

**Cheltenham & Gloucester plc**  
**Annual Report and financial statements year ended 31 December 2012**  
**Company No 2299428**



**Member of Lloyds Banking Group**

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## **DIRECTORS' REPORT**

The Directors have pleasure in presenting the audited consolidated financial statements for Cheltenham & Gloucester plc for the year ended 31 December 2012

Cheltenham and Gloucester plc is a public limited company domiciled in the UK

### **Principal activities**

The principal activities of Cheltenham & Gloucester plc (the "Company") are the arranging and administering of mortgage and savings accounts on behalf of Lloyds TSB Bank plc (the "Bank"), the immediate parent company

The Company's subsidiaries are dormant with the exception of C&G Property Holdings Limited whose principal activity was that of property leasing to the Company. C&G Property Holdings Limited disposed of all its properties in the current year and so its principal activity has now ceased. It is expected to be liquidated in the next accounting period.

The Company and its subsidiaries are referred to in these financial statements as "C&G" or the "Group".

### **Results and dividends**

The consolidated profit on ordinary activities before tax for the year ended 31 December 2012 is £59.2 million (2011: £102.0 million).

The Directors recommend a dividend of £50 million for the year (2011: £50 million).

### **Business review and future developments**

The Company's primary objectives are to ensure that mortgages and savings accounts are sold and maintained properly and efficiently and the Company continues to focus on providing quality service to these account holders of the Bank.

The Company operates to service standards that have been agreed with the Bank, and is reimbursed for these services by the Bank. The Company remains well placed to continue to sell and administer mortgage and savings accounts for the Bank at the current high quality levels.

The Company's performance is measured by the Bank using a number of key performance indicators which are monitored and reviewed by the Bank on an on-going basis and are disclosed in the financial statements of Lloyds Banking Group. These indicators include, but are not limited to, dividends per share and profit before tax.

Within the Group, the subsidiaries of the Company are dormant except for C&G Property Holdings Limited. C&G Property Holdings Limited ceased to trade in the current year and is expected to be subjected to a Members Voluntary Liquidation in the next period.

### **Directors**

The Directors of the Company who were in office during the year and up to the date of signing the financial statements were as follows:

SJ Noakes  
AB Lenman (resigned 7 September 2012)  
RA Purdy (appointed 8 October 2012)  
PA Masserano (appointed 8 October 2012)

The Company Secretary who served during the year was P Gittins.

### **Policy and practice on payment of suppliers**

The Company follows "The Better Payment Practice Code" published by the Department for Business Innovation and Skills (BIS) regarding the making of payments to suppliers. A copy of the code and information about it may be obtained from the BIS Publications Order Line 0845 0150 010 quoting ref. URN 04/606.

The Company's policy is to agree terms of payment with suppliers and these normally provide for settlement within

**DIRECTORS' REPORT (Continued)**

**Policy and practice on payment of suppliers (continued)**

30 days after the date of the invoice, except where other arrangements have been negotiated. It is the policy of the Company to abide by the agreed terms of payment, provided the supplier performs according to the terms of the contract. The creditor days for 2012 are 14 (2011 22)

**Financial risk management**

The consideration of risks and uncertainties of the business such as interest rate risk, foreign currency risk, credit risk and liquidity risk are set out in note 23 to the financial statements. There are no areas of concern that carry significant risks of causing material changes to the carrying value of the Company's assets and liabilities.

**Independent auditors and disclosure of information to auditors**

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

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

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

PricewaterhouseCoopers LLP have indicated their willingness to continue in office and a resolution re-appointing them as auditors and authorising the Directors to set their remuneration will be proposed at the annual general meeting.

**Employees**

C&G and Lloyds Banking Group believe that diversity helps differentiate us from our competitors. We are committed to providing employment practices and policies which recognise the diversity of our workforce and ensure equality of opportunity for employees regardless of sex, race, disability, age, sexual orientation or religious belief. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with Lloyds Banking Group continues and the appropriate training is arranged.

We monitor progress on diversity annually and put in place programmes to improve the career experience of diverse groups. We believe that a committed workforce that reflects the diversity of our customers will have a positive impact on our results.

In the UK, Lloyds Banking Group belongs to employer groups including Employers' Forum on Disability, Employers' Forum on Age, Stonewall and the Race for Opportunity. Our involvement with these organisations enables us to identify and implement best practice for our staff.

Lloyds Banking Group operates a number of employee share schemes details of which are set out in note 20.

Employees are kept closely involved in major changes affecting them through such measures as team meetings, briefings, internal communications and opinion surveys. There are well established procedures, including regular meetings with recognised unions, to ensure that the views of employees are taken into account in reaching decisions.

Lloyds Banking Group is committed to providing employees with comprehensive coverage of the economic and financial issues affecting the Group. We have established a full suite of communication channels, including an extensive face-to-face briefing programme which allows us to update our employees on our performance and any financial issues throughout the year.

**Directors' indemnities**

The Directors have the benefit of a deed of indemnity which constitutes a "qualifying third party indemnity provision". These deeds are in force during the whole of the financial year (or from the date of appointment in respect of the

**DIRECTORS' REPORT (Continued)**

**Directors' indemnities (continued)**

Directors who join the board during the financial year) The indemnities remain in force at the date of signing these financial statements. Deeds for existing Directors are available for inspection at the registered office of Lloyds Banking Group plc

**Statement On Going Concern**

The Company is reliant on fee income provided by Lloyds TSB Bank plc which is a subsidiary of Lloyds Banking Group plc. The Directors are satisfied that it is the intention of Lloyds Banking Group plc that its subsidiaries including the Company will continue to have access to adequate liquidity and capital resources for the foreseeable future and, accordingly, the financial statements have been prepared on a going concern basis.

**DIRECTORS' RESPONSIBILITIES STATEMENT**

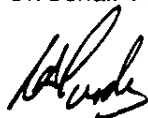
The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

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

- select suitable accounting policies and then apply them consistently,
- make judgements and accounting estimates that are reasonable and prudent,
- state whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements.

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

On behalf of the Board



**RA Purdy**  
Director

**17 April 2013**

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CHELTENHAM & GLOUCESTER PLC**

We have audited the group and parent company financial statements (the "financial statements") of Cheltenham & Gloucester plc for the year ended 31<sup>st</sup> December 2012 which comprise the Consolidated Statement of Comprehensive Income, Statements of financial position, Statements of Changes in Equity, Cash Flow Statements and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

**Respective responsibilities of directors and auditors**

As explained more fully in the Directors' Responsibilities Statement set out on page 4, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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

**Scope of the audit of the financial statements**

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

**Opinion on financial statements**

In our opinion:

- the financial statements give a true and fair view of the state of the group's and of the parent company's affairs as at 31<sup>st</sup> December 2012 and of the group's profit and group's and parent company's cash flows for the year then ended,
- the group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union,
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006, and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

**Opinion on other matter prescribed by the Companies Act 2006**

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

**Matters on which we are required to report by exception**

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us, or

**INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF CHELTENHAM & GLOUCESTER PLC**  
**(continued)**

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



Scott Berryman (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London  
17<sup>th</sup> April 2013

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME  
FOR THE YEAR ENDED 31 DECEMBER 2012**

	<b>Note</b>	<b>2012 £m</b>	<b>2011 £m Restated</b>
Interest income		2 3	-
Interest expense		(0 1)	(0 1)
<b>Net interest income</b>		<u>2 2</u>	<u>(0 1)</u>
Fee and commission income		340 5	435 7
<b>Other income</b>		<u>340 5</u>	<u>435 7</u>
<b>Total net income</b>		<u>342 7</u>	<u>435 6</u>
Operating expenses	2	(283 5)	(333 6)
<b>Profit before tax</b>	3	<u>59 2</u>	<u>102 0</u>
Taxation	4	(12 5)	(29 7)
<b>Profit for the financial year / total comprehensive income for the year</b>	5	<u>46 7</u>	<u>72 3</u>
<b>Profit for the financial year / total comprehensive income for the year attributable to shareholders arising from:</b>			
- Continuing operations		46 3	72 3
- Discontinued operations	24	0 4	-
		<u>46 7</u>	<u>72 3</u>

The activities of C&G Property Holdings Limited discontinued from 22 June 2012. All other activities of the Group continued throughout the year.

The 2011 figures have been restated to incorporate the release of the deferred tax asset in one of the Company's subsidiaries, this is explained in full in note 11.

The 2011 figures have also been restated to account for the reclassification of interest expense from fee and commission income.

The accompanying notes on pages 12 to 34 are an integral part of the financial statements.



**STATEMENTS OF FINANCIAL POSITION  
AT 31 DECEMBER 2012**

	<b>Note</b>	<b>Group 2012 £m</b>	<b>Group 2011 £m Restated</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
<b>Current assets</b>					
Loans and advances to banks	6	103 5	195 6	103 5	195 6
Due from Group Companies	7	265 1	197 1	265 1	201 0
Other assets		3 4	3 6	3 4	3 5
<b>Total current assets</b>		<u>372 0</u>	<u>396 3</u>	<u>372 0</u>	<u>400 1</u>
<b>Non-current assets</b>					
Tangible fixed assets	8	23 8	37 3	23 8	28 7
Deferred tax asset	11	8 0	8 8	8 0	8 8
Shares in subsidiaries	12	-	-	-	1 3
<b>Total non-current assets</b>		<u>31 8</u>	<u>46 1</u>	<u>31 8</u>	<u>38 8</u>
<b>Total assets</b>		<u>403 8</u>	<u>442 4</u>	<u>403 8</u>	<u>438 9</u>
<b>Equity and liabilities</b>					
<b>Current liabilities</b>					
Current tax liabilities		35 9	24 2	35 7	24 0
Owed to Group Companies	13	104 3	123 3	109 6	123 1
Other liabilities	14	27 1	49 1	27 1	49 4
Provisions	15	-	-	-	-
<b>Total current liabilities</b>		<u>167 3</u>	<u>196 6</u>	<u>172 4</u>	<u>196 5</u>
<b>Non-current liabilities</b>					
Other borrowed funds	17	5 0	5 0	5 0	5 0
Retirement benefit obligations	16	45 3	51 3	45 3	51 3
<b>Total non-current liabilities</b>		<u>50 3</u>	<u>56 3</u>	<u>50 3</u>	<u>56 3</u>
<b>Total liabilities</b>		<u>217 6</u>	<u>252 9</u>	<u>222 7</u>	<u>252 8</u>
<b>Equity</b>					
Called up share capital	18	70 0	70 0	70 0	70 0
Retained earnings		116 2	119 5	111 1	116 1
<b>Total equity attributable to owners of the parent</b>		<u>186 2</u>	<u>189 5</u>	<u>181 1</u>	<u>186 1</u>
<b>Total equity and liabilities</b>		<u>403 8</u>	<u>442 4</u>	<u>403 8</u>	<u>438 9</u>

The 2011 figures have been restated to incorporate the release of the deferred tax asset in one of the Company's subsidiaries, this is explained in full in note 11

**Cheltenham & Gloucester plc**

**STATEMENTS OF FINANCIAL POSITION (continued)**  
**AT 31 DECEMBER 2012**

The accompanying notes on pages 12 to 34 are an integral part of the financial statements

The Directors approved the financial statements on 17 April 2013



**RA Purdy**  
Director

**STATEMENTS OF CHANGES IN EQUITY  
FOR THE YEAR ENDED 31 DECEMBER 2012**

	Note	Called up share capital £m	Retained earnings £m	Total £m
<b>Group</b>				
Balance sheet at 1 January 2012		70 0	119 5	189 5
Profit for the year		-	46 7	46 7
Dividends	19	-	(50 0)	(50 0)
Balance at 31 December 2012		<u>70 0</u>	<u>116 2</u>	<u>186 2</u>
<b>Company</b>				
Balance sheet at 1 January 2012		70 0	116 1	186 1
Profit for the year	5	-	45 0	45 0
Dividends	19	-	(50 0)	(50 0)
Balance at 31 December 2012		<u>70 0</u>	<u>111 1</u>	<u>181 1</u>
<b>Group - Restated</b>				
Balance sheet at 1 January 2011		70 0	97 2	167 2
Profit for the year		-	72 3	72 3
Dividends	19	-	(50 0)	(50 0)
Balance at 31 December 2011		<u>70 0</u>	<u>119 5</u>	<u>189 5</u>
<b>Company</b>				
Balance sheet at 1 January 2011		70 0	94 3	164 3
Profit for the year	5	-	71 8	71 8
Dividends	19	-	(50 0)	(50 0)
Balance at 31 December 2011		<u>70 0</u>	<u>116 1</u>	<u>186 1</u>

The 2011 figures have been restated to incorporate the release of the deferred tax asset in one of the Company's subsidiaries, this is explained in full in note 11

The accompanying notes on pages 12 to 34 are an integral part of the financial statements

**CASH FLOW STATEMENTS**  
**FOR THE YEAR ENDED 31 DECEMBER 2012**

	Note	Group 2012 £m	Group 2011 £m	Company 2012 £m	Company 2011 £m
<b>Profit before tax</b>		59.2	102.0	57.5	101.8
Adjusted for					
Depreciation & impairment of Property Plant and Equipment	8	2.2	3.2	2.2	2.7
Loss / (profit) on disposal of fixed assets		(0.4)	0.9	-	0.9
Impairment of subsidiary	12	-	-	1.3	-
Income tax (paid) / received		-	(18.1)	-	(17.7)
		<u>61.0</u>	<u>88.0</u>	<u>61.0</u>	<u>87.7</u>
<b>Changes in operating assets and liabilities</b>					
Increase in debtors		(67.8)	(0.8)	(64.0)	(0.5)
Increase / (decrease) in creditors		(41.0)	6.5	(35.8)	6.5
Decrease in provisions	15	-	(1.6)	-	(1.6)
Reduction in retirement obligations	16	(6.0)	(16.4)	(6.0)	(16.4)
<b>Net cash used in operating activities</b>		<u>(53.8)</u>	<u>75.7</u>	<u>(44.8)</u>	<u>75.7</u>
<b>Cash flows from investing activities</b>					
Purchase of fixed assets		-	(2.1)	-	(2.1)
Proceeds from sale of fixed assets		11.7	2.7	2.7	2.7
<b>Net cash provided by investing activities</b>		<u>11.7</u>	<u>0.6</u>	<u>2.7</u>	<u>0.6</u>
<b>Cash flows from financing activities</b>					
Dividends paid		(50.0)	(50.0)	(50.0)	(50.0)
<b>Net cash used in financing activities</b>		<u>(50.0)</u>	<u>(50.0)</u>	<u>(50.0)</u>	<u>(50.0)</u>
Change in cash and cash equivalents		(92.1)	26.3	(92.1)	26.3
Cash and cash equivalents at beginning of year		195.6	169.3	195.6	169.3
<b>Cash and cash equivalents at end of year</b>	6	<u>103.5</u>	<u>195.6</u>	<u>103.5</u>	<u>195.6</u>

The accompanying notes on pages 12 to 34 are an integral part of the financial statements

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**1. ACCOUNTING POLICIES**

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and the Companies Act 2006, applicable to companies reporting under IFRS. The Group is incorporated and domiciled in England and Wales.

The Group has adopted the following new standards and amendments to standards which became effective for financial years beginning on or after 1 January 2012. Neither of these standards or amendments to standards has had a material impact on these financial statements.

- (i) *Disclosures – Transfers of Financial Assets (Amendments to IFRS 7)* Requires disclosures in respect of all transferred financial assets that are not derecognised in their entirety and transferred assets that are derecognised in their entirety but with which there is continuing involvement.
- (ii) *Deferred Tax – Recovery of Underlying Assets (Amendment to IAS 12)* Introduces a rebuttable presumption that investment property measured at fair value is recovered entirely through sale and that deferred tax in respect of such investment property is recognised on that basis. The Group's existing practices are consistent with this Amendment.

Details of those IFRS pronouncements which will be relevant to the Group but which were not effective at 31 December 2012 and which have not been applied in preparing these financial statements are given in note 25.

The financial information has been prepared under the historical cost convention as modified by the revaluation of land and buildings.

The financial statements have been prepared on a going concern basis.

The Group's accounting policies are set out below.

**Consolidation**

The assets, liabilities and results of Group undertakings (subsidiaries) are included in the financial statements on the basis of financial statements made up to the reporting date.

**Subsidiaries**

Subsidiaries include entities over which the Group has the power to govern the financial and operating policies which generally accompanies a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group; they are de-consolidated from the date that control ceases. Details of the principal subsidiaries are given in note 12.

Intercompany transactions, balances and unrealised gains and losses on transactions between Group companies are eliminated on consolidation.

**Revenue recognition**

Fees and commissions are generally recognised when the service has been provided, the income arises from the administration of mortgage and savings on behalf of Lloyds TSB Bank plc.

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

The effective interest rate is calculated on initial recognition of the financial asset or liability, estimating the future cash flows after considering all the contractual terms of the instrument but not future credit losses. The calculation includes amounts expected to be paid or received by the Company including expected early redemption fees and related penalties and premiums and discounts that are an integral part of the overall return. Direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument are also taken into account in the calculation.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**1 ACCOUNTING POLICIES (continued)**

**Loans and receivables**

Loans and receivables include loans and advances to banks and customers and eligible loans and receivables are initially recognised when cash is advanced to the borrowers at fair value inclusive of transaction costs or, for eligible assets transferred into this category, their fair value at the date of transfer. Loans and receivables are initially recognised at fair value and subsequently held at amortised cost.

**Borrowings**

Borrowings are recognised initially at fair value, being their issue proceeds net of transaction costs incurred. These instruments are subsequently stated at amortised cost using the effective interest method.

Preference shares and other instruments which carry a mandatory coupon or are redeemable on a specific date are classified as financial liabilities. The coupon on these instruments is recognised in the income statement as interest expense.

**Tangible fixed assets**

Tangible fixed assets are included at cost less accumulated depreciation. The value of land (included in premises) is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate the difference between the cost and the residual value over their estimated useful lives, as follows:

Premises (excluding land)

- Freehold / long and short leasehold premises: shorter of 50 years or the remaining period of the lease
- Leasehold improvements: shorter of 10 years or, if lease renewal is not likely, the remaining period of the lease

Equipment

- Fixtures and furnishings: 10-20 years
- Other equipment: 3-8 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. In the event that an asset's carrying amount is determined to be greater than its recoverable amount, it is written down immediately. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

**Leases**

The leases entered into by the Group are primarily operating leases. Operating lease rentals payable are charged to the income statement on a straight-line basis over the period of the lease.

When an operating lease is terminated before the end of the lease period, any payment made to the lessor by way of penalty is recognised as an expense in the period of termination.

**Pensions and other post-retirement benefits**

The Company's immediate parent company operates a number of post-retirement benefit schemes for its employees, including the employees of the Company, including both defined benefit and defined contribution pension plans. A defined benefit scheme is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, dependent on one or more factors such as age, years of service and salary. A defined contribution plan is a pension plan into which the Group pays fixed contributions; there is no legal or constructive obligation to pay further contributions.

Full actuarial valuations of the principal defined benefit schemes are carried out every three years with interim reviews in the intervening years; these valuations are updated to 31 December each year by qualified independent actuaries. For the purposes of these annual updates, scheme assets are included at their fair value and scheme liabilities are measured on an actuarial basis using the projected unit credit method adjusted for unrecognised actuarial gains and losses. The defined benefit scheme liabilities are discounted using rates equivalent to the market yields at the balance sheet date on high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension liability.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**1.ACCOUNTING POLICIES (continued)**

**Pensions and other post-retirement benefits (continued)**

The Group's income statement charge includes the current service cost of providing pension benefits, the expected return on the schemes' assets, net of expected administration costs, and the interest cost on the schemes' liabilities. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are not recognised unless the cumulative unrecognised gain or loss at the end of the previous reporting period exceeds the greater of 10 per cent of the scheme assets or liabilities ('the corridor approach'). In these circumstances the excess is charged or credited to the income statement over the employees' expected average remaining working lives. Past service costs are charged immediately to the income statement, unless the charges are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortised on a straight-line basis over the vesting period.

The Group's balance sheet includes the net surplus or deficit, being the difference between the fair value of scheme assets and the discounted value of scheme liabilities at the balance sheet date adjusted for any cumulative unrecognised actuarial gains or losses. A surplus is only recognised to the extent that they are recoverable through reduced contributions in the future or through refunds from the schemes.

The Group recognises the effect of material changes to the terms of its defined benefit pension plans which reduce future benefits as curtailments, gains and losses are recognised in the income statement when the curtailments occur.

The costs of the Group's defined contribution plans are charged to the income statement in the period in which they fall due.

**Share-based compensation**

The Company's ultimate parent company operates a number of equity-settled, share-based compensation plans in respect of services received from certain of its employees including those employed by the Company. The value of the employee services received in exchange for equity instruments granted under these plans is recognised as an expense over the vesting period of the instruments, with a corresponding increase in equity. This expense is determined by reference to the fair value of the number of equity instruments that are expected to vest. The fair value of equity instruments granted is based on market prices, if available, at the date of grant. In the absence of market prices, the fair value of the instruments at the date of grant is estimated using an appropriate valuation technique, such as a Black-Scholes option pricing model. The determination of fair values excludes the impact of any non-market vesting conditions, which are included in the assumptions used to estimate the number of options that are expected to vest. At each balance sheet date, this estimate is reassessed and if necessary revised. Any revision of the original estimate is recognised in the income statement over the remaining vesting period, together with a corresponding adjustment to equity. Cancellations by employees of contributions to the Group's Save As You Earn plans are treated as non-vesting conditions and in accordance with the revised IFRS 2 the Group recognises, in the year of cancellation, the amount of the expense that would have otherwise been recognised over the remainder of the vesting period. Modifications are assessed at the date of modification and any incremental charges are charged to the income statement over any remaining vesting period.

**Taxation**

Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax is determined using tax rates that have been enacted or substantively enacted by the balance sheet date which are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**1 ACCOUNTING POLICIES (continued)**

**Taxation (continued)**

Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax is provided on temporary differences arising from investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future. Income tax payable on profits is recognised as an expense in the period in which those profits arise. The tax effects of losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

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

**Provisions**

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

The Group recognises provisions in respect of vacant leasehold property where the unavoidable costs of the present obligations exceed anticipated rental income.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are not recognised in the financial statements but are disclosed unless they are remote.

**Dividends**

Dividends paid on the Group's ordinary shares are recognised as a reduction in equity in the period in which they are paid.

**Cash and cash equivalents**

For the purposes of the cash flow statement, cash and cash equivalents comprise cash and non-mandatory balances with central banks and amounts due from banks with a maturity of less than three months.

**Critical accounting estimates and judgements**

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, actual results reported in future periods may be based upon amounts which differ from those estimates. Estimates, judgements and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

The Group makes judgements and estimates in the preparation of the results and financial position however none of these are deemed to be critical.



**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**2 OPERATING EXPENSES**

	<b>Note</b>	<b>2012 £m</b>	<b>2011 £m</b>
Wages and salaries		55.7	62.2
Share-based payments		1.2	1.6
Social security costs		4.1	4.7
Other pension costs	16		
Defined benefit scheme		6.1	1.9
Defined contribution scheme		2.3	2.2
Staff costs		<u>69.4</u>	<u>72.6</u>
Other administrative expenses		<u>214.1</u>	<u>261.0</u>
		<u>283.5</u>	<u>333.6</u>

The average number of persons employed by the Group and the Company during the year was as follows

	<b>Group 2012</b>	<b>Group 2011 Restated</b>	<b>Company 2012</b>	<b>Company 2011 Restated</b>
UK	<u>2,178</u>	<u>2,296</u>	<u>2,178</u>	<u>2,296</u>
	<u>2,178</u>	<u>2,296</u>	<u>2,178</u>	<u>2,296</u>

The comparative has been restated to reflect the requirements of the Companies Act 2006. The data for employee numbers is now based on headcount of employees, rather than Full Time Equivalents as disclosed in the 2011 statutory financial statements.

No compensation has been paid or is payable to key management personnel in the year (2011: £nil).

**Auditors' remuneration**

	<b>2012 £'000</b>	<b>2011 £'000</b>
Fees payable to the Company's Auditor for the audit of the Company's annual financial statements	21	20
Fees payable to the Company's Auditor and its associates for other services		
- The audit of the Company's subsidiaries, pursuant to legislation	2	2

It is the Group's policy to use the auditors on assignments in cases where their knowledge of the Group means that it is neither efficient nor cost effective to employ another firm of accountants. Such assignments typically relate to the provision of advice on tax issues, assistance in transactions involving the acquisition and disposal of businesses, and accounting advice.

The Group has procedures to ensure that fees for audit and non-audit services are approved in advance of the service being provided.

**3 PROFIT BEFORE TAX**

Profit before tax is stated after taking account of

	<b>2012 £m</b>	<b>2011 £m</b>
(Profit) / loss on disposal of premises & equipment	(0.4)	0.9
Depreciation	2.2	2.8
Impairment loss	-	0.4
Operating lease rental charges paid	11.2	11.8

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**4 TAXATION**

**(a) Analysis of charge in year:**

	<b>Note</b>	<b>2012 £m</b>	<b>2011 £m Restated</b>
<b>UK corporation tax</b>			
Current tax on profits for the year		13.2	24.2
Prior year adjustment		(1.5)	-
Corporation tax charge		<u>11.7</u>	<u>24.2</u>
<b>Deferred tax</b>	<b>11</b>		
Current year		0.2	3.7
Prior year		0.6	1.8
<b>Total tax charge</b>		<u>12.5</u>	<u>29.7</u>

**(b) Factors affecting tax charge for the year**

A reconciliation of the total tax charge for the year to the charge that would result from applying the standard UK corporation tax rate to profit before tax is given below

	<b>2012 £m</b>	<b>2011 £m Restated</b>
Tax charge at UK corporation tax rate of 24.5% (2011 26.5%)	14.5	27.1
Non-allowable items	(1.7)	0.8
Effect of reduction in corporation tax rate to 23%	0.7	0.8
Deferred tax release	-	(0.8)
Adjustment to tax charge in respect of prior years	(0.9)	1.8
Gains exempted / covered by capital losses	(0.1)	-
<b>Total tax charge</b>	<u>12.5</u>	<u>29.7</u>

On 21 March 2012, the Government announced a reduction in the rate of corporation tax to 24% with effect from 1 April 2012. This reduction was enacted under the Provisional Collection of Taxes Act 1968 on 26 March 2012. Accordingly, the Group's profits for this accounting period are taxed at an effective rate of 24.5%. In addition, the Finance Act 2012, which passed into law on 3 July 2012, included legislation to reduce the main rate of corporation tax from 24% to 23% with effect from 1 April 2013.

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

The comparatives have been restated to account for an adjustment to deferred tax which is detailed within note 11.

**5. PROFIT FOR THE FINANCIAL YEAR ATTRIBUTABLE TO SHAREHOLDERS**

The profit attributable to shareholders includes a profit of £45.0 million (2011 £71.8 million) dealt with in the financial statements of the parent company, for which no income statement is presented as permitted of section 408 of the Companies Act 2006.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**6 LOANS AND ADVANCES TO BANKS**

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
Loans and advances to banks	<u>103.5</u>	<u>195.6</u>	<u>103.5</u>	<u>195.6</u>
Included above				
Due from Lloyds Banking Group subsidiary Undertakings				
All unsubordinated	<u>103.5</u>	<u>195.6</u>	<u>103.5</u>	<u>195.6</u>

At 31 December 2012, £nil (2011: £nil) of loans and advances to banks of the Group and Company had a contractual residual maturity of greater than one year.

**7. DUE FROM GROUP COMPANIES**

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
Due from Lloyds Banking Group subsidiary undertakings				
All unsubordinated	<u>265.1</u>	<u>197.1</u>	<u>265.1</u>	<u>201.0</u>

At 31 December 2012, £nil (2011: £nil) of intercompany debtors had a contractual residual maturity of greater than one year.

**8 TANGIBLE FIXED ASSETS**

	<b>Group Premises £m</b>	<b>Group Equipment £m</b>	<b>Group Total £m</b>	<b>Company Premises £m</b>	<b>Company Equipment £m</b>	<b>Company Total £m</b>
<b>Cost</b>						
At 1 January 2011	59.3	46.1	105.4	47.4	46.1	93.5
Additions	2.1	-	2.1	2.1	-	2.1
Disposals	(2.1)	(38.7)	(40.8)	(2.1)	(38.7)	(40.8)
At 31 December 2011	<u>59.3</u>	<u>7.4</u>	<u>66.7</u>	<u>47.4</u>	<u>7.4</u>	<u>54.8</u>
Disposals	(16.6)	(1.6)	(18.2)	(5.0)	(1.6)	(6.6)
At 31 December 2012	<u>42.7</u>	<u>5.8</u>	<u>48.5</u>	<u>42.4</u>	<u>5.8</u>	<u>48.2</u>
<b>Accumulated depreciation</b>						
At 1 January 2011	21.8	41.6	63.4	19.1	41.5	60.6
Charge for the year	2.3	0.9	3.2	1.8	0.9	2.7
Disposals	(0.5)	(36.7)	(37.2)	(0.5)	(36.7)	(37.2)
At 31 December 2011	<u>23.6</u>	<u>5.8</u>	<u>29.4</u>	<u>20.4</u>	<u>5.7</u>	<u>26.1</u>
Charge for the year	1.6	0.6	2.2	1.6	0.6	2.2
Disposals	(5.4)	(1.5)	(6.9)	(2.5)	(1.4)	(3.9)
At 31 December 2012	<u>19.8</u>	<u>4.9</u>	<u>24.7</u>	<u>19.5</u>	<u>4.9</u>	<u>24.4</u>
<b>Net book value</b>						
31 December 2012	<u>22.9</u>	<u>0.9</u>	<u>23.8</u>	<u>22.9</u>	<u>0.9</u>	<u>23.8</u>
31 December 2011	<u>35.7</u>	<u>1.6</u>	<u>37.3</u>	<u>27.0</u>	<u>1.7</u>	<u>28.7</u>

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**8 TANGIBLE FIXED ASSETS (continued)**

	<b>Group 2012</b>	<b>Group 2011 Restated</b>	<b>Company 2012</b>	<b>Company 2011 Restated</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Net book value of premises comprises				
Freeholds	15.3	25.7	15.3	17.0
Leaseholds 50 years and over unexpired	5.8	6.4	5.8	6.4
Leaseholds less than 50 years unexpired	0.5	0.9	0.5	0.9
Adaptation costs	1.3	2.7	1.3	2.7
	<u>22.9</u>	<u>35.7</u>	<u>22.9</u>	<u>27.0</u>

A valuation of the land and buildings at 31 December 2012 was undertaken by Jones Lang LaSalle, independent valuers not connected with the Group, on the basis of market valuation. The valuation conforms to International Valuation Standards and was based on recent market transactions on arm's length terms for similar properties. The market valuation of the land and buildings was not deemed to be materially different to current net book value and so no revaluation is noted for these financial statements.

The comparatives have been restated to reflect an accurate NBV split for premises, with consistent treatment to that of the 2012 year end.

**9 OPERATING LEASE COMMITMENTS**

At the balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	<b>Group 2012</b>	<b>Group 2011</b>	<b>Company 2012</b>	<b>Company 2011</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
Not later than 1 year	10.1	11.9	10.1	12.7
Later than 1 year and not later than 5 years	34.8	42.1	34.8	45.4
Later than 5 years	26.0	39.2	26.0	60.4
	<u>70.9</u>	<u>93.2</u>	<u>70.9</u>	<u>118.5</u>

**10. CAPITAL COMMITMENTS**

Capital expenditure contracted, but not provided for, at 31 December 2012 amounted to nil for the Group and the Company (2011: Group and Company nil).

**11 DEFERRED TAX ASSET**

	<b>Group 2012</b>	<b>Group 2011</b>	<b>Company 2012</b>	<b>Company 2011</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
		<b>Restated</b>		
At 1 January	8.8	14.3	8.8	14.7
Income statement debit	(0.8)	(5.5)	(0.8)	(5.9)
At 31 December	<u>8.0</u>	<u>8.8</u>	<u>8.0</u>	<u>8.8</u>

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**11. DEFERRED TAX ASSET (continued)**

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

	<b>Group 2012 £m</b>	<b>Group 2011 £m Restated</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
Accelerated depreciation allowances	0.4	0.3	0.4	0.3
Retirement benefit obligations	(2.4)	(5.5)	(2.4)	(5.5)
Other provisions	(0.8)	-	(0.8)	-
Other temporary differences	2.0	(0.3)	2.0	(0.7)
<b>Total movement in deferred tax</b>	<b>(0.8)</b>	<b>(5.5)</b>	<b>(0.8)</b>	<b>(5.9)</b>

The net deferred tax asset is comprised as follows

	<b>Group 2012 £m</b>	<b>Group 2011 £m Restated</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
Deferred tax assets				
Retirement benefit obligations	10.4	12.8	10.4	12.8
Deferred tax liabilities				
Accelerated capital allowances	(0.4)	(1.2)	(0.4)	(1.2)
Other temporary differences	(2.0)	(2.8)	(2.0)	(2.8)
	<b>(2.4)</b>	<b>(4.0)</b>	<b>(2.4)</b>	<b>(4.0)</b>
	<b>8.0</b>	<b>8.8</b>	<b>8.0</b>	<b>8.8</b>

The comparatives have been restated to reflect an adjustment that had been applied to the 2011 financial statements of the subsidiary, C&G Property Holdings Limited, but which had not been applied to the 2011 Group financial statements

**12. SHARES IN SUBSIDIARIES**

	<b>Company 2012 £m</b>	<b>2011 £m</b>
Cost		
At 1 January	1.3	1.3
Impairment	(1.3)	-
At 31 December	<b>-</b>	<b>1.3</b>

The principal Group undertakings, all of which prepare financial statements to 31 December and whose results are included in the consolidated financial statements of Cheltenham & Gloucester plc, are

	<b>Country of registration / incorporation</b>	<b>Nature of business</b>	<b>Ownership</b>
C&G Property Holdings Limited	England and Wales	Property holding and leasing	100%
C&G Estate Agents Limited	England and Wales	Dormant	100%
C&G Financial Services Limited	England and Wales	Dormant	100%
C&G Homes Limited	England and Wales	Dormant	100%
Central Mortgage Finance Limited	England and Wales	Dormant	100%
Lloyds TSB Mortgages Limited	England and Wales	Dormant	100%

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**12 SHARES IN SUBSIDIARIES (continued)**

During the year to 31 December 2012 C&G Property Holdings Limited disposed of all its remaining interest in properties. The principal activity of this subsidiary has therefore ceased in the current year. There is an intention to subject this subsidiary to a Members Voluntary Liquidation within the next accounting period and hence the investment has been written down to £nil.

**13 OWED TO GROUP COMPANIES**

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
Due to Lloyds Banking Group subsidiary undertakings	<u>104.3</u>	<u>123.3</u>	<u>109.6</u>	<u>123.1</u>

At 31 December 2012, £nil (2011: £nil) of intercompany creditors had a contractual residual maturity of greater than one year.

**14. OTHER LIABILITIES**

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
Accruals and deferred income	27.1	32.8	27.1	32.8
Other liabilities	-	16.3	-	16.6
	<u>27.1</u>	<u>49.1</u>	<u>27.1</u>	<u>49.4</u>

**15 PROVISIONS**

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>	<b>Company 2012 £m</b>	<b>Company 2011 £m</b>
At 1 January	-	1.6	-	1.6
Additional provision in the year	-	-	-	-
Utilisation of provision	-	(1.6)	-	(1.6)
<b>At 31 December</b>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

Provisions are made for staff and other costs related to Group restructuring initiatives at the point at which the Group becomes irrevocably committed to the expenditure.

**16. RETIREMENT BENEFIT OBLIGATIONS**

**Defined contribution schemes**

The Company's ultimate parent company operates a number of defined contribution pension schemes, principally the defined contribution sections of the Lloyds TSB Group Pension Schemes No's 1 and 2, new employees are offered membership of the defined contribution section of the Lloyds TSB Group Pension Scheme No. 1.

**NOTES TO THE FINANCIAL STATEMENTS  
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**16 RETIREMENT BENEFIT OBLIGATIONS (continued)**

**Defined benefit schemes**

The Company's ultimate parent company has established a number of defined benefit pension schemes in the UK and overseas. The majority of the Company's employees are members of the defined benefit sections of the Lloyds TSB Group Pension Schemes No's 1 and 2. These are funded schemes providing retirement benefits calculated as a percentage of final salary depending upon the length of service, the minimum retirement age under the rules of the schemes is 50.

The latest full valuations of the two main schemes were carried out as at 30 June 2011, these have been updated to 31 December 2012 by qualified independent actuaries.

The amounts shown below relate to the Company's share of obligations arising from membership by the Company's employees of the defined benefit schemes operated by the Company's ultimate parent company.

Amount included in the balance sheet

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
Company's share of present value of funded obligations	1,151.3	1,085.2
Company's share of fair value of scheme assets	(998.4)	(968.8)
	<u>152.9</u>	<u>116.4</u>
Company's share of unrecognised actuarial losses	(107.6)	(65.1)
Liability in the balance sheet	<u>45.3</u>	<u>51.3</u>

The movements in the liability recognised in the balance sheet are as follows

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
At 1 January	51.3	67.7
Net charge to the income statement	6.1	1.9
Contributions paid	(12.1)	(18.3)
At 31 December	<u>45.3</u>	<u>51.3</u>

The expense recognised in the income statement comprises

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
Current service cost	5.3	4.5
Interest cost	29.3	25.5
Expected return on scheme assets	(29.2)	(28.1)
Past service cost	0.5	-
Curtailment	0.2	-
	<u>6.1</u>	<u>1.9</u>

**The following information relates to Lloyds TSB Group Pension Schemes No's 1 and 2 as at 31 December 2012**

In accordance with IAS 19, the remaining information below relates to the No's 1 and 2 schemes operated by the Company's ultimate parent company and amounts are shown in £ millions unless otherwise stated.

The Company's ultimate parent company expects to pay contributions of approximately £645 million in respect of the No's 1 and 2 schemes in 2013.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**16. RETIREMENT BENEFIT OBLIGATIONS (continued)**

Movements in the defined benefit obligation

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
At 1 January	17,332	16,627
Merger of No 1 and Asset Finance schemes	518	-
Current service cost	166	166
Interest cost	876	897
Actuarial gains	1,654	236
Benefits paid	(662)	(604)
Past service cost	16	10
Curtailment	4	-
Exchange and other adjustments	(1)	-
At 31 December	<u>19,903</u>	<u>17,332</u>

Changes in the fair value of scheme assets

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
At 1 January	17,254	16,290
Merger of No 1 and AMC schemes	424	-
Expected return	897	1,009
Employer contributions	273	413
Actuarial gains/(losses)	287	146
Benefits paid	(662)	(604)
At 31 December	<u>18,473</u>	<u>17,254</u>
Actual return on scheme assets	<u>1,184</u>	<u>1,155</u>

The principal actuarial and financial assumptions used in valuations of the pension schemes were as follows

	<b>2012</b>	<b>2011</b>
	<b>%</b>	<b>%</b>
Discount rate	4.60	5.00
Rate of inflation		
Retail Prices Index	2.90	3.00
Consumer Price Index	2.00	2.00
Rate of salary increases	2.00	2.00
Rate of increase for pensions in payment and deferred pensions	2.70	2.80
	<b>Years</b>	<b>Years</b>
Life expectancy for member aged 60, on the valuation date		
- Men	27.4	27.3
- Women	29.7	28.4
Life expectancy for member aged 60, 15 years after the valuation date		
- Men	28.5	28.8
- Women	30.9	30

The mortality assumptions used in the scheme valuations are based on standard tables published by the Institute and Faculty of Actuaries which were adjusted in line with both current industry experience and the actual experience of the relevant schemes

An analysis of the impact of a reasonable change in these assumptions is provided in the 2012 annual report and financial statements of the Company's ultimate parent company (note 23)



**NOTES TO THE FINANCIAL STATEMENTS  
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**16. RETIREMENT BENEFIT OBLIGATIONS (continued)**

The expected return on scheme assets for the No 1 and 2 pension schemes is based on the following assumptions

	<b>2012</b>	<b>2011</b>
	<b>%</b>	<b>%</b>
Equities	7.3	8.3
Fixed interest gilts	3.0	4.0
Index linked gilts	2.8	3.9
Non-government bonds	4.9	4.9
Property	6.6	7.3
Cash	2.6	3.9

The expected return on scheme assets in 2013 for the No 1 and 2 pension schemes will be calculated using the following assumptions

	<b>2013</b>
	<b>%</b>
Equities	6.8
Fixed interest gilts	2.3
Index linked gilts	2.8
Non-government bonds	3.1
Property	6.8
Cash	2.4

Composition of scheme assets

	<b>2012</b>	<b>2011</b>
	<b>£m</b>	<b>£m</b>
Equities	7,820	6,495
UK fixed interest gilts	287	391
UK index linked gilts	5,115	4,692
Sterling non-government bonds	2,965	2,882
Property	1,132	1,311
Derivative assets	429	642
Cash, and other assets and liabilities	725	841
At 31 December	<u>18,473</u>	<u>17,254</u>

The assets of all the funded plans are held independently of the Lloyds Banking Group's assets in separate trustee administered funds

The expected return on plan assets was determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields at the balance sheet date. Expected returns on equity and property investments reflect long-term real rates of return experienced in the respective markets.

**NOTES TO THE FINANCIAL STATEMENTS  
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**16. RETIREMENT BENEFIT OBLIGATIONS (continued)**

Experience adjustments history (since the date of adoption of IAS 19)

	2012 £m	2011 £m	2010 £m	2009 £m	2008 £m
Present value of defined benefit obligation	19,903	17,332	16,627	16,962	14,089
Fair value of scheme assets	(18,473)	(17,254)	(16,290)	(14,662)	(12,433)
	1,430	78	337	2,300	1,656
Unrecognised actuarial losses	(2,182)	(769)	(679)	(2,146)	(217)
(Asset)/Liability in the balance sheet	(752)	(691)	(342)	154	1,439
Experience losses on scheme liabilities	(371)	(132)	(396)	(3)	(29)
Experience gains/(losses) on scheme assets	287	146	1,052	(440)	(3,227)

The expense recognised in the ultimate parent company's income statement comprises

	2012 £m	2011 £m
Current service cost	166	166
Interest cost	876	897
Expected return on scheme assets	(897)	(1,009)
Past service cost	16	10
Total pension expense	161	64

**17. OTHER BORROWED FUNDS**

	2012 £m	2011 £m
Preference shares	5 0	5 0

	2012 Number (m) and £m	2011 Number (m) and £m
Authorised		
Preference shares of £1 each	10	10
'B' preference shares of £1 each	10	10
Issued and fully paid		
Preference shares of £1 each	3 8	3 8
'B' preference shares of £1 each	1 2	1 2

The terms of the preference shares require the Company to declare a non-cumulative dividend at the rate of LIBOR plus 75 basis points per cent per annum on the amount paid up on each preference share. This is paid annually on 30 June. Other borrowed funds are all classed as non-current.

**18. CALLED UP SHARE CAPITAL**

	2012 Number in millions	2011 Number in millions	2012 £m	2011 £m
Authorised ordinary shares of £1 each				
At 1 January and 31 December	311 7	311 7	311 7	311 7
Issued and fully paid ordinary shares of £1 each				
At 1 January and 31 December	70 0	70 0	70 0	70 0

The company has one class of ordinary voting shares which carry no right to fixed income.

**NOTES TO THE FINANCIAL STATEMENTS  
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**19 ORDINARY DIVIDENDS**

The dividends paid in the year were as follows

	2012 £m	2011 £m
Final dividend in respect of preceding year	50 0	50 0
At 31 December	<u>50 0</u>	<u>50 0</u>
Dividend per share	<u>71 4p</u>	<u>71 4p</u>

**20 SHARE BASED PAYMENTS**

**Share-based payments**

During the year ended 31 December 2012 the Company's ultimate parent company operated the following share-based payment schemes, all of which are equity settled

**Save-As-You-Earn schemes**

Eligible employees may enter into contracts through the Save- As- You- Earn schemes to save up to £250 per month and, at the expiry of a fixed term of three, five or seven years, have the option to use these savings within six months of the expiry of the fixed term to acquire shares in the Lloyds Banking Group plc at a discounted price of no less than 80 per cent of the market price at the start of the invitation

**Other share option plans**

***Lloyds Banking Group Executive Share Plan 2003***

The Plan was adopted in December 2003 and under the Plan share options may be granted to senior employees Options under this plan have been granted specifically to facilitate recruitment and as such were not subject to any performance conditions The Plan's usage has now been extended to not only compensate new recruits for any lost share awards but also to make grants to key individuals for retention purposes with, in some instances, the grant being made subject to individual performance conditions

***Lloyds Banking Group Share Buy Out Awards***

As part of arrangements to facilitate the recruitment of certain Executives, options have been granted by individual deed and, where appropriate, in accordance with the Listing Rules of the UK Listing Authority

The awards were granted in recognition that the Executives' outstanding awards over shares in their previous employing company lapsed on accepting employment with the Lloyds Banking Group

**Other share plans**

***Lloyds Banking Group Long-Term Incentive Plan***

The Long-Term Incentive Plan (LTIP) introduced in 2006 is aimed at delivering shareholder value by linking the receipt of shares to an improvement in the performance of Lloyds Banking Group plc over a three year period Awards are made within limits set by the rules of the Plan, with the limits determining the maximum number of shares that can be awarded equating to three times annual salary In exceptional circumstances this may increase to four times annual salary

The performance conditions for awards made in April, May and September 2009 were as follows

- (i) Earnings per share (EPS) relevant to 50 per cent of the award Performance was measured based on EPS growth over a three- year period from the baseline EPS of 2008
- (ii) Economic Profit (EP) relevant to 50 per cent of the award Performance was measured based on the extent to which cumulative EP targets were achieved over the three-year period

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**20. SHARE BASED PAYMENTS (continued)**

**Other share plans (continued)**

***Lloyds Banking Group Long-Term Incentive Plan (continued)***

An additional discretionary award was made in April, May and September 2009. The performance conditions for those awards were as follows:

(i) **Synergy Savings** The release of 50 per cent of the shares was dependent on the achievement of target run-rate synergy savings in 2009 and 2010 as well as the achievement of sustainable synergy savings of at least £1.5 billion by the end of 2011. The award was broken down into three equally weighted annual tranches. Performance was assessed at the end of each year against annual performance targets based on a trajectory to meet the 2011 target. The extent to which targets were achieved determined the proportion of shares to be banked each year. Any release of shares was subject to the Lloyds Banking Group plc Remuneration Committee judging the overall success of the delivery of the integration programme.

(ii) **Integration Balanced Scorecard** The release of the remaining 50 per cent of the shares was dependent on the outcome of a Balanced Scorecard of non-financial measures of the success of the integration in each of 2009, 2010 and 2011. The Balanced Scorecard element was broken down into three equally weighted tranches. The tranches were crystallised and banked for each year of the performance cycle subject to separate annual performance targets across the four measurement categories of Building the Business, Customer, Risk and People and Organisation Development.

The performance conditions for awards made in March and August 2010 were as follows:

(i) **EPS** relevant to 50 per cent of the award. Performance was measured based on EPS growth over a three-year period from the baseline EPS of 2009.

(ii) **Economic Profit** relevant to 50 per cent of the award. Performance was measured based on the compound annual growth rate of adjusted EP over the three financial years starting on 1 January 2010 relative to an adjusted 2009 Economic Profit base.

The performance conditions for awards made in March and September 2011 are as follows:

(i) **EPS** relevant to 50 per cent of the award. The performance target is based on 2013 adjusted EPS outcome.

(ii) **EP** relevant to 50 per cent of the award. The performance target is based on 2013 adjusted EP outcome.

The performance conditions for awards made in March and September 2012 are as follows:

(i) **EP** relevant to 30 per cent of the award. The performance target is based on 2014 adjusted EP outcome.

(ii) **Absolute Total Shareholder Return (ATSR)** relevant to 30 per cent of the award. Performance will be measured against the annualised return over the three year period ending 31 December 2014.

(iii) **Short-term funding as a % of total funding** relevant to 10 per cent of the award. Performance will be measured relative to 2014 targets.

(iv) **Non-core assets at the end of 2014** relevant to 10 per cent of the award. Performance will be measured by reference to balance sheet non-core assets at 31 December 2014.

(v) **Net simplification benefits** relevant to 10 per cent of the award. Performance will be measured by reference to the run rate achieved by the end of 2014.

(vi) **Customer satisfaction** relevant to 10 per cent of the award. Performance will be measured by reference to the total number of FSA reportable complaints per 1,000 customers over the three year period to 31 December 2014.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**20 SHARE BASED PAYMENTS (continued)**

**Share incentive plan**

***Free shares***

An award of shares may be made annually to employees based on a percentage of each employee's salary in the preceding year up to a maximum of £3,000. The percentage is normally announced concurrently with Lloyds Banking Group plc's annual results and the price of the shares awarded is announced at the time of award. The shares awarded are held in trust for a mandatory period of three years on the employee's behalf, during which period the employee is entitled to any dividends paid on such shares. The award is subject to a non-market based condition: if an employee leaves the Lloyds Banking Group plc within this three year period for other than a 'good' reason, all of the shares awarded will be forfeited.

The last award of free shares was made in 2008.

***Matching shares***

Lloyds Banking Group plc undertakes to match shares purchased by employees up to the value of £30 per month, these matching shares are held in trust for a mandatory period of three years on the employee's behalf, during which period the employee is entitled to any dividends paid on such shares. The award is subject to a non-market based condition: if an employee leaves within this three year period for other than a 'good' reason, 100 per cent of the matching shares are forfeited. Similarly if the employees sell their purchased shares within three years, their matching shares are forfeited.

**Other information**

The charge made to the income statement represents the Company's share of the cost of the above schemes. This charge has been allocated to the Company based on the number of the Company's employees who participate in the above schemes. It is not practicable for the Company to provide information regarding the ranges of exercise prices, weighted average exercise prices, weighted average remaining contractual life information and the number of options outstanding that is specific to the Company's employees without incurring significant additional cost.

Full details of the ranges of exercise prices, weighted average exercise prices, weighted average remaining contractual life information and number of options outstanding for the above schemes overall can be found in the 2012 annual report and financial statements of the Company's ultimate parent company. Copies of the ultimate parent company's 2012 annual report and financial statements may be obtained from the Company Secretary's Department, Lloyds Banking Group plc, 25 Gresham Street, London, EC2V 7HN.

**21. DIRECTORS' EMOLUMENTS**

The Directors are employed by other companies in the Lloyds Banking Group and consider that their services to the company are incidental to their other activities within the Group and therefore their emoluments have not been disclosed.

**22. RELATED PARTY TRANSACTIONS**

There are a number of transactions with Lloyds Banking Group plc and its subsidiary companies. Where applicable the transactions have been disclosed in the notes to the financial statements.

The following table details the impact of transactions with Lloyds Banking Group companies through the income statement.

	2012 £m	2011 £m
Interest income	2.3	-
Preference share interest expense	0.1	0.1
Commission receivable	336.6	423.5
Administrative expenses	191.1	215.2

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**22 RELATED PARTY TRANSACTIONS (continued)**

The Company leased a property from its subsidiary C&G Property Holdings Limited for which it paid rental charges of £0.3m during the year (2011: £0.8m). In addition, the Company received interest on a loan outstanding from the subsidiary which was £0.0m for the year (2011: £0.0m), this loan was repaid during the reporting period. The principal amount of the loan outstanding at 31 December 2012 was £nil (2011: £4.0m).

At 31 December 2012 the Company also owed C&G Property Holdings Limited an amount of £5.2m (2011: £nil). This amount relates to the settlement of intercompany transactions.

In addition, there are amounts due to the Company from its dormant subsidiary companies which have been written off in these consolidated financial statements as the amounts are not deemed to be recoverable, given the dormant nature of the entities. The amounts which have been included in the subsidiary company financial statements but have previously been written off by C&G are C&G Estate Agents Limited of £1.9m, C&G Homes Limited of £13.6m, and Central Mortgage Finance Limited of £4.3m.

In the current year an amount totalling £1.3m was written off in C&G plc company financial statements. This amount was the investment in C&G Property Holdings Limited and it is still included in the subsidiary company financial statements. Please see note 12 for further details.

The Group's related parties also include key management personnel. Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, which for the Group is the board of Directors of C&G.

A number of banking transactions were entered into with key management in the normal course of business. These included loans and deposits. The Directors of C&G who hold C&G products ceased to have a related party relationship in relation to these mortgages and savings balances on transfer of the balances to the Bank in 2007.

**23. FINANCIAL RISK MANAGEMENT POLICIES**

The Directors are responsible for establishing a framework for evaluating, measuring, monitoring and controlling risk. They are responsible for ensuring that the risks within the business are identified, assessed, monitored and controlled. These controls and procedures where relevant comply with Lloyds Banking Group policies and standards.

**Interest Rate Risk**

The Company has no interest-bearing assets from third parties and no deposits are placed outside of the Lloyds Banking Group. Assets due from Lloyds Banking Group Companies are subject to variable interest rates. Interest was received on a loan from a subsidiary company at the Bank of England base rate, this loan was settled within the current year. As such, this represents exposure to fluctuations in interest rates. If interest rates for the year ended 31 December 2012 had been 150 basis points higher with all other variables held constant, post-tax profits for the year would have been £29.2k (2011: £52.5k) higher, as a result of increased interest income on the Company's loan from the subsidiary company.

**Currency Risk**

The Company holds no foreign currency assets or liabilities and transacts all business in GBP and therefore has no significant exposure to currency risks.

**Credit Risk**

All material financial assets of the Company are amounts due from Group Companies, none of which are past due but not impaired or impaired. As such, the Directors are of the opinion that the carrying value of these assets are the best representation of the maximum exposure to credit risk.

## NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2012

### 23. FINANCIAL RISK MANAGEMENT POLICIES (continued)

#### Liquidity risk

The Group is deemed to have low exposure to the risk of being unable to meet its financial obligations as they fall due or only being able to do so at an unacceptably high cost. This is because the Group is funded by companies within Lloyds Banking Group plc and, as a result, liquidity risk is managed within the Lloyds Banking Group.

The table below analyses liabilities of the Group on an undiscounted future cash flows basis according to contractual maturity into relevant maturity groupings based on the remaining period at the balance sheet date. Balances with no fixed maturity are included in the over 5 years category.

As at 31 December 2012	Up to 1 month £m	1-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
<b>Liabilities</b>						
Current tax	-	-	35.9	-	-	35.9
Owed to Group Companies	104.3	-	-	-	-	104.3
Other liabilities	27.1	-	-	5.0	45.3	77.4
<b>Total</b>	<b>131.4</b>	<b>-</b>	<b>35.9</b>	<b>5.0</b>	<b>45.3</b>	<b>217.6</b>

As at 31 December 2011	Up to 1 month £m	1-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
<b>Liabilities</b>						
Current tax	-	-	24.2	-	-	24.2
Owed to Group Companies	123.3	-	-	-	-	123.3
Other liabilities	49.1	-	-	5.0	51.3	105.4
<b>Total</b>	<b>172.4</b>	<b>-</b>	<b>24.2</b>	<b>5.0</b>	<b>51.3</b>	<b>252.9</b>

#### Fair value of financial instruments

Financial instruments include financial assets and financial liabilities. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

There are no significant differences between the carrying amounts and the fair value of financial instruments included in these financial statements, as the majority of financial instruments are held at variable rates.

#### Capital

The managed capital of the Company constitutes total shareholder's funds. These consist entirely of issued ordinary share capital and retained profit and loss.

The Company is authorised and regulated by the Financial Services Authority ('FSA') and is subject to the FSA's capital resource requirements per the FSA IPRU(Inv) and MIPRU Rulebooks. Capital is actively managed at an appropriate level of frequency and regulatory capital levels are a key factor in the Group's budgeting and planning processes. All FSA capital requirements imposed on the Company during the year were met.

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

**24. DISCONTINUED OPERATIONS**

Analysis of the result of discontinued operations is as follows

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>
Pre-tax gain recognised on disposal of assets	0.4	-
Tax	-	-
<b>Profit for the year from discontinued operations</b>	<b>0.4</b>	<b>-</b>

The cash flows relating to discontinued operations are as follows

	<b>Group 2012 £m</b>	<b>Group 2011 £m</b>
Operating cash flows	0.4	-
Investing cash flows	8.8	-
Financing cash flows	(9.2)	-
<b>Total cash flows</b>	<b>-</b>	<b>-</b>

**25. FUTURE ACCOUNTING DEVELOPMENTS**

The following pronouncements may have a significant effect on the Group's financial statements but are not applicable for the year ending 31 December 2012 and have not been applied in preparing these financial statements. The full impact of these accounting changes is being assessed by the Group.

Pronouncement	Nature of change	IASB effective date
IFRS 9 Financial Instruments <sup>1</sup>	Replaces those parts of IAS 39 <i>Financial Instruments Recognition and Measurement</i> relating to the classification, measurement and derecognition of financial assets and liabilities. Requires financial assets to be classified into two measurement categories, fair value and amortised cost, on the basis of the objectives of the entity's business model for managing its financial assets and the contractual cash flow characteristics of the instrument. The available-for-sale financial asset and held-to-maturity investment categories in existing IAS 39 will be eliminated. The requirements for financial liabilities and derecognition are broadly unchanged from IAS 39.	Annual periods beginning on or after 1 January 2015
IFRS 10 Consolidated Financial Statements	Supersedes IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation – Special Purpose Entities and establishes principles for the preparation of consolidated financial statements when an entity controls one or more entities.	Annual periods beginning on or after 1 January 2013



# NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2012

## 25. FUTURE ACCOUNTING DEVELOPMENTS (continued)

Pronouncement	Nature of change	IASB effective date
IFRS 10 Consolidated Financial Statements	Supersedes IAS 27 <i>Consolidated and Separate Financial Statements</i> and SIC-12 <i>Consolidation – Special Purpose Entities</i> and establishes principles for the preparation of consolidated financial statements when an entity controls one or more entities	Annual periods beginning on or after 1 January 2013
IAS 1 Presentation of Financial Statements – ‘Presentation of Items of Other Comprehensive Income’	Requires entities to group items presented in other comprehensive income on the basis of whether they are potentially reclassified to profit or loss subsequently	Annual periods beginning on or after 1 July 2012
IFRS 7 Financial Instruments Disclosures – ‘Disclosures–Offsetting Financial Assets and Financial Liabilities’	Requires an entity to disclose information to enable users of its financial statements to evaluate the effect or potential effect of netting arrangements on the entity's balance sheet	Annual and interim periods beginning on or after 1 January 2013
IAS 32 Financial Instruments Presentation – ‘Offsetting Financial Assets and Financial Liabilities’	Inserts application guidance to address inconsistencies identified in applying the offsetting criteria used in the standard. Some gross settlement systems may qualify for offsetting where they exhibit certain characteristics akin to net settlement	Annual periods beginning on or after 1 January 2014
IFRS 12 Disclosure of Interests in Other Entities	Requires an entity to disclose information that enables users of financial statements to evaluate the nature of, and risks associated with, its interests in other entities and the effects of those interests on its financial position, financial performance and cash flows	Annual periods beginning on or after 1 January 2013
IFRS 13 Fair Value Measurement	The standard defines fair value, sets out a framework for measuring fair value and requires disclosures about fair value measurements. It applies to IFRSs that require or permit fair value measurements or disclosures about fair value measurements	Annual periods beginning on or after 1 January 2013
IAS 19 Employee Benefits	Prescribes the accounting and disclosure by employers for employee benefits. Actuarial gains and losses (remeasurements) in respect of defined benefit pension schemes are no longer deferred using the corridor approach and are recognised immediately in other comprehensive income	Annual periods beginning on or after 1 January 2013

<sup>1</sup> IFRS 9 is the initial stage of the project to replace IAS 39. Future stages are expected to result in amendments to IFRS 9 to deal with changes to the impairment of financial assets measured at amortised cost and hedge accounting. Until all stages of the replacement project are complete, it is not possible to determine the overall impact on the financial statements of the replacement of IAS 39.

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

None of the future accounting developments detailed within this note are considered to have a material impact on these financial statements.

## 26. GUARANTEES

Under the Building Societies Act 1986, Cheltenham & Gloucester Building Society had an obligation to discharge the liabilities of its subsidiary companies in so far as they were unable to discharge the liabilities out of their own assets. Under the Building Societies (Transfer of Business) Regulations 1988, any obligations which existed at 31 July 1995 remain as obligations of Cheltenham & Gloucester plc.

**NOTES TO THE FINANCIAL STATEMENTS  
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**27 PARENT COMPANIES**

The Company's immediate parent company is Lloyds TSB Bank plc. The company regarded by the Directors as the ultimate parent company is Lloyds Banking Group plc, a limited liability company incorporated and domiciled in Scotland, which is also the parent undertaking of the largest group of undertakings for which group financial statements are drawn up and of which the Company is a member. The Bank is the parent undertaking of the smallest such group of undertakings. Copies of the group financial statements of both companies may be obtained from Group Secretariat, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN.

Cheltenham & Gloucester plc

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2012**

Cheltenham & Gloucester plc  
Chief Office and Registered Office  
Barnett Way  
Gloucester  
GL4 3RL

Registered in England No 2299428