the West Brom

Annual Report and Accounts

Year Ended 31 March 2013

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Contents

Key highlights from the 2012/13 financial year include:

- An increase in the Group's Core Tier 1 capital ratio from 13.3% to 14.1%, remaining one of the highest among UK banks and building societies.
- A strong focus on effective liquidity management with robust levels of high quality liquid assets held throughout the period.
- Retail savings inflows of £1.7bn, attracting some 26,400 new savers, with residential mortgages covered 1.16 times by retail deposits.
- Net interest margin improving to 0.49% (2011/12: 0.47%).
- Pre-tax losses reducing for the fourth consecutive year to £9.4m (2011/12: £9.5m), despite challenging economic conditions.

"A further reduction in losses has again confirmed the validity of our Back to Basics strategy and its focus on the core building society activities of retail savings, investments and prime residential mortgages."

Chairman's Statement

Mark Nicholls

During a period where the UK economy has again experienced considerable uncertainty, it says a great deal about the success of the Society's Back to Basics strategy that the West Brom has, over the past year, recorded a resilient performance.

Back to Basics – an effective strategy

Savers are suffering due to the combination of an historically low Bank Rate and relatively high inflation, which is why the Society has been conscious of the importance of offering customers a genuinely competitive choice of products. In relation to borrowers, the West Brom has actively sought to help people hoping to buy their own home by offering competitively priced mortgages.

This focus on the needs of savers and borrowers is an integral part of a building society's priorities, as embodied in the Society's Back to Basics strategy. In line with this strategy, the Society has remained steadfast in its aim of exiting non-core business, particularly commercial lending. Given that the commercial property market is especially vulnerable to the challenging economic environment, this withdrawal will take time and will continue to impact on financial performance. Despite these challenges, I am pleased to report a reduction in the pre-tax loss for the fourth year in a row since the new management team came together.

Regulation – stronger oversight

Customers should have complete trust in the integrity of financial services providers. In that sense, the West Brom welcomes the regulatory changes recently introduced to make scrutiny and oversight even more embedded within the industry.

The Financial Services Authority (FSA) has now been succeeded by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA). The separate oversight of prudential matters (the financial strength of a firm) and retail conduct (how customers are dealt with) should ensure that consumers can have greater confidence that the organisations they deal with are both financially sound and customer focused.

The Society has already developed constructive working relationships with both of these regulatory bodies and is committed to working with them in the coming years. However, members should be aware that this higher level of scrutiny comes at a price. In the next financial year, we estimate that the Society will be required to pay some £1m to the key regulatory bodies – Prudential Regulation Authority (PRA), Financial Conduct Authority (FCA) and Financial Ombudsman Service (FOS) – as well as the cost of the Financial Services Compensation Scheme (FSCS).

Looking to the future – grounds for optimism

Predicting the timing of any significant upturn in the UK economy is fraught with difficulty. Forecasts for substantial growth are hesitant at best. This suggests Bank Rate is set to stay at historically low levels, maintaining the pressure on our interest margins.

Despite this economic backdrop, the West Brom has much to be satisfied with, as demonstrated by our continued trend of improved financial performance. Looking after the financial interests of members by providing prime residential mortgages, savings and investments remains our top priority as a traditional independent building society. Moreover, our strong capital and liquidity positions offer further assurance to members that the Society can be relied upon as a secure place for their money.

I conclude by acknowledging the skill, effort and commitment shown by our staff and strong Executive team in serving our members and communities. I also thank the Society's members for their consistent loyalty and support.

Mark Nicholls
Chairman
31 May 2013

Chief Executive's Review


Jonathan Westhoff

Over the last year we have been repeatedly reminded of how difficult and volatile the economic recovery is going to be. While a return to recession was narrowly averted, we have nonetheless witnessed downgrades to the UK credit rating, a series of high profile corporate failures and the need for further stimulus measures from the coalition government. Although these measures have included actions targeted to improve conditions in the housing market, we have not yet seen any signs of a sustained improvement.

Despite these challenging conditions, the West Brom produced another very satisfactory performance, confirming once again the validity of the Society's Back to Basics strategy and its focus on the core building society activities of retail savings, investments and prime residential mortgages.

An overview of performance

Since implementing this strategy in 2009, the Society has reported four consecutive years of improved financial performance, with the pre-tax loss for 2012/13 reducing to £9.4m. This has been achieved despite the continuing pressure on interest margins, resulting from Bank Rate remaining at 0.5%, and a further deterioration in the commercial property market.

The increase in net interest margin (including net realised profits and fair value losses), from 0.50% to 0.58%, was attributable to a combination of the Society's successful return to the securitisation market, the realisation of gains in financial instruments held in the Society's liquidity portfolio, and an easing of funding costs in the second half of the year as the introduction of the Funding for Lending Scheme (FLS) contributed to a general softening of interest rates.

During the year, a further £10.8m (2011/12: £10.5m) was set aside for potential credit losses, primarily in respect of the commercial lending book, which reduced in size by a further 11%. Since exiting the market for this higher risk lending, the amount of loans outstanding has been reduced by circa £600m, a 35% fall. The success of this de-risking programme is reflected in the improvement in the Core Tier 1 capital ratio (a fundamental measure of financial strength) which increased from 13.3% in 2011/12 to 14.1%. This ratio has now more than doubled since the implementation of the Back to Basics strategy, giving the West Brom one of the highest Core Tier 1 ratios in the UK banking and building society sector.

The Society continues to maintain a robust and balanced funding base. The majority of our funding remains retail savings balances, but this is supported by complementary wholesale funding programmes. In the course of the year, the Society attracted gross retail inflows of £1.7bn and raised £250m of wholesale funds via a residential mortgage backed securitisation transaction, the Society's first such transaction since 2005. This positive demonstration of increased market confidence in the Society has continued after the year end with the successful completion of a second securitisation transaction, raising a further £380m of funds.

Commitment to members

All of the West Brom's activities are guided by the defining principle of a traditional building society: looking after the financial interests of members by offering savings, investments and prime residential mortgages geared to their specific needs.

Savings – choice and convenience

Being at an all-time low of 0.5% for the fourth consecutive year, Bank Rate has had an unavoidable and marked impact on savers. Throughout this period, the West Brom has featured regularly in the Best Buy tables, offering savers a choice of products tailored to their particular needs. These were provided through a variety of channels to suit the convenience of the customer – branch, telephone or post, or online with more and more customers finding the internet a preferred and flexible way to manage their savings affairs.

The Society was able to offer several market-leading products for online savers with new issues of its WeBSave Easy Access and WeBSave ISA accounts. We also had a Best Buy Branch Easy Access Account and continued to encourage the value of regular saving through our Fixed Rate Regular Saver Accounts.

During the second half of the year, savers have felt the impact of the Funding for Lending Scheme (FLS), which was introduced by the Government to stimulate the housing and mortgage markets. Access to this lower cost source of funding reduced the demand for retail savings, resulting in a material reduction in rates paid to savers.

Borrowers – increasing opportunities

In the last year, we made substantial progress in positioning ourselves to support the aspirations of people wishing to buy their own home as the building society sector again asserted itself in the lending market.

After implementing a new and efficient automated processing system, the West Brom bolstered its support for borrowers with a range of mortgage deals and improved customer service. Having the right systems and processes in place is essential to the Society's commitment to borrowers, but success in the mortgage market also entails having the right products.

The Society has actively supported borrowers at a time of widespread financial constraint for many people. Throughout the year, the Society launched a range of new products to ensure our best terms were available to both new and existing customers. Allied to this, we also offered borrowers a set of product options, including a series of fixed rate mortgages and related incentives, to make mortgages more affordable and accessible.

For many of our borrowers, the low interest rate environment eases affordability by reducing dramatically the level of repayments. As a result, the level of arrears in our core residential mortgage book remains low at 1.74%. Where customers face genuine financial problems, the Society works with them, wherever possible, to come to an acceptable and affordable arrangement that will enable them to remain in their homes.

Managing costs efficiently

The responsible and efficient use of member funds drives the need to keep the Society's costs under constant review. During the past year, we have taken steps to improve our operational systems and processes as part of the Society's growth aspirations. These improvements are integral to the future aims of the West Brom. Providing efficient and excellent service and facilities for customers lies at the heart of this ambition.

Strategic investments, notably the modernisation of the whole of the branch network and a new automated lending system, have meant an increase in management costs of 4.4%. This investment is essential in enabling the Society to build a stable and solid platform for growth.

The financial services industry has experienced a substantial increase in the number of complaints arising from Payment Protection Insurance (PPI). The requirements of the Financial Conduct Authority (FCA) dispute resolution rules and the process determined by the Financial Ombudsman Service (FOS) mean that the Society must respond to and investigate every claim. The costs relating to the investigation of these claims increased markedly during the year, to over £100,000. Yet as the vast majority of claims are unfounded, no material amounts have been awarded to customers. However, if the trend continues, the cost of handling these speculative claims, which are frequently raised via claims management companies, could escalate to over £500,000 per year.

A constant focus on customer satisfaction

We want customers to feel the West Brom lives up to its commitment of providing a service that is friendly, professional and attuned to their particular circumstances. This focus on customer service is always at the forefront of our thinking but, in the end, the arbiters of how well we are doing are, of course, our customers.

In gauging how our customers perceive the West Brom, the Customer Experience Tracker survey is a valuable source of feedback. Undertaken by an independent research consultancy, the survey involves interviewing a wide cross-section of customers and inviting them to rate the West Brom against a variety of measures. It was, therefore, extremely encouraging to see from the survey that around 9 out of 10 of our customers would recommend the West Brom. What makes this finding even more heartening is that the levels of customer satisfaction compared very favourably with those of our competitors. Significantly, the survey highlighted the fact that this quality of service was consistent across all of the Society's operational channels, whether through branches, direct, or online.

Whilst we can take considerable heart from the survey its main value lies in telling us how we might make things even better for customers. In that sense, we have acted on suggestions from customers in recent surveys, such as enhancing our online facilities and increasing the number of transactions processed right first time.

Valuing the views of members

Mutuality means an organisation owned and run for the benefit of its members, which is why we use a variety of methods for finding out their views and opinions. The previously mentioned Customer Experience Tracker survey is one example of this, but members also have opportunities to engage with the Society in a very direct sense, showing how mutuality is also about accountability. This is particularly seen in the Society's Annual General Meeting (AGM) where members can not only voice their views and ask questions on key issues, but are also entitled to vote on the election of the West Brom's Board of Directors.

We also have our Members' ViewPoint which provides a format whereby members are able to discuss issues directly with the Chief Executive and other senior executives at the Society, helping us to gain a detailed impression of what members think and feel about the West Brom.

Most of all, the insights of members can go towards improving how we do things at the West Brom. In the past year, Members' ViewPoints have been held in Birmingham and Stourbridge and suggestions made at these events have since been incorporated into our service and product improvements.

Making the community count

The West Brom is proud of its position as the largest building society in the Black Country and Birmingham region, but this sense of pride also comes from the Society's support for people facing difficulty and disadvantage within the local community. In particular, it has been immensely moving to see the generosity and compassion our staff showed towards the Society's chosen charity for the last year, Acorns Children's Hospice. Staff have organised numerous fundraising ventures for the charity while some 150 of our people have also devoted time to voluntary work for Acorns as part of our corporate volunteering policy.

This spirit of community commitment is also illustrated by the Society's Community Counts campaign, which channels support through our branches to grassroots projects which do so much in responding to real human need. Last year, that encompassed health, dementia, disabled children, people with learning difficulties, terminal illness, bereavement, and domestic violence.

Community Counts is underpinned by the West Brom's longstanding affinity partnership with the Diocese of Lichfield via our Community Account. Through the fund-giving function of the Mercian Community Trust, the Society was again able to assist agencies engaged in helping people in hardship and difficulty.

A number of other affinity relationships enable the West Brom to lend its backing to organisations concerned with health, social and sporting provision, including widening opportunities for children and young people. Pride of place is the affinity arrangement – the Red Balloon Account – we have with Birmingham Children's Hospital. This has been a tremendous success since its launch in 2007, with over £470,000 so far given to the Hospital, which is renowned internationally, as well as regionally, for the care and treatment it gives to children and young people.

A confident outlook for the Society

As many commentators have found over the past few years, it would be a mistake to make any bold predictions about the general economic outlook. The most we can say is that it is likely to remain unpredictable and the UK's recovery might take some time. What is more certain is that this will have an unavoidable impact upon the financial services sector and its customers, especially if Bank Rate languishes at its current all-time low point, which is widely anticipated to be the case. However, the improvement we have seen in the net interest margin is expected to continue into the next financial year.

The progress we have made under our Back to Basics strategy indicates that the West Brom has real grounds for confidence as a business that is actively investing for the future. Completing the modernisation of the whole of our branch network, including the relocation of several branches to more favourable high street sites, is proof of this forward-looking approach. Similarly, progress in the mortgage market represents a crucial step for the West Brom as a building society that looks after the needs of members.

Likewise with our new Head Office development, which is very much a symbol of a building society that sees a positive future for itself. We are now at the stage where plans and designs are gathering pace with actual construction set to start towards the end of the year, giving our staff a working environment that is modern, efficient and befitting our position as the largest building society in the region.

I would like to praise the dedication and hard work of our people and thank them for consistently striving to do their best for both our customers and the communities we serve. It is through this that we can continue to earn the trust and loyalty of the people who matter most at the West Brom – our members.

Jonathan Westhoff
Chief Executive
31 May 2013

Board of Directors

John Ainley LLB (Hons), CCIPD
Non-Executive Director Age 56

John was appointed to the Board in May 2011. He was formerly Group Human Resources and Corporate Social Responsibility Director with global insurance provider, Aviva plc. Prior to that, John was Group Human Resources Director with WH Smith plc. He has served as a Director of the European Centre for Executive Development at INSEAD and as a member of the CBI's Climate Change Board. He is a Trustee of the Bloomsbury Festival. John chairs the Remuneration Committee and is a member of the Nominations Committee.

Mark Gibbard BSc, FCA, MCT
Group Finance Director Age 51

Mark was appointed to the Board in February 2011 as Group Finance Director. He has worked in the financial services sector for more than 25 years, including some seven years as Finance Director on the Board of Cheltenham & Gloucester plc. Prior to joining the West Brom, he was Divisional Director Risk Management at Nationwide Building Society. Mark chairs the Society's Assets & Liabilities Committee and is a member of the Group Risk Committee.

Claire Hafner MA, ACA
Non-Executive Director Age 53

Claire was appointed to the Board in September 2011. She is currently Chief Financial Officer for VocaLink, a specialist provider of transaction services to banks, their corporate customers and to the public sector. Prior to that, Claire was Finance Director for the international law firm, Eversheds, where she headed a team of finance professionals across the UK and overseas. Claire is a member of the Audit and Remuneration Committees.

Andrew Jones BSc (Hons), FCIB, FCIS
Group Risk Director Age 56

Andrew was appointed to the Board as Group Risk Director in November 2010, having joined the Society in March 2009. With over 30 years' experience in the sector, latterly in risk and compliance, Andrew worked at Portman Building Society as Group Secretary and, more recently, as Group Risk Director at HML, the UK's largest third party mortgage administrator. Andrew is a member of the Group Risk and Assets & Liabilities Committees.

Mark Nicholls MA (Cantab), MBA
Chairman Age 64

Mark was appointed to the Board in January 2010 and has considerable knowledge of financial services, including at SG Warburg Group Plc and as Managing Director of the private equity group of the Royal Bank of Scotland. Mark also held non-executive directorships at Portman and Nationwide building societies. He is currently Chairman of Rathbone Brothers Plc and Protector of the National Lottery Fair Share Fund. Mark chairs the Nominations Committee and is a member of the Remuneration Committee.

Mark Preston BA (Hons), ACIB
Non-Executive Director Age 53

Mark was appointed to the Board in May 2011. He is a Principal of the financial advisory firm Valere Capital, which advises institutions on complex financial risks. Mark has been involved in financial markets for nearly 30 years, including the roles of Chief Executive Officer for the Products and Markets Division of Lloyds TSB and Co-Head of the Bank's Corporate Markets. He chairs the Development Council of Opportunity International UK, a charity active in microfinance activities in Africa. Mark is a member of the Group Risk Committee.

Martin Ritchley FCA, FCIB, Hon DBA (Coventry)
Deputy Chairman and Senior Independent Director Age 66

Martin was appointed to the Board in September 2009. He was formerly Chief Executive of Coventry Building Society and Chairman of the Building Societies Association. He is currently a Trustee of the ARC Addington Fund, a charity concerned with the sustainability of the farming community. Martin is a member of the Audit, Remuneration, Nominations and Group Risk Committees.

Richard Sommers MA (Oxon), ACIB
Non-Executive Director Age 56

Richard was appointed to the Board in October 2009. Currently Treasurer of Lady Margaret Hall, a college in the University of Oxford, Richard has in-depth experience of retail and commercial banking, having held senior positions with the Barclays Group, particularly as Chief Financial Officer with Barclaycard and Risk Director of Retail Financial Services. Richard chairs the Group Risk Committee and is a member of the Audit and Nominations Committees.

Colin Walklin BSc, FCA
Non-Executive Director Age 59

Colin was appointed to the Board in July 2011. He is presently Chief Operating Officer and Finance Director for Standard Life Investments with responsibility for operations, technology, change management and all aspects of the financial management of the business. A qualified chartered accountant by profession, he is a member of the Financial Reporting Review Panel. Colin chairs the Audit Committee and is a member of the Group Risk Committee.

Jonathan Westhoff BA (Hons) Financial Services, FCMA, CGMA, ACIB
Chief Executive Age 48

Jonathan was appointed to the Board in May 2009 and was Group Finance Director and Deputy Chief Executive before his appointment as Chief Executive in May 2011. He has 30 years' experience in the financial services sector, including some 17 years with Barclays Bank, before moving into the mutual sector in 2000. Prior to joining the West Brom, he served as Finance Director at Portman and Newcastle building societies. Jonathan is a member of the Society's Group Risk and Assets & Liabilities Committees.

Financial Review

Throughout the most challenging economic environment for decades, the Board's principal focus has been to safeguard member assets while providing outstanding products and service to its members. And in this primary aim, the West Brom has continued to make solid progress.

The Society reduced losses for the fourth consecutive year while continuing to manage down its legacy activities and maintain its emphasis on the core building society activities of retail savings, investments and prime residential lending. The Board is very satisfied with the progress in delivering a sound base from which to develop its strategic focus on growth.

The Society has consolidated its position and been able to deliver strong results over the year in the following key areas:

Increasing net interest margin – Net interest margin (including net realised profits and losses from financial instruments) increased to 0.58% (2011/12: 0.50%) with a modest rise in core net interest margin at 0.49% (2011/12: 0.47%), reflecting the extended low interest rate environment;

De-risking the balance sheet – Risk weighted assets down 8% to £2.8bn strengthening the Group's Core Tier 1 ratio, which further increased to 14.1% (2011/12: 13.3%);

Managing risk – Loan impairment provisions of £94.3m, increasing coverage of the total loan book to 1.9% compared with 1.8% in 2011/12; and

Effective liquidity management – Controlled reduction of excess liquidity while maintaining its quality throughout the period; focus on effective liquidity management and no exposure to non-UK sovereign debt.

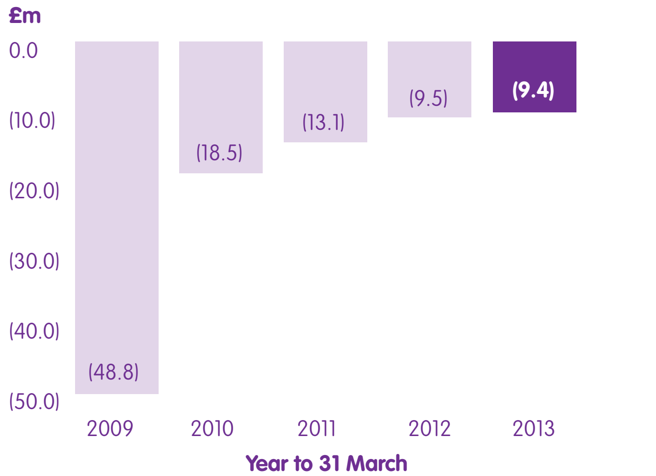
Performance overview

Key Performance Indicator: *The statutory results before tax are the most commonly used measure of profitability. The Board assesses the Society's performance using the results before tax at both a total Group and individual business division level as this presents a more transparent view of the performance of the core and non-core elements of the Society.*

Year to 31 March Group results

	2013 £m	2012 £m
Net interest receivable	**33.7**	34.9
Other income and charges	**9.9**	10.5
Fair value losses on financial instruments	**(1.7)**	(3.0)
Net realised profits	**7.3**	5.2
Administrative expenses	**(44.9)**	(43.0)
Operating profit before impairments, provisions and revaluation losses	**4.3**	4.6
Losses on investment properties	**(0.2)**	(1.0)
Impairment losses on loans and advances	**(10.8)**	(10.5)
Provisions for liabilities – FSCS Levy	**(2.7)**	(2.9)
Provisions for liabilities – other	**-**	0.3
Loss before tax	**(9.4)**	(9.5)
Taxation	**4.4**	0.3
Loss for the financial year	**(5.0)**	(9.2)

Profit before tax on continuing operations



Total Group pre-tax loss for the year reduced for the fourth consecutive year to £9.4m (2011/12: £9.5m). This year's results reflect the pressure on margin arising from the continued low Bank Rate, combined with the impact of further deterioration in the commercial real estate (CRE) market.

Overview by business division

The Group is organised into three main business divisions:

- Retail – consisting of residential lending, savings, investments and protection;
- Commercial – primarily loans for commercial property investment; and
- Property – a portfolio of residential properties held to generate rental income.

Year to 31 March

	2013 £m	2012 £m
Retail	**4.1**	4.3
Commercial	**(14.3)**	(13.6)
Property	**0.5**	(0.4)
Intercompany adjustments	**0.3**	0.2
Total Group loss before tax	**(9.4)**	(9.5)

Retail

The Retail division's main activity is residential lending primarily funded by retail savings. Results for the year are indicative of a UK economy that is struggling to return to growth, together with challenging economic conditions in the Eurozone. Interest income has remained depressed due to the Society's high concentration of legacy mortgage assets linked to the low Bank Rate. Relatively high retail funding costs, as a result of intense competition, and a stagnant housing market contributed to the difficult operating environment. Notwithstanding these factors, the division has achieved a satisfactory performance for the year.

The strength of the asset base has continued to improve, with loan balances reducing by 6.5% to £4.0bn. The decrease in the level of higher risk loans has supported the Society's strategic goal of rebalancing its activities to those of a leading regional building society.

A conservative approach to residential credit management has been consistently employed throughout the period. Despite the contracting mortgage book and a rigorous approach to assessing the borrower's ability to service a forbearance arrangement, just 1.92% of accounts were in arrears by three months or more at the end of the year.

The Society has successfully completed the redevelopment of its lending systems and processes, facilitating a firm presence in the residential mortgage market. This has enabled the Society to launch a competitive range of products aimed at supporting members in their aspirations for home ownership.

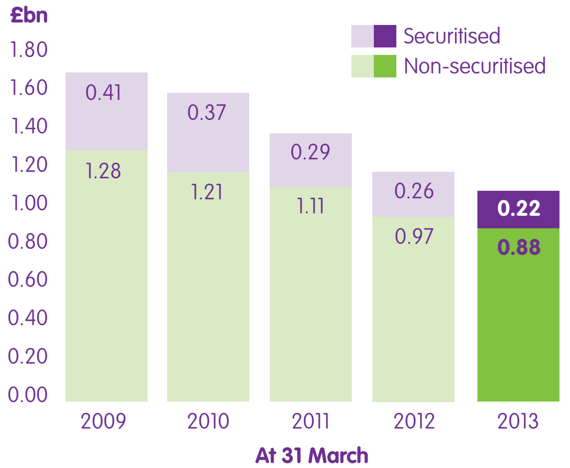
Fee and commission income has been maintained at a similar level to the prior year. A more resilient property market and increasing investment advice activity have again offset reductions in insurance business arising from a contracting loan book.

Commercial

While the UK economy is yet to demonstrate any sustained period of growth, the commercial property market has suffered a difficult year, as evidenced by numerous high street business failures and further decreases in commercial property valuations.

A key measure of the success of our current strategy is the reduction achieved in the Society's exposure to the commercial lending sector over the last four years. Since 2008/9, when we announced our plan to exit this market, the level of exposure has reduced significantly, from £1.7bn to £1.1bn, of which £216.6m (2011/12: £262.8m) is securitised.

Commercial lending balances



Against a backdrop of a prolonged economic downturn, our prudent credit risk management policy and balance sheet conservatism have resulted in an impairment charge against commercial loans of £6.7m (2011/12: £6.2m). This contributed to the loss of the division, which increased slightly from 2011/12.

Property

The Property division (West Bromwich Homes Limited) contributes to the results of the Group in two separate ways: trading profit from the rental of residential properties and changes in the fair value of these properties.

The underlying trading profit increased to £0.7m (2011/12: £0.6m) reflecting a positive property rental market and efficiency improvements in the management of the portfolio.

Although the housing market has shown some signs of modest recovery and increased activity, this is yet to result in an increase in property values. The value of the West Bromwich Homes Limited property portfolio reduced slightly to £112.5m (2011/12: £112.7m).

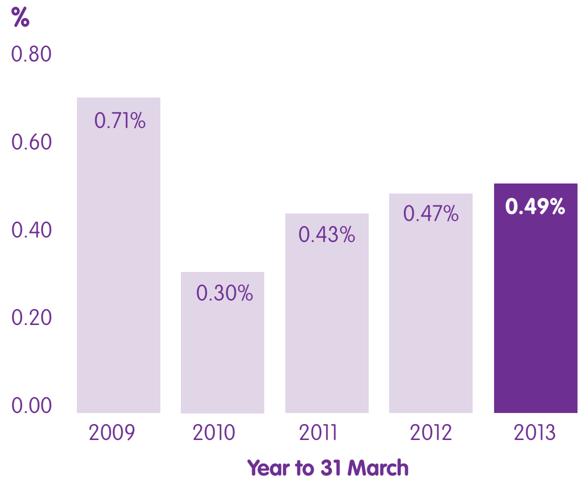
Financial performance – Group

Net interest margin

Key Performance Indicator: *The net interest margin is calculated as net interest income as a percentage of mean total assets.*

The key drivers of this measure are the level of return received from the assets held by the Group and the interest paid on its borrowings. As the primary constituents of this measure are member related, being mortgages to borrowers and savings from retail customers, the Board's goal is not to maximise this ratio but to maintain a measured level that balances continued security with long-term value for the members.

Net interest margin (core)



During 2012/13 the net interest margin increased to 0.49% (2011/12: 0.47%) with the principal drivers being:

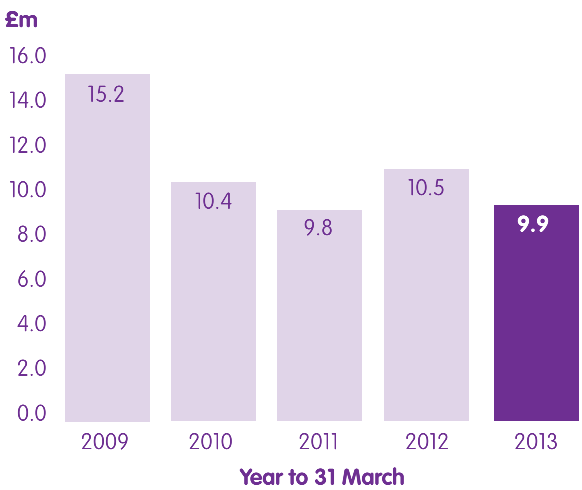
- An increased proportion of our residential mortgage borrowers benefiting from the low Bank Rate, with an average interest rate charged on loans in the financial year of 2.54% (2011/12: 2.75%), as many of our loans matured from initial fixed rates;
- Maintaining a focus on de-risking the balance sheet through the managed run-off of non-core mortgage assets, irrespective of their contribution to net interest margin. This meant that in the year the margin on these non-core assets fell from 2.30% to 2.27%;
- Robust liquidity management, meaning holding sufficient levels of high quality liquid assets (such as gilts, government guaranteed securities and treasury bills) balanced with the need to optimise returns; and
- An easing of funding costs in the second half of the year as the introduction of the Funding for Lending Scheme (FLS) contributed to a general softening of interest rates.

Going forwards, the low returns on high quality liquid assets and the significant proportion of mortgage assets linked to Bank Rate mean that the net interest margin will remain under pressure until Bank Rate increases.

Other income

Key Performance Indicator: *Other income primarily represents income earned from the sale of non-margin related products. These include commission on the sale of insurance (in particular home and contents) and investment related products, together with fees earned on lending and property rental activity.*

Other income



Other income was £9.9m compared with £10.5m in 2011/12. Higher investment advisory fees and net returns from the rental property business (West Bromwich Homes Limited) were not quite sufficient to offset lower arrears mortgage management income, as a result of a contracting mortgage book.

The Society continues to deliver value to members by offering investment, insurance and protection products which match their needs. Given the market context of low mortgage volumes and a rapidly changing regulatory environment, the Board considers this performance to be satisfactory.

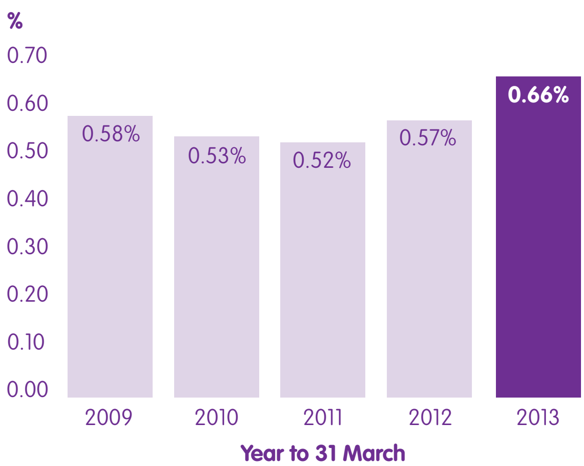
Management expenses

Key Performance Indicator: *The management expenses ratio is a measure of cost efficiency, reflecting costs as a proportion of total assets managed. It is calculated as total management expenses (including depreciation and amortisation) as a percentage of mean total assets.*

The Board reviews this measure at both the statutory and underlying level. The underlying management expenses ratio is calculated by stripping out all costs that are considered to be one-off and not reflective of the ongoing costs of the Group.

The key drivers in this ratio are the underlying costs of the Group and its asset base.

Management expenses ratio



Since 2009, the Society has invested in its future through strategic projects, including an extensive branch modernisation programme and a more efficient lending system. This has prepared the Society as it shifts towards a period of expected growth. This has resulted in an increase in the depreciation charge of £0.9m which accounted for a high proportion of the increase in expenses year on year.

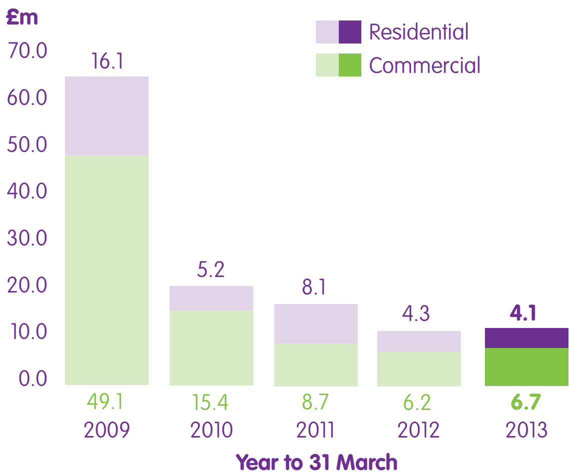
This essential investment in the future, combined with a contracted asset base, has meant that the Society will be running with an elevated management expenses ratio for a period of time. This has been the prime cause of the higher management expense ratio of 0.66% (2011/12: 0.57%); the reduction in the balance sheet size was responsible for two thirds of this increase.

Impairment provisions on loans and advances

Key Performance Indicator: *The Board monitors the level of impairment provisions in absolute terms. The indicator measures the credit risk performance of the assets (i.e. the lower the credit performance of the assets, the higher the losses). Provisions include the losses incurred or those losses expected to be incurred (based upon events that have already happened) and are calculated both individually and collectively on groups of assets with the same credit characteristics.*

The key drivers of the quantum of losses incurred include unemployment, interest rates, movements in property prices, tenant defaults on commercial property and the availability of funding in the market.

Charge for impairment losses on loans and advances



The Board continues to take a prudent view when determining the appropriate level of provisions. The total charge for impairment losses on loans and advances was slightly up on the prior year, to £10.8m (2011/12: £10.5m).

The charge for new residential provisions has reduced for the second consecutive year to £4.1m (2011/12: £4.3m) reflecting the strong underlying quality of our residential lending in both prime residential and buy-to-let exposures.

The recovery of the UK economy has stuttered, with reduced output from the key business sectors, further failures of high street retailers and continued uncertainty in the global markets. The impact of this has been most visible in the Commercial Real Estate market, where the downward trend in property values, caused by falls in rental returns and increased voids, has continued in some sectors.

Impairment charges against commercial loans have been raised to £6.7m (2011/12: £6.2m) to ensure an appropriate level of coverage against these non-core assets is maintained. At the end of the period, the Group had £62.8m (2011/12: £67.4m) set aside for potential losses from exposures to the commercial lending portfolio, equivalent to 5.7% of the current loan book (2011/12: 5.5%). The Board remains resolute in its aim of reducing the level of non-core assets and, alongside this aim, it continues to make appropriate provisions where emerging difficulties are identified.

A key strategy in mitigating the losses incurred on commercial loans is identifying circumstances where the Society taking control of the underlying security will result in a better outcome in terms of recovery. This means that at the end of the year £338.3m (2011/12: £288.1m) of the commercial loan book was managed through a Law of Property Act Receiver (LPAR).

Underlying results

Key Performance Indicator: *The statutory and underlying results before tax are used together to monitor the performance of the Group. The statutory results before tax are the most commonly used measure of profitability. However, this includes a number of items that are not considered to reflect the ongoing profitability of the Group. These items are excluded from underlying results to present a core ongoing performance measure.*

Year to 31 March

	2013 £m	2012 £m
Reported Group loss before tax	**(9.4)**	(9.5)
Net fair value movements	**1.7**	3.0
Gains from sale of financial instruments	**(7.3)**	(5.2)
FSCS levy charge	**2.7**	2.9
Restructuring costs	**1.0**	0.6
Underlying loss before tax on continuing operations	**(11.3)**	(8.2)

The underlying performance primarily reflects the impact of the persistently low Bank Rate environment and the additional provisions set aside to protect against further deterioration of the commercial loan portfolio.

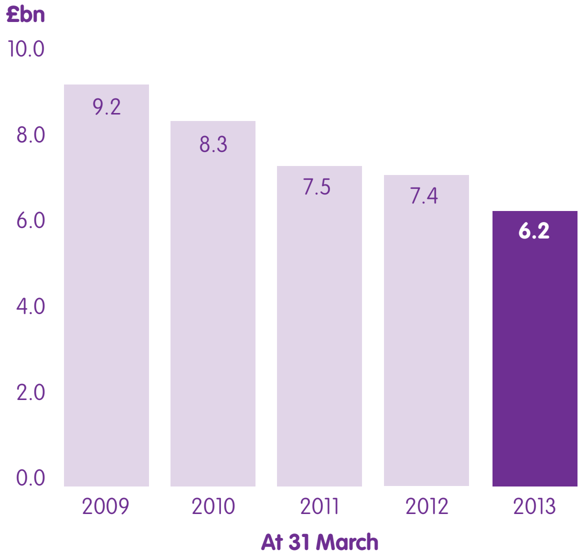
The major elements, which are not considered reflective of the Group's underlying performance, are explained below:

- Net fair value movements. These reflect the impact of changes in the fair value of derivative financial instruments and the effect of Group hedge accounting decisions;
- Gains from sale of financial instruments. These gains arose through the ongoing management of the treasury portfolio and the requirement to prove the liquidity of the Group's liquid assets;
- Financial Services Compensation Scheme (FSCS) levy charge. This relates to the provision for the Society's share of the management costs for the scheme year 2013/14, combined with the additional requirement for participants to contribute to capital shortfalls on the outstanding debt; and
- Restructuring costs. These costs reflect the one-off costs incurred on key strategic initiatives, primarily the accelerated write-off of the current head office and onerous lease provisions.

Financial position

The Board has remained committed to eliminating the legacy risks inherent in the balance sheet, further strengthening the Group's capital position and providing a safe home for members' deposits. In delivering against these objectives, the West Brom is now a more focused Society, with total assets reducing 16.4% to £6.2bn.

Group total assets



Loans and advances to customers

Loans to customers principally comprise residential lending through the Society, West Bromwich Mortgage Company Limited and White Label Lending Limited and, in the case of commercial property lending, through West Bromwich Commercial Limited.

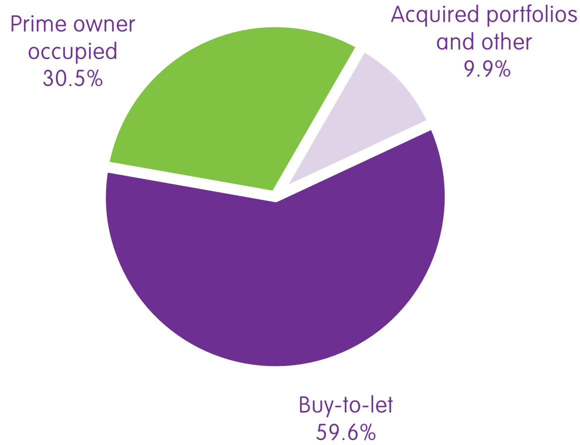
The Society has continued with its controlled reduction of legacy assets, thereby increasing its focus on prime residential lending.

Residential

Residential mortgages represent prime advances, including buy-to-let, made through the Society's branches and intermediary channels. Also included are mortgage portfolios acquired through the Society's subsidiary company, West Bromwich Mortgage Company Limited, although no such portfolios have been acquired since 2005.

At the end of the period, the residential mortgage portfolio was divided 30.5% prime owner occupied, 59.6% buy-to-let and only 9.9% acquired portfolios and other.

Analysis by lending type at 31 March 2013



The table below shows that the Group has a relatively diverse geographic spread of residential loans with no individual region exceeding 20% of the total residential lending book.

At 31 March Residential loans analysis by region

	2013 £m	2012 £m
East Anglia	**95.4**	101.0
East Midlands	**341.3**	363.1
Greater London	**675.9**	719.2
Northern Ireland	**7.0**	7.5
North	**116.4**	123.9
North West	**403.0**	426.2
Scotland	**161.3**	169.1
South East	**691.2**	736.7
South West	**304.2**	326.4
Wales	**201.4**	216.8
West Midlands	**720.1**	787.9
Yorkshire	**242.1**	255.9
Total	**3,959.3**	4,233.7

Key Performance Indicator: *The Board reviews the credit performance of the Group's loans and receivables using a variety of measures that report on different characteristics and behaviours of both the loan and the customer. This is to ensure that all indicators of potential problems are identified as early as possible.*

The principal industry standard and Board measure is the number of cases where the borrower has missed more than three monthly payments. With a contracting book, the percentage arrears figures can increase without any significant increase in the absolute number of accounts in arrears.

At 31 March 2013 Group arrears

	Total balances £m	3 months+ %
Prime	**1,208.6**	**1.80**
Buy-to-let	**2,359.0**	**0.96**
Acquired portfolios and other	**356.9**	**6.21**
Core residential	**3,924.5**	**1.74**
Second charge lending	**34.8**	**6.77**
Total	**3,959.3**	**1.92**

At 31 March 2012 Group arrears

	Total balances £m	3 months+ %
Prime	1,360.4	1.54
Buy-to-let	2,443.4	0.97
Acquired portfolios and other	390.3	6.17
Core residential	4,194.1	1.66
Second charge lending	39.6	6.43
Total	4,233.7	1.84

Residential mortgage arrears are in line with expectation given the fragile economic environment, rising levels of unemployment, a responsible forbearance strategy and a contracting mortgage portfolio. At 1.92% (2011/12: 1.84%), they remain below the sector average. Excluding the impact of the closed, non-core second charge and acquired portfolios, the level of loans three months or more in arrears in the residential loan book is significantly lower at 1.34% (2011/12: 1.24%).

The Society actively seeks to support those borrowers who are experiencing genuine financial hardship, so enabling them to remain in their homes if this is believed to be in their best interests (e.g. where the loss to the customer is not increased over time). Forbearance measures take a number of forms depending on individual customer circumstances. Short-term solutions focus on temporary reductions to contractual payments. For customers with longer term financial difficulties, term extensions may be offered, which may also include interest rate concessions. The Society's approach to forbearance is described in more detail in note 34 to the Accounts.

Commercial

Supporting the drive to manage down the legacy higher risk assets and return the Society to a safe and conservative risk profile, the exposure to the commercial property sector has further reduced over the period. This focus has been maintained as a result of the high degree of balance sheet stringency employed, despite the unfavourable impact on margin through the redemption of certain higher yielding but higher risk assets. The loans that redeemed in the year provided a margin of 2.66%, reducing the average margin of the remaining loans to 2.27%.

Balances secured on commercial property assets are down by 7.9% to £1,060.8m (2011/12: £1,152.2m). Of this remaining balance, £216.6m is securitised (2011/12: £262.8m) with any residual risk for the Society already fully provided for. Loans fully secured on residential property portfolios managed by the Commercial division reduced to £36.4m (2011/12: £75.5m).

At 31 March Loans fully secured on commercial property

	2013 £m	2012 £m
Healthcare and leisure	**222.4**	228.7
Industrial and warehouse	**62.3**	61.3
Office	**178.8**	204.4
Retail	**484.0**	560.0
Other	**26.4**	6.8
Fair value adjustments	**86.9**	91.0
Total	**1,060.8**	1,152.2

The sustained level of high profile business failures during the year is evidence of the adverse impact that the challenges facing the UK economy have exerted on the commercial property market. Correspondingly, the Board has ensured that the controlled winding down of the commercial loan book has remained a priority, and considers the reduction in exposure since 2008/9 of circa £600m to represent a considerable success.

Funding

The Society has a robust, balanced and diverse funding base. In line with core building society principles, it obtains the majority of its funding through retail savings balances, supported by strategically appropriate wholesale funding programmes.

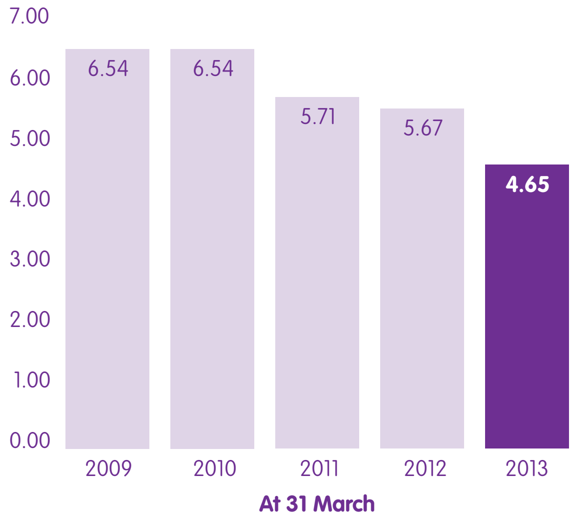
Key Performance Indicator: *The key funding measure that the Board uses to assess the risk in its funding base is the wholesale funding ratio. The wholesale funding ratio measures the proportion of total Society shares and borrowings (including non-recourse finance) not in the form of retail savings products. It assesses the Society's relative exposure to the wholesale funding markets and it is the Board's aim to maintain this ratio at a stable low level.*

One of the main tenets of the Back to Basics strategy is to return to core building society principles. A key way that the Board measures the success of this strategy is by reviewing the proportion of total residential mortgage assets that are funded by retail deposits.

Retail

The proportion of funding in the form of retail member deposits remained strong with residential mortgage assets comfortably funded 1.16 times (2011/12: 1.31 times) by these deposits.

Retail balances
£bn



Retail funding costs remained relatively high for much of the period as a consequence of intense competition. The introduction of the Bank of England's Funding for Lending Scheme (FLS) – in which the Society is participating – has increased the availability of low cost funding to support lending to UK households and small/medium sized businesses. The overall effect has been far-reaching with Best Buy savings rates reducing by over 1% in the second half of the financial year.

Wholesale

While the wholesale markets are considered to be a secondary source of funding compared with retail deposits, a degree of diversification in the funding base is beneficial.

Following the repayment of £500m funding raised in 2009 under the Government's Credit Guarantee Scheme, the level of wholesale funding fell markedly. However, in April 2012 the Society raised £250m via a residential mortgage backed securitisation transaction, the first such transaction for the Society since 2005, demonstrating market confidence in the Society, and delivering a significant improvement in the level of term funding held. This resulted in a year end wholesale funding ratio of 16.7% (2011/12: 16.3%).

The table below analyses the Society's wholesale funding portfolio:

At 31 March Wholesale funding sources

	2013 £m	2012 £m
Repo and other secured agreements	**376.8**	695.0
Deposits	**221.5**	178.3
Certificates of deposit	**4.0**	4.0
Medium term notes	**-**	3.0
Securitisation	**328.3**	225.4
Total	**930.6**	1,105.7

Wholesale funding balances
£bn

Since the end of the year the Society has successfully completed a further residential mortgage backed securitisation transaction, raising £380m of long-term secured wholesale funding. This achievement is a further indication of the significant progress the Society has made in diversifying its funding base.

Liquidity

Key Performance Indicator: *The Society's liquidity position is monitored in a number of different ways, including reviewing the components of our funding and liquidity portfolios, testing liquidity by selling into the market and monitoring the impact under a number of stressed scenarios. However, the key measures that the Board uses to monitor its liquidity position are:*

- *The liquidity ratio – liquid assets as a proportion of shares and borrowings; and*
- *The total level of 'buffer liquidity' versus our regulatory requirement (set by the PRA). Eligible buffer liquidity, which represents the most liquid and secure form of holding, constitutes gilts, treasury bills, supranational bonds and reserves with the Bank of England.*

The Society continues to adopt prudent, robust and effective liquidity management processes. During the year, the Society has consolidated liquidity holdings to levels which exceed regulatory requirements while minimising the detrimental impact that these assets have on margin.

Liquidity holdings consist solely of high quality liquid assets with 100% of treasury investments rated single A or better at 31 March 2013 (2011/12: 100%). The Society has no exposure to those markets that the European governments have expressed concern about, to non-UK sovereign debt or to any mortgage market outside the UK.

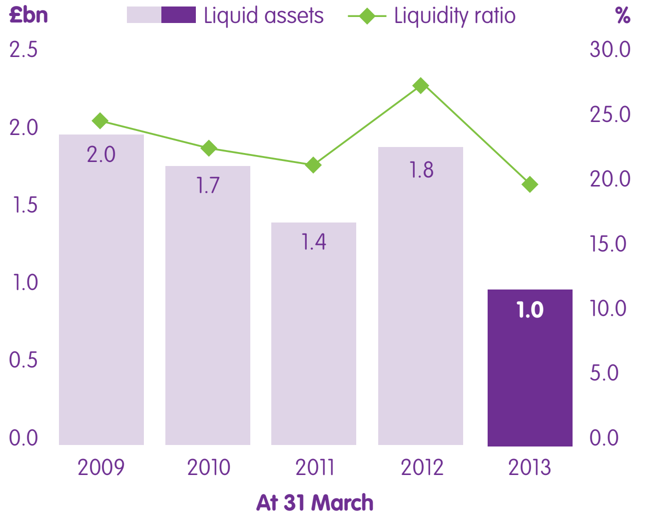
Rigorous credit assessment processes are employed to ensure the continued quality of liquid assets. There were no impairment charges against treasury investment assets during the year (2011/12: £nil).

An analysis of the Group's liquidity position is shown below.

At 31 March 2013 Liquidity portfolio	**£m**	**%**
Buffer liquidity		
- Bank of England Reserve	**384.5**	**37.0**
- Supranationals	**198.9**	**19.2**
Total buffer liquidity	**583.4**	**56.2**
Other securities – rated single A or better	**300.6**	**28.9**
Subsidiary/other liquidity	**154.9**	**14.9**
Total liquidity	**1,038.9**	**100.0**

At 31 March 2012 Liquidity portfolio	£m	%
Buffer liquidity		
- Bank of England Reserve	760.9	42.0
- Supranationals	350.3	19.3
- Gilts	20.5	1.1
Total buffer liquidity	1,131.7	62.4
Other securities – rated single A or better	553.4	30.6
Subsidiary/other liquidity	126.1	7.0
Total liquidity	1,811.2	100.0

Liquid assets and liquidity ratio



The Society's liquidity ratio decreased to 19.8% (2011/12: 27.6%) due to the Society holding substantial additional liquidity at 31 March 2012 in preparation for the repayment of £500m of Government guaranteed funding and, also, as a result of the managed run-down of excess holdings.

Capital structure

Key Performance Indicator: *Capital is held as the ultimate protection for depositors. The Board sets the internal level of capital with the aim of ensuring capital levels are always above minimum regulatory requirements.*

The primary indicators used to monitor capital are:

- *Core Tier 1 ratio – Core Tier 1 capital comprises historic profits generated over time plus profit participating deferred shares, a long-term secure form of funding, less a number of regulatory adjustments made for the purposes of capital adequacy. Core Tier 1 capital is the strongest form of capital for any financial institution. This capital is compared to the risk weighted assets of the financial institution. The risk weighted assets are calculated by asset class under Basel II using the Standardised approach. This allocates a weighting to each asset class based upon an estimate of the credit, market and other risks associated with the asset and counterparty. The higher this ratio the more capital held relative to its risk weighted assets; and*
- *Solvency ratio – this is the total capital as a proportion of risk weighted assets.*

The following table shows the composition of regulatory capital and the key capital ratios. As at 31 March 2013, the Solvency ratio strengthened to 17.2% (2011/12: 16.2%) driven by the focused reduction in risk weighted assets.

At 31 March

	2013 £m	2012 £m
Regulatory capital		
Tier 1		
General reserves	**236.1**	241.1
Permanent interest bearing shares (note 1)	**74.9**	74.9
Profit participating deferred shares	**173.7**	175.0
Intangible assets (note 2)	**(7.9)**	(7.5)
Deductions from Tier 1 capital (note 3)	**(3.7)**	(3.5)
	473.1	480.0
Tier 2		
Revaluation reserve	**3.7**	3.7
Collective impairment allowance	**15.1**	24.1
Contingency against collective provision add back (note 4)	**(8.3)**	(10.2)
Deductions from Tier 2 capital (note 3)	**(0.1)**	(3.5)
	10.4	14.1
Total capital	**483.5**	494.1
Risk weighted assets – Pillar 1		
Retail mortgages	**1,577.9**	1,676.3
Commercial loans	**888.4**	957.6
Treasury assets	**114.4**	151.1
Other assets	**157.0**	157.4
Market risk	**9.5**	12.9
Operational risk	**70.0**	94.8
	2,817.2	3,050.1
Key capital ratios (note 5)	**%**	%
Core Tier 1 ratio	**14.1**	13.3
Tier 1 ratio	**16.8**	15.7
Solvency ratio	**17.2**	16.2

Notes

1 Permanent interest bearing shares include any adjustments for unamortised premiums and discounts.

2 Intangible assets do not qualify as capital for regulatory purposes.

3 Certain deductions from capital are required to be allocated, 50% to Tier 1 and 50% to Tier 2 capital. Other deductions are Tier specific.

4 Deduction from the collective provision add back, reflecting the proportion of the provision that is disallowable for capital purposes.

5 Calculated as relevant capital divided by risk weighted assets. Core Tier 1 represents Tier 1 capital excluding permanent interest bearing shares.

The Society's capital strength is an indication of its financial resilience in this period of protracted economic turbulence. At 14.1% (2011/12: 13.3%), the Core Tier 1 ratio is one of the highest in the UK bank and building society sector and has more than doubled over the last four years (6.8% in 2008/9). The Tier 1 ratio is up from 15.7% to 16.8%.

The prime driver for the improvement in capital ratios is the ongoing success of the balance sheet de-risking programme, with risk weighted assets down by 7.6% to £2.8bn.

Member engagement

At the West Brom we constantly look at how we can improve our products and services. One of the ways we do this is through customer research, which helps us to understand our members' needs and expectations. In addition to financial and performance indicators, the Board monitors the feedback from our customer research to assess how well we are meeting the financial needs and interests of our members, as well as improvements we can make to deliver high quality products and services.

Key Performance Indicator: *The Board reviews a range of customer research programmes, with the key ones being:*

- *Mystery Shopper – conducted across our branch network. Mystery shoppers record their experience on a scorecard against the standards that we expect our customers to receive;*
- *Real-time survey – a survey within our Contact Centre where members are asked to score our service at the end of their call and give us reasons for that score;*
- *Customer Experience Tracker – a telephone satisfaction survey where we contact a variety of members ranging from those who have recently visited a branch to make a transaction or to see a Financial Planning Manager through to those who have opened an account through either our Direct or WeBSave channels;*
- *Postal and email surveys – we send our members short surveys by mail/email on a range of subjects e.g. a recent product purchase; and*
- *Members' ViewPoint – these events provide face-to-face feedback from our members on our products, services and our work in the community. Two of these events have been held during the past year in Birmingham and Stourbridge.*

Our Mystery Shopper programme is an ongoing monthly measure of how our branches are performing against agreed standards. These standards have been devised to ensure we deliver the high level of service that our members expect to receive. One of the changes to the programme this year is that these mystery shops are now recorded, so providing a valuable coaching tool to our Branch Managers.

Our Customer Experience Tracker, which measures satisfaction across a representative sample of our member base, has continued to score well throughout 2012/13. Some of the highlights from the latest survey are:

- An average satisfaction score of 4.4 (out of 5) across the channels measured;

- 68% of members surveyed stated that we exceeded their expectations and went the 'extra mile'; and
- 53% of our members would definitely recommend us with another 34% likely to recommend us.

New to the West Brom research programme for 2012/13 was the introduction of a real-time survey in our Contact Centre. This short survey, offered to both existing and potential customers at the end of a phone call, captures both a score and verbatim commentary. It also allows us to gain immediate feedback within a few minutes of the service being provided. The survey has already proved a valuable motivational tool for staff but feedback from the survey also provides us with the opportunity to cascade customer improvements throughout the entire organisation, and not just the Contact Centre.

The Board also reviews a number of measures in relation to customer complaints. One key indicator is the Financial Ombudsman Service (FOS) 'complaint overturn' rates. This shows the percentage of instances where the FOS has overturned, in the customer's favour, outcomes where individual firms originally found against the customer.

The latest table, published in Q1 2013 and representing the period July 2012 to December 2012, quoted the performance of approximately 50 of the largest qualifying firms. Our performance for that period was around 84% resolved in favour of the Society; considerably better than our comparator firms. The Board considers this to be an excellent performance.

Risk Management

Overview
Effective management of risks and opportunities is essential to achieving the Society's corporate objectives. The Board aims to manage effectively all the risks that arise from its activities and believes that its approach to risk management reflects an understanding of actual and potential risk exposures, the quantification of the impact of such exposures and the development and implementation of controls that manage exposures within the Board's agreed risk appetite.

Risk management framework
The Society's activities are governed by its constitution, principles and values. The Directors have also agreed a set of statements which describe the Board's risk appetite in terms of a number of key risk categories: business, capital, liquidity, credit, market, operational, pension liability and conduct (the Society's Risk Appetite Statements).

These Risk Appetite Statements drive corporate planning activity, including capital and liquidity planning, as well as providing the basis for key risk measures.

The final element of the framework is the formal structure for managing risk across the Group. This is based on the '3 lines of defence' model which is illustrated below.

	Activity	Responsibility	Governance
1st	Business Operation	Line Management	Line Management Oversight
2nd	Policy, Controls, Measure, Monitor	Control Functions	Management and Board Committees
3rd	Assurance	Internal Audit	Audit Committee

Governance structure
Risk governance is provided by a structure consisting of seven key risk management committees:

- **Group Risk Committee (GRC)** – This committee is chaired by a Non-Executive Director and is responsible for the oversight and management of the key strategic risks identified by the Board.
- **Assets & Liabilities Committee (ALCo)** – This committee is chaired by the Group Finance Director and is responsible for the assessment of exposure to Treasury counterparty credit, market, liquidity and interest rate risk.
- **Residential Mortgage Committee (RMC)** – This committee is chaired by the Group Risk Director and is responsible for monitoring the Society's residential lending activity and its exposure to credit risks in the retail loan books.
- **Commercial Loans Risk Committee (CLRC)** – This committee is chaired by the Group Risk Director and is responsible for monitoring the Society's exposure to credit risks in the commercial loan book.
- **Operational Risk Committee (ORC)** – This committee is chaired by the Group Risk Director and is responsible for the oversight of the management of operational risks arising from the Society's business activities.
- **Group Capital Committee (GCC)** – This committee is chaired by the Group Finance Director and is responsible for reviewing the Group's capital and capital requirements.
- **Retail Conduct Risk Committee (RCRC)** – This committee is chaired by the Chief Executive and is responsible for reviewing and monitoring all retail conduct related matters.

Independent assurance is provided by the Internal Audit function which has a direct reporting line into the Audit Committee (AC).

Risk categories
In order to identify the key risk categories most relevant to the Society, the Board considered an overall risk universe relating to firms in the financial services sector. This has been distilled into eight material risk categories as shown below.

Business risk
The risk of the Society failing to meet its business objectives through the inappropriate selection or implementation of strategic plans.

Credit risk
The risk that losses may arise as a result of borrowers, debtors or market counterparties failing to meet their obligations to repay.

Capital risk
The risk that the Society has insufficient capital to cover stressed losses or to meet regulatory requirements.

Liquidity risk
The risk that the Society either does not have sufficient financial resources to enable it to meet its obligations as they fall due or can secure such resources only at excessive cost.

Market risk
The risk of changes in the value of, or income arising from, the Society's assets and liabilities as a result of unexpected changes in financial prices, primarily interest rates, property prices, bond yields and inflation.

Operational risk
The risk of loss and/or negative impact to the Society resulting from inadequate or failed internal processes or systems, inability to attract, retain and motivate people, or from external events.

Retail conduct risk
The risk that inappropriate behaviours by the Society result in adverse outcomes to retail consumers.

Pension liability risk
The risk that there will be a shortfall in the value of the Society's pension fund assets over and above the guaranteed liability to its employees under the defined benefit pension scheme. This may result from a number of sources including investment strategy, investment performance, market factors and mortality rates.

For each risk category the Board has agreed an appetite statement and key metrics which, together, define the level of risk the Board is prepared to accept or tolerate. In addition, key threats and the corresponding Society responses or mitigants, as well as opportunities, have been identified. The mitigating controls and the effectiveness of the controls are monitored by line management, with control functions providing a second line of defence. Internal Audit, through an approved assurance programme, provides the third line.

The Group Risk Committee meets at least quarterly to review the Society's exposure to the risk categories. During this financial year, the committee met on eight occasions.

Business conditions and the economic environment

The environment in 2012 was again dominated by the eurozone crisis and by reduced growth expectations for the Organisation for Economic Co-operation and Development (OECD) economies. In the UK, the Bank of England maintained interest rates at an historically low level and expanded the policy of quantitative easing to inject money into the economy. In a bid to encourage lending to consumers and small businesses the Government launched the Funding for Lending Scheme which provides lenders access to liquid assets with the rate of interest dependent on the level of net lending undertaken.

The West Brom is exclusively focused in the UK and, therefore, the general UK macro-economic environment is key to its success. The external factors that impact the Society include:

- Interest rates (Bank Rate and LIBOR);
- Inflation;
- Unemployment; and
- The housing and commercial property markets.

Day-to-day management of key risks

Primary responsibility for risk management, including the design and operation of effective controls, rests with the management of each business function – the 'first line of defence'. Support and challenge is provided through specialist risk functions – Credit Risk, Operational Risk and Assets & Liabilities Management – the 'second line of defence'. These functions develop and review policies, monitor and support compliance with those policies, and support the business functions to manage risk.

Governance and oversight is provided through a number of management and executive committees as detailed on page 17.

Credit risk

Credit risk refers to the risk that a customer or counterparty to a contract will not be able to meet their obligations as they fall due. For the purposes of the Society, this normally means the risk that a borrower will not repay their mortgage loan, or that a financial institution will not repay funds invested by the Society in that institution.

During the year the Society engaged in only limited lending activity. All such lending was in accordance with the approved credit policy, which is consistent with the risk appetite established by the Board. Currently, no new non-conforming property lending (i.e. commercial, buy-to-let, sub-prime or self-certified) is being undertaken.

The Society's exposure to residential and commercial credit risk is managed by a specialist Credit Risk department with a reporting line into the Group Risk Director. The Credit Risk department is responsible for setting the credit risk management framework and associated limits. It also provides regular reports to the Group Risk Committee, which is chaired by a Non-Executive Director and includes the Chief Executive, Group Finance Director, Group Risk Director and three other Non-Executive Directors as members.

Additionally, credit risk can arise within treasury transactions (used to meet liquidity requirements and those hedging instruments used for interest rate risk purposes). This type of credit risk is managed by the Treasury Middle Office team. On a daily basis, this team monitors exposures to counterparties and countries, and ensures operations remain within Board approved limits. ALCo and the Board review the Treasury Policy and limits, with reports presented to ALCo on a monthly basis confirming compliance with such policy limits.

Throughout the last financial year, a conservative approach to liquidity management has been maintained, investing for short periods with selected financial institutions. The Society has also moved towards a position of holding a significant proportion of liquidity in UK Government guaranteed and supranational financial institution assets, which are considered to be both highly liquid and secure. Treasury operates a strict control framework and exposures are monitored on a daily basis.

Market risk

Market risk refers to the possible changes in the value of, or income arising from, the Society's assets and liabilities as a result of changes in interest/exchange rates, property prices or equities. Market risk exposures are managed through the Treasury department which is responsible for managing exposure to all aspects of market risk within parameters set by the Board.

ALCo reviews the Treasury Policy, recommending changes to the Board as appropriate, and ensures that regular reports on all aspects of market risk are assessed and reported to the Board. The principal market risk is interest rate risk, which arises as a result of differences in the timing of interest rate re-pricing of assets and liabilities. To mitigate this, Society Treasury uses natural balance sheet hedging (e.g. matching 2 year fixed rate mortgages with 2 year fixed rate saving bonds) and derivative instruments. The use of derivatives is only permitted in accordance with the provisions of the Building Societies Act 1986, which place restrictions on their use.

The maximum level of interest rate risk is governed by the Board approved Treasury Policy in line with the Board's risk appetite.

In line with regulatory requirements and best practice, the impact of a parallel shift in interest rates in both directions, subject to a floor at 0%, is considered. In addition, the impact of alternative non-parallel scenarios upon income and market value is also considered.

Interest rate sensitivity also arises from the potential for different interest rates to move in different ways, e.g. Bank Rate mortgages are funded by LIBOR-linked liabilities. The impact of these mismatches (basis risks) is monitored by Treasury and reported to ALCo.

The Society's main exposure to equities is through the defined benefit pension scheme. While the Society does attract funds through index-linked savings products, all exposures to equity indices are fully hedged. There is no exposure to foreign exchange rates.

The Society has invested in property through its subsidiary West Bromwich Homes Limited and offers residential property for rent. This non-core business exposes the Society to movements in house prices. The Board's strategy is to exit from this business when market conditions are opportune.

Liquidity risk

The Society's principal purpose is to make loans secured by way of mortgage on residential property. It funds these loans substantially from short term deposits provided by its saving members. The contractual maturity of the mortgages is typically up to 25 years although loans are often repaid early due to borrowers moving house or remortgaging. On average, loans made by the Society last for seven years.

Savers' deposits, whilst accessible predominantly on demand, at short notice or for fixed periods, nevertheless tend to remain with the Society for longer periods. A substantial proportion of savers have long established relationships with the Society.

This difference in the nature of borrowers' and savers' relationships causes a structural mismatch between the speed at which the Group can generate cash from its business assets and the demand for funds to meet its liabilities. To mitigate this risk, the Group holds sufficient liquid resources to meet the normal day-to-day operations of the business and, in addition, maintains a buffer of high quality assets which can be converted quickly into cash to cover outflows in severely stressed conditions. Processes are in place to ensure that the quantity, quality and availability of these liquid resources is adequate at all times.

The Board undertakes a detailed annual review of its liquidity adequacy assessment processes (Individual Liquidity Adequacy Assessment or ILAA) and submits this to the PRA for supervisory review. The ILAA specifies the daily processes that the Society will use to determine the amount of liquidity required to cover its potential cash flow needs under a range of stresses, including three PRA standard scenarios 'name-specific', 'market-wide' and 'combined'.

The supervisory review also informs the PRA's view of the amount of 'buffer' or highest quality liquid assets that the Society should hold to meet the three standard regulatory stress scenarios and the maximum allowable gap between maturing wholesale assets and wholesale liabilities (wholesale refinancing gap). It issues Individual Liquidity Guidance (ILG) on these and other liquidity risk matters which the Society must meet. Treasury maintains liquid resources at the greater of the ILG measures or the internal assessment of liquidity adequacy.

The Board has established a Liquidity Risk Policy which lays down a rigorous framework of limits to control the Society's liquidity risk. The governance process surrounding liquidity risk management activities is as follows:

- The Board has delegated authority for the governance of Liquidity Risk Management to the Assets & Liabilities Committee (ALCo) which meets monthly;
- Operational management of liquidity risk is further delegated to the Liquidity Management Committee (LMC) which meets weekly. LMC looks at liquidity stresses over a horizon of up to three months and plans cash flows over a rolling 12 month planning period;
- Treasury is responsible for day-to-day management and maintenance of adequate liquid resources under delegated authority from ALCo; and
- The Group Risk Committee monitors independently the overall liquidity adequacy process, including the activities of ALCo, LMC and Treasury.

The Society is responsible for the liquidity and cash flow requirements of wholly owned subsidiaries.

Capital risk

The Society conducts an Internal Capital Adequacy Assessment Process (ICAAP) covering all risks. This is used to assess the Society's capital adequacy and determine the levels of capital required going forward to support the current and future risks in the business. This analysis is collated into an Internal Capital Assessment (ICA) that is approved by the Board. The ICA incorporates expected future capital requirements from changes in business volumes, mix of assets and activities within the context of current and anticipated future risks, and multiple, stressed scenarios. The ICA is used by the PRA to set the Society's capital requirements as Individual Capital Guidance (ICG).

Society capital requirements are reviewed on a monthly basis and the results of this monitoring are reported to the Group Capital Committee, Group Risk Committee and the Board.

The detailed breakdown of the Society's capital position can be found on page 15.

Operational risk

Each business function has a clearly articulated responsibility for identifying, monitoring and controlling its operational risks. The business function receives support and guidance from the Operational Risk team, which co-ordinates regular reviews with the function managers and collates the output for review by executive management, the Operational Risk Committee and the Group Risk Committee.

The Risk Division also provides independent input and challenge to the business functions, both through the regular review of operational risks and day-to-day business initiatives.

Retail conduct risk

The regulatory focus on retail conduct risk has increased with the separation of the Financial Services Authority into the Prudential Regulation Authority and Financial Conduct Authority. The Society has formally mirrored this separation by recognising a specific risk category – retail conduct risk. During the last financial year, a strong governance framework was implemented which included the establishment of a Retail Conduct Risk Committee chaired by the Society's Chief Executive. During 2013/14, further activities are planned to embed a strong conduct culture throughout the organisation and to enhance the Society's conduct related management information.

Principal risks and uncertainties

Set out in the table overleaf are the key external threats which have been identified by the Group Risk Committee.

Risk Category	Key External Threats	Society Response and Mitigants
Business risk	Continuation of ultra low interest rates leading to continuing strain on margins or adverse changes to the operating environment: • Demand for retail funds. • House price movements. • Low or flat economic growth. • Increasing regulatory costs.	Business plans continue to model the impact of a range of scenarios. Income projections are reviewed regularly to identify mitigation actions.
Credit risk	Higher unemployment and/or an increase in Bank Rate (leading to increased arrears and losses).	The Society's provisioning and stress testing models assume a range of unemployment levels. Should an increase occur, the Society would expand its credit management resource.
	Reduction in property prices (leading to a higher incidence of voluntary possessions).	The Society is committed to work with its borrowers to avoid possession wherever possible. In the event that possessions were to increase the Society has provided prudently and regularly reviews its impairment provisions.
	Low or flat economic growth (leading to further tenant failures).	The Society has a well resourced and highly experienced team dealing with commercial property mortgages and, as has been the case throughout 2012/13, works with borrowers to lessen the impact. The Board has set aside impairment provisions to limit the impact of losses.
Capital risk	Rules for calculating capital (amount required and/or amount held) are changed.	Maintain regular dialogue with the Regulator and ensure full understanding of the relevant rules.
Liquidity risk	Intensification of competition for retail funding.	The Society continues to attract new retail savers despite intense competition. Balance sheet management ensures this risk is minimised.
Market risk	Residential tracker mortgage assets whose rate is linked to Bank Rate with no floor.	All new residential tracker mortgages subject to a minimum rate.
	Falling HPI, leading to a reduction in the book value of West Bromwich Homes Limited properties.	No new homes being added to the portfolio and active steps being taken to reduce the Society's exposure.
Operational risk	Insurance arrangements do not sufficiently cover an event (requiring the Society to pick up the cost).	The annual review of insurance arrangements is based on advice from brokers and an annual benchmarking exercise.
	A significant business continuity event.	Detailed business plans in place which are regularly tested.
Pension liability risk	Increased longevity and/or poor investment returns (requiring the Society to contribute more to the scheme).	The defined benefit scheme is closed to new members and existing members are no longer accruing service benefits. The Trustees take extensive advice (actuarial, investment etc.) to minimise the impact of the risks identified.
Retail conduct risk	Actions of third party suppliers leading to adverse customer outcomes.	A robust supplier framework is in place to oversee the activities of key suppliers.

Mark Gibbard
Group Finance Director
31 May 2013

Directors' Report

The Directors are pleased to present their Annual Report, together with the audited Accounts, for the financial year ended 31 March 2013.

Business objectives

The main purpose of the Society and its subsidiaries (the Group) is to work together to meet the prime financial needs of our members. This entails provision of a diverse range of personal financial services, offering competitive pricing and excellent service.

Business review

The Group's business and future plans are referred to in the Chairman's Statement on page 2, the Chief Executive's Review on pages 3 to 5 and the Business Review on pages 7 to 20.

Key performance indicators

The Board measures performance against its strategic aims by reference to a number of key performance indicators which are described in the Business Review on pages 7 to 20.

Profit and capital

The Group's loss before tax (on continuing operations) amounted to £9.4m (2011/12: £9.5m). The total loss after tax transferred to reserves was £5.0m (2011/12: £9.2m).

The total Group reserves at 31 March 2013 were £249.2m (2011/12: £246.0m) after taking into account a revaluation reserve of £3.7m (2011/12: £3.7m) and the available for sale reserve of £9.4m (2011/12: £1.2m).

Gross capital at 31 March 2013 was £497.8m (2011/12: £495.9m) including £173.7m of profit participating deferred shares (2011/12: £175.0m) and £74.9m (2011/12: £74.9m) of subscribed capital.

The main Group ratios were as follows: gross capital ratio; 9.47% (2011/12: 7.57%), free capital ratio; 7.16% (2011/12: 5.83%) and liquidity ratio; 19.77% (2011/12: 27.64%). For further details see page 90.

Detailed Basel II Pillar 3 capital disclosures for the current year will be available on the Society website.

Risk management

As the Society operates in a very competitive environment, the management of risk and development of a suitable strategy are critical activities in achieving business success.

The Board and the Board Committees ensure that risk management and strategic direction are considered regularly and that appropriate actions are implemented. These considerations are detailed in the Society's Internal Capital Adequacy Assessment Process (ICAAP) document which is part of the Basel II process.

The principal risks inherent to our business and details of how these risks are managed are set out in the Business Review (pages 7 to 20).

In addition to these principal risks there are, as a result of the current uncertain economic environment for banks and building societies, ongoing actions under the PRA's supervisory review process, which include extensive stress testing exercises.
The Directors are aware, in arriving at their judgments, that the Society will be subject, in the same way as others within the sector, to these ongoing tests of capital and recognise the uncertainty inherent in the process as factors within each test change.

Financial risk management objectives and policies

The Board's objective is to minimise the impact of financial risk upon the Society's performance. Financial risks faced by the Society include interest rate, credit, liquidity and currency risks. The Board manages these risks through a risk management framework, Board policies and its Treasury and Credit Risk functions. Governance and oversight is provided through the Group Risk and Assets & Liabilities Committees. Details of the Society's financial instruments, hedging activity and risk mitigation can be found in note 13 and notes 33 to 36 to the Accounts.

Mortgage arrears

At 31 March 2013 there were 143 (2011/12: 148) residential and commercial mortgage accounts where payments were 12 months or more in arrears based on current monthly repayments. The total amount outstanding on these accounts was £72.2m (2011/12: £75.7m), representing 1.47% (2011/12: 1.42%) of mortgage balances, and the amount of arrears was £6.8m (2011/12: £6.9m). Appropriate provisions were made for potential losses on mortgages in accordance with the provisioning policy set out in note 1 to the Accounts.

Directors

The following served as Directors of the Society during the year:

John Ainley
Mark Gibbard*
Claire Hafner
Andrew Jones*
Mark Nicholls (Chairman)
Mark Preston
Martin Ritchley
Richard Sommers
Colin Walklin
Jonathan Westhoff*

* Executive Directors.

All Directors are members of the Society. None of the Directors have, at any time in the year or as at the year end, any beneficial interest in shares or debentures of any associated body of the Society.

Supplier payment policy

The Society's policy is to agree the terms of payment before trading with the supplier and to pay in accordance with its contractual and other legal obligations. At 31 March 2013, the creditor days figure was 20 days (2011/12: 21 days). This conforms with the aim of paying creditors promptly.

Charitable donations

During the year the Society donated £5,000 (2011/12: £5,000) to a local charitable organisation. The Society also raised significant sums through its community programme, affinity accounts and voluntary staff initiatives. These are outlined in the Corporate Responsibility Report (page 31).

No donations were made for political purposes. While encouraging any employees who wish to take part in community affairs, the Group does not support any employees in the pursuit of political activity.

Employees

The Society is an equal opportunities employer and gives proper consideration to all applications for employment with regard to vacancies that arise and to the applicant's own aptitude and abilities, regardless of race, creed, gender, sexual orientation, marital status, age, physical or mental disability. If current staff members become disabled, every effort is made to enable them to maintain their present position or to receive relevant training.

The Society has systems that provide information to employees, permitting them to participate in the operation and development of the business. The Society consults with the West Bromwich Building Society Staff Union and assesses the results of annual staff satisfaction surveys to ensure that staff conditions and workload are maintained at an acceptable level. Additionally, details of meetings, team briefings, circulars and information updates are placed on the Society's intranet to ensure that employees are aware of the Society's objectives and performance and conscious of the wider financial and commercial environment in which the Society functions.

Health and safety

The Society sets high standards to maintain the health and safety of all staff, customers and those affected by any of its operations.

The Society is committed to ensuring that all employees receive adequate training in health and safety to make them aware of their individual responsibilities to enable them to carry out their work tasks without injury or damage to the health of themselves or others affected by their work. All employees, on commencing employment with any business area, receive induction training which is reinforced through annual refresher training. Additional training is delivered when a need has been identified, such as Manager Training, Stress Awareness, Manual Handling, Fire Warden, First Aid etc.

The Society recognises the need to consult with its employees on health and safety issues and the rights of individuals and Trade Unions in respect of this. Accredited safety representatives are afforded every opportunity to effect this consultation and to receive training as appropriate from their Trade Union. A Health and Safety Committee is in place with representatives from across the business which meets quarterly to review health and safety.

Health and safety issues are brought to the attention of all employees through business specific communication channels. Employees are similarly encouraged to raise issues through their line management.

During the reporting year no enforcement notices were issued against the organisation by any of the enforcing authorities and no proceedings were instigated against the Society for breaches of health and safety regulations within the reporting period.

Directors' responsibilities in respect of the Annual Report, the Annual Business Statement, the Directors' Report and the Annual Accounts

The Directors are responsible for preparing the Annual Report, Annual Business Statement, Directors' Report and the Annual Accounts in accordance with applicable law and regulations.

The Building Societies Act (the Act) requires the Directors to prepare Group and Society Annual Accounts for each financial year. Under that law they are required to prepare the Group Annual Accounts in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and applicable law and have elected to prepare the Society Annual Accounts on the same basis.

The Group and Society Annual Accounts are required by law and IFRSs as adopted by the EU to present fairly the financial position and the performance of the Group and the Society; the Building Societies Act 1986 provides in relation to such Annual Accounts that references in the relevant part of that Act to Annual Accounts giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and Society Annual Accounts, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the Annual Accounts on the going concern basis unless it is inappropriate to presume that the Group and Society will continue in business.

In addition to the Annual Accounts the Act requires the Directors to prepare, for each financial year, an Annual Business Statement and a Directors' Report, each containing prescribed information relating to the business of the Group and Society.

A copy of the Annual Accounts is placed on the Society's website.

Directors' statement pursuant to the Disclosure and Transparency Rules

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware:

- the financial statements, prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and result of the Group and Society; and
- the management report contained in the Business Review includes a fair review of the development and performance of the business and the position of the Group and Society, together with a description of the principal risks and uncertainties that they face.

Directors' responsibilities for accounting records and internal control

The Directors are responsible for ensuring that the Group:

- keeps proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and Society in accordance with the Act; and
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with rules made by the Financial Services Authority under the Financial Services and Markets Act 2000. The rules are now regulated by the Prudential Regulation Authority under the Financial Services Act 2012.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Society's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' responsibilities in respect of going concern

In preparing the financial statements the Directors must satisfy themselves that it is reasonable for them to conclude it is appropriate to adopt the going concern basis. The Group meets its day-to-day liquidity requirements through managing both its retail and wholesale funding sources and is required to maintain a sufficient buffer over regulatory capital requirements in order to continue to be authorised to carry on its business.

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Chief Executive's Review on pages 3 to 5. The financial position of the Group, its capital structure and risk management and control processes for managing exposure to credit, market, liquidity and operational risk are described in the Business Review on pages 7 to 20.

In addition, notes 33 to 36 to the financial statements include further information on the Group's objectives, policies and processes for managing its exposure to liquidity, credit and interest rate risk, details of its financial instruments and hedging activities.

The Group's forecasts and projections, taking account of possible changes in trading performance and funding retention, and including stress testing and scenario analysis, show that the Group will be able to operate at adequate levels of both liquidity and capital for the foreseeable future. Furthermore, the Group's capital is in excess of the PRA requirement.

After making enquiries the Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future and that, therefore, it is appropriate to adopt the going concern basis in preparing the Annual Accounts.

Auditor

The auditor, KPMG Audit Plc, has expressed their willingness to continue in office. In accordance with Section 77 of the Building Societies Act 1986, a resolution for their re-appointment will be proposed at the Annual General Meeting.

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Society's auditor is unaware; and each Director has taken all the steps that they ought to have taken as a Director to make themselves aware of any relevant audit information and to establish that the Society's auditor is aware of that information.

By order of the Board

Mark Nicholls
Chairman
31 May 2013

Directors' Report on Corporate Governance

The Board is committed to high standards of corporate governance and believes they are central to the Society's culture and values.

Corporate governance – a brief history and recent developments

The widely accepted articulation of good practice is the UK Code on Corporate Governance (the Code). The first version of the Code was produced in 1992 by the Cadbury Committee which defined Corporate Governance as 'the system by which companies are directed and controlled'.

An updated version of the Code was issued in June 2010, following the 2008/9 financial crisis and the Walker Review into the governance of banks and other financial institutions.

In May 2011 the Financial Reporting Council began consulting on possible amendments to the Code that would require companies to publish their policy on boardroom diversity and report against it annually. The agreed changes have been implemented in a revised version of the Code issued in September 2012 and will apply to financial years beginning on or after 1 October 2012.

The remainder of this Report sets out how the Society complies with the 2010 Code and, where a different approach is taken, explains why that is the case.

The Code's Main Principles	What the Society does to meet the Principles
A1 The Role of the Board Every company should be headed by an effective board which is collectively responsible for the long-term success of the company	The principal functions of the Society's Board include: • Providing entrepreneurial leadership; • Setting the Society's strategic aims and risk appetite; • Implementing and maintaining a framework of prudent and effective controls, which enables risk to be assessed and managed; • Ensuring the necessary financial and human resources are in place for the Society to meet its objectives; and • Reviewing management performance. The Board meets as often as is necessary to fulfil its responsibilities. During the last financial year the Board met on 9 occasions. Details of Director attendance at Board and Committee meetings can be found in the table at the end of this Report. The minutes of Board and Committee meetings record all material discussion and challenge and are circulated to all Directors. The Chair of each Committee reports to the subsequent Board meeting the key matters discussed. A schedule of matters reserved to the Board is maintained and kept under regular review. The Board is supported by a number of Committees each with Board approved terms of reference. Details of the membership of those Committees and their key activities are reported elsewhere in this Report and Accounts. The Society has arranged appropriate insurance cover in respect of legal action against its Directors.
A2 Division of Responsibilities There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision	The positions of Chairman and Chief Executive are held by different people. The role of the Chairman includes establishing and developing an effective Board to provide support and constructive challenge to the management team. Further details of the Chairman's main responsibilities are set out in the commentary relating to Code Principle A3. The Chief Executive has overall responsibility for managing the Society and implementing Board agreed strategy.
A3 Chairman The chairman is responsible for leadership of the board and ensuring its effectiveness on all aspects of its role	The main responsibilities of the Chairman are: • Establish and develop an effective Board, including succession planning, recruitment and appraisal of Non-Executive Directors (NEDs); • Lead the Board as a team; • Ensure that the Board has agreed clear values and a Statement of Principles; • Plan and manage the Board's business, including ensuring that appropriate committees are established with the right objectives and membership and that the Board has the right agenda and information; • Ensure that the Board has established key priorities; • Maintain and develop a productive and open relationship with the Chief Executive, agree the Chief Executive's objectives and carry out regular appraisals. The Chairman is responsible for leading the appointment process for the Chief Executive; • Ensure there are appropriate arrangements for the evaluation and remuneration of senior executives; • Act as an accountability focus for the Society, including chairing the Annual General Meeting; • Represent the Society with Regulators and ensure that there is an open and trustworthy relationship; and • Ensure that the Board and its Committees periodically evaluate their own performance. The Board has satisfied itself that both at the time of his appointment, and currently, the Chairman is independent in character and judgment and meets the independence criteria set out in the Code.

The Code's Main Principles	What the Society does to meet the Principles
A4 Non-Executive Directors As part of their role as members of a unitary board, non-executive directors should constructively challenge and help develop proposals on strategy	NEDs are involved in all key decisions and receive detailed management information and reports to ensure they have a firm grasp of the Society's business and external operating environment. NEDs are responsible for all appointment, termination and remuneration decisions relating to the Society's Executive Directors. Martin Ritchley has been appointed as the Board's Senior Independent Director (he is also Deputy Chairman). As Senior Independent Director he leads the annual review of the Chairman's performance. The NEDs meet formally and informally without Executive Directors present.
B1 The Composition of the Board The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively	Board and Committee composition is kept under regular review by the Chairman and the Nominations Committee to ensure that it is of appropriate size, mix of Executive and Non-Executive Directors and has the right skills and experience to oversee the Society's business activities. The Board believes that all NEDs should meet the Code's independence criteria on appointment and throughout their term of office and has determined that each of the current Directors is independent in character and judgment and that there are no potential conflicts of interest which would affect their judgment.
B2 Appointments to the Board There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board	During the course of the last financial year, no new appointments were made to the Board. Three NEDs reached the end of their initial three year term of office. The Nominations Committee reviewed their performance and recommended to the Board, which subsequently approved the recommendation, to offer further three year terms of office in each case. The Board has considered the proposed changes to the Code relating to diversity. This has arisen as a result of the Davies Report entitled 'Women on Boards'. The Board agreed that diversity contributed positively to the quality of Board performance and agreed that this should be a factor in recruitment decisions, with the key focus that appointments be made on merit. The Board has decided to keep under review the setting of measurable objectives. Currently the percentages of females on the Board and senior management team are 10% and 22% respectively. The terms of reference of the Nominations Committee, which is made up of NEDs, are available on request from the Group Secretary.
B3 Commitment All directors should be able to allocate sufficient time to the company to discharge their responsibilities effectively	The standard letter of appointment for NEDs sets out the expected time commitment and explains what is required if there is any material change to their commitments.
B4 Development All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge	The Society has a range of induction activities and material for NED appointments which is tailored to their individual experience. These include site visits, meetings with senior management and reports/information concerning the Group's operations. Internally organised events on topics of particular relevance to the Society are used to aid development. NEDs are also encouraged to attend appropriate externally organised events. A development log records relevant development activities undertaken by individual Directors and an intranet site provides easy access to relevant material for NEDs.
B5 Information and Support The board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties	Board papers, including a management information pack are issued to Directors prior to Board meetings. Board agendas are agreed in advance of each meeting and focus on strategic matters, as well as ensuring that Directors are kept informed of key business activities and regulatory developments. Minutes of Board Committee meetings held since the last Board meeting are included in the papers. Where appropriate, papers are presented by the relevant member of the management team. The Board and its Committees are served by the Group Secretary who advises on governance matters and procedures. Directors have access to independent professional advice should that be required.
B6 Evaluation The board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors	The most recent formal evaluation of Board and individual Director performance concluded in the early part of the 2012/13 financial year. The evaluations were initiated by a questionnaire and were reviewed by the Chairman and the general output discussed with the whole Board. Specific points were fed back to individual Directors by the Chairman. Evaluation of the Chairman was led by the Deputy Chairman and took the form of a questionnaire completed by all Directors other than the Chairman and a meeting to review the responses. The conclusions were shared with the Chairman. The questionnaires also sought feedback from Committee members, evaluating the performance of the four Board Committees. Details of the current evaluation, which is being supported by external specialist firm – Lintstock – will be included in the 2013/14 report.
B7 Re-election All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance	All new Directors are required by the Society's Rules to stand for election at the first Annual General Meeting following their appointment to the Board. The Code's Main Principle relating to re-election of Directors requires that they be submitted for re-election at regular intervals. One of the Supporting Provisions is that all Directors of FTSE 350 companies should be subject to annual election. Although the Society is not a FTSE 350 company, the Board would normally adopt Code Provisions which apply to such firms. Having carefully reviewed the Provision, the Board has concluded that, although very unlikely, there could be circumstances where requiring all Directors to stand for election could have an adverse outcome for the stability of the Society and that this would not be in the best interests of members. The Society's Rules require that those Directors who are due for election or who have not been re-elected in the last three years must stand for election/re-election. This means that three Directors must stand for re-election. All of the other Directors were elected in 2011 or 2012 and are therefore not required by the Rules to stand for re-election in 2013. However, recognising the new Code Provision, the Board believes that it would be appropriate to bring forward the re-election (as permitted by the Rules) of two Directors so that half of the Board is standing for re-election in 2013. The Board has agreed to keep the arrangements under review and will explain any variation to the Code in future Corporate Governance Reports.

The Code's Main Principles	What the Society does to meet the Principles
C1 Financial and Business Reporting The board should present a balanced and understandable assessment of the company's position and prospects	The Directors' Report on pages 21 to 23 includes statements detailing the Directors' responsibilities. The Chief Executive's Review on pages 3 to 5 and the Business Review on pages 7 to 20 give an extensive report on the Society's performance, financial position and the key risks that will impact performance and risk management going forward.
C2 Risk Management and Internal Control The board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives. The board should maintain sound risk management and internal control systems	The Society's Board is responsible for the development of strategies relating to risk management and internal control. Operational responsibility rests with the Executive Directors and senior managers. The risk management systems and internal controls are designed to allow the Society to achieve its corporate objectives in a controlled manner and remain within defined risk appetite statements. These systems and controls are designed to manage rather than eliminate risk. The Board reviews the effectiveness of the risk management systems and internal controls in a number of ways, including: • Board review and approval of Risk Appetite Statements at least annually, with monthly reporting relating to those statements; • A formal committee structure, including an Audit Committee (see below for more detail) and a Group Risk Committee. The minutes of the meetings of these Committees are reviewed by the full Board, the relevant Committee Chairman highlighting any key issues; • Regular reports and presentations to the Board by the Executive Directors; and • Monthly Board report on key business performance. The Society's internal audit function, with a dual reporting line to the Chief Executive and Chair of Audit Committee, provides independent assurance regarding the adequacy and effectiveness of internal controls across all Group activities.
C3 Audit Committee and Auditors The board should establish formal and transparent arrangements for considering how they should apply the corporate reporting and risk management and internal control principles and for maintaining an appropriate relationship with the company's auditor	The Board has an Audit Committee comprising four NEDs, all of whom are considered independent according to the criteria contained in the Code. The Board is satisfied that at least one member of the Committee has recent and relevant financial experience. The Chairman of the Audit Committee receives additional fees in recognition of his added responsibilities. The terms of reference of the Committee are available from the Group Secretary on request. The Society has a policy on the engagement of external auditors to supply non-audit services, which is operated across the Group and in tandem with the external auditors' own internal policy on providing non-audit services. The Society has a well established Whistleblowing Policy to enable staff to raise concerns in confidence about possible improprieties in matters of financial reporting or other issues. This policy has taken account of the Public Interest Disclosure Act 1998. During the year, the Committee received a report summarising all of the reports made under this Policy. There have been four meetings of the Committee during the financial year 2012/13. Executive Directors and other members of senior management (by invitation only) attended the meetings. Those employees who regularly attend include the Chief Executive, Group Finance Director, Group Risk Director and Head of Internal Audit. The Board receives regular reports on Committee meetings and also receives copies of the minutes of these meetings. During the last financial year, the Audit Committee: • Validated the integrity of the Group's financial statements (including formal announcements relating to such statements); • Reviewed and approved significant financial reporting issues and accounting policies/issues; • Reviewed the Group's internal controls; • Monitored and reviewed the effectiveness of the Group's Internal Audit function; • Recommended the reappointment of the external auditor (following a review of the external auditor's independence and objectivity and the effectiveness of the audit process), the remuneration and terms of engagement; • Confirmed that the Internal Audit function was appropriately resourced; and • Met privately with the Head of Internal Audit and the external auditors.
D1 Level and Components of Remuneration Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance **D2 Procedure** There should be formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration	The Board has established a Remuneration Committee, comprising four NEDs, which considers and makes recommendations to the Board on key remuneration decisions relating to Society staff who have been identified in the FCA's Remuneration Code as Code Staff. The Directors' Remuneration Report on pages 28 to 30 explains how the Society, through the Remuneration Committee and Board, approaches the remuneration of Directors and other executives. The Society is subject to the FCA's Remuneration Code, requiring the Society to have a remuneration policy which promotes effective risk management, supports business strategy, objectives and values and is in the long-term interests of the Society. During the last financial year, the Remuneration Committee: • Reviewed the Society's Remuneration Policy; • Recommended to the Board the Performance-Related Pay Scheme and awards under that Scheme; • Reviewed employee benefits arrangements; • Made recommendations to the Board in respect of the annual salary review; • Reviewed the employee benefits package and sales incentive schemes; and • Reviewed the terms of appointment and benefits of Code Staff.

The Code's Main Principles	What the Society does to meet the Principles
E1 Dialogue with Stakeholders There should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility of ensuring that a satisfactory dialogue with shareholders takes place	As a mutual, the Society is owned by its members; the Society seeks feedback from members in a number of ways, including: • Regular Members' ViewPoint events held around the branch network; • Assessing enquiries from the Society's contact centre and website; • Analysing the quantity and nature of customer complaints; • Customer research on specific topics; and • Customer satisfaction surveys and Mystery Shopper programme.
E2 Constructive Use of the AGM The board should use the AGM to communicate with investors and to encourage their participation	All members who are eligible to vote are sent a Summary Financial Statement and details of the Annual General Meeting (AGM) at least 21 days before the date of the meeting. Proxy forms are also included in the AGM mailing to allow those members who do not attend the meeting to cast their vote. Members are also able to submit their proxy form electronically. The Society uses independent scrutineers to count proxy votes received through the post and via the internet. All Board members are expected to be present at the AGM each year (except in the case of unavoidable absence). The Chairmen of the Audit, Remuneration, Group Risk and Nominations Committees are available to answer questions at the AGM.

Meetings of the Nominations Committee

The Nominations Committee which is chaired by the Society's Chairman, met on three occasions in the last financial year. The key matters considered by the Committee were:

- Membership of Board committees;
- Board performance evaluation arrangements;
- Content of the Board Procedures Manual;
- 2013 AGM election of Directors;
- NEDs reaching the end of their three year term of office; and
- NED development.

The terms of reference of the Committee, which is made up of NEDs, are available on request from the Group Secretary.

The attendance of individual Directors during the year, with the number of meetings each was eligible to attend shown in brackets, is set out below:

Attendance Records – Board and Board Committee Meetings

	Board	Nominations	Audit	Group Risk	Remuneration
Mark Nicholls	9 (9)	3 (3)			5 (5)
John Ainley	7 (9)	3 (3)			5 (5)
Mark Gibbard	9 (9)			8 (8)	
Claire Hafner	7 (9)		4 (4)		5 (5)
Andrew Jones	9 (9)			8 (8)	
Mark Preston	8 (9)			7 (8)	
Martin Ritchley	9 (9)	3 (3)	4 (4)	8 (8)	5 (5)
Richard Sommers	9 (9)	3 (3)	4 (4)	8 (8)	
Colin Walklin	8 (9)		4 (4)	8 (8)	
Jonathan Westhoff	9 (9)			8 (8)	

Mark Nicholls
Chairman
31 May 2013

Directors' Remuneration Report

Introduction

This Report sets out the Remuneration Policy (the Policy) for the Society's Directors and details their remuneration for the year to 31 March 2013.

The Policy takes account of areas of the UK Corporate Governance Code that are considered appropriate to building societies, the disclosure requirements of the third EU Capital Requirements Directive and the detailed requirements of the Financial Conduct Authority's (FCA's), formerly the Financial Services Authority's (FSA's), Remuneration Code (the Code).

Under the Code, the Society is required to identify those staff who are considered to have a material impact on the Society's risk profile. This includes all Executive and Non-Executive Directors, all members of the Society's Executive Committee (ExCo) and other senior individuals in the Treasury and Compliance areas. These individuals are defined as 'Code Staff'.

All eligible members receive this Report and are entitled to participate in an advisory vote on the Report at the 2013 Annual General Meeting.

The Report covers the following areas:

- Remuneration Committee membership and responsibilities;
- Remuneration Policy and Practice;
- Executive Director remuneration;
- Details of Executive Director service contracts; and
- Non-Executive Director fees.

Remuneration Committee membership and responsibilities

Membership

The members of the Remuneration Committee during the financial year 2012/13 were: John Ainley (Chair), Mark Nicholls, Martin Ritchley and Claire Hafner.

All members of the Committee are Non-Executive Directors. Under the Committee's terms of reference, at least one member of the Committee must also be a member of either the Group Risk Committee or Audit Committee.

In addition, the Society's Chief Executive, Group Finance Director, Group Risk Director and Head of Human Resources attend meetings by invitation.

The Committee is required to meet at least twice per year. During the year there were five meetings.

The Committee receives an annual report, prepared jointly by the Head of Legal, Compliance and Customer Relations and the Head of Internal Audit. This report provides information on whether any activity or behaviour by any individual has been observed that should affect their eligibility to participate in performance-related pay arrangements.

No member or invitee is present when their own remuneration is discussed.

The Terms of Reference for the Committee were last updated in January 2012 to reflect the Code. The Terms of Reference are available on request from the Group Secretary.

Responsibilities

The Committee is responsible for setting the policy on remuneration, overseeing the implementation and making recommendations to the Board in respect of remuneration arrangements for Executive Directors and other Code Staff.

During the year the Code was amended, resulting in the Society being categorised as a 'Proportionality Level 3' firm, meaning that the Society is not subject to all of the Code's requirements. Details of the Code can be found at www.fca.org.uk.

Following each meeting the Chairman of the Committee reports to the Board on all substantive issues discussed.

Remuneration Policy and Practice

At the start of the year the Committee reviewed and recommended to the Board the Society's Remuneration Policy, which has subsequently been updated in line with the Code requirements. The Policy is designed to promote appropriate behaviours and is aligned with the Society's risk appetite.

The Society's remuneration principles are as follows:

- The Policy is in line with the strategy, objectives and values of the Society, thereby aligning it with both short and long term interests;
- The policies, procedures, remuneration practices and performance-related payment schemes are consistent with the promotion of good and effective risk management and are structured in such a way as to discourage risk-taking which is outside the Society's risk appetite;
- All remuneration packages are designed such that the Society can attract and retain high calibre individuals;
- Performance measures for individuals are challenging and robust and measured on a consistent basis;
- Performance-related pay is performance dependent and able to be earned at virtually every level of the Society; and
- The Policy follows, as a minimum, the requirements of the Code for Proportionality Level 3 firms; any breaches or suspected breaches will be reported to the FCA.

The Policy provides the framework for the Committee to make remuneration decisions in relation to Executive Directors and other Code Staff.

The approach of the Remuneration Committee is to provide remuneration that is sufficient to attract, retain and motivate Executive Directors of a sufficient calibre, with full consideration of other stakeholders such as regulators and members.

Remuneration decisions are made on the basis of total compensation comprising salary, performance-related pay and benefits, ensuring an appropriate balance between the fixed and variable components of remuneration. The variable element of the remuneration package creates flexibility to allow for changes in current and future performance.

In 2010, in advance of the previous requirement of the Remuneration Code, the Society introduced the use of deferral in respect of performance-related pay. Following changes in the Code's proportionality levels, the requirement for the Society to defer an element of performance-related pay no longer applies. Despite this, the Board decided to continue with deferral as a requirement of the Executive Performance-Related Pay Scheme.

Before the payment of any deferred element, the Remuneration Committee undertakes a review to ensure that the payment remains appropriate.

Executive Director remuneration

The component parts of the remuneration package for Executive Directors are as follows:

a) Basic salary

Basic salary is determined by the Committee and reflects individual skills and experience as well as the responsibilities of the role.

b) Performance-related pay

Performance-related pay is used to incentivise Executive Directors to achieve the longer term goals of the Society and is based on a number of financial and non-financial measures. In the past year these measures related to:

- Financial performance;
- Income;
- Risk management (credit, conduct and operational);
- Customer service; and
- Employee satisfaction.

The maximum payable is 50% of basic salary. As a result of the Board's decision to go further than the requirements of the Code, 40% of any award made is deferred over a three year period. Deferred payments are made in equal instalments over the following three years and are subject to annual review and recommendation by the Committee and require approval by the Non-Executive members of the Board. Some or all of the deferred element can be reduced or cancelled by the Non-Executive members of the Board. All performance-related payments are non-pensionable.

c) Pension

No Executive Director is or has been a member of any of the Society's Pension Schemes, except Mr Jones who is a deferred member of the Society's defined benefit scheme from the time he was a member of staff between 1979 and 1985. Instead, Executive Directors receive a pension allowance of 25% of basic salary for Mr Westhoff and 20% for Mr Gibbard and Mr Jones.

d) Other benefits

All Executive Directors receive a fully expensed car or a car allowance, private medical cover for themselves and their family, life assurance and, with the exception of Mr Gibbard, a housing allowance.

Executive Director service contracts

The Society's policy in relation to the duration of contracts for the Executive Directors is that their contract would normally continue until termination by either party, subject to the required notice or until retirement. The service contract is terminable with twelve months' notice if given by the Society or six months' notice if given by the Director.

All new service contracts for Executive Directors are subject to approval by the Remuneration Committee.

Non-Executive Director fees

The level of remuneration for Non-Executive Directors reflects their responsibilities and time commitment for Board and Board Committees. Non-Executive Directors only receive fees, they do not participate in any performance-related awards, nor do they receive any pension provision or any other benefits. Non-Executive Director fees are reviewed annually by the Chairman and the Executive Directors. The fees for the Chairman are reviewed and recommended by the Remuneration Committee and approved by the Board. The Chairman is not present when his fees are being discussed.

New fee levels were applied in April 2010 and no increase in fees has been awarded since for either the Chairman or other Non-Executive Directors. The fees for the Deputy Chairman, whose duties include acting as Senior Independent Director, were reset in July 2010 at a level that reflects his responsibilities and membership of all four Board Committees.

Non-Executive Directors do not have service contracts or a notice period and have instead letters of engagement which set out their time commitment and responsibilities.

Non-Executive Director Fees (Audited)

Non-Executive Director	Date Appointed	Date Appointment Ceased	2012/13 £000	2011/12 £000
Mark Nicholls	01/01/10		**100**	100
John Ainley	18/05/11		**55**	53
Claire Hafner	01/09/11		**50**	29
Huw Davies	27/09/06	27/07/11	**-**	17
Lesley James CBE	01/01/01	27/07/11	**-**	18
Mark Preston	18/05/11		**50**	44
Martin Ritchley	01/09/09		**70**	70
Richard Sommers	01/10/09		**60**	60
Colin Walklin	20/07/11		**60**	42
Total			**445**	433

Executive Director Remuneration – 2012/13 (Audited)

Executive Director	**Basic Salary £000**	**Performance-Related Pay [1] £000**	**Pension £000**	**Other Benefits £000**	**Total £000**
Jonathan Westhoff	327	98	82	18	**525**
Mark Gibbard	262	86	52	22	**422**
Andrew Jones	185	60	37	16	**298**
Total	**774**	**244**	**171**	**56**	**1,245**

Executive Director Remuneration – 2011/12 (Audited)

Executive Director	Basic Salary £000	Performance-Related Pay [1] £000	Pension £000	Other Benefits £000	Total £000
Jonathan Westhoff (CEO from 25/05/11)	316	77	77	18	488
Mark Gibbard	262	71	52	22	407
Andrew Jones	185	57	37	16	295
Robert Sharpe [2] (until 25/05/11)	62	-	16	5	83
Total	825	205	182	61	1,273

Notes:

1 Included in the amounts shown above is an element that is subject to deferral. The table below headed 'Executive Director Deferred Performance-Related Pay Payable in Future Years' details the amount due for payment, subject to review by the Remuneration Committee at the appropriate time.

2 Mr Sharpe resigned from the Board on 25 May 2011 and received no payments or benefits in lieu of notice and no performance-related pay in respect of service between 1 April 2011 and 25 May 2011.

A proportion of the Executive Directors' performance-related pay has been deferred as shown in the table below. Payment of any deferred award is subject to review by the Remuneration Committee and may be reduced or cancelled as appropriate.

Executive Director Deferred Performance-Related Pay Payable in Future Years

		Deferral due			
Executive Director	**Deferred From**	**2012/13 £000**	**2013/14 £000**	**2014/15 £000**	**2015/16 £000**
Jonathan Westhoff	2010/11	30	-	-	-
	2011/12	10	10	10	-
	2012/13	-	13	13	13
Total		**40**	**23**	**23**	**13**
Mark Gibbard	2010/11	3	-	-	-
	2011/12	9	9	9	-
	2012/13	-	12	12	12
Total		**12**	**21**	**21**	**12**
Andrew Jones	2010/11	6	-	-	-
	2011/12	8	8	8	-
	2012/13	-	8	8	8
Total		**14**	**16**	**16**	**8**
Robert Sharpe	2010/11	49	-	-	-
Total		**49**	**-**	**-**	**-**

Deferred elements due in 2012/13 (shown in the table above) have been paid in full since 31 March 2013.

John Ainley
Chairman of Remuneration Committee
31 May 2013

Corporate Responsibility Report

The West Brom has always believed in the importance of having a positive impact on the communities it serves. This reflects the Society's position as a mutual organisation where creating and developing supportive relationships with the wider community, including our members and business partners, is essential to the West Brom's position as the largest building society in the Black Country and Birmingham.

Community

The Society's contribution to the community, and its potential for improving the lives of people facing disadvantage and difficulty, is illustrated in a variety of ways:

- Providing financial aid to local community and charitable groups;
- Organising fundraising activities for the Society's chosen charity; and
- Offering opportunities, as part of the Society's volunteer programme, for staff to participate in activities that benefit local people.

During the past year, several highlights demonstrate this community commitment:

- The well-established affinity partnership with the Diocese of Lichfield (the Mercian Community Trust) remains central to the Society's contribution to the work of charities concerned with alleviating hardship and disadvantage. In the last year, this covered such issues as health, the pressures on carers, childhood deprivation, dementia, and improving the educational prospects of young people from disadvantaged backgrounds.
- The Society operates several other affinity partnerships, which mainly have the purpose of supporting organisations focused on sport, recreation and health. These affinity relationships with West Bromwich Albion Football Club, Warwickshire County Cricket Club and Severn Valley Railway do a tremendous amount to enhance social and educational opportunities for children and young people.
- A particular source of pride to the Society is the Red Balloon Account, which supports the world-renowned facilities at Birmingham Children's Hospital.
- As a result of the Society's Community Counts campaign the West Brom directs financial support through its branch network to charities and community groups working at a grassroots level. The campaign targets support for organisations within the immediate vicinity of the Society's branches, so making it a very localised way of responding to social needs. Significantly, as a mutual organisation, it enables the Society's members to have a say in how the West Brom's support is allocated within their specific community. Since the start of the campaign, the Society, through its partnership with the Mercian Community Trust, has made financial contributions to some 75 much-needed organisations, covering a wide a range of issues, such as bereavement, people with learning difficulties, mental health, disability, support for older people with dementia, and domestic violence.
- Staff at the West Brom have a well-deserved reputation for the fundraising efforts they make each year on behalf of the Society's chosen charity. For the second year running, the staff decided to support Acorns Children's Hospice, which occupies a precious place for many people within the region because of the care and treatment it gives to children with life-limiting conditions. To date, that fundraising figure has surpassed £30,000 which, once again, illustrates the compassion and generosity of the Society's staff.
- Active support for the community means more than fundraising, which is why the Society's volunteering programme is invaluable in enabling staff to devote time and energy to local charities and community organisations. The main focus has been Acorns Children's Hospice with over 150 staff having taken part in a host of volunteering projects, such as gardening, decorating and telephone campaigning. There are other examples of individuals from the Society, who have volunteered for other community initiatives, usually concerned with developing the potential of young people in particularly deprived localities.

Environment

As the largest building society within the Black Country and Birmingham region, the West Brom recognises the impact its business operations can have on the environment. Accordingly, the Society is keen to minimise any harmful effects to the environment by rigorously assessing its carbon footprint and limiting unnecessary waste and energy. It has, therefore, been exploring a number of options, as in recycling, managing paper use, purchasing, storage and archiving.

In promoting responsible policies and practices in terms of environmental impact, the Society has taken a series of steps, notably:

- The Society is represented on the Sandwell Climate Change Partnership, which consists of organisations from the private and public sectors who have the collective aim of tackling the challenges encountered by the borough on the issue of climate change.
- The West Brom's procurement policy obliges us to review the environmental and ethical policies of prospective suppliers so that they are consistent with the Society's criteria, including assessing the supply chain and lifecycle of products and services.
- Recycling has always been a prominent element in the Society's environmental aspirations, particularly on more tangible commodities, such as waste paper and toner cartridges. This promotion of sustainable development is also visible in how certain consumables are sourced by the Society, for example, paper supplies. In addition, the Society continually evaluates any new consumables for their possible environmental ramifications.
- The planned new head office is a considerable undertaking where the Society is very conscious of its environmental responsibilities. This awareness is at the forefront of the West Brom's thinking on design and materials for the new building, where the Society is looking to achieve a high BREEAM rating, the world's leading design and assessment method for sustainable buildings. The Society is also aiming for a good Energy Performance Certificate (EPC) which will be aided by the quality of design and proposed heating and ventilating systems. Furthermore, the Society's travel plans for the new head office will also take into account the West Brom's responsibilities to the environment and the surrounding community.
- Operating in ways that take proper account of the Society's impact on the environment underpins the West Brom's determined outlook on corporate responsibility. Integral to this is the belief in adopting policies and practices that best promote more sustainable environmental practices, as in the plans for the Society's new head office, which can be seen as a symbol of an organisation that takes seriously its commitment to the environment and the immediate community.

Taxation

The statutory reported tax credit for the year is £4.4m (2011/12: £0.3m). This represents an effective tax rate of 47% (2011/12: 3%), which is higher than the statutory rate in the UK of 24% (2011/12: 26%). The higher rate is due principally to timing of the recognition of tax adjustments on our securitised entities, adjustments with respect to prior periods and the effect on deferred tax of the forthcoming change in the UK corporation tax rate from 24% to 23%.

Corporation tax rate change

A reduction in the UK Corporation tax rate from 24% (effective from 1 April 2012) to 23% (effective from 1 April 2013) was substantively enacted on 3 July 2012. As a result, the Group has written off £1m of its deferred tax asset through a debit to the Income Statement.

Total tax contribution

During 2012/13 the Group incurred taxes of £4.1m (2011/12: £5.4m) including £2.0m (2011/12: £3.4m) of irrecoverable VAT, which represents a cost to the Group charged to profit before tax as part of administrative expenses and depreciation.

Year to 31 March		
Taxes paid	**2013 £m**	2012 £m
Indirect taxes (Irrecoverable VAT)	**2.0**	3.4
Employment taxes (Employer's NI)	**2.1**	2.0
Total	**4.1**	5.4

In addition, the Group collected and remitted on behalf of HM Revenue & Customs a further £25.3m (2011/12: £26.8m).

Year to 31 March		
Taxes collected and remitted	**2013 £m**	2012 £m
Tax withheld at source (on savings accounts)	**19.4**	21.2
Payroll taxes (PAYE and Employee's NI)	**5.8**	5.6
Indirect taxes (Insurance Premium Tax and VAT)	**0.1**	-
Total	**25.3**	26.8

Independent Auditor's Report

Independent Auditor's Report to the members of West Bromwich Building Society

We have audited the Group and Society Annual Accounts of West Bromwich Building Society for the year ended 31 March 2013 set out on pages 34 to 89. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU.

This report is made solely to the Society's members, as a body, in accordance with section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditor

As explained more fully in the Directors' Responsibilities Statement set out on pages 22 to 23, the Directors are responsible for the preparation of Annual Accounts which give a true and fair view. Our responsibility is to audit, and express an opinion on, the Annual Accounts 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.

Scope of the audit of the Annual Accounts

A description of the scope of an audit of Annual Accounts is provided on the Financial Reporting Council's website at: **www.frc.org.uk/auditscopeukprivate.**

Opinion on Annual Accounts

In our opinion the Annual Accounts:

- Give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of affairs of the Group and of the Society as at 31 March 2013 and of the income and expenditure of the Group and of the Society for the year then ended; and
- Have been prepared in accordance with the requirements of the Building Societies Act 1986 and regulations made under it and, as regards the Group Annual Accounts, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Building Societies Act 1986

In our opinion:

- The Annual Business Statement and the Directors' Report have each been prepared in accordance with the applicable requirements of the Building Societies Act 1986 and regulations thereunder;
- The information given in the Directors' Report for the financial year for which the Annual Accounts are prepared is consistent with the accounting records and the Annual Accounts; and
- The information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Building Societies Act 1986 requires us to report to you if, in our opinion:

- Proper accounting records have not been kept by the Society; or
- The Annual Accounts are not in agreement with the accounting records; or
- We have not received all the information and explanations and access to documents we require for our audit.

Richard Gabbertas (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
One Snowhill
Snow Hill Queensway
Birmingham
B4 6GH
31 May 2013

Income Statements

for the year ended 31 March 2013

	Notes	**Group 2013 £m**	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Interest receivable and similar income	2	**161.1**	180.8	**155.4**	167.3
Interest expense and similar charges	3	**(127.4)**	(145.9)	**(130.3)**	(140.8)
Net interest receivable		**33.7**	34.9	**25.1**	26.5
Fees and commissions receivable		**5.6**	6.1	**3.4**	2.9
Other operating income	4	**4.3**	4.4	**0.5**	0.5
Total operating income		**43.6**	45.4	**29.0**	29.9
Fair value (losses)/gains on financial instruments	5	**(1.7)**	(3.0)	**1.0**	(2.9)
Net realised profits	6	**7.3**	5.2	**4.8**	5.2
Total income		**49.2**	47.6	**34.8**	32.2
Administrative expenses	7	**(39.3)**	(38.3)	**(32.4)**	(31.5)
Depreciation and amortisation	18,20	**(5.6)**	(4.7)	**(5.6)**	(4.6)
Operating profit/(loss) before impairments, provisions and revaluation losses		**4.3**	4.6	**(3.2)**	(3.9)
Losses on investment properties	19	**(0.2)**	(1.0)	**-**	-
Impairment losses on loans and advances	15	**(10.8)**	(10.5)	**(1.7)**	(3.2)
Provisions for liabilities – FSCS Levy	27	**(2.7)**	(2.9)	**(2.7)**	(2.9)
Provisions for liabilities – other	27	**–**	0.3	**-**	0.3
Loss before tax		**(9.4)**	(9.5)	**(7.6)**	(9.7)
Taxation	10	**4.4**	0.3	**2.5**	2.9
Loss for the financial year		**(5.0)**	(9.2)	**(5.1)**	(6.8)

The loss for the year derives wholly from continuing operations.

The notes on pages 41 to 89 form part of these accounts.

Statements of Comprehensive Income

for the year ended 31 March 2013

	Notes	Group 2013 £m	Group 2012 £m
Loss for the financial year		**(5.0)**	(9.2)
Other comprehensive income			
Available for sale investments			
Valuation gain taken to equity		**15.6**	10.5
Amounts transferred to Income Statement		**(4.8)**	(5.2)
Actuarial loss on retirement benefit obligations	32	**(1.7)**	(4.3)
Cash flow hedge gains taken to equity		**-**	0.1
Tax on items taken directly to equity	31	**(2.2)**	(0.5)
Other comprehensive income for the financial year, net of tax		**6.9**	0.6
Total comprehensive income for the financial year		**1.9**	(8.6)

	Notes	Society 2013 £m	Society 2012 £m
Loss for the financial year		**(5.1)**	(6.8)
Other comprehensive income			
Available for sale investments			
Valuation gain taken to equity		**15.6**	10.5
Amounts transferred to Income Statement		**(4.8)**	(5.2)
Actuarial loss on retirement benefit obligations	32	**(1.7)**	(4.3)
Cash flow hedge gains taken to equity		**-**	0.1
Tax on items taken directly to equity	31	**(2.2)**	(0.5)
Other comprehensive income for the financial year, net of tax		**6.9**	0.6
Total comprehensive income for the financial year		**1.8**	(6.2)

The notes on pages 41 to 89 form part of these accounts.

Statements of Financial Position

at 31 March 2013

	Notes	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Assets					
Cash and balances with the Bank of England	11	**392.3**	769.2	**392.3**	769.2
Loans and advances to credit institutions		**147.1**	117.5	**69.7**	50.9
Investment securities	12	**499.5**	924.5	**1,598.5**	2,056.4
Derivative financial instruments	13	**29.5**	64.5	**29.5**	81.7
Loans and advances to customers	14	**4,971.1**	5,373.6	**1,728.4**	1,896.3
Current tax assets		**-**	-	**0.2**	0.2
Deferred tax assets	21	**24.0**	25.7	**12.2**	12.2
Trade and other receivables	22	**2.8**	4.3	**2.3**	3.6
Investments	16	**-**	-	**2,292.7**	2,274.7
Intangible assets	17, 18	**7.9**	7.5	**7.3**	6.9
Investment properties	19	**112.5**	112.7	**-**	-
Property, plant and equipment	20	**16.5**	17.6	**16.5**	17.6
Retirement benefit assets	32	**0.4**	-	**0.4**	-
Total assets		**6,203.6**	7,417.1	**6,150.0**	7,169.7
Liabilities					
Shares	23	**4,652.2**	5,672.8	**4,652.2**	5,672.8
Amounts due to credit institutions		**28.5**	48.6	**28.5**	48.6
Amounts due to other customers	24	**193.0**	129.7	**485.5**	129.7
Derivative financial instruments	13	**99.4**	107.8	**80.4**	91.5
Debt securities in issue	25	**709.1**	927.4	**380.8**	702.0
Deferred tax liabilities	21	**4.3**	8.2	**0.4**	0.5
Trade and other payables	26	**12.5**	19.9	**11.1**	15.3
Provisions for liabilities	27	**6.8**	6.4	**6.8**	6.4
Retirement benefit obligations	32	**-**	0.4	**-**	0.4
Total liabilities		**5,705.8**	6,921.2	**5,645.7**	6,667.2
Equity					
Profit participating deferred shares	29	**173.7**	175.0	**173.7**	175.0
Subscribed capital	28	**74.9**	74.9	**74.9**	74.9
General reserves		**236.1**	241.1	**242.6**	247.7
Revaluation reserve		**3.7**	3.7	**3.7**	3.7
Available for sale reserve		**9.4**	1.2	**9.4**	1.2
Total equity attributable to members		**497.8**	495.9	**504.3**	502.5
Total liabilities and equity		**6,203.6**	7,417.1	**6,150.0**	7,169.7

The accounting policies and notes on pages 41 to 89 form part of these accounts.

Approved by the Board of Directors on 31 May 2013 and signed on its behalf by:

Mark Nicholls
Chairman

Jonathan Westhoff
Chief Executive

Mark Gibbard
Group Finance Director

Statements of Changes in Members' Interest

for the year ended 31 March 2013

Group	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2012	**175.0**	**74.9**	**241.1**	**3.7**	**1.2**	**-**	**495.9**
Loss for the financial year	(1.3)	-	(3.7)	-	-	-	**(5.0)**
Other comprehensive income for the period							
Available for sale investments: current year movement net of tax	-	-	-	-	8.2	-	**8.2**
Actuarial loss on retirement benefit obligations	-	-	(1.3)	-	-	-	**(1.3)**
Total other comprehensive income	**-**	**-**	**(1.3)**	**-**	**8.2**	**-**	**6.9**
Total comprehensive income for the year	**(1.3)**	**-**	**(5.0)**	**-**	**8.2**	**-**	**1.9**
At 31 March 2013	**173.7**	**74.9**	**236.1**	**3.7**	**9.4**	**-**	**497.8**

for the year ended 31 March 2012

Group	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2011	177.3	74.9	251.3	3.7	(2.6)	(0.1)	504.5
Loss for the financial year	(2.3)	-	(6.9)	-	-	-	(9.2)
Other comprehensive income for the period							
Available for sale investments: current year movement net of tax	-	-	-	-	3.8	-	3.8
Actuarial loss on retirement benefit obligations	-	-	(3.3)	-	-	-	(3.3)
Cash flow hedge gains taken to equity	-	-	-	-	-	0.1	0.1
Total other comprehensive income	-	-	(3.3)	-	3.8	0.1	0.6
Total comprehensive income for the year	(2.3)	-	(10.2)	-	3.8	0.1	(8.6)
At 31 March 2012	175.0	74.9	241.1	3.7	1.2	-	495.9

Under the terms of the profit participating deferred shares (PPDS), 25% of the annual post tax profits or (losses) are allocated against the PPDS reserve.
The notes on pages 41 to 89 form part of these accounts.

Statements of Changes in Members' Interest

for the year ended 31 March 2013

Society	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2012	**175.0**	**74.9**	**247.7**	**3.7**	**1.2**	**-**	**502.5**
Loss for the financial year	(1.3)	-	(3.8)	-	-	-	**(5.1)**
Other comprehensive income for the period							
Available for sale investments: current year movement net of tax	-	-	-	-	8.2	-	**8.2**
Actuarial loss on retirement benefit obligations	-	-	(1.3)	-	-	-	**(1.3)**
Total other comprehensive income	**-**	**-**	**(1.3)**	**-**	**8.2**	**-**	**6.9**
Total comprehensive income for the year	**(1.3)**	**-**	**(5.1)**	**-**	**8.2**	**-**	**1.8**
At 31 March 2013	**173.7**	**74.9**	**242.6**	**3.7**	**9.4**	**-**	**504.3**

for the year ended 31 March 2012

Society	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2011	177.3	74.9	255.5	3.7	(2.6)	(0.1)	508.7
Loss for the financial year	(2.3)	-	(4.5)	-	-	-	(6.8)
Other comprehensive income for the period							
Available for sale investments: current year movement net of tax	-	-	-	-	3.8	-	3.8
Actuarial loss on retirement benefit obligations	-	-	(3.3)	-	-	-	(3.3)
Cash flow hedge gains taken to equity	-	-	-	-	-	0.1	0.1
Total other comprehensive income	-	-	(3.3)	-	3.8	0.1	0.6
Total comprehensive income for the year	(2.3)	-	(7.8)	-	3.8	0.1	(6.2)
At 31 March 2012	175.0	74.9	247.7	3.7	1.2	-	502.5

Under the terms of the profit participating deferred shares (PPDS), 25% of the annual post tax profits or (losses) are allocated against the PPDS reserve.
The notes on pages 41 to 89 form part of these accounts.

Statements of Cash Flows

for the year ended 31 March 2013

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Net cash (outflow)/inflow from operating activities (see overleaf)	**(566.8)**	465.8	**(484.8)**	164.5
Cash flows from investing activities				
Purchase of investment securities	**(672.1)**	(2,018.8)	**(841.8)**	(2,018.8)
Proceeds from disposal of investment securities	**870.7**	2,201.4	**1,073.3**	2,234.9
Purchase of property, plant and equipment and intangible assets	**(5.0)**	(10.3)	**(5.0)**	(10.3)
Proceeds from disposal of property, plant and equipment	**0.2**	0.2	**0.2**	0.2
New funding to subsidiaries	**-**	-	**(125.5)**	(117.8)
Repayment of funding from subsidiaries	**-**	-	**107.5**	341.4
Net cash flows from investing activities	**193.8**	172.5	**208.7**	429.6
Cash flows from financing activities				
Issue of mortgage backed loan notes	**175.0**	-	**-**	-
Repayment of mortgage backed loan notes	**(67.3)**	(52.1)	**-**	-
Net repayment of other debt securities	**(318.2)**	(27.6)	**(318.2)**	(27.6)
Net cash flows from financing activities	**(210.5)**	(79.7)	**(318.2)**	(27.6)
Net (decrease)/increase in cash	**(583.5)**	558.6	**(594.3)**	566.5
Cash and cash equivalents at beginning of year	**1,133.8**	575.2	**1,067.2**	500.7
Cash and cash equivalents at end of year	**550.3**	1,133.8	**472.9**	1,067.2

For the purposes of the statements of cash flows, cash and cash equivalents comprise the following balances with less than 90 days maturity:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Cash in hand (including Bank of England Reserve account)	**386.8**	763.7	**386.8**	763.7
Loans and advances to credit institutions	**147.0**	116.1	**69.6**	49.5
Investment securities	**16.5**	254.0	**16.5**	254.0
	550.3	1,133.8	**472.9**	1,067.2

The Group is required to maintain certain mandatory balances with the Bank of England which, at 31 March 2013, amounted to £5.5m (2011/12: £5.5m). The movement in these balances is included within cash flows from operating activities.

Statements of Cash Flows (continued)

for the year ended 31 March 2013

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Cash flows from operating activities				
Loss on ordinary activities before tax from continuing activities	**(9.4)**	(9.5)	**(7.6)**	(9.7)
Movement in prepayments and accrued income	**0.9**	(0.8)	**1.4**	(0.8)
Movement in accruals and deferred income	**(3.6)**	4.3	**(2.0)**	2.0
Impairment losses on loans and advances	**10.8**	10.5	**1.7**	3.2
Depreciation and amortisation	**5.6**	4.7	**5.6**	4.6
Revaluations of investment properties, land and buildings	**0.2**	1.0	**-**	-
Movement in provisions for liabilities	**0.4**	(0.4)	**0.4**	(0.4)
Movement in derivative financial instruments	**26.6**	36.9	**41.1**	30.1
Movement in fair value adjustments	**(11.8)**	(15.0)	**(13.4)**	0.7
Change in retirement benefit obligations	**(2.5)**	(2.1)	**(2.5)**	(2.1)
Cash flows from operating activities before changes in operating assets and liabilities	**17.2**	29.6	**24.7**	27.6
Movement in loans and advances to customers	**387.5**	517.1	**168.1**	217.3
Movement in loans and advances to credit institutions	**1.3**	(1.1)	**1.3**	(1.1)
Movement in shares	**(1,009.5)**	(38.1)	**(1,009.5)**	(38.1)
Movement in deposits and other borrowings	**40.2**	(42.8)	**332.7**	(42.8)
Movement in trade and other receivables	**0.5**	2.3	**-**	0.2
Movement in trade and other payables	**(4.0)**	(3.3)	**(2.3)**	1.4
Tax received	**-**	2.1	**0.2**	-
Net cash (outflow)/inflow from operating activities	**(566.8)**	465.8	**(484.8)**	164.5

The notes on pages 41 to 89 form part of these accounts.

Notes to the Accounts for the year ended 31 March 2013

1. Accounting policies

The principal accounting policies applied consistently in the preparation of these consolidated Annual Accounts are set out below.

Basis of preparation

The Annual Accounts of the Group and the Society have been prepared in accordance with International Financial Reporting Standards (IFRS) and its interpretations as adopted by the EU and effective at 31 March 2013; and with those parts of the Building Societies (Accounts and Related Provisions) Regulations 1998 and the Building Societies Act 1986 applicable to societies reporting under IFRS.

The Annual Accounts have been prepared under the historical cost convention as modified by the revaluation of available for sale assets, derivatives, investment properties, property, plant and equipment and other financial assets at fair value through profit or loss.

The Annual Accounts are presented in pounds Sterling and, except where otherwise indicated, have been rounded to the nearest one hundred thousand.

Going concern

The Directors have prepared forecasts for the Group, including its capital position, for a period in excess of 12 months from the date of approval of these financial statements. The Directors have also considered the effect upon the Group's business, financial position, liquidity and capital of more pessimistic, but plausible, trends in its business using stress testing and scenario analysis techniques. The resultant forecasts and projections show that the Group will be able to operate at adequate levels of both liquidity and capital for the foreseeable future.

The Directors, therefore, consider that the Society and Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly they continue to adopt the going concern basis in preparing the financial statements. For further details see the Directors' Report on page 23.

Accounting developments

The following Accounting Standard amendments have been applied for the first time in 2012/13:

- Amendment to IFRS 7 'Financial Instruments: Disclosures' (October 2010) which extends the scope of IFRS 7 disclosures but does not change the recognition or measurement of transactions in the financial statements.
- IAS 12 (revised) 'Income Taxes'. The application of this revised standard does not have a material impact on the financial statements.

The following Accounting Standard amendments were issued but not effective for 2012/13:

- IAS 27 (revised) 'Separate Financial Statements'. The amendment is effective for annual periods beginning on or after 1 January 2013 and endorsed by the EU for application from 1 January 2014. The application of this revised standard is not expected to have a material impact on the financial statements.
- IAS 28 (revised) 'Investments in Associates and Joint Ventures'. The amendment is effective for annual periods beginning on or after 1 January 2013 and endorsed by the EU for application from 1 January 2014. The application of this revised Standard is not expected to have a material impact on the financial statements.
- IFRS 10 'Consolidated Financial Statements'. The new standard is effective for annual periods beginning on or after 1 January 2013 and endorsed by the EU for application from 1 January 2014. It introduces a single consolidation model for all entities based on control. The Group is reviewing the new standard and considering the associated impact on the Annual Report and Accounts.
- IFRS 11 'Joint Arrangements'. The new standard is effective for annual periods beginning on or after 1 January 2013 and endorsed by the EU for application from 1 January 2014. It requires a party to a joint arrangement to account for its rights and obligations in accordance with the type of joint arrangement. The application of this new standard is not expected to have a material impact on the financial statements.
- IFRS 12 'Disclosure of Interests in Other Entities'. The new standard is effective for annual periods beginning on or after 1 January 2013 and endorsed by the EU for application from 1 January 2014. It requires extensive disclosures with respect to interests in other entities. Other than the additional disclosure requirements, the application of this new standard is not expected to have a significant impact on the financial statements.
- IFRS 13 'Fair Value Measurement'. The new standard is effective for annual periods beginning on or after 1 January 2013 and replaces the existing IFRS guidance on fair value measurement with a single standard. Other than the additional disclosure requirements, the application of this new standard is not expected to have a significant impact on the financial statements.
- IAS 19 (revised) 'Employee Benefits'. The amendment is effective for annual periods beginning on or after 1 January 2013 and revises the recognition and presentation requirements for pensions and other post-retirement benefits. The application of this revised standard is not expected to have a material impact on the financial statements.
- IAS 1 (revised) 'Presentation of Financial Statements'. The amendment is effective for annual periods beginning on or after 1 July 2012 and revises the presentation of items of other comprehensive income. The application of this revised standard is not expected to have a material impact on the financial statements.
- Amendment to IFRS 7 'Financial Instruments: Disclosures' (December 2011). The amendment is effective for annual periods beginning on or after 1 January 2013 and requires disclosures about financial instruments which are offset in the Statement of Financial Position. The application of this revised standard is not expected to have a material impact on the financial statements.
- Amendment to IAS 32 'Financial Instruments: Presentation'. The amendment is effective for annual periods beginning on or after 1 January 2014 and clarifies requirements for offsetting financial assets and financial liabilities. The application of this revised standard is not expected to have a material impact on the financial statements.

The following Accounting Standard was neither adopted by the European Union nor effective for 2012/13:

- IFRS 9 'Financial Instruments'. This standard introduces new requirements with respect to classification and measurement of financial instruments. IFRS 9 is subject to EU endorsement, the timing of which is uncertain. The standard is currently expected to be effective for annual periods beginning on or after 1 January 2015. The Group is monitoring developments and considering the associated impact on the Annual Report and Accounts.

The Group did not early-adopt any of the above in the financial year ended 31 March 2013.

Basis of consolidation

The Group financial statements consolidate the financial statements of the Society and its subsidiary undertakings.

Subsidiaries

Subsidiaries are all entities controlled by the Society. Control exists when the Society has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of the subsidiaries are included in the results from the date that control commences until the date that control ceases.

1. Accounting policies (continued)

The purchase method of accounting has been adopted, under which the results of subsidiary undertakings acquired or disposed of in a year are included in the Income Statement from the date of acquisition or up to the date of disposal. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the Income Statement.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Society, investments in subsidiary undertakings are carried at cost less any charges for impairment.

Securitisation transactions

The Group has entered into securitisation transactions in which it sells mortgages to Special Purpose Entities (SPEs). In accordance with IAS 39, the Group continues to recognise securitised assets as loans and advances to customers. In subsequent periods, income from the securitised mortgages is recognised by the Group as disclosed below.

The equity of the SPEs created for these securitisations is not owned by the Group. However, to comply with the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004 and Standing Interpretations Committee (SIC) 12, the SPEs are included as subsidiaries in the consolidated financial statements.

During the year, the Society entered into a securitisation transaction in which it sold residential mortgages to an SPE. In accordance with IAS 39, the Society continues to recognise the securitised assets as loans and advances to customers and consequently also shows a deemed loan liability to the SPE. The deemed loan is included within amounts due to other customers.

Segmental reporting

IFRS 8, 'Operating Segments', requires operating segments to be identified on the basis of internal reports and components of the Group regularly reviewed by the chief operating decision maker to allocate resources to segments and to assess their performance. In terms of the Group, the chief operating decision maker has been deemed to be the Board of Directors.

Each segment is determined according to the distinguishable operating component of the Group that is regularly reviewed by the Group's chief operating decision maker and for which discrete financial information is available.

Information regarding the results of each reportable segment is included in note 39.

Interest receivable and expense

Interest receivable and expense are recognised in the Income Statement for all instruments measured at amortised cost or available for sale using the effective interest method. Interest income or expense on other financial instruments is recognised within interest receivable/interest payable. Interest on impaired financial assets is calculated by applying the original effective interest rate of the financial asset to the carrying amount as reduced by any allowance for impairment.

Effective interest rate

The effective interest rate is the method used to calculate the amortised cost of financial instruments and to recognise interest receivable or payable over the relevant period. The effective interest rate is the rate that exactly discounts estimated cash flows (excluding credit losses) to zero, through the expected life of the instrument. The main impact for the Group relates to mortgage advances where fees, such as application and arrangement fees, and costs are incorporated in the calculation. This has the effect of spreading these fees and costs over the expected life of the mortgage. Expected lives are estimated using historic data and management judgment and the calculation is adjusted when actual experience differs from estimates, with changes in deferred amounts being recognised immediately in the Income Statement.

Fees and commissions receivable and payable

Fees and commissions are generally recognised on an accruals basis when the service has been provided. Mortgage arrangement fees and other direct costs are deferred and recognised as an adjustment to the effective interest rate on the loan. Commissions and fees arising from negotiating or participating in the negotiation of a transaction with a third party are recognised on completion of the underlying transaction.

Investment properties

Investment properties are properties held for long-term rental yields and capital appreciation. Investment properties are carried in the Statement of Financial Position at fair value, representing open market value determined annually by a qualified internal valuer and at least every five years by an external valuer. Changes in fair values are recorded in the Income Statement in accordance with IAS 40 (revised 2003). Leasehold properties held for long-term rental yields are classified as investment properties and carried at fair value.

Financial instruments

In accordance with IAS 39, all financial assets and liabilities – which include derivative financial instruments – have to be recognised in the Statement of Financial Position and measured in accordance with their assigned category.

a) Financial assets

The Group allocates financial assets to the following IAS 39 categories: financial assets at fair value through profit or loss; loans and receivables; held to maturity investments; and available for sale financial assets. Management determines the classification of its financial instruments at initial recognition. Purchases and sales of financial assets are accounted for at settlement date.

Financial assets at fair value through profit or loss

This category comprises two sub-categories: financial assets classified as held for trading, and financial assets designated by the Group as at fair value through profit or loss upon initial recognition.

The Group uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risk arising from operational, financing and investment activities.

In accordance with its treasury policy and the Building Societies Act 1986, the Group does not hold or issue derivative financial instruments for trading purposes.

Derivative financial instruments (both assets and liabilities) are initially recognised and subsequently held at fair value in the Statement of Financial Position with changes in their fair value going through the Income Statement. However, by applying the hedge accounting rules set out in IAS 39, the changes in fair value of derivatives used to hedge particular risks can either be offset in the Income Statement or deferred to equity.

There are two types of hedge accounting strategies that the Group undertakes and these are summarised below:

- hedges of the fair value of recognised assets or liabilities or unrecognised firm commitments (fair value hedges); or
- hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedges).

Hedge accounting is used for derivatives designated in this way provided that certain criteria are met.

The Group documents, at the inception of any hedging transaction, the relationship between the hedging instrument and the hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

i) Fair value hedges – Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the Income Statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item, for which the effective interest method is used, is amortised to profit or loss over the remaining expected life of the previously hedged item.

ii) Cash flow hedges – The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised within the Statement of Comprehensive Income and the cash flow hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in the Income Statement. Amounts accumulated in equity are recycled to the Income Statement in the periods in which the hedged item will affect profit or loss (for example, when the forecast mortgage completion that is hedged takes place).

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in other operating income within the Income Statement. If a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the Income Statement.

iii) Derivatives that do not qualify for hedge accounting – Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the Income Statement. Certain derivatives are embedded within other non-derivative financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risk of the host instrument and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivative recognised in the Income Statement. Depending on the classification of the host instrument, the host instrument is then measured in accordance with the relevant IFRS standard.

The Group designates certain financial assets upon initial recognition as at fair value through profit or loss (fair value option). This designation cannot subsequently be changed. According to IAS 39, the fair value option is only applied when the following conditions are met:

- the application of the fair value option reduces or eliminates an accounting mismatch that would otherwise arise; or
- the financial asset is part of a portfolio of financial instruments which is risk managed and reported to senior management on a fair value basis; or
- the financial asset consists of a debt host and embedded derivative that must be separated.

To reduce accounting mismatch, the fair value option is applied to certain loans and receivables that are hedged with credit derivatives or interest rate swaps but for which the hedge accounting conditions of IAS 39 are not fulfilled. The loans would have been otherwise accounted for at amortised cost, whereas the derivatives are measured at fair value through profit or loss.

Financial assets for which the fair value option is applied are recognised in the notes to the accounts as financial assets designated at fair value. Fair value changes relating to financial assets designated at fair value through profit or loss are recognised as net gains on financial instruments designated at fair value through profit or loss.

Available for sale (AFS)
Available for sale investments are financial assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices or that are not classified as loans and receivables, held to maturity investments or financial assets at fair value through profit or loss. The Group's investment securities (e.g. certificates of deposit, gilts, etc) are classified as available for sale assets.

Available for sale financial assets are initially recognised at fair value, which is the cash consideration including any directly attributable transaction costs, and measured subsequently at fair value with gains and losses being recognised in the consolidated Statement of Comprehensive Income, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognised, whereupon the cumulative gains and losses previously recognised in other comprehensive income are reclassified to the Income Statement as a reclassification adjustment.

Interest is calculated using the effective interest method, and foreign currency gains and losses on monetary assets classified as available for sale are recognised in the consolidated Income Statement. Dividends on available for sale equity instruments are recognised in the Income Statement in dividend income when the Group's right to receive payment is established.

The Group assesses at each year end date whether there is objective evidence that a financial asset has been impaired. If an available for sale financial asset is determined to be impaired, the cumulative gain or loss previously recognised in the Statement of Comprehensive Income is recognised in the Income Statement. If in a subsequent period the fair value increases, the impairment loss is reversed with the amount of the reversal recognised in the Income Statement.

The fair values of available for sale assets are based on quoted prices or, if these are not available, valuation techniques developed by the Group. These include, but are not limited to, the use of discounted cash flow models, option pricing models and recent arm's length transactions.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- those that the Group intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; or
- those that the Group upon initial recognition designates as available for sale; or
- those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

Loans and receivables are initially recognised at fair value – which is the cash consideration to originate or purchase the loan including any directly attributable transaction costs – and measured subsequently at amortised cost using the effective interest method. Loans and receivables are reported in the Statement of Financial Position as loans and advances to credit institutions or customers or as investment securities. Interest on loans is included in the consolidated Income Statement and is reported as interest receivable and similar income. In the case of an impairment, the impairment loss is reported as a deduction from the carrying value of the loan and recognised in the Income Statement as impairment losses on loans and advances.

1. Accounting policies (continued)

Held to maturity financial assets
Held to maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity, other than:

- those that the Group upon initial recognition designates as at fair value through profit or loss;
- those that the Group designates as available for sale; and
- those that meet the definition of loans and receivables.

These are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method. Interest on held to maturity investments is included in the Income Statement and reported as interest receivable and similar income. In the case of an impairment, the impairment loss has been reported as a deduction from the carrying value of the investment and recognised in the Income Statement as net gains/(losses) on investment securities.

b) Financial liabilities
The Group's holding in financial liabilities is in financial liabilities at fair value through profit or loss, financial liabilities at amortised cost and hedging derivatives. Financial liabilities are derecognised when extinguished.

All financial liabilities including shares, deposits, debt securities in issue and subordinated liabilities held by the Group are recognised initially at fair value, being the issue proceeds, net of premia, discounts and directly attributable transaction costs incurred.

Financial liabilities are subsequently measured at amortised cost using the effective interest method, except for those financial liabilities, for example derivative liabilities, which are measured at fair value through profit or loss.

c) Financial instruments designated at fair value through profit or loss
Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below, and are so designated by management. The Group may designate financial instruments at fair value when the designation eliminates or significantly reduces measurement or recognition inconsistencies that would otherwise arise from measuring financial assets or financial liabilities, or recognising gains and losses on them, on different bases. Under this criteria, the main classes of financial instruments designated by the Group are where:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis; or
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

The fair value designation, once made, is irrevocable. Designation of financial assets and financial liabilities are recognised when the Group enters into the contractual provisions of the arrangements with counterparties and are normally derecognised when sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken directly to the Income Statement. Subsequently, the fair values are remeasured, and gains and losses from changes therein are recognised in net income from financial instruments designated at fair value. Note 30 sets out the amount of each class of financial asset or liability that has been designated at fair value through profit or loss.

d) Impairment of financial assets
Impairment of mortgage loans and advances
The Group assesses at each year end date whether there is objective evidence that a financial asset is impaired. Objective evidence of impairment can be defined as one or more events occurring after the initial recognition of the asset that have an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

The Group first assesses whether objective evidence of impairment exists for financial assets using the following criteria:

- Deterioration in payment status;
- Tenant failure;
- Expected future increase in arrears due to change in loan status;
- Breach of loan covenants; and
- Any other information discovered during annual review suggesting that a loss is likely in the short to medium term.

If the Group 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 for impairment, and for which an impairment loss is or continues to be recognised, are not included in a collective assessment of impairment.

A collective provision is made against a group of loans and advances where there is objective evidence that credit losses have been incurred but not identified at the reporting date. The collective impairment calculation takes into account a number of factors, including forbearance measures applied to the loans, such as term extensions and short-term interest only conversions.

If there is objective evidence of an impairment of loans and receivables, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. This calculation takes into account the Group's experience of default rates, loss emergence periods, the effect of regional movements in house prices based upon a recognised index and adjustments to allow for ultimate forced sales values and realisation costs. The amount of the loss is recognised in the Income Statement.

Where a loan is not recoverable, it is written off against the related provision for loan impairment once all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses recorded in the Income Statement.

Impairment losses on debt instruments
At each year end date the Group assesses whether or not there is objective evidence that individual debt instruments are impaired. In determining whether there is any objective evidence of impairment the Group takes into account a number of factors including:

- significant financial difficulties of the issuer or obligor;
- any breach of contract or covenants;
- the granting of any concession or rearrangement of terms;
- the disappearance of an active market;

- any significant downgrade of ratings; and
- any significant reduction in market value.

In some cases a significant adverse change in one of the above factors will cause the Group to determine that there is objective evidence of impairment. In other cases it may not be possible to identify a single event that identifies impairment. The Group may additionally determine that there is impairment where there are a number of factors contributing to that view.

Where the Group determines that there is objective evidence of impairment or that trigger events exist at the year end date, then, in the case of available for sale instruments, the cumulative gain or loss that had been recognised directly in reserves is removed from reserves and recognised in the Income Statement. In the case of held to maturity instruments an appropriate charge is made to the Income Statement.

If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be related to an event occurring after the impairment loss was recognised through the Income Statement, the impairment loss shall be reversed, with the amount of the reversal recognised through the Income Statement.

e) Derecognition of financial assets and liabilities

The Group's policy is to derecognise financial assets when the contractual right to the cash flows from the financial asset expires. The Group also derecognises financial assets that it transfers to another party provided the transfer of the asset also transfers the right to receive the cash flows of the financial asset and substantially all the risks and rewards of ownership.

The Group derecognises financial liabilities only when the obligation specified in the contract is discharged, cancelled or has expired.

f) Determination of fair value

The Group determines fair values by the three tier valuation hierarchy as defined within IAS 39 and Amendments to IFRS 7 'Financial Instruments: Disclosures'.

Level 1: For financial instruments traded in active markets, the determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations. This includes listed equity securities and quoted debt instruments on major exchanges (for example, FTSE, NYSE) and broker quotes from Bloomberg and Reuters.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indications that a market is inactive are when there is a wide bid-offer spread or significant increase in the bid-offer spread or there are few recent transactions.

Level 2: For all other financial instruments, fair value is determined using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques, using inputs (for example, LIBOR yield curve, FX rates, volatilities and counterparty spreads) existing at the reporting dates.

The Group uses widely recognised valuation models for determining fair values of non-standardised financial instruments of lower complexity, such as options or interest rate and currency swaps. For these financial instruments, inputs into models are generally market observable.

Level 3: Fair value is determined using valuation techniques where significant inputs are not based on observable market data. None of the Group's financial assets or liabilities are valued using this technique.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

g) Sale and repurchase agreements

Investment and other securities may be lent or sold subject to a commitment to repurchase them. Where substantially all of the risks and rewards of ownership remain with the Group, the securities are retained on the Statement of Financial Position. The counterparty liability is recognised separately in the Statement of Financial Position as appropriate. The difference between the sale and repurchase price is accrued over the life of the agreements.

Intangible assets

Goodwill

Goodwill arising on the acquisition of subsidiary undertakings, joint ventures, associates or businesses represents the excess of the fair value of consideration over the fair value of identifiable net assets and contingent liabilities acquired at the date of acquisition. In accordance with IFRS 3, 'Business Combinations', goodwill is not systematically amortised but is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised in the Income Statement and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's applicable cash generating units. Each unit is tested at least annually and reviewed for impairment indicators at each reporting date, with a further impairment test performed if indicators deem necessary. The impairment test compares the carrying value of goodwill to the higher of its fair value less costs of sale and its value in use. The value in use calculations are carried out by discounting the future cash flows of the cash generating unit.

On the sale of a subsidiary undertaking, the profit or loss on sale is calculated after charging or crediting the net book value of any related goodwill. Negative goodwill arising on an acquisition would be recognised directly in the Income Statement.

Computer software

Computer software which is not an integral part of the related hardware is recorded as an intangible asset. The identifiable and directly associated external and internal costs of acquiring and developing software are capitalised where the software is controlled by the Group, and where it is probable that future economic benefits that exceed its cost will flow from its use over more than one year. Intangible assets are held at amortised cost, amortisation is charged to the Income Statement on a straight line basis over the estimated useful life of 3 to 7 years; they are subject to regular impairment reviews. Costs associated with maintaining software are recognised as an expense when incurred.

Other acquired intangible assets

Other acquired intangible assets are capitalised if they can be separately identified from goodwill. Their useful lives are based on the period for which they are expected to generate economic benefits. If there are any signs of a decrease in value the asset will be subject to impairment testing. If there is no foreseeable limit on this period, their life is deemed to be indefinite and the asset tested at each reporting date for impairment.

These intangible assets are held at amortised cost, amortisation is charged to the Income Statement on a straight line basis over the estimated useful life of 20 years.

1. Accounting policies (continued)

Property, plant and equipment

Land and buildings comprise mainly branches and offices. All property is stated at valuation less depreciation and plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. All gains on the revaluation of property are recognised in the revaluation reserve when they arise.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the Income Statement during the financial period in which they are incurred.

Land is not depreciated. Depreciation on other assets is calculated using the straight line method (unless otherwise stated) to allocate their cost less their residual values over their estimated useful lives, as follows:

Buildings	Up to 50 years
Short leasehold properties	Annual instalments over the period of the lease
Equipment, fixtures and fittings and motor vehicles	
• Office equipment	3 to 7 years
• Computer equipment	3 to 7 years
• Motor vehicles	25% per annum reducing balance
• Refurbishments	5 to 10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each year end date. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the Income Statement.

Leases

The leases entered into by the Group are primarily operating leases. The total payments made under operating leases are charged to the Income Statement on a straight line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Cash and cash equivalents

For the purposes of the cash flow statement, cash comprises cash in hand and loans and advances to credit institutions repayable on demand. Cash equivalents comprise highly liquid investments that are convertible into cash with an insignificant risk of changes in value, with maturities of 90 days or less.

Taxation

Tax on the profits for the year comprises current tax and deferred tax. Income tax is recognised in the Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity or items recognised in other comprehensive income, where it is recognised in the Statement of Comprehensive Income.

Current tax is the expected tax payable on the taxable income for the year, using the tax rate which applies to the accounting period ending at the date of the Statement of Financial Position, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided in full, using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is determined using tax rates (and laws) that have been substantively enacted by the year end date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.

Employee benefits

The Group provides both a defined benefit scheme (closed to new employees from 2002/3 and accruals from 2009/10) and a defined contribution scheme on behalf of staff and Directors. The defined benefit scheme is funded by contributions from the Society at rates assessed by independent actuaries. These contributions are invested separately from the Group's assets. The Scheme assets are measured at market value at each year end date and the liabilities are measured using the projected unit valuation method, by qualified actuaries, discounted using a corporate bond rate. The resulting pension scheme surplus or deficit is recognised immediately in the Statement of Financial Position, net of deferred tax.

Actuarial gains and losses are recognised in full in the period in which they occur. As permitted by the revised standard, actuarial gains and losses are recognised outside profit or loss and presented in other comprehensive income.

Following the curtailment, any increase in the present value of the liabilities of the defined benefit scheme is expected to arise only from changes in actuarial assumptions surrounding the existing liabilities which would be charged to the Statement of Comprehensive Income. The expected return on the defined benefits scheme's assets and the increase in the scheme's liabilities, arising from the passage of time, are disclosed as a pension finance charge/income. Any resulting actuarial gains or losses, that is gains or losses arising from differences in the expected return on scheme assets compared to the actual return and changes in assumptions, or factors which affect those assumptions, used in measuring the scheme liabilities, are recognised immediately in the Statement of Comprehensive Income.

For defined contribution plans, the contributions are recognised as employee benefit expense in the Income Statement when they are due, in accordance with the rules of the scheme. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

Critical accounting estimates and judgments in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Pensions

The Group operates a defined benefit pension scheme. Significant judgments (on areas such as future interest and inflation rates and mortality rates) have to be exercised in estimating the value of the assets and liabilities of the scheme.

These judgments, which are based upon the Board receiving external advice from the scheme actuaries, are outlined in note 32 to the Accounts.

Impairment losses on loans and advances

The creation of impairment provisions for a portfolio of mortgage loans is inherently uncertain and requires the exercise of a significant degree of judgment. Provisions are calculated using historic default and loss experience, but require judgment to be exercised in predicting economic conditions (e.g. interest rates and house prices), customer behaviour (e.g. default rates) and the length of time before impairments are identified (emergence period). The most critical estimate is of the level of house prices where a variance of 10% equates to £1.2m of provision. Other sensitivities include the emergence period, where a variance of six months equates to £0.7m, and the loss given default rate, where a 10% variance equates to £0.4m of provision.

Impairment of treasury investments

Treasury investments are regularly reviewed for objective evidence of impairment. In determining whether objective evidence exists, the Group considers, amongst other factors, current market conditions, fair value volatility, appropriateness of valuation techniques and the financial stability of the counterparty.

Effective interest rate

The calculation of an effective interest rate requires the Group to make assumptions around the expected lives of mortgages and the likely levels of early repayment fees (ERFs) to be received. Management regularly reviews these assumptions and compares with actual results.

If the average lives of the mortgages were to increase by 5%, the carrying value of mortgages would change by £3.2m with a corresponding change to income.

Investment properties

The calculation of the fair value of investment properties involves house price assumptions which are regularly reviewed by management.

If house prices were to change by 5%, the carrying value of the investment properties would change by £5.6m with a corresponding change to income.

Financial Services Compensation Scheme (FSCS)

Following FSA guidance, the Society provides for an estimate of the management expense levy payable for those years triggered by the reporting date. The amount provided by the Group is based upon the following factors:

- The FSCS' estimate of the total management expense levy;
- The Directors' estimate of the Group's share of qualifying deposits; and
- The Directors' estimate of future interest rates.

The impact of a 1% increase in the estimate of 12 month LIBOR rate would increase the provision by £0.9m and vice versa.

Taxation

Significant estimates are required in determining the provision for corporation tax. There are a number of transactions for which the final tax determination is uncertain at the year end date.

Fair value of derivatives and financial assets

The most reliable fair values of derivative financial instruments and available for sale assets are quoted market prices in an actively traded market. Where there is no active market, valuation techniques are used. Techniques adopted include valuation models used to calculate the present value of expected future cash flows, and options pricing models, if market values are not available. These techniques make use of observable market data and hence fair value estimates can be considered to be reliable. Where inputs are not observable they may be based on historic data. Changes in assumptions used in the models could affect the reported fair value of derivatives and available for sale assets.

Where previously active markets no longer provide prices, other market sources are monitored, such as real-time market information, custodian and independent financial institution valuations, and management judgment is exercised in determining fair values for these or similar instruments.

Basis risk derivatives are valued using discounted cash flow models, using observable market data and will be sensitive to benchmark interest rate curves.

Deferred tax assets

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. The recognition of the deferred tax asset is dependent upon the projection of future taxable profits and future reversals of existing taxable temporary differences and it is necessary for management to evaluate whether the deferred tax asset has arisen due to temporary factors or is instead indicative of a permanent decline in earnings.

Based on its analysis, management has determined that the tax losses held by the Society and various other Group Companies primarily result from the recent economic downturn. The housing and credit market conditions in existence during the UK recession led to increases in credit losses and contracting margins, with higher unemployment levels also leading to higher credit losses. Management has made detailed forecasts of future taxable income in order to determine that profits will be available to offset the deferred tax asset. These projections are based on business plans, future capital requirements and the current economic situation. They include assumptions about the depth and severity of potential further house price depreciation and about the UK economy, including unemployment levels and their related impact on credit losses.

The assumptions surrounding future expected credit losses and increases in the Bank Rate of interest represent the most subjective areas of judgment in management's projections of future taxable profits. Management's forecasts support the assumption that it is probable that the results of future operations will generate sufficient taxable income to utilise the deferred tax assets and it is on this basis that the deferred tax assets have been recognised. Deferred tax has been recognised at 23%, being the rate substantively enacted at the date of the Statement of Financial Position.

1. Accounting policies (continued)

Securitisation transactions

In order to determine whether the Society controls a Special Purpose Entity (SPE) or not, the Society has to make judgments about risks and rewards and assess the ability to make operational decisions for the SPE in question. In many instances, elements are present that, considered in isolation, indicate control or lack of control over an SPE, but when considered together make it difficult to reach a clear conclusion. When assessing whether the Group has to consolidate an SPE it evaluates a range of factors. The following are the prime factors that are considered and the applicable accounting treatment in each case:

- When the Group, in substance, controls the entity to which financial assets have been transferred, the entity is included in these consolidated financial statements and the transferred assets are recognised in the Group's Statement of Financial Position;
- When the Group transfers financial assets to an unconsolidated entity and it retains substantially all of the risk and rewards relating to the transferred assets, the transferred assets are recognised in the Group's Statement of Financial Position;
- When the Group transfers substantially all the risks and rewards relating to the transferred financial assets to an unconsolidated entity, the assets are derecognised from the Group's Statement of Financial Position; and
- When the Group neither transfers nor retains substantially all the risks and rewards relating to a transferred financial asset and it retains control of the transferred asset, the Group continues to recognise the transferred financial asset to the extent of its continuing involvement in that transferred financial asset. Details of the Group's securitisation activities are given in note 14.

2. Interest receivable and similar income

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
On loans fully secured on residential property	**113.8**	127.0	**47.3**	69.4
On deemed loans	**-**	-	**13.2**	-
On other loans				
Connected undertakings	**-**	-	**77.3**	85.3
Loans fully secured on land	**51.4**	63.7	**1.9**	0.6
On investment securities	**12.7**	15.9	**26.0**	27.7
On other liquid assets	**2.5**	3.0	**2.0**	2.3
Net expense on derivative financial instruments	**(19.3)**	(28.8)	**(12.3)**	(18.0)
Total interest income	**161.1**	180.8	**155.4**	167.3
Interest receivable includes:				
Income from fixed income securities	**9.1**	14.7	**9.1**	14.7

Included within interest receivable and similar income is interest accrued on impaired residential mortgage assets: Group £3.2m (2011/12: £4.5m) and Society £2.4m (2011/12: £1.8m) and interest accrued on impaired commercial mortgage assets: Group £20.4m (2011/12: £19.7m) and Society £nil (2011/12: £nil).

3. Interest expense and similar charges

	Group 2013 £m	Group 2012* £m	Society 2013 £m	Society 2012* £m
On shares held by individuals	**113.6**	125.1	**113.6**	125.1
On deposits from banks and other deposits	**16.0**	33.9	**7.4**	28.8
On deemed loans	**-**	-	**11.5**	-
Net income on derivative financial instruments	**(2.2)**	(13.1)	**(2.2)**	(13.1)
Total interest expense	**127.4**	145.9	**130.3**	140.8

* The prior year figures have been recategorised within interest expense for consistency of presentation with the current year.

4. Other operating income

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Other operating income includes:				
Net rent receivable on investment property	**4.0**	3.8	**-**	-
Pension fund income (note 32)	**0.4**	0.7	**0.4**	0.7
Other	**(0.1)**	(0.1)	**0.1**	(0.2)
Total other operating income	**4.3**	4.4	**0.5**	0.5

5. Fair value (losses)/gains on financial instruments

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Derivatives designated as fair value hedges	**(1.0)**	(24.0)	**(22.2)**	(17.4)
(Loss)/gain on hedged items attributable to hedged risk	**(0.4)**	21.3	**20.9**	14.8
Fair value losses on hedge accounting	**(1.4)**	(2.7)	**(1.3)**	(2.6)
Other derivatives	**(0.3)**	(0.3)	**2.3**	(0.3)
Total fair value (losses)/gains on financial instruments	**(1.7)**	(3.0)	**1.0**	(2.9)

6. Net realised profits

Net realised profits arise on the sale of treasury instruments. The Society is required to periodically sell a proportion of its liquid assets to prove that they remain liquid. The Society also takes opportunities to realise an improvement in the underlying market value of assets without impacting the core business. By their nature these sources of income are highly variable.

7. Administrative expenses

	Group 2013 £m	Group 2012* £m	**Society 2013 £m**	Society 2012 £m
Staff costs				
Wages and salaries	**22.2**	21.0	**21.0**	19.6
Social security costs	**2.1**	2.0	**1.9**	1.9
Other pension costs	**1.1**	1.1	**1.0**	1.1
Rental charges payable under operating leases	**0.5**	0.5	**0.5**	0.5
Other administrative expenses	**13.4**	13.7	**8.0**	8.4
	39.3	38.3	**32.4**	31.5
Other administrative expenses include:				
Remuneration of auditor				
Audit of these financial statements	**0.1**	0.1	**0.1**	0.1
Audit of the subsidiary financial statements	**0.1**	0.1	**-**	-

* The prior year figures have been recategorised within administrative expenses for consistency of presentation with the current year.

8. Employee numbers

	Group 2013	Group 2012	**Society 2013**	Society 2012
The average number of employees employed throughout the year was:				
Full time	**637**	623	**631**	612
Part time	**124**	129	**122**	128
	761	752	**753**	740
Building Society				
Central administration	**483**	471	**483**	471
Branches	**270**	269	**270**	269
Subsidiaries	**8**	12	**-**	-
	761	752	**753**	740

9. Directors' emoluments

Total Directors' emoluments amounted to £1.690m (2011/12: £1.706m). Full details are given in the Directors' Remuneration Report on pages 28 to 30.

10. Taxation

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
UK corporation tax at 24% (2011/12: 26%)	**(2.0)**	(1.0)	**(2.0)**	(1.0)
Corporation tax – adjustment in respect of prior years	**-**	-	**(0.2)**	(0.3)
Total current tax	**(2.0)**	(1.0)	**(2.2)**	(1.3)
Deferred tax				
Current year	**(1.0)**	(0.2)	**1.0**	(0.3)
Adjustment in respect of prior periods	**(1.4)**	0.9	**(1.3)**	(1.3)
Tax on loss on ordinary activities	**(4.4)**	(0.3)	**(2.5)**	(2.9)

UK corporation tax has been calculated at the applicable prevailing rate.

10. Taxation (continued)

Further information about deferred tax is presented in note 21.

The tax credit is reconciled to the loss before tax in the Income Statement as follows:

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Loss before tax	**(9.4)**	(9.5)	**(7.6)**	(9.7)
Loss before tax multiplied by the UK standard rate of tax of 24% (2011/12: 26%)	**(2.3)**	(2.5)	**(1.8)**	(2.5)
Effects of:				
Income not taxable and expenses not deductible for tax purposes	**(1.4)**	0.3	**0.3**	0.3
Changes to tax rate	**0.9**	1.4	**0.5**	0.9
Adjustment in respect of prior years	**(1.4)**	0.9	**(1.5)**	(1.6)
Revaluation	**(0.2)**	(0.4)	**-**	-
Tax credit	**(4.4)**	(0.3)	**(2.5)**	(2.9)

11. Cash and balances with the Bank of England

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Cash in hand	**2.3**	2.8	**2.3**	2.8
Cash ratio deposit with the Bank of England	**5.5**	5.5	**5.5**	5.5
Other deposits with the Bank of England	**384.5**	760.9	**384.5**	760.9
	392.3	769.2	**392.3**	769.2

Cash ratio deposits are mandatory deposits with the Bank of England which are not available for use in the Group's day to day operations. Cash in hand and the mandatory deposit with the Bank of England are non-interest bearing.

12. Investment securities

	Group 2013 £m	Group 2012 £m	**Society 2013 £m**	Society 2012 £m
Investment securities: available for sale				
listed	**499.5**	717.0	**499.5**	717.0
unlisted	**-**	207.5	**-**	207.5
Investment securities: held to maturity				
listed	**-**	-	**1,099.0**	1,131.9
Total investment securities	**499.5**	924.5	**1,598.5**	2,056.4

In accordance with IAS39, available for sale investment securities are stated at fair value and held to maturity investment securities are stated at amortised cost. Gains/(losses) on disposal of investment securities are disclosed as net realised profits on the face of the Income Statement.

12. Investment securities (continued)

The movement in investment securities may be summarised as follows:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
At beginning of year	**924.5**	918.6	**2,056.4**	2,084.0
Additions	**684.1**	2,267.7	**853.8**	2,267.7
Disposals (sale and redemption)	**(1,124.7)**	(2,272.3)	**(1,327.3)**	(2,305.8)
Gains from changes in fair value	**15.6**	10.5	**15.6**	10.5
At end of year	**499.5**	924.5	**1,598.5**	2,056.4

The Directors consider that the primary purpose for holding investment securities is prudential. The investment securities are held as liquid assets with the intention of use on a continuing basis in the Group's activities.

At 31 March 2013, £337.1m (2011/12: £207.6m) of Group investment securities and £0.1m (2011/12: £1.4m) of cash were pledged as collateral under sale and repurchase agreements. All sale and repurchase transactions are conducted in line with market standard terms and conditions as defined in ISMA PSA Global Master Repurchase Agreements.

Included within investment securities are £18.4m of residential mortgage backed securities which have a registered charge on them in favour of the Society pension scheme. The charge was registered on 27 March 2013. The future cash flows from these assets will be used as contributions by the Society to the pension scheme estimated at £3m per year.

13. Derivative financial instruments

A description of the derivative financial instruments used by the Group for hedging purposes is given in note 35.

The fair values of derivative instruments held at 31 March 2013 are set out below. The other derivatives held for hedging are held for economic hedging purposes.

Group	**Notional principal amount 2013 £m**	**Fair values Assets 2013 £m**	**Fair values Liabilities 2013 £m**
Derivatives held for hedging			
Derivatives designated as fair value hedges	**1,052.0**	**6.5**	**(91.1)**
Other derivatives held for hedging	**987.1**	**23.0**	**(8.3)**
Total derivative assets/(liabilities) held for hedging	**2,039.1**	**29.5**	**(99.4)**

Society	**Notional principal amount 2013 £m**	**Fair values Assets 2013 £m**	**Fair values Liabilities 2013 £m**
Derivatives held for hedging			
Derivatives designated as fair value hedges	**979.4**	**6.5**	**(80.1)**
Other derivatives held for hedging	**637.9**	**23.0**	**(0.3)**
Total derivative assets/(liabilities) held for hedging	**1,617.3**	**29.5**	**(80.4)**

Group	Notional principal amount 2012 £m	Fair values Assets 2012 £m	Fair values Liabilities 2012 £m
Derivatives held for hedging			
Derivatives designated as fair value hedges	1,821.3	19.1	(87.2)
Other derivatives held for hedging	547.8	45.4	(20.6)
Total derivative assets/(liabilities) held for hedging	2,369.1	64.5	(107.8)

Society	Notional principal amount 2012 £m	Fair values Assets 2012 £m	Fair values Liabilities 2012 £m
Derivatives held for hedging			
Derivatives designated as fair value hedges	1,671.2	19.1	(60.1)
Other derivatives held for hedging	640.5	62.6	(31.4)
Total derivative assets/(liabilities) held for hedging	2,311.7	81.7	(91.5)

At 31 March 2013, £70.0m (2011/12: £49.4m) of cash was pledged as collateral against derivative financial instruments.

14. Loans and advances to customers

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Loans and receivables				
Loans fully secured on residential property	**4,004.5**	4,319.9	**1,716.6**	1,885.4
Other loans				
Loans fully secured on land	**990.3**	1,062.8	**31.6**	30.2
Other loans	**0.1**	0.2	**-**	-
	4,994.9	5,382.9	**1,748.2**	1,915.6
At fair value through profit or loss				
Other loans				
Loans fully secured on land	**70.5**	89.4	**-**	-
	5,065.4	5,472.3	**1,748.2**	1,915.6
Less: impairment provisions	**(94.3)**	(98.7)	**(19.8)**	(19.3)
	4,971.1	5,373.6	**1,728.4**	1,896.3

Certain residential and commercial mortgage balances are used to secure external funding as follows:

Group	Assets pledged 2013 £m	Secured funding 2013 £m	Assets pledged 2012 £m	Secured funding 2012 £m
Securitisations	**350.0**	**328.3**	262.8	225.4

Included within loans and advances to customers are £216.6m (2011/12: £399.2m) of commercial mortgage balances and £1,228.9m (2011/12: £976.5m) of residential mortgage balances that the Group has sold to bankruptcy remote special purpose entities (SPEs). The SPEs have been funded by issuing mortgage backed securities (MBSs) of which £1,103.2m (2011/12: £1,137.2m) are held by the Group.

The Group has made subordinated loans to the SPEs to provide some level of credit enhancement to the MBSs. In future periods the Group will earn interest income on the subordinated loans and fees for managing the loans. The Group will earn deferred consideration once the cash flows generated by the SPEs have been used to pay interest and capital to the holders of the MBSs. Since the Group maintains substantially all of the risks (key risk being an exposure to credit risk through the subordinated loan agreements) and rewards emanating from the mortgages, they have been retained on the Group's Statement of Financial Position in accordance with IAS 39.

15. Allowance for losses on loans and advances

	Loans fully secured on residential property		Loans fully secured on land		Total		
Group	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
At 1 April 2012	31.0	9.5	43.6	14.6	74.6	24.1	**98.7**
Amounts written off	(5.4)	-	(11.6)	-	(17.0)	-	**(17.0)**
Charge/(Credit) for the year comprising:							
Provision/(Release) for loan impairment	8.2	(1.2)	11.3	(5.5)	19.5	(6.7)	**12.8**
Provision/(Release) in excess of the securitisation first loss	-	-	4.1	(2.3)	4.1	(2.3)	**1.8**
Change in carrying value of debt securities in issue	-	-	(4.1)	2.3	(4.1)	2.3	**(1.8)**
Adjustments to provisions resulting from recoveries	(1.8)	-	(0.2)	-	(2.0)	-	**(2.0)**
Charge/(Credit) for the year	6.4	(1.2)	11.1	(5.5)	17.5	(6.7)	**10.8**
Non-recourse finance on securitised advances	-	-	4.1	(2.3)	4.1	(2.3)	**1.8**
At 31 March 2013	**32.0**	**8.3**	**47.2**	**6.8**	**79.2**	**15.1**	**94.3**

Included within loans fully secured on residential property are loans originated through the commercial division. At 31 March 2013, the provision against these loans totalled £8.8m (2011/12: £9.2m), with a net charge for the year of £1.1m (2011/12: £3.4m). The total provision balance relating to the commercial division is £62.8m (2011/12: £67.4m), with a charge for the year of £6.7m (2011/12: £6.2m).

The charge for the year includes impairments of £1.8m (2011/12: £13.5m) against loans in securitised entities, Sandwell Commercial Finance No.1 Plc: £2.3m credit (2011/12: £5.3m charge) and Sandwell Commercial Finance No. 2 Plc: £4.1m charge (2011/12: £8.2m charge). The loss from these impairments is borne by the external loan note holders as it exceeds the first loss exposure held by the Group. The carrying value of the external loan notes has been adjusted by an equivalent amount.

15. Allowance for losses on loans and advances (continued)

Society	**Loans fully secured on residential property** Individual £m	Collective £m	**Loans fully secured on land** Individual £m	Collective £m	**Total** Individual £m	Collective £m	**Total £m**
At 1 April 2012	12.4	6.9	-	-	12.4	6.9	**19.3**
Amounts written off	(1.2)	-	-	-	(1.2)	-	**(1.2)**
Charge/(Credit) for the year comprising:							
Provision/(Release) for loan impairment	3.1	(0.7)	-	-	3.1	(0.7)	**2.4**
Adjustments to provisions resulting from recoveries	(0.7)	-	-	-	(0.7)	-	**(0.7)**
Charge/(Credit) for the year	2.4	(0.7)	-	-	2.4	(0.7)	**1.7**
At 31 March 2013	**13.6**	**6.2**	**-**	**-**	**13.6**	**6.2**	**19.8**

Group	Loans fully secured on residential property Individual £m	Collective £m	Loans fully secured on land Individual £m	Collective £m	Total Individual £m	Collective £m	Total £m
At 1 April 2011	29.1	9.8	43.2	9.1	72.3	18.9	91.2
Amounts written off	(6.1)	-	(10.4)	-	(16.5)	-	(16.5)
Charge/(Credit) for the year comprising:							
Provision/(Release) for loan impairment	9.9	(0.3)	(0.3)	3.1	9.6	2.8	12.4
Provision in excess of the securitisation first loss	-	-	11.1	2.4	11.1	2.4	13.5
Reduction in carrying value of debt securities in issue	-	-	(11.1)	(2.4)	(11.1)	(2.4)	(13.5)
Adjustments to provisions resulting from recoveries	(1.9)	-	-	-	(1.9)	-	(1.9)
Charge/(Credit) for the year	8.0	(0.3)	(0.3)	3.1	7.7	2.8	10.5
Non-recourse finance on securitised advances	-	-	11.1	2.4	11.1	2.4	13.5
At 31 March 2012	31.0	9.5	43.6	14.6	74.6	24.1	98.7
Society							
At 1 April 2011	12.0	5.6	-	-	12.0	5.6	17.6
Amounts written off	(1.5)	-	-	-	(1.5)	-	(1.5)
Charge for the year comprising:							
Provision for loan impairment	3.0	1.3	-	-	3.0	1.3	4.3
Adjustments to provisions resulting from recoveries	(1.1)	-	-	-	(1.1)	-	(1.1)
Charge for the year	1.9	1.3	-	-	1.9	1.3	3.2
At 31 March 2012	12.4	6.9	-	-	12.4	6.9	19.3

16. Investments

Subsidiary undertakings

	Society 2013 £m	Society 2012 £m
Shares held in subsidiary undertakings	**0.6**	0.6
Loans to subsidiary undertakings	**2,292.1**	2,274.1
	2,292.7	2,274.7

Shares in subsidiary undertakings are held at cost less impairment. Investments in subsidiary undertakings are financial fixed assets. The net movement in loans to subsidiary undertakings during the year is as follows:

	Society £m
At 1 April 2012	2,274.1
Increase in loans to subsidiaries	18.0
At 31 March 2013	**2,292.1**

All subsidiary loans are provided at open market rates.

The Society holds directly (unless otherwise stated) the following interests in key subsidiary undertakings, all of which are registered in England:

Name	Major activities	Class of shares held	Interest of Society
West Bromwich Mortgage Company Limited	Hold and dispose of debts secured on land and lend money on the security of land	Ordinary £1 shares	100%
West Bromwich Commercial Limited	Commercial lending	Ordinary £1 shares	100%
WBBS Computer Finance Limited	Leasing and licensing computer equipment	Ordinary £1 shares	100%
CL Mortgages Limited (1)	Hold and dispose of debts secured on land and lend money on the security of land	Ordinary £1 shares	100%
West Bromwich Homes Limited	Investment in property for rental	Ordinary £1 shares	100%
West Bromwich Financial Planning Limited	Financial services product vendor	Ordinary £1 shares	100%
Insignia Finance Limited	Second charge lending	Ordinary £500 shares	100%
White Label Lending Limited (2)	Second charge lending	Ordinary £1 shares	100%
Millinet Limited (3)	Hold investments in loan notes secured on commercial mortgage portfolios	Ordinary £1 shares	100%

(1) The entire share capital of CL Mortgages Limited is held by West Bromwich Mortgage Company Limited.
(2) The entire share capital of White Label Lending Limited is held by Insignia Finance Limited.
(3) The entire share capital of Millinet Limited is held by West Bromwich Commercial Limited.

Securitisation entities
The results of the following securitisation entities are consolidated into the results of the Group under the rules and guidance of Standing Interpretations Committee (SIC) 12:

Name	Country of incorporation	Principal activity
Sandwell Commercial Finance No.1 Plc	United Kingdom	Securitisation entity
Sandwell Finance Holdings Limited	United Kingdom	Holding company
Sandwell Commercial Finance No.2 Plc	United Kingdom	Securitisation entity
Hawthorn Hold Co Limited	United Kingdom	Holding company
Hawthorn Asset Co Limited	United Kingdom	Securitisation entity
Hawthorn Finance Limited	Jersey	Securitisation entity
Sandwell Commercial Finance No.3 Limited	Jersey	Securitisation entity
Kenrick No. 1 Plc	United Kingdom	Securitisation entity
Kenrick No. 1 Holdings Limited	United Kingdom	Holding company

The Society has no shareholdings in any of the companies listed above. Unless stated otherwise above, all are incorporated in the United Kingdom and operate in Great Britain.

The assets and liabilities within Sandwell Commercial Finance No.1 Plc have been accounted for using the fair value option available under IAS 39.

17. Goodwill

	Group 2013 £m	Group 2012 £m
Cost		
At beginning and end of year	**0.6**	0.6
Aggregate impairment		
At beginning and end of year	**-**	-
Net book value at end of year	**0.6**	0.6

The goodwill has been assessed as having an indefinite life. In accordance with IAS38, 'Intangible Assets', the Group carries out an annual impairment test in relation to goodwill. When assessing the recoverable amount of goodwill, the Group allocates the goodwill to the lowest cash generating unit (CGU) within the Group.

The recoverable amount of the remaining CGU (Insignia) has been calculated with reference to future earnings and value in use. The calculations incorporate cash flow projections from the three year business plan approved by the Group Board and cash flow forecasts for the following 10 years, reflecting the enduring nature of the business concerned. The long term growth rates of 3.0% (2011/12: 3.0%) are based upon management's expectations of long term GDP growth over the forecast period. The pre-tax rate used to discount projected cash flows is 12.5% (2011/12: 12.5%), reflecting management's required return from the CGU.

18. Intangible assets

Group and Society	Computer software 2013 £m	Computer software 2012 £m
Cost		
At beginning of year	**13.8**	13.3
Additions	**2.6**	2.2
Disposals	**-**	(1.7)
At end of year	**16.4**	13.8
Aggregate amortisation		
At beginning of year	**6.9**	6.7
Charge for the year	**2.2**	1.9
Disposals	**-**	(1.7)
At end of year	**9.1**	6.9
Net book value at end of year	**7.3**	6.9
Net book value at beginning of year	**6.9**	6.6

19. Investment properties

	Group 2013 £m	Group 2012 £m
Valuation		
At beginning of year	**112.7**	113.7
Net losses from fair value adjustments	**(0.2)**	(1.0)
At end of year	**112.5**	112.7

A national firm of specialist residential valuers, e.surv Limited, has carried out a valuation review of the residential investment properties held by West Bromwich Homes Limited. This review involved a physical 'drive by' inspection of a sample of approximately 10% of the total portfolio, together with a review of desktop market value assessments and output from an automated valuation model of all remaining properties on an individual basis.

e.surv Limited confirms that, based on the valuation output reviewed, it is satisfied that the overall valuation of the portfolio at 31 March 2013 is a fair reflection of market value. The valuation was prepared in accordance with the Valuation Standards issued by the Royal Institution of Chartered Surveyors (known as the 'Red Book'), in particular UK Practice Statement 1. Market value is as defined in Practice Statement 3.2.

If the land and buildings were carried at cost, the carrying amount would be £88.9m (2011/12: £88.9m).

The Group leases investment properties to non-commercial individuals for a contract period of up to 18 months. The future minimum lease receipts under non-cancellable operating leases that end within 12 months are £2.4m (2011/12: £2.3m). The Group has not recognised any contingent rent in the period (2011/12: £nil).

20. Property, plant and equipment

Group	Land and buildings Freehold £m	Short leasehold £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation				
At 1 April 2012	7.8	0.7	18.5	**27.0**
Additions	-	-	2.5	**2.5**
Disposals	(0.2)	-	(0.1)	**(0.3)**
At 31 March 2013	**7.6**	**0.7**	**20.9**	**29.2**
Accumulated depreciation				
At 1 April 2012	1.5	0.6	7.3	**9.4**
Charge for the year	0.8	-	2.6	**3.4**
Disposals	-	-	(0.1)	**(0.1)**
At 31 March 2013	**2.3**	**0.6**	**9.8**	**12.7**
Net book value				
At 31 March 2013	**5.3**	**0.1**	**11.1**	**16.5**

Group	Land and buildings Freehold £m	Short leasehold £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation				
At 1 April 2011	7.8	1.0	14.8	23.6
Additions	-	-	8.0	8.0
Disposals	-	(0.3)	(4.3)	(4.6)
At 31 March 2012	7.8	0.7	18.5	27.0
Accumulated depreciation				
At 1 April 2011	0.7	0.9	9.4	11.0
Charge for the year	0.8	-	2.0	2.8
Disposals	-	(0.3)	(4.1)	(4.4)
At 31 March 2012	1.5	0.6	7.3	9.4
Net book value				
At 31 March 2012	6.3	0.1	11.2	17.6

20. Property, plant and equipment (continued)

Society	**Land and buildings** Freehold £m	Short leasehold £m	**Equipment, fixtures, fittings and vehicles £m**	**Total £m**
Cost or valuation				
At 1 April 2012	7.8	0.7	18.3	**26.8**
Additions	-	-	2.5	**2.5**
Disposals	(0.2)	-	(0.1)	**(0.3)**
At 31 March 2013	**7.6**	**0.7**	**20.7**	**29.0**
Accumulated depreciation				
At 1 April 2012	1.5	0.6	7.1	**9.2**
Charge for the year	0.8	-	2.6	**3.4**
Disposals	-	-	(0.1)	**(0.1)**
At 31 March 2013	**2.3**	**0.6**	**9.6**	**12.5**
Net book value				
At 31 March 2013	**5.3**	**0.1**	**11.1**	**16.5**

Society	Land and buildings Freehold £m	Short leasehold £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation				
At 1 April 2011	7.8	1.0	14.6	23.4
Additions	-	-	8.0	8.0
Disposals	-	(0.3)	(4.3)	(4.6)
At 31 March 2012	7.8	0.7	18.3	26.8
Accumulated depreciation				
At 1 April 2011	0.7	0.9	9.3	10.9
Charge for the year	0.8	-	1.9	2.7
Disposals	-	(0.3)	(4.1)	(4.4)
At 31 March 2012	1.5	0.6	7.1	9.2
Net book value				
At 31 March 2012	6.3	0.1	11.2	17.6

The net book value of land and buildings occupied for the Society's own use is £5.4m (2011/12: £6.4m).

The Group's freehold branch properties were revalued at 31 March 2010 by Colliers International, a firm of independent chartered surveyors. The valuations were undertaken in accordance with the Valuation Standards issued by the Royal Institution of Chartered Surveyors in the United Kingdom.

These valuations have been incorporated into the financial statements and the resulting revaluation adjustments taken to the revaluation reserve. If the land and buildings were carried at cost, the carrying amount would be £4.4m (2011/12: £4.5m).

21. Deferred tax

Deferred tax is calculated on all temporary differences under the liability method using an effective tax rate of 23% (2011/12: 24%). The movement on the deferred tax account is as follows:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
At beginning of year	**17.5**	17.6	**11.7**	9.5
Current year Income Statement credit/(charge)	**1.0**	0.2	**(1.0)**	0.3
Amount recognised directly in equity	**(0.2)**	0.6	**(0.2)**	0.6
Adjustments in respect of prior years	**1.4**	(0.9)	**1.3**	1.3
At end of year	**19.7**	17.5	**11.8**	11.7

Deferred tax assets and liabilities are attributable to the following items:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Deferred tax assets				
Accelerated tax depreciation	**4.0**	3.1	**3.9**	3.1
Carried forward tax losses	**17.5**	17.0	**6.3**	7.4
Pensions and other post retirement benefits	**-**	0.2	**-**	0.2
Other temporary differences	**2.5**	5.4	**2.0**	1.5
	24.0	25.7	**12.2**	12.2
Deferred tax liabilities				
Property valuations	**(3.4)**	(3.8)	**(0.4)**	(0.4)
Other temporary differences	**(0.9)**	(4.4)	**-**	(0.1)
	(4.3)	(8.2)	**(0.4)**	(0.5)

The deferred tax credit/(charge) in the Income Statement comprises the following temporary differences:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Accelerated tax depreciation	**0.8**	0.4	**0.8**	0.5
Other provisions	**0.7**	(2.4)	**0.6**	(0.7)
Carried forward tax losses	**0.5**	0.6	**(1.1)**	1.8
Property valuations	**0.4**	0.7	**-**	-
	2.4	(0.7)	**0.3**	1.6

Deferred tax assets are recognised only to the extent that realisation of the related tax benefit against future taxable profits is probable over the foreseeable future. The deferred tax asset balances attributable to carried forward losses are expected to be recoverable against future taxable profits (as projected in the latest Strategic Plan) within eight years. The assumptions surrounding future expected credit losses and increases in the Bank Rate of interest represent the most subjective areas of judgment in management's projections of future taxable profits. The deferred tax assets have not been discounted.

Deferred tax assets and liabilities are offset where there is a legally enforceable right to do so.

Deferred tax assets and liabilities have been calculated at 23% (2011/12: 24%), being the rate substantively enacted at the Statement of Financial Position date. The rate of corporation tax will be further reduced by 2% to 21% by 1 April 2014 and a further 1% to 20% by 1 April 2015. As the further reductions were not substantively enacted by 31 March 2013, the impact of the anticipated rate changes is not reflected in the tax provisions reported in these accounts. If the deferred tax assets and liabilities of the Group were to reverse after 1 April 2015, the effect of the changes from 23% to 20% would be to reduce the net deferred tax asset by £2.6m. To the extent that the deferred tax reverses more quickly than this, the impact of the further rate changes on the net deferred tax asset will be reduced.

22. Trade and other receivables

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Prepayments and accrued income	**2.4**	3.3	**1.9**	3.3
Other	**0.4**	1.0	**0.4**	0.3
	2.8	4.3	**2.3**	3.6

23. Shares

Group and Society	2013 £m	2012 £m
Held by individuals	**4,651.1**	5,671.7
Other shares	**1.1**	1.1
	4,652.2	5,672.8

24. Amounts due to other customers

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Deemed loans	**-**	-	**290.7**	-
Other customers	**193.0**	129.7	**194.8**	129.7
	193.0	129.7	**485.5**	129.7

25. Debt securities in issue

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
GBP medium term notes	**-**	3.0	**-**	3.0
Certificates of deposit	**4.0**	4.0	**4.0**	4.0
Other debt securities	**376.8**	695.0	**376.8**	695.0
Non-recourse finance on securitised advances	**328.3**	225.4	**-**	-
	709.1	927.4	**380.8**	702.0

The non-recourse finance comprises mortgage backed floating rate notes (the Notes) secured over a portfolio of mortgage loans secured by first charges over residential and commercial properties in the United Kingdom (see note 14). Prior to redemption of the Notes on the final interest payment date, the Notes will be subject to mandatory and/or optional redemption, in certain circumstances, on each interest payment date. See note 30 for details of assets held at fair value through profit or loss.

26. Trade and other payables

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Accruals	**5.5**	9.0	**4.8**	6.7
Other creditors	**3.7**	7.6	**3.0**	5.0
Income tax	**3.3**	3.3	**3.3**	3.3
Amounts due to subsidiary undertakings	**-**	-	**-**	0.3
	12.5	19.9	**11.1**	15.3

27. Provisions for liabilities

	FSCS 2013 £m	Onerous contracts 2013 £m	Total 2013 £m	FSCS 2012 £m	Onerous contracts 2012 £m	Total 2012 £m
Group and Society						
At beginning of year	**5.2**	**1.2**	**6.4**	4.6	2.2	6.8
Utilised in the year	**(1.9)**	**(0.4)**	**(2.3)**	(2.3)	(0.7)	(3.0)
Charge/(Release) for the year	**2.7**	**-**	**2.7**	2.9	(0.3)	2.6
At end of year	**6.0**	**0.8**	**6.8**	5.2	1.2	6.4

Financial Services Compensation Scheme (FSCS)

In common with all regulated UK deposit takers, the Society pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. The FSCS levy consists of two parts: a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes using the rights that have been assigned to it. During 2008 and 2009 claims were triggered against the FSCS in relation to Bradford & Bingley plc, Kaupthing Singer and Friedlander, Heritable Bank plc, Landsbanki Islands hf, London Scottish Bank plc and Dunfermline Building Society.

The FSCS meets these current claims by way of loans received from HM Treasury. The terms of these loans were interest only for the first three years, and the FSCS seeks to recover the interest cost, together with ongoing management expenses, by way of annual management levies on members over this period.

The Society FSCS provision reflects market participation up to the reporting date. £4.2m of the provision relates to the estimated management expense levy for the scheme years 2012/13 and 2013/14. This amount was calculated on the basis of the Society's current share of protected deposits taking into account the FSCS estimate of total management expense levies for each scheme year.

The management expenses levy for scheme year 2011/12, which formed part of the provision at 31 March 2012, was calculated using the agreed funding rate of 12 month LIBOR + 30bps. Following the expiry of the initial three year fixed interest term, extensive negotiations between HMT and FSCS resulted in an agreed funding rate of 12 month LIBOR + 100bps which is the rate that will be charged for the HMT loans for the period from 1 April 2012, on which the management expenses levy for scheme years 2012/13 and 2013/14 has been based.

In addition to the management levies, from scheme year 2013/14, triggered by participation in the market at 31 December 2012, the FSCS is to levy over three years the current estimated shortfall on capital loans outstanding of £802m. In common with the management expenses levy, the capital loan repayment was calculated on the basis of the Society's current share of UK protected deposits. The Society has therefore recognised a provision of £1.8m related to the compensation levy.

Onerous contracts

The provision for onerous contracts covers the loss anticipated in connection with future lease expenses from non-cancellable lease commitments in branches that the Society has, as part of its branch restructure, decided are no longer required. The provision should be utilised £0.3m in year 1 and £0.5m in years 2 to 5.

28. Subscribed capital

Group and Society	2013 £m	2012 £m
Permanent interest bearing shares	**74.9**	74.9

In a winding up or dissolution of the Society the claims of the holders of permanent interest bearing shares (PIBS) would rank behind all other creditors of the Society, with the exception of holders of profit participating deferred shares (PPDS) with which the PIBS rank pari-passu, and the claims of members holding shares as to principal and interest. The holders of PIBS are not entitled to any share in any final surplus upon winding up or dissolution of the Society.

With respect to future interest payments, as a condition of the PPDS (see note 29), the Society has undertaken to pay an amount which, when annualised, represents the lower of: 6.15% of the outstanding principal amount of the PIBS and the dividend yield attributable to the PPDS with respect to the prior financial year ending 31 March whose payment is at the discretion of the Society.

29. Profit participating deferred shares

Group and Society	2013 £m	2012 £m
Book value		
Nominal value	**182.5**	182.5
Cumulative fair value adjustments at date of transition	**3.8**	3.8
Capitalised issue costs	**(2.2)**	(2.2)
	184.1	184.1
Cumulative reserve deficit		
At beginning of year	**(9.1)**	(6.8)
Share of loss for the financial year	**(1.3)**	(2.3)
	(10.4)	(9.1)
Net value at end of year	**173.7**	175.0

The profit participating deferred shares (PPDS) are entitled to receive a distribution, at the discretion of the Society, of up to 25% of the Group's post-tax profits in the future (calculated prior to payment of the PPDS dividend). No such distribution may be made if the cumulative reserves are in deficit.

30. Financial assets and liabilities at fair value through profit or loss

Financial assets and liabilities are valued at fair value through profit or loss when this results in more relevant information because it significantly reduces a measurement inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases. The 'Fair Value Option' is used by the Group where financial assets or liabilities would otherwise be measured at amortised cost, the associated derivatives used to economically hedge the risk are held at fair value, and it is not practical to apply hedge accounting. The table below shows the carrying value of financial assets and liabilities that upon initial recognition, or at 1 April 2005 on the adoption of IAS 39, were valued at fair value through profit or loss, and the net gains or losses on these instruments:

	Group 2013 £m	Group 2012 £m
Financial assets at fair value through profit or loss		
Loans fully secured on land		
Carrying value at 31 March	67.6	89.4
Net losses in the year	(2.7)	(0.1)
Financial liabilities at fair value through profit or loss		
Non-recourse finance on securitised advances		
Carrying value at 31 March	62.7	83.6
Net gains in the year	3.0	-
Derivative financial instruments		
Carrying value at 31 March	(5.1)	(4.8)
Net (losses)/gains in the year	(0.3)	0.1

31. Tax effects relating to each component of other comprehensive income

Group and Society	Before tax amount 2013 £m	Tax (expense) /benefit 2013 £m	Net of tax amount 2013 £m
Available for sale financial assets	10.8	(2.6)	8.2
Actuarial loss on retirement benefit obligations	(1.7)	0.4	(1.3)
Other comprehensive income	9.1	(2.2)	6.9

Group and Society	Before tax amount 2012 £m	Tax (expense) /benefit 2012 £m	Net of tax amount 2012 £m
Available for sale financial assets	5.3	(1.5)	3.8
Cash flow hedges	0.1	-	0.1
Actuarial loss on retirement benefit obligations	(4.3)	1.0	(3.3)
Other comprehensive income	1.1	(0.5)	0.6

32. Retirement benefit obligations

Amounts recognised in the Statement of Financial Position:

Group and Society	2013 £m	2012 £m	2011 £m	2010 £m	2009 £m
Defined benefit pension scheme (asset)/obligation	**(0.4)**	0.4	(1.8)	2.0	1.6

Defined benefit plans

The Society operates the West Bromwich Building Society Staff Retirement Scheme (SRS), a funded pension scheme providing benefits for some of its employees based on final pensionable emoluments. The assets of the scheme are held in a separate trustee administered fund. In addition, the Society has some unregistered arrangements in place in respect of former Directors. The financial effect of these arrangements is included in this note.

The results of a formal actuarial valuation at 31 March 2010 carried out by the appointed actuary to the scheme were updated to the accounting date by an independent qualified actuary in accordance with IAS 19, 'Employee benefits'.

The Society closed the scheme to the future accrual of benefits with effect from 1 August 2009, at which date all previously active members became entitled to deferred pensions in the scheme.

The expected rate of return at 31 March 2013 was 4.9% pa (2011/12: 5.3% pa). This rate was derived by taking the weighted average of the long term expected rate of return on each of the asset classes that the scheme invested in, based on the allocation to each asset class at 31 March 2013.

As in the prior year, administrative expenses have been allowed for by way of a 2.0% loading to the defined benefit obligation.

On 27 March 2013, a priority charge was granted by the Society to the Trustees over £18.4m of residential mortgage backed securities. The future cash flows from these assets will be used as contributions by the Society to the pension scheme. The estimated amount of Society contributions expected to be paid to the scheme during 2013/14 is £3.0m (2012/13: £2.1m actual).

The key assumptions used by the actuary in the updated calculation were:

Group and Society	2013	2012	2011	2010	2009
Pension increases in payment (RPI capped at 5%)	**3.30%**	3.20%	3.40%	3.60%	3.20%
Pension increases in payment (RPI capped at 2.5%)	**-**	-	-	2.40%	2.30%
Pension increases in payment (CPI capped at 2.5%)	**2.00%**	1.90%	2.20%	-	-
Discount rate	**4.40%**	4.80%	5.40%	5.60%	7.00%
Expected return on assets	**4.90%**	5.30%	6.20%	6.20%	6.00%
Life expectancy of male aged 65 at year end date	**22.3**	22.2	22.1	22.8	22.7
Life expectancy of female aged 65 at year end date	**23.7**	24.5	24.4	24.8	24.6
Life expectancy of male aged 65 at year end date plus 20 years	**24.6**	23.7	23.6	24.7	24.3
Life expectancy of female aged 65 at year end date plus 20 years	**26.1**	26.0	26.0	25.8	25.6

32. Retirement benefit obligations (continued)

The amounts recognised in the Statement of Financial Position are as follows:

Group and Society	**2013 £m**	2012 £m	2011 £m	2010 £m	2009 £m
Present value of funded obligations	**87.9**	79.1	72.1	70.7	49.1
Present value of unfunded obligations	**0.9**	0.8	0.7	0.8	0.6
	88.8	79.9	72.8	71.5	49.7
Fair value of scheme assets	**(89.2)**	(79.5)	(74.6)	(69.5)	(48.1)
Net (asset)/liability in the Statement of Financial Position	**(0.4)**	0.4	(1.8)	2.0	1.6

The amounts recognised in the Income Statement are as follows:

Group and Society	**2013 £m**	2012 £m	2011 £m
Interest cost	**3.8**	3.9	3.9
Expected return on plan assets	**(4.2)**	(4.6)	(4.3)
Total pension fund income	**(0.4)**	(0.7)	(0.4)

Interest cost and expected return on plan assets are disclosed as other operating income. The actual return on scheme assets was £10.0m (2011/12: £5.2m).

Change in benefit obligations

Group and Society	**2013 £m**	2012 £m	2011 £m
Benefit obligations at beginning of year	**79.9**	72.8	71.5
Interest cost	**3.8**	3.9	3.9
Actuarial losses	**7.5**	4.9	0.2
Benefits paid	**(2.4)**	(1.7)	(2.8)
Benefit obligations at end of year	**88.8**	79.9	72.8

Change in scheme assets

Group and Society	**2013 £m**	2012 £m	2011 £m
Fair value of scheme assets at beginning of year	**79.5**	74.6	69.5
Expected return on scheme assets	**4.2**	4.6	4.3
Actuarial gains	**5.8**	0.6	0.9
Contribution by employer	**2.1**	1.4	2.7
Benefits paid	**(2.4)**	(1.7)	(2.8)
Fair value of scheme assets at end of year	**89.2**	79.5	74.6

The amount recognised outside profit and loss in the Statement of Comprehensive Income for 2012/13 is an actuarial loss of £1.7m (2011/12: £4.3m). The cumulative amount recognised outside profit and loss at 31 March 2013 is an actuarial loss of £24.2m.

32. Retirement benefit obligations (continued)

History of experience gains and losses

Group and Society	2013	2012	2011	2010	2009
Experience gains/(losses) on scheme assets:					
amount (£m)	**5.8**	0.6	0.9	13.1	(15.7)
percentage of scheme assets	**7%**	1%	1%	19%	(33%)
Experience (gains)/losses on scheme liabilities:					
amount (£m)	**(0.2)**	2.1	2.0	0.5	-
percentage of scheme liabilities	**(0%)**	3%	3%	1%	-

Scheme assets

The assets in the scheme and their expected rates of return at 31 March were:

Group and Society	Long-term rate of return expected 2013 %	Value 2013 £m	Long-term rate of return expected 2012 %	Value 2012 £m	Long-term rate of return expected 2011 %	Value 2011 £m
Equities	**6.8**	**12.8**	7.1	30.3	7.6	34.4
Bonds	**4.2**	**-**	4.7	4.7	5.3	4.9
Gilts	**2.8**	**34.8**	3.1	31.6	4.1	26.3
Tactical asset allocation	**6.8**	**3.0**	7.1	3.1	7.0	3.2
Diversified growth fund	**6.3**	**33.1**	6.4	9.6	7.3	5.6
Cash and other assets	**3.0**	**5.5**	3.3	0.2	4.3	0.2
	4.9	**89.2**	5.3	79.5	6.2	74.6

Provisional asset information at bid value was supplied by the investment managers as at 31 March 2013. The unaudited value of the invested assets at this date was £83.7m. The SRS also had net current assets of £5.5m of which £5.4m represented cash in transit arising on the sale of corporate bonds on 28 March 2013 being reinvested on 3 April 2013.

	2013 £m
Black Rock Advisors UK Limited (Equity portfolio)	**12.8**
Black Rock Advisors UK Limited (Bond portfolio)	**34.8**
Black Rock Advisors UK Limited (Tactical Asset Allocation portfolio)	**3.0**
Diversified Growth Fund	**33.1**
Total invested assets	**83.7**
Cash and net current assets	**5.5**
Total assets	**89.2**

Stakeholder scheme

The total cost for the year of the stakeholder plan to the Group and Society was £0.9m (2011/12: £0.9m) and there were no outstanding contributions at the end of the year (2011/12: £nil).

For the period through to 31 July 2009 staff could contribute between 2% and 9% with the Society contributing on a sliding scale between 2% and 7%. From 1 August 2009 staff have been able to contribute between 2% and 10% with the Society providing matched funding.

33. Financial instruments

A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability or equity of another entity.

The Group is a retailer of financial instruments, mainly in the form of mortgages and savings. The Group uses wholesale financial instruments to invest liquid asset balances and raise wholesale funding, and to manage the risks arising from its operations. As a result of these activities, the Group is exposed to a variety of risks, the most significant of which are credit risk, liquidity risk and market risk (principally interest rate, foreign currency and equity risk). These risks are described in notes 34 to 36.

The use of derivative financial instruments for risk management purposes is described in note 35.

Classification of financial assets and financial liabilities

The following tables show the classification of the Group's and Society's financial assets and liabilities:

At 31 March 2013

Group	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	392.3	-	-	**392.3**
Loans and advances to credit institutions	147.1	-	-	**147.1**
Investment securities	-	499.5	-	**499.5**
Derivative financial instruments	-	-	29.5	**29.5**
Loans and advances to customers	4,903.5	-	67.6	**4,971.1**
Total financial assets	**5,442.9**	**499.5**	**97.1**	**6,039.5**
Other non-financial assets				**164.1**
Total assets				**6,203.6**
Liabilities				
Shares	4,652.2	-	-	**4,652.2**
Amounts due to credit institutions	28.5	-	-	**28.5**
Amounts due to other customers	193.0	-	-	**193.0**
Derivative financial instruments	-	-	99.4	**99.4**
Debt securities in issue	646.4	-	62.7	**709.1**
Total financial liabilities	**5,520.1**	**-**	**162.1**	**5,682.2**
Other non-financial liabilities				**23.6**
Total liabilities				**5,705.8**

At 31 March 2012

Group	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	769.2	-	-	769.2
Loans and advances to credit institutions	117.5	-	-	117.5
Investment securities	-	924.5	-	924.5
Derivative financial instruments	-	-	64.5	64.5
Loans and advances to customers	5,284.2	-	89.4	5,373.6
Total financial assets	6,170.9	924.5	153.9	7,249.3
Other non-financial assets				167.8
Total assets				7,417.1
Liabilities				
Shares	5,672.8	-	-	5,672.8
Amounts due to credit institutions	48.6	-	-	48.6
Amounts due to other customers	129.7	-	-	129.7
Derivative financial instruments	-	-	107.8	107.8
Debt securities in issue	333.9	-	593.5	927.4
Total financial liabilities	6,185.0	-	701.3	6,886.3
Other non-financial liabilities				34.9
Total liabilities				6,921.2

33. Financial instruments (continued)

Classification of financial assets and financial liabilities (continued)

At 31 March 2013

Society	**Amortised cost £m**	**Available for sale £m**	**Fair value through profit or loss £m**	**Total £m**
Assets				
Cash and balances with the Bank of England	392.3	-	-	**392.3**
Loans and advances to credit institutions	69.7	-	-	**69.7**
Investment securities	1,099.0	499.5	-	**1,598.5**
Derivative financial instruments	-	-	29.5	**29.5**
Loans and advances to customers	1,728.4	-	-	**1,728.4**
Investments	2,292.7	-	-	**2,292.7**
Total financial assets	**5,582.1**	**499.5**	**29.5**	**6,111.1**
Other non-financial assets				**38.9**
Total assets				**6,150.0**
Liabilities				
Shares	4,652.2	-	-	**4,652.2**
Amounts due to credit institutions	28.5	-	-	**28.5**
Amounts due to other customers	485.5	-	-	**485.5**
Derivative financial instruments	-	-	80.4	**80.4**
Debt securities in issue	380.8	-	-	**380.8**
Total financial liabilities	**5,547.0**	**-**	**80.4**	**5,627.4**
Other non-financial liabilities				**18.3**
Total liabilities				**5,645.7**

At 31 March 2012

Society	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	769.2	-	-	769.2
Loans and advances to credit institutions	50.9	-	-	50.9
Investment securities	1,131.9	924.5	-	2,056.4
Derivative financial instruments	-	-	81.7	81.7
Loans and advances to customers	1,896.3	-	-	1,896.3
Investments	2,274.7	-	-	2,274.7
Total financial assets	6,123.0	924.5	81.7	7,129.2
Other non-financial assets				40.5
Total assets				7,169.7
Liabilities				
Shares	5,672.8	-	-	5,672.8
Amounts due to credit institutions	48.6	-	-	48.6
Amounts due to other customers	129.7	-	-	129.7
Derivative financial instruments	-	-	91.5	91.5
Debt securities in issue	192.1	-	509.9	702.0
Total financial liabilities	6,043.2	-	601.4	6,644.6
Other non-financial liabilities				22.6
Total liabilities				6,667.2

The Group and Society financial assets and liabilities recorded at fair value through profit or loss consist of derivative financial instruments and instruments that were designated as such upon initial recognition to avoid an accounting mismatch. As discussed in notes 1 and 30, these are economically hedged but where it is not practical to apply hedge accounting.

33. Financial instruments (continued)

Fair values of financial assets and financial liabilities

The tables below are a comparison of the book and fair values of the Group and Society's financial instruments by category at the reporting date. Where available, market values have been used to determine fair values. Where market values are not available, fair values have been calculated by discounting cash flows at prevailing interest rates.

	Group carrying value 2013 £m	Group fair value 2013 £m	Society carrying value 2013 £m	Society fair value 2013 £m
Financial assets				
Cash and balances with the Bank of England	**392.3**	392.3	**392.3**	392.3
Investment securities	**499.5**	499.5	**1,598.5**	1,598.5
Loans and advances to credit institutions	**147.1**	147.1	**69.7**	69.7
Loans and advances to customers	**4,971.1**	4,876.6	**1,728.4**	1,801.6
Financial liabilities				
Shares	**4,652.2**	4,639.8	**4,652.2**	4,639.8
Amounts due to credit institutions	**28.5**	28.5	**28.5**	28.5
Amounts due to other customers	**193.0**	193.0	**485.5**	485.5
Debt securities in issue	**709.1**	709.1	**380.8**	380.8

	Group carrying value 2012 £m	Group fair value 2012 £m	Society carrying value 2012 £m	Society fair value 2012 £m
Financial assets				
Cash and balances with the Bank of England	769.2	769.2	769.2	769.2
Investment securities	924.5	924.5	2,056.4	2,056.4
Loans and advances to credit institutions	117.5	117.5	50.9	50.9
Loans and advances to customers	5,373.6	5,342.2	1,896.3	1,898.3
Financial liabilities				
Shares	5,672.8	5,710.7	5,672.8	5,710.7
Amounts due to credit institutions	48.6	48.6	48.6	48.6
Amounts due to other customers	129.7	129.7	129.7	129.7
Debt securities in issue	927.4	927.4	702.0	702.0

a) Loans and advances to customers

The fair value of loans and advances to customers has been calculated on an individual loan basis taking into account factors such as impairment and interest rates. It is not considered appropriate to value them collectively as a portfolio sale.

Impairment is calculated on an incurred loss basis except to the extent that acquired mortgage books have been fair valued on a basis which makes allowances for anticipated losses over the remaining life of the loans.

b) Deposits and borrowings

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand.

The estimated fair value of fixed interest-bearing deposits and other borrowings without quoted market price is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

c) Debt securities in issue

The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, a discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

The fair values have been calculated on a product basis and as such do not necessarily represent the value that could have been obtained for a portfolio if it were sold at 31 March 2013.

33. Financial instruments (continued)

Fair value measurement

The following table summarises the fair value measurement basis used for assets and liabilities held on the Statement of Financial Position at fair value:

Group	Level 1 2013 £m	Level 2 2013 £m	Level 3 2013 £m	Total 2013 £m
Financial assets				
Investment securities	499.5	-	-	**499.5**
Loans and advances to customers	-	67.6	-	**67.6**
Derivative financial instruments	-	29.5	-	**29.5**
	499.5	**97.1**	**-**	**596.6**
Financial liabilities				
Debt securities in issue	-	62.7	-	**62.7**
Derivative financial instruments	-	99.4	-	**99.4**
	-	**162.1**	**-**	**162.1**

Society	Level 1 2013 £m	Level 2 2013 £m	Level 3 2013 £m	Total 2013 £m
Financial assets				
Investment securities	499.5	-	-	**499.5**
Derivative financial instruments	-	29.5	-	**29.5**
	499.5	**29.5**	**-**	**529.0**
Financial liabilities				
Derivative financial instruments	-	80.4	-	**80.4**
	-	**80.4**	**-**	**80.4**

Group	Level 1 2012 £m	Level 2 2012 £m	Level 3 2012 £m	Total 2012 £m
Financial assets				
Investment securities	717.0	207.5	-	924.5
Loans and advances to customers	-	89.4	-	89.4
Derivative financial instruments	-	64.5	-	64.5
	717.0	361.4	-	1,078.4
Financial liabilities				
Debt securities in issue	-	593.5	-	593.5
Derivative financial instruments	-	107.8	-	107.8
	-	701.3	-	701.3

Society	Level 1 2012 £m	Level 2 2012 £m	Level 3 2012 £m	Total 2012 £m
Financial assets				
Investment securities	717.0	207.5	-	924.5
Derivative financial instruments	-	81.7	-	81.7
	717.0	289.2	-	1,006.2
Financial liabilities				
Debt securities in issue	-	509.9	-	509.9
Derivative financial instruments	-	91.5	-	91.5
	-	601.4	-	601.4

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

Level 2: Valuation techniques where all inputs are taken from observable market data, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Valuation techniques where significant inputs are not based on observable market data. None of the Group's financial assets or liabilities are valued using this technique.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist and other valuation models. Assumptions and market observable inputs used in valuation techniques include risk-free and benchmark interest rates, equity index prices and expected price volatilities. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

Observable prices are those that have been seen either from counterparties or from market pricing sources including Bloomberg. The use of these depends upon the liquidity of the relevant market.

34. Credit risk

Credit risk

Credit risk can be described as the risk of customers or counterparties being unable to meet their financial obligations to the Group as they become due.

The Group is exposed to this risk through its lending to:

- individuals (consumers – residential mortgages, including buy-to-let);
- businesses (non-consumers – previous commercial lending and elements of buy-to-let exposure). The Group ceased new commercial lending and buy-to-let in July 2008; and
- wholesale counterparties (including other financial institutions). Specifically within the treasury portfolio assets, where credit risk arises from the investments held by the Group in order to meet liquidity requirements and for general business purposes.

Changes in the credit quality and the recoverability of loans and amounts due from counterparties influence the Group's exposure to credit risk. Adverse changes in the credit quality of counterparties, collateral values or deterioration in the wider economy, including rising unemployment, worsening household finances and further tightening in the UK property market, resulting in declining property values, could affect the recoverability and value of the Group's assets and influence its financial performance. A prolonged economic downturn and the possible continuation of falls in property values (either residential or commercial) could affect the level of impairment losses currently recognised.

The controlled management of credit risk is critical to the Group's overall strategy. The Group has therefore embedded a comprehensive and robust credit risk management framework with clear lines of accountability and oversight as part of its overall governance framework. The Group has effective policies and procedures to identify, monitor, control, mitigate and manage credit risk within the Group's risk appetite.

The Group Risk Committee is responsible for the management of the credit risk appetite that has been established by the Board and for approving lending policy and setting limits on credit exposures, which are monitored and reviewed on a monthly basis. The minutes of this committee are presented to the Board. This committee is supported by two Executive sub-committees; the Residential Mortgage Committee and the Commercial Loans Risk Committee and their role in the credit risk framework is outlined below:

- The Residential Mortgage Committee is responsible for the monitoring of the Group's residential credit exposures and approving changes to the credit scoring systems that are utilised. In addition, the committee reviews the type and quality of approved residential mortgage business and appraises actual arrears and repossession levels against trends and industry averages. A summary of the minutes of this committee are presented to the Group Risk Committee.
- The Commercial Loans Risk Committee reviews individual commercial loans at levels mandated by the Board. This may involve reviewing each case on a quarterly, half yearly or annual basis.

The Group adopts a responsible approach to lending and ensures that the servicing of the loan meets the customer's ability to repay.

The maximum credit risk exposure is the carrying value as shown in the tables on page 70. The Group's most significant exposures to credit risk are loans secured on UK residential properties and loans secured on UK land.

Residential assets

Concentration by loan type	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Prime owner occupied	**1,378.2**	1,551.1	**1,080.2**	1,216.2
Buy-to-let	**2,458.6**	2,549.4	**617.4**	649.9
Other	**122.5**	133.2	**2.9**	3.2
Gross balances	**3,959.3**	4,233.7	**1,700.5**	1,869.3
Impairment provisions	**(31.5)**	(31.3)	**(19.8)**	(19.3)
Fair value adjustments	**8.8**	10.6	**8.8**	8.8
	3,936.6	4,213.0	**1,689.5**	1,858.8

The table below shows the geographic spread of the residential loan portfolio at the year end date:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
East Anglia	**95.4**	101.0	**26.8**	29.3
East Midlands	**341.3**	363.1	**135.3**	150.3
Greater London	**675.9**	719.2	**188.5**	204.0
Northern Ireland	**7.0**	7.5	**1.4**	1.6
North	**116.4**	123.9	**39.4**	44.5
North West	**403.0**	426.2	**167.8**	182.3
Scotland	**161.3**	169.1	**58.9**	63.7
South East	**691.2**	736.7	**246.4**	267.9
South West	**304.2**	326.4	**127.8**	141.4
Wales	**201.4**	216.8	**101.8**	112.6
West Midlands	**720.1**	787.9	**527.3**	585.7
Yorkshire	**242.1**	255.9	**79.1**	86.0
	3,959.3	4,233.7	**1,700.5**	1,869.3

34. Credit risk (continued)

The table below shows analysis of the indexed loan to value distribution of the residential loan portfolio at the year end date:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
>95%	**1,055.9**	1,045.4	**277.0**	254.8
90% - 95%	**413.7**	455.4	**102.8**	137.5
85% - 90%	**434.9**	449.4	**122.9**	146.0
75% - 85%	**680.4**	756.3	**300.7**	324.9
50% - 75%	**800.4**	882.6	**458.7**	511.3
<50%	**574.0**	644.6	**438.4**	494.8
	3,959.3	4,233.7	**1,700.5**	1,869.3

The Group's average indexed loan to value at the year end date is 68.2% (2011/12: 67.1%).

The table below provides further information on the Group's residential loans and advances to customers by payment due status at 31 March 2013:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Loans neither past due or impaired	**3,769.3**	4,039.1	**1,592.2**	1,762.1
Past due but not impaired				
Past due 1 to 3 months	**60.8**	58.0	**28.5**	26.4
Past due 3 to 6 months	**13.0**	23.1	**7.6**	10.7
Past due 6 to 12 months	**8.9**	8.7	**5.5**	4.1
Past due over 12 months	**3.4**	2.7	**2.0**	1.5
Impaired				
Past due 1 to 3 months	**32.0**	35.0	**30.4**	31.9
Past due 3 to 6 months	**21.8**	18.3	**8.2**	8.0
Past due 6 to 12 months	**17.8**	15.3	**8.0**	6.9
Past due over 12 months	**18.7**	21.2	**12.0**	13.5
Possessions	**13.6**	12.3	**6.1**	4.2
	3,959.3	4,233.7	**1,700.5**	1,869.3

The following table indicates collateral held against residential loans and advances to customers:

Fair value of collateral held

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Not impaired	**6,331.2**	6,918.9	**3,279.6**	3,675.7
Impaired	**116.5**	117.1	**57.5**	59.6
Possessions	**16.8**	13.9	**6.2**	4.1
	6,464.5	7,049.9	**3,343.3**	3,739.4

The collateral held consists of properties included within the above categories. The use of such collateral is in line with terms that are usual and customary to standard lending activities.

Forbearance strategies and renegotiated loans

A range of forbearance strategies is employed in order to work with our borrowers to control arrears and, wherever possible, avoid repossession. The agreed strategy will reflect the customer's individual circumstances and will be used in line with industry guidance. Our policies and practices are based on criteria which, in the judgment of senior management, indicate that repayment is likely to continue. Forbearance arrangements include extended payment terms, a reduction in interest or principal repayments, and approved external debt management plans.

Some of these forbearance activities are applied on a small number of commercial mortgages.

Our credit risk management policy sets out restrictions on the number and frequency of restructures. The application of this policy varies according to the nature of the market, the product and the management of customer relationships through the occurrence of exceptional events.

Loans that have been restructured and would otherwise have been past due or impaired are classified as renegotiated.

The carrying amount of loans that have been classified as renegotiated retain this classification until maturity or derecognition. Interest is recorded on renegotiated loans on the basis of new contractual terms following renegotiation.

34. Credit risk (continued)

The table below analyses residential mortgage balances with renegotiated terms at the year end date:

Group	Arrangements 2013 £m	Concessions 2013 £m	Capitalisation 2013 £m	Short-term interest only conversions 2013 £m	Term extensions 2013 £m	Total 2013 £m
Loans neither past due or impaired	6.1	2.2	-	2.1	0.6	**11.0**
Past due but not impaired						
Past due 1 to 3 months	8.6	1.6	0.2	0.6	0.2	**11.2**
Past due 3 to 6 months	3.9	0.1	-	0.2	-	**4.2**
Past due 6 to 12 months	3.3	0.2	-	0.4	-	**3.9**
Past due over 12 months	1.0	-	-	0.1	-	**1.1**
Impaired						
Past due 1 to 3 months	-	0.1	-	-	-	**0.1**
Past due 3 to 6 months	4.3	0.7	-	0.2	0.2	**5.4**
Past due 6 to 12 months	5.1	0.4	-	0.2	0.1	**5.8**
Past due over 12 months	0.9	0.2	-	0.3	-	**1.4**
	33.2	**5.5**	**0.2**	**4.1**	**1.1**	**44.1**

Group	Arrangements 2012 £m	Concessions 2012 £m	Capitalisation 2012 £m	Short-term interest only conversions 2012 £m	Term extensions 2012 £m	Total 2012 £m
Loans neither past due or impaired	14.9	2.7	6.9	2.5	0.9	27.9
Past due but not impaired						
Past due 1 to 3 months	15.5	1.2	0.7	0.9	0.4	18.7
Past due 3 to 6 months	4.9	0.2	0.5	0.4	-	6.0
Past due 6 to 12 months	2.4	0.3	0.2	-	-	2.9
Past due over 12 months	0.5	0.2	-	0.1	-	0.8
Impaired						
Past due 3 to 6 months	6.9	0.4	0.3	0.3	0.2	8.1
Past due 6 to 12 months	4.5	0.2	-	0.2	-	4.9
Past due over 12 months	0.4	0.5	-	0.2	0.1	1.2
Possessions	-	-	-	0.1	-	0.1
	50.0	5.7	8.6	4.7	1.6	70.6

34. Credit risk (continued)

Commercial assets

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Concentration by loan type				
Loans secured on commercial property	**973.9**	1,061.2	**23.1**	23.1
Loans to housing associations	**0.1**	0.1	**-**	-
Loans secured on residential property	**36.4**	75.5	**7.3**	7.3
Gross balances	**1,010.4**	1,136.8	**30.4**	30.4
Impairment provisions	**(62.8)**	(67.4)	**-**	-
Fair value adjustments	**86.9**	91.0	**8.5**	7.1
	1,034.5	1,160.4	**38.9**	37.5

The analysis of loans secured on commercial property by industry type is as follows:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Healthcare and leisure	**222.4**	228.7	**-**	-
Industrial and warehouse	**62.3**	61.3	**2.6**	2.6
Office	**178.8**	204.4	**10.8**	10.8
Retail	**484.0**	560.0	**9.7**	9.7
Other	**26.4**	6.8	**-**	-
	973.9	1,061.2	**23.1**	23.1

The table below shows the geographic spread of the commercial loan portfolio at the year end date:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
East Anglia	**24.2**	24.6	**0.4**	0.4
East Midlands	**62.6**	66.6	**1.3**	1.3
Greater London	**194.6**	243.6	**15.8**	15.8
North	**56.1**	58.1	**-**	-
North West	**247.7**	250.4	**4.4**	4.4
Scotland	**22.2**	20.9	**1.4**	1.4
South East	**163.9**	197.4	**0.8**	0.8
South West	**61.5**	67.4	**0.2**	0.2
Wales	**28.7**	38.1	**0.6**	0.6
West Midlands	**84.5**	95.8	**0.5**	0.5
Yorkshire	**64.4**	73.9	**5.0**	5.0
	1,010.4	1,136.8	**30.4**	30.4

The Group's average indexed loan to value at the year end date is 121.1% (2011/12: 112.0%).

34. Credit risk (continued)

The table below provides further information on the Group's commercial assets by payment due status at 31 March 2013:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Loans neither past due or impaired	**622.8**	781.5	**30.4**	30.4
Not past due but impaired	**176.6**	161.0	**-**	-
Past due but not impaired				
Past due up to 3 months	**52.4**	10.5	**-**	-
Past due 3 to 6 months	**0.9**	2.0	**-**	-
Past due 6 to 12 months	**1.5**	0.9	**-**	-
Past due over 12 months	**24.6**	18.3	**-**	-
Impaired				
Past due up to 3 months	**6.4**	20.9	**-**	-
Past due 3 to 6 months	**9.8**	16.2	**-**	-
Past due 6 to 12 months	**17.2**	9.5	**-**	-
Past due over 12 months	**98.2**	116.0	**-**	-
	1,010.4	1,136.8	**30.4**	30.4

The following table indicates collateral held against commercial loans and advances to customers:

Value of collateral held

Group	Indexed 2013 £m	Unindexed 2013 £m	Indexed 2012 £m	Unindexed 2012 £m
Not impaired	**873.0**	**884.7**	1,081.4	1,051.4
Impaired	**213.8**	**218.7**	269.6	267.5
	1,086.8	**1,103.4**	1,351.0	1,318.9

Value of collateral held

Society	Indexed 2013 £m	Unindexed 2013 £m	Indexed 2012 £m	Unindexed 2012 £m
Not impaired	**48.7**	**51.1**	51.7	51.1

The collateral held consists of properties, land or other guarantees or cash included within the above categories. The use of such collateral is in line with terms that are usual and customary to standard lending activities.

The table below analyses commercial mortgage balances with renegotiated terms at the year end date:

Group	Arrangements 2013 £m	Capitalisation 2013 £m	Term extensions 2013 £m	Total 2013 £m
Loans neither past due or impaired	-	-	17.0	**17.0**
Not past due but impaired	-	10.3	0.4	**10.7**
Past due but not impaired				
Past due up to 3 months	3.7	-	-	**3.7**
Past due 3 to 6 months	-	-	0.9	**0.9**
Past due over 12 months	3.2	-	-	**3.2**
Impaired				
Past due over 12 months	11.3	-	-	**11.3**
	18.2	**10.3**	**18.3**	**46.8**

34. Credit risk (continued)

Credit risk – impairment

As described in note 1, the Group uses a number of experience-based and judgmental factors to determine the appropriate level of impairment provisions. The key assumptions applied are as follows:

Group and Society	2013	2012
Probability of possession given default*	7% to 85%	15% to 85%
Loss emergence period	6 to 12 months	6 to 12 months
House price inflation		
2013/14	0.00%	0.00%
2014/15	1.50%	1.50%
2015/16	3.00%	3.00%
2016/17	4.00%	4.00%
2017/18 onwards	4.75%	4.75%
Forced sale discount	11% to 33%	14% to 36%

* Default is defined as 3 months+ arrears

Credit risk - loans and advances to credit institutions and investment securities

The Group holds treasury investments in order to meet liquidity requirements and for general business purposes. The credit risk arising from these investments is monitored, managed and controlled closely by the Group.

The Group determines that a treasury asset is impaired when there has been a significant or prolonged decline in the fair value below its cost. The determination of 'significant or prolonged' requires judgment. In making this judgment, the Group evaluates among other factors, the normal volatility in valuation, evidence of deterioration in the financial health of the investee, industry and sector performance and operational and financing cash flows. At 31 March 2013 and 31 March 2012 none of the Group's treasury investments were either past due or impaired and no impairment charges were required during the year.

At 31 March 2013, 100.0% (2011/12: 100.0%) of the Group's treasury assets were invested in or deposited with counterparties rated single A or better. The Group has no exposure in its liquidity portfolio to Cyprus, Greece, Ireland, Italy, Portugal or Spain, the emerging markets or to any mortgage market other than the UK and no exposure to non-UK sovereign debt. The tables below show the relative concentrations of the Group's treasury investment portfolio:

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
Concentration by credit grading				
AAA	707.1	1,284.7	707.1	1,284.7
AA+ to AA-	92.8	175.2	41.9	126.0
A+ to A-	207.9	268.0	181.4	250.6
Building societies	31.1	83.3	31.1	83.3
Other	-	-	1,099.0	1,131.9
	1,038.9	1,811.2	2,060.5	2,876.5
Concentration by sector				
Financial institutions	278.4	526.5	201.0	459.9
Asset backed securities	169.3	144.4	1,268.3	1,276.3
Supranational institutions	198.9	350.3	198.9	350.3
Sovereign	392.3	790.0	392.3	790.0
	1,038.9	1,811.2	2,060.5	2,876.5
Concentration by region				
UK	770.7	1,264.2	1,840.7	2,378.8
Europe (excluding UK)	64.1	140.4	15.7	91.1
North America	-	0.3	-	0.3
Australasia	5.2	56.0	5.2	56.0
Supranational	198.9	350.3	198.9	350.3
	1,038.9	1,811.2	2,060.5	2,876.5

35. Market risk

Market risk is the potential adverse change in Group income or the value of Group net worth arising from movements in interest rates, exchange rates, equity prices or other market prices. The Board recognises that the effective management of market risk is essential to the maintenance of stable earnings and the preservation of member value.

The Group's exposure to market risk is governed by the Board approved Treasury and Financial Risks Management Policy, which sets out the nature of risks that may be taken and defines aggregate risk limits. Within this Policy, the Board has delegated responsibility for the management and control of market rate risk to the Assets & Liabilities Committee (ALCo). At each meeting, ALCo reviews reports which show the Group's current and forecast exposure to market risks together with the results of extensive stress testing.

The Society's Treasury function is responsible for operational management of the Group's exposure to market risk. It achieves this by taking advantage of natural hedges arising within the Group's businesses and transacting appropriate hedging instruments where no natural hedges exist.

Interest rate risk

The main market risk faced by the Group is interest rate risk. The Board's appetite for interest rate risk is low.

Interest rate risk is managed within a clearly defined framework of Policy limits. It is measured and reported using a variety of techniques appropriate to the exposures concerned. These techniques include net interest income and market value sensitivity analysis, scenario analysis, stress testing, interest rate gap analysis and basis risk analysis.

The Group's exposure to interest rate risk is reported against target operating ranges set by ALCo, which themselves fall within Board Policy limits. The effect upon the Group's current and forecast net market value of assets and liabilities is determined for parallel yield curve shifts in the range +2% to -2% and for stressed non-parallel yield curve shifts. The impact upon net interest income is also assessed for parallel rate movements in the range -0.5% to +2% and for extreme convergent and divergent Bank Rate and LIBOR paths.

Analysis is also presented to show the mismatches between assets and liabilities whose rates move in line with different variable rate benchmarks such as Bank Rate, LIBOR and rates administered by the Group. Such mismatches generate additional interest rate risks to those assessed by parallel and non-parallel shift analysis. The Board has imposed limits upon these absolute basis mismatches.

To ensure that the overall reported interest rate risk position does not mask excessive offsetting concentrations in different periods, reprice gap concentration limits are in place to limit the maximum mismatch between assets and liabilities repricing in any one month. In conducting this analysis, general reserves, PPDS and PIBS are allocated over a range of time buckets against treasury and other assets in accordance with targets set by ALCo. The resulting 'reverse cumulative gap report' allows the income and market value sensitivity of a one basis point movement in interest rates upon the whole balance sheet to be calculated.

The Group's gap and basis mismatch positions are reported quarterly to the Prudential Regulation Authority (PRA).

The levels of Group pre-tax interest rate risk exposures, to a +2% parallel shift, through the reporting period were as follows:

	At 31 March 2013 £m	Average 2013 £m	High 2013 £m	Low 2013 £m
Market value	**0.7**	(0.4)	(3.5)	1.8
Net interest income	**(1.7)**	(0.7)	(1.7)	0.3

Foreign currency risk

The Group had no foreign currency exposure at 31 March 2013 (2011/12: £nil).

Equity risk

Equity risk arises from index linked savings products offered by the Group and is managed through the use of derivative contracts. The Group's only exposure to equity risk at 31 March 2013 was £154.3m (2011/12: £297.0m) of fully hedged savings products.

Derivative financial instruments

Instruments used for risk management purposes include derivative financial instruments (derivatives). Derivatives are instruments whose value is derived from one or more underlying price, rate or index (such as interest rates, exchange rates or stock market indices) but have a smaller or no initial net investment relative to financial assets/liabilities offering the same risk/return, as cash flows are generally settled at a future date.

The Group uses derivatives to reduce market risk in its daily activities. Derivatives are not used in trading activity or for speculative purposes. The nature of these instruments means that the nominal value of these transactions is not included in the Statement of Financial Position. The interest payments, receipts and changes in fair value of effective hedges are recognised in the Income Statement. Fair values are recorded in the Statement of Financial Position.

Types of derivatives

The principal derivatives used by the Group are interest rate swaps and index linked swaps that are used to hedge Group Statement of Financial Position exposures.

The following table describes the significant activities undertaken by the Group, the related risks associated with such activities and the type of derivatives which are typically used in managing such risks. Such risks may also be managed using Statement of Financial Position instruments as part of an integrated approach to risk management.

Activity	Risk	Managed by
Management of the investment of reserves and other non-interest bearing liabilities	Sensitivity to changes in interest rates	Matching against fixed rate assets
Fixed rate mortgage lending and other assets	Sensitivity to rises in interest rates	Pay fixed rate interest rate swaps and swaptions, matching against fixed rate receipts
Fixed rate savings products and funding	Sensitivity to falls in interest rates	Receive fixed rate interest rate swaps and swaptions, matching against fixed rate liabilities
Equity linked investment products	Sensitivity to changes in equity indices	Equity linked swaps and options
Cap, collared or floored products	Sensitivity to changes in interest rates	Matching against appropriate cap, collar or floor derivatives or suitable assets or liabilities

36. Liquidity risk

The Society's principal purpose is to make loans secured by way of mortgage on residential property funded substantially by short-term savings from its members. The contractual maturity of the mortgages is typically up to 25 years although loans are often repaid early due to borrowers moving house or remortgaging. In contrast, the majority of members' savings are available on demand or at short notice. It is this inherent mismatch between the maturity profile of mortgage lending and the easy accessibility of savings that creates liquidity risk.

The Group's exposure to liquidity risk is governed by the Liquidity and Funding Policy sections of the Board approved Treasury and Financial Risks Management Policy. The Liquidity and Funding Policy limit framework is designed to ensure that adequate liquid assets are held to cover statutory, regulatory and operational cash requirements in both business as usual and stressed environments.

The Group's liquidity risk is managed as follows:

- The Board has delegated authority for the management of liquidity risk to the Assets & Liabilities Committee (ALCo) within risk tolerances set out in the Liquidity and Funding Policies. ALCo meets monthly;
- Operational management of liquidity risk is further delegated to the Liquidity Management Committee (LMC). LMC meets weekly to agree, based upon detailed customer behavioural analysis, the amount of funding required to maintain the adequacy of Group liquidity over horizons of up to three months. LMC plans cash requirements at a higher level over an extended rolling 12 month plan period;
- LMC also considers a series of daily, weekly and monthly stress tests which are designed to ensure that the Committee maintains sufficient liquidity to meet the Group's cash flow needs under any one of a number of adverse scenarios. These scenarios simulate both Group specific, general market and combined events including severe savings outflows and the unavailability of wholesale funding; and
- Under the PRA's liquidity regime, the Group is required to hold high quality liquid assets ('buffer liquidity') such as government securities, supranational bonds and cash deposited with the Bank of England. The minimum amount to be held is laid down in Individual Liquidity Guidance (ILG) issued to the Society by the PRA. The Group holds buffer and other high quality liquidity above that required by the ILG in accordance with its own day-to-day assessment of liquidity adequacy.

There are three key measures that the Group considers key to monitoring its liquidity position:

- Buffer liquidity – assesses daily the amount of high quality liquid assets necessary to meet its ILG and maintain liquidity adequacy;
- Wholesale refinancing gap – sets the maximum net wholesale outflow permitted over the following two weeks; and
- Liquidity stress tests – models the adequacy of Group liquidity under a number of different stress scenarios within the context of the Board's liquidity risk tolerance.

Further details of liquidity management are contained within the Risk Management Report on pages 17 to 20.

The table below analyses the Group's assets and liabilities across maturity periods that reflect the residual maturity from the year end date to the contractual maturity date. The actual repayment profile of loans and advances is likely to be significantly different to that shown in the analysis.

At 31 March 2013

Group	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	386.8	-	-	-	-	5.5	**392.3**
Loans and advances to credit institutions	28.7	118.3	0.1	-	-	-	**147.1**
Investment securities	-	16.5	81.6	299.9	101.5	-	**499.5**
Derivative financial instruments	-	2.1	-	24.4	3.0	-	**29.5**
Loans and advances to customers	-	143.4	291.9	596.5	3,939.3	-	**4,971.1**
Deferred tax assets	-	-	-	-	-	24.0	**24.0**
Trade and other receivables	-	-	-	-	-	2.8	**2.8**
Intangible assets	-	-	-	-	-	7.9	**7.9**
Investment properties	-	-	-	-	-	112.5	**112.5**
Property, plant and equipment	-	-	-	-	-	16.5	**16.5**
Retirement benefit assets	-	-	-	-	-	0.4	**0.4**
	415.5	**280.3**	**373.6**	**920.8**	**4,043.8**	**169.6**	**6,203.6**
Liabilities and equity							
Shares	3,541.9	410.0	245.6	454.7	-	-	**4,652.2**
Amounts due to credit institutions	-	27.0	1.5	-	-	-	**28.5**
Amounts due to other customers	16.8	76.9	94.1	5.2	-	-	**193.0**
Derivative financial instruments	-	-	1.0	40.7	57.7	-	**99.4**
Debt securities in issue	-	195.0	119.8	217.2	177.1	-	**709.1**
Deferred tax liabilities	-	-	-	-	-	4.3	**4.3**
Trade and other payables	-	-	-	-	-	12.5	**12.5**
Provisions for liabilities	-	-	-	-	-	6.8	**6.8**
Profit participating deferred shares	-	-	-	-	-	173.7	**173.7**
Subscribed capital	-	-	-	-	-	74.9	**74.9**
General reserves	-	-	-	-	-	236.1	**236.1**
Revaluation reserve	-	-	-	-	-	3.7	**3.7**
Available for sale reserve	-	-	-	-	-	9.4	**9.4**
	3,558.7	**708.9**	**462.0**	**717.8**	**234.8**	**521.4**	**6,203.6**

36. Liquidity risk (continued)

At 31 March 2013

Society	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	386.8	-	-	-	-	5.5	**392.3**
Loans and advances to credit institutions	(0.3)	69.9	0.1	-	-	-	**69.7**
Investment securities	-	16.5	81.6	446.4	1,054.0	-	**1,598.5**
Derivative financial instruments	-	2.1	-	24.4	3.0	-	**29.5**
Loans and advances to customers	-	4.5	19.3	167.5	1,537.1	-	**1,728.4**
Current tax assets	-	-	-	-	-	0.2	**0.2**
Deferred tax assets	-	-	-	-	-	12.2	**12.2**
Trade and other receivables	-	-	-	-	-	2.3	**2.3**
Investments	-	-	-	-	-	2,292.7	**2,292.7**
Intangible assets	-	-	-	-	-	7.3	**7.3**
Property, plant and equipment	-	-	-	-	-	16.5	**16.5**
Retirement benefit assets	-	-	-	-	-	0.4	**0.4**
	386.5	**93.0**	**101.0**	**638.3**	**2,594.1**	**2,337.1**	**6,150.0**
Liabilities and equity							
Shares	3,541.9	410.0	245.6	454.7	-	-	**4,652.2**
Amounts due to credit institutions	-	27.0	1.5	-	-	-	**28.5**
Amounts due to other customers	18.5	77.0	95.4	22.2	272.4	-	**485.5**
Derivative financial instruments	-	-	1.0	36.1	43.3	-	**80.4**
Debt securities in issue	-	195.0	119.8	66.0	-	-	**380.8**
Deferred tax liabilities	-	-	-	-	-	0.4	**0.4**
Trade and other payables	-	-	-	-	-	11.1	**11.1**
Provisions for liabilities	-	-	-	-	-	6.8	**6.8**
Profit participating deferred shares	-	-	-	-	-	173.7	**173.7**
Subscribed capital	-	-	-	-	-	74.9	**74.9**
General reserves	-	-	-	-	-	242.6	**242.6**
Revaluation reserve	-	-	-	-	-	3.7	**3.7**
Available for sale reserve	-	-	-	-	-	9.4	**9.4**
	3,560.4	**709.0**	**463.3**	**579.0**	**315.7**	**522.6**	**6,150.0**

36. Liquidity risk (continued)

At 31 March 2012

Group	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	763.7	-	-	-	-	5.5	769.2
Loans and advances to credit institutions	21.5	94.6	1.4	-	-	-	117.5
Investment securities	-	254.0	114.9	482.4	73.2	-	924.5
Derivative financial instruments	-	14.1	15.8	17.1	17.5	-	64.5
Loans and advances to customers	-	30.0	378.8	634.2	4,330.6	-	5,373.6
Deferred tax assets	-	-	-	-	-	25.7	25.7
Trade and other receivables	-	-	-	-	-	4.3	4.3
Intangible assets	-	-	-	-	-	7.5	7.5
Investment properties	-	-	-	-	-	112.7	112.7
Property, plant and equipment	-	-	-	-	-	17.6	17.6
	785.2	392.7	510.9	1,133.7	4,421.3	173.3	7,417.1
Liabilities and equity							
Shares	3,767.1	638.8	618.7	633.4	14.8	-	5,672.8
Amounts due to credit institutions	-	48.6	-	-	-	-	48.6
Amounts due to other customers	-	91.4	36.3	2.0	-	-	129.7
Derivative financial instruments	-	-	1.0	23.8	83.0	-	107.8
Debt securities in issue	-	610.9	91.1	-	225.4	-	927.4
Deferred tax liabilities	-	-	-	-	-	8.2	8.2
Trade and other payables	-	-	-	-	-	19.9	19.9
Provisions for liabilities	-	-	-	-	-	6.4	6.4
Retirement benefit obligations	-	-	-	-	-	0.4	0.4
Profit participating deferred shares	-	-	-	-	-	175.0	175.0
Subscribed capital	-	-	-	-	-	74.9	74.9
General reserves	-	-	-	-	-	241.1	241.1
Revaluation reserve	-	-	-	-	-	3.7	3.7
Available for sale reserve	-	-	-	-	-	1.2	1.2
	3,767.1	1,389.7	747.1	659.2	323.2	530.8	7,417.1

36. Liquidity risk (continued)

At 31 March 2012

Society	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	763.7	-	-	-	-	5.5	769.2
Loans and advances to credit institutions	0.1	49.4	1.4	-	-	-	50.9
Investment securities	-	254.0	114.9	620.9	1,066.6	-	2,056.4
Derivative financial instruments	-	14.1	15.8	23.1	28.7	-	81.7
Loans and advances to customers	-	4.2	14.0	172.3	1,705.8	-	1,896.3
Current tax assets	-	-	-	-	-	0.2	0.2
Deferred tax assets	-	-	-	-	-	12.2	12.2
Trade and other receivables	-	-	-	-	-	3.6	3.6
Investments	-	-	-	-	-	2,274.7	2,274.7
Intangible assets	-	-	-	-	-	6.9	6.9
Property, plant and equipment	-	-	-	-	-	17.6	17.6
	763.8	321.7	146.1	816.3	2,801.1	2,320.7	7,169.7
Liabilities and equity							
Shares	3,767.1	638.8	618.7	633.4	14.8	-	5,672.8
Amounts due to credit institutions	-	48.6	-	-	-	-	48.6
Amounts due to other customers	-	91.4	36.3	2.0	-	-	129.7
Derivative financial instruments	-	-	0.8	18.3	72.4	-	91.5
Debt securities in issue	-	610.9	91.1	-	-	-	702.0
Deferred tax liabilities	-	-	-	-	-	0.5	0.5
Trade and other payables	-	-	-	-	-	15.3	15.3
Provisions for liabilities	-	-	-	-	-	6.4	6.4
Retirement benefit obligations	-	-	-	-	-	0.4	0.4
Profit participating deferred shares	-	-	-	-	-	175.0	175.0
Subscribed capital	-	-	-	-	-	74.9	74.9
General reserves	-	-	-	-	-	247.7	247.7
Revaluation reserve	-	-	-	-	-	3.7	3.7
Available for sale reserve	-	-	-	-	-	1.2	1.2
	3,767.1	1,389.7	746.9	653.7	87.2	525.1	7,169.7

36. Liquidity risk (continued)

The significant development of liquidity stress testing and forecast models has continued throughout 2013 due to economic and market conditions. A wide range of scenarios is considered including mild and severe distresses, credit downgrades and a total closure of the wholesale market. An analysis of the liquidity portfolio is set out in the table below:

Group	2013 £m	2013 %	2012 £m	2012 %
Cash in hand and balances with the Bank of England	**392.3**	**37.8**	769.2	42.5
Cash with banks and building societies	**147.1**	**14.2**	117.5	6.5
Gilts	**-**	**-**	20.5	1.1
Certificates of deposit	**-**	**-**	207.5	11.5
Fixed rate bonds	**244.8**	**23.5**	417.6	23.0
Floating rate notes	**85.4**	**8.2**	134.2	7.4
Residential mortgage backed securities	**169.3**	**16.3**	144.7	8.0
Total	**1,038.9**	**100.0**	1,811.2	100.0

During the year the liquidity balances have decreased from £1,811.2m at 31 March 2012 to £1,038.9m at 31 March 2013. Expressed as a proportion of combined shares and deposits liabilities, this represents a decrease from 27.64% to 19.77%.

The following table is an analysis of the gross contractual cash flows payable under financial liabilities:

At 31 March 2013

Group	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total £m
Liabilities					
Shares	3,998.5	246.4	436.3	-	**4,681.2**
Amounts owed to credit institutions, other customers and holders of debt securities	284.5	216.9	72.4	74.9	**648.7**
Derivative financial instruments	7.5	22.2	100.1	221.4	**351.2**
	4,290.5	**485.5**	**608.8**	**296.3**	**5,681.1**

At 31 March 2012

Group	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total £m
Liabilities					
Shares	4,429.2	616.2	631.0	14.8	5,691.2
Amounts owed to credit institutions, other customers and holders of debt securities	672.2	179.0	2.1	74.9	928.2
Derivative financial instruments	7.4	21.4	100.6	85.5	214.9
	5,108.8	816.6	733.7	175.2	6,834.3

For each material class of financial liability a maturity analysis is provided on pages 79 to 82.

36. Liquidity risk (continued)

At 31 March 2013

Society	**Less than 3 months £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**Total £m**
Liabilities					
Shares	3,998.5	246.4	436.3	-	**4,681.2**
Amounts owed to credit institutions, other customers and holders of debt securities	284.5	216.9	72.4	74.9	**648.7**
Derivative financial instruments	4.9	14.3	58.2	27.0	**104.4**
	4,287.9	**477.6**	**566.9**	**101.9**	**5,434.3**

At 31 March 2012

Society	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total £m
Liabilities					
Shares	4,429.2	616.2	631.0	14.8	5,691.2
Amounts owed to credit institutions, other customers and holders of debt securities	672.2	179.0	2.1	74.9	928.2
Derivative financial instruments	5.3	15.1	67.2	32.5	120.1
	5,106.7	810.3	700.3	122.2	6,739.5

37. Financial commitments

	Group 2013 £m	Group 2012 £m	Society 2013 £m	Society 2012 £m
a) Capital commitments				
Capital expenditure contracted but not yet provided for in the accounts	**0.9**	0.7	**0.9**	0.7
b) Leasing commitments				
Total commitments under non-cancellable leases				
Rental commitments arising:				
Within one year	**0.5**	0.6	**0.5**	0.6
Later than one year and not later than five years	**1.7**	1.9	**1.7**	1.9
After five years	**0.6**	1.0	**0.6**	1.0
	2.8	3.5	**2.8**	3.5
c) Loan commitments				
Undrawn loan facilities	**25.5**	-	**18.3**	-

38. Related party transactions

i) Subsidiary, parent and ultimate controlling party

The subsidiaries of the Society (the ultimate controlling party) are detailed in note 16.

ii) Key management personnel

The Board considers key management personnel to comprise Executive and Non-Executive Directors. Details of Directors' emoluments are disclosed in note 9.

iii) Transactions with key management personnel and their close family members

The table below shows outstanding balances and transactions with key management personnel, which comprises Group Directors and their close family members:

Group and Society	No. of key management personnel 2013	Amount in respect of key management personnel and their close family members 2013 £000	No. of key management personnel 2012	Amount in respect of key management personnel and their close family members 2012 £000
Mortgage loans outstanding at 31 March	**-**	**-**	-	-
Savings balances at 31 March	**10**	**112**	10	93
Interest receivable on mortgage loans	**-**	**-**	1	-
Interest payable on savings balances	**10**	**3**	10	1

Mortgage loans and savings are available to key management personnel and members of their close family at normal commercial terms and no specific provisions are held against them. At 31 March 2013, there were no mortgage loans (2011/12: nil) outstanding to Directors and their connected persons, amounting to £nil (2011/12: £nil).

A register is maintained by the Society containing details of loans and transactions and arrangements made between the Society or its subsidiary undertakings and Directors of the Society or persons connected with Directors of the Society. The register will be available for inspection by members at the Annual General Meeting and during normal office hours at the Society's Principal Office (374 High Street, West Bromwich) during the period 15 days prior to the meeting.

iv) Contributions to pension schemes

During the year the Group paid contributions of £2.1m (2011/12: £1.4.m) to defined benefit pension schemes, which are classified as related parties.

38. Related party transactions (continued)

v) Transactions with Group companies

	Interest paid to Society 2013 £m	Interest paid to Society 2012 £m
West Bromwich Mortgage Company Limited	**29.2**	31.8
West Bromwich Commercial Limited	**44.0**	49.4
West Bromwich Homes Limited	**3.2**	3.1
Insignia Finance Limited	**0.8**	1.0
Millinet Limited	**0.1**	-
	77.3	85.3

At the year end the following balances were outstanding with Group companies:

	Loans owed by subsidiaries 2013 £m	**Loans owed to subsidiaries 2013 £m**	Loans owed by subsidiaries 2012 £m	Loans owed to subsidiaries 2012 £m
West Bromwich Mortgage Company Limited	**1,279.5**	**-**	1,354.2	-
West Bromwich Commercial Limited	**872.7**	**-**	794.2	-
WBBS Computer Finance Limited	**(0.2)**	**-**	(0.2)	-
Governangle Limited - dormant	**-**	**-**	-	0.2
Governafter Limited - dormant	**-**	**-**	-	0.1
West Bromwich Financial Planning Limited	**(0.9)**	**-**	(0.4)	-
West Bromwich Homes Limited	**92.2**	**-**	92.2	-
Insignia Finance Limited	**28.4**	**-**	34.1	-
Millinet Limited	**2.9**	**-**	-	-
Kenrick No. 1 Plc	**17.5**	**-**	-	-
	2,292.1	**-**	2,274.1	0.3

Transactions and balances between Group companies are on normal commercial terms and conditions.

39. Business segments

Operating segments are reported in accordance with the internal reporting provided to the Group Board (the chief operating decision maker), which is responsible for allocating resources to the reportable segments and assessing their performance.

The Group has three main business segments:

- Retail – incorporating residential lending, savings, investments and protection;
- Commercial – primarily representing loans for commercial property investment; and
- Property – a portfolio of residential properties for rent.

Central Group operations have been included in Retail and comprise risk management, funding, treasury services, human resources and computer services, none of which constitute a separately reportable segment.

There were no changes to reportable segments during the year.

39. Business segments (continued)

Transactions between the business segments are carried out at arm's length. The revenue from external parties reported to the Group Board is measured in a manner consistent with that in the consolidated Income Statement.

Funds are ordinarily allocated between segments, resulting in funding cost transfers disclosed in inter-segment net interest income. Interest charged for these funds is based on the Group's cost of capital. Central administrative costs are also allocated between segments and are disclosed in inter-segment administrative expenses. There are no other material items of income or expense between the business segments.

Income statements

for the year ended 31 March 2013

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Interest receivable and similar income	165.9	28.8	-	(33.6)	**161.1**
Interest expense and similar charges	(124.1)	(33.6)	(3.2)	33.5	**(127.4)**
Net interest receivable/(expense)	**41.8**	**(4.8)**	**(3.2)**	**(0.1)**	**33.7**
Fees and commissions receivable	5.5	0.1	-	-	**5.6**
Other operating income	0.3	-	4.0	-	**4.3**
Total operating income/(expense)	**47.6**	**(4.7)**	**0.8**	**(0.1)**	**43.6**
Fair value losses on financial instruments	(1.7)	-	-	-	**(1.7)**
Net realised profits	7.3	-	-	-	**7.3**
Total income/(expense)	**53.2**	**(4.7)**	**0.8**	**(0.1)**	**49.2**
Administrative expenses	(36.7)	(2.9)	(0.1)	0.4	**(39.3)**
Depreciation and amortisation	(5.6)	-	-	-	**(5.6)**
Operating profit/(loss) before impairments, provisions and revaluation losses	**10.9**	**(7.6)**	**0.7**	**0.3**	**4.3**
Losses on investment properties	-	-	(0.2)	-	**(0.2)**
Impairment losses on loans and advances	(4.1)	(6.7)	-	-	**(10.8)**
Provisions for liabilities - FSCS Levy	(2.7)	-	-	-	**(2.7)**
Profit/(Loss) before tax	**4.1**	**(14.3)**	**0.5**	**0.3**	**(9.4)**
Taxation	4.4	(0.3)	0.1	0.2	**4.4**
Profit/(Loss) for the financial year	**8.5**	**(14.6)**	**0.6**	**0.5**	**(5.0)**

Statements of financial position

at 31 March 2013

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Total assets	**6,050.6**	**1,000.0**	**118.0**	**(965.0)**	**6,203.6**
Total liabilities	**5,508.4**	**1,068.7**	**96.4**	**(967.7)**	**5,705.8**
Capital expenditure	**5.1**	**-**	**-**	**-**	**5.1**

39. Business segments (continued)

Income statements

for the year ended 31 March 2012

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Interest receivable and similar income	183.7	52.9	-	(55.8)	180.8
Interest expense and similar charges	(140.7)	(57.8)	(3.1)	55.7	(145.9)
Net interest receivable/(expense)	43.0	(4.9)	(3.1)	(0.1)	34.9
Fees and commissions receivable	5.4	0.7	-	-	6.1
Other operating income	1.4	0.7	3.8	(1.5)	4.4
Total operating income/(expense)	49.8	(3.5)	0.7	(1.6)	45.4
Fair value (losses)/gains on financial instruments	(2.9)	(0.2)	-	0.1	(3.0)
Net realised profits	5.2	-	-	-	5.2
Total income/(expense)	52.1	(3.7)	0.7	(1.5)	47.6
Administrative expenses	(36.2)	(3.7)	(0.1)	1.7	(38.3)
Depreciation and amortisation	(4.7)	-	-	-	(4.7)
Operating profit/(loss) before impairments, provisions and revaluation losses	11.2	(7.4)	0.6	0.2	4.6
Losses on investment properties	-	-	(1.0)	-	(1.0)
Impairment losses on loans and advances	(4.3)	(6.2)	-	-	(10.5)
Provisions for liabilities - FSCS Levy	(2.9)	-	-	-	(2.9)
Provisions for liabilities - other	0.3	-	-	-	0.3
Profit/(Loss) before tax	4.3	(13.6)	(0.4)	0.2	(9.5)
Taxation	2.9	(1.4)	0.3	(1.5)	0.3
Profit/(Loss) for the financial year	7.2	(15.0)	(0.1)	(1.3)	(9.2)

Statements of financial position

at 31 March 2012

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Total assets	8,187.7	1,116.4	111.3	(1,998.3)	7,417.1
Total liabilities	7,657.2	1,170.4	90.4	(1,996.8)	6,921.2
Capital expenditure	10.2	-	-	-	10.2

40. Capital management

Capital is held as the ultimate protection for depositors. The Board sets the internal level of capital with the aim of ensuring capital levels are always above minimum regulatory requirements. Group capital requirements are reviewed on a monthly basis and the results of this monitoring are reported to the Group Capital Committee, Group Risk Committee and the Board.

The Group's capital structure is shown in the table below. For details of the Group's capital management processes see pages 17 to 20 of the Business Review.

Regulatory capital	Group 2013 £m	Group 2012 £m
Tier 1		
General reserves	**236.1**	241.1
Permanent interest bearing shares (note 1)	**74.9**	74.9
Profit participating deferred shares	**173.7**	175.0
Intangible assets (note 2)	**(7.9)**	(7.5)
Deductions from Tier 1 capital (note 3)	**(3.7)**	(3.5)
	473.1	480.0
Tier 2		
Revaluation reserve	**3.7**	3.7
Collective impairment allowance	**15.1**	24.1
Contingency against collective provision add back (note 4)	**(8.3)**	(10.2)
Deductions from Tier 2 capital (note 3)	**(0.1)**	(3.5)
	10.4	14.1
Total capital	**483.5**	494.1

Notes

1) Permanent interest bearing shares include any adjustments for unamortised premiums and discounts.

2) Intangible assets do not qualify as capital for regulatory purposes.

3) Certain deductions from capital are required to be allocated 50% to Tier 1 and 50% to Tier 2 capital. Other deductions are Tier specific.

4) Deduction from the collective provision add back, reflecting the proportion of the provision that is disallowable for capital purposes.

Annual Business Statement for the year ended 31 March 2013

1. Statutory percentages

	2013 %	Statutory limit %
Lending limit	**19.2**	25.0
Funding limit	**11.5**	50.0

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986.

The lending limit measures the proportion of business assets not in the form of loans secured on residential property. Business assets are the total assets of the Group plus allowance for losses on loans and advances less liquid assets, investment properties, intangible assets and property, plant and equipment as shown in the Group Statement of Financial Position.

The funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals.

Securitised assets and related liabilities are excluded from the lending limit and funding limit calculations in line with the Building Societies Act 1986 as updated by the Modification of the Lending Limit and Funding Limit Calculations Order 2004.

The statutory limits are as laid down under the Building Societies Act 1986 as amended by the Building Societies Act 1997 and ensure that the principal purpose of a building society is that of making loans which are secured on residential property and are funded substantially by its members.

2. Other percentages

	2013 %	2012 %
As a percentage of shares and borrowings:		
Gross capital	**9.47**	7.57
Free capital	**7.16**	5.83
Liquid assets	**19.77**	27.64
As a percentage of mean total assets:		
Loss for the financial year	**(0.07)**	(0.12)
Management expenses	**0.66**	0.57

The above percentages have been prepared from the Group's accounts and in particular:

- 'Shares and borrowings' represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue excluding non-recourse finance, in each case including accrued interest.
- 'Gross capital' represents the aggregate of general reserves, available for sale reserve, revaluation reserve, cash flow hedging reserve, subscribed capital and profit participating deferred shares.
- 'Free capital' represents the aggregate of gross capital and collective impairment provisions for losses on loans and advances less intangible assets, investment properties and property, plant and equipment.
- 'Mean total assets' represent the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.
- 'Liquid assets' represent the total of cash and balances with the Bank of England, loans and advances to credit institutions and investment securities.
- 'Management expenses' represent the aggregate of administrative expenses, depreciation and amortisation.

Information relating to Directors' and Officers' other directorships and interests at 31 March 2013

Name, qualification and date of birth	Role	Date of appointment	Other directorships and interests
John Ainley LLB (Hons), CCIPD 28 September 1956	Non-Executive Director	18 May 2011	Trustee of Bloomsbury Festival The Leaders' Coach Limited
Claire Hafner MA, ACA 24 June 1959	Non-Executive Director	1 September 2011	LINK Interchange Network Limited OneVu Limited Vocalink Limited Vocalink Holdings Limited Voca Limited Voca Holdings Limited Immediate Payments Limited
Mark Nicholls MA (Cantab), MBA 5 May 1949	Chairman	1 January 2010	Burcot House Management Limited Northern Investors Company PLC EcoSecurities Group plc Rathbone Brothers Plc Rathbone Investment Management Ltd Protector of the National Lottery Fair Share Fund
Mark Preston BA (Hons), ACIB 11 February 1960	Non-Executive Director	18 May 2011	Chair of Development Council of Opportunity International UK Principal of Valere Capital
Martin Ritchley FCA, FCIB, Hon DBA (Coventry) 1 July 1946	Deputy Chairman and Senior Independent Director	1 September 2009	The ARC Addington Fund Royal Shakespeare Theatre Trust
Richard Sommers MA (Oxon), ACIB 4 September 1956	Non-Executive Director	1 October 2009	Treasurer and Fellow of Lady Margaret Hall
Colin Walklin BSc, FCA 9 May 1954	Non-Executive Director	20 July 2011	Aida Capital Limited SLTM Limited Standard Life Investments (Corporate Funds) Limited Standard Life Investments (Holdings) Limited Standard Life Investments Limited Standard Life Portfolio Investments Limited
Mark Gibbard BSc, FCA, MCT 31 August 1961	Group Finance Director	16 February 2011	
Andrew Jones BSc (Hons), FCIB, FCIS 21 April 1957	Group Risk Director	24 November 2010	Insignia Finance Limited White Label Lending Limited West Bromwich Homes Limited
Jonathan Westhoff BA (Hons) Financial Services, FCMA, CGMA, ACIB 11 July 1964	Chief Executive	5 May 2009	Millinet Limited West Bromwich Commercial Limited West Bromwich Homes Limited WBBS Computer Finance Limited

All Directors are members of the Society. None of the Directors have at any time in the year, or at the year end, any beneficial interest in shares or debentures of any associated body of the Society.

Service contracts

The Society's policy in relation to the duration of contracts for the Executive Directors is that their contract would normally continue until termination by either party, subject to the required notice or until retirement. The service contract is terminable with 12 months' notice if given by the Society or six months' notice if given by the Director. Jonathan Westhoff entered into his contract as Chief Executive on 25 May 2011, Mark Gibbard and Andrew Jones entered into their service contracts on 23 November 2010, on this basis.

For further details of the Executive Directors' service contracts, see the Directors' Remuneration Report on pages 28 to 30.

Documents may be served on any of the above named Directors at the following address: Addleshaw Goddard, Sovereign House, Sovereign Street, Leeds LS1 1HQ.

Senior management	Role	Society and subsidiary directorships
Andrew Conroy BSc (Hons), ACA	Divisional Director, Finance	Millinet Limited Central Processing Limited CL Mortgages Limited
Paul Field CMS	Divisional Director, Operations	West Bromwich Homes Limited CL Mortgages Limited West Bromwich Mortgage Company Limited
Manjit Hayre	Divisional Director, Credit Risk	
Richard J Hopwood	Sales and Marketing Director	West Bromwich Financial Planning Limited
Ian J Kilmartin BA (Hons), MSc	Divisional Director, Business Transformation and Change	
Thomas M Lynch MA, ACA	Divisional Director, Treasury & Capital Management	West Bromwich Mortgage Company Limited CL Mortgages Limited WBBS Computer Finance Limited West Bromwich Financial Planning Limited Sandwell Commercial Finance No. 1 Plc Sandwell Commercial Finance No. 2 Plc Sandwell Finance Holdings Limited
John McErlean MIIA, FIIA	Head of Internal Audit	
Jacqui Randle BSc, Chartered FCIPD	Head of Human Resources	WBBS (SRS) Limited

Glossary

Set out below are the definitions of the terms used within the Annual Report and Accounts to assist the reader and to facilitate comparison with other financial institutions:

Arrears – Customers are said to be in arrears when they are behind in fulfilling their obligations with the result that an outstanding loan commitment is unpaid or overdue. The value of the arrears is the value of the payments that have been missed.

Asset backed securities (ABS) – Securities that represent an interest in an underlying pool of referenced assets. Typically these assets are pools of residential or commercial mortgages.

Basel II – Basel II is the second of the Basel Accords, which are recommendations on banking laws and regulations issued by the Basel Committee on Banking Supervision. Basel II defines the methods by which firms should calculate their regulatory capital requirements to hold sufficient levels of capital to protect the financial system against unexpected losses.

Basel III – In December 2010, the Basel Committee on Banking Supervision issued the Basel III rules text, which presents the details of the strengthened global regulatory standards on bank capital adequacy and liquidity. The standards will be phased in gradually from 2014.

Buffer liquidity – Cash and investments with the UK government (deposits with the Bank of England or holdings of UK Gilts and similar investments) and with supranational institutions. The limit is set by the Prudential Regulation Authority (PRA).

Commercial lending – Loans secured on commercial assets. Commercial assets can include office buildings, industrial property, hotels, medical centres, shopping centres, farm land, buy-to-let and housing association properties.

Commercial mortgage backed securities (CMBS) – Securities that represent interests in a pool of commercial mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and/or principal).

Contractual maturity – The final payment date of a loan or other financial instrument, at which point all the remaining outstanding principal and interest is due to be paid.

Core Tier 1 capital – The highest quality regulatory capital resources, defined by the PRA as general reserves plus profit participating deferred shares less intangible assets and other deductions, including excess impairment provisions and securitisation positions.

Core Tier 1 ratio – Core Tier 1 capital as a percentage of risk weighted assets.

Credit risk – The risk that a customer or counterparty is unable to honour their obligations as they fall due.

Debt securities in issue – Transferable certificates of indebtedness of the Group to the bearer of the certificates. These are liabilities of the Group and include certificates of deposit and non-recourse finance.

Delinquency – A debt or financial obligation is considered to be in a state of delinquency when payments are overdue. When a person is in arrears, their entire outstanding balance is said to be delinquent.

Derivative financial instruments – A derivative financial instrument is a type of financial instrument (or an agreement between two parties) whose value depends on the underlying asset, index or reference rate it is linked to. The Group uses derivative financial instruments to hedge its exposures to market risks such as interest rate, equity and currency risk.

Effective interest method – The method used to measure the carrying value of a financial asset or a liability and to allocate associated interest income or expense over the relevant period. The calculation includes all fees and penalties paid or received between parties to the contract that are considered integral.

Fair value – Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial Services Compensation Scheme (FSCS) – The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the PRA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.

Free capital – The aggregate of gross capital and collective impairment provisions for losses on loans and advances to customers less intangible assets, investment properties and property, plant and equipment.

Funding limit – Measures the proportion of shares and borrowings not in the form of shares held by individuals excluding non-recourse finance.

Gross capital – The aggregate of general reserves, available for sale reserve, revaluation reserve, cash flow hedging reserve, subscribed capital and profit participating deferred shares.

Goodwill – Goodwill arises on the acquisition of subsidiary undertakings, joint ventures, associates or businesses and represents the excess of the fair value of consideration over the fair value of identifiable net assets and contingent liabilities acquired at the date of acquisition.

Impaired loans – Loans which have been assessed and there is evidence to suggest that the Group will not receive all of the cash flows or there is an expectation that these will be received at a later date.

Individual Liquidity Adequacy Assessment (ILAA) – The Group's internal assessment of the levels of liquidity that need to be held by the Society to meet its regulatory liquidity requirements.

Individually/collectively assessed – At each statement of financial position date the Group assesses whether or not there is objective evidence that individual financial assets (or groups of financial assets with similar credit characteristics) are impaired.

Interest rate risk – Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Internal Capital Adequacy Assessment Process (ICAAP) – The Group's own assessment, as part of Basel II requirements, of the levels of capital that it needs to hold in respect of the risks it faces under a business as usual scenario and a variety of stress scenarios.

International Swaps and Derivatives Association (ISDA) master agreement – A standardised contract developed by ISDA and used to enter into bilateral derivatives transactions.

Investment securities – Assets representing certificates of indebtedness of credit institutions, public bodies or other undertakings excluding those issued by central banks.

Investors in People – An accreditation which recognises the support the Group provides for its people.

Lending limit – Measures the proportion of business assets not in the form of loans fully secured on residential property. The calculation of the lending limit is explained in the Annual Business Statement.

Liquid assets – Total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and investment securities.

Liquidity risk – The risk that the Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash inflows and outflows.

Loan to value ratio (LTV) – A ratio which expresses the amount of a mortgage as a percentage of the value of the property. The Group calculates residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index (HPI)).

Loans past due/past due loans – Loans on which payments are overdue including those on which partial payments are being made.

Management expenses – Management expenses represent administrative expenses. The management expense ratio is management expenses expressed as a percentage of mean total assets.

Market risk – The risk that movements in market risk factors, including foreign exchange rates, interest rates, credit spreads and customer-driven factors will reduce income or portfolio values.

Mean total assets – Represents the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.

Medium term notes (MTN) – Corporate notes continuously offered by a company to investors through a dealer.

Member – A person who has a share investment or a mortgage loan with the Society.

Mortgage backed securities (MBS) – Assets which are referenced to underlying mortgages.

Net interest income – The difference between interest received on assets and interest paid on liabilities.

Net interest margin – This ratio calculates the net interest income as a percentage of mean total assets.

Non-recourse finance – A secured loan (debt) that is secured by a pledge of collateral but for which the borrower is not personally liable. If the borrower defaults, the lender/issuer can seize the collateral, but the lender's recovery is limited to the collateral alone.

OECD – Used to refer to member countries of the OECD (Organisation for Economic Co-operation and Development). The OECD is an international organisation of countries with highly developed economies and democratic governments. The OECD has 34 member countries including (but not limited to) key European countries, the United States, Canada and Japan.

Operational risk – The risk of loss arising from inadequate or failed internal processes, people and systems or from external events.

Other income – The income received from selling non-mortgage and savings products (e.g. home and contents insurance, investment products, other insurances and property rental income).

Permanent interest bearing shares (PIBS) – Unsecured, deferred shares that are a form of Tier 1 capital. PIBS rank behind the claims of all depositors, payables and investing members of the West Brom and rank pari-passu with profit participating deferred shares.

Profit participating deferred shares (PPDS) – A form of unsecured capital that are included as Core Tier 1 capital. PPDS rank behind the claims of all depositors, payables and investing members of the West Brom and rank pari-passu with PIBS.

Prime – Prime mortgages are those granted to the most credit worthy category of borrower.

Renegotiated loans – Loans are classed as renegotiated with the customer's consent, when their terms have changed during the year. Loans and advances are generally renegotiated either as part of an ongoing customer relationship or in response to an adverse change in the circumstances of the borrower.

Repo/Reverse repo – Short to medium-term funding agreements which allow a borrower to sell a financial asset, such as ABS or Government bonds as security for cash. As part of the agreement the borrower agrees to repurchase the security at some later date. For the party selling the security (and agreeing to repurchase it in the future) it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future), it is a reverse repurchase agreement or reverse repo.

Residential loans – Money loaned to individuals rather than institutions. Residential mortgage lending is secured against residential property.

Residential mortgage backed securities (RMBS) – A category of asset backed securities (ABS) that represents interests in a group of residential mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and/or principal).

Risk appetite – The articulation of the level of risk that the Group is willing to take (or not take) in order to safeguard the interests of the Society's members whilst achieving business objectives.

Risk weighted assets (RWA) – The value of assets, after adjustment, under Basel II rules to reflect the degree of risk they represent.

Securitisation – A process by which a group of assets, usually loans, are aggregated into a pool which is used to back the issuance of new securities. A company transfers these assets to a special purpose entity which then issues securities backed by the assets. The Group has established securitisation structures as part of its funding activities.

Shares – Money deposited by a person in a retail savings account with the Society. Such funds are recorded as liabilities for the Society.

Shares and borrowings – The total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue, including accrued interest and fair value adjustments for hedged risk.

Sub-prime – Loans to borrowers typically having weakened credit histories that include payment delinquencies and, in some cases, potentially more severe problems such as court judgments and discharged bankruptcies.

Tier 1 capital – A measure of financial strength. Tier 1 capital is divided into Core Tier 1 and other Tier 1 capital. Core Tier 1 capital comprises general reserves from retained profits and profit participating deferred shares. The book values of goodwill and intangible assets are deducted from Core Tier 1 capital and other regulatory adjustments may be made for the purposes of capital adequacy. Qualifying capital instruments such as PIBS are included in other Tier 1 capital (i.e. not Core Tier 1).

Tier 2 capital – Comprises the Group's revaluation reserve and collective impairment allowance (for exposures treated on a Basel II standardised basis). Certain regulatory deductions may be made for the purposes of assessing capital adequacy.

Wholesale funding – The total of amounts owed to credit institutions, amounts owed to other customers and debt securities in issue.

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