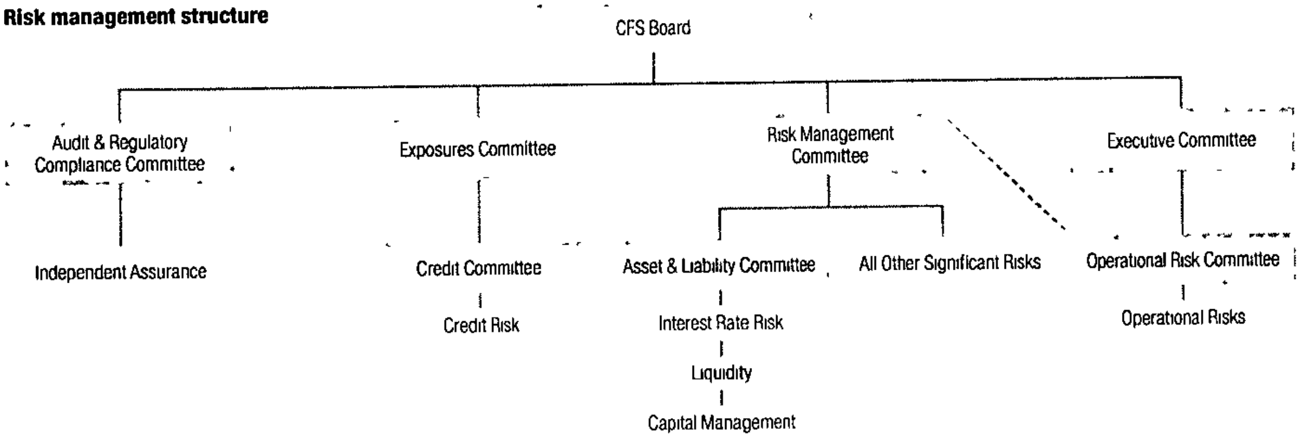
The CFS Board has ultimate responsibility for the management of all risks across CFS

The Board is responsible for approving the Bank's 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 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



CFS Risk Management Committee (RMC): this committee is the most senior forum within the organisation that focuses in depth on risk management activity It reviews and challenges risk management information and processes, approving risk policy and credit models and setting standards

CFS Audit & Regulatory Compliance Committee (ARCC)· this committee provides independent oversight in relation to financial reporting, internal control and risk management, regulatory compliance, external audit and internal audit

CFS Exposures Committee. this committee ensures that non-executive directors are actively involved in major credit decisions (including sanctioning large counterparty transactions) and monitoring large exposures

CFS Credit Committee: this committee is chaired by the Director of Banking Risk and Capital Management The Chair has delegated authority for approving credit facilities within approved strategies and delegated authorities

CFS Shareholder Asset & Liability Committee (ALCO): this committee is chaired by the Chief Executive It is primarily responsible for overseeing the management of interest rate, market, liquidity and funding risks and to advise on the composition and sourcing of adequate capital

CFS Executive Committee· this committee manages the business in line with the Board Risk Appetite Statement It also maintains oversight of risk management processes and management information

CFS Operational Risk Committee· this committee is chaired by the Head of 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 Each division within CFS is represented on the committee

Bank Significant Risks

The Bank's significant risks arise in four broad categories

- Credit risk
- Market risk
- Liquidity risk
- Operational risk

Credit risk

Credit risk arises from the possibility of customers and counterparties failing to meet their obligations to the Bank

The Credit Risk Management Policies are approved by the Board annually and determine the criteria for the management of personal, corporate and wholesale market exposures They specify credit management standards, including country, sector and counterparty limits, along with delegated authorities Larger corporate facilities are sanctioned by the Board's Exposures Committee who also review, each month, facilities granted within the Chief Executive's discretion

The Bank's Personal Lending 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 Personal lending is tightly controlled through advanced credit and behavioural scoring techniques administered by a specialist department The Risk Management Committee receives regular reports on the performance of the portfolio

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 Exposures Committee receives regular reports on new facilities and changes in facilities, sector exposures, bad debt provisions and the realisation of problem loans

Credit policy for wholesale market counterparties involves establishing limits for each of these counterparties based on their financial strength and credit rating Counterparty limits are largely uncommitted All counterparties are reviewed at least annually by the Financial Institutions Credit Team and the counterparty list is also reviewed annually by the Exposures Committee

Credit exposure

Group	Notes	**Gross balance 2007**	**Credit commitments 2007**	**Credit risk exposure 2007**	Gross balance 2006	Credit commitments 2006	Credit risk exposure 2006
Loans and advances to banks	12	**1,204.0**	**226.3**	**1,430.3**	1,367 0	50 8	1,417 8
Loans and advances to customers	13	**9,169 7**	**6,236.3**	**15,406.0**	8,302 9	5,840 7	14,143 6
Debt securities	14	**2,462.7**	**–**	**2,462.7**	2,753 1	–	2,753 1
Derivative financial instruments	15	**88.2**	**–**	**88.2**	84 4	–	84 4
		12,924.6	**6,462 6**	**19,387.2**	**12,507.4**	**5,891.5**	**18,398 9**
Allowance for impairment losses on loans and advances	13			**(160 7)**			(155 3)
Allowance for impairment losses on structured investments	14			**(31.8)**			–
Carrying amount				**19,194.7**			18,243 6

Bank	Notes	**Gross balance 2007**	**Credit commitments 2007**	**Credit risk exposure 2007**	Gross balance 2006	Credit commitments 2006	Credit risk exposure 2006
Loans and advances to banks	12	**1,211 2**	**226.3**	**1,437.5**	1,369 4	50 8	1,420 2
Loans and advances to customers	13	**9,075 1**	**6,225.7**	**15,300.8**	8,207 1	5,827 5	14,034 6
Debt securities	14	**2,017.5**	**–**	**2,017 5**	2,369 6	–	2,369 6
Derivative financial instruments	15	**88 5**	**–**	**88.5**	85 5	–	85 5
		12,392 3	**6,452.0**	**18,844.3**	**12,031.6**	**5,878.3**	**17,909.9**
Allowance for impairment losses on loans and advances	13			**(160.7)**			(155 3)
Allowance for impairment losses on structured investments	14			**(31 8)**			–
Carrying amounts				**18,651 8**			17,754 6

Credit risk analysis:
2007

Group	Loans and advances to banks	Loans and advances to customers	Debt securities	Derivative financial instruments	Total
Individually impaired					
90 days past due or evidence of impairment	–	94.6	63.2	–	157.8
Allowance for impairment	–	(35.6)	(31.8)	–	(67.4)
Carrying amount	–	59 0	31.4	–	90.4
Collectively impaired					
Less than 90 days past due	–	75.9	–	–	75.9
90-179 days past due	–	29.3	–	–	29.3
180 days plus past due	–	102.9	–	–	102.9
Allowance for impairment	–	(125 1)	–	–	(125 1)
Carrying amount	–	83.0	–	–	83.0
Past due but not impaired					
0-30 days	–	7.3	–	–	7.3
30-60 days	–	2.1	–	–	2.1
60-90 days	–	1 5	–	–	1 5
Carrying amount	–	10.9	–	–	10.9
Watchlist	–	93.0	–	–	93 0
Neither past due or impaired					
Low to medium risk	1,430.3	12,984.2	2,399.5	88.2	16,902.2
Medium to high risk	–	2,015.2	–	–	2,015.2
Carrying amount	1,430.3	14,999.4	2,399.5	88.2	18,917.4
Total carrying amount	1,430.3	15,245 3	2,430 9	88.2	19,194.7

2006

Group	Loans and advances to banks	Loans and advances to customers	Debt securities	Derivative financial instruments	Total
Individually impaired					
90 days past due or evidence of impairment	–	80 8	–	–	80 8
Allowance for impairment	–	(27 5)	–	–	(27 5)
Carrying amount	–	53 3	–	–	53 3
Collectively impaired					
Less than 90 days past due	–	83 0	–	–	83 0
90-179 days past due	–	42 9	–	–	42 9
180 days plus past due	–	96 3	–	–	96 3
Allowance for impairment	–	(127 8)	–	–	(127 8)
Carrying amount	–	94 4	–	–	94 4
Past due but not impaired					
0-30 days	–	7 3	–	–	7 3
30-60 days	–	3 6	–	–	3 6
60-90 days	–	2 4	–	–	2 4
Carrying amount	–	13 3	–	–	13 3
Watchlist	–	165 0	–	–	165 0
Neither past due or impaired					
Low to medium risk	1,413 5	11,173 3	2,753 1	84 4	15,424 3
Medium to high risk	4 3	2,489 0	–	–	2,493 3
Carrying amount	1,417 8	13,662 3	2,753 1	84 4	17,917 6
Total carrying amount	1,417.8	13,988.3	2,753.1	84 4	18,243.6

2007 Bank	Loans and advances to banks	Loans and advances to customers	Debt securities	Derivative financial instruments	Total
Individually impaired					
90 days past due or evidence of impairment	–	94.6	63.2	–	157.8
Allowance for impairment	–	(35.6)	(31.8)	–	(67.4)
Carrying amount	–	59 0	31.4	–	90.4
Collectively impaired					
Less than 90 days past due	–	75.9	–	–	75.9
90-179 days past due	–	29.3	–	–	29.3
180 days plus past due	–	102.9	–	–	102.9
Allowance for impairment	–	(125 1)	–	–	(125.1)
Carrying amount	–	83 0	–	–	83.0
Past due but not impaired					
0-30 days	–	7.3	–	–	7.3
30-60 days	–	2.1	–	–	2.1
60-90 days	–	1.5	–	–	1.5
Carrying amount	–	10.9	–	–	10.9
Watchlist	–	89.5	–	–	89.5
Neither past due or impaired					
Low to medium risk	1,437 5	12,882 5	1,954.3	88.5	16,362.8
Medium to high risk	–	2,015.2	–	–	2,015.2
Carrying amount	1,437.5	14,897.7	1,954 3	88.5	18,378 0
Total carrying amount	1,437.5	15,140.1	1,985 7	88.5	18,651 8

2006 Bank	Loans and advances to banks	Loans and advances to customers	Debt securities	Derivative financial instruments	Total
Individually impaired					
90 days past due or evidence of impairment	–	80 8	–	–	80 8
Allowance for impairment	–	(27 5)	–	–	(27 5)
Carrying amount	–	53 3	–	–	53 3
Collectively impaired					
Less than 90 days past due	–	83 0	–	–	83 0
90-179 days past due	–	42 9	–	–	42 9
180 days plus past due	–	96 3	–	–	96 3
Allowance for impairment	–	(127 8)	–	–	(127 8)
Carrying amount	–	94 4	–	–	94 4
Past due but not impaired					
0-30 days	–	6 7	–	–	6 7
30-60 days	–	3 6	–	–	3 6
60-90 days	–	2 4	–	–	2 4
Carrying amount	–	12 7	–	–	12 7
Watchlist	–	159 1	–	–	159 1
Neither past due or impaired					
Low to medium risk	1,415 9	11,070 8	2,369 6	85 5	14,941 8
Medium to high risk	4 3	2,489 0	–	–	2,493 3
Carrying amount	1,420 2	13,559 8	2 369 6	85 5	17,435 1
Total carrying amount	1,420.2	13,879 3	2,369 6	85.5	17,754.6

Analysis of impaired assets and associated collateral
Description of collateral
Corporate loans and Retail Mortgage lending with evidence of impairment including 90 days past due are individually assessed for impairment

Collectively impaired assets include unsecured retail lending balances Provisions are applied to credit card balances at 30 days past due and at 45 days past due to all other unsecured retail lending balances

Past due but not impaired represents mortgage and unsecured retail lending balances past due but not considered impaired This includes credit card exposures less than 30 days and 45 days for other retail unsecured lending

Watchlist represents corporate accounts indentified for closer management although not necessarily in arrears

Low to medium risk has been defined as exposures where probability of default (PD) is 1% or below over a 1 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 as a probability of default of greater than 1% over a 1 year time horizon for exposure on IRB Approach under Basel II and slotting category weak for specialised lending exposures under the slotting approach

No loans which would otherwise be presented as past due or impaired are excluded as a result of renegotiation

Within the Treasury debt security portfolio over 90% of exposures have an external credit rating equivalent to Fitch A or above The Bank has no direct exposure to Asset Backed Securities (ABS) It is only indirectly exposed within the portfolios held by the £31 4m (net of provision) holding of Structured Investments

Within Loans and advances to customers collateral is held in the form of the residential mortgages for personal customers and collateral for corporate lending is largely in the form of residential and commercial property The latter is recognised in numerous ways such as security for property development or investment customers (i e 'property' lending) or owner occupied premises to secure mainstream loan and overdraft facilities Other security taken, but only in modest proportion to the total portfolio, includes life policies, stocks & shares, cash cover and debentures / floating charges Where exposures are agreed on a secured basis, security cover is recognised only where

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

any shortfall of security for an exposure is generally regarded as unsecured and assessment includes this element of residual risk

Collateral is not generally held against loans and advances to banks except as part of reverse repurchase agreements Collateral is not held against investment securities

At the reporting date the fair value of collateral as security against financial assets that are past due but not impaired was £21 9m (2006 - £21 0m Group and Bank)
At the reporting date the fair value of collateral as security against individually impaired financial assets was £44 3m (2006 - £41 9m Group and Bank)
At the reporting date the carrying value of assets obtained by taking possession of collateral or by calling on guarantees was £2 0m (2006 - £1 1m Group and Bank)

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 inter-bank business and proprietary trading The majority of the risk arises from changes in interest rates as the Bank does not trade in equities or commodities and has limited foreign currency activities

Interest rate risk policy statements, approved by the CFS Risk Management Committee on behalf of the Board, specify the scope of the Bank's wholesale market activity, market risk limits and delegated authorities The policy is executed by the Bank's ALCO ALCO meets monthly and its prime task is to assess the interest rate risk inherent in the maturity and re-pricing characteristics of the Bank's assets and liabilities It sets limits within which Treasury and the CFS' Shareholder Capital & Interest Rate Risk department manages the effect of interest rate changes on the Bank's overall net interest income The principal analytical techniques involve assessing the impact of different interest rate scenarios and changes in balances over various time periods

The table below illustrates the sensitivity analysis relating to Bank's non–trading book (excluding Treasury) prepared by CFS' Shareholder Capital & Interest Rate Risk department, a primary measure in the approach to managing interest rate risk

Interest rate risk is primarily managed through assessing the sensitivity of the Banks non-trading book to standard and non-standard interest rate scenarios The Board has established a limit of a variance of less than 2% of net interest income over the next twelve months to be at risk to a 100bp rise and fall in all yield curve rates, assuming the external rate on all retail products changes to maintain constant margins

Percentage change in net interest income over next 12 months based on 100bp shock in interest rates

2007	**100bp parallel increase**	**100bp parallel decrease**
At the year end	(0 6%)	0 5%
Average for the period	(0 9%)	0 9%
Maximum for the period	(1 3%)	1 4%
Minimum for the period	(0 6%)	0 5%
2006		
At the year end	(0 9%)	0 9%
Average for the period	(0 5%)	0 3%
Maximum for the period	(0 8%)	0 8%
Minimum for the period	(0 1%)	(0 5%)

The table shows the estimated charge in net interest income over the next 12 month period to a 1% shock in interest rates across the yield curve for Co-operative Bank Group excluding Treasury

Treasury executes 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 re-pricing and maturity mismatches as a common unit of measurement Value at Risk (VaR) measures the daily maximum potential gain or loss due to recent market volatility to a statistical confidence level of 95% and a one day holding period 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 by the Bank as the sole measure of risk

The Board receive quarterly 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
PV01 is used as an additional risk measure to supplement VaR This risk measure is based upon a full revaluation and indicates the change in value of a fixed income product, or portfolio, given a 1 basis point movement in interest rates A number of different scenarios including +/– 10bp, 100bp are also calculated PV100 is provided below

Trading value at risk
At 12 January 2008, total Treasury VaR of **£0 5 million** (2006 £1 4 million) represents the maximum potential daily gain or loss in market rates within a confidence level of 95% based on recent market performance The average, highest and lowest VaR, as calculated on a daily basis, for the accounting year ended 12 January 2008 were **£0.7 million** (2006 £0 6million) **£1 4 million** (2006 £1 4million) and **£0.4 million** (2006 £0 3million)

PV100
The table below illustrates the change in valuation on a fixed income portfolio experienced given a 1% increase and decrease in interest rates for Treasury

	1% increase in interest rates		**1% decrease in interest rates**	
	2007	2006	**2007**	2006
At reporting date	**(4.4)**	(16 1)	**4 4**	17 2
Average in the period	**(11.8)**	(12 9)	**14 1**	17 7
Maximum	**(16.9)**	(17 9)	**21.4**	25 8
Minimum	**(4.4)**	(7 5)	**4 4**	11 7

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 dollars by raising funds and investing these to generate a return, and
- performing limited intra-day 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	£ 2007	$ 2007	€ 2007	Other 2007	Total 2007	£ 2006	$ 2006	€ 2006	Other 2006	Total 2006
Assets										
Cash and balances at central banks	**171 1**	**–**	**1.8**	**–**	**172.9**	185 4	–	1 5	–	186 9
Loans and advances to banks	**1,154.9**	**37 3**	**9.7**	**2.1**	**1,204 0**	1,068 7	296 0	0 5	1 8	1,367 0
Loans and advances to customers	**8,685.9**	**159.6**	**152.1**	**11.4**	**9,009.0**	8,024 9	64 9	45 8	12 0	8,147 6
Debt securities	**2,052.2**	**173.2**	**205.5**	**–**	**2,430 9**	2,094 7	563 1	95 3	–	2,753 1
Derivative financial instruments	**88.2**	**–**	**–**	**–**	**88 2**	84 0	0 3	0 1	–	84 4
Equity shares	**8.8**	**–**	**–**	**–**	**8.8**	1 7	–	–	–	1 7
Intangible fixed assets	**5.2**	**–**	**–**	**–**	**5.2**	7 2	–	–	–	7 2
Property, plant and equipment	**79 8**	**–**	**–**	**–**	**79.8**	93 8	–	–	–	93 8
Deferred tax assets	**–**	**–**	**–**	**–**	**–**	1 9	–	–	–	1 9
Other assets	**11.8**	**1.9**	**2 6**	**0 2**	**16.5**	28 9	14 1	1 0	0 1	44 1
Prepayments & accrued income	**71.6**	**–**	**–**	**–**	**71.6**	91 5	–	–	–	91 5
Total assets	**12,329 5**	**372.0**	**371.7**	**13.7**	**13,086 9**	**11,682 7**	**938.4**	**144.2**	**13.9**	**12,779.2**

Group	£ 2007	$ 2007	€ 2007	Other 2007	Total 2007	£ 2006	$ 2006	€ 2006	Other 2006	Total 2006
Liabilities										
Deposits by banks	**420.7**	**106.4**	**134.2**	**–**	**661.3**	440 7	168 6	91 3	–	700 6
Customer accounts	**10,504.5**	**24.4**	**27.8**	**2.8**	**10,559.5**	9,497 8	25 6	19 1	1 8	9,544 3
Debt securities in issue	**90.9**	**234 4**	**210.5**	**–**	**535.8**	342 9	737 6	32 8	–	1,113 3
Derivative financial instruments	**68.2**	**13.2**	**10 9**	**–**	**92.3**	117 3	0 4	–	–	117 7
Other borrowed funds	**358.1**	**–**	**–**	**–**	**358.1**	387 8	–	–	–	387 8
Other liabilities	**100.7**	**2.2**	**0.9**	**–**	**103.8**	101 2	6 5	0 4	–	108 1
Accruals and deferred income	**37.5**	**–**	**–**	**–**	**37.5**	82 8	–	–	–	82 8
Provisions	**9 4**	**–**	**–**	**–**	**9.4**	6 8	–	–	–	6 8
Current tax liabilities	**6.1**	**–**	**–**	**–**	**6 1**	18 6	–	–	–	18 6
Deferred tax liabilities	**6.2**	**–**	**–**	**–**	**6.2**	–	–	–	–	–
Total liabilities	**11,602.3**	**380.6**	**384.3**	**2 8**	**12,370.0**	**10,995.9**	**938.7**	**143 6**	**1.8**	**12,080.0**
Net on-balance sheet position	**727.2**	**(8.6)**	**(12.6)**	**10.9**	**716.9**	**686.8**	**(0 3)**	**0.6**	**12.1**	**699.2**

Bank	£ 2007	$ 2007	€ 2007	Other 2007	Total 2007	£ 2006	$ 2006	€ 2006	Other 2006	Total 2006
Assets										
Cash and balances at central banks	**171.1**	**–**	**1.8**	**–**	**172.9**	185 4	–	1 5	–	186 9
Loans and advances to banks	**1,162.1**	**37.3**	**9 7**	**2 1**	**1,211 2**	1,071 1	296 0	0 5	1 8	1,369 4
Loans and advances to customers	**8,591.3**	**159 6**	**152.1**	**11 4**	**8,914.4**	7,929 1	64 9	45 8	12 0	8,051 8
Debt securities	**1,607 0**	**173.2**	**205 5**	**–**	**1,985 7**	1,711 2	563 1	95 3	–	2,369 6
Derivative financial instruments	**88 5**	**–**	**–**	**–**	**88 5**	85 1	0 3	0 1	–	85 5
Equity shares	**8.8**	**–**	**–**	**–**	**8.8**	1 7	–	–	–	1 7
Interests in group undertakings	**2.7**	**–**	**–**	**–**	**2.7**	2 7	–	–	–	2 7
Intangible fixed assets	**4.3**	**–**	**–**	**–**	**4.3**	6 3	–	–	–	6 3
Property, plant and equipment	**74.0**	**–**	**–**	**–**	**74.0**	87 8	–	–	–	87 8
Deferred tax assets	**–**	**–**	**–**	**–**	**–**	8 3	–	–	–	8 3
Other assets	**11.7**	**1.9**	**2.6**	**0.2**	**16.4**	28 7	14 1	1 0	0 1	43 9
Prepayments & accrued income	**44.9**	**–**	**–**	**–**	**44.9**	79 3	–	–	–	79 3
Total assets	**11,766.4**	**372.0**	**371.7**	**13.7**	**12,523.8**	**11,196 7**	**938.4**	**144 2**	**13.9**	**12,293.2**

Bank	£ 2007	$ 2007	€ 2007	Other 2007	Total 2007	£ 2006	$ 2006	€ 2006	Other 2006	Total 2006
Liabilities										
Deposits by banks	**420.7**	**106.4**	**134.2**	**–**	**661.3**	440 7	168 6	91 3	–	700 6
Customer accounts	**10,013 1**	**24.4**	**27 8**	**2 8**	**10,068.1**	9,072 8	25 6	19 1	1 8	9,119 3
Debt securities in issue	**90.9**	**234.4**	**210 5**	**–**	**535 8**	342 9	737 6	32 8	–	1,113 3
Derivative financial instruments	**68.7**	**13.2**	**10.9**	**–**	**92.8**	117 6	0 4	–	–	118 0
Other borrowed funds	**358 1**	**–**	**–**	**–**	**358.1**	387 8	–	–	–	387 8
Other liabilities	**99.4**	**2.2**	**0.9**	**–**	**102.5**	100 0	6 5	0 4	–	106 9
Accruals and deferred income	**32.5**	**–**	**–**	**–**	**32 5**	75 3	–	–	–	75 3
Provisions	**8.8**	**–**	**–**	**–**	**8.8**	5 9	–	–	–	5 9
Current tax liabilities	**2.9**	**–**	**–**	**–**	**2.9**	16 5	–	–	–	16 5
Deferred tax liabilities	**0 7**	**–**	**–**	**–**	**0.7**	–	–	–	–	–
Total liabilities	**11,095.8**	**380.6**	**384.3**	**2.8**	**11,863.5**	**10,559.5**	**938.7**	**143.6**	**1.8**	**11,643.6**
Net on-balance sheet position	**670.6**	**(8.6)**	**(12.6)**	**10 9**	**660 3**	**637 2**	**(0 3)**	**0.6**	**12.1**	**649.6**

At 12 January 2008 the Group's open position, including off-balance sheet positions, was **£2 9 million** (2006 £1 2 million) representing a potential loss of **£0.1 million** given a 3% appreciation in sterling (2006 loss of £0 04 million given a 3% appreciation in sterling)

All figures are in £ sterling equivalent

Interest rate risk

Interest rate sensitivity gap

The table below summarises the repricing periods for the assets and liabilities Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date

2007

Group	Within 3 months	Over 3 months but within 6 months	Over 6 months but within 1 year	Over 1 year but within 5 years	More than 5 years	Non-interest bearing	Trading book	Total
Assets								
Loans and advances to banks	**1,192.8**	**–**	**–**	**–**	**–**	**11 2**	**–**	**1,204.0**
Loans and advances to customers	**6,386 9**	**278.0**	**491 2**	**1,537.4**	**315.5**	**–**	**–**	**9,009.0**
Debt securities and equity shares	**1,727.8**	**350 2**	**125 4**	**219 9**	**7.6**	**8.8**	**–**	**2,439.7**
Other assets	**173.0**	**–**	**–**	**–**	**–**	**250.7**	**10.5**	**434.2**
Loans to trading book	**0.6**	**–**	**–**	**–**	**–**	**(2 0)**	**1.4**	**–**
Total assets	**9,481.1**	**628.2**	**616.6**	**1,757.3**	**323.1**	**268.7**	**11.9**	**13,086.9**
Liabilities and equity								
Deposits by banks	**652 2**	**1.5**	**2.0**	**–**	**–**	**5.6**	**–**	**661.3**
Customer accounts	**8,572.3**	**61 3**	**224.0**	**178 9**	**–**	**1,523.0**	**–**	**10,559.5**
Debt securities in issue	**444.2**	**91.6**	**–**	**–**	**–**	**–**	**–**	**535.8**
Other borrowed funds	**–**	**–**	**–**	**–**	**360 0**	**(1 9)**	**–**	**358.1**
Other liabilities	**–**	**–**	**–**	**–**	**–**	**243 4**	**11.9**	**255.3**
Equity	**–**	**–**	**–**	**–**	**–**	**716.9**	**–**	**716.9**
Total liabilities and equity	**9,668.7**	**154.4**	**226.0**	**178 9**	**360 0**	**2,487.0**	**11.9**	**13,086 9**
Derivatives	**(918.6)**	**(168.7)**	**–**	**822.3**	**265.0**	**–**	**–**	
Interest rate sensitivity gap	**(1,106.2)**	**305.1**	**390.6**	**2,400.7**	**228.1**	**(2,218 3)**	**–**	
Cumulative gap	**(1,106.2)**	**(801.1)**	**(410.5)**	**1,990.2**	**2,218.3**	**–**	**–**	

2006
Group

	Within 3 months	Over 3 months but within 6 months	Over 6 months but within 1 year	Over 1 year but within 5 years	More than 5 years	Non-interest bearing	Trading book	Total
Assets								
Loans and advances to banks	1,211 4	50 0	95 0	–	–	10 6	–	1,367 0
Loans and advances to customers	5,536 5	221 9	358 0	1,727 2	304 0	–	–	8,147 6
Debt securities and equity shares	1,478 9	423 2	491 8	350 9	10 0	–	–	2,754 8
Other assets	187 1	–	–	–	–	283 8	38 9	509 8
Loans to trading book	7 4	–	–	–	–	(4 1)	(3 3)	–
Total assets	**8,421.3**	**695.1**	**944.8**	**2,078.1**	**314.0**	**290.3**	**35.6**	**12,779.2**
Liabilities and equity								
Deposits by banks	661 3	33 6	–	–	–	5 7	–	700 6
Customer accounts	7,711 2	80 6	85 8	237 4	–	1,429 3	–	9,544 3
Debt securities in issue	996 9	114 4	2 0	–	–	–	–	1,113 3
Other borrowed funds	–	30 0	–	–	360 0	(2 2)	–	387 8
Other liabilities	–	–	–	–	–	298 4	35 6	334 0
Equity	–	–	–	–	–	699 2	–	699 2
Total liabilities and equity	**9,369.4**	**258 6**	**87 8**	**237.4**	**360.0**	**2,430.4**	**35.6**	**12,779.2**
Derivatives	**(918.7)**	**(304.5)**	**(20.0)**	**963 2**	**280.0**	–	–	
Interest rate sensitivity gap	**(1,866 8)**	**132.0**	**837.0**	**2,803.9**	**234.0**	**(2,140 1)**	–	
Cumulative gap	**(1,866.8)**	**(1,734.8)**	**(897.8)**	**1,906.1**	**2,140.1**	–	–	

2007
Bank

	Within 3 months	Over 3 months but within 6 months	Over 6 months but within 1 year	Over 1 year but within 5 years	More than 5 years	Non-interest bearing	Trading book	Total
Assets								
Loans and advances to banks	1,200 0	–	–	–	–	11.2	–	1,211.2
Loans and advances to customers	6,304.4	277.7	490.5	1,534.4	307.6	–	–	8,914.4
Debt securities and equity shares	1,417.7	215.2	125 4	219.9	7.5	8.8	–	1,994.5
Other assets	175.5	–	–	–	–	217 7	10.5	403.7
Loans to trading book	0 6	–	–	–	–	(2.0)	1.4	–
Total assets	**9,098.2**	**492.9**	**615.9**	**1,754.1**	**315.1**	**235.7**	**11.9**	**12,523.8**
Liabilities and equity								
Deposits by banks	652 2	1.5	2.0	–	–	5.6	–	661.3
Customer accounts	8,126.7	61.3	224.0	178.9	–	1,477 2	–	10,068.1
Debt securities in issue	444.2	91.6	–	–	–	–	–	535.8
Other borrowed funds	–	–	–	–	360.0	(1.9)	–	358.1
Other liabilities	–	–	–	–	–	228.3	11.9	240.2
Equity	–	–	–	–	–	660 3	–	660 3
Total liabilities and equity	**9,223.1**	**154 4**	**226.0**	**178.9**	**360 0**	**2,369.5**	**11 9**	**12,523.8**
Derivatives	**(838.6)**	**(168 7)**	**(10.0)**	**752.3**	**265.0**	–	–	
Interest rate sensitivity gap	**(963.5)**	**169.8**	**379.9**	**2,327.5**	**220.1**	**(2,133.8)**	–	
Cumulative gap	**(963.5)**	**(793 7)**	**(413.8)**	**1,913.7**	**2,133.8**	–	–	

2006
Bank

	Within 3 months	Over 3 months but within 6 months	Over 6 months but within 1 year	Over 1 year but within 5 years	More than 5 years	Non interest bearing	Trading book	Total
Assets								
Loans and advances to banks	1,213 8	50 0	95 0	–	–	10 6	–	1,369 4
Loans and advances to customers	5,461 0	221 5	357 2	1,720 5	291 6	–	–	8,051 8
Debt securities and equity shares	1,248 8	309 7	451 9	350 9	10 0	–	–	2,371 3
Other assets	189 5	–	–	–	–	272 3	38 9	500 7
Loans to trading book	7 4	–	–	–	–	(4 1)	(3 3)	–
Total assets	**8,120.5**	**581.2**	**904.1**	**2,071.4**	**301 6**	**278 8**	**35.6**	**12,293.2**
Liabilities and equity								
Deposits by banks	661 3	33 6	–	–	–	5 7	–	700 6
Customer accounts	7,329 4	80 6	85 8	237 4	–	1,386 1	–	9,119 3
Debt securities in issue	996 9	114 4	2 0	–	–	–	–	1,113 3
Other borrowed funds	–	30 0	–	–	360 0	(2 2)	–	387 8
Other liabilities	–	–	–	–	–	287 0	35 6	322 6
Equity	–	–	–	–	–	649 6	–	649 6
Total liabilities and equity	**8,987.6**	**258.6**	**87.8**	**237.4**	**360.0**	**2,326.2**	**35.6**	**12,293.2**
Derivatives	**(868.7)**	**(299.5)**	**(30 0)**	**918.2**	**280.0**	**–**	**–**	
Interest rate sensitivity gap	**(1,735.8)**	**23.1**	**786 3**	**2,752 2**	**221.6**	**(2,047 4)**	**–**	
Cumulative gap	**(1,735 8)**	**(1,712.7)**	**(926 4)**	**1,825 8**	**2,047.4**	**–**	**–**	

The period end position shown above is regarded as materially representative of the Group and Bank's position throughout the year and reflects the policies on risk management, subject to the following comments

–The gap analysis disclosed reflects contractual repricing in accordance with accounting standards
–Interest free current account balances are included in the 'non-interest bearing' maturity band
–The Group's asset and liability policies reflect the historic stability of customer accounts

Liquidity risk

Liquidity risk arises from the timing of cash flows generated from the Group's assets, liabilities and off-balance sheet instruments The Group's liquidity management policies are reviewed and approved annually by the Risk Management Committee and compliance is reviewed against these policies monthly by ALCO

Liquidity risk arising from the structure of the balance sheet (structural liquidity) is managed by policies developed by ALCO The primary policy is funding 85% of retail assets by retail deposits to ensure there is no over-reliance on wholesale funding The group's structural liquidity risk management is therefore retail based and is dependent on behavioural analysis of both customer demand deposit and loan drawdown profiles by product category based on experience over the last eight years The behaviour of retail products is reviewed by ALCO on a quarterly basis The Policy is to hold sufficient marketable assets for the worst gross monthly outflow (excluding offsetting inflows) experienced on a gross product basis

In addition the Group has maturity mismatch limits to control the exposure to longer term mismatches

Day-to-day cash flows (tactical liquidity) are managed by Treasury within guidelines laid down by ALCO and in accordance with the standards established for all banks by banking regulators Short-term liquidity standards, including holding a portfolio of liquid assets, ensure the Group can always meet its immediate obligations without recourse to the wholesale markets (for at least the next five working days) The Group undertakes tactical liquidity stress tests, assuming restricted access to wholesale market funding, with the aim of having sufficient liquidity for six months non-access

The Group is dependent on marketable assets, the asset quality of these is controlled via credit limits Concentration limits are set by issuer name and holding per bond to ensure diversity of assets

The following table analyses the Group and Bank's 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 as the retail and corporate deposit bases are very stable The behaviour is based on daily customer experience over the last eight years The deposits are attracted to the Bank by good customer service and its ethical policy Therefore, contractual maturity analysis is not used for risk management purposes

On a behavioural basis, the net liquidity gap for 1 month or less is a £1 9bn outflow (2006 £1 6bn outflow) for the Group and £1 5bn outflow (2006 £1 3bn outflow) for the Bank which the Group and Bank have sufficient liquid assets to cover

Risk management

2007
Group

	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Non cash items	Total
Assets							
Loans and advances to banks	2.7	1,190.0	–	–	11 3	–	1,204.0
Loans and advances to customers	732.5	2,174.7	664.4	1,508.2	4,089.9	(160.7)	9,009.0
Debt securities	–	1,015 3	511.2	818 8	85.6	–	2,430.9
Other assets	261.1	–	–	–	–	181.9	443.0
	996.3	4,380.0	1,175.6	2,327.0	4,186.8	21.2	13,086.9
Liabilities							
Deposits by banks	46 1	611.7	3.5	–	–	–	661.3
Customer accounts	8,118.9	1,979 5	282 3	178.8	–	–	10,559 5
Debt securities in issue	–	444.2	91.6	–	–	–	535 8
Other borrowed funds	–	–	–	–	360.0	(1.9)	358.1
Other liabilities	92.3	–	–	–	–	163 0	255.3
	8,257 3	3,035.4	377.4	178.8	360.0	161.1	12,370.0
Net liquidity gap	(7,261.0)	1,344 6	798 2	2,148.2	3,826 8	(139.9)	716 9

2006
Group

	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Non cash items	Total
Assets							
Loans and advances to banks	2 9	1,208 5	145 0	–	10 6	–	1,367 0
Loans and advances to customers	716 5	1,635 3	689 0	1,875 9	3,386 2	(155 3)	8,147 6
Debt securities	–	864 1	932 3	855 9	100 8	–	2,753 1
Other assets	271 3	–	–	–	–	240 2	511 5
	990 7	3,707.9	1,766 3	2,731 8	3,497.6	84 9	12,779.2

2006
Group

	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Non cash items	Total
Liabilities							
Deposits by banks	63 9	603 1	33 6	–	–	–	700 6
Customer accounts	7,265 9	1,882 5	158 3	237 6	–	–	9,544 3
Debt securities in issue	–	696 9	416 4	–	–	–	1,113 3
Other borrowed funds	–	–	–	30 0	360 0	(2 2)	387 8
Other liabilities	117 7	–	–	–	–	216 3	334 0
	7,447.5	3,182.5	608.3	267.6	360.0	214.1	12,080.0
Net liquidity gap	(6,456.8)	525.4	1,158.0	2,464.2	3,137 6	(129.2)	699.2

2007 Bank	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Non cash items	Total
Assets							
Loans and advances to banks	2.7	1,197.2	–	–	11.3	–	1,211.2
Loans and advances to customers	712.8	2,196.3	659.8	1,488.9	4,017.3	(160.7)	8,914.4
Debt securities	–	705.2	376.1	818.8	85.6	–	1,985.7
Other assets	261.4	–	–	–	–	151.1	412.5
	976.9	4,098 7	1,035.9	2,307.7	4,114.2	(9.6)	12,523.8
Liabilities							
Deposits by banks	46.1	611.7	3 5	–	–	–	661.3
Customer accounts	7,758 9	1,853.2	277.2	178.8	–	–	10,068.1
Debt securities in issue	–	444.2	91.6	–	–	–	535.8
Other borrowed funds	–	–	–	–	360.0	(1.9)	358.1
Other liabilities	92 8	–	–	–	–	147.4	240.2
	7,897.8	2,909.1	372.3	178.8	360.0	145.5	11,863.5
Net liquidity gap	(6,920.9)	1,189.6	663.6	2,128.9	3,754.2	(155.1)	660.3

2006 Bank	Repayable on demand	3 months or less but not repayable on demand	1 year or less but over 3 months	5 years or less but over 1 year	Over 5 years	Non cash items	Total
Assets							
Loans and advances to banks	2 9	1,210 9	145 0	–	10 6	–	1,369 4
Loans and advances to customers	687 3	1,663 6	681 1	1,845 9	3,329 2	(155 3)	8,051 8
Debt securities	–	634 0	779 0	855 9	100 7	–	2,369 6
Other assets	272 4	–	–	–	–	230 0	502 4
	962.6	3,508.5	1,605.1	2,701.8	3,440.5	74.7	12,293.2
Liabilities							
Deposits by banks	63 9	603 1	33 6	–	–	–	700 6
Customer accounts	6,942 5	1,780 9	158 3	237 6	–	–	9,119 3
Debt securities in issue	–	696 9	416 4	–	–	–	1,113 3
Other borrowed funds	–	–	–	30 0	360 0	(2 2)	387 8
Other liabilities	118 0	–	–	–	–	204 6	322 6
	7,124 4	3,080 9	608.3	267.6	360.0	202.4	11,643 6
Net liquidity gap	(6,161.8)	427.6	996.8	2,434.2	3,080.5	(127.7)	649.6

Gross contractual cash flow analysis

The following is an analysis of gross contractual cash flows of financial liabilities held at the balance sheet date

2007
Group

	Carrying value	Gross nominal outflow	less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Deposits by banks	661.3	664.0	599.3	61.1	3.6	-	-
Customer accounts	10,559.5	10,637.0	9,882.2	223.9	324.7	206.2	-
Debt securities in issue	535.8	540.5	246 8	202.1	91.6	-	-
Derivative financial instruments	92.3	92.3	92.3	-	-	-	-
Other borrowed funds	358.1	514.5	-	8 8	11.2	91.2	403.3
Total liabilities	**12,207.0**	**12,448 3**	**10,820 6**	**495.9**	**431.1**	**297.4**	**403.3**
Other liabilities	163.0						
Total recognised liabilities	**12,370.0**	**12,448.3**	**10,820.6**	**495.9**	**431 1**	**297 4**	**403.3**
Unrecognised loan commitments	6,371.7	6,371.7	6,301.8	7.9	14.9	47.1	-
Total	**18,741.7**	**18,820.0**	**17,122.4**	**503 8**	**446.0**	**344.5**	**403.3**

2006
Group

	Carrying value	Gross nominal outflow	less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Deposits by banks	700 6	704 4	615 5	54 3	34 6	-	-
Customer accounts	9,544 3	9,623 4	8,864 6	289 5	166 6	302 7	-
Debt securities in issue	1,113 3	1,128 0	317 7	387 8	422 5	-	-
Derivative financial instruments	117 7	117 7	117 7	-	-	-	-
Other borrowed funds	387 8	557 4	-	-	54 8	91 2	411 4
Total liabilities	**11,863.7**	**12,130.9**	**9,915.5**	**731.6**	**678 5**	**393.9**	**411.4**
Other liabilities	216 3						
Total recognised liabilities	**12,080.0**	**12,130.9**	**9,915.5**	**731.6**	**678 5**	**393.9**	**411.4**
Unrecognised loan commitments	5,814 5	5,814 5	5,754 2	1 8	13 8	44 7	-
Total	**17,894 5**	**17,945 4**	**15,669 7**	**733 4**	**692.3**	**438 6**	**411.4**

2007
Bank

	Carrying value	Gross nominal outflow	less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Financial liabilities							
Deposits by banks	661.3	664.0	599 3	61 1	3 6	-	-
Customer accounts	10,068.1	10,141.1	9,451.5	164 0	319 4	206.2	-
Debt securities in issue	535.8	540.5	246 8	202.1	91.6	-	-
Derivative financial instruments	92.8	92.8	92.8	-	-	-	-
Other borrowed funds	358 1	514 5	-	8.8	11.2	91.2	403.3
Total liabilities	**11,716.1**	**11,952.9**	**10,390.4**	**436 0**	**425 8**	**297.4**	**403.3**
Other liabilities	147.4						
Total recognised liabilities	**11,863.5**	**11,952.9**	**10,390.4**	**436 0**	**425.8**	**297.4**	**403.3**
Unrecognised loan commitments	6,364.5	6,364.5	6,294 6	7.9	14.9	47.1	-
Total	**18,228.0**	**18,317.4**	**16,685.0**	**443.9**	**440.7**	**344.5**	**403.3**

2006
Bank

	Carrying value	Gross nominal outflow	less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years
Deposits by banks	700 6	704 4	615 5	54 3	34 6	–	–
Customer accounts	9,119 3	9,194 5	8,539 4	185 8	166 6	302 7	–
Debt securities in issue	1,113 3	1,128 0	317 7	387 8	422 5	–	–
Derivative financial instruments	118 0	118 0	118 0	–	–	–	–
Other borrowed funds	387 8	557 4	–	–	54 8	91 2	411 4
Total liabilities	**11,439.0**	**11,702 3**	**9,590.6**	**627.9**	**678.5**	**393 9**	**411.4**
Other liabilities	204 6						
Total recognised liabilities	**11,643.6**	**11,702.3**	**9,590.6**	**627.9**	**678.5**	**393.9**	**411.4**
Unrecognised loan commitments	5,805 4	5,805 4	5,745 1	1 8	13 8	44 7	–
Total	**17,449.0**	**17,507.7**	**15,335.7**	**629.7**	**692.3**	**438.6**	**411.4**

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

Fair values of financial assets and liabilities
The table below sets out a comparison of the book value and the fair value at 12 January 2008 of all of the Group's financial instruments, where book value does not equate to fair value

2007	Group		Bank	
	Carrying value	**Fair value**	**Carrying value**	**Fair value**
Assets				
Loans and advances to banks	**1,204 0**	**1,204 0**	**1,211 2**	**1,211.2**
Loans and advances to customers	**9,009.0**	**9,035.2**	**8,914.4**	**8,939.9**
Liabilities				
Deposits by banks	**661.3**	**661.3**	**661.3**	**661 3**
Customer accounts	**10,559.5**	**10,561.4**	**10,068.1**	**10,070.0**
Debt securities in issue	**535.8**	**539.2**	**535.8**	**539 2**
Other borrowed funds	**358.1**	**357.5**	**358.1**	**357 5**

2006	Group		Bank	
	Carrying value	**Fair value**	**Carrying value**	**Fair value**
Financial assets				
Loans and advances to banks	1,367 0	1,367 0	1,369 4	1,369 4
Loans and advances to customers	8,147 6	8,124 2	8,051 8	8,028 0
Financial liabilities				
Deposits by banks	700 6	700 6	700 6	700 6
Customer accounts	9,544 3	9,543 1	9,119 3	9,118 1
Debt securities in issue	1,113 3	1,113 8	1,113 3	1,113 8
Other borrowed funds	387 8	415 5	387 8	415 5

(a) Loans and advances to banks
Loans and advances to banks include inter-bank 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

(b) Loans and advances to customers
Loans and advances are net of provisions for impairment The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received Expected cash flows are discounted at current market interest rates based on original credit spends to determine fair value

(c) Deposits by banks
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 remaining maturity

(d) 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

(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

Additionally, debt securities and derivatives are measured at fair value

(f) Debt 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 detailed by IAS 39

Balance sheet categories	Trading	Designated at fair value	Loans and receivables	Available-for-sale	Other amortised cost	Cash flow hedges	Total
2007							
Group							
Assets							
Cash and balances at central banks	–	–	172.9	–	–	–	172.9
Loans and advances to banks	–	–	1,204.0	–	–	–	1,204.0
Loans and advances to customers	–	29.1	8,979.9	–	–	–	9,009.0
Debt securities	–	6.9	–	2,424 0	–	–	2,430.9
Derivative financial instruments	9.6	67.9	–	–	–	10.7	88.2
Equity shares	–	–	–	8.8	–	–	8 8
Total financial assets	**9.6**	**103.9**	**10,356.8**	**2,432.8**	–	**10.7**	**12,913.8**
Non financial assets							173.1
Total assets							**13,086 9**
Liabilities							
Deposits by banks	–	–	–	–	661 3	–	661.3
Deposits from customers	–	–	–	–	10,559.5	–	10,559.5
Debt securities in issue	–	–	–	–	535.8	–	535 8
Derivative financial instruments	8.0	71.9	–	–	–	12.4	92.3
Other borrowed funds	–	–	–	–	358.1	–	358.1
Total financial liabilities	**8 0**	**71.9**	–	–	**12,114 7**	**12.4**	**12,207 0**
Non financial liabilities							163.0
Total liabilities							12,370.0
Capital and reserves							716.9
Total liabilities and equity							**13,086.9**

Balance sheet categories	Trading	Designated at fair value	Loans and receivables	Available-for-sale	Other amortised cost	Cash flow hedges	Total
2006							
Group							
Assets							
Cash and balances at central banks	–	–	186 9	–	–	–	186 9
Loans and advances to banks	–	–	1,367 0	–	–	–	1,367 0
Loans and advances to customers	–	35 6	8,112 0	–	–	–	8,147 6
Debt securities	–	–	–	2,753 1	–	–	2,753 1
Derivative financial instruments	6 3	75 5	–	–	–	2 6	84 4
Equity shares	–	–	–	1 7	–	–	1 7
Total financial assets	**6 3**	**111.1**	**9,665.9**	**2,754.8**	**–**	**2.6**	**12,540.7**
Non financial assets							238 5
Total assets							**12,779.2**
Liabilities							
Deposits by banks	–	–	–	–	700 6	–	700 6
Deposits from customers	–	–	–	–	9,544 3	–	9,544 3
Debt securities in issue	–	–	–	–	1,113 3	–	1,113 3
Derivative financial instruments	7 2	79 1	–	–	–	31 4	117 7
Other borrowed funds	–	–	–	–	387 8	–	387 8
Total financial liabilities	**7.2**	**79.1**	**–**	**–**	**11,746 0**	**31.4**	**11,863.7**
Non financial liabilities							216 3
Total liabilities							**12,080.0**
Capital and reserves							699 2
Total liabilities and equity							**12,779 2**

Balance sheet categories	Trading	Designated at fair value	Loans and receivables	Available-for-sale	Other amortised cost	Cash flow hedges	Total
2007							
Bank							
Assets							
Cash and balances at central banks	–	–	**172.9**	–	–	–	**172.9**
Loans and advances to banks	–	–	**1,211.2**	–	–	–	**1,211.2**
Loans and advances to customers	–	**29.1**	**8,885.3**	–	–	–	**8,914.4**
Debt securities	–	**6.9**	–	**1,978.8**	–	–	**1,985.7**
Derivative financial instruments	**10.5**	**67.9**	–	–	–	**10 1**	**88.5**
Equity shares	–	–	–	**8 8**	–	–	**8.8**
Total financial assets	**10.5**	**103 9**	**10,269.4**	**1,987 6**	**–**	**10.1**	**12,381.5**
Non financial assets							**142.3**
Total assets							**12,523.8**
Liabilities							
Deposits by banks	–	–	–	–	**661.3**	–	**661.3**
Deposits from customers	–	–	–	–	**10,068 1**	–	**10,068.1**
Debt securities in issue	–	–	–	–	**535.8**	–	**535.8**
Derivative financial instruments	**8.7**	**71.8**	–	–	–	**12.3**	**92.8**
Other borrowed funds	–	–	–	–	**358 1**	–	**358.1**
Total financial liabilities	**8.7**	**71.8**	**–**	**–**	**11,623.3**	**12.3**	**11,716.1**
Non financial liabilities							**147.4**
Total liabilities							**11,863.5**
Capital and reserves							**660.3**
Total liabilities and equity							**12,523.8**

Balance sheet categories	Trading	Designated at fair value	Loans and receivables	Available-for-sale	Other amortised cost	Cash flow hedges	Total
2006							
Bank							
Assets							
Cash and balances at central banks	–	–	186 9	–	–	–	186 9
Loans and advances to banks	–	–	1,369 4	–	–	–	1,369 4
Loans and advances to customers	–	35 6	8,016 2	–	–	–	8,051 8
Debt securities	–	–	–	2,369 6	–	–	2,369 6
Derivative financial instruments	7 4	75 5	–	–	–	2 6	85 5
Equity shares	–	–	–	1 7	–	–	1 7
Total financial assets	**7.4**	**111.1**	**9,572.5**	**2,371.3**	**–**	**2.6**	**12,064.9**
Non financial assets							228 3
Total assets							**12,293.2**
Liabilities							
Deposits by banks	–	–	–	–	700 6	–	700 6
Deposits from customers	–	–	–	–	9,119 3	–	9,119 3
Debt securities in issue	–	–	–	–	1,113 3	–	1,113 3
Derivative financial instruments	8 3	79 1	–	–	–	30 6	118 0
Other borrowed funds	–	–	–	–	387 8	–	387 8
Total financial liabilities	**8.3**	**79.1**	**–**	**–**	**11,321 0**	**30 6**	**11,439.0**
Non financial liabilities							204 6
Total liabilities							**11,643.6**
Capital and reserves							649 6
Total liabilities and equity							**12,293.2**

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 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
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 Debt securities also underpin the Bank's liquidity requirements and generate incremental net interest and trading income

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 £60 million 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

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

Operational Risk Framework
Operational Risks are identified, managed and mitigated through ongoing risk management practices including risk assessments, formal internal 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, the Operational Risk Committee and the Risk Management Committee These meet regularly to monitor the suitability of the risk management framework and management of significant risks within CFS

CFS continues to develop its approach to managing Operational Risk 2007 has seen significant enhancements in the process for quantifying operational risks, providing a means of translating operational risk exposures into capital requirements In addition the Incident Reporting process has been revised and relaunched, incorporating a centralised reporting hotline, and supported by the Integrated Risk System

Responsibilities
Whilst the Board is ultimately responsible for Operational Risks across the Bank and the wider CFS organisation, this is delegated to the Chief Executive and Executive Directors within CFS who are responsible for controlling the Operational Risks in their direct areas of accountability and for compliance with CFS policies

Each Executive has a nominated Divisional Risk Owner who is a member of the Operational Risk Committee and is responsible for ensuring the consistent application of the Operational Risk framework within their division Divisional Risk Owners are supported from within their business divisions

The central Operational Risk team facilitate the consistent identification, management and reporting of Operational Risks across CFS in line with regulatory and business requirements, support development and testing of business continuity arrangements for the business, and manage the CFS Corporate Insurance programme

Risk themes
CFS categorises Operational Risk into a number of distinct themes for internal management, monitoring and reporting Key Operational Risk themes managed by CFS include

Financial crime
This relates to the effectiveness of controls to minimise financial losses arising from the fraudulent activities of employees, customers and third parties

The organisation recognises the increasing concerns of customers, regulatory authorities and the media in respect of the loss or theft of confidential customer information It has responded pro-actively to these concerns by reviewing, in detail, its arrangements for the security of confidential customer files Whilst these were found to be robust, enhancements to provide additional customer protection continue to be assessed and implemented where appropriate

Controls include training and awareness to develop an anti-fraud culture, IT security infrastructure, tools and specialists to protect CFS systems and customer details, documented procedures, controls and automated solutions to detect/prevent fraud, Know Your Customer (KYC) procedures, employee pre-recruitment vetting and screening, dual control and segregation of duties where appropriate and Security and Major Investigations function working closely with Internal Audit and Operational Risk management

Compliance (with regulatory and legal requirements)
As a regulated business, CFS places great emphasis on maintaining compliance with our regulatory and legal obligations by
- Regulatory - supporting CFS's business objectives through the provision of advice, and the recommendation of solutions where appropriate, in respect of the regulatory implications of business developments and assisting the business in assessing and addressing new and enhanced regulatory expectations This is supported by appropriate and effective monitoring, aimed at influencing the business to mitigate or eliminate regulatory risk and demonstrate that we are meeting our regulatory obligations
- Legal - seeking to pro-actively manage legal issues in relation to commercial, contractual, employment and litigation activities

Employee practices/workplace safety
It is acknowledged that our people are a key asset The Financial Services sector as an industry is reliant on its people and the skills, knowledge and experience they provide The risk of failure to maintain employee relations, or provide a safe environment in line with legislative requirements and with the ethical, diversity and discrimination rules is managed with support from our Human Resources department

Property and facilities
The risk of unforeseen operational disruption caused through the denial of access to major occupancies or other interruptions to business operations is managed through our business continuity framework and corporate insurance programme

Customer service
As a financial services business, providing fair and high-quality customer service is a must Controls that could prevent such risks occurring are regularly assessed

and monitored These include customer service levels, getting things right first time, availability of customer facing systems, together with trained and skilled resource to service customer demand

Suppliers
CFS looks to source cost-effective and quality services, both internal and external to the Co-operative Group Given the reliance on our business partners who provide services and products, a major or prolonged disruption to the supply of their services and products would impact on CFS Risks are monitored relating to the effectiveness of contracts and relationship management to ensure that CFS' expected performance levels are achieved

Major IT systems/major payments systems failure
Financial service providers have a heavy reliance on the availability and performance of underlying systems and applications, and the processes and frameworks which underpin these Consequently the effectiveness of controls over the IT systems and infrastructure supporting IT processes and controls, major payment systems and clearing and business processes are monitored on a regular basis

Change management
Given the integration of The Co-operative Bank and the Co-operative Insurance Society businesses, and the ongoing business transformation to integrate and improve the service offerings, competitiveness and efficiency of CFS in our journey to become the UK's most admired financial services business, there is a substantial change programme in place In order to ensure delivery to time, cost or quality, and minimise risks arising from this there is a dedicated Change Risk & Governance team in place

Basel II is an internationally agreed framework for banking regulation and capital management The FSA issued final guidance and implementation requirements on these new standards during 2006, in preparation for firms to commence parallel running with the introduction of the new regulations from 2007 onwards The Bank submitted its Permission Application Pack (PAP) to the FSA in December 2006 and commenced its parallel run activities during 2007 In December 2007, the FSA formally approved the PAP allowing the bank to operate an internal rating based (IRB) approach which was fully implemented at the start of 2008

The Basel II programme continued to be a key risk management development in the Bank in 2007, which enabled the Bank to submit it's first Internal Capital Adequacy Assessment Process (ICAAP) to the FSA in the second half of 2007 This was fully reviewed and in December 2007, the FSA fedback the Bank's Individual Capital Guidance (ICG) for 2008

The Pillar 3 disclosure for the Co-operative Bank Group based on the year ended 12 January 2008 will be made available on the CFS website (www cfs co uk)

Principal risks
As part of the Bank's preparation for its first ICAAP submission to the FSA in 2007, and as part of CFS' ongoing preparation for Solvency 2 for CIS and CISGIL, a review of CFS' Risk Management Framework was conducted in the latter part of 2006 A revised, ICAAP compliant, CFS Risk Management Framework was introduced in Quarter 1 2007

In addition to the significant risks covered above, the following risks are also reported in the new CFS Risk Management Framework
- Group wide risks, to include pensions, reputational and group risk
- Business risk

Pensions risk: arises from the volatility of future pension contributions required from the Bank to fund the Co-operative Group PACE scheme These contributions may be affected by valuations of the PACE scheme for which the key assumptions are mortality, inflation, rate of salary/pension increase and the investment return

Pensions 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

Reputational risk: is the current or prospective risk to the Bank's earnings and capital arising from adverse perception of the Bank's or another member of the Co-operative Group's image on the part of customers, counterparties, shareholders, investors or regulators

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

Group risk: includes contagion risk, being the risk that losses or liabilities from one part of the group deplete or divert financial resources from another part of the Group

Group Risks are identified at the Bank entity level As part of the assessment of this risk, consideration is given to the impact of other CFS and Co-operative Group entities on the Bank

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, including the ability to provide suitable products and services to customers In a narrow sense, business risk is the risk the Bank suffers losses because income falls or is volatile relative to the fixed cost base However, in a broader sense, it is the Bank's exposure to a wide range of macro-economic, geopolitical, industry, regulatory and other external risks

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 1 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

Our submission 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 period

	2007	2006
Core tier one capital		
Permanent share capital	**55.0**	55 0
Retained earnings	**652 6**	658 7
Share premium account	**8.8**	8 8
Perpetual non cumulative preference shares	**60.0**	60 0
Total tier one capital before regulatory deductions	**776.4**	782 5
Tier two capital		
Long term subordinated debt	**298.1**	327 8
Total tier two capital before deductions	**298.1**	327 8
Tier 1 ratio	**8 8%**	9 9%
Total risk asset ratio	**13.5%**	15 3%

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 The preference shares carry the right to a 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

The tier two capital includes two subordinated debt issues, £150m Step Up Callable Subordinated Notes 2019 and £150m Callable Subordinated Notes 2021 fixed rate until 2016, then moving to floating rate The £30m Subordinated Perpetual Floating Rate Notes were redeemed on 9 January 2008

The rights of repayment 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 23

During the reporting period the Bank has moved from reporting on a Basel I basis to a Basel II basis using the IRB approach The Group obtained FSA permission to report on this basis in December 2007 This change impacts on the regulatory capital deductions from Tier 1 and Tier 2 capital for certain risks, particularly credit risk where deductions are now calculated with reference to the expected loss on the Group's assets under various scenarios

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 Each new product must earn at least the Group's minimum target return on equity

Critical judgements

The Bank makes estimates and assumptions that affect the reported assets and liabilities Critical estimates and judgements are continually assessed and reviewed, and are based on historical experience and reasonable expectations of future events

Impairment on loans and advances
The loan portfolios are reviewed on a continuous basis to assess impairment In determining whether a bad debt provision should be recorded, judgements 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 impaired 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 also 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

Impairment on structured investments
Structured investments
The Bank holds £63m of Structured Investments The accounting treatment for these assets is 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

The impact of the 'credit crunch' and subsequent reductions in liquidity in wholesale markets has led to reductions in values for these assets but has also increased the subjectivity of valuation as there is no active market or traded price available for such assets

The Bank has adopted a valuation policy of published Net Asset Value (NAV) information, unless a restructuring proposal is in place at the year end which provides better valuation evidence

For assets in process of restructuring, the valuation is based on the present value of the estimated cash flows, taking account of levels of default and funding rates which will arise post restructure

Additionally, it has been necessary to consider whether these assets are impaired as this requires losses to be recognised in the income statement Impairment has been assessed by

- Is there evidence that a loss event has occurred, and
- Does the loss event have a negative impact on future cash flows

Each of the Bank's structured investments meet these criteria and therefore an impairment provision has been made

Credit trading funds
The Bank also holds £50m of Credit Trading Fund Investments The accounting treatment for these assets is 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 or contain embedded derivatives which result in movements being recognised in the income statement

The investments are measured using modelling techniques and external published prices and indices where available

These Bank investments have been assessed as above and are not considered to be impaired

1 Segmental analysis

The Group's primary basis of segmentation is by business activity Activities have been segmented between Retail banking, Corporate and Business banking and Wholesale Segment information is presented in the financial statements in respect of the Bank's business segments, reflecting the Bank's management and internal reporting structure Income and costs are allocated using transfer pricing and Activity Based Management methodologies

The Group is comprised of the following main business segments

- **Retail** – customer focused products and services for individuals, sole traders and small partnerships It includes mortgages, credit cards, consumer loans, small business loans, current accounts and savings products
- **Corporate** – customer focused products and services for business accounts This includes large corporate and commercial entities and SMEs (Small to Medium entities) It includes loans, asset finance, current accounts and savings products
- **Wholesale** – asset and liability management across the Bank's overall balance sheet, including trading activities

2007	**Retail**	**Corporate**	**Wholesale**	**Central costs**	**Total**
External gross revenue	**548.3**	**282.9**	**190 8**	**-**	**1,022 0**
External net revenue	**313.2**	**197.2**	**13 1**	**-**	**523.5**
Internal net revenue	**85.8**	**(69.5)**	**(16 3)**	**-**	**-**
Operating income	**399 0**	**127.7**	**(3.2)**	**-**	**523.5**
Operating profit	**47 1**	**57.5**	**(43.1)**	**(11 1)**	**50.4**
Profit based payments to members of the Co-operative Group					**(1.3)**
Significant Items					**(38.0)**
Profit before taxation					**11.1**
Income tax expense					**(5.2)**
Profit for the year					**5.9**
Other information					
Segmental assets	**5,085.2**	**3,522 1**	**4,091.9**	**-**	**12,699.2**
Unallocated assets					**387.7**
Consolidated assets					**13,086 9**
Segmental liabilities	**6,640.2**	**2,996.6**	**1,761 9**	**-**	**11,398.7**
Unallocated liabilities					**971 3**
Consolidated liabilities					**12,370.0**
Capital expenditure	**9.9**	**3.6**	**0 4**	**0.8**	**14.7**
Depreciation and amortisation	**17.5**	**2 9**	**0.7**	**1 6**	**22.7**

2006	**Retail**	**Corporate**	**Wholesale**	**Central costs**	**Total**
External gross revenue	553 9	214 3	175 6	–	943 8
External net revenue	371 7	148 7	1 1	–	521 5
Internal net revenue	27 6	(35 9)	8 3	–	-
Operating income	399 3	112 8	9 4	-	521 5
Operating profit	34 2	55 1	3 9	(16 9)	**76.3**
Profit based payments to members of the Co-operative Group					(1 2)
Significant Items					109 2
Profit before taxation					**184.3**
Income tax expense					(57 4)
Profit for the year					**126.9**

1. Segmental analysis (continued)

2006	Retail	Corporate	Wholesale	Central costs	Total
Other information					
Segmental assets	5,156 1	2,803 4	4,359 3	–	12,318 8
Unallocated assets					460 4
Consolidated assets					12,779 2
Segmental liabilities	6,039 5	2,836 0	2,358 4	–	11,233 9
Unallocated liabilities					846 1
Consolidated liabilities					12,080 0
Capital expenditure	38 2	3 5	0 4	0 5	42 6
Depreciation and amortisation	20 0	2 4	0 1	1 9	24 4

The group's activities are in the UK

2. Profit before taxation

	2007	2006
Profit before taxation is stated after	£'000	£'000
Audit of these financial statements	**238**	236
Other services		
Amounts receivable by auditors and their associates in respect of		
Audit of financial statements of subsidiaries pursuant to legislation	**60**	73
Other services pursuant to such legislation	**15**	14
Services relating to information technology	**–**	–
Services relating to recruitment and remuneration	**–**	7
All other services	**143**	752
Total	**456**	1,082

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

3. Directors' emoluments

	2007 £'000	2006 £'000
Non-Executive Directors	**–**	–
Executive Directors	**1,188**	545
Compensation for loss of office	**174**	–
	1,362	545

Retirement benefits are accruing to no Directors (2006 one) under defined benefit schemes

Further details of Directors' emoluments are included in the remuneration report on pages 34 to 38

4. Net interest income

	2007	2006
Interest and similar income on items not at fair value through profit or loss	**802.2**	705 9
Interest and similar income on items at fair value through profit or loss	**2.2**	1 1
Fair value movements	**(4 4)**	1 8
	800.0	708 8

Interest income accrued on impaired financial assets during the period was £14 6m (2006 £15 3m), interest due to unwinding of discount on impairment provisions relating to impaired financial assets amounted to £4 3m (2006 £4 5m)

Interest payable of £465 2m (2006 £388 5m) relates to liabilities not at fair value through profit or loss

5. Net fee and commission income and expense	2007	2006
Fee and Commission income on items not at fair value through profit or loss	216.0	231 8
Fee and Commission income on items at fair value through profit or loss	0.1	–
Fee and Commission income on trust or fiduciary activities that result from holding or investing in assets on behalf of others	0.4	0 3
Total fee and commission income	**216.5**	**232.1**
Fee and Commission expense on items not at fair value through profit or loss	33 1	33 5
Fee and Commission expense on items at fair value through profit or loss	0.2	0 3
Total fee and commission expense	**33.3**	**33.8**

6. Net trading income	2007	2006
Foreign exchange	5.2	5 0
Interest rate instruments	0.3	(2 2)
	5.5	2 8

'Foreign exchange' net trading income includes gains and losses from spot forward and forward contracts, options futures and translated foreign currency assets and liabilities
'Interest rate instruments' includes the result of making markets in instruments in government securities, corporate debt securities, moneymarket instruments, interest rate and currency swaps, options and other derivatives

7 Operating expenses	Before significant items 2007	Significant items 2007	After significant items 2007	Before significant items 2006	Significant items 2006	After significant items 2006
Staff costs (Note 8)	145 3	18.2	163.5	142 3	(109 2)	33 1
Administrative expenses	153.6	19.8	173 4	157 4	–	157 4
Depreciation (Note 18)	19 1	–	19.1	21 1	–	21 1
Loss on sale of property, plant and equipment	7.4	–	7 4	1 8	–	1 8
Software costs (Note 17)	3 6	–	3.6	3 3	–	3 3
Operating lease rentals	10.3	–	10 3	14 0	–	14 0
	339.3	38.0	377 3	339 9	(109 2)	230 7

8. Staff costs	Before significant items 2007	Significant items 2007	After significant items 2007	Before significant items 2006	Significant items 2006	After significant items 2006
Wages and salaries	111.1	2.5	113.6	109 6	–	109 6
Social security costs	9 2	0 2	9.4	8 6	–	8 6
Pension costs – defined benefit plans	0.3	–	0 3	4 3	(109 2)	(104 9)
– defined contribution plans	11.9	0 3	12.2	10 5	–	10 5
Other staff costs	12 8	15.2	28.0	9 3	–	9 3
	145 3	18 2	163 5	142 3	(109 2)	33 1

Average number of employees

The average number of persons working for the group during the year was made up as follows

	No of employees 2007	No of employees 2006
Full time	3,305	3,264
Part time	976	970
	4,281	4,234

Employee activities are undertaken across the CFS Group and the figures above reflect the Bank's share of these services The 2006 figures relate to people employed by the Bank

9. Income tax expense

	Before significant items 2007	Significant items 2007	After significant items 2007	Before significant items 2006	Significant items 2006	After significant items 2006
Current tax – current year	**18 6**	**(11 4)**	**7.2**	26 3	–	26 3
Current tax – prior year	**0.3**	**–**	**0.3**	0 2	–	0 2
Deferred tax (Note 26)	**(2.3)**	**–**	**(2.3)**	(1 9)	32 8	30 9
	16.6	**(11 4)**	**5 2**	24 6	32 8	57 4

Further information about deferred income tax is presented in Note 26 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

	2007	2006
Profit before tax	**11.1**	184 3
Tax calculated at a tax rate of 30% (2006 30%)	**3.3**	55 3
Effect of		
Preference share interest not deductible for tax purposes	**1.7**	1 7
Expenses not deductible for tax purposes	**0.1**	0 2
Depreciation of expenditure not qualifying for capital allowances	**0 5**	0 4
Adjustments to tax charge in respect of prior periods	**–**	(0 2)
Tax rate change on deferred tax to 28%	**(0.4)**	–
	5.2	57 4

10 Group profit attributable to equity shareholders dealt with in the accounts of The Co-operative Bank p l.c

£1.1 million loss (pre-significant items £25 5 million profit) (2006 £119 0 million profit, pre-significant items £44 4 million profit) of the Group profit attributable to equity shareholders has been dealt with in the accounts of The Co operative Bank p l c

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of The Co-operative Bank p l c has not been presented separately

11. Earnings per share

Basic earnings per share is calculated by dividing the net profit attributable to equity holders of the Bank by weighted average number of ordinary shares in issue during the year

	Before significant items 2007	Significant items 2007	After significant items 2007	Before significant items 2006	Significant items 2006	After significant items 2006
Profit attributable to equity holders of the Bank	**29.8**	**(26 6)**	**3.2**	48 3	75 1	123 4
Weighted average number of ordinary shares in issue (millions)	**1,100.0**	**1,100 0**	**1,100.0**	1,100 0	1,100 0	1,100 0
Basic earnings per share (expressed in pence per share)	**2.71**	**(2.42)**	**0.29**	4 39	6 83	11 22

12 Loans and advances to banks

	Group 2007	Group 2006	Bank 2007	Bank 2006
Items in course of collection from other banks	**141.3**	134 0	**141.0**	133 9
Placements with other banks	**1,062 7**	1,088 0	**1,070.2**	1,090 5
Included in cash equivalents	**1,204.0**	1,222 0	**1,211.2**	1,224 4
Other loans and advances to banks	**–**	145 0	**–**	145 0
	1,204.0	1,367 0	**1,211.2**	1,369 4
Of which				
Variable rate	**268.1**	66 6	**268.1**	66 6
Fixed rate	**935 9**	1,300 4	**943.1**	1,302 8

12. Loans and advances to banks (continued)

Mandatory reserve deposits of £11 3m (2006 £10 6m) are not available for use in the Group and Bank's day to day operations, are non-interest bearing and are included in cash equivalents Group and Bank collateral of £53 9m (2006 £139 9m) held under reverse repo agreements can be sold or repledged without default At the balance sheet date £nil (2006 £nil) was resold or repledged These transactions are conducted under standard repo agreement terms

13 Loans and advances to customers

	Group		Bank	
	2007	2006	**2007**	2006
Gross loans and advances	**9,169.7**	8,302 9	**9,075.1**	8,207 1
Less allowance for losses on loans and advances	**(160.7)**	(155 3)	**(160.7)**	(155 3)
	9,009.0	8,147 6	**8,914 4**	8,051 8
Of which				
Variable rate	**4,475 9**	4,288 8	**4,345 3**	4,157 0
Fixed rate	**4,533.1**	3,858 8	**4,569.1**	3,894 8

Concentration of exposure

The Group's exposure is virtually all within the United Kingdom The following industry concentrations of gross advances before provisions are considered significant

	Group		Bank	
	2007	2006	**2007**	2006
Property and construction	**1,309.5**	1,001 7	**1,309.5**	1,001 7
Retail distribution and services	**695 5**	504 1	**695.5**	504 1
Business and other services	**1,963.0**	1,530 7	**1,868.4**	1,434 9
Personal – unsecured	**1,890.9**	2,121 2	**1,890.9**	2,121 2
Personal – secured	**3,310.8**	3,145 2	**3,310 8**	3,145 2
	9,169.7	8,302 9	**9,075.1**	8,207 1

Allowance for losses on loans and advances

Movement in allowance for losses on loans and advances

	Individual 2007	**Collective 2007**	**Total 2007**	Individual 2006	Collective 2006	Total 2006
Group						
At the beginning of the year	**27 5**	**127 8**	**155.3**	47 7	108 7	156 4
Charge against profits	**13.9**	**88.1**	**102.0**	6 0	99 3	105 3
Amounts written off	**(5.0)**	**(87.9)**	**(92.9)**	(26 8)	(77 2)	(104 0)
Recoveries	**0.1**	**–**	**0.1**	0 4	–	0 4
Unwind of discount of allowance	**(1 4)**	**(2.9)**	**(4.3)**	(1 5)	(3 0)	(4 5)
Interest charged on impaired loans	**0.5**	**–**	**0 5**	1 7	–	1 7
At the end of the year	**35.6**	**125.1**	**160 7**	27 5	127 8	155 3

	Individual 2007	**Collective 2007**	**Total 2007**	Individual 2006	Collective 2006	Total 2006
Bank						
At the beginning of the year	**27.5**	**127.8**	**155 3**	47 5	108 7	156 2
Charge against profits	**13.9**	**88.1**	**102.0**	6 2	99 3	105 5
Amounts written off	**(5.0)**	**(87.9)**	**(92.9)**	(26 8)	(77 2)	(104 0)
Recoveries	**0.1**	**–**	**0.1**	0 4	–	0 4
Unwind of discount of allowance	**(1.4)**	**(2.9)**	**(4 3)**	(1 5)	(3 0)	(4 5)
Interest charged on impaired loans	**0 5**	**–**	**0.5**	1 7	–	1 7
At the end of the year	**35.6**	**125.1**	**160 7**	27 5	127 8	155 3

All provisions are held against loans and advances to customers Within Group and Bank individual allowance for losses £0 3m (2006 £0 6m) of the closing balance relates to mortgages, reflecting a charge of £0 3m (2006 £0 2m) and write offs of £0 6m (2006 £nil) made in the year The reminder of individual allowance for losses relate to corporate lending The collective allowance relates to retail unsecured lending

13 Loans and advances to customers (continued)

Group and Bank loans and advances to customers include £29 1m (2006 £35 6m) of financial assets at fair value through profit or loss designated at initial recognition to eliminate or significantly reduce a measurement or recognition inconsistency

Loans and advances to customers include finance lease receivables

	Group		Bank	
	2007	2006	**2007**	2006
Gross investment in finance leases, receivable				
No later than one year	**47.2**	52 7	**40 8**	45 9
Later than one year and no later than five years	**101.4**	109 6	**77 9**	83 1
Later than five years	**72.2**	78 8	**32.1**	32 9
	220.8	241 1	**150.8**	161 9
Unearned future finance income on finance leases	**(47.2)**	(57 0)	**(22 6)**	(28 7)
Net investment in finance leases	**173.6**	184 1	**128 2**	133 2

The net investment in finance leases may be analysed as follows

	Group		Bank	
	2007	2006	**2007**	2006
No later than one year	**35.6**	41 5	**32 7**	38 5
Later than one year and no later than five years	**77.7**	84 9	**65.5**	70 7
Later than five years	**60 3**	57 7	**30.0**	24 0
	173 6	184 1	**128.2**	133 2

There are no finance lease unguaranteed residual values
The Group enters into finance lease and hire purchase arrangements with customers in a wide range of sectors including transport, retail and utilities

14 Debt securities

	Group		Bank	
	2007	2006	**2007**	2006
Debt securities				
-Listed	**843.3**	792 8	**843.3**	792 8
-Unlisted	**1,587 6**	1,960 3	**1,142.4**	1,576 8
	2,430 9	2,753 1	**1,985 7**	2,369 6
Included in cash equivalents	**693 3**	191 0	**693.3**	191 0

Listed debt securities at a fair value of £nil (2006 £nil) had been pledged to third parties in sale and repurchase agreements

Gains and losses from debt securities, included within interest income, comprise:

	2007	2006
Derecognition of available for sale assets	**(0.3)**	(0 8)

14. Debt securities (continued)

The movement in debt securities is summarised as follows:

	Group		Bank	
	2007	2006	**2007**	2006
At the beginning of the year	**2,753.1**	2,269 1	**2,369.6**	1,912 8
Acquisitions	**10,806.7**	7,456 1	**9,889.7**	6,721 1
Disposals and maturities	**(11,108 9)**	(6,887 1)	**(10,253.0)**	(6,179 6)
Exchange adjustments	**19.6**	(75 0)	**19.6**	(75 0)
Amortisation	**1.0**	(0 1)	**1.0**	(0 1)
Fair value movements – through equity	**(3 2)**	(9 9)	**(3.8)**	(9 6)
Fair value movements – through profit or loss	**(5.6)**	–	**(5.6)**	–
Impairment losses	**(31.8)**	–	**(31.8)**	–
At the end of the year	**2,430.9**	2,753 1	**1,985.7**	2,369 6

	Group		Bank	
	2007	2006	**2007**	2006
Issue				
Investment securities issued by public bodies				
Government securities	**91.6**	75 6	**91.6**	75 6
Other public sector securities	**1 0**	10 3	**1 0**	10 3
	92 6	85 9	**92 6**	85 9
Investment securities issued by other issuers				
Bank and building society certificates of deposits	**1,533 5**	1,874 0	**1,088.3**	1,490 5
Other debt securities	**804.8**	793 2	**804.8**	793 2
	2,338.3	2,667 2	**1,893.1**	2,283 7
	2,430 9	2,753 1	**1,985.7**	2,369 6

The fair value of the Bank's net exposure to structured investments of £31 4m has continued to move since 12 January 2008 At 29 February 2008, the latest date for which relevant information is available, values had fallen by a further £13m

15. Derivative financial instruments

The Bank has entered into various derivatives as principal either as a trading activity, which includes proprietary transactions and customer facilitation, or as a hedging activity for the management of interest rate 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 in 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

2007	Group			Bank		
	Contractual/notional amount	**Fair values Assets**	**Fair values Liabilities**	**Contractual/notional amount**	**Fair values Assets**	**Fair values Liabilities**
Derivatives held for trading						
Interest rate derivatives						
Interest rate swaps	**1,450 3**	**9.1**	**(7.5)**	**1,620.3**	**10.0**	**(8.2)**
Over the Counter (OTC) interest rate options	**136.4**	**0.5**	**(0 5)**	**136.4**	**0.5**	**(0.5)**
Total OTC derivatives	**1,586.7**	**9.6**	**(8.0)**	**1,756.7**	**10.5**	**(8.7)**
Total derivative assets/(liabilities) held for trading	**1,586.7**	**9.6**	**(8.0)**	**1,756.7**	**10 5**	**(8.7)**

15 Derivative financial instruments

	Group			Bank		
	Contractual/notional amount	Fair values Assets	Fair values Liabilities	Contractual/notional amount	Fair values Assets	Fair values Liabilities
Derivatives held for hedging						
Derivatives designated as cash flow hedges						
Interest rate swaps	**2,376.9**	**10.7**	**(12.4)**	**2,291.9**	**10.1**	**(12.3)**
Total derivative assets/(liabilities) designated as hedges	**2,376 9**	**10.7**	**(12.4)**	**2,291.9**	**10.1**	**(12.3)**
Derivatives held for non-trading purposes for which hedge accounting has not been applied						
Interest rate swaps	**709 0**	**0 6**	**(3.9)**	**709 0**	**0.6**	**(3.9)**
Embedded derivatives – options	**600.0**	**66.9**	**(66.5)**	**600 0**	**66.9**	**(66.4)**
Forward currency transactions	**115.8**	**0.4**	**(1 5)**	**115.8**	**0.4**	**(1.5)**
Total derivative assets/(liabilities) held for non trading	**3,801.7**	**78.6**	**(84.3)**	**3,716.7**	**78.0**	**(84.1)**
Total recognised derivative assets/(liabilities)	**5,388.4**	**88.2**	**(92.3)**	**5,473.4**	**88 5**	**(92.8)**

2006	Group			Bank		
	Contractual/notional amount	Fair values Assets	Fair values Liabilities	Contractual/notional amount	Fair values Assets	Fair values Liabilities
Derivatives held for trading						
Interest rate derivatives						
Interest rate swaps	3,346 4	6 0	(6 9)	3,506 4	7 1	(8 0)
Over the Counter (OTC) interest rate options	123 8	0 3	(0 3)	123 8	0 3	(0 3)
Total OTC derivatives	3,470 2	6 3	(7 2)	3,630 2	7 4	(8 3)
Exchange-traded interest rate futures	500 0	–	–	500 0	–	–
Total derivative assets/(liabilities) held for trading	**3,970 2**	**6 3**	**(7.2)**	**4,130.2**	**7 4**	**(8.3)**
Derivatives held for hedging						
Derivatives designated as cash flow hedges						
Interest rate swaps	2,430 0	2 6	(31 4)	2,350 0	2 6	(30 6)
Total derivative assets/(liabilities) designated as hedges	2,430 0	2 6	(31 4)	2,350 0	2 6	(30 6)
Derivatives held for non-trading purposes for which hedge accounting has not been applied						
Interest rate swaps	950 5	1 4	(4 9)	950 5	1 4	(4 9)
Embedded derivatives – options	515 0	73 4	(73 7)	515 0	73 4	(73 7)
Forward currency transactions	200 9	0 7	(0 5)	200 9	0 7	(0 5)
Total derivative assets/(liabilities) held for non trading	**4,096.4**	**78 1**	**(110.5)**	**4,016.4**	**78.1**	**(109.7)**
Total recognised derivative assets/(liabilities)	**8,066.6**	**84.4**	**(117.7)**	**8,146.6**	**85 5**	**(118.0)**

The derivatives designated as cash flow 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

The number of non-margin exchange traded contracts held by the Bank at the year end was none (2006 none)

16. Equity shares

	Group and Bank 2007	2006
Investment securities – unlisted	**8.8**	1 7
Included above are the following trade investments		
Vocalink Limited **3,499,900** ordinary shares of £1 each (2006 nil)	**8.7**	–
BACS Limited **nil** ordinary shares of £1 each (2006 176,733)	**–**	1 2
LINK Interchange Network Limited **nil** ordinary shares of £1 each (2006 3,845)	**–**	0 4
and **nil** ordinary shares of £0 01 each (2006 78,396)	**8.7**	1 6

Equity shares are classified as available for sale

During 2007, BACS Limited and LINK Interchange Network Limited merged to form Vocalink Limited As a result, the Bank revalued its shareholding of the newly formed company

17 Intangible fixed assets

	Group 2007	Group 2006	Bank 2007	Bank 2006
Cost				
At the beginning of the year	**21 2**	18 6	**20.3**	18 6
Additions	**1.6**	4 1	**1 4**	3 2
Disposals	**–**	(1 5)	**–**	(1 5)
At the end of the year	**22.8**	21 2	**21 7**	20 3
Accumulated amortisation				
At the beginning of the year	**14.0**	12 0	**14.0**	12 0
Disposals	**–**	(1 3)	**–**	(1 3)
Charge for the year	**3.6**	3 3	**3.4**	3 3
At the end of the year	**17.6**	14 0	**17.4**	14 0
Net book value				
Net book value at the end of the year	**5.2**	**7 2**	**4.3**	**6.3**
Net book value at the beginning of the year	7 2	6 6	6 3	6 6

18 Property, plant and equipment

	Freehold and leasehold buildings	Computer and other equipment	Total
2007			
Group.			
Cost			
At the beginning of the year	**10.3**	**182 1**	**192.4**
Additions	**–**	**13.1**	**13.1**
Disposals	**–**	**(19.3)**	**(19.3)**
At the end of the year	**10.3**	**175.9**	**186.2**
Accumulated depreciation			
At the beginning of the year	**3.1**	**95.5**	**98.6**
Disposals	**–**	**(11.3)**	**(11.3)**
Charge for the year	**0.2**	**18.9**	**19.1**
At the end of the year	**3.3**	**103 1**	**106.4**
Net book value			
Net book value at the end of the year	**7.0**	**72.8**	**79.8**
Net book value at the beginning of the year	7 2	86 6	93 8

18. Property, plant and equipment (continued)

	Freehold and leasehold buildings	Computer and other equipment	Total
2007			
Bank:			
Cost			
At the beginning of the year	**2 8**	**178.9**	**181.7**
Additions	**-**	**12.8**	**12 8**
Disposals	**-**	**(17.8)**	**(17.8)**
At the end of the year	**2.8**	**173.9**	**176.7**
Accumulated depreciation			
At the beginning of the year	**1 0**	**92.9**	**93.9**
Disposals	**-**	**(9.8)**	**(9 8)**
Charge for the year	**-**	**18.6**	**18.6**
At the end of the year	**1.0**	**101.7**	**102.7**
Net book value			
Net book value at the end of the year	**1.8**	**72.2**	**74.0**
Net book value at the beginning of the year	1 8	86 0	87 8
2006			
Group:			
Cost			
At the beginning of the year	10 3	189 8	200 1
Additions	–	38 5	38 5
Disposals	–	(46 2)	(46 2)
At the end of the year	10 3	182 1	192 4
Accumulated depreciation			
At the beginning of the year	2 8	111 2	114 0
Disposals	–	(36 5)	(36 5)
Charge for the year	0 3	20 8	21 1
At the end of the year	3 1	95 5	98 6
Net book value			
Net book value at the end of the year	7 2	86 6	93 8
Net book value at the beginning of the year	7 5	78 6	86 1
2006			
Bank:			
Cost			
At the beginning of the year	2 8	186 5	189 3
Additions	–	38 4	38 4
Disposals	–	(46 0)	(46 0)
At the end of the year	2 8	178 9	181 7
Accumulated depreciation			
At the beginning of the year	1 0	108 5	109 5
Disposals	–	(36 3)	(36 3)
Charge for the year	–	20 7	20 7
At the end of the year	1 0	92 9	93 9
Net book value			
Net book value at the end of the year	1 8	86 0	87 8
Net book value at the beginning of the year	1 8	78 0	79 8

18 Property, plant and equipment (continued)

	Group 2007	Group 2006	Bank 2007	Bank 2006
The net book value of land and buildings comprises				
Freehold	**7.0**	7 2	**1.8**	1 8
Short leasehold	**–**	–	**–**	–
	7 0	7 2	**1.8**	1 8

All land and buildings are occupied by the Group for its own activities Included within property, plant and equipment are finance leased assets At 12 January 2008, the net book value of these assets was £nil (2006 £nil)

19. Other assets

	Group 2007	Group 2006	Bank 2007	Bank 2006
Trade debtors	**3.1**	6 8	**3.1**	6 7
Other assets	**13 4**	37 3	**13.3**	37 2
	16.5	44 1	**16.4**	43 9

20 Deposits by banks

	Group 2007	Group 2006	Bank 2007	Bank 2006
Items in course of collection	**5.6**	5 7	**5.6**	5 7
Deposits from other banks	**655.7**	694 9	**655.7**	694 9
	661.3	700 6	**661.3**	700 6
of which				
Variable rate	**54 2**	48 1	**54.2**	48 1
Fixed rate	**607.1**	652 5	**607 1**	652 5

21 Customer accounts

	Group 2007	Group 2006	Bank 2007	Bank 2006
Variable rate	**9,187.2**	8,050 6	**8,784 3**	7,686 1
Fixed rate	**1,372.3**	1,493 7	**1,283 8**	1,433 2
	10,559.5	9,544 3	**10,068 1**	9,119 3

22 Debt securities in issue

	Group 2007	Group 2006	Bank 2007	Bank 2006
Bonds and medium term notes	**–**	300 0	**–**	300 0
Other debt securities in issue	**535.8**	813 3	**535 8**	813 3
	535.8	1,113 3	**535.8**	1,113 3

23 Other borrowed funds

	Group 2007	Group 2006	Bank 2007	Bank 2006
£30,000,000 Subordinated Perpetual Floating Rate Notes	**–**	30 0	**–**	30 0
£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
Subordinated Notes 2021	**150.0**	150 0	**150.0**	150 0
Issue costs and discount	**(1.9)**	(2 2)	**(1 9)**	(2 2)
	358.1	387 8	**358.1**	387 8

The Group has not had any defaults of principal, interest or redemption amounts during the period on its borrowed funds (2006 Nil)

23 Other borrowed funds (continued)

Subordinated Perpetual Floating Rate Notes

The notes were issued on 9 January 1998

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 1 18% above six months LIBOR up to (but excluding) 9 January 2008 Thereafter the notes carry an annual interest rate of 2 18% above six months LIBOR Interest is payable half yearly in arrears on 9 January and 9 July each year

The Bank redeemed all of the notes at their principle amount on 9 January 2008

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 annual 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

No early repayment, which includes the purchase of the notes or stock by the Group for cancellation, of any of the above subordinated liabilities can be made without the prior written agreement of the Financial Services Authority

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 a 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

Subordinated Notes due November 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 a 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% per annum 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 3 month 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

24 Other liabilities

	Group		Bank	
	2007	2006	**2007**	2006
Trade creditors	**103 8**	108 1	**102.5**	106 9

25 Provision for liabilities

	2007				2006			
Group	**Property**	**Restructuring**	**Compensation**	**Total**	Property	Restructuring	Compensation	Total
At the beginning of the year	**5.5**	**–**	**1.3**	**6.8**	4 2	–	1 9	6 1
Utilised	**(1 5)**	**(8.2)**	**(0.1)**	**(9 8)**	(0 3)	–	(0 3)	(0 6)
Profit and loss charge	**1.7**	**11 0**	**(0.3)**	**12.4**	1 6	–	(0 3)	1 3
At the end of the year	**5 7**	**2.8**	**0.9**	**9.4**	5 5	–	1 3	6 8

25. Provision for liabilities (continued)

Bank	2007 Property	2007 Restructuring	2007 Compensation	2007 Total	2006 Property	2006 Restructuring	2006 Compensation	2006 Total
At the beginning of the year	**5.0**	**–**	**0.9**	**5.9**	3 8	–	1 4	5 2
Utilised	**(1 4)**	**(8.2)**	**(0.1)**	**(9.7)**	(0 2)	–	(0 1)	(0 3)
Profit and loss charge	**1 7**	**11 0**	**(0 1)**	**12.6**	1 4	–	(0 4)	1 0
At the end of the year	**5 3**	**2 8**	**0 7**	**8.8**	5 0	–	0 9	5 9

Payments under future unavoidable lease commitments, net of amounts receivable under sub-lettings, are due on leases terminating between 2008 and 2020 Payments relating to past pension and investment advice will be made as individual cases are settled The amounts provided in respect of compensation are based on a case by case review of expected payment for each outstanding claim and an estimate of the number and value of future claims based on past experience

26. Deferred tax

Deferred taxes are calculated on all temporary differences under the liability method using an effective tax rate of 28% (2006 30%)

The movement on the deferred tax accounts are as follows

	Group 2007	Group 2006	Bank 2007	Bank 2006
Net deferred tax at the beginning of the year	**1 9**	14 8	**8.3**	21 1
Income statement credit	**2.3**	1 9	**1 3**	1 4
Charged to equity				
Significant item	**–**	(32 8)	**–**	(32 0)
Unrealised appreciation on investments	**(2.2)**	–	**(2.2)**	–
Pension fund deficit	**–**	5 8	**–**	5 7
Cash flow hedges	**(8.2)**	12 2	**(8 1)**	12 1
Net deferred tax at the end of the year	**(6.2)**	1 9	**(0 7)**	8 3
Net deferred tax comprises				
Deferred tax asset	**5 4**	14 6	**5.3**	14 6
Deferred tax liability	**(11.6)**	(12 7)	**(6.0)**	(6 3)
	(6.2)	1 9	**(0.7)**	8 3
Deferred taxation				
Cash flow hedges	**0.5**	8 7	**0 6**	8 7
Unrealised appreciation on investments	**(2.2)**	–	**(2.2)**	–
Capital allowances on fixed assets	**(3 6)**	(4 9)	**(3 2)**	(4 5)
Capital allowances on assets leased to customers	**(6.4)**	(7 8)	**(1.1)**	(1 8)
Other temporary differences	**5.1**	5 9	**5.2**	5 9
Restatement of deferred tax to 28%	**0 4**	–	**–**	–
	(6 2)	1 9	**(0.7)**	8 3

The deferred tax charge in the income statement comprises the following temporary differences

	Group 2007	Group 2006	Bank 2007	Bank 2006
Capital allowances on fixed assets	**(1.3)**	(2 9)	**(1.3)**	(2 9)
Capital allowances on assets leased to customers	**(1.4)**	1 7	**(0.7)**	2 2
Other temporary differences	**0.8**	(0 7)	**0.7**	(0 7)
Restatement of deferred tax to 28%	**(0 4)**	–	**–**	–
	(2 3)	(1 9)	**(1 3)**	(1 4)

27. Pensions

Prior to 5 April 2006, The Bank operated a funded pension scheme of the defined benefit type This provided benefits based on final pensionable pay The assets of the scheme were held in a separate trustee administered fund

However, in common with the majority of other UK employers, Co-operative Group faced increasing costs and risks in the provision of occupational pension schemes for its employees, including Executives In view of this, a strategic review of employee pension provision was completed during 2005 The review covered pension arrangements for all employees, including Executives, in Co-operative Group and its financial services subsidiaries, CFS, CIS and the Bank

As a consequence of this review, some significant changes to occupational pension arrangements were implemented with effect from 6 April 2006, with the approval of the Trustees of the Co-operative Group Pension Fund, the CIS Employees' Pension Scheme and The Co-operative Bank Pension Scheme (the Former Schemes)

The key changes were
- The Former Schemes were transferred into a new pension scheme on 6 April 2006
- The new scheme, the Co-operative Group Pension (Average Career Earnings) Scheme (PACE), is available to all employees of the Trading Group and Financial Services businesses It provides pensions and other benefits based on Career Average Earnings, revalued for inflation, in respect of pensionable service from 6 April 2006
- Executives and employees are provided with benefits from PACE on the same terms
- Accrued benefits under the Former Schemes as at 5 April 2006 are linked to final pensionable salary at the Executive or employees' actual date of leaving or retirement, whichever earlier
- PACE members contribute 6% of their pensionable salary

Therefore, from 5 April 2006, the Bank has accounted for its funded pension obligations on a defined contribution basis As at 5 April 2006, the Bank had a scheme deficit of £109 2m which was transferred to the Co-operative Group for no consideration This meets the definition of a settlement under IAS 19 and the resultant gain was recognised as a significant item in the income statement

The Bank also operates a small unfunded pension scheme The pension charge was assessed in the same manner and using the same assumptions as the funded scheme

The pension charge was assessed in accordance with the advice of a qualified actuary The latest full actuarial valuation of the funded scheme was at 5 April 2003
The actuarial valuation was updated to 5 April 2006 The principal assumptions used to calculate the schemes' liabilities were

	2007	2006	2005
Expected return on scheme assets	**N/A**	N/A	6 1%
Rate of increase of pensions in payment	**3.4%**	2 9%	2 7%
Rate of increase in salaries	**4 9%**	4 4%	4 2%
Discount rate	**5.7%**	4 9%	4 6%

The assumptions used by the actuary were the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice

The values of the assets and liabilities of the schemes were

	Group		**Bank**	
	2007	2006	**2007**	2006
Present value of unfunded obligations	**(3.5)**	(3 1)	**(3.5)**	(3 1)
Deficit in the scheme	**(3.5)**	(3 1)	**(3 5)**	(3 1)
Related deferred tax asset	**1.0**	0 9	**1.0**	0 9
Net pension liability	**(2.5)**	(2 2)	**(2.5)**	(2 2)

The unfunded obligation has been reclassified to be shown within accruals

Analysis of amount charged to income statement				
Current service cost	**0.1**	4 8	**0 1**	4 7
Expected return on pension scheme assets	**-**	(5 9)	**-**	(5 7)
Interest on pension scheme liabilities	**0.2**	5 4	**0.2**	5 3
	0.3	4 3	**0.3**	4 3

27. Pensions (continued)

	Group		Bank	
	2007	2006	**2007**	2006
Expected return on scheme assets	–	5 9	–	5 7
Actuarial gains	–	8 8	–	8 7
Actual return on scheme assets	–	14 7	–	14 4

Changes in the present value of the scheme liabilities are as follows

	Group		Bank	
	2007	2006	**2007**	2006
Opening defined benefit liabilities	**3 1**	524 2	**3.1**	511 9
Current service cost	**0.1**	4 8	**0.1**	4 7
Interest on liabilities	**0.2**	5 4	**0.2**	5 3
Contributions by members	–	0 8	–	0 8
Actuarial losses	**0.3**	28 3	**0.3**	27 7
Benefits paid	**(0.2)**	(1 9)	**(0 2)**	(1 9)
Transferred on implementation of PACE	–	(558 5)	–	(545 4)
Closing defined benefit liabilities	**3.5**	3 1	**3 5**	3 1

Actuarial losses arose in the period to 5 April 2006 as the mortality assumptions used were strengthened to the PA92 mortality table with the medium cohort projections and an age rating of plus one year This was in line with the market median

Changes in the fair value of the scheme assets are as follows

	Group		Bank	
	2007	2006	**2007**	2006
Opening fair value of scheme assets	–	432 1	–	421 9
Expected return on scheme assets	–	5 9	–	5 7
Actuarial gains	–	8 8	–	8 7
Contributions by the employer	–	3 4	–	3 3
Contributions by members	–	0 8	–	0 8
Benefits paid	–	(1 7)	–	(1 7)
Transferred on implementation of PACE	–	(449 3)	–	(438 7)
Closing fair value of scheme assets	–	–	–	–

Amounts recognised in the statement of recognised income and expense

	Group		Bank	
	2007	2006	**2007**	2006
Actuarial losses on scheme liabilities during period	**(0 3)**	(28 3)	**(0.3)**	(27 7)
Actuarial gains on scheme assets during period	–	8 8	–	8 7
Total scheme (losses)/gains during period	**(0.3)**	(19 5)	**(0.3)**	(19 0)
Cumulative actuarial losses on scheme liabilities	**(44.0)**	(43 7)	**(43.0)**	(42 7)
Cumulative actuarial gains on scheme assets	**70.7**	70 7	**69.1**	69 1
Cumulative total scheme gains	**26.7**	27 0	**26.1**	26 4

The amounts for the current period are as follows

	Group		Bank	
	2007	2006	**2007**	2006
Defined benefit obligation	**(3.5)**	(3 1)	**(3.5)**	(3 1)
Scheme assets	–	–	–	–
Deficit	**(3 5)**	(3 1)	**(3.5)**	(3 1)
Experience adjustment on scheme liabilities	–	0 1	–	0 1
Experience adjustment on scheme assets	–	8 8	–	8 7

27 Pensions (continued)

Post-PACE

With effect from 6 April 2006 the Bank, along with other businesses within 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 the liabilities, assets and cost to individual companies participating in the Scheme Therefore the pension costs shown in these accounts in respect of the Scheme for the period after 6 April are the actual contributions paid by the Bank A surplus of £438m (2006 £295m) in respect of the PACE scheme is recognised within Co-operative Group Limited consolidated accounts as at 12 January 2008

28 Share capital

	Group and Bank	
	2007	2006
Authorised		
1,100,000,000 ordinary shares of 5p each	**55 0**	55 0
Allotted, called up and fully paid		
1,100,000,000 ordinary shares of 5p each	**55 0**	55 0
Share premium account	**8 8**	8 8
	63.8	63 8

The shareholders have one vote for every share held

29 Reserves and retained earnings

	Group	Bank
Retained earnings		
At 14 January 2006	**527.9**	**506.8**
Net profit for year	123 4	119 0
Dividend	(4 2)	(4 2)
Retirement benefit schemes	(13 4)	(13 3)
At 13 January 2007	**633.7**	**608.3**
Net profit/(loss) for year	3 2	(1 1)
Dividend	(9 0)	(9 0)
Retirement benefit schemes	(0 3)	(0 3)
At 12 January 2008	**627 6**	**597.9**

	Group		Bank	
	2007	2006	**2007**	2006
Other reserves				
Revaluation reserve – available for sale investments	**(0.2)**	(2 2)	**(0.2)**	(2 1)
Hedging reserve – cash flow hedges	**(1.2)**	(20 5)	**(1.2)**	(20 4)
	(1.4)	(22 7)	**(1 4)**	(22 5)

	Group		Bank	
	2007	2006	**2007**	2006
Revaluation reserve – available for sale investments				
At the beginning of the year	**(2.2)**	4 0	**(2.1)**	4 0
Net gains/(losses) from changes in fair value	**3.1**	(9 7)	**3.0**	(9 6)
Income tax	**(0 9)**	2 9	**(0.9)**	2 9
Net gains/(losses) transferred to net profit on disposal	**(0 3)**	0 8	**(0.3)**	0 8
Deferred tax	**0.1**	(0 2)	**0 1**	(0 2)
At the end of the year	**(0.2)**	(2 2)	**(0.2)**	(2 1)

29. Reserves and retained earnings (continued)

Hedging reserve – cash flow hedges	Group 2007	Group 2006	Bank 2007	Bank 2006
At the beginning of the year	**(20 5)**	8 0	**(20.4)**	7 9
Gains/(losses) from changes in fair value	**28.3**	(40 6)	**28.1**	(40 3)
Deferred tax	**(8.5)**	12 2	**(8.4)**	12 1
Transferred to net profit	**(0 5)**	(0 1)	**(0.5)**	(0 1)
At the end of the year	**(1 2)**	(20 5)	**(1.2)**	(20 4)

Dividends

After the balance sheet date the following dividends were proposed by the directors The dividends have not been provided for and there are no income tax consequences

	2007	2006
Nil per ordinary share (2006 0 82p)	–	9 0

30 Statement of changes in equity

	Group 2007	Group 2006	Bank 2007	Bank 2006
Equity at the beginning of the year	**699.2**	**626.6**	**649.6**	**582.5**
Total recognised income and expense for the year	**27.6**	77 7	**19.7**	71 3
Dividend – equity shareholders	**(9.0)**	(4 2)	**(9 0)**	(4 2)
Dividend – minority interests	**(0.9)**	(0 9)	–	–
Equity at the end of the year	**716.9**	**699.2**	**660.3**	**649 6**

31 Contingent liabilities and commitments

The tables below give, for the Group and the 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 Solvency Ratio Directive on capital adequacy for 2006 and the Capital Requirements Directive (CRD) for 2007

	Contract amount 2007	Credit equivalent amount (i) 2007	Average risk weight 2007	Risk weighted amount 2007	Contract amount 2006	Risk weighted amount 2006
Group						
Contingent liabilities						
– Guarantees and irrevocable letters of credit	**90.9**	**79.7**	**60 2%**	**48 0**	77 0	62 1
	90 9	**79.7**			77 0	62 1
Bank						
Contingent liabilities						
– Guarantees and irrevocable letters of credit	**87.6**	**78.1**	**59.3%**	**46 3**	72 9	60 0
	87 6	**78.1**			72 9	60 0
Group						
Other commitments						
– Documentary credits and short-term trade-related transactions	**1.6**	**0.3**	**77.1%**	**0 2**	1 9	0 4
Forward assets purchases and forward deposit placed	**215.0**	**215 0**	**6.4%**	**13 8**	50 0	10 0
Undrawn formal standby facilities, credit lines and other commitments to lend (includes revocable and irrevocable commitments)	**6,155 1**	**3,048.3**	**44 8%**	**1,364.6**	**5,762.6**	**213.8**
	6,371.7	**3,263.6**	**42.2%**	**1,378 6**	5,814 5	224 2

31. Contingent liabilities and commitments (continued)

	Contract amount 2007	Credit equivalent amount (i) 2007	Average risk weight 2007	Risk weighted amount 2007	Contract amount 2006	Risk weighted amount 2006
Bank						
Other commitments						
– Documentary credits and short-term trade-related transactions	**1.6**	**0.3**	**77.1%**	**0.2**	1 9	0 4
Forward assets purchases and forward deposit placed	**215.0**	**215.0**	**6.4%**	**13.8**	50 0	10 0
Undrawn formal standby facilities, credit lines and other commitments to lend (includes revocable and irrevocable commitments)	**6,147.8**	**3,048.3**	**44.8%**	**1,364.6**	5,753 5	213 8
	6,364 4	**3,263.6**	**42.2%**	**1,378 6**	5,805 4	224 2

Notes

(i) Under the Solvency Ratio Directive, credit equivalent amounts, obtained by applying credit conversion factors, are risk weighted according to counterparty Under the CRD Credit conversion factors are applied to exposures subject to the Standardised 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 (EAD)

(ii) Undrawn loan commitments consist largely of undrawn credit card facilities

Assets pledged

Assets are pledged as collateral under repurchase agreements with other banks

Mandatory reserve deposits are also held with the Bank of England in accordance with statutory requirements

These deposits are not available to finance the Group's day-to-day operations

	Asset		Related liability	
	2007	2006	**2007**	2006
Balances with central banks	**11.3**	10 6	**–**	–

Operating lease commitments

	2007 Land and buildings	2006 Land and buildings
At the year end, the future minimum lease payments under non-cancellable operating leases were		
Group		
– Expiring		
– within one year	**1.4**	0 4
– between one and five years	**4 1**	5 5
– in five years or more	**105.4**	102 5
	110.9	108 4
Bank		
– Expiring		
– within one year	**1.4**	0 4
– between one and five years	**3 3**	4 5
– in five years or more	**109.6**	107 2
	114 3	112 1

Unauthorised overdraft charges

In July 2007, the Office of Fair Trading (OFT) launched a test case in the High Court to determine the status and enforceability of certain of the charges applied to customers in relation to requests for unplanned overdrafts Pending resolution of the test case, the Financial Services Authority has agreed, subject to conditions, that the handling of customer complaints on this issue can be suspended unless in the light of prevailing circumstances this would be inappropriate A range of outcomes is possible from the test case and any appeal, some of which could have a significant financial impact on the Group It is not considered appropriate to make provision or quantify for a wide range of potential outcomes before the conclusion of the legal process

32. Related party transactions

Co-operative Financial Services Limited owns 100% of the issued ordinary share capital of the Bank and is the Bank's immediate holding company 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 (formally known as Co-operative Group (CWS) Limited), which is incorporated in England and is 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 The principal operating subsidiaries of The Co-operative Bank p l c , all of which are incorporated in and operate in England, and none of which are quoted, are

Operating subsidiaries	**Nature of business**	**Total issued share capital at 12 January 2008**	**Group interest 2007**	Group interest 2006
Unity Trust Bank p l c *	Banking	16,428,460 Ordinary shares of £1 each	**27%**	27%
Co-operative Commercial Limited	Investment company	1,000,000 Ordinary shares of £1 each	**100%**	100%
Roodhill Leasing Limited	Leasing	2 Ordinary shares of £1 each	**100%**	100%
First Roodhill Leasing Limited	Leasing	100 Ordinary shares of £1 each	**100%**	100%
Second Roodhill Leasing Limited	Leasing	100 Ordinary shares of £1 each	**100%**	100%
Third Roodhill Leasing Limited	Leasing	100 Ordinary shares of £1 each	**100%**	100%
Fourth Roodhill Leasing Limited	Leasing	100 Ordinary shares of £1 each	**100%**	100%
Co-operative Bank Financial Advisers Limited	Financial advisers	1,600,000 Ordinary shares of £1 each	**100%**	100%

* Held through subsidiary undertaking

Shares in Group undertakings.

Bank	**Cost**	**Provision**	**Carrying value**
At 13 January 2007 and 12 January 2008	**3.1**	**(0 4)**	**2 7**

The above provision is held against dormant subsidiaries
Details of all Group companies will be annexed to the Bank's next annual return

Unity Trust Bank p l c is considered to be a subsidiary undertaking of The Co-operative Bank p l c as The Co-operative Bank p l c elects a majority of the Directors and appoints the Chair and Managing Director of Unity Trust Bank p l c This provides the power to control

The financial statements of the above undertaking are consolidated into the Group financial statements

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 are considered to be Board and Executive members of the Group and Board and Executives 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

	Group and Bank Directors and key management personnel 2007	2006
Loans outstanding at the beginning of the year	**0.5**	1 8
Interest and fee income earned	**–**	0 1
Net movement	**0 8**	(1 4)
Loans outstanding at the end of the year	**1.3**	0 5
Deposits at the beginning of the year	**2.7**	4 3
Interest and fee expense	**0.2**	0 2
Net movement	**(0.5)**	(1 8)
Deposits at end of the year	**2.4**	2 7

32 Related party transactions (continued)

	Associated companies			
	Group		Bank	
	2007	2006	**2007**	2006
Loans at the beginning of the year	**-**	0 3	**34.9**	40 9
Interest and fee income earned	**4.0**	2 6	**5.2**	4 1
Net movement	**88.9**	(2 9)	**86.3**	(10 1)
Loans at the end of the year	**92.9**	–	**126.4**	34 9
Deposits at the beginning of the year	**201 9**	154 7	**203 8**	161 7
Interest and fee income earned	**(0 4)**	(0 8)	**(0 4)**	(0 8)
Interest and fee income paid	**2.3**	1 9	**2.3**	1 9
Net movement	**30.4**	46 1	**28.5**	41 0
Deposits at the end of the year	**234.2**	201 9	**234.2**	203 8
Loans to banks include				
Due from subsidiary undertakings	**-**	–	**7.4**	2 5
Loans to customers include				
Due from subsidiary undertakings	**-**	–	**26.1**	32 4
Due from parent undertakings	**84.0**	–	**84.0**	–
Due from fellow subsidiary undertakings	**8 9**	–	**8 9**	–
Deposits by banks include				
Due to subsidiary undertakings	**-**	–	**-**	–
Customer accounts include				
Due to subsidiary undertakings	**-**	–	**3.7**	1 9
Due to parent undertakings	**92.2**	126 3	**92.2**	126 3
Due to fellow subsidiary undertakings	**139.0**	64 8	**139.0**	64 8
Due to associated undertakings	**-**	–	**-**	–

Key management compensation

	Group and Bank	
	2007	2006
Salaries and other short term benefits	**4 3**	3 8
Termination benefits	**0.4**	0 3
	4.7	4 1

Directors' remuneration

A listing of the members of the Board of Directors is shown on page 24
The total remuneration of the Directors was £3 2m (2006 £2 7m)

Futher details of Directors' remuneration are provided on pages 34 to 38

Consolidated income statement history

	2004	2005	2006	2007	Change	Change
Net interest income	318 0	320 5	320 3	**334.8**	14 5	4 5%
Non interest income	186 7	205 9	201 2	**188.7**	(12 5)	(6 2%)
Operating income	**504 7**	**526.4**	**521.5**	**523.5**	**2.0**	**0.4%**
Operating costs	(319 7)	(328 8)	(339 9)	**(339 3)**	0 6	0 2%
Profit before impairment losses	**185.0**	**197.6**	**181.6**	**184 2**	**2.6**	**1.4%**
Impairment losses on loans and advances	(70 7)	(99 8)	(105 3)	**(102 0)**	3 3	3 1%
Impairment losses on structured investments	–	–	–	**(31.8)**	(31 8)	–
Operating profit	**114 3**	**97 8**	**76.3**	**50.4**	**(25.9)**	**(34 0%)**
Membership dividend	–	(1 3)	(1 2)	**(1.3)**	(0 1)	(8 3%)
Profit before taxation	**114.3**	**96.5**	**75 1**	**49.1**	**(26.0)**	**(34.6%)**
Significant items	–	–	109 2	**(38 0)**	(147 2)	(134 8%)
Income tax expense	(36 0)	(30 9)	(57 4)	**(5.2)**	52 2	90 9%
Profit for the year	**78.3**	**65.6**	**126.9**	**5 9**	**(121.0)**	**(95.4%)**
Minority interest	(2 1)	(2 4)	(2 2)	**(2 7)**	(0 5)	(22 7%)
Dividends	(15 0)	(18 8)	(4 2)	**(9.0)**	(4 8)	(114 3%)
Retentions	61 2	44 4	120 5	**(5.8)**	(126 3)	(104 8%)
Average numbers of staff	4,356	4,238	4,234	**4,281**		
Net interest margin	3 3%	3 0%	2 7%	**2.7%**		
Cost/income ratio	63 3%	62 5%	65 2%	**64 8%**		
Earnings per share	6 93p	5 75p	11 22p	**0 29p**		

Summarised average balance sheet

	2004	2005	2006	2007	Change	Change
Customer Lending						
Retail Sector						
Visa	1,059	1,070	1,036	**914**	(122)	(11 8%)
Other	4,070	4,407	4,251	**4,134**	(117)	(2 7%)
Corporate Sector	1,845	2,089	2,443	**2,952**	509	20 8%
Total	6,974	7,566	7,730	**8,000**	270	3 5%
Wholesale Placements						
Debt Securities	1,723	2,012	2,821	**2,883**	62	2 2%
Wholesale Lending	915	1,193	1,286	**1,321**	35	2 7%
Other Assets	293	361	327	**273**	(54)	(16 5%)
Total Assets	**9,905**	**11,132**	**12,164**	**12,477**	**313**	**2 6%**
Customer Deposits						
Retail Sector	4,483	4,787	5,279	**5,756**	477	9 0%
Corporate Sector	2,083	2,244	2,371	**2,579**	208	8 8%
Total	6,566	7,031	7,650	**8,335**	685	9 0%
Wholesale Deposits	2,142	2,792	3,229	**2,801**	(428)	(13 3%)
Other Liabilities	255	266	246	**304**	58	23 5%
Subordinated Debt	354	325	286	**328**	42	14 6%
Preference Share Capital	60	60	60	**60**	–	–
Equity Share Capital, Reserves	528	658	693	**649**	(44)	(6 4%)
Total Liabilities	**9,905**	**11,132**	**12,164**	**12,477**	**313**	**2.6%**

NOTICE IS HEREBY GIVEN that the Annual General Meeting of The Co-operative Bank p l c will be held at the Board Room, 24th floor, CIS Building, Miller Street, Manchester, M60 0AL, on 16 May 2008 at 9 am for the following purposes

1 To receive the Notice convening the meeting
2 To receive the Annual Reports and adopt the Financial Statements for the year ended 12 January 2008 together with the Auditor's Report
3 To approve the Remuneration Report for the year ended 12 January 2008
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 2007 be confirmed
   (ii) that a dividend of 4 625p per £1 share be declared and paid on 30 May 2008 to the registered holders as at 2 May 2008 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
   (i) Terry Morton, Non-Executive Director
   (ii) Len Wardle, Non-Executive Director,
   (iii) Stephen Watts, Non-Executive Director,
6 To re-appoint the following Directors who were appointed to the Board since the last Annual General Meeting of the Company
   (i) Robert Newton who was appointed to the Board on 1 August 2007,
   (ii) Martyn Wates who was appointed to the Board on 13 November 2007
7 That KPMG Audit Plc be and are hereby re-appointed auditor of the Company, to hold office from the conclusion of this meeting until the conclusion of the next General Meeting at which accounts are laid before the Company, at a remuneration to be fixed by the Directors

Registered Office:
1 Balloon Street
Manchester M60 4EP
Reg No 990937 (England)
Tel 0161 832 3456
Fax 0161 829 4475

Registrar:
Computershare Investor Services PLC
P O Box 82
The Pavilions
Bridgwater Road
Bristol BS99 7NH
Tel 0870 702 0003

By Order of the Board
Moira Lees,
Secretary
3 April 2008

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 9 00pm on 14 May 2008 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 page 24 of the Report and 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 Shareholders' 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

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