

Granite Mortgages 04-3 plc  
Annual report and accounts  
for the year ended 31 December 2011

Registered Number 05168395

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# **Granite Mortgages 04-3 plc**

## **Annual report and accounts for the year ended 31 December 2011**

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# **Granite Mortgages 04-3 plc**

## **Directors' report for the year ended 31 December 2011**

The Directors present their report and the audited financial statements of Granite Mortgages 04-3 plc (the 'Company') for the year ended 31 December 2011

### **Principal activities**

The principal activity of the Company is to issue publicly listed floating rate notes in the international capital markets which are denominated in US Dollars, Euros and Sterling (the 'loan notes') and to enter into certain related financial arrangements in order to fund the activities of the Granite Finance Holdings Limited group (of which the Company is a member) by means of an inter-company loan to Granite Finance Funding Limited, a fellow member of that group

The activities of the Company and of the Granite Finance Holdings Limited group are managed in accordance with the securitisation transaction documents. The securitisation structure was established primarily as a means of raising finance for Northern Rock plc during 2004

The Company was registered as Granite Mortgages 04-3 plc in England and Wales on 1 July 2004 as a public limited company, with an authorised share capital of £50,000 comprising 50,000 ordinary shares of £1 each, of which £12,500 is paid up. The Company is domiciled in the United Kingdom

### **Controlling party**

Following the completion of a legal and capital restructuring on 1 January 2010, Northern Rock plc became Northern Rock Asset Management plc ('NRAM plc'). NRAM plc no longer operates as a deposit taking institution under the supervision of the Financial Services Authority ('FSA'), but continues to work as Administrator and Cash Manager to the Company. NRAM plc is now authorised and regulated by the FSA as a mortgage administration company and NRAM plc's Directors believe that it has appropriate and adequate levels of capital to support these activities

All shares in NRAM plc were transferred to the Treasury Solicitor as nominee for HM Treasury on 22 February 2008 as a result of 'The Northern Rock Transfer Order 2008'. On 1 October 2010 all shares in NRAM plc were acquired via a share-for-share exchange by UK Asset Resolution Limited ('UKAR Limited'), a private limited company incorporated in the United Kingdom under the Companies Act 2006 and registered in England and Wales, which is wholly owned by the Treasury Solicitor as nominee for HM Treasury. As such, the Company considers that Her Majesty's Government remains its ultimate controlling party (see note 18)

UKAR Limited is the holding company established to bring together the Government-owned businesses of Bradford & Bingley plc and NRAM plc

UKAR Limited is not authorised or regulated by the FSA. UKAR Limited does not deal with customers directly, who continue to be serviced through the subsidiary businesses of Bradford & Bingley plc and NRAM plc. UK Financial Investments Limited (UKFI Limited) manages HM Treasury's 100% shareholding in UKAR Limited

### **Review of the business**

During the year, Granite Finance Funding Limited made repayments totalling £184.2m (2010: £195.1m) to the Company in respect of the inter-company loan. These repayments were used to repay part of the loan notes back to note holders. The Company made all interest payments due in the year in line with the transaction

## **Granite Mortgages 04-3 plc**

documents. All payments made in 2011 were in accordance with the pass-through provisions that continue to apply following the breach of the non-asset trigger in November 2008.

On 20 January 2009, another NRAM plc group undertaking, Granite Mortgages 03-3 plc failed to exercise a call notice on the relevant step-up and call date of its loan notes in issue. As a consequence of this there is a requirement to increase Granite Mortgages 04-3 plc's issuer reserve fund (held by Granite Finance Funding Limited) by £10.8m. As at the year end, this increase was fully funded. There is also a requirement to increase the reserve fund of Granite Finance Funding Limited by £22.1m. As at the year end, this increase was fully funded. Any of the Granite Finance Funding Limited issuers including this Company can utilise this reserve fund should the need arise.

HM Treasury has confirmed that it is its intention to continue to fund NRAM plc so as to maintain that company as a going concern and enable that company to meet its debts as and when they fall due until at least 1 October 2013. It has also committed to convert up to £1.6bn of the Government loan to meet regulatory capital requirements if so required. This should be regarded as a positive development for the Company.

Following the completion of the legal and capital restructuring on 1 January 2010, customers of NRAM plc, which includes all mortgages loans acquired by Granite Finance Funding Limited, which as part of the securitisation, were assigned to Granite Finance Trustees Limited ('the Trust') are not entitled to any further loans or new mortgage products. This has significantly reduced the volume of loans repurchased by NRAM plc from the Trust (further advances and product switches being criteria for repurchase from the Trust). This has ultimately reduced the level of principal receipts available to the Company and hence slowed down repayments to noteholders. Other than this, it is not anticipated that the legal and capital restructuring will have any impact upon the Company. It remains the case that noteholders will only be paid interest and principal to the extent that funds are received on the Trust's mortgage portfolio and used by Granite Finance Funding Limited to repay the inter-company loan with the Company in accordance with the inter-company agreements.

### **Results and dividends**

The Company is entitled to a pre-determined retained profit under the securitisation transaction documents. Under the terms of the securitisation, the Company retains the right to 0.01% of the interest received under the inter-company loan (as defined within the securitisation transaction documents). This is reflected in the income statement on page 9 net of temporary volatility relating to mismatches between foreign exchange revaluation movements and fair value changes in derivative instruments. The profit for the year of £122,000 (2010 £1,041,000) has been transferred to reserves. The Directors do not recommend the payment of a dividend (2010 £Nil). The Company's profit over the lifetime of the securitisation will be limited to the predetermined retained profit.

### **Taxation**

The Company's tax charge for the year has been calculated in accordance with the permanent regime for securitisation companies. Under the permanent regime, as the tax charge is based purely on contractually retained profit, the tax charge will not be affected by any profits or losses arising on derivatives and other financial instruments. This means that under IAS12, no deferred tax arises on any differences between cost and fair value.

### **Future outlook**

Although the legal and contractual maturity of the loan notes issued by the Company is in September 2044, the rate at which the loan to Granite Finance Funding Limited and the loan notes will actually reduce will depend upon the Company's allocation of Granite Finance Funding Limited's share of the Trust's principal receipts. Any significant changes in the level of the Trust's underlying mortgage redemptions or removals will have an

## Granite Mortgages 04-3 plc

impact upon the maturity profiles of the loan to Granite Finance Funding Limited and the loan notes. As Note 15 shows, arrears affecting the residential mortgages that underpin the deemed loan (see page 13) from Granite Finance Funding Limited to NRAM plc remain significant. A significant increase in arrears and/or repossession losses could ultimately lead to Granite Finance Funding Limited failing to repay all amounts due to the Company in respect of the inter company loan. This in turn could result in the Company failing to make all payments due to note holders in respect of principal and/or interest. Such a situation would not render the Company insolvent because the Company is only obliged to make payments to note holders to the extent that the inter company loan repayments allow.

### Key Performance Indicators (KPIs)

Given the straight forward nature of the business, the Company's Directors are of the opinion that analysis using KPIs is not necessary for an understanding of the development, performance or position of the Company. This is primarily the case because the Company's profit for the year (excluding any temporary hedge ineffectiveness relating to foreign exchange revaluation movements and fair value changes in derivative instruments) is fixed as detailed within the Results and dividends section above.

However, any issues or developments affecting the Company are discussed at a monthly management meeting and a monthly checklist is completed and reviewed detailing all of the key requirements that must be met under the various legal agreements which underpin the Granite Finance Holdings Limited group structure. The items covered are predominantly consideration of whether there have been breaches of the transaction documents, however there are certain specific tangible measures which are verified and which are relevant to the Company including assessing whether

- There is a potential interest rate shortfall in the next period i.e. whether expected available revenue is sufficient to meet interest payable in respect of AAA notes,
- The reserve funds are fully funded including any increase required as a result of a step-up trigger breach. A step-up trigger event occurs if any Granite Finance Funding Limited issuer, of which the Company is one, fails to exercise its option to redeem any of its notes on the relevant step-up date pursuant to the terms and conditions of such notes. As the notes issued by Granite Mortgages 03-3 plc were not redeemed in January 2009, the step-up trigger has been breached. As a consequence of this there is a requirement to increase Granite Mortgages 04-3 plc's issuer reserve fund (held by Granite Finance Funding Limited) by £10.8m. As at the year end, this increase was fully funded. As a further consequence of this breach the Granite Finance Funding Limited reserve fund required amount has increased by £22.1m. As at the year end, this increase was fully funded. Any of the Granite Finance Funding Limited issuers can utilise this reserve fund should the need arise,
- NRAM plc's rating remains adequate to support its ongoing roles in the programme. This is monitored within the monthly Secured Funding Management Information Pack prepared for NRAM plc management,
- Any notes have not been called at the step-up and call date. The notes were not called on their step-up date in September 2011. The margins payable have now doubled as detailed in the offering circular.

Additionally, any changes to the credit ratings assigned to the loan notes in issue are monitored. On 11<sup>th</sup> July 2011 Standard & Poors downgraded the Class A notes from AAA to A+ and the class B notes from AA+ to A+. At the same time their ratings of the Class M notes were reaffirmed as A+ and Class C notes were reaffirmed as A-. Further revisions to ratings were notified by Standard & Poors in January 2012 as detailed

## Granite Mortgages 04-3 plc

within note 19 Changes to the ratings of the loan notes in issue have no impact upon the Company, but may have an impact upon the pricing of the loan notes in the secondary market

The arrears performance of the residential mortgage portfolio that underpins the deemed loan (see page 13) from Granite Finance Funding Limited to NRAM plc is continuously monitored by the NRAM plc group and external credit rating agencies The performance of this mortgage portfolio ultimately determines the amounts that Granite Finance Funding Limited is able to repay to the Company in respect of the inter company loan This in turn determines the amounts that the Company is able to repay to the loan note holders in respect of the debt securities in issue Note 15 provides information with regard to the mortgage portfolio

The credit ratings of the Company's derivative counterparties are continuously monitored and when necessitated by the associated credit support agreements, collateral is called to mitigate against the risk of counterparty default

### **Financial risk management**

In order to manage and control its risks, the Company has implemented a comprehensive set of policies and procedures The manner in which the principal risks faced by the Company are mitigated is described below

#### ***Foreign exchange risk***

'Foreign exchange risk' arises when exchange rate fluctuations change the Sterling equivalent value of assets, liabilities, income and expense denominated in foreign currencies When loan notes issued are denominated in foreign currencies, the Company enters into cross currency swap agreements that exchange the funds raised for equivalent amounts of Sterling The Company receives foreign currency interest from the swap agreements equivalent to that due on the loan notes, in exchange for the payment of Sterling interest based upon three month UK LIBOR As the loan note principal is repaid, equivalent reductions are made to the outstanding swap notional amounts so that effective hedges are maintained The effect of the above policy is to eliminate all of the risks associated with exchange rate fluctuations

#### ***Interest rate risk***

'Interest rate risk' arises as a result of timing differences on the re-pricing of assets and liabilities, unexpected changes in the slope and shape of yield curves and changes in correlation of interest rates between different financial instruments (often referred to as basis risk) The interest receivable on the loan to Granite Finance Funding Limited (a NRAM plc group undertaking) re-prices on the same quarterly basis as the interest payable in respect of the loan notes (as adjusted by cross currency swaps), so that interest rate risk is eliminated

#### ***Credit risk***

'Credit risk' is the exposure to loss if another party fails to meet its financial obligations to the Company, including failing to perform them in a timely manner The Company's primary exposure is the loan to Granite Finance Funding Limited, which used the proceeds to purchase an interest in a portfolio of residential mortgages from NRAM plc The credit risk associated with the mortgage portfolio is continually monitored by the NRAM plc group and external rating agencies Note 15 provides information with regard to the quality of the underlying mortgage portfolio as at the year end A significant increase in the arrears and/or repossession losses associated with this mortgage portfolio could result in Granite Finance Funding Limited being unable to make all repayments of interest and principal due in respect of the loan to the Company This in turn could mean that the Company is unable to make all repayments of interest and principal due in respect of the loan notes It should be noted however, that the Company is only obliged to make repayments of interest and principal in respect of the loan notes to the extent that the repayments received from the loan to Granite Finance Funding Limited allow To reduce the exposure of the noteholders should such a situation arise, there are reserve funds held within Granite Finance Funding Limited, which can be drawn upon to meet shortfalls in

## **Granite Mortgages 04-3 plc**

interest and ultimately principal repayments. Of these reserves funds at 31 December 2011 £66.0m (2010 £60.6m) was ring fenced for use by the Company and an additional £49.8m (2010 £49.1m) was available for the use of any of the Granite Finance Funding Limited group issuers.

Master netting agreements are in place with all derivative counterparties, whose creditworthiness is continually monitored and assessed. Under the terms of the relevant credit support agreements, Swiss Re and Citigroup are obliged to deposit collateral with the Company and have done so throughout the year. This mitigates the risk that derivative asset positions are impaired as a result of the counterparties failing to meet their obligations. Collateral held is disclosed in Note 17.

### ***Liquidity risk***

'Liquidity risk' arises from a mismatch in the cash flows generated from current and expected assets, liabilities and derivatives. The Company's policy is to ensure that interest and principal repayments due from the loan to Granite Finance Funding Limited are timed to coincide with amounts due on the loan notes and associated cross currency swaps. The Company is only obliged to make repayments of interest and principal in respect of the loan notes to the extent that repayments are received from Granite Finance Funding Limited in respect of the loan.

### **Directors and their interests**

The Directors who served during the year and up to the date of the signing of the financial statements were

L D C Securitisation Director No. 1 Limited,  
L D C Securitisation Director No. 2 Limited,  
Alan Weatherston (appointed 03 March 2011),  
Jerold Robert Williamson (resigned 03 March 2011)

None of the Directors had a beneficial interest in the shares of the Company, or of the ultimate holding company, The Law Debenture Intermediary Corporation plc.

Alan Weatherston is an employee of Bradford & Bingley plc and is contracted to provide services to NRAM plc.

Jerold Robert Williamson was until 04 March 2011 an employee of Bradford & Bingley plc and was contracted to provide services to NRAM plc.

### **Employees**

The Company does not have any employees (2010 Nil).

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

Invoices received are all paid in the first instance by NRAM plc and then recharged to the Company. NRAM plc's policy is to settle invoices within 25 days of the invoice date.

### **Post balance sheet events**

On the 20 January 2012 Standard & Poors rating agency updated the criteria they use for assessing counterparty risk. This resulted in the Class A notes being downgraded from A+ to A, the Class B notes from A+ to A, the Class M notes from A+ to A and the Class C notes being upgraded from A- to A.

### **Statement of directors' responsibilities**

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

## Granite Mortgages 04-3 plc

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

- Select suitable accounting policies and then apply them consistently,
- Make judgements and accounting estimates that are reasonable and prudent,
- State whether applicable International Financial Reporting Standards (IFRSs) as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements,
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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

### Independent auditors

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office and a resolution that they be reappointed will be proposed at the annual general meeting.

### Disclosure of information to auditors

So far as each Director is aware, there is no relevant audit information (that is, information needed by the Company's auditors in connection with preparing their report) of which the Company's auditors are unaware. Each Director has taken all the steps (such as making enquiries of other Directors and the auditors and any other steps required by the director's duty to exercise due care, skill and diligence) that he ought to have taken in his duty 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.

By order of the Board



For and on behalf of Law Debenture Corporate Services Limited, Company Secretary

24 April 2012  
Registered Office  
Fifth Floor  
100 Wood Street  
London  
EC2V 7EX



# **Granite Mortgages 04-3 plc**

## **Independent auditors' report to the members of Granite Mortgages 04-3 plc**

We have audited the financial statements of Granite Mortgages 04-3 plc for the year ended 31 December 2011 which comprise the Income statement, the Statement of comprehensive income, the Balance sheet, the Statement of changes in equity, the Cash flow statement, the Statement of accounting policies and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

### **Respective responsibilities of directors and auditors**

As explained more fully in the Statement of directors' responsibilities statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

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

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

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

### **Opinion on financial statements**

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 December 2011 and of its profit and cash flows for the year then ended,
- have been properly prepared in accordance with IFRSs as adopted by the European Union, and
- have been prepared in accordance with the requirements of the Companies Act 2006

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

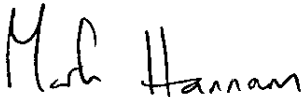
In our opinion the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

## Granite Mortgages 04-3 plc

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

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

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



Mark Hannam (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
Leeds  
24 April 2012

## Granite Mortgages 04-3 plc

### Income statement for the year ended 31 December 2011

	Note	2011 £'000	2010 £'000
Interest receivable and similar income	1	11,500	10,649
Interest payable and similar charges	2	(11,339)	(10,480)
Net interest income		161	169
Unrealised fair value gains and losses	3	121	1,041
Administrative expenses	4	(160)	(169)
Operating profit before taxation		122	1,041
Taxation	5	-	-
Profit for the year attributable to equity holders of the Company		122	1,041

### Statement of comprehensive income for the year ended 31 December 2011

Other than the profit for the year of £122,000 (2010 £1,041,000), there was no comprehensive income (2010 £Nil)

# Granite Mortgages 04-3 plc

## Balance sheet as at 31 December 2011

	Note	2011 £'000	2010 £'000
<b>Assets</b>			
Cash and cash equivalents	10	44,331	54,488
Loan due from group undertaking	7	757,380	941,625
Derivative financial instruments	8	44,235	59,510
Trade and other receivables	9	685	553
<b>Total assets</b>		<b>846,631</b>	<b>1,056,176</b>
<b>Liabilities</b>			
Financial liabilities (debt securities in issue)	11	798,657	998,293
Trade and other payables	12	44,926	54,957
Current tax liabilities		-	-
<b>Total liabilities</b>		<b>843,583</b>	<b>1,053,250</b>
<b>Equity shareholders' funds</b>			
Called up share capital	13	50	50
Retained surplus	14	2,998	2,876
<b>Total equity attributable to equity shareholders</b>		<b>3,048</b>	<b>2,926</b>
<b>Total equity and liabilities</b>		<b>846,631</b>	<b>1,056,176</b>

The financial statements on pages 9 to 46 were approved by the Board of Directors on 24 April 2012 and were signed on behalf of the Board of Directors by



L D C Securitisation Director No 1 Limited  
Director

Granite Mortgages 04-3 plc is registered in England and Wales under Company Number 05168395

## Granite Mortgages 04-3 plc

### Statement of changes in equity for the year ended 31 December 2011

	Share Capital	Retained Surplus	Total equity
	2011	2011	2011
	£'000	£'000	£'000
Balance at 1 January	50	2,876	2,926
Profit for the year and total comprehensive income	-	122	122
Balance at 31 December	50	2,998	3,048

	Share Capital	Retained Surplus	Total equity
	2010	2010	2010
	£'000	£'000	£'000
Balance at 1 January	50	1,835	1,885
Profit for the year and total comprehensive income	-	1,041	1,041
Balance at 31 December	50	2,876	2,926

# Granite Mortgages 04-3 plc

## Cash flow statement for the year ended 31 December 2011

	Note	2011 £'000	2010 £'000
<b>Net cash inflow/(outflow) from operating activities</b>			
Operating profit before taxation		122	1,041
		122	1,041
<b>Movements in operating assets</b>			
Movements in loan due from group undertaking		184,245	195,075
Movements in derivative financial instruments		15,275	12,707
Movements in trade and other receivables		(132)	(18)
		199,388	207,764
<b>Movements in operating liabilities</b>			
Movements in debt securities in issue		(199,636)	(208,834)
Movements in trade and other payables		(10,031)	(22,292)
		(209,667)	(231,126)
<b>Net cash outflow from operating activities</b>		(10,157)	(22,321)
Income taxes paid		-	(1)
<b>Net decrease in cash and cash equivalents</b>		(10,157)	(22,322)
Opening cash and cash equivalents		54,488	76,810
<b>Closing cash and cash equivalents</b>	10	44,331	54,488

Operating activities are the principal revenue producing activities of the Company and other activities which are not investing or financing activities

There were no cash flows from investing or financing activities during the year (2010 £Nil)

# Granite Mortgages 04-3 plc

## Statement of accounting policies

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

### **Basis of preparation**

These financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRS') and IFRIC interpretations, as endorsed by the European Union and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. The financial statements have been prepared on a going concern basis under the historical cost convention as modified by the revaluation of financial assets and liabilities held at fair value through profit and loss. A summary of the more important Company accounting policies is set out below.

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

### *Principles underlying going concern assumption*

The financial statements of the Company have been prepared on a going concern basis. The validity of this assumption is dependent upon the funding position of NRAM plc. If NRAM plc was unable to continue as a going concern, this may have an impact on the recoverability of certain assets in the balance sheet of the Company and a significant impact on its operations.

NRAM plc no longer operates as a deposit taking institution under the supervision of the FSA. NRAM plc is now authorised and regulated by the FSA as a mortgage administration company and NRAM plc's Directors believe that it has appropriate and adequate levels of capital to support these activities.

HM Treasury has confirmed that it is its intention to continue to fund NRAM plc so as to maintain that company as a going concern and enable that company to meet its debts as and when they fall due until at least 1 October 2013. It has also committed to convert up to £1.6bn of the Government loan to meet regulatory capital requirements if so required.

### *Deemed Loan*

The Company has a loan with Granite Finance Funding Limited, another NRAM plc group undertaking. Granite Finance Funding Limited originally used the proceeds of this loan to purchase an interest in a portfolio of residential mortgages written by NRAM plc and held in trust by Granite Finance Trustees Limited. Under IAS39 it is the case that although the mortgage portfolio has been legally sold by NRAM plc, this has not resulted in NRAM plc passing on substantially all of the risks and rewards associated with the mortgage portfolio. Accordingly the mortgage portfolio remains on NRAM plc's balance sheet and Granite Finance Funding Limited instead has a deemed loan with NRAM plc. The Directors have considered the quality of the mortgage assets issued by NRAM plc as represented by the deemed loan and have concluded that it is appropriate to prepare the accounts on a going concern basis. The Company is only obliged to make repayments to noteholders to the extent permitted by receipts from Granite Finance Funding Limited in respect of the loan. Such receipts are determined by Granite Finance Funding Limited's receipts from NRAM plc in respect of the deemed loan, which are in turn determined by the performance of the underlying mortgage portfolio.

## Granite Mortgages 04-3 plc

### *Guaranteed Investment Contract Amounts*

Granite Finance Funding Limited and Granite Finance Trustees Limited (another NRAM plc group undertaking) both hold cash in bank accounts held at NRAM plc. Under the terms of the transaction documents, NRAM plc is the Guaranteed Investment Contract (the 'GIC') account provider. Should NRAM plc's short term unsecured, unsubordinated, and unguaranteed debt obligations cease to be rated A-1 by S&P, P-1 by Moody's or F1 by Fitch then the GIC accounts must be transferred to another appropriately rated bank or NRAM plc must obtain a guarantee of its obligations under the Bank Account Agreement from a satisfactorily rated financial institution. The existing ratings remain strong enough to allow NRAM plc to continue as the GIC account provider.

If cash at bank and in hand was not recoverable, this may affect Granite Finance Funding Limited and Granite Finance Trustees Limited's ability to meet financial obligations due to the Company and subsequently the Company's ability to meet financial obligations due to the note holders.

Under the terms of the Bank of England and HM Treasury guarantees detailed above, the cash held in the GIC accounts at NRAM plc by Granite Finance Funding Limited and Granite Finance Trustees Limited is guaranteed.

### *Interest rate swap*

NRAM plc (in its capacity as the Interest Rate Swap Provider) has agreed to act as a swap provider to Granite Finance Funding Limited to hedge possible variances between the rates of interest payable on the Mortgage Loans that comprise the deemed loan between Granite Finance Funding Limited and NRAM plc and LIBOR for three month Sterling deposits by entering into the Interest Rate Swap Agreement with Granite Finance Funding Limited and the Security Trustee. The ability of Granite Finance Funding Limited to pay interest in respect of the loan from the Company is in part dependent upon the interest rate swap remaining in place. The Interest Rate Swap Provider will be required to obtain a guarantee of its obligations or put in place some other arrangement in the event that its short term unsecured, unsubordinated, and unguaranteed debt obligations cease to be rated A-1 by S&P, P-1 by Moody's or F1 by Fitch. The existing ratings remain strong enough to allow NRAM plc to continue as the Interest Rate Swap Provider.

Upon the termination of the Interest Rate Swap pursuant to an Interest Rate Swap Early Termination Event, Granite Finance Funding Limited or the Interest Rate Swap Provider may be liable to make a termination payment to the other in accordance with the provisions of the Interest Rate Swap Agreement.

Under the terms of the Bank of England and HM Treasury guarantees detailed above, the payments due under the Interest Rate Swap Agreement are guaranteed.

### *The servicer and the administration agreement*

Granite Finance Trustees Limited and the beneficial owners of the trust property have retained NRAM plc under the terms of the administration agreement as the servicer of the mortgage loans. NRAM plc has sub-contracted elements of the servicing to Northern Rock plc, a new bank formed on 1 January 2010 as part of the legal and capital restructure. The ability of Granite Finance Funding Limited to make the payments due in respect of the loan to the Company is in part dependent upon the servicer administering the mortgage balances (which form the Trust's property) and transactions affecting the mortgage balances in a prompt and accurate manner.

The servicer administers and services the mortgage loans and their related security in accordance with its administration, arrears and enforcement policies and procedures (collectively referred to as the 'administration procedures').



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Administration procedures include monitoring compliance with and administering the mortgage loan features and facilities applicable to the mortgage loans, responding to customer inquiries and management of mortgage loans in arrears

The appointment of the servicer may be terminated by Granite Finance Trustees Limited or Granite Finance Funding Limited and Granite Finance Funding 2 Limited (another NRAM plc group undertaking) immediately upon written notice to the servicer, on the occurrence of certain events (each a 'servicer termination event') including the occurrence of an insolvency event in relation to the servicer

Upon termination of the servicer, the Security Trustee has agreed to use their reasonable endeavours to appoint a substitute servicer. No such event has occurred.

### **Interest income and expense**

Interest income and expense are recognised in the income statement for all instruments measured at amortised cost using the effective interest rate method.

The effective interest rate method calculates the amortised cost of a financial asset or a financial liability, and allocates the interest income or interest expense over the relevant year. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through 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. When calculating the effective interest rate, the Company estimates cash flows considering all contractual terms of the financial instrument (for example prepayment options) but does not consider future credit losses. The calculation includes all amounts received or paid by the Company that are an integral part of the overall return, direct incremental transaction costs related to the acquisition or issue of a financial instrument and all other premiums and discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

### **Financial instruments**

The Company's loan to Granite Finance Funding Limited is classified as loans and receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, whose recoverability is based solely on the credit risk of the counterparty and where the Company has no intention of trading the loan.

Both loans and receivables and financial liabilities other than derivative financial instruments are initially recognised at fair value including direct and incremental transaction costs. Subsequent recognition is at amortised cost using the effective interest rate method. All regular way trades are accounted for on a trade date basis.

### **Offsetting financial instruments**

Financial assets and 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.

### **Derivative financial instruments and hedge accounting**

The Company undertakes transactions in derivative financial instruments, which include cross currency swaps. The Company's derivative activities are entered into for the purpose of matching or eliminating risk, from potential movements in interest and foreign exchange rates, inherent in the Company's liabilities. All

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derivative transactions are for economic hedging purposes and so it is therefore decided at the outset which position the derivative will be hedging. Derivatives are reviewed regularly for their effectiveness as hedges and corrective action taken, if appropriate. Derivatives are measured initially at fair value and subsequently remeasured to fair value. In the absence of a quoted price in an active market, fair values are obtained from valuation techniques including discounted cash flow models. Derivatives are not designated as part of accounting hedge relationships, therefore changes in fair value are recorded in the income statement, without any offsetting fair value adjustments to the underlying debt securities.

### **Impairment losses**

The Company assesses its financial assets for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event (or events) that has occurred after initial recognition and before the balance sheet date and has a reliably measurable impact on the estimated future cash flows of the financial assets.

Losses suffered by Granite Finance Funding Limited in respect of the deemed loan (see page 13) to NRAM plc will not cause impairment to the Company's loan to Granite Finance Funding Limited until all available credit enhancement is used up. Credit enhancement is represented by excess spread and reserve funds held by Granite Finance Funding Limited.

### **Assets held at amortised cost**

The Company first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the Company about the following loss events:

- (a) significant financial difficulty of the issuer or obligor,
- (b) a breach of contract, such as a default or delinquency in interest or principal repayments,
- (c) the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- (d) it becomes probable that the borrower will enter bankruptcy or other financial reorganisation,
- (e) the disappearance of an active market for that financial asset because of financial difficulties, or observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including
  - (i) adverse changes in the payment status of borrowers in the portfolio,
  - (ii) national or local economic conditions that correlate with defaults on the assets in the portfolio

If the Company determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment. If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an impairment allowance and the amount of the loss is recognised in the income statement. In future periods the unwind of the discount is recognised within interest income.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been

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determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the customer's credit rating), the previously recognised impairment loss is reversed by adjusting the impairment allowance. The amount of the reversal is recognised in the income statement.

The only asset held by the Company that is at risk of material impairment is the loan to Granite Finance Funding Limited, the repayment of which is dependent upon the performance of the residential mortgage portfolio as represented by the deemed loan from Granite Finance Funding Limited to NRAM plc. The risk of impairment is mitigated to a degree by the existence of reserve funds as detailed within the Credit risk section of the Directors' report. The performance of the mortgage portfolio is continually assessed by the NRAM plc group and external credit rating agencies. It follows that the impairment policies of the NRAM plc group are applied by the Company.

### **Debt and equity securities in issue**

Issued securities are classified as liabilities where the contractual arrangements result in the Company having an obligation to deliver either cash or another financial asset to the security holder, or to exchange financial instruments under conditions that are potentially unfavourable to the Company. Financial liabilities are carried at amortised cost using the effective interest rate method (see 'interest income and expense'). In the event that losses exceed the available credit enhancement, debt securities in issue may suffer principal write-downs and/or interest shortfalls. Any such losses will initially affect the Class C notes, followed by the M notes, then the B notes and finally the A notes. Issued securities are classified as equity where they meet the definition of equity and confer a residual interest in the Company's assets on the holder of the securities.

### **Foreign currency translation**

The Company's functional currency is Sterling and therefore under the guidance of IAS21 it follows that Sterling is the appropriate presentational currency.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are translated at the rate prevailing at the balance sheet date. Foreign exchange gains and losses resulting from the restatement and settlement of such transactions are recognised in the income statement.

### **Cash and cash equivalents**

For the purposes of the balance sheet and cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition.

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### **Collateral pledged and received**

Cash collateral is received as part of normal derivative operations and is recognised as an asset of the Company because the Company bears the risks and rewards associated with the investment of this cash with NRAM plc. In addition the Company may hold securities collateral. In the absence of counterparty default, the Company has no right to sell or repledge such securities and therefore in accordance with the provisions of IAS39 such securities are not recognised on the Company's balance sheet. No collateral is ever pledged.

### **Taxation**

Income tax payable on taxable profits ('current tax') is recognised as an expense in the year in which the profits arise. Income tax recoverable on tax allowances is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits.

During 2009 the Directors elected irrevocably to enter into the permanent regime for the taxation of securitisation companies. Taxable profits under the permanent regime will equal the contractually retained profit as defined by the original transaction documentation, being 0.01% of the interest received under the inter-company loan.

### **Segmental reporting**

The Directors of the Company consider that the Company has one operating segment due to the similarity of risks faced in relation to the investment of the proceeds of the issue of asset backed loan notes and therefore is not required to produce additional segmental disclosure.

### **Statement of compliance**

The Company Financial Statements have been prepared and approved by the Directors in accordance with International Financial Reporting Standards as adopted by the EU.

### **Implementation of new standards and amendments to published standards and interpretations effective during 2011**

For these 2011 Financial Statements, including the 2010 comparative financial information where applicable, the Company has adopted for the first time the following statement:

- The November 2009 amendments to IAS24 'Related Party Disclosures', which clarified the disclosure requirements for Government-related entities.

### **Standards, interpretations and amendments to published standards that are not yet effective and the early adoption of standards**

For these 2011 Financial Statements the Company has not adopted the following statements, but is continuing to assess whether these statements will have any impact on the Financial Statements:

- IFRS9 'Financial Instruments', sections of which have been issued as part of the International Accounting Standard Board's ('IASB's') project to replace IAS39 'Financial Instruments Recognition and Measurement', and the associated amendments to IFRS7 'Financial Instruments Disclosures'. These statements are expected to be mandatory for 2015 Financial Statements, with 2014 comparative information, but have not yet been adopted for use in the EU. The Group continues to monitor developments,
- IFRS13 'Fair Value Measurement'. This statement is expected to be mandatory for 2013 Financial Statements, with 2012 comparative information, but has not yet been adopted for use in the EU,
- The June 2011 amendments to IAS1 'Presentation of Financial Statements' relating to 'Presentation of Items of Other Comprehensive Income'. This statement is expected to be mandatory for 2013.

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Financial Statements, with 2012 comparative information, but has not yet been adopted for use in the EU

### **Critical accounting estimates**

#### ***Fair value calculations***

Fair value is defined as the value at which assets, liabilities or positions could be closed out or sold in a transaction with a willing and knowledgeable counterparty. For the majority of instruments carried at fair value, these are determined by reference to quoted market prices. Where these are not available, fair value is based upon cash flow models, which use wherever possible independently sourced market parameters such as interest rate yield curves, currency rates and option volatilities. Other factors are also considered, such as counterparty credit quality and liquidity. Management must use judgement and estimates where not all necessary data can be externally sourced or where factors specific to the Company's holdings need to be considered. The accuracy of the fair value calculations would therefore be affected by unexpected market movements, inaccuracies within the models used compared to actual outcomes and incorrect assumptions. For example, if management were to change the credit spread by 10 basis points, the fair values of liabilities and derivatives would change from the reported fair values by £0.2m (2010 £0.2m).

# Granite Mortgages 04-3 plc

## Notes to the financial statements for the year ended 31 December 2011

### 1 Interest receivable and similar income

	2011 £'000	2010 £'000
On loan due from Granite Finance Funding Limited	10,934	10,313
Other interest receivable from NRAM plc group undertakings	566	336
	11,500	10,649

### 2 Interest payable and similar charges

	2011 £'000	2010 £'000
On debt securities in issue (see note 11)	10,934	10,302
On collateral pledged by swap counterparties (see note 17)	405	178
	11,339	10,480

Under the terms of the associated credit support agreements, the Company is obliged to pay interest to swap counterparties in respect of any collateral pledged. All collateral is deposited with NRAM plc. Interest receipts in respect of such deposits are equal to amounts due to swap counterparties, hence the Company does not make any gain or loss from collateral deposits.

### 3 Unrealised fair value gains and losses

	2011 £'000	2010 £'000
Fair value movements of future cash flows excluding interest flows on non-hedging derivatives	(5,947)	(2,210)
Translation gains and losses on underlying instruments	6,068	3,251
Unrealised fair value gains and losses	121	1,041

The Company enters into certain derivative financial instruments which although highly effective as economic hedges are not included in hedge accounting relationships. These derivatives hedge foreign currency securitised funding recorded at amortised cost.

## Granite Mortgages 04-3 plc

### 3 Unrealised fair value gains and losses (continued)

The fair value movements of future cash flows excluding interest flows on such derivatives are separately identified within 'Unrealised fair value gains and losses', together with the translation gains and losses on underlying instruments arising from the revaluation from foreign currency into Sterling. The deemed interest flows on such derivatives are included within interest payable and similar charges.

### 4 Administrative expenses

	2010 £'000	2009 £'000
Administration charges – NRAM plc	117	117
Auditors remuneration – statutory audit services	7	12
Other administrative expenses	36	40
	160	169

The Company has no employees (2010: None). No emoluments were paid to the Directors for their services to the Company during the year (2010: £Nil). A fee for cash management services is charged by NRAM plc. The Company's audit fee is initially billed to NRAM plc and then subsequently recharged to the Company. There were no non-audit fees paid to the Company's auditors during the period (2010: £Nil).

### 5 Taxation

The income tax expense for the year comprises:

The taxation charge relates to the profit for the year as follows:

	2011 £'000	2010 £'000
Profit for the year	122	1,041
Tax on this calculated at the standard rate of corporation tax in the UK of 26.5% (2010: 28%)	(32)	(292)
Tax effect of income and expenses that are deductible in determining taxable profit	32	292
Income tax expense for the year	-	-

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## 5 Taxation (continued)

Analysis of tax charge in the year:

	2011 £'000	2010 £'000
<b>Current tax:</b>		
UK corporation tax on taxable profit for the year	-	-
	-	-

## 6 Analysis of financial assets and liabilities by measurement basis

2011	Financial liabilities at amortised cost £'000	Loans and receivables £'000	Held for trading £'000	Total £'000
<b>Financial assets</b>				
Cash and cash equivalents	-	44,331	-	44,331
Loan due from group undertaking	-	757,380	-	757,380
Derivative financial instruments	-	-	44,235	44,235
Trade and other receivables	-	685	-	685
<b>Total financial assets</b>	-	<b>802,396</b>	<b>44,235</b>	<b>846,631</b>
<b>Financial liabilities</b>				
Debt securities in issue	798,657	-	-	798,657
Trade and other payables	44,926	-	-	44,926
Current tax liabilities	-	-	-	-
Deferred tax liabilities	-	-	-	-
<b>Total financial liabilities</b>	<b>843,583</b>	-	-	<b>843,583</b>
Equity				3,048
				<b>846,631</b>



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### 6 Analysis of financial assets and liabilities by measurement basis (continued)

2010	Financial liabilities at amortised cost £'000	Loans and receivables £'000	Held for trading £'000	Total £'000
<b>Financial assets</b>				
Cash and cash equivalents	-	54,488	-	54,488
Loan due from group undertaking	-	941,625	-	941,625
Derivative financial instruments	-	-	59,510	59,510
Trade and other receivables	-	553	-	553
<b>Total financial assets</b>	-	<b>996,666</b>	<b>59,510</b>	<b>1,056,176</b>
<b>Financial liabilities</b>				
Debt securities in issue	998,293	-	-	998,293
Trade and other payables	54,957	-	-	54,957
Current tax liabilities	-	-	-	-
Deferred tax liabilities	-	-	-	-
<b>Total financial liabilities</b>	<b>1,053,250</b>	-	-	<b>1,053,250</b>
Equity				2,926
				<b>1,056,176</b>

### 7 Loan due from group undertaking

	2011 £'000	2010 £'000
Loans and advances to Granite Finance Funding Ltd	<b>757,380</b>	941,625
Current	<b>122,456</b>	144,731
Non-current	<b>634,924</b>	796,894
	<b>757,380</b>	941,625

The loans and advances are all denominated in Sterling and are at variable rates of interest, based on three month quoted LIBOR. The repayment of the loan due from Granite Finance Funding Limited is dependent upon that company's receipts in respect of the deemed loan with NRAM plc (see page 13). Although the underlying mortgage loans represented by the deemed loan all have contractual maturities in excess of one year, amounts classified as 'Current' represent expected repayments due within the next twelve months.

## 8 Derivative financial instruments

The Directors have authorised the use of derivative instruments for the purpose of supporting the strategic and operational business activities of the Company and reducing the risk of loss arising from changes in interest rates and exchange rates. All use of derivative instruments within the Company is to hedge risk exposure, and the Company takes no trading positions in derivatives. However, derivatives not in an accounting hedge relationship are classified as Held for Trading in accordance with IAS39.

The objective, when using any derivative instrument, is to ensure that the risk to reward profile of any transaction is optimised. The intention is to only use derivatives to create economically effective hedges. However, because of the specific requirements of IAS39 to obtain hedge accounting, no economic hedges are designated as accounting hedges, either because natural accounting offsets are expected or because obtaining hedge accounting would be especially onerous.

### Fair values at 31 December 2011

	Contract/ notional amount £'000	Assets £'000	Liabilities £'000
<b>Derivatives in economic hedging relationships but not in accounting hedge relationships</b>			
Cross currency swaps	200,326	44,235	-
<b>Total recognised derivative assets/(liabilities)</b>	<b>200,326</b>	<b>44,235</b>	<b>-</b>
<b>Expected maturities</b>			
< 3 months	9,762	1,956	-
3-6 months	8,246	1,652	-
6-12 months	14,277	2,861	-
1-5 years	103,019	20,940	-
> 5 years	65,022	16,826	-
	<b>200,326</b>	<b>44,235</b>	<b>-</b>

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## 8 Derivative financial instruments (continued)

	Fair values at 31 December 2010		
	Contract/ notional amount	Assets	Liabilities
	£'000	£'000	£'000
<b>Derivatives in economic hedging relationships but not in accounting hedge relationships</b>			
Cross currency swaps	248,900	59,510	-
<b>Total recognised derivative assets/(liabilities)</b>	<b>248,900</b>	<b>59,510</b>	<b>-</b>
<b>Expected maturities</b>			
< 3 months	10,172	2,237	-
3-6 months	9,433	2,075	-
6-12 months	18,553	4,081	-
1-5 years	101,687	22,367	-
> 5 years	109,056	28,750	-
	<b>248,901</b>	<b>59,510</b>	<b>-</b>

## 9 Trade and other receivables

	2011	2010
	£'000	£'000
Accrued interest receivable on loan to Granite Finance Funding Ltd	447	330
Called up share capital not paid	38	38
Other amounts owed by third parties	3	-
Other amounts owed by Granite Finance Funding Ltd	179	165
Accrued interest receivable on deposits with NRAM plc	18	20
	<b>685</b>	<b>553</b>
Current	<b>685</b>	<b>553</b>
Non-current	-	-
	<b>685</b>	<b>553</b>

## Granite Mortgages 04-3 plc

### 10 Cash and cash equivalents

	2011	2010
	£'000	£'000
Cash at bank and in hand	44,331	54,488
Current	44,331	54,488
Non-current	-	-
	44,331	54,488

The Company holds deposits totalling £44,328,000 (2010 £54,485,000) at NRAM plc. These deposits are covered by the HM Treasury guarantees that are currently in place. These amounts represent collateral received from derivative counterparties pursuant to the provisions of associated credit support agreements. NRAM plc invests these deposits on a short term basis and pays interest earned to the Company, which in turn pays the interest to the derivative counterparties. The Company holds a deposit of £3,000 (2010 £3,000) at a third party bank, which pays variable rate interest based on three months quoted LIBOR.

Cash deposits, excluding collateral, are utilised in accordance with the revenue and principal priorities of payment contained within the Company's offering circular. The Company will only be free to utilise collateral in the event that there is a default by the derivative counterparty in relation to the associated cross currency swaps.

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## 11 Financial liabilities (debt securities in issue)

	Currency of Issued Note	Interest Rate	2011 £'000	2010 £'000
Series 2 Class A1 Floating Rate Notes Sept 2044	USD	3M US LIBOR + 0.28	62,946	86,647
Series 2 Class A2 Floating Rate Notes Sept 2044	EUR	3M EURIBOR + 0.28	91,621	129,982
Series 2 Class B Floating Rate Notes Sept 2044	EUR	3M EURIBOR + 0.56	23,864	24,608
Series 2 Class M Floating Rate Notes Sept 2044	EUR	3M EURIBOR + 0.74	18,571	19,150
Series 2 Class C Floating Rate Notes Sept 2044	EUR	3M EURIBOR + 1.6	44,601	45,990
Series 3 Class A1 Floating Rate Notes Sept 2044	GBP	3M GBP LIBOR + 0.36	146,811	201,985
Series 3 Class A2 Floating Rate Bonds Sept 2044	GBP	3M GBP LIBOR + 0.38	214,193	293,881
Series 3 Class B Floating Rate Notes Sept 2044	GBP	3M GBP LIBOR + 0.7	54,350	54,350
Series 3 Class M Floating Rate Notes Sept 2044	GBP	3M GBP LIBOR + 0.9	42,250	42,250
Series 3 Class C Floating Rate Notes Sept 2044	GBP	3M GBP LIBOR + 1.76	99,450	99,450
<b>Debt securities in issue</b>			<b>798,657</b>	<b>998,293</b>
Current			128,779	152,248
Non-current			669,878	846,045
			<b>798,657</b>	<b>998,293</b>

Debt securities in issue as at 31 December 2011 and 31 December 2010 are shown in original currency translated at year end rates of exchange. Exchange rate fluctuations may cause the reported value of debt securities in issue to exceed the reported value of the loan due from Granite Finance Funding Limited (see note 7). The value of debt securities in issue as modified by applicable cross currency swaps is equal to the loan due from Granite Finance Funding Limited. The current/non-current split reflects the expected pattern of repayments and is based upon the expected repayment profile of the loan due from Granite Finance Funding Limited.

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### 11 Financial liabilities (debt securities in issue) (continued)

The Class A notes will rank in priority to the Class B notes in point of security as to the payment of principal and interest. The Class B notes will rank in priority to the Class M notes in point of security as to the payment of principal and interest. The Class M notes will rank in priority to the Class C notes in point of security as to the payment of principal and interest. Payments in respect of the Class B notes will only be made if and to the extent that, there are sufficient funds after paying certain liabilities, including liabilities in respect of the Class A notes. Payments in respect of the Class M notes will only be made if and to the extent that, there are sufficient funds after paying certain liabilities, including liabilities in respect of the Class B notes. Payments in respect of the Class C notes will only be made if and to the extent that, there are sufficient funds after paying certain liabilities, including liabilities in respect of the Class M notes.

The notes are contractually repayable in more than five years, but will pay down on each quarterly payment date to the extent that principal repayments have been received in respect of the Company's loan to Granite Finance Funding Limited. Interest is payable on the notes at variable rates based on the three-month Sterling LIBOR, three-month Euribor and three-month US Dollar LIBOR. The notes repriced on 20 March 2012. The notes were not called on their step-up date in September 2011. As a consequence, the margins payable have doubled as detailed in the offering circular.

The Company has not had any defaults of principal, interest or other breaches in respect of debt securities during the year (2010 Nil)

### 12 Trade and other payables

	2011 £'000	2010 £'000
Accrued interest payable	484	375
Amounts owed to NRAM plc group undertakings	112	97
Collateral pledged by swap counterparties	44,329	54,485
Amounts owed to third parties	1	-
	44,926	54,957
Current	44,926	54,957
Non-current	-	-
	44,926	54,957

## Granite Mortgages 04-3 plc

### 13 Called up share capital

	2011 £'000	2010 £'000
<b>Authorised</b>		
50,000 ordinary shares of £1 each	50	50
<b>Called up and allotted share capital</b>		
50,000 ordinary shares of £1 each	50	50
<b>Paid up share capital</b>		
12,500 ordinary shares of £1 each	12	12
<b>Called up share capital not paid</b>		
37,500 ordinary shares of £1 each	38	38

### 14 Retained surplus

	£'000
Balance at 31 December 2010	2,876
Profit for the financial year	122
Balance at 31 December 2011	2,998
	£'000
Balance at 31 December 2009	1,835
Profit for the financial year	1,041
Balance at 31 December 2010	2,876

### 15 Financial risk management

#### Risk management

In order to manage and control its risks, the Company has implemented a comprehensive set of policies and procedures. The manner in which the principal risks faced by the Company are mitigated is described below.

#### Concentration risk

Concentration risk refers to any exposure with the potential to produce losses large enough to threaten the Company's ability to maintain its core operations. This would include exposures to individual counterparties and counterparties in specific geographical locations.

## Granite Mortgages 04-3 plc

### 15 Financial risk management (continued)

The following table breaks down the Company's main credit exposures by geographical region at their carrying amounts. Exposures are allocated to regions based on the country of domicile of the counterparty.

2011	UK £'000	Europe £'000	Other countries £'000	US £'000	Total £'000
Cash and cash equivalents	44,331	-	-	-	44,331
Loan due from group undertaking	-	-	757,380	-	757,380
Derivative financial instruments	-	8,139	-	36,096	44,235
	<b>44,331</b>	<b>8,139</b>	<b>757,380</b>	<b>36,096</b>	<b>845,946</b>
2010					
Cash and cash equivalents	54,488	-	-	-	54,488
Loan due from group undertaking	-	-	941,625	-	941,625
Derivative financial instruments	-	11,339	-	48,171	59,510
	<b>54,488</b>	<b>11,339</b>	<b>941,625</b>	<b>48,171</b>	<b>1,055,623</b>

Concentration risk in respect of derivative financial instruments is managed through the terms of the cross currency swaps in place. In the event of downgrades, the swap counterparties are required to post one way collateral.

The 'Other countries' exposure is to Jersey, since this is where Granite Finance Funding Limited is incorporated. The ability of this company to repay the loan is dependent upon the performance of a residential mortgage portfolio originally issued by NRAM plc, held in trust by Granite Finance Trustees Limited, in which Granite Finance Funding Limited has a beneficial interest.



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### 15 Financial risk management (continued)

A further measure of concentration risk concerns the degree to which the mortgage loans are concentrated in particular regions of the United Kingdom. The following tables are derived from the monthly Investors' Reports of Granite Finance Trustees Limited. They show a geographical analysis of all non-reposessed loans held in the Trust, in which the Company has a beneficial interest.

Region	Number	% of Total	31 December 2011	
			Value (£)	% of Total
East Anglia	4,419	2.27%	472,253,262	2.35%
East Midlands	16,506	8.50%	1,605,935,782	8.00%
Greater London	18,247	9.39%	2,907,733,098	14.49%
North	18,161	9.35%	1,288,716,323	6.42%
North West	26,818	13.80%	2,376,858,247	11.85%
Scotland	23,403	12.04%	1,751,393,969	8.73%
South East	28,110	14.47%	3,818,312,765	19.03%
South West	13,825	7.12%	1,678,233,780	8.36%
Wales	8,732	4.49%	805,991,363	4.02%
West Midlands	15,416	7.93%	1,569,087,659	7.82%
Yorkshire & Humberside	20,664	10.64%	1,791,717,312	8.93%
<b>Total</b>	<b>194,301</b>	<b>100.00%</b>	<b>20,066,233,560</b>	<b>100.00%</b>

## Granite Mortgages 04-3 plc

### 15 Financial risk management (continued)

Region	Number	% of Total	31 December 2010	
			Value (£)	% of Total
East Anglia	5,341	2.35%	581,350,215	2.44%
East Midlands	18,818	8.28%	1,853,501,313	7.76%
Greater London	21,942	9.65%	3,564,011,728	14.93%
North	21,198	9.33%	1,526,862,050	6.40%
North West	30,632	13.47%	2,743,385,984	11.49%
Scotland	27,406	12.06%	2,087,443,913	8.75%
South East	33,692	14.82%	4,636,402,151	19.42%
South West	16,534	7.27%	2,019,987,981	8.46%
Wales	10,004	4.40%	931,047,976	3.90%
West Midlands	17,614	7.75%	1,811,628,185	7.59%
Yorkshire & Humberside	24,150	10.62%	2,115,844,909	8.86%
<b>Total</b>	<b>227,331</b>	<b>100.00%</b>	<b>23,871,466,405</b>	<b>100.00%</b>

A further measure of concentration risk concerns the degree to which the Trust's mortgage assets are concentrated in high loan to value (LTV) loans. The following tables are derived from the monthly Investors' Reports of Granite Finance Trustees Limited. They show the current LTV levels breakdown as at 31 December in each year of the Trust's non-reposessed mortgage assets, in which the Company has a beneficial interest.

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

31 December 2011			
LTV Levels Breakdown	Number	Value (£)	% of Total
0% to 25%	17,096	360,133,530	1.80%
25% to 50%	19,857	1,304,905,053	6.50%
50% to 55%	5,009	436,886,216	2.18%
55% to 60%	5,654	537,396,570	2.68%
60% to 65%	6,566	657,649,086	3.28%
65% to 70%	7,974	853,176,869	4.25%
70% to 75%	10,499	1,154,406,678	5.75%
75% to 80%	13,978	1,629,882,393	8.12%
80% to 85%	24,219	2,786,062,552	13.88%
85% to 90%	35,643	4,303,666,633	21.45%
90% to 95%	26,901	3,261,142,588	16.25%
95% to 100%	17,086	2,285,939,879	11.39%
>100%	3,819	494,985,513	2.47%
<b>Total</b>	<b>194,301</b>	<b>20,066,233,560</b>	<b>100.00%</b>

31 December 2010			
LTV Levels Breakdown	Number	Value (£)	% of Total
0% to 25%	19,195	454,563,206	1.90%
25% to 50%	25,683	1,776,784,308	7.44%
50% to 55%	6,387	580,759,572	2.43%
55% to 60%	7,104	699,785,139	2.94%
60% to 65%	8,002	828,963,446	3.47%
65% to 70%	9,380	1,048,840,161	4.39%
70% to 75%	11,888	1,375,573,564	5.77%
75% to 80%	15,101	1,848,894,562	7.75%
80% to 85%	23,464	2,863,347,932	11.99%
85% to 90%	41,854	5,038,126,978	21.11%
90% to 95%	34,810	4,156,827,792	17.41%
95% to 100%	19,917	2,626,644,083	11.00%
>100%	4,546	572,355,662	2.40%
<b>Total</b>	<b>227,331</b>	<b>23,871,466,405</b>	<b>100.00%</b>

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

### Credit risk

'Credit risk' is the exposure to loss if another party fails to meet its financial obligations to the Company, including failing to perform them in a timely manner

Master netting agreements are in place with all derivative counterparties, whose creditworthiness is continually monitored and assessed. In the event that derivative counterparties are downgraded by the credit rating agencies below certain thresholds (as defined by the associated credit support agreements) and the relevant derivatives are assets to the Company, the counterparties are obliged to deposit collateral with the Company. This mitigates the risk that derivative asset positions are impaired as a result of counterparties failing to meet their obligations.

The Company's primary exposure is the loan to Granite Finance Funding Limited, which used the proceeds to purchase an interest in a portfolio of residential mortgages held in trust by Granite Finance Trustees Limited. Although Granite Finance Funding Limited is not assigned a credit rating by external rating agencies, the credit risk associated with the mortgage portfolio is continually monitored by the NRAM plc group and external rating agencies.

The following tables are derived from the monthly Investors' Reports of Granite Finance Trustees Limited. They show the arrears performance of the Trust's non-reposessed mortgage loans, in which the Company has a beneficial interest.

Months in arrears	Number	Principal (£)	Arrears (£)	31 December 2011	
				By number (%)	By principal (%)
Not in arrears	173,680	17,531,344,507	-	89.39%	87.36%
>=1<2 Months	6,202	739,875,316	5,411,599	3.19%	3.68%
>=2<3 Months	3,670	444,188,085	5,722,835	1.89%	2.21%
>=3<4 Months	2,379	291,385,099	5,181,282	1.22%	1.45%
>=4<5 Months	1,681	204,095,148	4,673,230	0.87%	1.02%
>=5<6 Months	1,272	152,936,852	4,215,796	0.65%	0.76%
>=6<7 Months	1,016	125,559,374	4,020,101	0.52%	0.63%
>=7<8 Months	719	91,610,193	3,370,686	0.37%	0.46%
>=8<9 Months	655	81,735,271	3,412,366	0.34%	0.41%
>=9<10 Months	480	59,684,816	2,799,289	0.25%	0.30%
>=10<11 Months	416	53,371,093	2,722,231	0.21%	0.27%
>=11<12 Months	345	49,500,971	2,587,531	0.18%	0.25%
>=12	1,786	240,946,835	20,275,069	0.92%	1.20%
<b>Total</b>	<b>194,301</b>	<b>20,066,233,560</b>	<b>64,392,015</b>	<b>100.00%</b>	<b>100.00%</b>

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

Months in arrears	Number	Principal (£)	Arrears (£)	31 December 2010	
				By number (%)	By principal (%)
Not in arrears	206,791	21,322,764,545	-	90.96%	89.32%
>=1<2 Months	5,927	712,953,515	5,157,245	2.61%	2.99%
>=2<3 Months	3,187	389,532,788	4,949,540	1.40%	1.63%
>=3<4 Months	2,139	259,210,071	4,657,683	0.94%	1.09%
>=4<5 Months	1,640	199,077,556	4,542,872	0.72%	0.83%
>=5<6 Months	1,255	155,122,685	4,250,440	0.55%	0.65%
>=6<7 Months	957	118,943,682	3,842,213	0.42%	0.50%
>=7<8 Months	807	99,456,640	3,651,666	0.36%	0.42%
>=8<9 Months	723	87,289,348	3,599,324	0.32%	0.36%
>=9<10 Months	530	64,186,762	2,944,828	0.23%	0.27%
>=10<11 Months	493	63,038,807	3,221,917	0.22%	0.26%
>=11<12 Months	420	56,869,717	3,010,207	0.19%	0.24%
>=12	2,462	343,020,289	26,921,712	1.08%	1.44%
<b>Total</b>	<b>227,331</b>	<b>23,871,466,405</b>	<b>70,749,647</b>	<b>100.00%</b>	<b>100.00%</b>

The percentages in the above tables are calculated by reference to the total number of mortgage loans in the Trust of 194,301 (2010 227,331) and the principal balance of the Trust's mortgage assets of £20,066,233,560 (2010 £23,871,466,405) as at 31 December in each year

There were 1,045 properties in possession as at 31 December 2011 (31 December 2010 1,017 properties)  
Principal losses suffered in 2011 amounted to £99,801,535 (2010 £122,676,058)

Since 2010 it has been NRAM plc's general policy in their role as administrator that customers experiencing previous arrears within a twelve month period must make six consecutive full monthly payments before capitalisation can be offered. In addition, the number of instances of arrears capitalisation allowed during the lifetime of a loan will normally be limited to two. Finally, customers must agree to capitalisation rather than opt out of automatic capitalisation as was the case prior to 2010.

A mortgage is identified as being in arrears when, on any due date, the overdue amounts which were due on previous due dates equal, in the aggregate, one or more full monthly payments. In making an arrears determination, the administrator calculates as of the date of determination the difference between the sum of all monthly payments that were due and payable by a borrower on any due date up to that date of determination (less the aggregate amount of all authorised underpayments made by such borrower up to such date of determination) and the sum of all payments actually made by that borrower up to that date of determination. If the result arrived at by dividing that difference (if any) by the amount of the required monthly payment equals

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

or exceeds 1 the loan is deemed to be in arrears. Arrears classification is determined based on the number of full monthly payments that have been missed. A borrower that has missed payments that in the aggregate equal or exceed 2 monthly payments (but for which the aggregate of missed payments is less than 3 monthly payments) would be classified as being between 2-3 months in arrears, and so on.

Losses suffered in respect of the mortgage portfolio held by the Trust, reduce the share of cash available for distribution to Granite Finance Funding Limited. This in turn reduces the amount of cash that is available to pay interest and principal in respect of the loans between Granite Finance Funding Limited and the Granite Finance Funding issuers, which include the Company. A significant increase in losses could result in there being insufficient funds available to repay all interest and/or principal amounts due in respect of these loans. This could result in the Company being unable to pay all interest and/or principal amounts due in respect of the loan notes. However, the Company is only obliged to make payments in respect of the loan notes to the extent of the amounts received in respect of the loan to Granite Finance Funding Limited.

The loan note-holders are offered a degree of protection from default by credit enhancement provided by excess spread and reserve funds held by Granite Finance Funding Limited, which are available to absorb losses arising in respect of the mortgage portfolio.

### Currency risk

Currency risk arises as a result of the Company having liabilities that are denominated in currencies other than Sterling. In addition to issuing notes in Sterling, the Company has issued notes denominated in US Dollars and Euros. The Company's policy is to fully mitigate any exchange rate exposures by using cross currency swaps.

The table below shows foreign currency liabilities at Sterling carrying values and compares them to related cross currency swap notional amounts at Sterling carrying values at the balance sheet date. Similarly foreign currency liabilities in respect of collateral deposits pledged by swap counterparties are fully matched by foreign currency cash deposits held. The net currency exposure can be seen to be nil.

2011	US\$ £'000	€ £'000	Total £'000
<b>Assets</b>			
Cash deposits held in foreign currencies	-	44,329	44,329
Derivative financial instruments	62,946	178,657	241,603
<b>Total assets</b>	<b>62,946</b>	<b>222,986</b>	<b>285,932</b>
<b>Liabilities</b>			
Collateral pledged by swap counterparties	-	44,329	44,329
Debt securities in issue	62,946	178,657	241,603
<b>Total liabilities</b>	<b>62,946</b>	<b>222,986</b>	<b>285,932</b>
<b>Net position</b>	<b>-</b>	<b>-</b>	<b>-</b>

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

2010	US\$ £'000	€ £'000	Total £'000
<b>Assets</b>			
Cash deposits held in foreign currencies	-	54,485	54,485
Derivative financial instruments	86,647	219,730	306,377
<b>Total assets</b>	<b>86,647</b>	<b>274,215</b>	<b>360,862</b>
<b>Liabilities</b>			
Collateral pledged by swap counterparties	-	54,485	54,485
Debt securities in issue	86,647	219,730	306,377
<b>Total liabilities</b>	<b>86,647</b>	<b>274,215</b>	<b>360,862</b>
<b>Net position</b>	<b>-</b>	<b>-</b>	<b>-</b>

As the foreign currency exposures are fully matched by currency assets, the Directors believe it unnecessary to calculate any sensitivity analysis to movements in currency rates

### Liquidity risk

'Liquidity risk' arises from a mismatch in the cash flows generated from current and expected assets, liabilities and derivatives. Assets available to meet all of the liabilities as they fall due are cash and cash equivalents and the loan to group undertaking. The liquidity profile of the loan to group undertaking is designed to exactly replicate that of the debt securities in issue (on a post hedge basis where applicable).

Cash flows on the loan to group undertaking are dependent on the underlying mortgage loans. The actual lives of the mortgage loans within the Trust reflect the underlying lives of the mortgage loans which in general have a maximum term of 35 years, but the actual rate at which the mortgage loans are repaid may be in advance of the legal maturity date. Any principal receipts from Granite Finance Funding Limited's beneficial interest in the mortgage trust will be utilised by Granite Finance Funding Limited to repay the inter-company loan to the Company which in turn will be used to repay the debt securities in issue.

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

### Non derivative cash flows

The tables below analyse the Company's non derivative cash flows payable into relevant maturity groupings based on the remaining period at balance sheet date to expected maturity dates. The amounts disclosed are the expected undiscounted cash flows including future interest cash flows

2011	Within 3 months £'000	After 3 months but within 6 months £'000	After 6 months but within 1 year £'000	After 1 year but within 5 years £'000	After 5 years £'000	Total £'000
<b>Liabilities</b>						
Debt securities in issue	42,468	36,272	63,376	449,324	269,396	860,836
Trade and other payables	44,296	-	-	-	-	44,296
	<b>87,394</b>	<b>36,272</b>	<b>63,376</b>	<b>449,324</b>	<b>269,396</b>	<b>905,762</b>
2010	Within 3 months £'000	After 3 months but within 6 months £'000	After 6 months but within 1 year £'000	After 1 year but within 5 years £'000	After 5 years £'000	Total £'000
<b>Liabilities</b>						
Debt securities in issue	43,436	40,476	80,887	494,261	516,488	1,175,548
Trade and other payables	54,957	-	-	-	-	54,957
	<b>98,393</b>	<b>40,476</b>	<b>80,887</b>	<b>494,261</b>	<b>516,488</b>	<b>1,230,505</b>

### Derivative cash flows

No derivative cash flows are presented as at 31 December 2011 or 31 December 2010 because all of the Company's derivatives are assets and this disclosure is only applicable to liabilities



# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

### Fair values of non derivative financial assets and liabilities

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the Company's balance sheet at their fair value. Assets are presented at bid prices and offer prices are used for liabilities. Derivative financial instruments, which are already shown at fair value on the Company's balance sheet are included for completeness.

	Fair Value		Book Value	
	2011	2010	2011	2010
	£'000	£'000	£'000	£'000
<b>Financial assets</b>				
Cash and cash equivalents	44,331	54,488	44,331	54,488
Loan due from group undertaking	629,884	814,808	757,380	941,625
Trade and other receivables	685	553	685	553
<b>Total financial assets</b>	<b>674,900</b>	<b>869,849</b>	<b>802,396</b>	<b>996,666</b>
Derivative financial instruments	44,235	59,510	44,235	59,510
<b>Total assets</b>	<b>719,135</b>	<b>929,359</b>	<b>846,631</b>	<b>1,056,176</b>
<b>Financial liabilities</b>				
Debt securities in issue Class A	(494,949)	(669,709)	(515,571)	(712,495)
Debt securities in issue Class B	(63,353)	(63,987)	(78,213)	(78,958)
Debt securities in issue Class M	(43,791)	(47,636)	(60,822)	(61,400)
Debt securities in issue Class C	(72,025)	(92,985)	(144,051)	(145,440)
<b>Total debt securities in issue</b>	<b>(674,118)</b>	<b>(874,317)</b>	<b>(798,657)</b>	<b>(998,293)</b>
Trade and other payables	(44,926)	(54,957)	(44,926)	(54,957)
<b>Total financial liabilities</b>	<b>(719,044)</b>	<b>(929,274)</b>	<b>(843,583)</b>	<b>(1,053,250)</b>
<b>Total liabilities</b>	<b>(719,044)</b>	<b>(929,274)</b>	<b>(843,583)</b>	<b>(1,053,250)</b>

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

### Interest rate risk

'Interest rate risk' arises as a result of timing differences on the re-pricing of assets and liabilities, unexpected changes in the slope and shape of yield curves and changes in correlation of interest rates between different financial instruments (often referred to as basis risk). The interest receivable on the loan to Granite Finance Funding Limited (a NRAM plc group undertaking) re-prices on the same quarterly basis and on the same interest reference (3m GBP Libor) as the interest payable in respect of the loan notes (as adjusted by cross currency swaps), so that interest rate risk is eliminated. These provisions continue to apply following the failure to call the loan notes on their step up date in September 2011. As a result of this perfect offset, there is no sensitivity to movement in interest rates.

### Interest rate profile of financial assets and liabilities

2011	Floating rate £'000	Non interest bearing £'000	Total £'000
<b>Assets</b>			
Sterling	801,617	667	802,284
USD	-	-	-
Euros	44,329	18	44,347
	<b>845,946</b>	<b>685</b>	<b>846,631</b>
<b>Liabilities</b>			
Sterling	557,054	579	557,633
USD	62,946	-	62,946
Euros	222,986	18	223,004
	<b>842,986</b>	<b>597</b>	<b>843,583</b>

All floating rate assets and liabilities repriced on 20 March 2012

## Granite Mortgages 04-3 plc

### 15 Financial risk management (continued)

2010	Floating rate £'000	Non interest bearing £'000	Total £'000
<b>Assets</b>			
Sterling	1,001,138	532	1,001,670
USD	-	-	-
Euros	54,485	21	54,506
	<b>1,055,623</b>	<b>553</b>	<b>1,056,176</b>
<b>Liabilities</b>			
Sterling	691,916	451	692,367
USD	86,647	-	86,647
Euros	274,215	21	274,236
	<b>1,052,778</b>	<b>472</b>	<b>1,053,250</b>

#### Prepayment risk

'Prepayment risk' arises when it is possible that the assets may be realised earlier than it is possible to redeem the liabilities. Following the advent of the pass-through arrangements on 11 November 2008, this risk is fully mitigated because all available principal receipts are utilised to make repayments on the loan notes. There is no restriction on the amount which can be repaid on any given payment date as was the case when scheduled amortisation was applicable. The table on page 44 shows the impact on reported fair values should there be a hypothetical increase of 10% to customer prepayments.

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

### Fair value measurement

The following table summarises the fair value measurement basis used for assets and liabilities held on the balance sheet at fair value

2011	Level 1 £'000	Level 2 £'000	Level 3 £'000
<b>Financial assets</b>			
Derivative financial instruments	-	-	44,235
	-	-	44,235
<b>Financial liabilities</b>			
Derivative financial instruments	-	-	-
	-	-	-
<b>2010</b>	<b>Level 1 £'000</b>	<b>Level 2 £'000</b>	<b>Level 3 £'000</b>
<b>Financial assets</b>			
Derivative financial instruments	-	-	59,510
	-	-	59,510
<b>Financial liabilities</b>			
Derivative financial instruments	-	-	-
	-	-	-

Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2 Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as price) or indirectly (i.e. derived from prices)

Level 3 Inputs for the asset or liability that are not based on observable market data (unobservable inputs)

These definitions have been taken from the March 2009 amendment to IFRS7 'Improving Disclosures about Financial Instruments'

The movement in assets and liabilities measured using a valuation technique for which any significant input is not based on observable market data (Level 3) is as follows

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

2011	Financial assets £'000	Financial liabilities £'000	Total £'000
<b>Derivative financial instruments</b>			
At 1 January 2011	59,510	-	59,510
Total losses in profit and loss	(15,275)	-	(15,275)
Instruments changing classification			
Assets becoming liabilities	-	-	-
Liabilities becoming assets	-	-	-
<b>At 31 December 2011</b>	<b>44,235</b>	<b>-</b>	<b>44,235</b>

Total losses recognised in the income statement of £15,275,000 form part of interest payable and similar charges and unrealised fair value gains and losses and are a result of settlement gains of £10,125,000 and other fair value losses of £25,400,000

2010	Financial assets £'000	Financial liabilities £'000	Total £'000
<b>Derivative financial instruments</b>			
At 1 January 2010	72,217	-	72,217
Total losses in profit and loss	(12,707)	-	(12,707)
Instruments changing classification			
Assets becoming liabilities	-	-	-
Liabilities becoming assets	-	-	-
<b>At 31 December 2010</b>	<b>59,510</b>	<b>-</b>	<b>59,510</b>

Total losses recognised in the income statement of £12,707,000 form part of interest payable and similar charges and unrealised fair value gains and losses and are a result of settlement gains of £11,597,000 and other fair value losses of £24,304,000

# Granite Mortgages 04-3 plc

## 15 Financial risk management (continued)

### Sensitivity analysis of reasonably possible alternative assumptions for level 3 instruments

The main unobservable input that affects the valuation of the derivative financial instruments is the forecast level of customer prepayments in respect of mortgage loans assigned to the Trust. An increase in forecast prepayments will cause cross currency swaps associated with the notes in issue to pay down in an accelerated manner, so affecting their fair values. The following table shows the impact on reported fair values of a hypothetical 10% increase in customer prepayments.

2011	Reported fair value £'000	Revised fair value £'000	Favourable changes to Income Statement £'000	Unfavourable changes to Income Statement £'000
<b>Financial assets</b>				
Derivative financial instruments	44,235	44,151	-	(84)
	<b>44,235</b>	<b>44,151</b>	<b>-</b>	<b>(84)</b>
<b>Financial liabilities</b>				
Derivative financial instruments	-	-	-	-
	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

2010	Reported fair value £'000	Revised fair value £'000	Favourable changes to Income Statement £'000	Unfavourable changes to Income Statement £'000
<b>Financial assets</b>				
Derivative financial instruments	59,510	59,639	129	-
	<b>59,510</b>	<b>59,639</b>	<b>129</b>	<b>-</b>
<b>Financial liabilities</b>				
Derivative financial instruments	-	-	-	-
	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

# Granite Mortgages 04-3 plc

## 16 Related party transactions

A number of transactions are entered into with related parties as part of the Company's normal day to day business. These include a loan to Granite Finance Funding Limited (a NRAM plc group undertaking), a cash management fee payable to the Administrator and an administration fee payable to Law Debenture Corporate Services Limited. All of these transactions are governed by agreements that form part of the securitisation transaction documentation. The outstanding balances at the year end and related income and expense for the year are set out below.

	2011 £'000	2010 £'000
<b>Loan to Granite Finance Funding Limited</b>		
Loan outstanding at 1 January	941,625	1,136,700
Net amounts repaid	(184,245)	(195,075)
Loan outstanding at 31 December	757,380	941,625
Interest accrual at 31 December	447	330
Interest income earned	10,934	10,313

	2011 £'000	2010 £'000
<b>Cash management fee payable to NRAM plc</b>		
Fee accrual at 1 January	10	10
Amounts charged net of amounts paid	-	-
Fee accrual at 31 December	10	10
Expense	117	117

	2011 £'000	2010 £'000
<b>Administration fee payable to Law Debenture Corp. Servs. Ltd</b>		
Fee accrual at 1 January	-	-
Amounts charged net of amounts paid	-	-
Fee accrual at 31 December	-	-
Expense	8	8

## **Granite Mortgages 04-3 plc**

### **17 Collateral pledged and received**

Cash collateral is received as part of normal derivative operations and is recognised as an asset of the Company because the Company bears the risks and rewards associated with the investment of this cash with NRAM plc. At 31 December 2011 £44.3m (2010 £54.5m) had been received as cash collateral. In addition the Company held securities collateral with a value of £13.1m (2010 £19.8m). In the absence of counterparty default, the Company has no right to sell or repledge these securities and therefore in accordance with the provisions of IAS39 such securities are not recognised on the Company's balance sheet. No collateral is ever pledged.

### **18 Ultimate parent undertaking and controlling party**

The Company's ultimate parent is The Law Debenture Intermediary Corporation plc, a company registered in England and Wales, the shares being held under a trust arrangement. Copies of the financial statements of The Law Debenture Intermediary Corporation plc may be obtained from Law Debenture Intermediary Corporation plc, Fifth Floor, 100 Wood Street, London, EC2V 7EX.

The Company's results are included within the consolidated financial statements of Granite Finance Holdings Limited, NRAM plc and UKAR Limited. Copies of the financial statements of NRAM plc may be obtained from the NRAM plc website, [www.n-ram.co.uk](http://www.n-ram.co.uk). All shares in NRAM plc were transferred to the Treasury Solicitor as nominee for HM Treasury on 22 February 2008 as a result of The Northern Rock Transfer Order 2008. On 1 October 2010 all shares in NRAM plc were acquired via a share-for-share exchange by UKAR Ltd, a private limited company incorporated in the United Kingdom under the Companies Act 2006 and registered in England and Wales, which is wholly owned by the Treasury Solicitor as nominee for HM Treasury. As such, the Company considers that Her Majesty's Government remains its ultimate controlling party.

### **19 Post balance sheet events**

On the 20 January 2012 Standard & Poors rating agency updated the criteria they use for assessing counterparty risk. This resulted in the Class A notes being downgraded from A+ to A, the Class B notes from A+ to A, the Class M notes from A+ to A and the Class C notes being upgraded from A- to A.