Skipton Building Society
Annual Report & Accounts

2009

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SKIPTON BUILDING SOCIETY

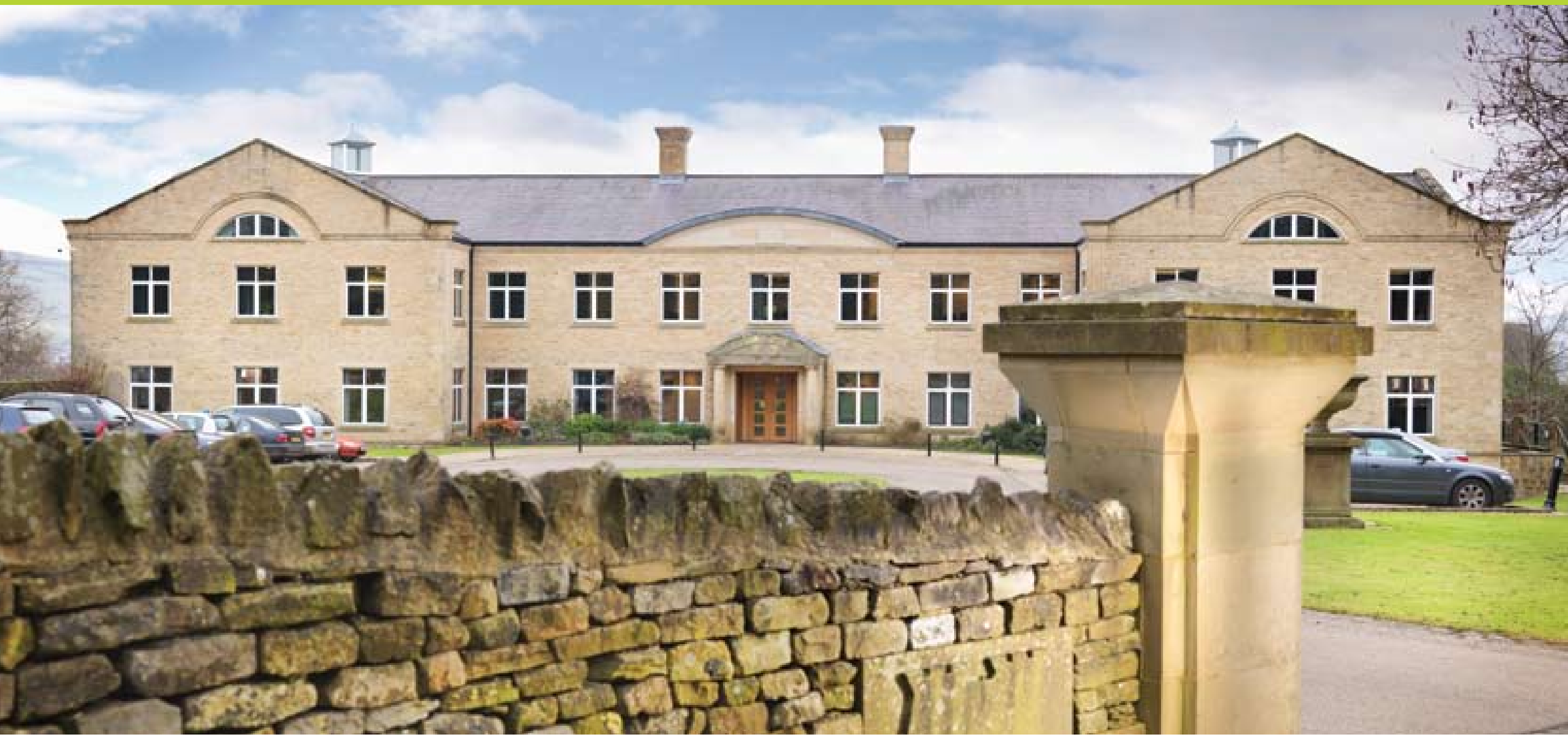
Contents

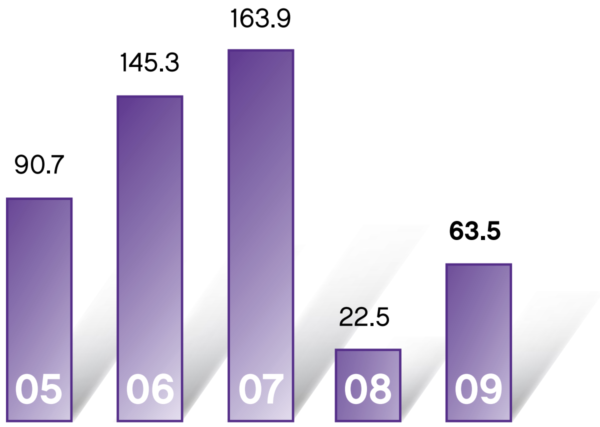
- Total Group pre-tax profit **£63.5m (2008: £22.5m)**
- Pre-tax profits from continuing operations **£18.0m (2008: £17.9m)**
- Solvency ratio Basel II **14.48% (2008: 12.28%)**
- Group retail share funding **up 29% to £10.5bn**
- Group total assets **up 14% to £15.6bn**
- Group management expenses **fell by 12% to 2.63%**
- Liquid assets **up 28% to £4.1bn**

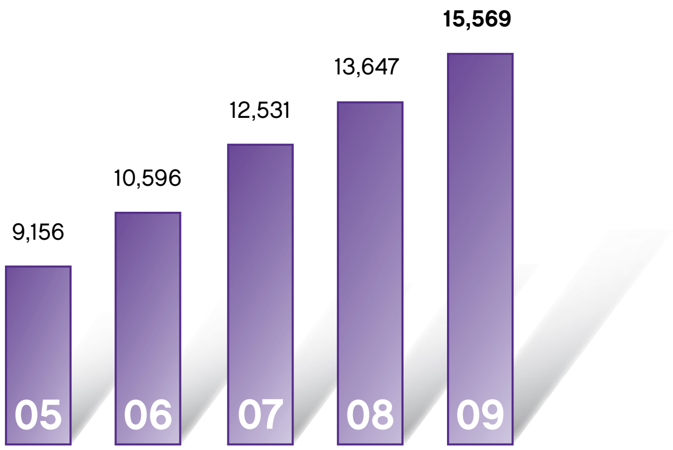
“It is testament to the robustness of the Group’s business model that Skipton ended the year with significant improvements to its capital ratios.”

D J Cutter
Group Chief Executive

Five Year Summary



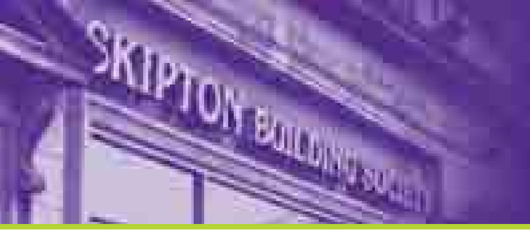




The Group's capital resources profile

	2005	2006	2007	2008	**2009**
Core Tier 1 ratio (%)	9.13	8.64	8.67	8.61	**9.37**
Total capital ratio (%)	13.10	12.88	12.30	12.28	**14.48**
Tier 1 ratio (%)	9.65	9.14	9.09	9.03	**10.77**
Tier 1 capital (before deductions*) (£m)	557	647	771	780	**873**
Tier 1 capital (after deductions*) (£m)	468	463	541	537	**691**
Gross capital (£m)	641	813	935	918	**1,063**
Free capital (£m)	480	557	631	606	**811**

* Intangible assets

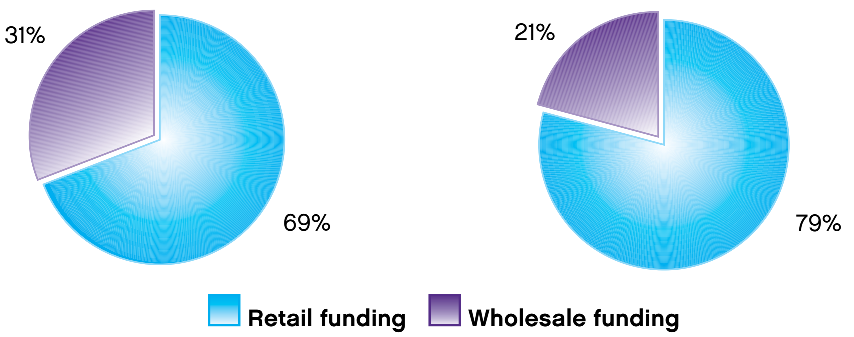


Group Income Statements	Re-presented* 2005 £m	Re-presented* 2006 £m	Re-presented* 2007 £m	Re-presented* 2008 £m	**2009 £m**
Net interest receivable	93.8	98.8	110.7	87.5	**53.3**
Other operating income	335.1	415.8	433.1	351.7	**386.5**
Total operating income	428.9	514.6	543.8	439.2	**439.8**
Share of profits from joint ventures and associates	1.3	1.0	3.7	3.9	**0.2**
Profit on disposals of subsidiary undertakings and associates	-	15.7	36.0	31.4	**-**
Administrative expenses	(328. 1)	(376.8)	(416.2)	(389.7)	**(383.7)**
Impairment losses on loans and advances	(7.9)	(5.6)	(5.4)	(34.6)	**(43.6)**
Impairment recoveries / (losses) on debt securities	-	-	-	(11.5)	**1.3**
Provisions for liabilities	0.4	(1.6)	(0.8)	(20.8)	**4.0**
Profit before tax from continuing operations	94.6	147.3	161.1	17.9	**18.0**
Tax (expense) / income	(25.9)	(32.6)	(36.3)	2.8	**(4.3)**
Profit from continuing operations	68.7	114.7	124.8	20.7	**13.7**
Operating profit / (loss) from discontinued operation (net of tax)	(2.8)	(1.6)	1.8	3.1	**4.2**
Profit on disposal of discontinued operation	-	-	-	-	**39.7**
Profit for the financial year	65.9	113.1	126.6	23.8	**57.6**
Attributable to:					
Members of Skipton Building Society	62.8	111.7	125.5	22.8	**57.4**
Non-controlling interests	3.1	1.4	1.1	1.0	**0.2**
	65.9	113.1	126.6	23.8	**57.6**
As at 31 December					
Total assets	9,156	10,596	12,531	13,647	**15,569**

* Prior periods have been re-presented in accordance with IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, to reflect the disposal of the 'Credit & Marketing Solutions' division, which became a discontinued operation during 2009.

	2008 £m	**2009 £m**
Profit before tax from continuing operations	17.9	**18.0**
Profit before tax from discontinued operations (note 17b)	4.6	**5.8**
Profit on sale of discontinued operations (note 17b)	-	**39.7**
Group profit before tax	22.5	**63.5**

2008 Retail v Wholesale funding **2009 Retail v Wholesale funding**



In 2009 your Society faced, along with other banks and building societies, a continuation of the worst financial crisis in a century. In order to come through these troubled times in the best possible shape, we focused on key imperatives: trading profitably; preserving and, if possible, increasing capital; maintaining our strong and diverse funding streams; holding good-quality liquid assets; managing impaired assets in a fair way; and improving efficiency across the Group. I am glad to say we achieved these core objectives and demonstrated once again the soundness of the diversification strategy which has featured heavily in my reports in recent years.

In late 2008 governments and central banks around the world had stared into the abyss at the prospect of a meltdown in the world's banking and financial systems. Thankfully, steps taken by governments around the world managed to stem contagion, but not before almost inconceivable losses were suffered by financial institutions. It goes without saying that financial impacts of this magnitude cannot be absorbed without having a profound and ongoing impact on the global financial system.

The Bank of England's response to the crisis was to pump liquidity into the system through steps like Quantitative Easing, to combat the wholesale funding market deadlock which ensued. It also lowered its Base Rate to 0.5% in order to support consumers struggling with debt against a backdrop of recession and increasing unemployment.

Both of these exceptional moves – the latter of which resulted in the lowest centrally set interest rate in the 315-year history of the Bank of England – have been broadly beneficial to the economy. They increased the supply of credit to businesses and individuals as well as boosting household disposable income for those remaining in employment as mortgage costs and inflation fell. However, while it is not certain that this will cause inflation to surge in the future, we need to be alert to this risk in the longer-term because of the sheer size of projected Government borrowing which in past decades has often precipitated a Sterling crisis.

> “As we enter calmer economic waters in the next few years, I am confident that the results of the Society will continue to underline the success of the unique strategy Skipton has pursued over the last two decades.”

All-in-all, the year did end better than it had begun. Most major economies, including the UK – albeit only marginally – seemed to have emerged by the year-end from the most severe recession since the Second World War. However, most commentators accept that the recovery journey will be tentative and slow, and therefore continued vigilance will be required by businesses and governments alike.

For the Society, such turbulent economic times have presented exceptional circumstances. One of the main impacts has been to dramatically reduce the interest income we earned and, in turn, the rates we could offer our savers, many of whom are partly – if not wholly – dependent on normal levels of interest rates for their day-to-day living. In 2009 we experienced, and continue to experience, fierce competition for retail savings as institutions reduced their reliance on wholesale funding. While this gave some relief to the proportion of the savings public who were able to take advantage of the attractive account offers which ensued, it significantly increased our overall cost of funds. In response to these circumstances, we announced action after the end of the financial year to increase our mortgage Standard Variable Rate ('SVR') from 3.50% to 4.95%. This change, which will come into effect from 1 March 2010, will redress the imbalance between our mortgage and savings rates and ensure our ongoing financial strength, while enabling us to maintain our long-term commitment to both our borrowers and our savers.

Given the uncertainty of funding sources, the mortgage market contracted over the year and we, like others, saw the size of our balance sheet reduce as a result, excluding the impact of the merger with Scarborough Building Society. In this environment our primary focus was on exercising the prudence and caution appropriate to current market conditions.

As a result, our prime residential mortgage portfolio is performing well compared to our peer group. We have seen an increase in arrears levels during the course of the year, mostly relating to our specialist lending subsidiaries which closed to new business in early 2008. However, while this has inevitably impacted our performance, we have seen arrears plateau in recent months due to our proactive but fair approach to supporting borrowers experiencing payment difficulties. Overall the percentage of the Group's mortgage portfolio in arrears continues to improve; however, we are acutely aware of the need to maintain vigilance to ensure this positive track record is maintained.

Against this background it may seem counter-intuitive to draw attention to our relatively strong Group results, headlined by a year-on-year increase in total pre-tax profit to £63.5m. This impressive performance is a direct result of the unique and successful diversification strategy we have pursued over many years, with most of our larger subsidiary investments recording profits. One particular highlight was the remarkable performance of Connells, our nationwide estate agency business, despite recent housing market volatility. The sale of our credit and marketing solutions business, Callcredit Information Group ('CIG'), also contributed £39.7m to our results.

Against this positive backdrop our main challenge is that our core mortgage and savings business posted an operating loss. This is why we are taking proactive steps including increasing our SVR – and the business re-organisation also announced after the end of the financial year – to ensure that this division returns to profit as quickly as possible.

Overall, we start 2010 in a strong financial position and this will improve further when interest rates start to rise. Caution will still be necessary as the extent of unemployment and the impact this could have on arrears trends cannot be predicted with certainty.

In such difficult economic times, the contributions of the individuals and organisations making up the Skipton Group become particularly important and I am glad to say that the staff of your Society and its subsidiaries have once again shown tremendous commitment, determination and creativity in order to ensure the continued success of this business.

The Society continues to demonstrate its staunch commitment, as a mutual, to the communities in which it operates, both through corporate donations and our independent Skipton Charitable Foundation.

Over the past year, we have donated more than £220,000 to organisations in the fields of Education, Sport, Financial Advice, the Arts and general community support. Our giving has ranged from small amounts in response to ad hoc requests from grass-roots charities and individuals doing special things, to major partnerships with organisations including the NSPCC children's charity; the Skipton Building Society Camerata orchestra which we helped to establish, and Molesey Boat Club, home to our team of 2012 Olympic rowing hopefuls.

Our Foundation has given a total of £139,000 over the year to charitable organisations nationwide.

This has also been a year of significant personnel change. David Cutter took over as Group Chief Executive in January and he and fellow Executive Director Richard Twigg were joined in the autumn by Tom Wood, our new Group Finance Director. This recently formed team of Executive Directors, underpinned by a new Society Retail Board and senior management structure, will ensure the business continues to focus on delivering outstanding products and services to its members.

Turning to Non-Executive Directors, we said goodbye during the course of the year to Bill Jack, who had served on the Board for nine years, part of the time as Vice Chairman. We wish him well for the future. We also welcome three new Non-Executive Directors. William Worsley and Nimble Thompson joined us on the completion of the merger with Scarborough Building Society in March, and John Spence, a former Director of Lloyds Bank who also served on the CIG Board for a time, was appointed in the summer.

This is my last Annual Statement as Chairman and I would like to take the opportunity of thanking all our staff in the Society and its many subsidiaries for the contribution they have made, in particular over the last five years. It has of course been a privilege to be Chairman of such an enterprising and committed business but it has also been fun, not perhaps a concept that would spring readily to mind in view of the difficult economic circumstances of the last couple of years. Yet this seems to me to aptly describe the sense of camaraderie, relish and sheer determination with which our Group rises to challenges arising from the environment in which we operate on behalf of the business and its members. As we enter calmer economic waters in the next few years, I am confident that the results of the Society will continue to underline the success of the unique strategy Skipton has pursued over the last two decades.

J B Rawlings

J B Rawlings

Chairman

24 February 2010

The Lyons family, customers of Bradford Branch

Introduction

It is pleasing to report an increase in total Group profits and capital in a year that will be remembered for the impact of the worst financial crisis in almost a century. The 'credit crunch' created a severe and deep recession resulting in the Bank of England Base Rate falling to 0.5% – a level never seen before in the Bank's 315-year history.

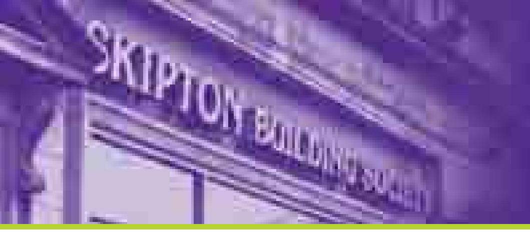
In light of the extreme trading conditions that these events caused, it is testament to the robustness of the Group's business model that Skipton ended the year with significant improvements to its capital ratios.

> "We all remain committed to ensuring that Skipton Building Society remains a successful and independent business run for the mutual benefit of the membership as a whole."

However, continued uncertainties around the strength of the economy; the condition of the Government's finances; the impact and unwinding of Quantitative Easing; the sustainability of asset prices; and, in particular, the distortions in the UK savings market, mean we remain vigilant and cautious.

Against this backdrop I am proud that our Group has achieved strong financial results which provide security to our members; the key financial highlights are as follows:

- **Improved profits**
  - Total Group pre-tax profit up £41.0m to £63.5m (2008: £22.5m)
  - Group pre-tax profit from continuing operations up £0.1m to £18.0m (2008: £17.9m)
- **Improved capital strength**
  - Core Tier One ratio up 9% to 9.4% (2008: 8.6%)
  - Tier One ratio up 20% to 10.8% (2008: 9.0%)
  - Solvency ratio up 18% to 14.5% (2008: 12.3%)
- **Strengthened our retail savings franchise**
  - 79% of funding is comprised of retail balances (2008: 69%), an increase of £2.3bn to £10.5bn partly due to the merger with Scarborough Building Society
- **Maintained high levels of liquidity**
  - Liquidity represents 29% of shares, deposits and liabilities (2008: 29%)
- **Prudent measured growth in mortgage assets**
  - Group mortgage assets increased by a net £1.3bn to £10.7bn predominantly due to the merger with Scarborough Building Society
  - Mortgage assets 98% funded by retail deposits (2008: 86%)



- **Net interest income reduced by £33m from £86m to £53m due to**
  - Operating in a low interest rate environment
  - The cost of holding high-quality, highly liquid balances compared to the cost of funding
  - Maintaining competitive rates paid to savers
- **Improved efficiency**
  - Society management expenses ratio of 0.35% (2008: 0.47%)

Savings

The ultra low interest rate environment has had a material impact on the income received by our saving members. However, as banks continue to reduce their over-reliance on the wholesale funding markets (one of the causes of the credit crunch), and building societies seek to protect their main source of funding, the demand for UK savings is intense. So, while the absolute rate of interest received by UK savers is low, the differential above Bank Base Rate is high. Skipton Building Society has not been immune to these conditions, which is a key reason for the reduction in our net interest rate margin.

The Society's savings balances increased by £2.3bn (or 29%) to £10.5bn during 2009. Balances increased by £1.8bn on the merger with Scarborough Building Society in March, and by £723m on acquisition of Capital One's savings portfolio (now rebranded as Castle Money) in July. During the year our savings customer numbers increased by 145,000 to 700,000.

Lending

In common with most lenders, our appetite for mortgage lending was modest by historical standards. Restricted wholesale markets and economic uncertainties meant that our priority in 2009 was to maintain high levels of liquidity and further improve our capital position. Gross mortgage lending was £0.4bn (2008: £1.5bn) and net mortgage lending was £(0.5)bn (2008: £0.4bn), ignoring the £2.1bn of balances transferred from Scarborough.

The low interest rate environment understandably helped our borrowers during the recession and it was pleasing to see total arrears balances reduce by 11% between their peak in May 2009 and the year-end.

Wholesale funding and capital

In January the Society raised a significant amount of wholesale funding at favourable rates under a repurchase agreement with a counterparty bank.

The unsecured wholesale funding markets were challenging at the start of the year and became more difficult for the Society and wider sector following our rating agency downgrades and the demise of Dunfermline Building Society.

In December, Skipton raised £650m under the Government Guarantee Scheme (one of only four societies which managed to launch such a transaction) which increased the percentage of wholesale funding not due until over one year to 58% (2008: 24%).

All of the Society's capital ratios improved markedly in the second half of the year. The Interim Results reported a Tier One capital ratio of 8.5% and this rose to 10.8% at 31 December 2009, largely due to the sale of the Society's investment in Callcredit Information Group ('CIG') and the benefit of the profit streams from our other trading subsidiaries.

Divisions

The advantages of the Society's diversification model came to the fore during 2009. Not only did the trading performance of the divisions contribute substantial profits to the Group during a time when low interest rates adversely impacted the Society, but the disposal of CIG demonstrated the inherent unrecognised value in the Society's investment portfolio.

Following a strategic review, the Society concluded that the ownership of a credit reference agency was no longer core to our long-term direction. Given that CIG had ambitious development plans both in the UK and overseas, we decided the time was right to realise this investment, achieving a profit on sale of £39.7m.

Our Estate Agency division produced an exceptional trading performance, recording a profit of £54.1m (2008: £10.4m) due to more favourable trading conditions and good cost control. It, too, benefited from its own diversified model including lettings, auctions and property asset

management. Following the significant housing market slump in the second half of 2008, Connells witnessed a welcome, and many would say unexpected, upturn in the number of housing transactions, although volumes remain approximately 20% below historic market norms.

Material events since the year-end

Although the Group remains profitable, it is important that the Society itself addresses the challenges of operating in such a low interest rate environment. Two announcements have been made since the year-end:

- On 1 March 2010, the Society is exercising its right to remove the ceiling on its mortgage Standard Variable Rate ('SVR') of 3% above Bank Base Rate, increasing its SVR to 4.95%. The ceiling will be reimposed once exceptional circumstances no longer prevail. This will help us to continue delivering long-term good value to both our borrowers and our savers.
- A business re-organisation programme which will control costs and prepare the business to seize future opportunities while re-emphasising our paramount focus on understanding and meeting the needs of our members. As part of this process a number of people will be leaving the business as we continue our focus on improving our operational productivity and efficiency.

> "Continued uncertainties around the strength of the economy… mean we remain vigilant and cautious."

Today, Skipton Building Society and Chesham Building Society announced their intention to merge, subject to a vote by Chesham's members and FSA approval. Chesham is already well known to Skipton, as we provide its IT systems. This transaction is in-keeping with our stated position of welcoming mergers which are in the best interests of our members. Although Chesham is comparatively small compared to Skipton, the transaction will provide three more branches for our members and will marginally improve the Group's capital position.

Outlook

Although we anticipate that any growth in the economy will be anaemic, and uncertainties still exist regarding the consequences of the Government's financial deficit, we remain confident that the Skipton Group will deliver another solid performance for our members in 2010 in spite of the challenges associated with operating in such a low interest rate environment.

Finally, my sincere thanks to our staff for their service and support for members during what has been a demanding year. We all remain committed to ensuring that Skipton Building Society remains a successful and independent business run for the mutual benefit of the membership as a whole.

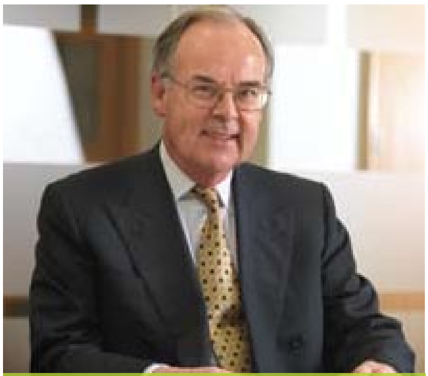
David Cutter

D J Cutter

Group Chief Executive

24 February 2010

Russell Smith, customer of Glasgow Branch


John Rawlings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Peter (Nimble) Thompson


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Noel Hutton


William Worsley

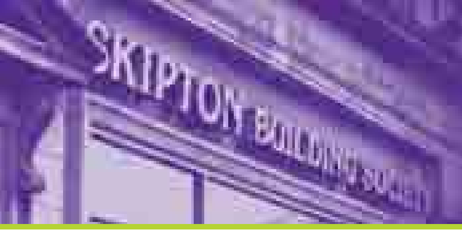

Paula Hay-Plumb


Alexandra (Sandy) Kinney


Alastair Findlay


Richard Twigg


Tom Wood



John Rawlings

Chairman

Age 63

John Rawlings was appointed to the Board as a Non-Executive Director in 1995 and became Chairman of the Society in 2005. He is also Chairman of the Nominations Committee. Since 1994 he has been a Non-Executive Director of a number of companies, chiefly in the financial sector, including the Financial Ombudsman Service. His earlier career was spent at the Foreign Office and the merchant bank, Morgan Grenfell & Co Ltd, where he became Deputy Chairman.

David Cutter

Group Chief Executive

Age 48

David Cutter, a Chartered Accountant, joined the Society as Head of Audit in 1993, was appointed to the Board in 2000 and became Chief Executive in January 2009. David was Chairman of the Society's Operational Board from 2002 until 2005 and had Board responsibility for the Group's subsidiary businesses until December 2008. He chairs the Society's Senior Management Committee and is a member of the Asset & Liability Committee and Group Retail Credit Committee. Externally, he is a Governor of Malsis Preparatory School.

Peter (Nimble) Thompson

Non-Executive Director

Age 63

Nimble Thompson joined Skipton in April 2009, and sits on the Audit Committee, having been on Scarborough's Board for three years. He qualified as a solicitor and became Senior Partner and then Deputy Chairman of Eversheds before he retired in 1999. Nimble is Chairman of N G Bailey and a Non-Executive Director of a number of other companies. He was also Chairman of Leeds Metropolitan University for six years, Chairman of Eureka! until 2007 and was Regional Chairman of the Institute of Directors in Yorkshire and the Humber until June 2009, and is a Non-Executive Director nationally.

Peter Hales

Non-Executive Director

Age 63

Peter Hales joined the Board as a Non-Executive Director in May 2007 and is also a member of the Audit Committee. Prior to joining the Board he was Sales and Marketing Director of Norwich Union, having previously been a Director of General Accident and CGU. He was President of the Chartered Insurance Institute, the professional body for the insurance industry in 2006. He is also a Director of Just Retirement Plc and Unum Ltd, a member of the Accenture Insurance Advisory Board and a member of the Advisory Board of Simply Biz plc.

John Spence

Non-Executive Director

Age 59

John Spence joined the Board in June 2009, having served on the Callcredit Board for two years prior to that. He serves on the Audit Committee. John was previously a Director of Lloyds TSB and other current appointments include directorship of HM Revenue & Customs and Capital for Enterprise Ltd. Blind himself, John is President or Chairman of several national charities, mainly in the disability field, and was awarded the OBE in 2006.

Noel Hutton

Non-Executive Director

Age 60

Noel Hutton joined the Board as a Non-Executive Director in July 2004. He is a member of the Nominations Committee and chairs the Remuneration Committee. Before his retirement in 2004, he was a partner of Hammonds, the international law firm, where he specialised in corporate finance.

William Worsley

Non-Executive Director

Age 53

William Worsley joined the Board in 2009 and serves on the Remuneration Committee. Formerly Chairman of Scarborough Building Society, he is a Fellow of the Royal Institution of Chartered Surveyors and is President of the Country Land & Business Association ('CLA'). A Non-Executive Director of The Brunner Investment Trust plc and a former member of the Private Banking Board of the merchant bank Guinness Mahon & Co. His early career was spent with property consultants Savills and Humberts.

Paula Hay-Plumb

Non-Executive Director

Age 49

Paula Hay-Plumb, a Chartered Accountant, joined the Board as a Non-Executive Director in June 2006. She chairs the Audit Committee and is a member of the Remuneration Committee. Paula's previous roles include Group Treasurer and then Group Financial Controller for Olympia & York Canary Wharf; Finance Director and subsequently Chief Executive of English Partnerships; and Corporate Finance and Group Reporting Director at Marks & Spencer. Paula is a Non-Executive Director of the Forensic Science Service. She also chaired the Coalfields Taskforce, and was a founding trustee of The Coalfields Regeneration Trust.

Alexandra (Sandy) Kinney

Non-Executive Director

Age 51

Sandy Kinney joined the Board as a Non-Executive Director in July 2003 and is a member of the Remuneration Committee and the Nominations Committee. During her career as an accountant, Sandy was a partner of PricewaterhouseCoopers and was previously a Director at KPMG. In June 2005, she was appointed by the FSA as a Non-Executive Director of the Financial Services Compensation Scheme.

Alastair Findlay

Vice Chairman

Age 57

Alastair Findlay, a Chartered Accountant, joined the Board as a Non-Executive Director in June 2006, and was appointed Vice Chairman in May 2008. He is a member of the Nominations Committee and has served on the Audit Committee. After a number of years' experience in the corporate finance department of a City investment bank, he was Group Finance Director of The Mersey Docks and Harbour Company from 1996 to 2005. Alastair is also Vice Chairman of the Countess of Chester Hospital NHS Foundation Trust and an independent Director of the trustees of the main AMEC plc pension funds.

Richard Twigg

Group Commercial Director

Age 45

Richard Twigg is a Chartered Accountant who joined the Skipton Group in 1993. Having previously been Finance Director of HML and then Connells, he was appointed to the Board in 2002 and served as Group Finance Director until 2009. As Group Commercial Director he has responsibility for managing the Group's portfolio of subsidiary companies. He chairs the Asset & Liability Committee and is a member of the Group's other risk management committees. Richard is a trustee of the Society's Charitable Foundation and is a governor of Ermysted's Grammar School, Skipton, and Menston Primary School.

Tom Wood

Group Finance Director

Age 37

Tom, a Chartered Accountant, was appointed to the Board in September 2009 on joining the Skipton Group as Group Finance Director. Prior to joining Skipton Group, Tom has worked in financial services holding senior leadership roles in Barclays (predominantly in the UK Retail Division); as Group Finance Director for Derbyshire Building Society; and worked with Northern Rock to deliver their legal and capital restructure. He is a member of the Senior Management Committee, chairs the Group Retail Credit Committee and is a member of each of the Group's risk management committees.

Group Structure

Skipton Building Society is the UK's fourth largest building society, with approximately 830,000 members, £15.6bn of assets and a national presence represented by its 89 branches. Founded in 1853, Skipton is an innovator in the field of mortgage and investment products. It heads up the Skipton Group, whose divisions have significant interests in estate agency and related businesses (through Connells); third party mortgage servicing (Homeloan Management); independent financial and related advisory businesses; and support services to the mutual sector.

The Group's operating results are regularly reviewed by the chief operating decision maker in the following reportable segments. Each segment offers different products and services and is managed on a divisional basis in line with the Group's management and internal reporting structure.

- Mortgages and Savings – principally the Society, but also includes specialist mortgage businesses Amber Homeloans and North Yorkshire Mortgages, and deposit taking and lending in Jersey and Guernsey through Skipton International.
- Mortgage Services – mortgage administration services, principally Homeloan Management ('HML'), also includes Specialist Mortgage Services and Baseline Capital.
- Estate Agency – including survey and valuations, conveyancing, lettings, asset management and mortgage broking carried out through Connells.
- Financial Advice – provision of financial advice and broking services through five separate financial advice companies.
- Credit & Marketing Solutions – provision of credit reference agency and database services by Callcredit Information Group, which became a discontinued operation from 7 December 2009 on disposal.
- Investment Portfolio – includes holding companies and a number of other small trading companies that do not fall within the core operating segments. These companies are not of a material size to the Group.

Overview

It is pleasing to report that the Skipton Group has traded profitably throughout the economic turmoil of the past two-and-a-half years, with an increase in pre-tax profits in 2009 to £63.5m compared to the profits reported in 2008 of £22.5m. Despite being faced with one of the toughest trading environments in decades, our unique Group structure has allowed us to generate improved profitability and thereby strengthen capital and liquidity.

The 2009 Annual Report & Accounts is the first to reflect the enlarged Skipton Group following its merger with Scarborough Building Society ('Scarborough') on 30 March 2009. On the date of merger, the Group's total assets increased by £2.6bn.

In the face of the challenging economic environment we have focused on a number of key imperatives:

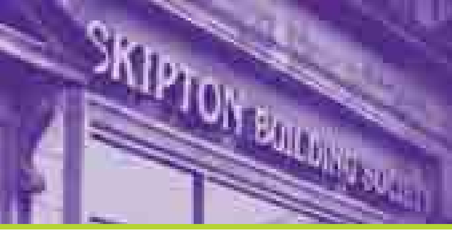
- Ensuring the Group continues to trade profitably.
- Increasing capital ratios.
- Maintaining a strong and diversified funding base.
- Holding high levels of quality liquid instruments.
- The effective management of impaired assets.
- Increasing efficiency across the business.

As a consequence of this focused approach the Group has continued to put measures in place to ensure that it emerges from the current economic cycle in a stronger position. Key management actions to deliver these imperatives included:

- Managing down the level of new mortgage lending, although still offering competitive products for customers meeting our prudent lending criteria. Excluding the merger with Scarborough, net mortgage balances have reduced by approximately 8%.
- Reducing the Group's reliance on wholesale funding markets by attracting new retail depositors with a range of competitive products. Overall, the level of wholesale funding within the Group has decreased from 31.0% to 20.6%.
- Placing more assets in high-quality liquidity and lower-risk investments, including placing more funds on deposit with the Bank of England.
- Reviewing the Group's underlying cost base to ensure the business remains efficient.
- Following a strategic review, the Credit & Marketing Solutions division (discontinued operations) was sold.

During the year, the Society, along with many others in the sector, was subject to a credit rating downgrade by Moody's and Fitch. Many wholesale depositors, such as local government authorities, use credit ratings as the main basis on which to place funds. Whilst the Group was already actively managing its reliance on wholesale funding, the ratings agencies' decisions accelerated our switch to higher levels of retail funding. The Group has attracted new retail customers and as part of this strategy acquired the UK retail savings of Capital One in July.

The incremental cost of retail deposits, at a time when rates charged to customers on variable rate mortgages has reduced, has resulted in the net interest margin of the Group reducing from 0.66% to 0.36%. The reduction



in interest margin in 2009 has been exacerbated by an increasingly distorted retail savings market, where the largest international banks, as well as the nationalised and part-nationalised banks, are seeking to increase their share of retail deposits.

The regulatory capital position of the Society (Solo) and Group (UK Group) remains strong with a capital adequacy, on a Basel II basis, of 186% (2008: 165%) and 192% (2008: 162%) respectively and a Group solvency ratio of 14.5% (2008: 12.3%). The Group's Tier One capital position is set out below:

	2009	2008
Tier 1 capital (£m)	**691**	537
Tier 1 capital (%)	**10.77**	9.03

Financial performance

Group pre-tax profits for 2009 were £63.5m (2008: £22.5m). The table below sets out the profit contribution of the Group's continuing and discontinued operations:

	2009 £m	2008 £m
Profit before tax from continuing operations	**18.0**	17.9
Profit before tax from discontinued operations (note 17b)	**5.8**	4.6
Profit on sale of discontinued operations (note 17b)	**39.7**	-
Group profit before tax	**63.5**	22.5

The Group's total profits include a number of items which we consider to be non-routine and the following table seeks to adjust the reported profit for such items:

	2009 £m	2008 £m
Group profit before tax	**63.5**	22.5
Non-routine items:		
Profit on sale of subsidiary companies	**(39.7)**	(9.1)
Profit on sale of investment in associate	**-**	(22.3)
Financial Services Compensation Scheme levy	**(4.3)**	16.3
(Recoveries) / impairment of investment securities	**(1.3)**	11.5
Curtailment gain on closure of pension schemes	**(10.4)**	(6.3)
Impairment of goodwill	**12.0**	5.9
Net (gains) / losses from fair value volatility	**(3.9)**	3.3
Merger expenses	**4.8**	0.7
Profit before tax after adjusting for non-routine items	**20.7**	22.5

The current year adjustments highlighted above are as a result of the following:

- During the year the Group disposed of its Credit & Marketing Solutions division achieving a profit of £39.7m, thereby bolstering its already strong capital position.
- The provision for the Financial Services Compensation Scheme levy, representing our share of the costs of the bank failures, covers a period of 24 months rather than the 36 months previously recognised (of which six months has been paid during the year). This change follows recently issued FSA guidance and means our approach is consistent with the emerging industry consensus and resulted in a provision release of £4.3m.
- Recoveries / impairment of investment securities includes a credit of £3.0m being the sale proceeds in relation to the Group's £11.0m exposure to Kaupthing Singer & Friedlander Limited which failed in 2008. We had provided for the full £11.0m exposure within the 2008 Accounts since it was unclear whether any of the investment would be realised. It also includes a provision of £0.8m against a small investment in a tranche of commercial mortgage backed securities (the total exposure is £6.7m), and a £0.9m loss on the sale of a small tranche of commercial mortgage backed securities.
- In light of performance in the continuing adverse market conditions, the Group, based upon objective evidence, provided £12.0m (2008: £5.9m) against the carrying value of goodwill in a number of subsidiary companies (see note 18 for details).
- During the year the Society closed its defined benefit pension scheme to future accrual, resulting in a curtailment gain of £10.4m recognised in the Income Statement.
- Net movements in fair value volatility arise from changes in the value of certain financial instruments, largely due to fluctuations in interest rates. These timing differences reverse over time.
- Merger expenses represent legal and other expenses related to the merger with Scarborough Building Society.

Whilst our adjusted pre-tax profits are slightly down on the performance achieved in 2008, the Group has remained consistently profitable throughout a severe economic recession. During this period we have maintained our prudent approach to impairment provisioning and the carrying value of our investments.

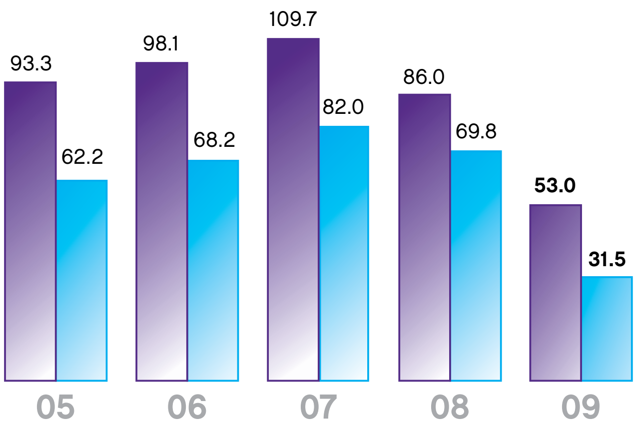
A further analysis of the Group's Income Statement, excluding the above non-routine items, is as follows:

	2009 £m			2008 £m		
	Total*	Continuing operations	Discontinued operations	Total*	Continuing operations	Discontinued operations
Net interest income	53.0	53.3	(0.3)	86.0	87.5	(1.5)
Other income	431.3	382.6	48.7	404.4	355.0	49.4
Share of profits from joint ventures and associates	0.2	0.2	-	3.9	3.9	-
Total income	484.5	436.1	48.4	494.3	446.4	47.9
Administrative expenses	(419.9)	(377.3)	(42.6)	(432.7)	(389.4)	(43.3)
Regulatory and other provisions	(0.3)	(0.3)	-	(4.5)	(4.5)	-
Impairment losses on loans and advances	(43.6)	(43.6)	-	(34.6)	(34.6)	-
Adjusted profit before tax	20.7	14.9	5.8	22.5	17.9	4.6

*The following income statement analysis on pages 18 and 19 is based upon the total profit columns above and excludes non-routine items.

Net interest income

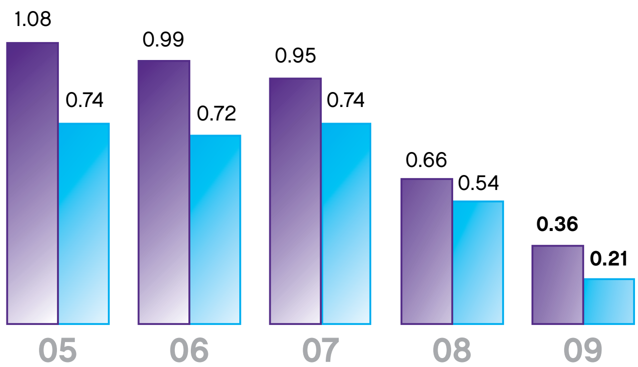
Since the commencement of the current economic downturn, the Group has sought to reduce its dependence on wholesale funding by offering competitive retail deposits to its savers. The Group is also holding a higher level of liquid assets with a focus on low-risk and highly liquid securities, such as gilts and deposits with the Bank of England.



Net interest income (£m)

These measures, required to ensure the stability of the business, have come at a cost to the interest margin – especially at a time of lower interest income from our variable rate mortgages. The Group's net interest income reduced by 38% during the year to £53m, with margin reducing from 0.66% to 0.36%. The main driver for the reduction in interest margin was the increasing costs of obtaining wholesale and retail funding and the continued low interest rate environment.

The Society's Standard Variable Rate ('SVR') is currently capped at 3% above Bank Base Rate, however, as exceptional economic conditions persist, in early 2010 the Group took the decision to raise its SVR to address the margin pressures experienced throughout 2009. From 1 March 2010 the Society's SVR will increase from 3.50% to 4.95% which will remain in line with the market place and below the average SVR of the top 10 UK building societies. This decision will also provide the Group with the flexibility to continue offering competitive rates to our savers, who have suffered in the low interest rate environment.



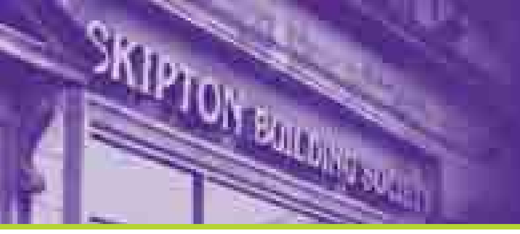
Interest margin (%)

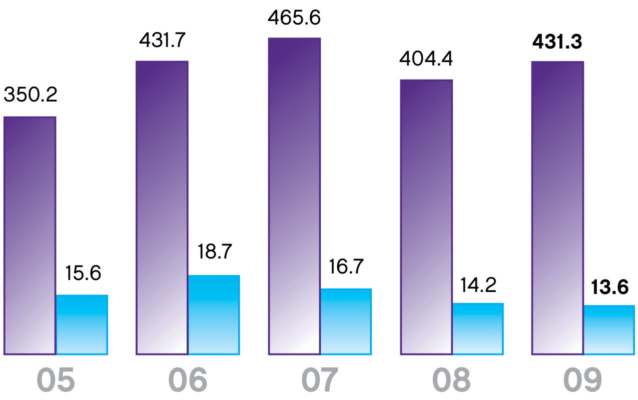
Other income

The Group's other income represents the income earned from our divisions together with insurance commissions, income from the sale of investment products and other non-margin income.

The Group's underlying other income for the year was £431m, up 7% (2008: £404m). Other income by division is set out below:

	2009 £m	2008 £m
Mortgages and Savings	18.1	15.8
Mortgage Services	86.4	88.7
Estate Agency	213.0	178.1
Financial Advice	37.8	35.1
Credit & Marketing Solutions	48.7	49.4
Investment Portfolio	38.8	49.8
Inter-division adjustments	(11.5)	(12.5)
	431.3	404.4





Other income (£m) Group Society

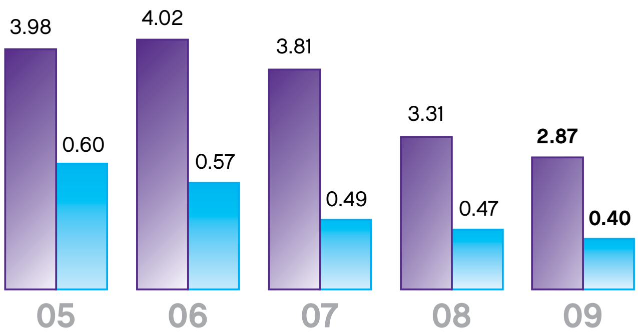
For details of the Group's performance by business area refer to pages 25 to 28.

Administrative expenses

Total administrative expenses, excluding non-routine items, fell marginally by 3% to £420m (2008: £433m) reflecting cost control measures across the Group that have been required as transaction levels have decreased and to ensure we reap the benefits of efficiency savings in future years.

The Society has managed, despite its increase in staff numbers following the merger with Scarborough, to reduce its ratio of administrative expenses to mean assets from 0.47% in 2008 to 0.40%. Including non-routine items this has reduced from 0.47% to 0.35%.

At a Group level, this management expense ratio (calculated by expressing administrative expenses as a percentage of mean assets) is less comparable, given the investments we have made in our trading businesses. However, the Group-wide cost reductions achieved in 2009 have resulted in this ratio falling from 3.31% to 2.87%. On a continuing basis, including non-routine items this ratio has fallen from 2.98% to 2.63%.



Management expense ratio (%) Group Society

Impairment losses on loans and advances

The Group's impairment charge on loans and advances increased year-on-year to £44m (2008: £35m), with the majority of the charge arising from the specialist residential mortgage loans held in Amber Homeloans. Impairment losses of £13m arising in the former Scarborough subsidiary, North Yorkshire Mortgages, were accounted for within merger fair value adjustments. In the Society an impairment charge of £10m (2008: £4m) was recognised against mortgage balances of £8,122m (2008: £7,594m). Whilst this charge has increased year-on-year in reflection of current market conditions, it remains a small ratio of overall mortgages held, once again demonstrating the high quality of the Society's core mortgage assets.

The performance of the Group's residential mortgages continued to be satisfactory in this context, with 1,522 cases (2008: 1,053) at the year-end where the arrears balance was greater than 2.5% of the total outstanding balance, representing 1.57% (2008: 1.16%) of the book.

The Group continues to direct its resources into operational areas which will have the most impact on containing the level of mortgages that go into arrears or possession. This has included ensuring that appropriate resources are allocated to the collections area of the business and developing proactive solutions for supporting struggling borrowers in getting their accounts back on track.

The loan books in our Guernsey-based subsidiary, Skipton International, and our debt factoring business, Skipton Business Finance, remain of high quality and the charge for impairment losses on these loans remains negligible at £0.4m (2008: £0.4m) for the year.

Mergers

On 30 March 2009 the Society merged with the former Scarborough Building Society. Scarborough's Board independently reached the conclusion that merging with Skipton was in the best interests of its members, given the current uncertain economic environment and in order to safeguard the long-term best interest of its members. From Skipton's perspective, the merger provided an opportunity for further growth, building on our strong position within the financial services sector by adding attractive and complementary customer franchises to our existing operations.

More details on how the merger impacted the Group position are shown in note 38 to these Accounts.

In February the Society announced its intention to merge with Chesham Building Society. If the proposal is approved by Chesham Building Society's members and subsequently confirmed by the FSA, the merger is expected to become effective through the transfer of all of Chesham Building Society's engagements to Skipton on 1 June 2010.

Financial position

Loans and advances to customers

The Group has continued its strategy of concentrating on maintaining a strong liquidity base by controlling new mortgage lending growth in 2009. Excluding balances arising from Scarborough and its subsidiaries, gross mortgage balances reduced by 8%. The combined Society has maintained prudent lending and further tightened its lending criteria where appropriate to attract higher quality borrowers.

An analysis of mortgage advances is shown below:

	2009 £m	2008 £m
Society	**298.9**	1,253.7
Amber Homeloans*	**3.5**	160.1
North Yorkshire Mortgages*	**0.5**	-
Skipton International	**104.1**	88.0
	407.0	1,501.8

*Following the decision to cease new lending in 2008, these advances represent further loans to existing borrowers and stage payments on self-build loans.

Of approved new mortgage lending, fixed rate products continued to be the most popular products, attracting 62% of all completions, as customers tried to protect themselves from the continued market uncertainty. Our lending continues to be well diversified by product type and geographical distribution, with 64% (2008: 70%) of the Society's new lending having a loan-to-value ('LTV') ratio of less than 75%. This well-managed spread of risk ensures that the quality of the Society's mortgage lending remains high.

The Group's buy-to-let mortgage portfolio increased during the year due to the merger with Scarborough Building Society which had £267m of such balances at the date of the merger. Total new advances on buy-to-let products were severely curtailed at £15m (2008: £202m). The risks attached to buy-to-let lending are managed by prudent consideration of the level of equity in the property, where we generally accept lower LTV ratios compared with our residential lending, and the level of rental cover compared with the mortgage payments.

Overall, including the impact of the merger, the Group has increased its loans and advances by 14% to £10,713m from £9,425m at the end of 2008, as set out in the table below:

	2009 £m	2008 £m
Total residential mortgages	**10,112.0**	8,815.7
Commercial loans	**523.9**	527.8
Other lending:		
Debt factoring loans	**32.7**	30.8
Other loans	**44.5**	50.2
Gross balances	**10,713.1**	9,424.5
Impairment provisions	**(85.1)**	(44.1)
Hedge fair value adjustments	**185.3**	187.3
	10,813.3	9,567.7

The Group has taken action to actively manage loans which have gone into arrears, supporting the borrower where possible whilst protecting the business for the benefit of all members.

The performance of the Society's residential mortgages remains good with only a modest increase in arrears during the year. At 31 December 2009 there were 411 cases (0.52%) where the arrears balance was greater than 2.5% of the total outstanding balance, compared with 320 cases (0.41%) a year ago. During the year the Society took 126 cases (2008: 74) into possession, of which 43 cases (2008: 37) remained in possession as at 31 December 2009.

The specialist nature of Amber Homeloans mortgages, means this subsidiary business has been more significantly impacted than the Society by the economic downturn. Consequently, we have seen a rise in arrears in the Amber portfolio and, as at 31 December 2009, there were 868 cases (8.48%) where the arrears balance was greater than 2.5% of the total outstanding balance, compared with 733 cases (6.45%) at 31 December 2008. Total new possessions within Amber were 313 cases (2008: 238), and 137 cases (2008: 184) remained in possession at the end of the year. Action taken in March 2008 to cease new lending has resulted in a gradual reduction in the level of arrears balances greater than 2.5% of the total outstanding balance in recent months from its peak of 8.95% in June 2009. Amber's management is now also focusing on the North Yorkshire Mortgages portfolio which came into the Group as a consequence of the Scarborough merger, where development of arrears has typically lagged behind Amber.

North Yorkshire Mortgages is also a specialist lender, albeit on a smaller scale than Amber. North Yorkshire Mortgages had 243 cases (4.00%) where the arrears balance was greater than 2.5% of the total outstanding balance at the end of December 2009, down from its peak of 5.67% in June 2009. Total new possessions, including those acquired when joining the Group, within North Yorkshire Mortgages were 111 cases and 63 cases remained in possession at the year-end. North Yorkshire Mortgages also ceased new lending in 2008. In addition, the Group stopped offering commercial loans in November 2008.

Skipton International continued to grow its Channel Islands mortgage book during the year, and mortgage balances stood at £401m at the year-end (2008: £357m); the quality of this book remains excellent with negligible arrears.

As demonstrated by the falling arrears rates in Amber, the Group has managed down the level of arrears through proactive collections processes. However, these processes have been applied responsibly, and, as part of our strategy to support customers in arrears we have capitalised arrears in a number of cases.

The Group applies a policy of capitalising residential arrears, with the customer's consent, once the customer has made at least six consecutive contractual monthly mortgage repayments following the instance of non-payment. The effect is to bring the loan account up to date and it is therefore no longer past due or individually impaired. If a customer's arrears have previously been capitalised, the customer is required to have made at least 12 consecutive contractual monthly repayments in order to qualify for further capitalisation.

The Society applies a similar policy for its commercial loan book as for its residential book, whereby customer arrears can be capitalised following six consecutive contractual monthly repayments following the instance of non-payment, or 12 such repayments if the account has previously had arrears capitalised.

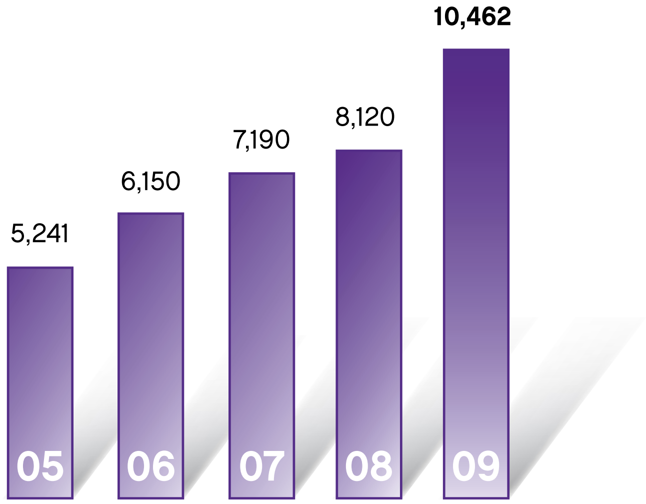
The following table shows the balance of those loans that have been renegotiated and would have been past due or impaired if their terms had not been renegotiated:

	Residential		Commercial	
	2009 £m	2008 £m	**2009 £m**	2008 £m
Society	**34.7**	14.1	**11.1**	3.5
Amber Homeloans	**43.8**	8.2	**-**	-
North Yorkshire Mortgages	**10.2**	-	**-**	-
Skipton International	**5.6**	4.8	**-**	-
	94.3	27.1	**11.1**	3.5

Funding

Retail

As a mutual, the Group is required to obtain the majority of its funding through retail member deposits and 79% (2008: 69%) of our funding comes from retail savings. Excluding £1,775m of retail deposits that were transferred to the Society at the date of the merger with Scarborough, the Society attracted £567m of net new retail savings in the year (2008: £930m). These inflows reflect the efforts made by the Society to rebalance its funding mix as a consequence of the ongoing impacts of the market dislocation that saw a reduction in access to wholesale funding, largely as a result of the sectoral re-rating by credit rating agencies in the first half of 2009. To assist in further reducing the Group's reliance on wholesale funding, during July 2009 we acquired £723m of retail savings from Capital One which brought over 45,000 new members to the Society.



Retail balances (£m)

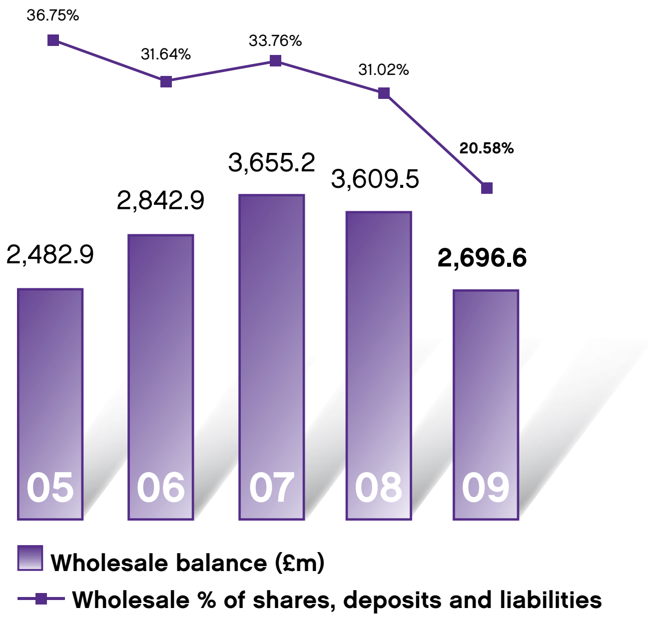
In addition to our UK retail funding, the Group also accepts deposits through our Guernsey-based operations which we merged with Scarborough's business, Scarborough Channel Islands, in September 2009. We saw balances increase to £855m largely as a result of the merger (2008: £468m). Excluding the impact of the merger, we are pleased to report that our Guernsey operations experienced net inflows, in a competitive environment, totalling £11.8m in 2009, as confidence returned to the Guernsey marketplace following the collapse of Landsbanki Guernsey in October 2008.

Wholesale

The remainder of the Group's funding comes from the wholesale markets. At 31 December 2009 our wholesale funding balances amounted to £2,697m (2008: £3,610m), a decrease of £913m. The increase in retail savings balances allowed us to reduce our reliance on the wholesale funding markets and our wholesale funding ratio fell from 31.02% at 31 December 2008 to 20.58% at the end of 2009.

Wholesale credit markets have remained tight since the economic downturn began in August 2007 and the long-term public issuance markets remain severely constrained. However, in the second half of 2009 a number of funders, including local authorities, resumed lending to the building society sector. In addition, and encouragingly, major names are now starting to issue commercial paper in unguaranteed format. Our key focus is on the retention of wholesale funding while seeking to lengthen maturities in order to protect against the prospect of the current market conditions continuing. These measures have allowed us to increase the proportion of our wholesale funding with a maturity of over one year to 58% at 31 December 2009, up from 24% at the end of 2008. This increase also includes successfully raising £650m of funding under the Government Guarantee Scheme in December 2009.

Wholesale funding



The following table analyses the change in the composition of our wholesale funding since December 2008. The analysis shows an overall reduction and lengthening of duration.

	2009 £m	2008 £m
Repo and other secured agreements	**285.2**	487.1
Deposits	**1,005.8**	1,748.0
Certificates of deposits	**135.7**	341.1
Medium-term notes	**1,168.5**	894.9
Hedge fair value adjustments	**101.4**	138.4
	2,696.6	3,609.5

During the first half of the year, the rating agencies were extremely active in reviewing the relative credit worthiness of all financial institutions. The ratings assigned to us are a key determinant of the funding markets the Group is able to access and the cost of funding. As at the end of 2009 our credit ratings, provided by Fitch and Moody's, were as follows:

	Fitch	Moody's
Long-term	A-	Baa1
Short-term	F2	P-2
Subordinated	BBB+	A3

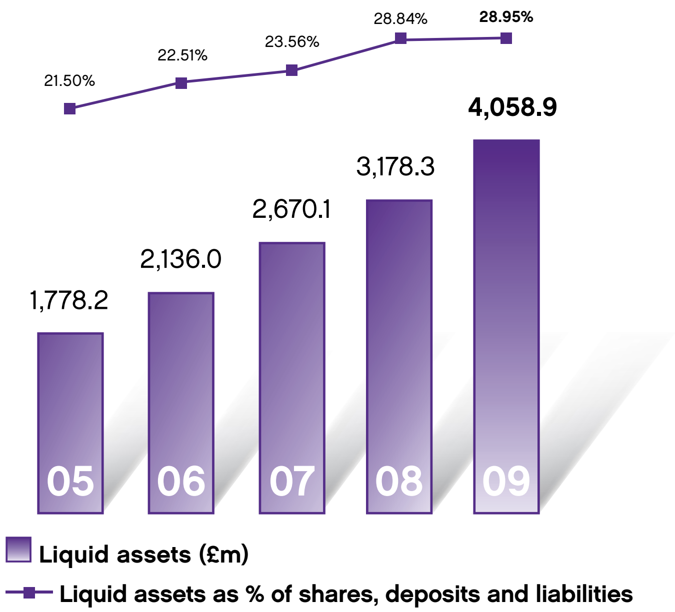
The downgrade of our rating, together with many other building societies, by Moody's in April 2009 was a reflection of market conditions in early 2009. In line with the majority of building societies, Fitch also downgraded our long-term credit rating from A to A-. We are pleased to have retained an AAA rating from both agencies on our covered bond programme.

Liquidity

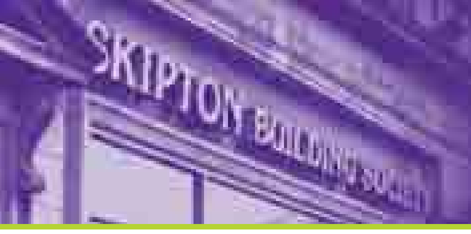
We have maintained high levels of liquidity throughout the year. The proportion of liquidity which is accessible within a short period of time has also been increased. The core 8-day liquidity ratio is managed to a level well in excess of the building society regulatory limit of 3.5% of funding liabilities. An analysis of the liquidity position of the Group is outlined below:

	2009	2008
Liquidity balance (£m)	**4,058.9**	3,178.3
As % of shares, deposits and liabilities (%)	**28.95**	28.84
Core 8-day ratio (%)	**17.01**	17.60
Core 8-day ratio as a proportion of total liquidity (%)	**55.18**	65.30

Liquid assets



With the continuing adverse market conditions, the focus remains on holding short-dated, high-quality investments. In reflection of this, the Group has increased the level of balances held on deposit with the Bank of England.



The Group continues to have no exposure to Structured Investment Vehicles ('SIVs'), conduits or to the US sub-prime market.

The Group's treasury investments are held to provide prudential liquidity and 98% (2008: 97%) of the Group's treasury investments are rated A or better. The Group policy is that initial investments in treasury assets must be investment grade or above. However, during the period the adverse market conditions have resulted in a small proportion of investments falling below this rating. These investments are monitored on a regular basis for impairment.

Rating	2009 £m	2008 £m
Aaa	**2,277.1**	843.8
Aa1	**205.9**	766.3
Aa2	**276.4**	461.0
Aa3	**881.0**	453.3
A1	**188.1**	180.0
A2	**93.0**	270.0
A3	**54.3**	102.7
Baa1	**37.5**	19.0
Baa2	**6.7**	25.5
Baa3	**3.5**	-
Ba3	**3.5**	-
Caa2	**3.9**	-
Unrated:		
Building societies	**17.6**	53.0
Local authorities	**10.4**	3.7
	4,058.9	3,178.3

The Group employs a rigorous credit assessment process and considers the risks of all assets before they are acquired and throughout the period they are held. Credit approval, along with monitoring the Group's exposure concentrations against a variety of criteria including industry sector and country of risk, is carried out by an independent Treasury Risk function.

The table below sets out the Group's treasury investments by industry sector / asset class:

	2009 £m	2008 £m
Cash in hand and balances with the Bank of England	**1,272.1**	359.4
Cash with banks and building societies	**437.4**	1,064.4
Gilts	**152.7**	111.0
Certificates of deposit	**903.6**	946.5
Local authority investments	**10.4**	3.7
Fixed rate bonds	**283.8**	1.7
Floating rate notes	**684.8**	390.0
Residential mortgage backed securities	**255.9**	243.0
Commercial mortgage backed securities	**58.2**	58.6
	4,058.9	3,178.3

Treasury assets are valued using quoted market prices or prices obtained from counterparties. Where reliable market prices are not available, discounted cash flow models are used.

Capital structure

The Group is regulated by the FSA who require us to manage our capital in accordance with the rules and guidance issued by the FSA. The capital requirements of the Group are monitored on a monthly basis and the results of this monitoring are reported to the Group Senior Management Committee and the Board. Capital is ultimately held for the protection of retail depositors and the internal level of capital is set with the aim of ensuring the minimum regulatory objective is exceeded. Throughout 2009, the Group has operated comfortably in excess of the minimum capital levels set by both the Society's regulator and the Board.

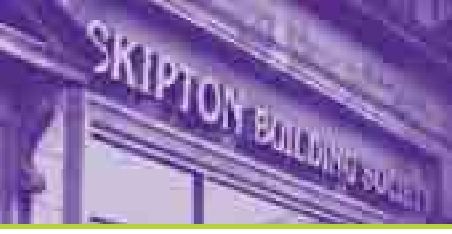
When the merger with Scarborough Building Society took place, the capital position of the Group was reduced by a number of fair value adjustments which were applied to the cessation accounts of the Scarborough Group (see note 38). The majority of these adjustments will be credited back over time, hence further improving the capital position of the Group.

The following table shows the composition of the Group's capital at 31 December 2009:

	2009 £m	2008 £m
Tier 1		
Reserves	**752.2**	703.6
Permanent Interest Bearing Shares (note 1)	**90.0**	25.0
Pension fund deficit add back (note 2)	**8.7**	16.7
Deductions from Tier 1 capital (note 3)	**(182.2)**	(242.5)
Unrealised losses on available-for-sale debt securities	**6.2**	13.2
Unrealised losses on cash flow hedges	**16.0**	21.2
Total Tier 1 capital	**690.9**	537.2
Tier 2		
Subordinated debt (note 1)	**207.8**	180.0
Collective impairment allowance	**29.6**	14.0
Total Tier 2 capital	**237.4**	194.0
Total capital	**928.3**	731.2
Risk weighted assets (unaudited)		
Retail mortgages	**4,250.8**	3,569.0
Commercial loans	**449.4**	464.7
Treasury assets	**505.2**	601.2
Other assets	**476.8**	462.3
Operational risk	**722.5**	846.1
Market risk	**8.1**	9.0
	6,412.8	5,952.3
Core Tier 1 (%) (note 4)	**9.37**	8.61
Tier 1 ratio (%) (note 4)	**10.77**	9.03
Total capital (%) (note 4)	**14.48**	12.28
Tier 2 to Tier 1 ratio (%)	**34.36**	36.11

Notes

1. Under FSA rules Permanent Interest Bearing Shares ('PIBS') and subordinated debt are included in the solvency calculation in accordance with UK GAAP rather than IFRS. The PIBS and subordinated debt are disclosed at par value therefore the associated merger fair value adjustments are recognised in the general reserve.
2. The regulatory capital rules allow the pension fund deficit to be added back to regulatory capital and a deduction taken instead for an estimate of the additional contributions to be made in the next five years, less associated deferred tax.
3. Under FSA rules intangible assets must be deducted from regulatory capital.
4. Calculated as relevant capital divided by risk weighted assets. Core Tier 1 relates to Tier 1 capital excluding PIBS.



For statutory purposes, under Basel II, we are required to calculate our capital ratios for both the Solo consolidation group and the UK consolidation group. The Solo consolidation group comprises the Group's UK-based mortgage lending businesses whilst the UK consolidation group consists of the entire Group except a small number of entities whose activities are not deemed to be closely aligned with the core business.

The table below sets out the capital resources of the Solo and the UK consolidation groups, together with the associated capital resource requirements as at 31 December 2009. Both ratios are comfortably above the regulatory threshold.

	UK consolidation group		Solo consolidation group	
	2009	2008	**2009**	2008
Capital resources (£m)	**912.5**	707.1	**822.0**	660.0
Pillar 1 capital resource requirement (£m)	**475.3**	436.3	**441.5**	400.0
Capital ratio (%)	**192.0**	162.1	**186.2**	165.0

Pension funds

The Group operates five defined benefit schemes as described in note 35, in addition to defined contribution stakeholder schemes open to current employees.

The aggregate valuation of the five funds at 31 December 2009 resulted in a deficit of £47.4m (2008: £37.9m) using the methodology set out in IAS19. We have taken steps to actively manage the deficit, including the following:

- The Skipton Building Society Pension & Life Assurance Scheme is closed to new members and existing members have accrued benefits on a Career Averaged Revalued Earnings basis since 2003. During the year, it was agreed that future pension accrual would cease in this scheme with effect from 1 January 2010 for all members who would then be eligible to participate in stakeholder schemes.
- The Connells Limited Pension & Life Assurance Scheme, the Sequence (UK) Limited (1997) Pension & Life Assurance Scheme and the Sequence (UK) Limited (South) Staff Pension Scheme were closed to new members in 2008. Future pension accruals ceased in these schemes with effect from 1 January 2009 for all members.
- Employee contributions were increased prior to the schemes' closures.
- Special contributions totalling £27.2m have been paid between 2006 and 2009 and plans have been agreed with the Trustees to actively manage the deficit and associated long-tail risk.

We will continue to monitor the deficit on the schemes to manage the funds in a responsible manner, with the aim of eliminating the actuarial funding deficit in the medium-term.

Bank Payroll Tax ('Bonus Tax')

Seven employees are expected to receive, during 2010, bonuses in respect of their 2009 performance that will be covered by the Bank Payroll Tax ('Bonus Tax'), announced in the Chancellor's 2009 Pre-Budget Report. The aggregate amount of such payments has provisionally been calculated as £315,000, of which £140,000 is in excess of the respective £25,000 thresholds. The associated tax, at 50%, on the excess amounting to £70,000, has been provided for in these Financial Statements.

Performance by business area

The Group operated in six main divisions until December 2009 when it disposed of its Credit & Marketing Solutions division, which comprised Callcredit Information Group. The five remaining divisions are as follows:

- Mortgages and Savings – principally the Society, but also includes specialist mortgage businesses Amber Homeloans and North Yorkshire Mortgages together with our Channel Island subsidiary Skipton International.
- Mortgage Services – mortgage administration services, principally HML, also includes Specialist Mortgage Services and Baseline Capital.
- Estate Agency – including survey and valuations, conveyancing, lettings, asset management and mortgage and insurance broking carried out through the Connells Group.
- Financial Advice – provision of financial advice and broking services through five separate financial advice companies.
- Investment Portfolio – comprising the ancillary businesses: Pink Homeloans, Skipton Business Finance, The Private Health Partnership, Sterling International Brokers, Mutual One and Jade Software Corporation.

Whilst, inevitably, the results of some of the Group's divisions have been impacted by the continuing adverse economic conditions, we are pleased that the strength of our diversified business model has, once again, resulted in the Group reporting a profit for the year.

Business area	2009 £m	2008 £m
Profit before non-routine items (see note 34):		
Mortgages and Savings	**(44.0)**	3.6
Mortgage Services	**4.7**	8.3
Estate Agency	**54.1**	10.4
Financial Advice	**1.9**	(1.0)
Credit & Marketing Solutions	**5.8**	4.7
Investment Portfolio	**(2.9)**	(1.4)
Inter-division adjustments	**1.1**	(2.1)
Sub-total	**20.7**	22.5
Non-routine items	**42.8**	-
Group profit before tax	**63.5**	22.5

Mortgages and Savings

The Group's Mortgages and Savings division comprises the Society, Amber Homeloans, North Yorkshire Mortgages, Skipton International, Skipton Covered Bonds LLP, Bailey Computer Services and Skipton Trustees.

The Mortgages and Savings division made an operating loss of £44.0m (2008: profit £3.6m). This was a result of an impairment charge of £43m (2008: £34m), with the majority of the charge arising from the specialist residential mortgage loans held by Amber, and the falling interest margin. Interest margin fell following the dramatic fall in Bank Base Rate, which reduced the earnings achievable on assets, many of which are linked to the Bank Base Rate, whilst, due to the ongoing dislocation in the savings market, the cost of funding could not be reduced at the same rate.

The Society's management expenses ratio reduced to 0.40% compared with 0.47% at the end of 2008. The Society's focus was on maintaining a prudent cost base post the merger with Scarborough Building Society.

As expected, Amber's results were impacted by impairment losses and the company saw an impairment charge for the year of £33m, up from £30m in 2008. Encouragingly, from a high of 8.95% (where the arrears balance was greater than 2.5% of the total outstanding balance) in June 2009, arrears have slowly declined throughout the remainder of 2009 and, at the year-end, stood at 8.48%. Having ceased new lending in early 2008, Amber's mortgage balances have fallen further and were £1,331m at 31 December 2009 (2008: £1,442m).

North Yorkshire Mortgages, which the Group acquired as part of the Scarborough merger on 30 March 2009, wrote similar business to Amber Homeloans, but also ceased lending in 2008. From a high of 5.67% (where the arrears balance was greater than 2.5% of the total outstanding balance) in June 2009, arrears in North Yorkshire Mortgages have also fallen during the year and amount to 4.00% at the year-end. Expected impairment losses arising on this portfolio were accounted for at the merger date and there is no impact on the Group's profits for 2009. The outstanding mortgage balances in North Yorkshire Mortgages were £828.9m at 31 December 2009.

Our Channel Island mortgage and savings business, Skipton International, was created on 30 September 2009, when Skipton Guernsey and Scarborough Channel Islands were amalgamated. Skipton International made a profit of £0.4m in 2009 (2008: £1.9m). This business suffered from the same margin pressures as the Society, with interest receivable on assets declining faster than the cost of funding, particularly as Skipton International is almost entirely funded by retail customers. Following the nervousness in the Guernsey deposit taking market in late 2008, following the collapse of Landsbanki Guernsey, we are pleased to report that retail funding has been retained and ended the year at £855m (2008: £468m). Skipton International continued to grow its mortgage book during the year, and outstanding mortgage balances were £401m at the year-end (2008: £357m); the quality of this book remains excellent with negligible arrears.

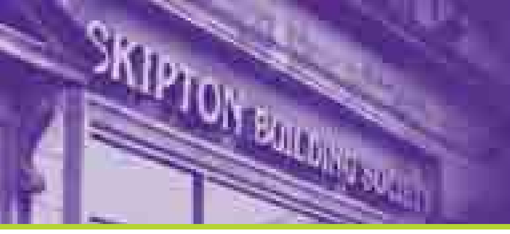
Mortgage Services

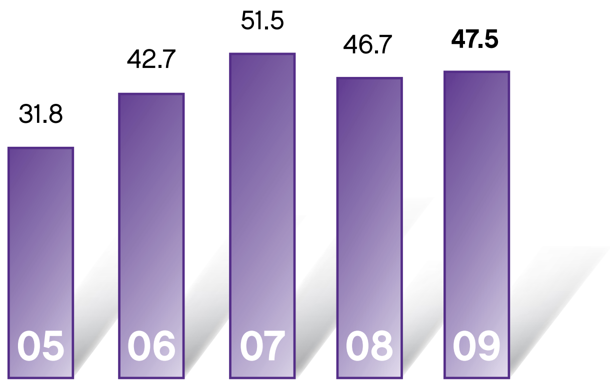
Mortgage Services provides outsourcing to a number of specialist and high street financial services companies. The business is the largest third party mortgage administrator in the UK with total assets under management of £47.6bn and generated underlying profits of £4.7m compared with £8.3m in 2008.

However, whilst operating performance remained strong and notwithstanding the pressure on costs, HML continued its business investment in both its IT capability and its physical infrastructure with a new purpose built Head Office in Skipton expected to be ready for occupation during the first half of 2010. This investment has had an impact on its 2009 profit.

Trading conditions in 2009 were extremely challenging, despite some improvement towards the end of the year, retail credit markets remained tight and levels of new mortgage origination in the UK and Ireland were constrained. It is undoubtedly the case that the turmoil of the past two-and-a-half years in financial markets has led to major changes in the operating models of many mortgage lenders.

There is clear evidence that this will present commercial opportunities to HML in the coming years. Indeed, during 2009 two new mortgage administration contracts and one new standby contract were signed. The programme of systems investment will ensure HML are in the best possible shape to exploit the opportunities that will arise.

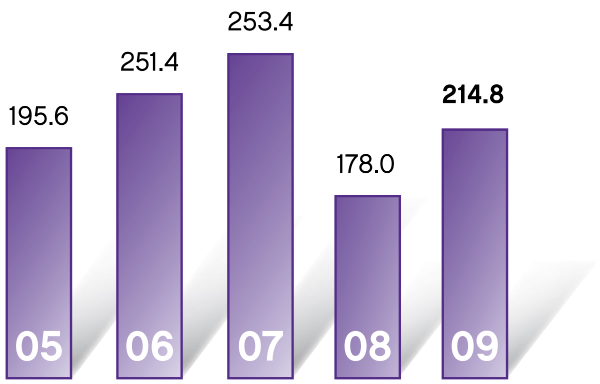




Assets under management (£bn)

Estate Agency

In 2008 the housing market tailed away markedly from April onwards. The picture for 2009 was very different, with a significant increase in second hand sales volumes, up by over 58% compared with the latter months of 2008 and 38% year-on-year. As a result of these volume increases our Estate Agency division turnover was £214.8m during 2009 compared with £178.0m in 2008.



Estate Agency total fee income (£m)

The Estate Agency division is now benefiting from the significant cost reduction programme that was instigated in 2007 and became an ongoing feature of management activities throughout 2008 and 2009. During this period over £40m of annual cost savings were made. These actions, together with the improvement in volumes, have driven an operating profit of £54.1m for the Group in 2009, which compares very favourably with the £10.4m generated last year.

Financial Advice

The Financial Advice division comprises five different businesses, each with their own brand, customer proposition and investment philosophy, differentiated either geographically or by sector. A range of competencies exist in the division, as diverse as execution-only investments, Financial Planning, and Employee Benefits.

Trading conditions remained very difficult to the half-year, with most asset classes delivering subdued performances, leading to continued low investor confidence. However, some confidence returned in the latter part of the year, augmented by refreshed and relaunched customer service propositions in both the mass affluent and wealth management sectors.

The division is well placed to meet the rigours of the Retail Distribution Review, has addressed its cost structure and has a clear strategy for the future.

An operating profit before tax of £1.9m was recorded for the year, compared with a £1.0m loss for 2008. An emphasis has been placed on managing costs throughout 2009 and this will continue in 2010.

Investment Portfolio

The Investment Portfolio had a mixed year. Skipton Business Finance, our debt factoring and invoice discounting business, had a very good year and produced record profits of £2.0m whilst maintaining a prudent approach to provisioning. The performance was helped by a tightening of credit and overdraft facilities by the banks and an expansion in the company's sales team who delivered in excess of budget in the year.

The Private Health Partnership Group, which includes medical insurance broking and the provision of nurse-led counselling support, delivered strong new business performance but the downturn in the economy did put pressure on retention levels.

In contrast, the reduced mortgage market volumes continued to affect Pink Homeloans, our mortgage network business, where a significant cost reduction programme was completed in 2009.

Sterling International Brokers, which specialises in money broking, also had a tough year as the volumes in the cash markets remained low due to the credit crunch.

Skipton also own a majority stake in Jade, which has its own proprietary computer language and also specialises in object orientated databases. Jade has won some notable contracts in 2009 and had a strong first half of the year but trading conditions in the second half of the year were more challenging.

Discontinued operation

The Credit & Marketing Solutions division primarily consisted of Callcredit Information Group ('CIG'). CIG supplies a wide range of credit referencing, marketing information and network planning services.

Following a Group-wide strategic review, management concluded that the future prospects of CIG were better suited outside of the Group and hence CIG was sold in December 2009 for £97.8m, generating £39.7m profit.

For the 11 months of the year prior to disposal, CIG made pre-tax profits of £5.8m, compared with operating profits of £4.7m for the full 12 months last year.

Principal risks and uncertainties

Risk management framework

The Group, through its risk management framework, has a formal structure for managing risks throughout the business. This framework is designed to deliver the Board's overall risk objectives and is based upon the best practice 'three lines of defence' model comprising:

- First line of defence, being line management within the business which, through the implementation of the organisation's risk framework, identifies, assesses, and manages risk.
- Second line of defence comprising independent risk functions (Operational, Credit and Market) and related risk functions including Compliance, Systems Security, Finance and Insurance. These functions challenge, monitor, guide and support the business in managing its risk exposure. The Risk framework includes a number of risk committees (Asset and Liability Committee ('ALCO'), Group Retail Credit Committee and Group Operational Risk Committee) responsible for setting policy and framework and monitoring implementation by the business. The independent Group risk functions are represented on each of the risk committees.
- Third line of defence, provided by Group Audit Services, is designed to provide independent assurance to the Board (via the Audit Committee) of the adequacy and effectiveness of control systems within the first and second lines in managing and controlling risk.

The key risks and uncertainties faced by the Group, which are managed within the framework described above, are set out below.

Business conditions and the economic environment

The Skipton Group is almost solely focused in the UK market and the main divisions are in large part exposed to the UK property market. Therefore the general UK macro-economic environment is a key determinant of the success of the Group. The main drivers that impact the Group include:

- Interest rates (Base and LIBOR);
- Inflation;
- Unemployment; and
- The housing market (volume of transactions and house price inflation).

The Mortgage and Savings division faces challenges from the low interest rate environment, with an overall reduction in its net interest margin. The margin compression is exacerbated by the dislocation in the retail savings market following the credit crunch and the need for all banks to reduce their reliance on wholesale funding. A reduction in our overall level of lending (new business and remortgages) would also adversely impact non-interest income in the division. The weak economy also impacts the division through the increase in the impairment charge driven by rising arrears prompted by increasing unemployment and the reduction in refinancing opportunities, which is compounded by weaker asset prices.

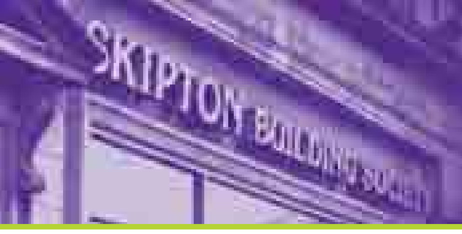
The main risk to the core business is the continuation of the exceptionally low base and LIBOR rates which has resulted in continued margin pressure in the core business. The Society's mortgage SVR was capped at 3% above bank base; however, given the continuation of these exceptional economic conditions, the Society has announced its intention to increase the SVR from 3.5% to 4.95% from 1 March 2010 to mitigate this risk.

The Mortgage Services division is impacted by the changing dynamic in the lending landscape as the impact of the credit crunch changes the dynamic of competition in the UK mortgage market, with a reduction in the overall level of mortgage lending. Whilst, inevitably, the business has seen a fall in the value of assets it manages, conversely there has been an increase in the incidence of accounts in arrears which has acted, to some extent, as a counter balance. The changing landscape will present both opportunities and challenges as existing lenders exit and new players come to the market.

The results of the Estate Agency division are principally driven by the volume of property transactions, particularly second hand property sales. This market is heavily influenced by consumer confidence, much of which is borne out of the overall level of unemployment and interest rates. The Estate Agency division has a partial counter-cyclical hedge against the performance of its core business through its Asset Management businesses that assist lenders in their management of non-performing loans.

The Financial Advice division is also exposed to the wider UK economy. The main influence on its performance is consumer confidence and the willingness of customers to invest in longer-term products.

The ability of the Group to maintain profitability and boost capital in the toughest external environment faced for at least a generation provides confidence that the Group is capable of withstanding the current challenging environment and the issues that would be faced should the current recovery lose momentum.



Credit risk

This is the risk that a customer or counterparty is unable to honour their obligations as they fall due. The Group faces this risk in respect of:

- Individual customers (retail mortgages);
- Businesses (through historic commercial lending). The Society ceased new commercial lending in November 2008 when we concluded that the outlook for commercial property was poor; and
- Other financial institutions (wholesale lending).

Credit risk within our retail and existing commercial mortgage portfolios is driven by general UK economic pressures, including rising unemployment, deterioration in household finances and further contraction in the UK property market leading to falling property values. A reversal of the economic recovery and the return of falls in house prices and commercial property values would affect the level of impairment losses.

In our residential mortgage business we closely monitor applicant quality, affordability and LTV multiples. The credit decision is always managed separately from the sales force originating the business. Retail mortgage credit risks are managed within credit policies and limits set by the Group Retail Credit Committee and loans which show signs of adverse performance are managed by specialist teams who manage the collections and recovery process.

Credit risk within our treasury portfolio assets arises from the investments held by the Group in order to meet liquidity requirements and for general business purposes. The wholesale credit markets remain volatile and dislocated and a further deterioration could lead to additional fair value adjustments in the Group's portfolio of available-for-sale assets coupled with further impairment of our treasury investments portfolio. This element of credit risk is managed by the Treasury team within strict limits set by ALCO with a regular review of credit policies and performance through the Group Wholesale Credit Committee.

Market risk

Market risk is the risk that the value of, or income from, the Group's assets and liabilities is impacted as a result of changes in market prices. The Group's market risk comprises three types of risk: interest rate risk, currency risk and equity risk.

Interest rate risk

This is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Interest rate risk arises from the mortgage, savings and other financial products that we offer. This risk is managed through the use of appropriate financial instruments, including derivatives, with established risk limits, reporting lines, mandates and other control procedures.

Other interest rate risk exposures, such as basis risk (the risk of loss arising from changes in the relationship between interest rates which have similar but not identical characteristics, for example, LIBOR and Bank of England Base Rate) are also monitored closely and regularly reported to ALCO.

Currency risk

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

As at 31 December 2009 and during the year, the Group had limited exposure to foreign currency fluctuations, with the main exposure relating to the Group's equity investments in Jade Software Corporation Limited and Northwest Investments NZ Limited which are denominated in New Zealand dollars. The foreign currency fluctuations in relation to the Group's equity investments are not material, and are recognised in the Group's translation reserve. Alongside this, HML has a number of contracts with customers in the Euro zone but this is not significant with options in place to manage exchange rate volatility.

Equity risk

As at 31 December 2009, the Group had a small amount of issued equity-linked savings products. Derivative contracts to eliminate this exposure are in place which exactly match the terms of the savings products and the market risk on such contracts is, therefore, fully hedged.

Liquidity risk

This is the risk that the Group is unable to meet its current and future financial obligations as they fall due. These obligations include investors' deposits as well as repayments of other borrowings and loan capital.

The Board sets limits over the level, composition and maturity of liquidity and deposit funding balances, reviewing these at least annually. Compliance with these limits is monitored daily by Finance personnel (ie independent of Treasury). In addition a series of liquidity stress tests are performed weekly by Group Market Risk, and formally reported to ALCO monthly, to ensure the Group maintains adequate liquidity for business purposes even under stressed conditions.

The wholesale markets remain extremely tight and opportunities for Skipton to raise longer-term unsecured funding in public debt markets remain limited. While we have access to Government schemes and to other sources of secured funding through repo agreements and covered bonds, these remain limited and expensive.

Around 80% of our funding comes from retail sources and we have been successful in increasing our balances over the past four years. As savers continue to demand a safe haven for their deposits we will continue to offer good value products to attract further balances.

We continue to maintain a close watching brief on the money markets, but until such times as we believe the markets are returning to more normal conditions we will continue to hold an historically high level of liquidity and fund growth in lending from retail balances.

The FSA has introduced new requirements (PS09/16 *Strengthening Liquidity Standards*) for liquidity management and reporting applicable from June 2010. The Society has made significant investment in its infrastructure to deliver this and will be compliant with the regulatory requirements within the prescribed timeframe.

Operational risk

Operational risk relates to the risk of loss arising from inadequate or failed processes, people, systems, or from external events. For the purposes of managing operational risk, we divide it into a number of discrete themes which include fraud, information security and business continuity planning. Responsibility for managing operational risks lies with individual business areas that identify and assess risks in line with the processes described in the framework earlier. An independent Group operational risk function reports to the Group Operational Risk Committee and the Board on the key operational risks facing the business.

As a business providing a service based on processing customer data we are very alert to the threats arising from computer hacking, theft or failed processes allowing unauthorised data disclosure. As would be expected of a leading financial services provider, appropriate organisational and technological controls are implemented. To ensure a robust framework is in place the Group Operational Risk Committee has established Information Security standards which all Group businesses must adhere to. Compliance with these standards is monitored by Group Risk and Group Audit Services.

Given the nature of the regulated sectors in which we operate, one of our key operational risks is the potential failure to maintain ongoing compliance with relevant external regulation across the Group. Each of the regulated businesses has an established Compliance team which both monitors compliance with existing legislation and considers the impact of new requirements. Oversight is provided by a central Group Compliance function which ensures best practice is adhered to and shared across the Group as appropriate.

Reputational risk

Reputational risk arises from a deterioration in the perception of the Society's or Group's standing in the eyes of either the wholesale markets or the general public. Management has considered how this might arise and what the impact could be. An event threatening the Society's or Group's reputation may result in an increase in retail deposit outflows and / or counterparties withdrawing funding lines to the Group. This is modelled and controlled under the Group's liquidity risk management framework described earlier.

Pension obligation risk

Pension obligation risk is the risk that the Group's obligations towards its pension schemes may lead to the Group not being able to pay its other liabilities as they fall due; and the risk that an increase in the funding requirements results in a significant reduction in the Group's capital resources. The Group's exposure to pension risk emanates from its five defined benefit pension schemes, all of which have been closed to new members for a number of years and are all now closed to future accrual of benefit.

The following controls are in place to limit the Group's exposure to pension obligation risk:

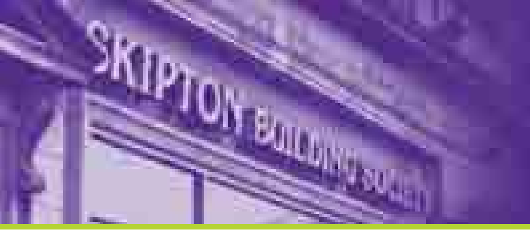
- Senior management and the scheme trustees receive professional advice, from separate actuarial advisers, regarding the management of the pension scheme obligations on a regular basis.
- The pension trustees meet every quarter to monitor and make, in consultation with the principal employer, investment decisions with regard to the plan assets within the five schemes.
- The pension obligation position is updated every quarter and reported to the Board and the pension scheme trustees.

The Group also performs stress testing on the pension scheme liabilities and assets as part of its capital planning methodologies. The 'Pension funds' section on page 25 sets out the steps management have undertaken to actively manage the current deficit.

Additional information on risk is also set out in the Group's Basel II Pillar 3 disclosures available on our website.

Outlook

The past two-and-a-half years have presented significant challenges to the financial markets and the wider economy. It would appear that the economy has technically emerged from recession, however, the structural deficit and the current position of the economic fundamentals would suggest that the challenging environment the UK faced during 2009 will continue for the foreseeable future. The timing and scale of action to reduce Government debt is unclear as is the impact of such action on the UK economy. In light of this uncertainty we will continue to remain vigilant and position the Group to ensure that we are well placed to react to opportunities as they emerge,



but also that the Group is well placed to deal with the effects of any further economic deterioration.

Following the crisis in the financial services sector the regulatory landscape has continued to evolve at pace and we expect the proposed changes to liquidity, funding and capital requirements, set out by the FSA, to have a significant impact on the financial services landscape. At this stage it is difficult to determine what the long-term impact of these changes will be on the Group – however, our continued focus on identifying and managing the risks the business faces will help to ensure that we are well placed to meet these challenges.

Despite the challenges that remain in the regulatory and external landscape we are confident that the Group will continue to perform in a difficult and challenging environment.

T F Wood

Group Finance Director

24 February 2010

The Directors have pleasure in presenting their Annual Report and Accounts for the year ended 31 December 2009.

As set out more fully in the statement of accounting policies, the Annual Report and Accounts are prepared in accordance with International Financial Reporting Standards ('IFRS'). All financial information given in this Directors' report is taken from the statutory accounts prepared on this basis. Further, unaudited information which allows comparison between 2009 and 2008 is set out in the Business review on pages 16 to 31.

Business objectives

The Society's long-term objectives remain to maximise the long-term value for an increasing number of retail savings and borrowing members, and to create safe and rewarding employment for its staff. The Directors believe that our status as a building society enables us to deliver attractive products to customers. Our focus on profitably growing our core business of retail savings and mortgages remains, but investment in related businesses, where appropriate opportunities are identified, will continue. The profits generated by our investment in subsidiary companies continue to deliver long-term benefit to our members.

The Skipton Group offers a comprehensive range of financial services products and services to individual consumers, from mortgages and investments, financial advice, outsourced mortgage servicing, estate agency services to life and other insurance sales.

Business review and future developments

The Chairman's statement, Chief Executive's report and Business review set out on pages 6 to 31 report on the performance of the business and its future objectives.

Key performance indicators ('KPI')

Understanding and managing the risks faced by the Group and maintaining sufficient levels of capital are pivotal to ensuring that the business remains protected. To grow and take the business forward we must exceed our customers' and potential customers' expectations.

This can be achieved by offering and delivering, through our staff, financial products and services they value. The KPIs used by management provide the framework to help ensure these strategic objectives are met. The Group's Financial KPIs are reported upon in the Business review on pages 17 to 24 and help to ensure we are focused upon:

- Ensuring the Group continues to trade profitably;
- Increasing capital ratios;
- Maintaining a strong and diversified funding base;
- Holding high levels of quality liquid instruments;
- The effective management of impaired assets; and
- Increasing efficiency across the business.

We also monitor a number of non-financial indicators, including customer and staff KPIs.

Profits and capital

Profit before tax based on continuing operations was £18.0m (2008: £17.9m). Total Group profit before tax was £63.5m (2008: £22.5m). The profit after tax transferred to the general reserve was £57.4m (2008: £22.8m).

Total Group reserves at 31 December 2009 were £762.9m (2008: £703.6m) after taking into account the available-for-sale reserve of £(6.2)m (2008: £(13.2)m) and the cash flow hedging reserve of £(16.0)m (2008: £(21.2)m).

Gross capital at 31 December 2009 was £1,063.0m (2008: £917.5m) including £213.0m (2008: £183.7m) of subordinated liabilities and £83.6m (2008: £26.3m) of subscribed capital. The ratio of gross capital as a percentage of shares and borrowings at 31 December 2009 was 7.58% (2008: 7.50%) and the free capital ratio was 5.79% (2008: 4.95%).

Mortgage arrears

Group mortgage balances at 31 December 2009 included 703 mortgage cases (2008: 287), either in possession or where payments were 12 months or more in arrears. The capital balances of these loans were £107.5m (2008: £48.3m). The total amount of the arrears was £8.6m (2008: £3.7m).

Charitable donations

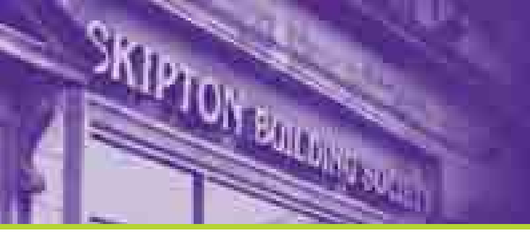
During the year the Group made charitable donations of £0.1m (2008: £0.3m). No contributions were made for political purposes.

Creditor payment policy

The Society's policy concerning the payment of suppliers is to negotiate and agree terms and conditions with all suppliers and upon complete provision of goods and services, unless there is an express provision for stage payments, undertake to pay suppliers within the agreed payment period. The number of trade creditor days as at 31 December 2009 was 3 days (2008: 5 days).

Risk management

As a result of its normal business activities, the Group is exposed to a variety of risks, the most significant of which are interest rate risk, operational risk, credit risk and liquidity risk. The Group has established a number of committees and policies to manage these risks. These principal risks and uncertainties are set out in the Business review on pages 28 to 31 and in note 33. In addition to these financial risks the Group is exposed to the effects of the economic cycle, particularly relating to the UK residential housing market, and the competitive nature of the UK personal financial services markets in which we operate.



The financial management objectives and policies of the Group are shown in the Business review on pages 28 to 31 and in note 33 on pages 89 to 105.

Employees

The Group remains committed to its policy of treating all employees and job applicants equally at all times. Our policy is that no employee, or potential employee, is treated less favourably on the grounds of race, colour, religion, nationality, ethnic origin, sex, marital status or sexual orientation. We also give all applications from disabled people full consideration in relation to the vacancy concerned and their own aptitudes and abilities. In the event of an existing employee becoming disabled, we make every effort to maintain their present position or to employ them in alternative suitable work.

We also aim to provide high-quality relevant training and development opportunities to all staff which enables them to achieve their full potential and helps the Group meet its corporate objectives. All employees have equal access to training and have the opportunity to acquire relevant professional qualifications for their respective roles.

The Group's Board meets on a monthly basis and the Society's management is briefed regularly on matters arising. There is a comprehensive internal communications structure to cascade relevant business information to staff throughout the organisation in an appropriate and timely way. The Society's subsidiary companies have similar arrangements in place to ensure that their employees are effectively managed.

The Society and certain Group companies recognise an independent staff association ('SURGE'), with which management meets regularly to consult and negotiate on a wide variety of matters and to which staff may make their views known on issues affecting their interests.

Property, plant and equipment

The Directors consider that the overall market value of the Group's freehold and leasehold properties, excluding the Society's Principal Office, is in excess of the book value. In arriving at this view the Directors have taken account of internal and external valuations of the Group's property portfolio, excluding the Society's Principal Office. The Society's Principal Office is a special purpose facility and the Board considers that its value in use to the Society is greater than its book value.

Directors' responsibilities in respect of the preparation of the Annual Accounts

This statement, which should be read in conjunction with the Independent auditor's report on pages 46 and 47, is made by the Directors to explain their responsibilities in relation to the preparation of the Annual Accounts, the Directors' emoluments disclosures within the Directors' remuneration report, the Directors' report and the Annual Business Statement.

The Directors are required by the Building Societies Act 1986 ('the Act') to prepare, for each financial year, Annual Accounts which give a true and fair view of the income and expenditure of the Society and the Group for the financial year and of the state of the affairs of the Society and the Group as at the end of the financial year, and which provide details of Directors' emoluments in accordance with Part VIII of the Act and regulations made under it.

The Act states that references to IFRS accounts giving a true and fair view are references to their achieving a fair presentation. In preparing those Annual Accounts, the Directors are required to:

- select appropriate accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the Annual Accounts; and
- prepare the Annual Accounts on the going concern basis, unless it is inappropriate to presume that the Group will continue in business.

The Directors are also required by the Disclosure and Transparency Rules of the Financial Services Authority to include a management report containing a fair review of the business and a description of the principal risks and uncertainties facing the Group.

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 Society and its connected undertakings.

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

Directors' responsibilities for accounting records and internal controls

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;
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Financial Services Authority under the Financial Services and Markets Act 2000.

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 UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

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 Annual Accounts, prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit 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.

Going concern

The Group's business activities, together with its financial position, capital resources and the factors likely to affect its future development and performance, are set out in the Business review on pages 16 to 31. In addition note 33 to the Annual Accounts includes the Group's objectives, policies and processes for managing its liquidity risk, details of financial instruments and hedging activities, and its exposure to credit risk and liquidity risk.

In common with many financial institutions, 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 forecasts and objectives, taking into account a number of potential changes in trading performance and funding retention, show that the Group should be able to operate at adequate levels of both liquidity and capital, for the foreseeable future.

Consequently, after reviewing the Group's forecasts and the risks it faces, the Directors are satisfied that there are no material uncertainties that may cast significant doubt about the Group's ability to continue as a going concern for the foreseeable future and have, therefore, continued to adopt the going concern basis in preparing the Annual Accounts.

Directors

The Directors of the Society during the year were as follows:

Mr J B Rawlings	(Chairman)
Mr A I Findlay	(Vice Chairman)
Mr D J Cutter*	(Chief Executive)
Mr P R Hales	
Ms P M Hay-Plumb	
Mr C N Hutton	
Mr W H Jack	(retired 1 May 2009)
Ms A B E Kinney	
Mr J Spence	(appointed 25 June 2009)
Mr P J S Thompson	(appointed 1 April 2009)
Mr R J Twigg*	
Mr T F Wood*	(appointed 7 September 2009)
Mr W R Worsley	(appointed 24 April 2009)

* Executive Directors

Details of Directors' service contracts are disclosed in the Directors' remuneration report.

No Director at 31 December 2009 had any interest in the shares of any group undertaking at any time during the year.

Auditors

In accordance with Section 77 of the Building Societies Act 1986, a resolution for the re-appointment of KPMG Audit Plc as auditors is to be proposed at the forthcoming 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 auditors are 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 auditors are aware of that information.

By Order of the Board

J B Rawlings

J B Rawlings
Chairman
24 February 2010

Keith Goodchild, customer of Malton Branch

The Board is committed to best practice in corporate governance and is currently assessing the recommendations arising from the Walker Review. This Report explains how the Board applies the principles of the Combined Code on Corporate Governance ('the Code') issued by the Financial Reporting Council (the most recent version being published in June 2008). The Board considers that the Society applies all the Code principles, except where stated below. The Board has also taken into consideration the BSA Guidance for Building Societies on the Code.

Governance Framework

The Skipton Group comprises Skipton Building Society together with its direct and indirect holdings in numerous legal entities, operating in different jurisdictions, many of which are regulated. A few subsidiaries have minority interests. In comparison to other UK building societies, it is an unusual and complex group structure. As such, the Society itself is both a large operating entity and the owner of many diverse business investments.

During 2009 the Board reviewed its governance arrangements to ensure that the requirements of its customers, employees and regulators are met and established a framework which organises the Group into five divisions (six prior to the sale of Callcredit Information Group on 7 December 2009):

- Mortgages and Savings
- Mortgage Services
- Estate Agency
- Financial Advice
- Investment Portfolio

The Board established Governance Principles, which are summarised below, to provide the framework through which Skipton Building Society establishes its systems and processes concerned with planning and delivering the overall direction, effectiveness, supervision and accountability of the Group.

Directors

The Board

The Society recognises that it must be headed by an effective Board, which is collectively responsible for the success of the Society.

The Board operates under terms of reference which clearly set out its responsibility for the overall stewardship of the Group. As part of its review of governance arrangements, the Board has adopted 'Principles of Governance', which may be summarised as follows:

1. **Governing Body** - The Society is headed by the Board, which is responsible for the success of the Society. The Board formulates strategy and establishes the Society's risk appetite and balance sheet strategy. It has a proper understanding of, and competence to deal with, the current and emerging issues of the business of the Society and its businesses; effectively reviewing and challenging the performance of management and exercising independent judgement. The Board also develops well-defined and understood values and standards.
2. **Management and Oversight** - The Society's management and oversight framework enables the Board to provide strategic guidance and effective oversight of management for both the Society and its divisions. The framework clarifies the respective roles and responsibilities of Board members and Senior Executives in order to facilitate Board and management accountability to both the Society and its members and ensures a balance of authority such that no single individual has unfettered powers. It has clear (risk based) lines of sight into activities to support challenge and direction which enables the Board to ensure that assurance is obtained over the integrity of reporting and the adequacy of the control framework and control activities.
3. **Recognise and Manage Risk** - The Board has a sound system of risk oversight and management and internal control. Its risk framework identifies, assesses, manages and monitors risk. It informs Senior Executives and the Board of material changes to the risk profile of the Society or any of its divisions and monitors and provides assurance over the effectiveness of the control framework and control activities and integrity of reporting.

The Society Board has established a framework of authorities in place which maps out the structure of high level delegation below Board level and specifies those issues which remain the responsibility of the Board. The Board also has a general duty to ensure that the Skipton Group operates within the Society's Rules, rules and guidance issued by relevant regulatory authorities and all relevant laws and that proper accounting records and effective systems of internal control are established, maintained, documented and audited.

In addition to the formal schedule of matters which are reserved to it, the Board has also delegated authority in other matters to a number of Board committees, as described below. The Board has set clear terms of reference for each of these committees, and has established an organisational structure with clearly defined and documented delegated authority to Executive management, together with reporting systems for financial results, risk exposure and control assessment.

The Board meets monthly (except August), and also holds an annual strategy review meeting. The Non-Executive Directors also meet, without Executive Directors present, at least once a year.

All Directors have access to independent professional advice, if required, and have the benefit of appropriate liability insurance cover at the Society's expense.

Chairman and Chief Executive

The offices of the Chairman and Chief Executive are distinct and are held by different individuals. The role of each is set out in their terms of appointment or contract respectively. The Chairman is responsible for leading the Board and communicating with the Society's members on behalf of the Board. The Chairman is independent and has no conflicting relationships or circumstances that could affect his judgement.

The Chief Executive is responsible for managing the Group's business within the parameters set by the Board.

The Board elects its Chairman and Vice Chairman annually at the Board meeting immediately following the Annual General Meeting ('AGM').

Board balance and independence

The Society's Rules detail the appointment process for Directors and require that the Board comprises not less than six nor more than 15 Directors.

The Board has determined that its current composition of nine Non-Executive Directors (including the Chairman) and three Executive Directors is appropriate. The Board considers all the Non-Executive Directors to be independent in accordance with the criteria set out in the Code. One of the criteria is whether a Director has served for more than nine years from the date of their first appointment. Mr Rawlings, Chairman, was appointed in 1995 and has therefore served for more than nine years. Mr Rawlings was re-elected as Chairman at the 2009 AGM and the Board is satisfied that he remains independent.

The Code proposes that a Senior Independent Director be appointed, primarily to act as a separate point of contact for institutional shareholders. However, the Board has concluded that such an appointment is not appropriate for a building society given its mutual status and that all the Non-Executive Directors are independent and accessible to members.

Appointments to the Board

The Board has a Nominations Committee to lead the process for Board appointments and succession planning. The Committee, at least annually, reviews the structure, size and composition of the Board to ensure it contains the required balance of skills, knowledge and experience relevant to the activities of the Group.

Candidates for Non-Executive positions are identified in a number of ways, including the use of external search consultants. In addition, members of the Society have the right, under the Society's Rules, to nominate candidates for election to the Board. All Directors must meet the FSA's fitness and propriety standards and be registered with the FSA as an Approved Person in order to fulfil their Controlled Function as a Director. A copy of the Non-Executive Director appointment letter can be obtained from the Group Secretary.

Following recommendation by the Nomination Committee, three Non-Executive Directors and one Executive Director were appointed to the Board during 2009. Following the merger with Scarborough Building Society, the Board appointed two additional Non-Executive Directors, Mr P J S Thompson and Mr W R Worsley, both of whom had acted as Non-Executive Directors for the Scarborough Building Society. These appointments were confirmed by the Society's members following election at the Annual General Meeting in April 2009. Further, following the resignation of Mr W H Jack, who retired in May 2009, the Board undertook a process to appoint a new Non-Executive Director, following which Mr J Spence was appointed. In addition, Mr T F Wood was appointed as an Executive Director in September 2009. All four appointments have been approved by the FSA. Mr J Spence and Mr T F Wood will offer themselves for election at the 2010 Annual General Meeting.

Information and professional development

On appointment, new Directors receive appropriate induction; ongoing training and development needs are identified and addressed through an annual performance evaluation process.

Through the Group Secretary, the Chairman ensures that the Directors receive accurate, timely and clear information to facilitate effective contribution to Board discussions and decision making.

The Directors have access to the advice and services of the Group Secretary, whose appointment is a matter for the Board, and who is responsible for ensuring that Board procedures are followed and for advising the Chairman on matters relating to governance.

Performance evaluation

The Board reviews its performance and effectiveness annually. During 2009 the Board undertook an evaluation of the Directors' performance and the Board's effectiveness including the Board's interactions with its sub-committees and Society and Group management. As part of the governance review undertaken during 2009, the terms of reference and composition of all the Board committees has been reviewed and changes approved.

Individual Non-Executive Directors are evaluated on a one-to-one basis by the Chairman. Executive Directors are evaluated by the Group Chief Executive against agreed performance targets for their areas of responsibility and their own personal performance. The Chairman evaluates the Chief Executive's performance and the Vice Chairman evaluates the Chairman's performance.

Re-election Policy

The Society's Rules require that Directors stand for election at the AGM following their appointment and for re-election every three years thereafter. Non-Executive Directors are appointed for an initial period of three years and are not expected to serve more than three terms.

Remuneration

Details relating to Directors' remuneration and contracts are contained in the Directors' remuneration report set out on pages 42 to 45.

Accountability and Audit

Financial reporting

The responsibilities of the Directors in relation to the preparation of the Society's Annual Accounts and a statement that the Society is a going concern are contained in the Statement of Directors' Responsibilities Statement, set out on pages 33 and 34.

Internal control

The Board is responsible for determining the Society's strategy for managing risk and overseeing its systems of internal control. The Executive Directors and senior management are responsible for designing, operating and monitoring risk management and internal controls. Such systems are designed to manage rather than eliminate the risk of failure to achieve the Society's business objectives. The principal categories of financial risk inherent in the Group are described in greater detail in the Business review under the heading 'Principal Risks and Uncertainties' on pages 28 to 31, together with an explanation of the framework adopted by the Group for managing financial risk.

The Group's appetite and risk management policy framework are formally approved by the Board on an annual basis.

The Board reviews the effectiveness of systems of internal control through a combination of processes including:

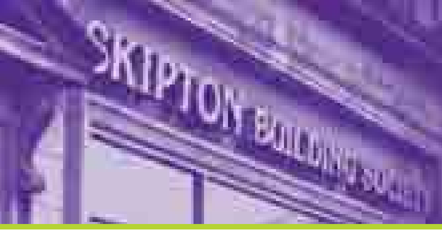
- Regular reports and presentations to the Board by the Chairmen of the various Board committees (see below);
- Presentations to the Board by Divisional Managing Directors about the performance of companies within each of the divisions, summarising both historic and future performance together with key business risks, issues and strategies. Significant risk areas are highlighted, and appropriate control strategies and accountabilities are agreed;
- Regular reports to the Board, through the Audit Committee, from the internal audit function in respect of their independent audits of risk management processes and internal controls' effectiveness across the Society and its subsidiaries. The General Manager, Audit Services, has direct access to the Chairman of the Audit Committee;
- Regular reports to the Board, through the Group Operational Risk Committee, on the principal operational risks facing the Group and the strength of the controls in place to mitigate such risks;
- Regular reports to the Board by the Group Compliance function on regulatory compliance; and
- Reports on at least a quarterly basis presented by the Director of Group Risk.

Steps continue to be taken to embed internal control and risk management further into the operation of the Group and to deal with areas of improvement, which come to the attention of Executive management and the Board.

The Society has a comprehensive system for reporting financial results to the Board. Each of the divisions prepares monthly results with comparisons against budget. The Board reviews these for the Group as a whole and determines appropriate action.

The Society has a number of functions comprising Group Finance, Group Treasury, Group Taxation, Group Compliance, Group Risk and Group Secretariat to establish and monitor the implementation of business standards across the Group. Each of these functions has a detailed procedures manual and is also subject both to self-assessment and to reviews by the internal audit function.

The internal audit function is responsible for independently reviewing and reporting on the adequacy and effectiveness of internal controls operated by management throughout the Group, thereby helping to evaluate and improve the effectiveness of risk management, regulatory compliance, control and governance processes. Through its programme of work,



agreed by the Audit Committee, the internal audit function is able to provide assurance on control effectiveness. The Board is satisfied that the Society maintained an adequate system of internal control that meets the requirements of the Combined Code and the supplementary Turnbull guidance.

Board Committees

In addition to the Audit Committee (see below), the following Board committees exist:

The Nominations Committee is responsible for assessing the necessary and desirable competencies of Board members, evaluating the Board's performance, succession planning and the appointment and removal of Directors. Executive Director appointments and the appointment of the Group Secretary are confirmed by the full Board. The members of the Committee are:

Mr J B Rawlings, Chairman (and also Committee Chairman)
Mr A I Findlay, Vice Chairman
Mr C N Hutton, Non-Executive Director
Ms A B E Kinney, Non-Executive Director

The Remuneration Committee is responsible for reviewing the adequacy and effectiveness of the Society's remuneration policy, considering the risk management implications of the policy and for approving the Directors' remuneration report included within this report. Further detail is set out in the Directors' remuneration report. The members of the Committee are:

Mr C N Hutton, Non-Executive Director (Committee Chairman)
Ms P M Hay-Plumb, Non-Executive Director
Ms A B E Kinney, Non-Executive Director
Mr W R Worsley, Non-Executive Director

The Non-Executive Remuneration Committee is responsible for the review of the fees to be paid to the Vice Chairman and other Non-Executive Directors, in accordance with the Society rules. The members of the Committee are:

Mr J B Rawlings, Chairman (and also Committee Chairman)
Mr D J Cutter, Group Chief Executive
Mr T F Wood, Group Finance Director

Additionally, the Board has delegated responsibility to the following bodies:

The Group Operational Risk Committee meets bi-monthly and its primary responsibility is to develop and keep under review the Group's operational risk management framework. Mrs Davidson (Group Secretary) chairs the Committee which comprises the Group Finance Director, Group Commercial Director, Director of Group Risk, Senior Executives from each of the divisions and members of the Group Operational risk team.

The Asset and Liability Committee is primarily responsible for developing and maintaining policies on structural risk management, liquidity and deposit funding, recommending changes to these policies to the Board, monitoring implementation to ensure that the Group operates within risk limits and that the Society has adequate liquid financial resources to meet its liabilities. Mr Twigg (Group Commercial Director) chairs the Committee which comprises the Group Chief Executive, Group Finance Director, Director of Group Risk and Senior Executives from Treasury, Marketing, Risk and the Group's Mortgages and Savings division.

The Group Retail Credit Committee is primarily responsible for developing and maintaining policies for monitoring and controlling the risks to the Group arising from the credit quality of its retail loan books and the residual values of lending assets, recommending changes to these policies to the Board and monitoring implementation to ensure that the Group operates within risk limits. Mr Wood (Group Finance Director) chairs the Committee which comprises the Group Chief Executive, Group Commercial Director, Director of Group Risk and Group Secretary together with Senior Executives from the Credit Risk team, and the Group's Mortgages and Savings division.

The Group Senior Management Committee is responsible for ensuring that the Group meets its strategic and operational objectives as defined in the corporate plan. Mr Cutter (Group Chief Executive) chairs the Committee which comprises the Group Finance Director, Group Commercial Director, Group Secretary and the Director of Group Risk.

Divisional Boards have been established for the Estate Agency, the Mortgage Services and (up to 7 December 2009) the Credit & Marketing Solutions divisions. Each Divisional Board is chaired by a Senior Executive from that division. Also represented on the Board are two Shareholder Directors (Executive Directors, Group Secretary or other senior Society executives) and the divisional executive management. The Divisional Boards are responsible for the prudent management of the division, within delegated authorities, to meet its strategic and operational objectives as defined in the corporate plan.

Each business within the Mortgages and Savings, Financial Advice and Investment Portfolio divisions is governed by an **Operational Board**. Each Operational Board is chaired by the Divisional Managing Director. Also represented on the Board are at least one Shareholder Director (Executive Director, Group Secretary or other senior Society executive) and the business executive management. The Operational Boards are responsible for the prudent management of the business, within delegated authorities, to meet its strategic and operational objectives as defined in the corporate plan. The **Society Retail Board**, within the Mortgages and Savings division, is primarily responsible for overseeing the day-to-day management of the Society and its operations, corporate planning and changes to Society policy. Mr Cutter (Group Chief Executive) is Chairman of the Society Retail Board which comprises the Group Finance Director, Society General Managers and the Head of Human Resources.

The terms of reference of key Board committees are available from the Group Secretary on request.

Audit Committee and Auditors

The Audit Committee, which meets at least four times a year, comprises four Non-Executive Directors, currently Ms Hay-Plumb (Chairperson) and Messrs Hales, Thompson and Spence. In addition, the Group Chief Executive, Group Finance Director, Director of Group Risk, external audit representatives and the General Manager, Audit Services, regularly attend meetings, by invitation. The Board is satisfied that the composition of the Audit Committee contains Directors with relevant, recent financial experience to provide appropriate challenge to management. Ms Hay-Plumb is a Chartered Accountant and Mr Spence is a fellow of the Chartered Institute of Bankers in Scotland; biographical details for all of the Board are set out in page 15 of this report.

The responsibilities of the Committee are in line with the provisions of the Financial Reporting Council Guidance on Audit Committees. The Audit Committee's primary responsibilities include:

- monitoring the integrity of the Group's financial statements, any formal announcements relating to the Group's financial performance and significant reporting judgments contained in them;
- monitoring the effectiveness of the external audit process and making recommendations to the Board on the appointment, re-appointment and remuneration of the external auditor;
- ensuring that an appropriate relationship between the Group and the external auditor is maintained, including reviewing non-audit services which can be provided and fees; and
- reviewing the effectiveness of the internal audit function. The Committee is responsible for approving, upon the recommendation of the Group Chief Executive, the appointment and removal of the General Manager, Audit Services.

The Board has delegated responsibility for reviewing the effectiveness of the Group's internal controls and risk management systems to the Audit Committee.

In 2009, the Committee met six times in the execution of its responsibilities and, in particular, considered reports on the following matters:

- the system of internal controls;
- the integrity of financial statements;
- the activities of internal and external auditors;
- the effectiveness of the internal audit function;
- the performance of the external auditor;
- the effectiveness of the Committee; and
- the whistle-blowing arrangements.

The Committee also held private discussions with the external auditor, the Director of Group Risk, the General Manager, Audit Services, Group Secretary and the Head of Group Compliance.

The minutes of the Audit Committee are distributed to the Board and the Committee Chairman reports verbally to the Board meeting following Committee meetings.

The Audit Committee regularly monitors the Society's relationship with the external auditor and has adopted a framework for ensuring auditor independence and objectivity, which defines unacceptable non-audit assignments, pre-approval of acceptable non-audit assignments and procedures for approval of other non-audit assignments across the Group. The external auditor, KPMG Audit Plc, undertook a number of non-audit related assignments for the Group during 2009. These were conducted in accordance with the framework and are considered to be consistent with the professional and ethical standards expected of the external auditor. Details of the fees paid to the external auditor for audit and non-audit services are set out in note 7 to these Annual Accounts.

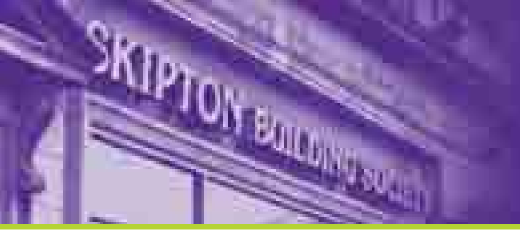
Board and Committee membership attendance record

The attendance of Directors at the scheduled Board, Audit Committee, Nominations Committee and Remuneration Committee meetings during the year is set out below:

Relations with members

As a mutual, the Society's membership is comprised almost exclusively of individuals (rather than institutions), all of whom are our customers.

The Society encourages communication with its members and seeks to respond quickly to all enquiries received. Publications are sent to members regularly throughout the year inviting feedback. We also conduct customer service feedback surveys, market research and analyse customer feedback received through branches and at our Principal Office.



	Board	Audit Committee	Nominations Committee	Remuneration Committee
Mr J B Rawlings (Chairman)	10/11	-	2/2	2/2
Mr A I Findlay (Vice Chairman)	10/11	4/4	1/2	-
Mr D J Cutter	11/11	-	-	-
Mr P R Hales	11/11	6/6	-	-
Ms P M Hay-Plumb	11/11	6/6	-	5/5
Mr C N Hutton	10/11	-	2/2	5/5
Mr W H Jack (retired 1 May 2009)	4/4	-	-	2/2
Ms A B E Kinney	10/11	1/2	2/2	4/4
Mr J Spence (appointed 25 June 2009)	6/6	3/3	-	-
Mr P J S Thompson (appointed 1 April 2009)	7/8	4/4	-	-
Mr R J Twigg	11/11	-	-	-
Mr T F Wood (appointed 7 September 2009)	4/4	-	-	-
Mr W R Worsley (appointed 24 April 2009)	8/8	-	-	3/3

Constructive use of the Annual General Meeting

Each year the Society gives all eligible members at least 21 days' notice of the Annual General Meeting ('AGM'). At the AGM, the Chairman and Group Chief Executive give presentations on the previous year's performance and the main developments in the business. Members present have the opportunity to raise questions and put forward their views. All Directors attend the AGM (unless exceptionally their absence is unavoidable) and are available for questions both during a 'question and answer' session in the meeting and on an individual basis before and after the meeting.

All eligible members are encouraged to participate in the AGM, either in person or by voting proxy. Members can vote by post, in any of the branches, online at skipton.co.uk/agm or at the AGM. All votes are returned to independent scrutineers. A poll is called in relation to each resolution at the AGM and the results of the vote are published on the Society's website and in branches.

In addition, the Summary Financial Statement is included as part of the AGM magazine, the format of which is aimed at making its reading as accessible as possible.

Copies of the full Annual Report and Accounts 2009 are also available on request in branches or by post.

J B Rawlings

J B Rawlings
Chairman
24 February 2010

This report aims to provide information about the Skipton Group's policies on remunerating Directors and discloses the remuneration of the Directors. The Board is committed to best practice in its remuneration policy for Directors and this report explains how the Skipton Group applies the principles in the Combined Code relating to remuneration, in so far as they are considered appropriate to building societies. During 2009, the Board has also taken into account the requirements of the FSA's Remuneration Code.

A summary of this report will again be sent to all members entitled to vote at this year's Annual General Meeting, where members will have the opportunity to vote on the report.

Remuneration Committee

The Remuneration Committee is responsible for determining, on behalf of the Board, the Skipton Group's remuneration policy and reviewing its adequacy and effectiveness. The Committee is also responsible for setting, reviewing and approving remuneration for the Chairman, the Executive Directors and certain other key individuals. The Committee also receives recommendations from the Group Chief Executive for approval of the remuneration for Senior Executives.

During 2009, the Committee reviewed the Skipton Group's remuneration policies leading to the adoption of Remuneration Principles set out below. The Committee will receive a report annually from the Director of Group Risk on the implications of the remuneration policy for risk and risk management and reports from each of the divisions which provides an overview of incentive arrangements (short and long-term), demonstrating how the Remuneration Principles have been applied. The first of these reports will be received in 2010.

The Committee reports to the Board and all recommendations are considered by the Board, but no Director participates in any decisions relating to their own remuneration.

The Remuneration Committee met five times during 2009. In discharging its duties, the Committee reviews and takes into account independently produced data and professional advice in similar financial services organisations. Remuneration consultants were appointed by the Committee during the year, to advise the Committee. These consultants have no other connection with the Skipton Group.

The Committee comprises four Non-Executive Directors, Messrs Hutton (Chairman) and Worsley, Ms Hay-Plumb and Ms Kinney. The Chairman, Group Chief Executive, Head of Human Resources, Director of Group Risk and external advisers may be invited to attend meetings as and when appropriate.

The Non-Executive Directors' Remuneration Committee, which comprises Messrs Rawlings (Chairman), Cutter and Wood, determines the level of the other Non-Executive Directors' fees.

Directors' remuneration policy

Executive Directors' remuneration

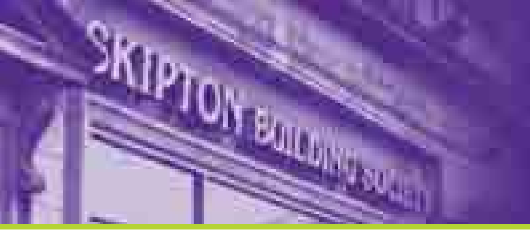
The Board's policy is designed to ensure that Executive Directors' remuneration reflects performance and enables the Skipton Group to attract, retain and motivate a sufficient number of high-calibre individuals to lead and direct the organisation and deliver continually improving business performance.

During the course of 2009, the Committee adopted the Skipton Group's Remuneration Principles which the Committee follows in establishing, implementing and maintaining the remuneration policy. The Principles are relevant to the Society and each of its divisions and references to 'Group' include the Society. The Remuneration Principles are:

- Remuneration at Skipton encourages the highest levels of stewardship and corporate governance;
- Remuneration does not encourage inappropriate taking of risk;
- Remuneration is sufficient to secure and retain the services of talented individuals from other companies or mutuals, recognising the diverse nature of the Group and the nature of its stakeholders;
- Remuneration recognises the appropriate level of Group / divisional and individual performance which will create a strong and sustainable Society for the benefit of borrowers and savers, now and in the future;
- Remuneration for senior management has an element tied to the longer-term performance of the Group / division to reflect the time horizons of the decisions made by Group leaders; and
- Remuneration arrangements are straightforward to communicate, understand, and administer.

The main components of Executive Directors' remuneration are as follows:

- Basic salary – which takes into account job content and responsibilities, individual performance (assessed annually) and salary levels of similar positions in comparable organisations.
- Annual bonus – which is calculated by reference to Group and Society performance measured together with individual performance against personal objectives, both of which are linked to the achievement of the Group's strategic objectives.



Mr Wood, who was appointed as an Executive Director on 7 September 2009, received as a term of his engagement a guaranteed bonus of £25,000 payable in respect of the year ended 31 December 2009.

- Pensions – Messrs Cutter and Twigg are members of the defined benefit pension scheme, the Skipton Building Society Pension & Life Assurance Scheme. During the year, it was agreed that future pension accrual would cease in this scheme with effect from 1 January 2010. From 1 January 2010 all the Executive Directors receive contributions of 20% of basic salary payable into defined contribution schemes.
- Other benefits include provision of a car, or car allowance, and private medical insurance.

Non-Executive Directors' remuneration

Non-Executive Directors' fees (excluding the Chairman) are reviewed annually by the Non-Executive Remuneration Committee with recommendations made to the Board. The reviews are based on the responsibilities and time commitment required for Board and Board sub-committee meetings and also reflect comparable data from similar financial services organisations. Additional fees are paid to those Non-Executives Directors who undertake additional duties and responsibilities, including chairmanship of certain Board committees.

Non-Executive Directors are only entitled to receive fees and do not participate in any performance pay scheme, nor do they receive pension benefits or other benefits.

The Chairman's fees are reviewed and approved by the Remuneration Committee.

Service contracts

The Executive Directors are employed on rolling service contracts which can be terminated by either the Society or the Director giving one year's notice. Unless notice to terminate is given by either party, the contracts continue automatically to the age of 65.

In addition, the Society has agreed that, in the event of certain circumstances arising prior to 31 December 2010, Mr Wood will have the right to terminate his contract within 12 months of such circumstances arising. On such termination he will be entitled to 12 months' salary in addition to any other contractual rights and the Society will indemnify him for any loss he incurs on the sale of his residential property (subject to certain conditions).

Non-Executive Directors do not have service contracts.

Directors' emoluments

KPMG have audited the information set out in the next three tables.

Non-Executive Directors

	2009			2008		
		Committee			Committee	
	Fees	**Fees**	**Total**	Fees	Fees	Total
	£000	**£000**	**£000**	£000	£000	£000
Mr J B Rawlings (Chairman)	**70**	**-**	**70**	70	-	70
Mr A I Findlay (Vice Chairman) (note 1)	**48**	**4**	**52**	44	6	50
Mr P R Hales	**40**	**-**	**40**	40	-	40
Ms P M Hay-Plumb (note 2)	**40**	**3**	**43**	40	-	40
Mr C N Hutton (note 3)	**40**	**3**	**43**	40	2	42
Mr W H Jack (retired 1 May 2009) (note 4)	**13**	**-**	**13**	44	-	44
Ms A B E Kinney (note 5)	**40**	**-**	**40**	40	1	41
Mr R F Marriott (retired 27 May 2008)	**-**	**-**	**-**	13	-	13
Mr J Spence (appointed 1 June 2009)	**23**	**-**	**23**	-	-	-
Mr P J S Thompson (appointed 1 April 2009)	**30**	**-**	**30**	-	-	-
Mr W R Worsley (appointed 24 April 2009)	**30**	**-**	**30**	-	-	-
	374	**10**	**384**	331	9	340

Notes

1. Mr Findlay became Vice Chairman from 24 June 2008 and chaired the Audit Committee from 20 February 2008 until 31 July 2009. Up until 31 July 2009, the fee for Audit Committee Chairman was £6,000 per annum, and from 1 August 2009 the fee increased to £8,000 per annum.

2. Ms Hay-Plumb became Chairperson of the Audit Committee from 1 August 2009.

3. Mr Hutton has chaired the Remuneration Committee since 24 June 2008. Up until 31 July 2009, the fee for Remuneration Committee Chairman was £3,000 per annum, and from 1 August 2009 the fee increased to £4,000 per annum.

4. Mr Jack was Vice Chairman until 24 June 2008.

5. Ms Kinney chaired the Audit Committee until 20 February 2008.

Executive Directors 2009

	Salary £000	Bonus £000	Benefits(†) £000	Sub total £000	Increase in accrued pension £000	Total £000
Mr D J Cutter	**320**	**-**	**41**	**361**	**19**	**380**
Mr R J Twigg	**247**	**-**	**34**	**281**	**7**	**288**
Mr T F Wood (appointed 7 September 2009) (note 1)	**80**	**25**	**118**	**223**	**-**	**223**
	647	**25**	**193**	**865**	**26**	**891**

Executive Directors 2008

	Salary £000	Bonus £000	Benefits(†) £000	Sub total £000	Increase in accrued pension £000	Total £000
Mr J G Goodfellow (retired 31 December 2008) (note 2)	363	37	56	456	7	463
Mr D J Cutter	246	26	41	313	7	320
Mr S W Haggerty (resigned 3 December 2008) (note 3)	210	-	34	244	12	256
Mr R J Twigg	238	24	39	301	6	307
	1,057	87	170	1,314	32	1,346

(†) Benefits comprise the provision of a car, or car allowance, the Society's contributions to the Skipton Building Society Pension & Life Assurance Scheme and private medical insurance contributions.

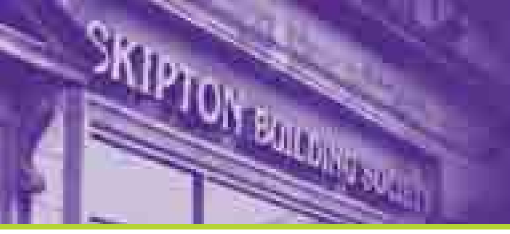
Notes

1. Mr Wood was appointed as an Executive Director on 7 September 2009, and received benefits amounting to £97,770 in relation to relocation costs incurred by him in taking up his appointment.

2. Mr Goodfellow retired as a Director on 31 December 2008 and remained employed as a consultant to the Board until 31 December 2009. Under his settlement agreement, the Society paid a total of £781,000 to Mr Goodfellow. This comprised salary and benefits of £385,000 in accordance with his service agreement and payments of £259,000 in respect of his early retirement and £137,000 in consideration of his entering into certain restrictive covenants. Additionally, Mr Goodfellow accrued pension benefits of £16,710 in the Skipton Building Society Pension & Life Assurance Scheme ('the Scheme') until 31 December 2009. As part of these arrangements the Society also agreed to waive the early retirements discount factors applicable to his benefits in the scheme with effect from 10 January 2010.

   In considering the arrangements, the Committee sought advice from external advisers to reach an agreement that was both fair and reasonable to both the Society and Mr Goodfellow. The Committee believes that the amounts agreed are fair and reasonable and adhere to good practice.

3. Mr Haggerty resigned as an Executive Director on 3 December 2008. In addition to the amounts shown above, Mr Haggerty received a compensation payment of £242,000 in line with his contractual arrangements.

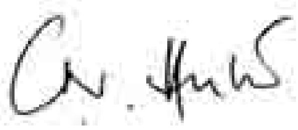


Directors' pension benefits

The information below shows the value of Directors' pension benefits in the Skipton Building Society Pension & Life Assurance Scheme. The increase in accrued pension represents the change in the annual pension to which each Director is entitled as the result of changes in pensionable earnings (excluding inflation) and increases in pensionable service during the year. The transfer value equivalent represents the present capital value of the changes in Directors' accrued pension entitlements excluding members' contributions for the year.

	Increase in accrued pension in the year to 31 December 2009 £000	**Accrued pension entitlement as at 31 December 2009 £000**	**Transfer value of accrued rights at 31 December 2008 £000**	**Members' contribution for the year ended 31 December 2009 £000**	**Transfer values equivalent of increase in accrued pension for the year ended 31 December 2009 £000**	**Transfer values of accrued rights at 31 December 2009 £000**
Mr D J Cutter	**19**	**79**	**421**	**22**	**457**	**900**
Mr R J Twigg	**7**	**64**	**346**	**18**	**293**	**657**
Mr T F Wood (appointed 7 September 2009)	**-**	**-**	**-**	**-**	**-**	**-**

	Increase in accrued pension in the year to 31 December 2008 £000	Accrued pension entitlement as at 31 December 2008 £000	Transfer value of accrued rights at 31 December 2007 £000	Members' contribution for the year ended 31 December 2008 £000	Transfer values equivalent of increase in accrued pension for the year ended 31 December 2008 £000	Transfer values of accrued rights at 31 December 2008 £000
Mr J G Goodfellow (retired 31 December 2008)	7	134	2,014	18	257	2,289
Mr D J Cutter	7	60	451	17	(47)	421
Mr S W Haggerty (resigned 3 December 2008)	12	60	566	15	36	617
Mr R J Twigg	6	57	378	17	(49)	346



C N Hutton
Chairman of the Remuneration Committee
24 February 2010

We have audited the Group and Society Annual Accounts of Skipton Building Society for the year ended 31 December 2009 which comprise the Group and Society Income Statements, the Group and Society Statements of Comprehensive Income, the Group and Society Statements of Financial Position, the Group and Society Statements of Changes in Members' Interest, the Group and Society Statements of Cash Flows and the related notes. These Annual Accounts have been prepared under the accounting policies set out therein.

We have examined the Annual Business Statement (other than the details of Directors and officers upon which we are not required to report) and the Directors' report.

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 auditors

The Directors' responsibilities for preparing the Annual Report & Accounts including the Directors' report, the Annual Business Statement and the Annual Accounts in accordance with applicable law and International Financial Reporting Standards ('IFRSs') as adopted by the EU are set out in the Statement of Directors' Responsibilities on page 33.

Our responsibility is to audit the Annual Accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). We are also responsible for examining the Annual Business Statement (other than the details of Directors and officers) and for reading the information in the Directors' report and assessing whether it is consistent with the accounting records and the Annual Accounts.

We report to you our opinion as to whether the Annual Accounts give a true and fair view and are properly prepared in accordance with the Building Societies Act 1986, regulations made under it and, as regards the Group Annual Accounts, Article 4 of the IAS Regulation. In addition, we report to you our opinion as to whether certain information in the Annual Business Statement gives a true representation of the matters in respect of which it is given, whether the information in the Directors' report is consistent with the accounting records and the Annual Accounts and whether 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 made under it. The information given in the Directors' report includes that information presented in the Chairman's statement, Group Chief Executive's report and Business review that is cross referred from the 'Business review and future developments' section of the Directors' report.

We also report to you if, in our opinion, the Annual Accounts are not in agreement with the accounting records or if we have not received all the information and explanations that we require for our audit.

We read the other information contained in the Annual Report & Accounts and consider whether it is consistent with the audited Annual Accounts. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Annual Accounts, Annual Business Statement and Directors' report. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Annual Accounts and the Annual Business Statement. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the Annual Accounts, and of whether the accounting policies are appropriate to the Group's and Society's circumstances, consistently applied and adequately disclosed.

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

Opinion

In our opinion:

a) 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 December 2009 and of the income and expenditure of the Group and of the Society for the year then ended;

b) 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;

c) the information given in the Directors' report is consistent with the accounting records and the Annual Accounts; and

d) the Annual Accounts, the Annual Business Statement and the Directors' report have each been prepared in accordance with the applicable requirements of the Building Societies Act 1986, regulations made under it and, as regards the Group Annual Accounts, Article 4 of the IAS Regulation.

J L Ellacott (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor

Chartered Accountants

Leeds

24 February 2010

Income Statements

For the year ended 31 December 2009	Notes	Group 2009 £m	Re-presented* Group 2008 £m	Society 2009 £m	Society 2008 £m
Continuing operations					
Interest receivable and similar income	2	**421.8**	771.4	**408.7**	746.8
Interest payable and similar charges	3	**(368.5)**	(683.9)	**(377.2)**	(677.0)
Net interest receivable		**53.3**	87.5	**31.5**	69.8
Fees and commissions receivable	4	**389.0**	371.6	**11.7**	13.5
Fees and commissions payable	5	**(19.4)**	(27.0)	**(2.3)**	(2.0)
Fair value gains / (losses) on financial instruments		**3.9**	(3.3)	**6.6**	(2.9)
Income from shares in subsidiary undertakings		**-**	-	**52.7**	22.6
Profit on disposal of subsidiary undertakings	17b)	**-**	9.1	**-**	-
Share of profits from joint ventures and associates	17c)	**0.2**	3.9	**-**	-
Profit on disposal of associate	17c)	**-**	22.3	**-**	-
Other operating income	6	**13.0**	10.4	**4.2**	2.7
Total income		**440.0**	474.5	**104.4**	103.7
Administrative expenses	7	**(383.7)**	(389.7)	**(53.1)**	(61.4)
Impairment losses on loans and advances	16	**(43.6)**	(34.6)	**(10.4)**	(4.2)
Impairment recoveries / (losses) on debt securities	13	**1.3**	(11.5)	**1.3**	(11.5)
Provisions for liabilities	27	**4.0**	(20.8)	**4.3**	(15.3)
Provisions against investment in subsidiary undertakings	17a)	**-**	-	**(2.8)**	-
Provisions against loans to subsidiary undertakings	17a)	**-**	-	**(2.5)**	-
Profit before tax		**18.0**	17.9	**41.2**	11.3
Tax (expense) / income	11	**(4.3)**	2.8	**2.5**	2.4
Profit for the financial year from continuing operations		**13.7**	20.7	**43.7**	13.7
Discontinued operation					
Profit from discontinued operation	17b)	**43.9**	3.1	**-**	-
Profit for the financial year		**57.6**	23.8	**43.7**	13.7
Profit for the financial year attributable to:					
Members of Skipton Building Society					
Profit for the financial year from continuing operations		**13.5**	19.7	**43.7**	13.7
Profit for the financial year from discontinued operations		**43.9**	3.1	**-**	-
		57.4	22.8	**43.7**	13.7
Non-controlling interests					
Profit for the financial year from continuing operations		**0.2**	1.0	**-**	-
		0.2	1.0	**-**	-
		57.6	23.8	**43.7**	13.7

*2008 has been re-presented to provide the comparatives for the 2009 discontinued operations, see note 17b) for details.

Segmental performance of the Group is shown in note 34.

The notes on pages 55 to 118 form part of these Accounts.

For the year ended 31 December 2009	Notes	Group 2009 £m	Re-presented* Group 2008 £m	Society 2009 £m	Society 2008 £m
Profit for the financial year		**57.6**	23.8	**43.7**	13.7
Other comprehensive income:					
Available-for-sale investments: valuation gains / (losses) taken to equity		**9.4**	(10.5)	**8.7**	(10.5)
Cash flow hedges: gains / (losses) taken to equity		**7.1**	(22.6)	**6.6**	(22.6)
Exchange differences on translation of foreign operations		**2.6**	0.1	**-**	-
Non-controlling interests share restructure		**(0.6)**	(0.6)	**-**	-
Actuarial loss on retirement benefit obligations	35	**(17.9)**	(24.1)	**(9.3)**	(11.7)
Income tax relating to components of other comprehensive income	31	**0.7**	16.2	**(1.6)**	12.6
Other comprehensive income for the year, net of tax		**1.3**	(41.5)	**4.4**	(32.2)
Total comprehensive income for the year		**58.9**	(17.7)	**48.1**	(18.5)
Total comprehensive income attributable to:					
Members of Skipton Building Society		**58.7**	(18.7)	**48.1**	(18.5)
Non-controlling interests		**0.2**	1.0	**-**	-
		58.9	(17.7)	**48.1**	(18.5)

*2008 has been re-presented to provide the comparatives for the 2009 discontinued operations, see note 17b) for details.

The notes on pages 55 to 118 form part of these Accounts.

Statements of Financial Position

As at 31 December 2009	Notes	**Group 2009 £m**	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Assets					
Cash in hand and balances with the Bank of England		**1,272.1**	359.4	**1,272.0**	359.4
Loans and advances to credit institutions	12	**447.5**	1,084.3	**309.1**	1,041.5
Debt securities	13	**2,339.3**	1,734.6	**2,273.6**	1,734.6
Derivative financial instruments	14	**265.5**	429.9	**315.4**	500.4
Loans and advances to customers	15	**10,813.3**	9,567.7	**8,273.1**	7,740.6
Corporation tax asset		**5.6**	12.5	**4.2**	7.2
Deferred tax asset	28	**45.0**	28.1	**19.6**	14.7
Investments in group undertakings	17c)	**1.7**	1.5	**3,322.6**	2,658.7
Intangible assets	18	**182.2**	242.5	**4.0**	2.8
Property, plant and equipment	19	**88.7**	74.3	**37.4**	17.2
Investment property	20	**10.3**	9.1	**17.9**	16.7
Other assets	21	**97.6**	103.1	**9.6**	7.3
Total assets		**15,568.8**	13,647.0	**15,858.5**	14,101.1
Liabilities					
Shares	22	**10,470.2**	8,158.2	**10,470.2**	8,158.2
Amounts owed to credit institutions	23	**942.2**	690.0	**1,371.5**	822.4
Amounts owed to other customers	24	**1,203.9**	2,012.8	**1,339.9**	2,622.6
Debt securities in issue	25	**1,405.6**	1,375.0	**1,405.6**	1,375.0
Derivative financial instruments	14	**263.7**	280.3	**251.1**	247.3
Other liabilities	26	**89.7**	97.8	**6.6**	7.9
Accruals and deferred income		**50.0**	46.4	**4.9**	5.7
Deferred tax liability	28	**13.8**	7.1	**7.5**	3.3
Provisions for liabilities	27	**19.3**	24.0	**11.8**	16.7
Retirement benefit obligations	35	**47.4**	37.9	**19.5**	18.1
Subordinated liabilities	29	**213.0**	183.7	**224.3**	183.7
Subscribed capital	30	**83.6**	26.3	**83.6**	26.3
Total liabilities		**14,802.4**	12,939.5	**15,196.5**	13,487.2
Members' interests					
General reserve		**781.5**	737.0	**685.4**	648.3
Available-for-sale reserve		**(6.2)**	(13.2)	**(7.0)**	(13.2)
Cash flow hedging reserve		**(16.0)**	(21.2)	**(16.4)**	(21.2)
Translation reserve		**3.6**	1.0	**-**	-
Attributable to Members of Skipton Building Society		**762.9**	703.6	**662.0**	613.9
Non-controlling interests		**3.5**	3.9	**-**	-
Total members' interests		**766.4**	707.5	**662.0**	613.9
Total members' interests and liabilities		**15,568.8**	13,647.0	**15,858.5**	14,101.1

These Accounts were approved by the Board of Directors on 24 February 2010 and were signed on its behalf by:

J B Rawlings — Chairman
D J Cutter — Group Chief Executive
T F Wood — Group Finance Director

The notes on pages 55 to 118 form part of these Accounts.

For the year ended 31 December 2009

Group

	General reserve £m	Available-for-sale financial assets £m	Cash flow hedges £m	Translation of foreign operations £m	Sub Total £m	Non-controlling interests £m	Total £m
Balance at 1 January 2009	**737.0**	**(13.2)**	**(21.2)**	**1.0**	**703.6**	**3.9**	**707.5**
Profit for the financial year	57.4	-	-	-	**57.4**	0.2	**57.6**
Other comprehensive income							
Actuarial loss on retirement benefit obligations	(12.9)	-	-	-	**(12.9)**	-	**(12.9)**
Net gains from changes in fair value	-	5.6	5.2	-	**10.8**	-	**10.8**
Exchange differences on translation of foreign operations	-	-	-	2.6	**2.6**	(1.1)	**1.5**
Non-controlling interests share restructure	-	-	-	-	**-**	0.5	**0.5**
Transfer of engagements	-	1.4	-	-	**1.4**	-	**1.4**
Total other comprehensive income (note 31)	**(12.9)**	**7.0**	**5.2**	**2.6**	**1.9**	**(0.6)**	**1.3**
Total comprehensive income for the year	**44.5**	**7.0**	**5.2**	**2.6**	**59.3**	**(0.4)**	**58.9**
Balance at 31 December 2009	**781.5**	**(6.2)**	**(16.0)**	**3.6**	**762.9**	**3.5**	**766.4**
Balance at 1 January 2008	731.4	(5.7)	(4.9)	0.9	721.7	3.5	725.2
Profit for the financial year	22.8	-	-	-	22.8	1.0	23.8
Other comprehensive income							
Actuarial loss on retirement benefit obligations	(17.2)	-	-	-	(17.2)	-	(17.2)
Net gains from changes in fair value	-	(7.5)	(16.3)	-	(23.8)	-	(23.8)
Exchange differences on translation of foreign operations	-	-	-	0.1	0.1	-	0.1
Non-controlling interests share restructure	-	-	-	-	-	(0.6)	(0.6)
Total other comprehensive income (note 31)	(17.2)	(7.5)	(16.3)	0.1	(40.9)	(0.6)	(41.5)
Total comprehensive income for the year	5.6	(7.5)	(16.3)	0.1	(18.1)	0.4	(17.7)
Balance at 31 December 2008	737.0	(13.2)	(21.2)	1.0	703.6	3.9	707.5

For the year ended 31 December 2009

Society

	General reserve £m	Available-for-sale financial assets £m	Cash flow hedges £m	Total £m
Balance at 1 January 2009	**648.3**	**(13.2)**	**(21.2)**	**613.9**
Profit for the financial year	43.7	-	-	**43.7**
Other comprehensive income				
Actuarial loss on retirement benefit obligations	(6.6)	-	-	**(6.6)**
Net gains from changes in fair value	-	6.2	4.8	**11.0**
Total other comprehensive income (note 31)	**(6.6)**	**6.2**	**4.8**	**4.4**
Total comprehensive income for the year	**37.1**	**6.2**	**4.8**	**48.1**
Balance at 31 December 2009	**685.4**	**(7.0)**	**(16.4)**	**662.0**

Balance at 1 January 2008	643.0	(5.7)	(4.9)	632.4
Profit for the financial year	13.7	-	-	13.7
Other comprehensive income				
Actuarial loss on retirement benefit obligations	(8.4)	-	-	(8.4)
Net losses from changes in fair value	-	(7.5)	(16.3)	(23.8)
Total other comprehensive income (note 31)	(8.4)	(7.5)	(16.3)	(32.2)
Total comprehensive income for the year	5.3	(7.5)	(16.3)	(18.5)
Balance at 31 December 2008	648.3	(13.2)	(21.2)	613.9

The notes on pages 55 to 118 form part of these Accounts.

For the year ended 31 December 2009	Notes	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Cash flows from operating activities					
Profit before taxation from continuing operations		**18.0**	17.9	**41.2**	11.3
Profit before taxation from discontinued operations		**45.5**	4.6	**-**	
Adjustments for:					
Impairment losses on loans and advances	16	**43.6**	34.6	**10.4**	4.2
Impairment losses on debt securities	13	**(1.3)**	11.5	**(1.3)**	11.5
Loans and advances written off, net of recoveries		**(29.9)**	(6.5)	**(2.7)**	(0.9)
Provisions against investment in subsidiary undertakings	17a)	**-**	-	**2.8**	-
Provisions against loans to subsidiary undertakings	17a)	**-**	-	**2.5**	-
Goodwill impairment	18	**12.0**	5.9	**-**	-
Depreciation and amortisation	18,19,20	**23.2**	22.8	**4.4**	3.1
Dividends received		**-**	-	**(52.7)**	(22.6)
Interest on capital and subordinated liabilities		**23.3**	14.2	**23.3**	14.2
Loss on sale of property, plant and equipment and investment property		**0.2**	0.3	**0.1**	-
Share of profits from joint ventures and associates	17c)	**(0.2)**	(3.9)	**-**	-
Profit on disposal of subsidiary undertakings	17b)	**(39.7)**	(9.1)	**-**	-
Profit on sale of associate	17c)	**-**	(22.3)	**-**	-
Other non-cash movements		**54.2**	(145.2)	**130.0**	(215.6)
		148.9	(75.2)	**158.0**	(194.8)
Changes in operating assets and liabilities:					
Movement in prepayments and accrued income		**7.9**	4.6	**28.1**	6.7
Movement in accruals and deferred income		**(197.8)**	10.9	**(197.6)**	19.8
Movement in provisions for liabilities		**(8.3)**	20.5	**(7.9)**	15.1
Movement in loans and advances to customers		**329.2**	(680.0)	**940.0**	(651.6)
Movement in shares		**997.2**	1,340.8	**997.2**	1,340.8
Interest received from loans and advances to customers		**482.4**	564.0	**(341.5)**	433.0
Interest paid on shares		**(283.3)**	(404.9)	**(283.3)**	(404.9)
Net movement in amounts owed to credit institutions and other customers		**(1,152.8)**	71.6	**(1,242.4)**	1,087.4
Net movement in debt securities in issue		**47.7**	(277.0)	**35.3**	(276.9)
Net movement in loans and advances to credit institutions		**851.7**	(657.9)	**851.2**	(657.3)
Purchase of mortgage portfolios		**-**	(8.1)	**-**	-
Net movement in other assets		**3.2**	(4.5)	**1.1**	9.6
Net movement in other liabilities		**12.3**	3.5	**(1.2)**	2.0
Income taxes paid		**(0.3)**	(20.6)	**2.2**	(5.6)
Net cash flows from operating activities		**1,238.0**	(112.3)	**939.2**	723.3

Statements of Cash Flows – continued

For the year ended 31 December 2009	Notes	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Net cash flows from operating activities		**1,238.0**	(112.3)	**939.2**	723.3
Cash flows from investing activities					
Purchase of debt securities	13	**(6,036.0)**	(6,648.4)	**(6,036.0)**	(6,648.4)
Proceeds from disposal of debt securities	13	**5,771.8**	7,016.6	**5,747.0**	7,016.6
Purchase of intangible assets	18	**(11.7)**	(12.5)	**(1.1)**	(1.8)
Purchase of property, plant and equipment and investment property	19,20	**(23.9)**	(15.9)	**(17.7)**	(7.5)
Proceeds from disposal of property, plant and equipment and investment property		**0.9**	4.0	**0.1**	1.1
Dividends received		**-**	-	**52.7**	22.6
Dividends paid to non-controlling interests		**-**	(0.5)	**-**	-
Purchase of subsidiary undertakings in the year		**-**	(16.5)	**-**	-
Cash acquired on transfer of engagements		**17.9**	-	**-**	-
Net cash acquired with subsidiary undertakings		**-**	1.3	**-**	-
Further investment in subsidiary undertakings	17a)	**(6.9)**	(13.0)	**(1.5)**	(1.2)
Cash received from sale of subsidiary undertakings	17b)	**97.8**	13.4	**3.2**	-
Debt repaid on sale of subsidiary undertakings		**(19.7)**	-	**-**	-
Cash received from sale of associate and joint venture		**-**	35.0	**-**	-
Net cash flows from investing activities		**(209.8)**	363.5	**(253.3)**	381.4
Cash flows from financing activities					
Proceeds from issue of subordinated liabilities		**-**	75.0	**-**	75.0
Redemption of subordinated liabilities		**-**	(75.0)	**-**	(75.0)
Decrease / (increase) in loans to subsidiary undertakings		**-**	-	**246.6**	(865.7)
Interest paid on subordinated liabilities		**(16.2)**	(10.9)	**(16.2)**	(10.9)
Interest paid on Permanent Interest Bearing Shares		**(7.1)**	(3.2)	**(7.1)**	(3.2)
Net cash flows from financing activities		**(23.3)**	(14.1)	**223.3**	(879.8)
Net increase in cash and cash equivalents		**1,004.9**	237.1	**909.2**	224.9
Cash and cash equivalents at 1 January		**391.4**	154.3	**351.1**	126.2
Cash and cash equivalents at 31 December		**1,396.3**	391.4	**1,260.3**	351.1

Analysis of the cash balances as shown in the Statement of Financial Position:

	Notes	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Cash in hand and balances with the Bank of England		**1,272.1**	359.4	**1,272.0**	359.4
Mandatory reserve deposit with the Bank of England		**(11.7)**	(8.3)	**(11.7)**	(8.3)
		1,260.4	351.1	**1,260.3**	351.1
Loans and advances to credit institutions repayable on demand	12	**135.9**	40.3	**-**	-
Cash and cash equivalents as at 31 December		**1,396.3**	391.4	**1,260.3**	351.1

The notes on pages 55 to 118 form part of these Accounts.

1. Accounting policies

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

a) 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 December 2009; 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 and other financial assets at fair value through the Income Statement.

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

The Directors have adopted IAS 1, *Presentation of Financial Statements (2007)*; IAS 23, *Borrowing Costs (Revised);* Amendments to IFRS 7, *Financial Instruments: Disclosures;* and IFRS 8, *Operating Segments* (see note 36).

The Directors have not adopted IAS 27, *Consolidated and Separate Financial Statements (2008)* and IFRS 3, *Business Combinations (2008)* which, although endorsed by the EU, are not yet effective (see note 36).

In 2007 the Directors adopted IAS 1, *Presentation of Financial Statements – Capital Disclosure*. An analysis of the Group's capital resources and approach to capital management are set out on pages 23 and 24 and form part of the audited Accounts.

Note 36 to the Accounts sets out details of forthcoming standards and interpretations, which are likely to affect the Group, and summarises their impact as at 31 December 2009, and also details the impact of newly adopted standards.

b) Business combinations between mutual organisations

On 30 March 2009, the Society merged with Scarborough Building Society.

The Group has chosen not to early adopt IFRS 3 (2008 Revised): *Business Combinations*, however, in the absence of any other directly applicable GAAP, the principles of IFRS 3 (2008 Revised) have been applied in accordance with the principles applicable to the selection of accounting policies laid out in IAS 8. The revised standard extends its scope to mutual organisations and applies the acquisition method to business combinations which has resulted in some significant prospective changes to the Group's accounting policies. For example, all assets and liabilities acquired, including intangible assets which may not have been recognised by the acquiree, have been measured at fair value at the acquisition date. Notes 1u and 38 to the Accounts set out the approach in detail.

c) Basis of consolidation

Subsidiary undertakings

Subsidiary undertakings are 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 subsidiary undertakings are included in the results from the date that control commences until the date that control ceases. The Group Accounts consolidate the financial statements of the Society and all its subsidiary undertakings, eliminating intra-group balances.

The results of subsidiary undertakings acquired or disposed of during the year are included in the consolidated Income Statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the accounts of subsidiary undertakings to bring the accounting policies in line with those used by the Group. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

As part of the Group's acquisition strategy, within a number of subsidiary undertakings which have less than 100% ownership, there is an option for non-controlling shareholders to sell their shares to the Group at some point in the future. In accordance with IAS 32, *Financial Instruments: Disclosure and Presentation*, the Group recognises the present value of the non-controlling options as a financial obligation, along with recognition of further goodwill on the purchase of remaining non-controlling interests. Under this accounting policy the Group consolidates 100% of the results of affected subsidiary undertakings to reflect the 100% ownership implicit in the recording of the future purchase of the non-controlling remaining shareholdings (that is, put option liability).

Non-controlling interests in the net assets of non-100% consolidated subsidiary undertakings are identified separately from the Group's equity therein. Non-controlling interests comprise the amount of those interests at the date of the original business combination and the non-controlling changes in equity since that date. Losses applicable to the non-controlling

1. Accounting policies (continued)

interests in excess of the non-controlling interests in the subsidiary's equity are allocated against the interests of the Group except to the extent the non-controlling entity has a binding obligation and is able to make an additional investment to cover the losses.

Joint ventures and associates

A joint venture is an undertaking in which the Group has joint control, established by contractual agreement.

An associate is a company over which the Group has significant influence and that is neither a subsidiary undertaking nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is neither control nor joint control over those policies.

The results and assets and liabilities of joint ventures and associates are accounted for in these consolidated financial statements using the equity method of accounting. Investments in joint ventures and associates are carried in the Statement of Financial Position at cost, as adjusted by post-acquisition changes in the Group's share of the net assets of the joint venture or associate, less any impairment in the value of individual investments.

d) 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 cash generating units expected to benefit from the synergies of combination. The impairment test compares the carrying value of goodwill to its associated value in use. The value in use calculations are carried out by discounting the future cash flows of the cash generating unit (note 18). Future cash flows are based upon approved profit budgets for the next three years (adjusted for non-cash items) and assumed growth thereafter for the next 12 years in line with the Bank of England's long-term target for inflation. The Group estimates the discount rate based on current costs of capital adjusted for the risks inherent in each cash generating unit. A 15-year time horizon has been used to reflect that cash generating units are held for the long-term.

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.

Goodwill arising on acquisitions before the transition to IFRS on 1 January 2005 has been retained at the previous UK GAAP amounts subject to being tested for impairment at that date. Goodwill written off to reserves under UK GAAP prior to that date has not been reinstated and is not included in determining any subsequent profit or loss on disposal.

Negative goodwill arising on an acquisition would be recognised directly in the Income Statement.

Computer software, databases and customer contracts

In accordance with IAS 38, *Intangible Assets*, computer software development costs, databases and customer contracts (including internally generated costs) are recognised as an intangible asset only if all of the following tests are met:

- An asset is created that can be identified (such as software and new processes);
- It is probable that the asset created will generate future economic benefits; and
- The development cost of the asset can be measured reliably.

Expenditure incurred to maintain existing levels of performance are recognised as an expense.

Computer software licences, databases and customer contracts recognised as intangible assets are initially recognised at cost and subsequently amortised from the date they are available for use using the straight-line method over their estimated useful economic lives, which range from three to ten years.

Intangible assets are tested for impairment at each reporting date or when there is an indication of impairment. The Group identifies impairment by comparing the future economic benefit against the carrying value of the asset.

1. Accounting policies (continued)

e) Financial assets

In accordance with IAS 39, *Financial Instruments: Recognition and Measurement*, the financial assets of the Group have been classified into the following three categories:

At fair value through profit or loss

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 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:

- Fair value hedges - Where a derivative financial instrument hedges the changes in fair value of a recognised asset or liability or an unrecognised firm commitment, any gain or loss on the hedging instrument is recognised in the Income Statement. To the extent that there is an effective hedge relationship, the associated hedged items (for example, mortgage assets) are stated at fair value in respect of the hedged risk, with any gain or loss also recognised in the Income Statement. As a result the hedging instrument and hedged items offset each other and reduce profit volatility. Any residual fair value hedge ineffectiveness is recognised in the Income Statement.
- Cash flow hedges – Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability, or a highly probable forecast transaction, the effective part of any gain or loss on the derivative financial instrument is recognised directly in equity. Any ineffective portion of the gain or loss on the hedging instrument is recognised in the Income Statement immediately. If the forecast transaction is no longer expected to occur, the cumulative unrealised gain or loss recognised in equity is then recognised immediately in the Income Statement.

The Group discontinues hedge accounting when:

- it is evident from testing that a derivative is not, or has ceased to be, highly effective as a hedge;
- the derivative expires, or is sold, terminated or exercised; or
- the underlying item matures or is sold or repaid.

The Group may also decide to cease hedge accounting even though the hedge relationship continues to be highly effective by ceasing to designate the financial instrument as a hedge.

If the derivative no longer meets the criteria for hedge accounting, the cumulative fair value hedging adjustment is immediately reflected in the Income Statement.

Derivatives that do not qualify for hedge accounting are held at fair value with changes in fair value recognised in the Income Statement with no offset within the Income Statement or deferral to equity.

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivative 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 is then measured in accordance with the relevant accounting policy.

Fair values are obtained from quoted market prices in active markets, recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative. Income and expense on derivative financial instruments is recognised in interest in the Income Statement. Gains and losses on all derivatives, hedged items, and on the sale of available-for-sale assets are recognised in the Income Statement, 'Fair value gains and losses on financial instruments' caption.

1. Accounting policies (continued)

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Group's loans and advances to customers together with certain investment securities are classified as loans and receivables, which are measured at amortised cost using the effective interest method. The effective interest method implies an interest rate which exactly discounts the forecast cash flows of an asset over its expected life back to its carrying value.

In accordance with the effective interest method, upfront costs and fees such as cashbacks, mortgage premia paid on acquisition of mortgage books, mortgage indemnity guarantee insurance paid by customers, procuration fees and completion fees are deferred and recognised over the expected life of mortgage assets. Mortgage discounts are also recognised over the expected life of mortgage assets. Historical and forecast mortgage redemption data and management judgement are used to estimate the expected lives of mortgage assets.

Available-for-sale

Available-for-sale assets are non-derivative financial assets that are not classified into either of the two categories above. Available-for-sale assets are initially recognised at fair value plus directly attributable transaction costs, with subsequent changes in their fair value recognised in equity, except for impairment losses which are recognised in the Income Statement. Interest income is recognised in the Income Statement on an effective yield basis.

The premia and discounts arising on the purchase of these assets are amortised over the period to the maturity date of the security on an effective yield basis. Any amounts amortised are charged or credited to the Income Statement in the relevant financial years.

The fair values of available-for-sale assets are based on quoted prices or, if these are not available, fair value valuation techniques developed by the Group. For quoted prices the bid price is used for assets and the ask price is used for liabilities. Fair value valuation techniques include, but are not limited to, the use of discounted cash flow models, option pricing models and recent arm's-length transactions.

The Group has not classified any assets as held to maturity.

Purchases and sales of financial assets are accounted for at trade date.

f) Financial liabilities

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 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 and loss.

Permanent Interest Bearing Shares with no fixed maturity are classified as financial liabilities and are carried at amortised cost.

g) Impairment of financial assets

Impairment of loans and advances secured on residential property or land

Individual assessments are made of all mortgage loans where objective evidence indicates losses are likely or the property is in possession or where fraud or negligence has been identified. Objective evidence of impairment may include indications that the borrower or group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments or the debt being renegotiated to reduce the burden on the borrower. Based upon these assessments an individual impairment reduction of these assets is made.

In addition, a collective impairment provision is made against the remaining group of loans and advances where objective evidence indicates that it is likely that losses may be realised. The impairment value is calculated by applying various economic factors to our mortgage portfolio exposures. These factors take into account the Group's experience of default rates, loss emergence periods, the effect of regional movements in house prices based on a recognised index and adjustments to allow for ultimate forced sales values and realisation costs.

Impairment provisions are recognised in the Income Statement and reflected as a deduction against the carrying value of the asset. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment losses to decrease, the decrease in impairment loss is recognised through the Income Statement.

1. Accounting policies (continued)

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.

Capitalisation of arrears

Loans are classed as renegotiated when their terms have changed during the year. Those loans that would have been past due or impaired if their terms had not been renegotiated, are as follows:

Loans and advances secured on residential property

The Group applies a policy of capitalising arrears, with the customer's consent, once the customer has made at least six consecutive contractual monthly mortgage repayments following the instance of non-payment. The effect is to bring the loan account up to date and it is therefore no longer past due nor individually impaired (if indeed the individual impairment trigger was the fact that the account was in arrears). If a customer's arrears have previously been capitalised, the customer is required to have made at least 12 consecutive contractual monthly repayments in order to qualify for further capitalisation.

Loans and advances secured on land

The Society applies a similar policy for its commercial loan book as for its residential book, whereby customer arrears can be capitalised following six consecutive contractual monthly repayments following the instance of non-payment, or 12 such repayments if the account has previously had arrears capitalised.

Impairment of other loans and advances

Individual impairment provisions are made to reduce the value of other impaired loans and advances to the amount that the Directors consider is likely ultimately to be received, based upon objective evidence.

Impairment of other financial assets

At each reporting date the Group assesses, on an individual security basis, whether there is objective evidence that financial assets (not at fair value through profit or loss) held by the Group are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

Objective evidence that financial assets are impaired may include default or delinquency by a counterparty, the disappearance of an active market for a security, indications that a counterparty will enter bankruptcy or a significant and prolonged decline in the fair value of a security.

Impairment losses on financial assets carried at amortised cost are measured as the difference between the carrying value of the asset and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognised in the Income Statement and reflected as a deduction against the carrying value of the asset. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment losses to decrease, the decrease in impairment loss is recognised through the Income Statement.

Impairment losses on available-for-sale assets are recognised by transferring the cumulative loss that has been recognised directly in equity to the Income Statement. The cumulative loss that is removed from equity and recognised in the Income Statement is measured as the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss on that asset previously recognised in the Income Statement.

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

h) Derecognition of financial assets and liabilities

Financial assets are derecognised when the contractual rights to receive cash flows have expired or where substantially all the risks and rewards of ownership have been transferred. The Group has not derecognised the loans securing its issue of covered bonds because substantially all the risks and rewards are retained. Financial liabilities are derecognised only when the obligation is discharged, cancelled or has expired.

1. Accounting policies (continued)

i) Foreign currency transactions

All non-Sterling assets and liabilities are translated at the closing rate of exchange. All exchange differences are taken to the Income Statement as they arise.

Foreign exchange transactions are translated into Sterling using the exchange rates prevailing at the dates of the transactions.

The Income Statements of subsidiary undertakings with non-Sterling functional currencies are translated into Sterling at the monthly average rates for the period, and assets and liabilities are translated at the closing rate of exchange at the reporting date. Any exchange differences arising on the translation of net assets of overseas subsidiary undertakings are taken to reserves as a separate component of equity and disclosed in the Statement of Comprehensive Income.

j) Taxation

The income tax expense 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.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted on the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the Statement of Financial Position liability method, which recognises temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor income and expenditure, and differences relating to investments in subsidiary undertakings to the extent that it is probable they will not reverse in the foreseeable future. Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which temporary differences reverse, based on tax rates and laws enacted or substantively enacted at the reporting date.

A deferred tax asset is only recognised to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at least annually and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

k) Leases

Where the Group enters into a lease, which entails taking substantially all the risks and rewards of ownership of an asset, the lease is treated as a finance lease. The asset is recorded in the Statement of Financial Position as an item of property, plant and equipment and is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease less accumulated depreciation and impairment losses. Future instalments under such leases, net of finance charges, are included within payables. Rentals payable are apportioned between the finance element, which is charged to the Income Statement at a constant annual rate, and the amount which reduces the outstanding obligation for future instalments.

All other leases are accounted for as operating leases and the rental charges are charged to the Income Statement on a straight-line basis.

Assets held by the Group on which operating leases are granted are included as items of property, plant and equipment. Rents receivable under operating leases are recognised in the Income Statement on a straight-line basis over the term of the lease.

Where leasehold premises cease to be occupied by the Society or its subsidiary undertakings and current market conditions are expected to preclude sub-letting for a rental sufficient to cover the rental costs, a provision is made to cover the expected deficit.

l) Employee benefits

Defined contribution pension arrangements

Obligations for contributions to defined contribution pension arrangements are recognised as an expense in the Income Statement as incurred.

1. Accounting policies (continued)

Defined benefit schemes

The Group operates five funded defined benefit pension schemes administered by trustees, the funds of which are separate from those of the Group.

Included in the Statement of Financial Position are the Group's net obligations in respect of the defined benefit pension schemes. The obligation of each scheme is calculated separately by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods.

That benefit is discounted to determine its present value, and the fair value of any scheme assets is deducted. The discount rate is based on the average yield available from long-dated AA-rated corporate bonds. The calculation is performed by a qualified actuary using the projected unit credit method.

Past and current service costs are recognised immediately in the Income Statement. Actuarial gains and losses arise from the differences between previous actuarial assumptions and what has actually occurred. These gains and losses are recognised in the Statement of Comprehensive Income.

Contributions are transferred to the trustees on a regular basis to secure the benefits provided under the rules of the scheme. Pension contributions are assessed in accordance with the advice of a professionally qualified actuary.

m) Fees and commissions

Other than those included in the 'effective interest method', fees and commissions receivable are generally recognised, net of VAT (where applicable), when all contractual obligations have been fulfilled. Commissions earned on the sales of properties are recognised as earned on the date contracts are exchanged if thereafter the contract is, or is expected to be, completed.

Commission receivable from the sale of third party Regulated Financial Services products is recognised upon fulfilment of contractual obligations, that is when policies go on risk or, on completion of a mortgage, with a provision for future clawbacks for repayment in the event of early termination by the customer.

Commission income received monthly over the life of a policy is recognised on a cash received basis as this approximates to recognition of income over the period of the service.

Fees and commissions payable are generally recognised on an accruals basis as services are provided.

n) Government grants

Grants relating to expenditure on property, plant and equipment are treated as deferred income and are credited to the Income Statement over the useful economic lives of qualifying assets. Grants relating to revenue expenditure are matched with the expenditure to which they relate.

o) Property, plant and equipment

Property, plant and equipment are measured at historical cost less accumulated depreciation and accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of those items.

Depreciation is calculated to write down the cost of items of property, plant and equipment less estimated residual values over their estimated useful lives as set out below, on a straight-line basis unless stated otherwise.

Freehold and long-leasehold buildings	50 to 100 years
Special purpose head office facility	40 years
Refurbishment of freehold and long-leasehold buildings	5 to 10 years
Short-leasehold buildings	Period of lease
Equipment, fixtures and fittings	2 to 10 years
Motor vehicles	25% of net book value

Land is not depreciated. Major items of property, plant and equipment purchased are depreciated on a monthly basis from the date the asset is available for utilisation. In accordance with IAS 36, *Impairment of assets*, all items of property, plant and equipment are regularly reviewed for indications of impairment. Any impairment identified is charged to the Income Statement.

1. Accounting policies (continued)

p) Segmental reporting

The Group adopted IFRS 8, *Operating Segments*, on 1 January 2009. IFRS 8 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 34.

q) Cash and cash equivalents

For the purposes of the Statements of Cash Flows, cash comprises cash in hand and loans and advances to credit institutions repayable on demand, and cash equivalents comprise highly-liquid investments that are readily convertible into cash with an insignificant risk of changes in value with original maturities of less than three months.

The Statements of Cash Flows have been prepared using the indirect method.

r) Investment properties

Properties held by the Group either being surplus to Group requirements or to earn rentals or for capital appreciation are recognised as investment properties at cost less depreciation. The market value of investment properties is disclosed within the notes to the Accounts, and a valuation is carried out internally on an annual basis.

The depreciation policy for investment properties is consistent with the policy for property, plant and equipment. In accordance with IAS 36, *Impairment of Assets*, investment properties are regularly reviewed for indications of impairment. Any impairment identified would be charged to the Income Statement.

s) Financial guarantee contracts

Where the Society had entered into financial guarantee contracts with a Group company, the Society had previously asserted explicitly that these were insurance contracts. Therefore, under IAS 39, the Society has elected to apply IFRS 4, *Insurance Contracts*, to such financial guarantee contracts and as a result does not fair value such contracts. Under this election the Group assesses at each reporting date whether a financial liability needs to be recognised in relation to the financial guarantee contracts.

t) Sale and repurchase agreements

Investment and other securities may be lent or sold subject to a commitment to repurchase them (a 'repo'). Such securities are retained in the Statement of Financial Position when substantially all the risks and rewards of ownership remain within the Group, and the counterparty liability is included separately in the Statement of Financial Position as appropriate.

The difference between sale and repurchase price is accrued over the life of the agreements.

u) Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year.

The Group also has to make judgements in applying its accounting policies which affect the amounts recognised in the financial statements.

Estimates and judgements 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. The key estimates, assumptions and judgements are set out below:

Effective interest rate

The valuation of assets or liabilities measured at amortised cost is calculated using the effective interest method. The effective interest method implies an interest rate which discounts the future forecast cash flows of an asset over its expected life back to its carrying value. The most critical factor in calculating the amortised cost of assets and liabilities held by the Group is the expected lives of these assets and liabilities which are determined on the basis of historical data and management judgement.

1. Accounting policies (continued)

The impact of a one month increase in the anticipated life of mortgage assets would result in an increase in interest income of Group £2.1m (2008: £2.6m) and Society £1.1m (2008: £1.7m).

Impairment of mortgage loans and advances

The Group regularly reviews its loan portfolios to assess the level of impairment. In determining whether an impairment loss should be recorded in the Income Statement, management makes judgements as to whether there is any objective data indicating that there is a measurable impairment loss. Specifically, management regularly assesses key assumptions such as the probability of an account going into possession, the time period over which an account will exhibit objective evidence of impairment loss (the 'emergence period') and the eventual loss incurred in the event of forced sale or write-off.

Based upon loss modelling techniques used by the Group, and using the Group's stress testing impairment approach, an 18% increase in the forecast unemployment rate above the current view, combined with a fall in house prices of approximately 20-25%, would increase the 2009 year-end provision by £28m.

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 (including the disappearance of an active market), fair value volatility (including any significant reduction in market value), any breach of contract or covenants and the financial stability or any financial difficulties of the counterparty.

Put option obligation

Where the Group acquires a majority shareholding in a subsidiary undertaking, but grants the non-controlling shareholders an option to sell their shares to the Group at some future date, on acquisition the Group estimates the fair value of the total consideration payable in calculating the goodwill arising.

The fair value of both the put option obligation and the associated goodwill recognised are dependent on the following assumptions: an estimate of when the put option will be exercised by the non-controlling shareholders, the market value growth of the obligation and the discount rate used at the reporting date. These assumptions are reviewed on a regular basis by senior management.

Extending the estimated exercise date of all put options by one year would result in the reduction of the aggregate put option obligation by £0.5m (2008: £0.7m). A 10% increase in the aggregate market value of these businesses would increase the put option liability by £1.2m (2008: £3.2m).

Fair value of derivatives and financial assets

Fair values are determined by the three tier valuation hierarchy as defined within IAS 39 and Amendments to IFRS 7, *Financial Instruments: Disclosures*.

Level 1

The most reliable fair values of derivative financial instruments and available-for-sale assets are quoted market prices in an actively traded market.

Level 2

These are valuation techniques for which all significant inputs are taken from observable market data. These include valuation models used to calculate the present value of expected future cash flows and may be employed either when no active market exists or when there are quoted prices available for similar instruments in active markets.

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

Level 3

These are valuation techniques for which any one or more significant input is not based on observable market data.

Valuation techniques include net present value and discounted cashflow models, comparison to similar instruments for which market observable prices exist, Black-Scholes and other valuation models. Assumptions and market observable inputs used in valuation techniques include risk-free and benchmark interest rates, foreign currency exchange 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.

1. Accounting policies (continued)

Taxation

Judgement is required in determining the provision for corporation tax. There are a number of transactions for which the final tax determination is uncertain at the reporting date.

Retirement benefit obligations

In conjunction with its actuaries, the Group makes key financial assumptions which are used in the actuarial valuation of the defined pension benefit obligation and, therefore, changes to these assumptions have an impact on the defined pension obligation, service cost and expected return on plan assets. These assumptions include the inflation and discount rates, the expected return on plan assets and the rate of increase of pensions in payment; see note 35 for further details on these assumptions.

One key assumption is the discount rate used to discount future plan liabilities where currently a 0.25% increase in the discount rate would reduce the pension obligation by £10.5m (2008: £7.8m) and vice versa. Another key assumption surrounds mortality rates where a one year increase in expected lives would increase the pension obligation by £4.0m (2008: £3.2m) and vice versa.

Provisions for liabilities

The ultimate liability for levies payable to the Financial Services Compensation Scheme ('FSCS') to safeguard protected deposits from the five banks and one building society which failed still remains uncertain. The FSCS continues to have significant borrowings of some £20bn in the form of loans from HM Treasury to cover the compensation costs paid and payable in respect of the major bank defaults.

Following FSA guidance, the Society provides for an estimate of the management expense levy payable for those scheme 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 the 12-month LIBOR rate would increase the provision by £1.8m and vice versa.

Fair value business combination calculations

The transfer of engagements of the Scarborough Building Society has been accounted for in accordance with IFRS 3 (2008 Revised): *Business Combinations* (note 1b). All assets and liabilities acquired including intangible assets which may not have been recognised by the acquiree, have been measured at fair value at the acquisition date.

The most significant fair value adjustments relate to the write down of debt securities and the credit and interest rate risk on the acquired mortgage books.

The debt securities fair value adjustment was calculated by applying the latest mark-to-market valuation. The methodology used is fully consistent with the Group's accounting policies.

The credit risk adjustments are based on a number of assumptions with the most significant being the expectation of future house price movements, probabilities of default, and the discount required in the event of a forced sale. To the extent that the expectation of future house price movements on the merger date reduced from that estimated by 10%, the credit risk adjustment would have increased by an estimated £1.8m and vice versa. To the extent that the estimated probability of default was 10% higher, the credit risk adjustment would have increased by an estimated £1.0m and vice versa. To the extent that the discount required in the event of a forced sale increased from the original estimate by 10%, the credit risk adjustment would have increased by an estimated £0.4m and vice versa.

The interest rate adjustment is dependent upon the discount rate used, which represents the rates available in the market on similar product types at the time of the transaction. This rate is adjusted to remove the credit spread inherent in the interest rate, as credit losses have already been accounted for through the credit risk adjustment.

1. Accounting policies (continued)

Similar adjustments apply to the fair value adjustment made in respect of interest rate risk on the acquired savings book. The valuation is similarly dependent upon the discount rate used, which is based on the rate available in the market on similar product types at the time of the transaction.

The fair value adjustment for subscribed capital and subordinated liabilities reflect both the credit and interest rate risk associated with these liabilities.

2. Interest receivable and similar income

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
On loans fully secured on residential property	**460.1**	524.4	**341.5**	402.8
On other loans:				
To subsidiary undertakings	**-**	-	**66.6**	100.6
Other	**22.6**	41.1	**20.3**	34.6
On debt securities	**41.1**	106.8	**39.8**	106.5
On other liquid assets	**10.3**	75.2	**11.9**	73.1
Net (expense) / income on derivative financial instruments	**(112.3)**	23.9	**(71.4)**	29.2
	421.8	771.4	**408.7**	746.8

Included within Group and Society interest receivable and similar income on debt securities is income from fixed income securities of £9.2m (2008: £5.9m).

Included within interest receivable and similar income is interest accrued on impaired financial assets: Group £13.3m (2008: £10.1m), Society £2.5m (2008: £2.2m).

3. Interest payable and similar charges

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
On shares held by individuals	**281.8**	404.8	**281.8**	404.8
On other shares	**-**	0.1	**-**	0.1
On subscribed capital	**7.1**	3.2	**7.1**	3.2
On deposits and other borrowings:				
Subordinated liabilities	**16.2**	10.9	**16.2**	10.9
Subsidiary undertakings	**-**	-	**51.5**	17.9
Wholesale and other funding	**80.9**	239.9	**64.4**	210.6
Net (income) / expense on derivative financial instruments	**(17.7)**	23.1	**(43.8)**	29.5
Other	**0.2**	1.9	**-**	-
	368.5	683.9	**377.2**	677.0

4. Fees and commissions receivable

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
Mortgage related fees	**113.3**	138.9	**2.7**	4.6
General insurance fees	**17.3**	25.1	**5.0**	5.2
Commissions earned on property sales	**128.5**	97.5	**-**	-
Other fees and commissions	**129.9**	110.1	**4.0**	3.7
	389.0	371.6	**11.7**	13.5

5. Fees and commissions payable

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
Mortgage related fees	**13.4**	20.7	**0.1**	0.2
Other fees and commissions	**6.0**	6.3	**2.2**	1.8
	19.4	27.0	**2.3**	2.0

6. Other operating income

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
Investment property income	**0.5**	0.4	**1.5**	1.4
Expected return on pension scheme assets (note 35)	**8.8**	9.9	**4.3**	4.4
Interest on pension scheme liabilities (note 35)	**(10.2)**	(9.7)	**(5.2)**	(4.3)
Government grants	**0.1**	0.1	**-**	-
Other	**13.8**	9.7	**3.6**	1.2
	13.0	10.4	**4.2**	2.7

7. Administrative expenses

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
Employee costs:				
Wages and salaries	**214.2**	213.5	**31.9**	30.5
Social security costs	**19.5**	18.9	**2.8**	2.8
Pension costs:				
Defined contribution arrangements (note 35)	**6.5**	5.8	**2.0**	1.7
Defined benefit schemes service costs (note 35)	**0.8**	2.3	**0.8**	1.2
Defined benefit schemes curtailments (note 35)	**(10.4)**	(6.3)	**(10.4)**	-
	230.6	234.2	**27.1**	36.2
Other administrative expenses	**153.1**	155.5	**26.0**	25.2
	383.7	389.7	**53.1**	61.4
Other administrative expenses include:				
Amortisation of intangible assets (note 18)	**8.5**	7.2	**2.1**	1.0
Depreciation of property, plant and equipment (note 19) and investment properties (note 20)	**10.8**	11.8	**2.3**	2.1
Impairment of goodwill (note 18)	**12.0**	5.9	**-**	-
Auditors' and their associates' remuneration:				
Audit of the Society and Group accounts	**0.2**	0.1	**0.2**	0.1
Audit of the Group's subsidiary undertakings	**0.6**	0.5	**-**	-
Other services pursuant to legislation	**-**	0.1	**-**	-
Other services relating to taxation	**0.1**	0.1	**-**	-
All other services	**0.7**	0.2	**0.4**	0.2
Amounts payable under operating leases:				
Plant and machinery	**4.7**	5.7	**2.9**	3.6
Other	**18.4**	18.7	**5.2**	4.9

8. Staff numbers

The average number of persons employed (including Executive Directors and part-time staff) during the year was as follows:

	Group 2009	Group 2008	**Society 2009**	Society 2008
Principal office and administration centres	**746**	726	**746**	726
Society branch offices	**524**	511	**524**	511
Subsidiary undertakings	**7,288**	7,900	**-**	-
	8,558	9,137	**1,270**	1,237

9. Directors' emoluments

Directors' emoluments are set out within the Directors' remuneration report.

Total Directors' emoluments amounted to £1.3m (2008: £2.8m, including £1.0m compensation for loss of office).

10. Related party transactions

A number of transactions are entered into with related parties in the normal course of business; these are detailed below.

Key management personnel

Key management personnel comprises the Executive Directors and Non-Executive Directors, who are responsible for ensuring that the Society and its subsidiary undertakings meet their strategic and operational objectives.

The table below summarises the benefits paid to key management personnel in the year.

	2009 £m	2008 £m
Short-term employee benefits such as wages and bonuses	**1.2**	2.7
Employer pension contributions	**0.1**	0.1
	1.3	2.8

The table below sets out the outstanding balances in relation to related party transactions with key management personnel and persons who are connected with key management personnel.

	2009 £m	2008 £m
Mortgage loans outstanding at 31 December	**0.8**	0.2

	2009 £m	2008 £m
Savings balances at 31 December	**1.2**	1.4

Interest receivable and payable on the above accounts:	**2009 £m**	2008 £m
Interest receivable	**-**	-
Interest payable	**-**	0.1

Loans and savings of key management personnel are at normal commercial rates. There are no provisions for impairment against these loans.

10. Related party transactions (continued)

Directors' loans and transactions

At 31 December 2009 there were outstanding mortgage loans granted in the ordinary course of business amounting in aggregate to £0.8m (2008: £0.2m) to four (2008: three) Directors and persons who are connected with Directors.

A register is maintained at the Principal Office of the Society which shows details of all loans, transactions and arrangements with Directors and connected persons. A statement for the current financial year of the appropriate details contained in the register will be available for inspection at the Principal Office for a period of 15 days up to and including the Annual General Meeting.

Contributions to pension schemes

During the year, the Group and Society paid contributions of £12.5m (2008: £10.0m) and £6.9m (2008: £4.2m) respectively to pension schemes, which are classified as related parties.

Related party transactions

During the year the Society had the following related party transactions with subsidiary undertakings:

	2009 £m	2008 £m
Rendering and receiving of services	**3.0**	2.6
Recharges of central costs	**12.9**	11.5
Interest received	**66.6**	100.7
Interest paid	**(51.5)**	(17.9)
Other income	**1.0**	1.1
Collateral transferred for covered bond programme	**300.0**	968.9

All above transactions were entered into on an arm's-length basis. For details of the relationship between the Society and its principal subsidiary undertakings see note 17.

At 31 December 2009 the Society owed subsidiary undertakings £1,420.4m (2008: £1,210.5m) and was owed £3,169.3m (2008: £2,580.7m) by subsidiary undertakings and associated companies. Interest on Group borrowings is charged at the appropriate market rate.

During the year, the Group had the following related party transactions with joint ventures and associates.

	2009 £m	2008 £m
Services provided to the Group	**-**	1.1
Services provided by the Group	**1.1**	1.2

11. Taxation expense / (income)

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
Current tax	**8.5**	(4.5)	**(0.9)**	(2.0)
Deferred tax (note 28)	**(2.6)**	3.2	**(1.6)**	(0.4)
	5.9	(1.3)	**(2.5)**	(2.4)

A reconciliation of the tax expense / (income) on profit before tax at the standard UK corporation tax rate to the actual tax expense / (income) is as follows:

	Group 2009 £m	Re-presented Group 2008 £m	Society 2009 £m	Society 2008 £m
Profit before tax from continuing operations	**18.0**	17.9	**41.2**	11.3
Less share of profits of joint venture and associate (net of tax)	**(0.2)**	(3.9)	**-**	-
	17.8	14.0	**41.2**	11.3
Tax calculated at UK standard rate of 28% (2008: 28.5%)	**5.0**	4.0	**11.5**	3.2
Effects of:				
Expenses not deductible for tax purposes	**7.6**	2.7	**2.2**	0.4
Adjustment to tax expense in respect of prior periods	**(5.1)**	(0.8)	**(0.6)**	0.2
Utilisation of tax losses	**-**	-	**-**	-
Tax on dividends receivable	**-**	(0.7)	**(14.7)**	(6.3)
Profit on disposals not taxable	**-**	(8.8)	**-**	-
Other	**(3.2)**	0.8	**(0.9)**	0.1
Tax expense / (income) excluding tax on sale of discontinued operation	**4.3**	(2.8)	**(2.5)**	(2.4)
Tax expense / (income) from continuing operations	**4.3**	(2.8)	**(2.5)**	(2.4)
Tax from discontinued operation	**1.6**	1.5	**-**	-
	5.9	(1.3)	**(2.5)**	(2.4)
Tax on gain on disposal of discontinued operation	**-**	-	**-**	-
Total tax expense / (income)	**5.9**	(1.3)	**(2.5)**	(2.4)

The effective tax rate for the Group for the year ended 31 December 2009 is 24.2% (2008: negative 20.0%) and is lower than the standard rate of corporation tax due to the impact of prior period adjustments arising following the merger with Scarborough Building Society.

12. Loans and advances to credit institutions

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Repayable on demand	**135.9**	40.3	**-**	-
In not more than three months	**307.7**	1,044.0	**305.2**	1,041.5
In more than three months but not more than one year	**-**	-	**-**	-
In more than one year	**3.9**	-	**3.9**	-
	447.5	1,084.3	**309.1**	1,041.5

13. Debt securities

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Issued by public bodies	**223.0**	116.0	**157.7**	116.0
Issued by other borrowers	**2,116.3**	1,618.6	**2,115.9**	1,618.6
	2,339.3	1,734.6	**2,273.6**	1,734.6
Debt securities have remaining maturities as follows:				
In not more than one year	**1,203.8**	1,209.5	**1,173.0**	1,209.5
In more than one year	**1,135.5**	525.1	**1,100.6**	525.1
	2,339.3	1,734.6	**2,273.6**	1,734.6
Transferable debt securities comprise:				
Listed on a recognised investment exchange	**1,435.7**	777.6	**1,370.0**	777.6
Unlisted	**903.6**	957.0	**903.6**	957.0
	2,339.3	1,734.6	**2,273.6**	1,734.6
Market value of listed transferable debt securities	**1,435.7**	777.6	**1,370.0**	777.6

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

At 31 December 2009, £392.2m (2008: £590.5m) of investment securities 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.

Movements in debt securities during the year may be summarised as follows:

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
At 1 January	**1,734.6**	2,124.8	**1,734.6**	2,124.8
Acquired on transfer of engagements	**325.2**	-	**234.8**	-
Additions	**6,036.0**	6,648.4	**6,036.0**	6,648.4
Disposals	**(5,771.8)**	(7,016.6)	**(5,747.0)**	(7,016.6)
Impairment recoveries / (losses)	**1.3**	(11.5)	**1.3**	(11.5)
Changes in fair value	**14.0**	(10.5)	**13.9**	(10.5)
At 31 December	**2,339.3**	1,734.6	**2,273.6**	1,734.6

Pursuant to the amendments to IAS 39, *Financial Instruments: Recognition and Measurement* and IFRS 7, *Financial Instruments: Disclosures*, the Group reclassified certain available-for-sale investment securities to the loans and receivables category. In 2008 the Group identified £339.4m of financial assets that would have met the definition of loans and receivables (if they had not been designated as available-for-sale) for which at 1 July 2008 it had the intention and the ability to hold them for the foreseeable future or until maturity. The average effective interest rate of those investment securities that have transferred is 0.78% (2008: 5.10%).

The table below sets out the financial assets reclassified and their carrying and fair values:

	Group and Society 31.12.09 £m	Group and Society 31.12.08 £m
Carrying value of reclassified assets	**314.1**	303.4
Fair value of reclassified assets	**283.6**	288.9

Included within the 31 December 2009 carrying value of reclassified assets is £68.7m of assets in relation to the transfer of engagements from the Scarborough Building Society.

If these assets had not been reclassified, the fair value gain / (loss) arising in the Statement of Comprehensive Income would have been £4.1m (2008: £(54.4)m).

14. Derivative financial instruments

	Group		Society	
	Positive market value 2009 £m	**Negative market value 2009 £m**	**Positive market value 2009 £m**	**Negative market value 2009 £m**
Derivatives designated as fair value hedges:				
Interest rate swaps	48.9	166.8	48.4	154.6
Currency swaps	185.5	-	185.5	-
	234.4	**166.8**	**233.9**	**154.6**
Derivatives designated as cash flow hedges:				
Interest rate swaps	2.5	25.3	2.0	25.3
	2.5	**25.3**	**2.0**	**25.3**
Other derivatives held at fair value:				
Quanto swaps	0.5	0.2	0.5	0.2
Mortgage products – embedded derivatives	0.1	1.5	0.1	1.5
Equity swaps	4.2	41.0	4.2	41.0
Investment products – embedded derivatives	8.5	4.3	8.5	4.3
Interest rate swaps	14.6	24.6	65.5	24.2
Options	0.7	-	0.7	-
	28.6	**71.6**	**79.5**	**71.2**
	265.5	**263.7**	**315.4**	**251.1**

	Group		Society	
	Positive market value 2008 £m	Negative market value 2008 £m	Positive market value 2008 £m	Negative market value 2008 £m
Derivatives designated as fair value hedges:				
Interest rate swaps	101.8	187.0	101.8	154.2
Currency swaps	255.3	-	255.3	-
	357.1	187.0	357.1	154.2
Derivatives designated as cash flow hedges:				
Interest rate swaps	5.5	33.6	5.5	33.6
	5.5	33.6	5.5	33.6
Other derivatives held at fair value:				
Quanto swaps	0.6	0.1	0.6	0.1
Mortgage products – embedded derivatives	0.2	1.2	0.2	1.2
Equity swaps	-	8.0	-	8.0
Investment products – embedded derivatives	7.5	0.1	7.5	0.1
Interest rate swaps	57.2	50.3	127.7	50.1
Options	1.8	-	1.8	-
	67.3	59.7	137.8	59.5
	429.9	280.3	500.4	247.3

All derivatives held are held for economic hedging purposes.

15. Loans and advances to customers

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Loans fully secured on residential property	**10,036.9**	8,774.8	**7,560.5**	7,031.8
Other loans:				
Loans fully secured on land	**516.8**	526.3	**516.8**	526.3
Other loans	**74.3**	79.3	**23.7**	27.2
Fair value adjustment for hedged risk	**185.3**	187.3	**172.1**	155.3
	10,813.3	9,567.7	**8,273.1**	7,740.6
The remaining maturity of loans and advances to customers from the date of the Statement of Financial Position is as follows:				
On call and at short notice	**40.7**	42.6	**6.2**	5.8
In not more than three months	**5.5**	3.5	**4.4**	2.8
In more than three months but not more than one year	**30.0**	20.8	**24.9**	18.1
In more than one year but not more than five years	**371.1**	262.2	**327.9**	241.3
In more than five years	**10,451.1**	9,282.7	**7,930.3**	7,481.5
	10,898.4	9,611.8	**8,293.7**	7,749.5
Less: Impairment (note 16)	**(85.1)**	(44.1)	**(20.6)**	(8.9)
	10,813.3	9,567.7	**8,273.1**	7,740.6

The maturity analysis above is based on contractual maturity not actual redemption levels experienced by the Group or Society.

Covered bonds

Loans and advances to customers include £992.9m (2008: £968.9m) for both the Group and Society which have been transferred from the Society to Skipton Covered Bonds LLP, a Limited Liability Partnership which is consolidated into the Group Accounts. The loans secure £750.0m (2008: £750.0m) of covered bonds issued by the Society. The loans are retained in the Society's Statement of Financial Position as the Society substantially retains the risks and rewards relating to the loans.

16. Impairment losses on loans and advances

Group

	Loans fully secured on residential property £m	Loans fully secured on land £m	Other loans £m	Total £m
At 1 January 2009				
Individual impairment	27.7	0.7	1.7	**30.1**
Collective impairment	13.2	0.8	-	**14.0**
	40.9	**1.5**	**1.7**	**44.1**
Transfer of engagements				
Individual impairment	4.3	-	-	**4.3**
Collective impairment	23.0	-	-	**23.0**
	27.3	**-**	**-**	**27.3**
Amounts written off during the year				
Individual impairment	(29.5)	-	(0.4)	**(29.9)**
	(29.5)	**-**	**(0.4)**	**(29.9)**
Unwind of merger fair value adjustments				
Collective impairment	(12.5)	-	-	**(12.5)**
	(12.5)	**-**	**-**	**(12.5)**
Income Statement				
Impairment losses on loans and advances				
Individual impairment	48.7	1.1	1.6	**51.4**
Collective impairment	0.6	4.5	-	**5.1**
	49.3	**5.6**	**1.6**	**56.5**
Adjustment to impairment losses on loans and advances resulting from recoveries during the year				
Individual impairment	(0.4)	-	-	**(0.4)**
Charge for the year	**36.4**	**5.6**	**1.6**	**43.6**
At 31 December 2009				
Individual impairment	**50.8**	**1.8**	**2.9**	**55.5**
Collective impairment	**24.3**	**5.3**	**-**	**29.6**
	75.1	**7.1**	**2.9**	**85.1**
At 1 January 2008				
Individual impairment	3.1	0.5	2.5	6.1
Collective impairment	10.1	0.8	-	10.9
	13.2	1.3	2.5	17.0
Amounts written off during the year				
Individual impairment	(5.5)	(0.4)	(0.6)	(6.5)
	(5.5)	(0.4)	(0.6)	(6.5)
Income Statement				
Impairment losses on loans and advances				
Individual impairment	30.5	0.6	0.8	31.9
Collective impairment	3.1	-	-	3.1
	33.6	0.6	0.8	35.0
Adjustment to impairment losses on loans and advances resulting from recoveries during the year				
Individual impairment	(0.4)	-	-	(0.4)
Charge for the year	33.2	0.6	0.8	34.6
Disposal of subsidiary undertakings	-	-	(1.0)	(1.0)
At 31 December 2008				
Individual impairment	27.7	0.7	1.7	30.1
Collective impairment	13.2	0.8	-	14.0
	40.9	1.5	1.7	44.1

16. Impairment losses on loans and advances (continued)

Society

	Loans fully secured on residential property £m	Loans fully secured on land £m	Other loans £m	Total £m
At 1 January 2009				
Individual impairment	2.7	0.7	1.4	**4.8**
Collective impairment	3.3	0.8	-	**4.1**
	6.0	**1.5**	**1.4**	**8.9**
Transfer of engagements				
Collective impairment	4.0	-	-	**4.0**
	4.0	**-**	**-**	**4.0**
Amounts written off during the year				
Individual impairment	(2.7)	-	-	**(2.7)**
	(2.7)	**-**	**-**	**(2.7)**
Income Statement				
Impairment losses on loans and advances				
Individual impairment	4.2	1.1	1.0	**6.3**
Collective impairment	-	4.5	-	**4.5**
	4.2	**5.6**	**1.0**	**10.8**
Adjustment to impairment losses on loans and advances resulting from recoveries during the year				
Individual impairment	(0.4)	-	-	**(0.4)**
Charge for the year	**3.8**	**5.6**	**1.0**	**10.4**
At 31 December 2009				
Individual impairment	**3.8**	**1.8**	**2.4**	**8.0**
Collective impairment	**7.3**	**5.3**	**-**	**12.6**
	11.1	**7.1**	**2.4**	**20.6**
At 1 January 2008				
Individual impairment	0.1	0.5	0.9	1.5
Collective impairment	3.3	0.8	-	4.1
	3.4	1.3	0.9	5.6
Amounts written off during the year				
Individual impairment	(0.4)	(0.4)	(0.1)	(0.9)
	(0.4)	(0.4)	(0.1)	(0.9)
Income Statement				
Impairment losses on loans and advances				
Individual impairment	3.4	0.6	0.6	4.6
	3.4	0.6	0.6	4.6
Adjustment to impairment losses on loans and advances resulting from recoveries during the year				
Individual impairment	(0.4)	-	-	(0.4)
Charge for the year	3.0	0.6	0.6	4.2
At 31 December 2008				
Individual impairment	2.7	0.7	1.4	4.8
Collective impairment	3.3	0.8	-	4.1
	6.0	1.5	1.4	8.9

Included within the charge to the Income Statement is the impact of the change in impairment charge due to the time value of money. For the Group this amounted to £1.1m (2008: £1.1m); for the Society it amounted to £0.4m (2008: £0.2m).

17. Investments in group undertakings

a) Subsidiary undertakings

Investments in subsidiary undertakings are recorded at cost, which includes an estimate of the remaining liability to purchase the non-controlling shareholdings at a future date (where applicable), which is the fair value of the consideration paid, less impairment and dividends paid out of pre-acquisition reserves.

The net movement in investments in subsidiary undertakings during the year is as follows:

Society	**Shares in subsidiary undertakings**		**Loans to subsidiary undertakings**		**Total**	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
Cost						
At 1 January	**78.0**	76.8	**2,580.7**	1,722.0	**2,658.7**	1,798.8
Acquired on transfer of engagements	**79.8**	-	**837.7**	-	**917.5**	-
Additions	**1.5**	1.2	**33.5**	1,023.3	**35.0**	1,024.5
Disposals	**(3.2)**	-	**(280.1)**	(164.6)	**(283.3)**	(164.6)
At 31 December	**156.1**	78.0	**3,171.8**	2,580.7	**3,327.9**	2,658.7
Provisions						
At 1 January	**-**	-	**-**	7.0	**-**	7.0
Provided in the year	**2.8**	-	**2.5**	-	**5.3**	-
Utilised in the year	**-**	-	**-**	(7.0)	**-**	(7.0)
At 31 December	**2.8**	-	**2.5**	-	**5.3**	-
Net book value at 31 December	**153.3**	78.0	**3,169.3**	2,580.7	**3,322.6**	2,658.7

Group goodwill was subject to impairment testing (as detailed in note 18) and of the £12.0m impairment charged in the year, £8.4m was allocated to a number of subsidiary undertakings within the Investment Portfolio operating segment. The Society also had direct investments in subsidiary undertakings within this operating segment and as a result of the same review, £2.8m was provided against the carrying value of these investments.

17. Investments in group undertakings (continued)

At 31 December 2009, the Group held a controlling interest in the following principal trading subsidiary undertakings:

Name of subsidiary undertaking	Principal business activity	Percentage of ownership interest 2009	2008
Advance Mortgage Funding Limited T/A Pink Home Loans *	Provider of mortgage packaging services	**97.5**	97.5
Amber Homeloans Limited	Lending body	**100.0**	100.0
Bailey Computer Services Limited	Provider of IT services	**100.0**	100.0
Baseline Capital Limited	Provider of data analysis solutions	**100.0**	92.5
Connells Limited and subsidiary undertakings *	Estate agency and related businesses	**96.7**	96.7
Homeloan Management Limited and subsidiary undertakings	Provider of mortgage services	**100.0**	100.0
Jade Software Corporation Limited and subsidiary undertakings	Provider of software development services	**54.2**	53.9
Mutual One Limited *	Provider of support services	**82.5**	82.5
North Yorkshire Mortgages Limited	Lending body	**100.0**	-
Northwest Investments NZ Limited	Provider of software development services	**100.0**	100.0
Parnell Fisher Child Holdings Limited *	Independent financial adviser	**79.0**	79.0
Pearson Jones Plc	Independent financial adviser	**100.0**	96.5
Skipton Business Finance Limited	Provider of debt factoring services	**100.0**	100.0
Skipton Covered Bonds Limited Liability Partnership	Mortgage acquisition and guarantor of covered bonds	**(See below)**	(See below)
Skipton Financial Services Limited	Financial adviser	**100.0**	100.0
Skipton Group Holdings Limited ('SGHL')	Intermediate holding company	**100.0**	100.0
Scarborough Investment Services Limited	Intermediate holding company	**100.0**	-
Skipton International Limited (formerly Skipton Guernsey Limited)	Offshore deposit taker and lender	**100.0**	100.0
Skipton Trustees Limited	Provider of will writing services	**100.0**	100.0
Skipton Premises Limited	Property developer	**100.0**	100.0
Scarborough Properties Limited	Property developer	**100.0**	-
Sterling International Brokers Limited *	Money broker	**97.4**	92.0
The Private Health Partnership Limited *	Medical insurance broker	**88.7**	88.7
Thomson Shepherd Limited *	Financial adviser	**75.0**	75.0
Torquil Clark Holdings Limited *	Financial adviser	**86.6**	85.7

* Indicates where an option to purchase non-controlling interests in the future exists. The Group holds a majority stake in these subsidiary undertakings, and the non-controlling shareholders have options to require SGHL to purchase the remaining shareholding at some future date. Under IAS 32, *Financial Instruments: Presentation* and IAS 39, *Financial Instruments: Recognition and Measurement*, these options are designated as 'financial instruments'. As such, the net present value of the estimated future payments under such put options are shown as a financial liability, with a corresponding entry to goodwill. In subsequent periods, any adjustment to the Group's estimation of the present value of the liability will result in a restatement in goodwill. The estimate of liability is principally dependent on the forecast performance of the businesses and the estimated timing of the exercise of the option. The change in fair value of the financial liability due to the accretion of the discount on the liability is expensed in the Income Statement. At 31 December 2009 this financial liability was £17.3m (2008: £28.7m).

17. Investments in group undertakings (continued)

The remaining subsidiary undertakings are 100% owned except for Jade Software Corporation Limited where the Group holds a 54.2% interest (2008: 53.9%) and no put options exist.

The Society's interests in Skipton Covered Bonds Limited Liability Partnership is, in substance, no different than if it was a 100% held subsidiary undertaking and consequently it is consolidated in the Group Accounts.

All the above bodies are incorporated and registered in the United Kingdom except for Skipton International Limited, which is incorporated and registered in Guernsey, and operates in Guernsey and Jersey; and Jade Software Corporation Limited and Northwest Investments NZ Limited, which are both incorporated, registered and operate in New Zealand.

All the above subsidiary undertakings have prepared accounts to 31 December 2009 and their audited results have been included in the Group Accounts.

During the year the Group increased its shareholdings in a number of existing subsidiary undertakings at a total cost of £6.9m (2008: £13.0m). Together with the reassessment of the expected future payments under the put options, this resulted in a further £36,000 (2008: £(0.7)m) of goodwill being recognised.

b) Disposals

During the year the Group disposed of its entire holding in the following subsidiary undertaking:

Name of subsidiary undertaking	Principal business activity	Date of disposal	Cash received £m	Profit on disposal £m
Callcredit Information Group Limited ('CIG')	Credit reference agency, database specialist and related businesses	7 December 2009	97.8	39.7
			97.8	**39.7**

CIG was not a discontinued operation or classified as held-for-sale as at 31 December 2008 and the comparative Income Statement and Statement of Comprehensive Income have been re-presented to show the discontinued operation seperately from continuing operations.

An analysis of the contribution made by CIG to the Group is shown in the table below:

	11 months to 7.12.2009 £m	12 months to 31.12.2008 £m
Interest payable and similar charges	**(0.3)**	(1.5)
Fees and commission receivable	**48.7**	49.4
Administrative expenses	**(42.6)**	(43.3)
Impairment losses	**-**	-
Results from operating activity	**5.8**	4.6
Taxation	**(1.6)**	(1.5)
Results from operating activities after taxation	**4.2**	3.1
Profit on sale of discontinued operation	**39.7**	-
Taxation	**-**	-
Profit on sale of discontinued operation after taxation	**39.7**	-
Profit for the period	**43.9**	3.1

As a result of the disposal of CIG, goodwill of £39.4m was eliminated.

An analysis of the cash flows included within the Group Statement of Cash Flows made by CIG to the Group is shown in the table below:

	11 months to 7.12.2009 £m	12 months to 31.12.2008 £m
Net cash flows from operating activites	**5.5**	5.1
Net cash flows from investing activites	**(5.2)**	(5.4)
Net cash flows from financing activites	**-**	-
Net cash flows from discontinued operation	**0.3**	(0.3)

During 2008 the Group disposed of its entire holding in Direct Life and Pension Services Limited and Amber Select Limited, generating a profit of £9.1m.

17. Investments in group undertakings (continued)

c) Joint ventures and associates

The Group's interests relate to a joint venture where Connells Limited owns 33.3% (2008: 33.3%) of TMG Holdings Limited, a property search provider.

In 2008 an associate where Connells Limited held an interest of 16.4% of Rightmove Plc, an internet property portal, was disposed of during the year, resulting in a profit of £22.3m and a reduction in goodwill of £4.1m.

	Group 2009 £m	Group 2008 £m
Share of joint ventures and associates		
Gross assets	**2.6**	2.3
Gross liabilities	**(0.9)**	(0.8)
At 31 December	**1.7**	1.5
Share of joint ventures and associates		
Income	**11.0**	23.2
Expense	**(10.7)**	(17.8)
Taxation	**(0.1)**	(1.5)
Share of joint ventures' profit after tax	**0.2**	3.9

Joint ventures and associates are recognised within the Group's financial statements using the equity accounting method. The joint ventures and associates are incorporated in England and Wales.

18. Intangible assets

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Software, databases and customer contracts	**22.4**	31.6	**4.0**	2.8
Goodwill	**159.8**	210.9	**-**	-
	182.2	242.5	**4.0**	2.8

Software, databases and customer contracts	**Group 2009 £m**	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Cost				
At 1 January	**75.2**	68.4	**8.0**	6.6
Acquisitions	**-**	1.2	**-**	-
Acquired on transfer of engagements	**2.9**	-	**2.3**	-
Additions	**11.7**	12.5	**1.1**	1.8
Disposals	**(0.4)**	(0.5)	**(0.2)**	(0.4)
Disposals of subsidiary undertakings	**(33.5)**	(6.4)	**-**	-
At 31 December	**55.9**	75.2	**11.2**	8.0
Amortisation and impairment				
At 1 January	**43.6**	40.3	**5.2**	4.6
Charge for the year - continuing operations	**8.5**	7.2	**2.1**	1.0
Charge for the year - discontinued operations	**2.7**	2.6	**-**	-
Write offs	**-**	-	**-**	-
Disposals	**(0.3)**	(0.5)	**(0.1)**	(0.4)
Disposal of subsidiary undertakings	**(21.0)**	(6.0)	**-**	-
At 31 December	**33.5**	43.6	**7.2**	5.2
Net book value at 1 January	**31.6**	28.1	**2.8**	2.0
Net book value at 31 December	**22.4**	31.6	**4.0**	2.8

18. Intangible assets (continued)

Goodwill	**Group 2009 £m**	Group 2008 £m
Cost less amortisation to 1 January 2004		
At 1 January	**222.4**	208.8
Acquisitions of subsidiary undertakings and business units	**0.2**	24.7
Acquired on transfer of engagements	**0.3**	-
Additions and reallocations	**(0.2)**	(0.7)
Disposals	**(41.7)**	(10.4)
At 31 December	**181.0**	222.4
Impairment losses		
At 1 January	**11.5**	6.5
Provisions for impairment loss in the year	**12.0**	5.9
Disposals	**(2.3)**	(0.9)
At 31 December	**21.2**	11.5
Net book value at 1 January	**210.9**	202.3
Net book value at 31 December	**159.8**	210.9

Goodwill acquired in a business combination is allocated, at acquisition, to the cash generating unit (operating segment) that is expected to benefit from that business combination. Before recognition of impairment losses, the cost of goodwill before impairment had been allocated as follows:

Operating segment	**Group 2009 £m**	Group 2008 £m
Mortgage Services	**2.9**	2.4
Estate Agency	**104.3**	99.9
Financial Advice	**36.9**	39.2
Credit & Marketing Solutions	**-**	43.7
Investment Portfolio	**36.9**	37.2
Cost of goodwill	**181.0**	222.4

The recoverable amounts of the operating segments are determined from value in use calculations. The key assumptions for the value in use calculations are those regarding the cash flows, discount rates and growth rates.

The Group prepares cash flow forecasts on the assumption that the subsidiary undertakings within each operating segment are held for long-term investment. The cash flows are derived from the most recent financial budgets for the next three years, which take into account the risks inherent in the businesses, and extrapolates cash flows for subsequent years (up to an additional 12 years) based on a long-term growth rate of 2.0% (2008 2.0%).

The Group estimates discount rates based on the current cost of capital adjusted for the risks inherent in each cash generating unit which fall within a range (pre-tax) of between 10% and 12% (2008: 10% and 12%).

18. Intangible assets (continued)

At 31 December 2009, impairment of £21.2m (2008: £11.5m) was allocated to cash generating units as follows to reduce the goodwill to its estimated recoverable amount, based upon current revised forecasts:

Operating segment	Group 2009 £m	Group 2008 £m
Estate Agency	**3.3**	3.3
Financial Advice	**3.8**	0.2
Credit & Marketing Solutions	**-**	2.3
Investment Portfolio	**14.1**	5.7
Impairment of goodwill	**21.2**	11.5

At 31 December 2009, before impairment testing, goodwill of £36.7m was allocated to the Financial Advice segment. Business volumes have fallen in this sector and the Group has revised its future cash flow forecasts for this operating segment. As a result, an impairment loss of £3.6m has been recognised.

At 31 December 2009, before impairment testing, goodwill of £31.2m was allocated to a number of subsidiary undertakings within the Investment Portfolio operating segment. Due to the downturn in the housing market and reductions in business volumes the Group has revised its cash flows for some of these subsidiary undertakings. As a result, an impairment of £8.4m has been recognised.

19. Property, plant and equipment

Group	2009			2008		
	Land and buildings £m	**Equipment, fixtures and fittings £m**	**Total £m**	Land and buildings £m	Equipment, fixtures and fittings £m	Total £m
Cost						
At 1 January	68.8	111.5	**180.3**	67.2	114.4	181.6
Acquisitions	-	-	**-**	0.1	0.3	0.4
Acquired on transfer of engagements	6.0	-	**6.0**	-	-	-
Additions	17.1	6.4	**23.5**	3.8	7.8	11.6
Disposals	(0.4)	(3.1)	**(3.5)**	(2.3)	(7.9)	(10.2)
Disposal of subsidiary undertakings	(1.7)	(8.0)	**(9.7)**	-	(3.1)	(3.1)
At 31 December	**89.8**	**106.8**	**196.6**	68.8	111.5	180.3
Depreciation						
At 1 January	17.5	88.5	**106.0**	17.0	85.0	102.0
Charge for the year - continuing operations	2.2	8.3	**10.5**	2.0	9.5	11.5
Charge for the year - discontinued operations	0.2	1.0	**1.2**	0.2	1.0	1.2
Disposals	(0.2)	(2.4)	**(2.6)**	(1.7)	(4.3)	(6.0)
Disposal of subsidiary undertakings	(0.8)	(6.4)	**(7.2)**	-	(2.7)	(2.7)
At 31 December	**18.9**	**89.0**	**107.9**	17.5	88.5	106.0
Net book value at 1 January	51.3	23.0	**74.3**	50.2	29.4	79.6
Net book value at 31 December	**70.9**	**17.8**	**88.7**	51.3	23.0	74.3

19. Property, plant and equipment (continued)

Society	**2009** Land and buildings £m	**2009** Equipment, fixtures and fittings £m	**2009** Total £m	2008 Land and buildings £m	2008 Equipment, fixtures and fittings £m	2008 Total £m
Cost						
At 1 January	24.0	28.9	**52.9**	23.7	29.5	53.2
Acquired on transfer of engagements	5.0	-	**5.0**	-	-	-
Additions	16.8	0.5	**17.3**	1.9	1.3	3.2
Disposals	-	(0.5)	**(0.5)**	(1.6)	(1.9)	(3.5)
At 31 December	**45.8**	**28.9**	**74.7**	24.0	28.9	52.9
Depreciation						
At 1 January	9.4	26.3	**35.7**	9.9	26.4	36.3
Charge for the year	1.1	0.9	**2.0**	0.8	1.0	1.8
Disposals	-	(0.4)	**(0.4)**	(1.3)	(1.1)	(2.4)
At 31 December	**10.5**	**26.8**	**37.3**	9.4	26.3	35.7
Net book value at 1 January	14.6	2.6	**17.2**	13.8	3.1	16.9
Net book value at 31 December	**35.3**	**2.1**	**37.4**	14.6	2.6	17.2

The net book value of land and buildings comprises:

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Freehold	**65.5**	45.5	**31.1**	11.2
Long leasehold	**2.9**	2.1	**2.5**	2.1
Short leasehold	**2.5**	3.7	**1.7**	1.3
	70.9	51.3	**35.3**	14.6

20. Investment property

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Cost				
At 1 January	**12.0**	7.7	**20.3**	16.0
Acquired on transfer of engagements	**1.1**	-	**1.1**	-
Additions	**0.4**	4.3	**0.4**	4.3
Disposals	**-**	-	**-**	-
At 31 December	**13.5**	12.0	**21.8**	20.3
Depreciation				
At 1 January	**2.9**	2.6	**3.6**	3.3
Charge for the year	**0.3**	0.3	**0.3**	0.3
Disposals	**-**	-	**-**	-
At 31 December	**3.2**	2.9	**3.9**	3.6
Net book value at 1 January	**9.1**	5.1	**16.7**	12.7
Net book value at 31 December	**10.3**	9.1	**17.9**	16.7

20. Investment property (continued)

The aggregate estimated market value of investment properties is set out in the table below:

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Market value of investment property	**10.7**	10.0	**18.5**	21.9

The estimated market values of the investment properties were determined by an appropriately qualified internal valuer in accordance with RICS Appraisal and Valuation Standards.

21. Other assets

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Trade receivables	**61.2**	65.0	**0.5**	-
Prepayments and accrued income	**28.7**	28.3	**7.6**	5.9
Other	**7.7**	9.8	**1.5**	1.4
	97.6	103.1	**9.6**	7.3

The ageing of the Group's trade receivables at the reporting date was:

	2009			2008		
	Gross £m	**Impairment £m**	**Past due but not impaired £m**	Gross £m	Impairment £m	Past due but not impaired £m
Not past due	**41.8**	**-**	**-**	42.5	-	-
Past due:						
Up to 30 days	**12.4**	**(0.2)**	**12.2**	12.3	(0.3)	12.0
30 to 120 days	**6.6**	**(1.5)**	**5.1**	9.5	(1.2)	8.3
Over 120 days	**5.5**	**(3.4)**	**2.1**	6.1	(3.9)	2.2
	66.3	**(5.1)**	**19.4**	70.4	(5.4)	22.5

The movement in the allowance for impairment in respect of trade receivables during the year was as follows:

	Group 2009 £m	Group 2008 £m
At 1 January	**(5.4)**	(2.0)
Provisions made during the year	**(1.5)**	(4.2)
Receivables written off during the year	**1.1**	0.4
Provisions no longer required	**0.7**	0.4
At 31 December	**(5.1)**	(5.4)

Trade receivables that are neither past due nor impaired arise in the ordinary course of business, £24.6m (2008: £17.2m) of which relates to the debtors of our debt factoring clients and therefore the primary risk of non-payment is borne by the client.

In determining whether trade receivables are impaired, the ageing of the debtor is a key factor.

22. Shares

	Group and Society 2009 £m	Group and Society 2008 £m
Held by individuals	**10,457.6**	8,117.2
Other shares	**3.9**	2.7
Fair value adjustment for hedged risk	**8.7**	38.3
	10,470.2	8,158.2
Shares are repayable from the reporting date in the ordinary course of business as follows:		
On demand	**3,042.0**	2,257.1
In not more than three months	**3,508.8**	3,472.7
In more than three months but not more than one year	**1,354.9**	1,568.2
In more than one year but not more than five years	**1,880.0**	719.4
In more than five years	**684.5**	140.8
	10,470.2	8,158.2

23. Amounts owed to credit institutions

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Amounts owed to subsidiary undertakings	**-**	-	**429.3**	132.4
Other	**942.2**	690.0	**942.2**	690.0
	942.2	690.0	**1,371.5**	822.4
Amounts owed to credit institutions are repayable from the reporting date in the ordinary course of business as follows:				
Repayable on demand	**23.5**	28.3	**452.8**	153.5
In not more than three months	**231.2**	252.1	**231.2**	259.3
In more than three months but not more than one year	**1.0**	159.0	**1.0**	159.0
In more than one year but not more than five years	**686.5**	250.6	**686.5**	250.6
	942.2	690.0	**1,371.5**	822.4

Included in amounts owed to credit institutions is £285.2m (2008: £487.1m) relating to securities sold under agreements to repurchase, the carrying and market value of the related securities is £392.2m (2008: £590.5m) and £375.4m (2008: £477.5m) respectively.

All sale and repurchase transactions are conducted in line with market standard terms and conditions as defined in ISMA PSA Global Master Repurchase Agreements.

24. Amounts owed to other customers

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Amounts owed to subsidiary undertakings	**-**	-	**991.1**	1,078.1
Other	**1,203.9**	2,012.8	**348.8**	1,544.5
	1,203.9	2,012.8	**1,339.9**	2,622.6
Amounts owed to other customers are repayable from the reporting date in the ordinary course of business as follows:				
Repayable on demand	**453.0**	232.4	**991.1**	1,078.1
In not more than three months	**575.6**	1,282.4	**249.9**	1,046.5
In more than three months but not more than one year	**100.1**	426.7	**77.3**	426.7
In more than one year but not more than five years	**75.2**	71.3	**21.6**	71.3
	1,203.9	2,012.8	**1,339.9**	2,622.6

25. Debt securities in issue

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Certificates of deposit	**135.7**	341.1	**135.7**	341.1
Other debt securities	**1,168.5**	895.5	**1,168.5**	895.5
Fair value adjustment for hedged risk	**101.4**	138.4	**101.4**	138.4
	1,405.6	1,375.0	**1,405.6**	1,375.0
Debt securities in issue are repayable from the date of the Statement of Financial Position in the ordinary course of business as follows:				
In not more than one year	**605.1**	818.8	**605.1**	818.8
In more than one year	**800.5**	556.2	**800.5**	556.2
	1,405.6	1,375.0	**1,405.6**	1,375.0

Included in Group and Society other debt securities are 19 (2008: 33) floating rate notes issued to the capital markets totalling £395.5m (2008: £732.4m).

26. Other liabilities

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Trade payables	**7.0**	7.4	**0.3**	0.4
Tax deducted at source from interest paid	**3.5**	4.5	**2.6**	4.0
Fair value of put option obligation	**17.3**	28.7	**-**	-
Other payables	**61.9**	57.2	**3.7**	3.5
	89.7	97.8	**6.6**	7.9

The movement within the fair value of put obligation is summarised below:

	Group 2009 £m	Group 2008 £m
At 1 January	**28.7**	40.6
Unwind of the discount factor	**-**	1.9
Exercise of put options by non-controlling shareholders	**(8.1)**	(2.2)
Revaluation of market value and future exercise dates	**3.2**	(11.3)
Acquisition of subsidiary undertakings during the year	**-**	2.9
Disposal of subsidiary undertakings during the year	**(2.7)**	(2.7)
Dividends paid to non-controlling shareholders	**(3.8)**	(0.5)
At 31 December	**17.3**	28.7

27. Provisions for liabilities

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Provision for the costs of closed branches	**5.7**	5.3	**0.2**	-
Financial Services Compensation Scheme	**11.1**	16.3	**11.1**	16.3
Regulatory and other provisions	**2.5**	2.4	**0.5**	0.4
	19.3	24.0	**11.8**	16.7

Movements in provisions during the year:

Group	Provision for the costs of closed branches		Financial Services Compensation Scheme		Regulatory and other		Total	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
At 1 January	**5.3**	0.9	**16.3**	-	**2.4**	2.6	**24.0**	3.5
Acquired on transfer of engagements	**0.8**	-	**2.7**	-	**-**	-	**3.5**	-
(Release) / charge for the year	**0.2**	4.5	**(4.3)**	16.3	**0.1**	-	**(4.0)**	20.8
Utilised during the year	**(0.6)**	(0.1)	**(3.6)**	-	**-**	(0.2)	**(4.2)**	(0.3)
At 31 December	**5.7**	5.3	**11.1**	16.3	**2.5**	2.4	**19.3**	24.0

Society	Provision for the costs of closed branches		Financial Services Compensation Scheme		Regulatory and other		Total	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
At 1 January	**-**	-	**16.3**	-	**0.4**	1.6	**16.7**	1.6
Acquired on transfer of engagements	**0.8**	-	**2.7**	-	**-**	-	**3.5**	-
(Release) / charge for the year	**-**	-	**(4.3)**	16.3	**-**	(1.0)	**(4.3)**	15.3
Utilised during the year	**(0.6)**	-	**(3.6)**	-	**0.1**	(0.2)	**(4.1)**	(0.2)
At 31 December	**0.2**	-	**11.1**	16.3	**0.5**	0.4	**11.8**	16.7

The provision for the costs of closed branches is expected to reverse over the remaining life of the leases or period to anticipated date of disposal, if sooner.

Included in 'Regulatory and other provisions' is a provision for claims and potential claims that arise during the normal course of business in relation to surveys and valuations performed by the Group. The provision is calculated on a case by case basis, the provisioning for which takes into account market conditions and a prudent attitude to risk. These provisions are classed as non-current.

27. Provisions for liabilities (continued)

As a result of notifications it received from the Financial Services Authority, the Society recognised in last year's results a provision of £16.3m in respect of the management expenses in relation to its share of the interest cost of the first three years of the FSCS' loans from HM Treasury. Since then, the Financial Services Authority has revised its position and notified firms that accruals should now be made only for liabilities incurred as a result of market participation up to the reporting date. This has resulted in a provision release of £4.3m. The first FSCS invoice of £3.6m has also been paid in the year which, together with the provision release and an additional £2.7m provision transferred as part of the merger with the Scarborough, has resulted in a remaining provision of £11.1m as at 31 December 2009.

The Society's provision does not include management expense levies for any further scheme years, nor for any compensation levies which may arise from any ultimate payout on the claims.

For further details on the Financial Services Compensation Scheme see note 32.

28. Deferred tax

Deferred taxes are calculated on timing differences under the liability method using an effective tax rate of 28% (2008: 28%).

The movement in deferred tax during the year is as follows:

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
At 1 January	**21.0**	11.8	**11.4**	1.9
Income Statement (note 11)	**2.6**	(3.2)	**1.6**	0.4
Items taken directly to reserves	**(3.7)**	11.9	**(3.2)**	9.1
Acquired on transfer of engagements	**11.9**	-	**2.3**	-
Acquisitions / disposals	**(0.6)**	0.5	**-**	-
At 31 December	**31.2**	21.0	**12.1**	11.4

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

Deferred tax assets	**Group 2009 £m**	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Fixed asset temporary differences	**2.8**	3.4	**-**	-
Pension benefits	**13.3**	11.5	**5.5**	5.4
Provisions for loan impairment	**1.4**	0.3	**0.5**	0.1
Corporation tax losses	**4.1**	2.4	**2.7**	1.0
Derivatives and loans	**20.6**	8.2	**10.9**	8.2
Other	**2.8**	2.3	**-**	-
	45.0	28.1	**19.6**	14.7

Deferred tax liabilities	**Group 2009 £m**	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Fixed asset temporary differences	**4.0**	4.7	**1.6**	1.7
Derivatives and loans	**9.0**	1.6	**5.9**	1.6
Other	**0.8**	0.8	**-**	-
	13.8	7.1	**7.5**	3.3
Net deferred tax asset	**31.2**	21.0	**12.1**	11.4

28. Deferred tax (continued)

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

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Fixed asset temporary differences	**(0.6)**	(0.5)	**(0.4)**	-
Provisions	**(7.6)**	2.2	**-**	-
Unwind of merger fair value adjustments	**6.4**	-	**(0.8)**	-
Other	**(0.8)**	1.5	**(0.4)**	(0.4)
	(2.6)	3.2	**(1.6)**	(0.4)

There is no unrecognised deferred tax relating to trading losses brought forward at 31 December 2009 (2008: £Nil).

29. Subordinated liabilities

	Group		**Society**	
	2009 £m	2008 £m	**2009 £m**	2008 £m
Floating rate notes	**-**	-	**11.3**	-
Subordinated fixed rate notes 2014	**15.2**	15.3	**15.2**	15.3
Subordinated fixed rate notes 2015	**19.5**	-	**19.5**	-
Subordinated fixed rate notes 2017	**9.9**	-	**9.9**	-
Subordinated fixed rate notes 2018	**128.1**	128.1	**128.1**	128.1
Subordinated fixed rate notes 2019	**10.2**	10.2	**10.2**	10.2
Subordinated fixed rate notes 2022	**31.2**	31.2	**31.2**	31.2
	214.1	184.8	**225.4**	184.8
Unamortised discount on issue	**(1.1)**	(1.1)	**(1.1)**	(1.1)
	213.0	183.7	**224.3**	183.7

All the fixed rate notes are denominated in Sterling. Coupons are paid on a fixed basis annually except for the notes repayable in 2014, the notes repayable in 2017, £75.0m (2008: £75.0m) of the notes repayable in 2018 and the notes repayable in 2019 where coupons are paid on a fixed basis semi-annually.

All the notes are repayable at maturity or earlier, at the option of the Society. In each case the option for early repayment may only be exercised with the prior consent of the Financial Services Authority. The note holders' rights are subordinate to those of the depositors and other payables, and also to those of the shareholders in respect of share principal and accrued interest.

The £11.3m 2009 Society Floating Rate Notes in the above table relates to a floating rate subordinated debt Issue from Scarborough Building Society to Scarborough Channel Islands Limited which was acquired by Skipton as a result of the merger. The variable rate coupons on this issue are paid on a quarterly basis.

All of the values in the above table have been calculated using the face value plus accrued interest with the exception of the 'Unamortised discount on issue' values which are the difference between the associated face values and current book values.

30. Subscribed capital

	Group and Society 2009 £m	2008 £m
6.875% Permanent Interest Bearing Shares	**42.0**	-
8.500% Permanent Interest Bearing Shares	**15.3**	-
12.875% Permanent Interest Bearing Shares	**26.3**	26.3
	83.6	26.3

All Permanent Interest Bearing Shares are unsecured and rank pari passu with each other. They are deferred shares of the Society and rank behind the claims against the Society of all subordinated note holders, depositors, payables and investing members of the Society. These shares are measured at amortised cost.

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

Group	2009			2008		
	Before-tax amount £m	**Tax (expense) / benefit £m**	**Net-of-tax amount £m**	Before-tax amount £m	Tax (expense) / benefit £m	Net-of-tax amount £m
Available-for-sale financial assets	**9.4**	**(2.4)**	**7.0**	(10.5)	3.0	(7.5)
Cash flow hedges	**7.1**	**(1.9)**	**5.2**	(22.6)	6.3	(16.3)
Actuarial (loss) / gains on retirement benefit obligations	**(17.9)**	**5.0**	**(12.9)**	(24.1)	6.9	(17.2)
Translation of foreign operations	**2.6**	**-**	**2.6**	0.1	-	0.1
Non-controlling interests share restructure	**(0.6)**	**-**	**(0.6)**	(0.6)	-	(0.6)
Other comprehensive income	**0.6**	**0.7**	**1.3**	(57.7)	16.2	(41.5)

Society	2009			2008		
	Before-tax amount £m	**Tax (expense) / benefit £m**	**Net-of-tax amount £m**	Before-tax amount £m	Tax (expense) / benefit £m	Net-of-tax amount £m
Available-for-sale financial assets	**8.7**	**(2.5)**	**6.2**	(10.5)	3.0	(7.5)
Cash flow hedges	**6.6**	**(1.8)**	**4.8**	(22.6)	6.3	(16.3)
Actuarial (loss) / gains on retirement benefit obligations	**(9.3)**	**2.7**	**(6.6)**	(11.7)	3.3	(8.4)
Other comprehensive income	**6.0**	**(1.6)**	**4.4**	(44.8)	12.6	(32.2)

32. Other financial commitments

a) The Society is obliged under Section 22 of the Building Societies Act 1986 to discharge the liabilities of its subsidiary undertakings incurred prior to 11 June 1996 when this section was repealed. Additionally, the Society has given a legal undertaking agreeing to discharge the liabilities of Skipton International Limited in so far as it is unable to discharge them out of its own assets whilst it remains a subsidiary undertaking of Skipton Building Society. Furthermore, the Society has confirmed it will provide continuing support to those subsidiary undertakings that have net liabilities at 31 December 2009.

32. Other financial commitments (continued)

b) 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 have been triggered against the FSCS in relation to Bradford and Bingley plc, Kaupthing Singer & Friedlander, Heritable Bank Plc, Landsbanki Islands hf, London Scottish Bank Plc and Dunfermline Building Society.

The FSCS will meet these current claims by way of loans received from HM Treasury. The terms of these loans are interest only for the first three years, and the FSCS will seek to recover the interest cost, together with ongoing management expenses, by way of annual management expenses levies on member firms over this period. Subsequently, should there be insufficient funds from the realisation of the failed banks' assets to fully extinguish the FSCS' loans from HM Treasury, this may result in the FSCS raising a compensation levy on member firms.

c) Capital commitments at 31 December for which no provision has been made were as follows:

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Contracted but not provided for	**2.1**	15.1	**1.2**	15.0

d) Total commitments under non-cancellable operating leases are as follows:

	Land and buildings 2009 £m	**Other 2009 £m**	Land and buildings 2008 £m	Other 2008 £m
Group				
Amounts falling due:				
Within one year	**18.0**	**4.9**	18.6	3.9
Within two to five years inclusive	**56.0**	**7.8**	60.7	3.3
Over five years	**40.5**	**0.3**	43.1	-
	114.5	**13.0**	122.4	7.2
Society				
Amounts falling due:				
Within one year	**5.8**	**3.7**	5.3	2.8
Within two to five years inclusive	**22.6**	**5.5**	19.8	1.5
Over five years	**19.7**	**-**	21.1	-
	48.1	**9.2**	46.2	4.3

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 Society 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. The Group does not run a trading book.

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 tend to have a smaller or no initial net investment relative to financial assets / liabilities offering the same risk / return as cash flows and are generally settled at a future date.

The Board has authorised the use of derivatives by the Group to reduce the risk of loss arising from changes in market risks in accordance with Section 9A (4) of the Building Societies Act 1986 and are used by the Group for economic hedging purposes only.

33. Financial instruments (continued)

Types of derivatives

The principal derivatives used by the Group are interest rate swaps, interest rate options, forward rate agreements and foreign exchange contracts 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	Type of hedge
Fixed rate savings products	Sensitivity to falls in interest rates	Receive fixed interest rate swaps (fair value hedge)
Variable rate funding	Sensitivity to increases in interest rates	Pay fixed interest rate swaps (cash flow hedge)
Fixed rate mortgage lending	Sensitivity to increases in interest rates	Pay fixed interest rate swaps (fair value hedge)
Variable rate liquidity	Sensitivity to falls in interest rates	Receive fixed interest rate swaps (cash flow hedge)
Fixed rate funding	Sensitivity to falls in interest rates	Receive fixed interest rate swaps (fair value hedge)
Fixed rate asset investments	Sensitivity to increases in interest rates	Pay fixed interest rate swaps (fair value hedge)
Mortgage and savings products with embedded options	Sensitivity to changes in interest rates	Interest rate swaps, caps and floors and other options
Equity linked investment products	Sensitivity to changes in equity indices	Equity linked interest rate swaps
Investment and funding in foreign currencies	Sensitivity to changes in foreign exchange rates	Cross currency interest rate swaps and foreign exchange contracts (fair value hedge)

Derivative products, which are combinations of more basic derivatives, are used only in circumstances where the underlying position being hedged contains similar risk features.

In such cases the derivative used will be designed to minimise the risks of the underlying asset or liability.

Controls over financial instruments

The Group has a formal structure of managing risk, including established risk limits, reporting requirements, mandates and other control procedures. This structure is reviewed regularly by the Asset and Liability Committee ('ALCO'), which is charged with the responsibility for managing and controlling the Statement of Financial Position exposures of the Group.

Credit exposures arising on derivative contracts with certain counterparties are collaterised with cash deposits, to mitigate credit exposures. All derivative activity is contracted with OECD financial institutions.

The accounting policies for derivatives are described in note 1 to the Accounts.

Hedge accounting

A fair value hedge is a hedge of the exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect profit or loss. For each main class of fair value hedge, documentation is produced in accordance with requirements of IAS 39.

A cash flow hedge is a hedge of the exposure to variability in cash flows that (i) is attributable to a particular risk associated with a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction and (ii) could affect profit or loss. For each main class of cash flow hedge, documentation is produced in accordance with requirements of IAS 39.

33. Financial instruments (continued)

Cash flow hedging is used primarily for interest rate swaps taken out to pre-hedge fixed mortgage completions and pre-hedge fixed savings products prior to receipt of funds. The weighted average maturity of interest rate swaps being cash flow hedged at 31 December 2009 was approximately 2.9 years (2008: 3.3 years); the amounts held in the cash flow hedging reserve will be recognised in the Income Statement over this period.

Financial risks

The principal financial risks to which the Group is exposed are liquidity risk, market risk and credit risk. Each of these is considered below. An overview of how the Group manages the risks it faces is also disclosed in the 'Principal risks and uncertainties' section of the Business review.

Liquidity risk

Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due or can do so only at excessive cost.

The Group's liquidity policy is to maintain sufficient liquid resources to cover imbalances and fluctuations in funding, to retain full public confidence in the solvency of the Group and to enable the Group to meet its financial obligations as they fall due. This is achieved through maintaining a prudent level of liquid assets, maintaining an appropriate mix between savings and deposit funding balances and through rigorous management control of the growth of the business. In practice this is achieved by ensuring the prudential liquidity ratio (prudential liquidity as a percentage of share and deposit liabilities) is held within a certain range at all times, by ensuring reliance on deposit funding is not excessive and through the planning, implementation and management control and review of business flows.

The Board is responsible for setting limits over the level, composition and maturity of liquidity and deposit funding balances. Such limits are reviewed by the Board at least annually. Compliance against these limits is monitored daily by Finance and Group Risk personnel (ie independent of Treasury staff).

In addition a series of liquidity stress tests are performed weekly by Group Market Risk personnel, and formally reported to ALCO monthly, to ensure the Group maintains adequate liquidity for business purposes even under stressed conditions.

A significant development of liquidity stress testing and forecast models has been carried out in 2009 as part of the standards set out by the FSA in PS09/16 *Strengthening Liquidity Standards*. A wide range of scenarios are considered in addition to the idiosyncratic, market-wide and combined stress scenarios prescribed by the FSA. An analysis of the liquidity portfolio is set out in the table below:

	Group 2009		Group 2008	
	£m	**%**	£m	%
Cash in hand and balances with the Bank of England	**1,272.1**	**31.3**	359.4	11.3
Cash with banks and building societies	**437.4**	**10.8**	1,064.4	33.5
Gilts	**152.7**	**3.8**	111.0	3.5
Certificates of deposit	**903.6**	**22.3**	946.5	29.8
Local authority investments	**10.4**	**0.2**	3.7	0.1
Fixed rate bonds	**283.8**	**7.0**	1.7	0.1
Floating rate notes	**684.8**	**16.9**	390.0	12.3
Residential mortgage backed securities	**255.9**	**6.3**	243.0	7.6
Commercial mortgage backed securities	**58.2**	**1.4**	58.6	1.8
	4,058.9	**100.0**	3,178.3	100.0

During the year the liquidity balances have increased from £3,178.3m at 31 December 2008 to £4,058.9m at 31 December 2009, expressed as a proportion of our combined shares and deposit liabilities this represents an increase from 28.84% to 28.95%.

33. Financial instruments (continued)

The following table is an analysis of gross contractual cash flows payable under financial liabilities (which is not expected to differ significantly to the expected maturity):

Group **2009**

Liabilities	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Shares	**6,551.6**	**1,369.6**	**1,909.1**	**684.5**	**10,514.8**
Amounts owed to credit institutions, customers and debt securities	**1,236.7**	**151.1**	**1,271.4**	**-**	**2,659.2**
Derivative financial instruments	**46.9**	**116.3**	**239.0**	**102.1**	**504.3**
Subordinated liabilities	**4.0**	**11.9**	**78.5**	**259.0**	**353.4**
Subscribed capital	**1.6**	**6.3**	**31.7**	**103.5**	**143.1**
	7,840.8	**1,655.2**	**3,529.7**	**1,149.1**	**14,174.8**

Group 2008

Liabilities	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Shares	5,736.3	1,633.2	793.4	140.8	8,303.7
Amounts owed to credit institutions, customers and debt securities	1,585.2	1,005.3	886.2	51.6	3,528.3
Derivative financial instruments	45.2	129.1	175.2	23.3	372.8
Subordinated liabilities	3.7	10.4	56.4	254.2	324.7
Subscribed capital	1.6	1.6	12.9	22.5	38.6
	7,372.0	2,779.6	1,924.1	492.4	12,568.1

For each material class of financial liability a maturity analysis is provided in notes 22 to 25.

Society **2009**

Liabilities	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Shares	**6,551.6**	**1,369.6**	**1,909.1**	**684.5**	**10,514.8**
Amounts owed to credit institutions, customers and debt securities	**1,712.8**	**167.3**	**1,277.0**	**-**	**3,157.1**
Derivative financial instruments	**47.1**	**116.8**	**239.0**	**102.2**	**505.1**
Subordinated liabilities	**4.1**	**12.0**	**79.7**	**264.4**	**360.2**
Subscribed capital	**1.6**	**6.3**	**31.7**	**103.5**	**143.1**
	8,317.2	**1,672.0**	**3,536.5**	**1,154.6**	**14,680.3**

Society 2008

Liabilities	0-3 months £m	3-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Shares	5,736.3	1,633.2	793.4	140.8	8,303.7
Amounts owed to credit institutions, customers and debt securities	1,758.7	1,005.3	886.2	51.6	3,701.8
Derivative financial instruments	45.8	129.2	175.3	23.4	373.7
Subordinated liabilities	3.7	10.4	56.4	254.2	324.7
Subscribed capital	1.6	1.6	12.9	22.5	38.6
	7,546.1	2,779.7	1,924.2	492.5	12,742.5

33. Financial instruments (continued)

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: interest rate risk, currency risk and other price risk. These risks are measured and managed at a Group level.

Interest rate risk

The main market risk faced by the Group is 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.

The net interest income and market value of the Group is exposed to movements in interest rates. This exposure is managed on a continuous basis, within limits set by the Board, using financial instruments.

The Group uses a number of different metrics to monitor interest rate risk and details of these are set out below.

The primary interest rate risk metrics employed by the Group incorporate earnings-at-risk, market value and value-at-risk methodologies, which calculate interest rate risk exposure positions based on 250 historical data observations going back over approximately the last seven years. Monthly observation periods are used (3 observations per month, 10th to 10th; 20th to 20th and month end to month end), with equal weight being applied to all observations. All of these approaches employ 95% confidence intervals and are multi-currency. These advanced interest rate risk measurement exposures, which are compared to Board and Operational limits weekly and formally reported to ALCO and the Board monthly, are used to guide interest rate risk management decisions.

Although these measures provide valuable insights to the market risk to which the Group is exposed, they need to be viewed in the context of the limitations that:

- historical data is not necessarily a good guide to future events;
- the use of 95% confidence levels, by definition, does not take account of changes that may occur beyond this level of confidence and therefore may not fully take into account extreme events; and
- exposures are calculated on static Statement of Financial Position positions and therefore future changes in the structure of the Statement of Financial Position are ignored.

In addition, the Group also monitors interest rate risk exposure against limits by determining the effect on the Group's current net notional value of assets and liabilities for a shift in interest rates equivalent to 2% for all maturities.

The levels of Group interest rate risk exposures through the reporting period were as follows:

	As at 31 December 2009 £m	Average 2009 £m	High 2009 £m	Low 2009 £m	As at 31 December 2008 £m
Static Earnings-at-Risk	**2.9**	**1.6**	**3.1**	**0.5**	1.5
Historical Value-at-Risk	**0.7**	**0.2**	**0.7**	**-**	0.4
Stateside Quanto Value-at-Risk	**0.6**	**0.8**	**0.9**	**0.6**	0.8
2% Parallel interest rate shift	**1.6**	**7.2**	**21.7**	**-**	6.6

Other interest rate risk exposures, such as basis risk (the risk of loss arising from changes in the relationship between interest rates which have similar but not identical characteristics – say LIBOR and the Bank of England Base Rate) are also monitored closely and regularly reported to ALCO.

33. Financial instruments (continued)

Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

Both at the year-end and during the year, the Group had no material direct exposure to foreign currency exchange fluctuations, with the exception of the Group's equity investments in Jade Software Corporation Limited and Northwest Investments NZ Limited which are denominated in New Zealand dollars. The foreign currency fluctuations in relation to the Group's equity investments are not material and are not hedged, and are recognised in the Group's translation reserve.

The Group has a small exposure to foreign currency interest rates at the year-end arising from a hedging mismatch on a Sterling mortgage product whose rate is linked to US Dollar interest rates. In addition, the Group has Euro debt issuances, however due to the effect of cross currency swaps the net exposure is immaterial.

Other price risk

As at 31 December 2009, the Group had a small amount of issued equity savings products outstanding. Derivative contracts to eliminate this exposure are taken out by the Group which exactly match the terms of the savings products and the market risk on such contracts is therefore fully hedged. The book and fair values of equity swaps are shown in note 14.

Credit risk

This is the risk that a customer or counterparty is unable to honour their obligations to us as they fall due. The Group faces this risk in respect of:

- individual customers (retail mortgages);
- businesses (through historical commercial lending). The Society ceased new commercial lending in November 2008 when we concluded that the outlook for commercial property was poor; and
- other financial institutions (wholesale lending).

Credit risk within our retail and existing commercial mortgage portfolios is driven by general UK economic pressures, including rising unemployment, deterioration in household finances and further contraction in the UK housing market leading to falling property values. A reversal of the economic recovery and the return of falls in house prices will affect the level of impairment losses.

In our residential mortgage business we monitor closely applicant quality, affordability and LTV multiples. The credit decision is always managed separately from the sales force originating the business. Retail mortgage credit risks are managed within credit policies and limits set by the Group Retail Credit Committee and loans which show signs of adverse performance are managed by specialist teams who manage the collections and recovery process.

Credit risk within our treasury portfolio assets arises from the investments held by the Group in order to meet liquidity requirements and for general business purposes. The wholesale credit markets remain volatile and dislocated and a further deterioration could lead to additional fair value adjustments in the Group's portfolio of AFS assets coupled with further impairment of our treasury investments portfolio. This element of credit risk is managed by the Treasury team within strict limits set by ALCO and regular review of credit policies and performance.

The most significant credit risk which the Group is exposed to is in relation to Loans and advances to customers (note 15), Debt securities (note 13), Loans and advances to credit institutions (note 12) and Derivative financial instruments (note 14). The maximum exposure to credit risk is represented by the carrying amount of each financial asset, except for loans and advances to customers where a fair value adjustment for hedged risk of £185.3m (2008: £187.3m) is included.

33. Financial instruments (continued)

Credit risk - Loans and advances to customers

The table below shows the mix of the Group's loans and advances to customers.

Loans and advances to customers	**Group**			
	2009		2008	
	£m	**%**	£m	%
Total residential mortgages	**10,112.0**	**94.4**	8,815.7	93.6
Commercial loans	**523.9**	**4.9**	527.8	5.6
Other lending:				
Debt factoring loans	**32.7**	**0.3**	30.8	0.3
Other loans	**44.5**	**0.4**	50.2	0.5
Gross balances	**10,713.1**	**100.0**	9,424.5	100.0
Impairment provisions	**(85.1)**		(44.1)	
Fair value adjustment	**185.3**		187.3	
	10,813.3		9,567.7	

a) Residential mortgages

The majority of loans and advances to customers are secured on UK residential properties with no particular geographic concentrations. By their nature, our residential lending books are comprised of a large number of smaller loans, and historically have a low volatility of credit risk outcomes.

The Group's portfolio of loans fully secured on residential property includes the specialist mortgage lending in Amber Homeloans and North Yorkshire Mortgages. Amber Homeloans balances outstanding at the year-end were £1,330.6m (2008: £1,442.0m) of which £148.5m (2008: £161.0m) were in respect of buy-to-let. North Yorkshire Mortgages balances outstanding at the year-end were £828.9m of which £219.3m were in respect of buy-to-let.

Loan-to-value information on the Group's residential loan portfolio is set out as follows:

Indexed loan-to-value analysis	**Group**		**Society**	
	2009	2008	**2009**	2008
	%	%	**%**	%
Total book:				
<70%	**43.9**	49.2	**52.7**	55.8
70% - 80%	**12.7**	14.3	**13.9**	15.1
80% - 90%	**13.8**	14.3	**14.2**	14.1
>90%	**29.6**	22.2	**19.2**	15.0
Average indexed loan-to-value	**54.4**	49.7	**49.5**	46.3

The indexed loan-to-value is updated on a quarterly basis to reflect changes in the house price index.

33. Financial instruments (continued)

The table below provides further information on residential loans and advances by payment due status:

	Group				Society			
	2009		2008*		**2009**		2008*	
	£m	**%**	£m	%	**£m**	**%**	£m	%
Neither past due nor individually impaired	**9,502.1**	**94.0**	8,342.7	94.6	**7,410.1**	**97.9**	6,909.8	98.2
Past due but not individually impaired:								
Up to 3 months	**82.3**	**0.8**	120.7	1.4	**65.7**	**0.9**	57.3	0.8
3 to 6 months	**12.8**	**0.1**	9.0	0.1	**7.5**	**0.1**	6.0	0.1
6 to 9 months	**5.8**	**0.1**	4.9	0.1	**3.6**	**-**	2.7	-
9 to 12 months	**1.4**	**-**	1.4	-	**0.8**	**-**	0.8	-
Over 12 months	**4.9**	**-**	1.0	-	**2.4**	**-**	0.7	-
Total	**9,609.3**	**95.0**	8,479.7	96.2	**7,490.1**	**98.9**	6,977.3	99.1
Individually impaired	**463.4**	**4.6**	297.9	3.4	**75.3**	**1.0**	55.2	0.8
Possessions	**39.3**	**0.4**	38.1	0.4	**6.2**	**0.1**	5.3	0.1
	10,112.0	**100.0**	8,815.7	100.0	**7,571.6**	**100.0**	7,037.8	100.0

Loans in the analysis above which are less than one month past due have collective impairment allowances set aside to cover credit losses on loans which are in the early stages of arrears. For details refer to note 16.

Loans are classed as renegotiated when their terms have changed during the year. Those renegotiated loans that would have been past due or impaired had their terms not been renegotiated are as follows:

	2009	2008
	£m	£m
Society	**34.7**	14.1
Amber Homeloans	**43.8**	8.2
North Yorkshire Mortgages	**10.2**	-
Skipton International	**5.6**	4.8
	94.3	27.1

Fair value of collateral held:	Group		Society	
	2009	2008*	**2009**	2008*
	£m	£m	**£m**	£m
Not individually impaired	**18,098.9**	17,379.8	**15,210.0**	14,824.2
Impaired	**465.7**	321.7	**84.0**	64.9
Possessions	**36.2**	39.9	**5.6**	6.8
	18,600.8	17,741.4	**15,299.6**	14,895.9

*Prior year comparatives have been re-presented.

The collateral held predominately consists of residential houses. The use of such collateral is in line with terms that are usual and customary to standard lending activities.

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated by reference to market price or indices of similar assets.

33. Financial instruments (continued)

b) Commercial loans

Loans secured on commercial property are well diversified by industry type and an analysis is provided below:

	Group and Society			
	2009		2008	
	£m	%	£m	%
Leisure and hotel	**51.3**	**9.8**	53.5	10.1
Retail	**18.0**	**3.4**	19.8	3.8
Nursing / residential homes	**35.0**	**6.7**	42.3	8.0
Offices	**16.4**	**3.1**	17.4	3.3
Commercial investment and industrial units	**373.9**	**71.4**	372.0	70.5
Miscellaneous	**29.3**	**5.6**	22.8	4.3
	523.9	**100.0**	527.8	100.0

The table below provides further information on commercial loans and advances by payment due status:

	Group and Society			
	2009		2008	
	£m	%	£m	%
Neither past due nor individually impaired	**504.9**	**96.4**	511.5	96.9
Past due but not individually impaired:				
Up to 3 months	**11.6**	**2.2**	10.6	2.0
3 to 6 months	**0.4**	**0.1**	1.8	0.4
6 to 9 months	**0.2**	**-**	0.1	-
9 to 12 months	**-**	**-**	0.1	-
Over 12 months	**0.2**	**-**	-	-
Total	**517.3**	**98.7**	524.1	99.3
Individually impaired	**6.6**	**1.3**	3.7	0.7
	523.9	**100.0**	527.8	100.0

Loans in the analysis above which are less than three months past due have collective impairment allowances set aside to cover credit losses on loans which are in the early stages of arrears.

£11.1m (2008: £3.5m) of loans would be past due or impaired had their terms not been renegotiated.

Fair value of collateral held:	Group and Society	
	2009	2008
	£m	£m
Not individually impaired	**890.9**	883.5
Individually Impaired	**5.6**	4.1
	896.5	887.6

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

33. Financial instruments (continued)

c) Other lending

	Group				Society			
	2009		2008		**2009**		2008	
	Gross £m	**Impairment £m**	Gross £m	Impairment £m	**Gross £m**	**Impairment £m**	Gross £m	Impairment £m
Factored debt and invoice discounting	**32.7**	**(0.4)**	30.8	(0.4)	**-**	**-**	-	-
Other loans	**44.5**	**(2.5)**	50.2	(1.3)	**26.1**	**(2.5)**	28.6	(1.4)
	77.2	**(2.9)**	81.0	(1.7)	**26.1**	**(2.5)**	28.6	(1.4)

The majority of these loans have an original maturity of less than one year. There are no loans which are past due.

The balances of those assets within our factored debt and invoice discounting business which are deemed to be individually impaired amount to £0.6m (2008: £0.7m). The factors considered in determining whether these assets are impaired include the existence of objective evidence to doubt the ultimate recoverability of the company's net exposure, due to client insolvency.

The balances of those assets within other loans which are deemed to be individually impaired amount to £2.6m (2008: £2.7m) in both Group and Society. The factors considered in determining whether these assets are impaired include the existence of objective evidence that the customer is unable to honour their obligations as they fall due.

The loans in the 'Other lending' category are predominantly secured by way of a floating charge over book debts or other securities.

Credit risk – debt securities, loans and advances to credit institutions and derivative financial instruments

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

As at 31 December 2009 £6.7m (2008: £14.7m) of the Group's treasury portfolio exposure was either past due or impaired. There are no assets that would otherwise be past due or impaired whose terms have been renegotiated. In assessing the potential impairment of its treasury assets, the Group, among other factors, considers objective evidence of deterioration in the financial health of the investee, the normal volatility in valuation, and industry and sectorial performance.

As at 31 December 2009, 98% of the Group's treasury investment assets are rated single A or better. The Group policy is that initial investments in treasury assets must be investment grade or above. The Group continues to have no exposure to emerging markets and only limited exposure to non-investment grade debt.

The table below provides further details of the ratings of the Group's treasury investment portfolio:

Rating	**2009**		2008	
	£m	**%**	£m	%
Aaa	**2,277.1**	**56.1**	843.8	26.5
Aa1	**205.9**	**5.1**	766.3	24.1
Aa2	**276.4**	**6.8**	461.0	14.5
Aa3	**881.0**	**21.7**	453.3	14.3
A1	**188.1**	**4.6**	180.0	5.7
A2	**93.0**	**2.3**	270.0	8.5
A3	**54.3**	**1.3**	102.7	3.2
Baa1	**37.5**	**0.9**	19.0	0.6
Baa2	**6.7**	**0.2**	25.5	0.8
Baa3	**3.5**	**0.1**	-	-
Ba3	**3.5**	**0.1**	-	-
Caa2	**3.9**	**0.1**	-	-
Unrated:				
Building societies	**17.6**	**0.4**	53.0	1.7
Local authorities	**10.4**	**0.3**	3.7	0.1
	4,058.9	**100.0**	3,178.3	100.0

33. Financial instruments (continued)

The Group also monitors exposure concentrations against a variety of criteria including industry sector / asset class and country of risk.

Industry sector / asset class	**2009**		2008	
	£m	**%**	£m	%
Cash in hand and balances with the Bank of England	**1,272.1**	**31.3**	359.4	11.3
Cash with banks and building societies	**437.4**	**10.8**	1,064.4	33.5
Gilts	**152.7**	**3.8**	111.0	3.5
Certificates of deposit	**903.6**	**22.3**	946.5	29.8
Local authority investments	**10.4**	**0.3**	3.7	0.1
Fixed rate bonds	**283.8**	**7.0**	1.7	0.1
Floating rate notes	**684.8**	**16.9**	390.0	12.3
Residential mortgage backed securities	**255.9**	**6.3**	243.0	7.6
Commercial mortgage backed securities	**58.2**	**1.3**	58.6	1.8
	4,058.9	**100.0**	3,178.3	100.0

The Group does not hold any mortgage backed securities with US institutions as collateral.

Geographical exposure	**2009**		2008	
	£m	**%**	£m	%
UK	**3,032.6**	**74.7**	1,724.5	54.3
Rest of Europe	**765.5**	**18.9**	1,043.4	32.8
North America	**129.8**	**3.2**	106.3	3.3
Australasia	**96.2**	**2.4**	214.1	6.7
Far East	**34.8**	**0.8**	90.0	2.9
	4,058.9	**100.0**	3,178.3	100.0

Collateral held for treasury assets is determined by the nature of the instrument. Loans and debt securities are generally unsecured with the exception of asset backed securities which are secured by pools of financial assets. The International Swaps and Derivatives Association ('ISDA') Master Agreement is the Group's preferred agreement for documenting derivative activity. In addition a Credit Support Annex ('CSA') has been executed with certain counterparties in conjunction with the ISDA Master Agreement. Under a CSA, collateral is passed between parties to mitigate the market contingent counterparty risk inherent in outstanding derivative positions. The posting of collateral is also used to reduce the credit exposure arising on sale and repurchase transactions and guaranteed equity bonds.

Netting arrangements do not generally result in an offset of Statement of Financial Position assets and liabilities, as transactions are usually settled on a gross basis. The Group's legal documentation for derivative transactions does grant legal rights of set-off for those transactions. Accordingly the credit risk associated with such contracts is reduced to the extent that negative mark to market valuations on derivatives will offset positive mark-to-market values on derivatives, subject to an absolute exposure of zero.

Fair values of financial instruments

The tables below are a comparison of the book and fair values of the Group and Society's financial instruments by category as 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 for options by using option-pricing models and for other financial instruments by discounting cash flows at prevailing interest rates.

33. Financial instruments (continued)

Group	2009				
	Positive book value £m	Positive fair value £m	Negative book value £m	Negative fair value £m	Notional value / principal £m
Cash and cash equivalents	1,272.1	1,272.1	-	-	1,272.1
Debt securities	2,339.3	2,308.8	-	-	2,365.5
Loans and advances to customers	10,813.3	10,986.3	-	-	11,590.6
Loans and advances to credit institutions	447.5	447.5	-	-	308.7
Trade receivables	61.2	61.2	-	-	61.2
Shares	-	-	(10,470.2)	(10,461.5)	10,342.2
Amounts owed to credit institutions	-	-	(942.2)	(942.2)	601.2
Amounts owed to other customers	-	-	(1,203.9)	(1,082.1)	1,199.1
Debt securities in issue	-	-	(1,405.6)	(1,299.5)	1,303.2
Subordinated liabilities and subscribed capital	-	-	(296.6)	(247.2)	300.0
Trade payables	-	-	(7.0)	(7.0)	7.0
Derivatives designated as fair value hedges	234.4	234.4	(166.8)	(166.8)	5,820.1
Derivatives designated as cash flow hedges	2.5	2.5	(25.3)	(25.3)	1,424.1
Other derivatives and embedded derivatives	28.6	28.6	(71.6)	(71.6)	3,489.6
	15,198.9	**15,341.4**	**(14,589.2)**	**(14,303.2)**	

Group	2008				
	Positive book value £m	Positive fair value £m	Negative book value £m	Negative fair value £m	Notional value / principal £m
Cash and cash equivalents	359.4	359.4	-	-	359.4
Debt securities	1,734.6	1,721.4	-	-	1,757.7
Loans and advances to customers	9,567.7	9,509.5	-	-	9,361.7
Loans and advances to credit institutions	1,084.3	1,084.3	-	-	1,079.4
Trade receivables	65.0	65.0	-	-	65.0
Shares	-	-	(8,158.2)	(8,119.9)	7,925.5
Amounts owed to credit institutions	-	-	(690.0)	(690.0)	686.9
Amounts owed to other customers	-	-	(2,012.8)	(1,916.7)	1,994.5
Debt securities in issue	-	-	(1,375.0)	(1,227.5)	1,224.7
Subordinated liabilities and subscribed capital	-	-	(210.0)	(209.9)	205.0
Trade payables	-	-	(7.4)	(7.4)	7.4
Derivatives designated as fair value hedges	357.1	357.1	(187.0)	(187.0)	4,583.5
Derivatives designated as cash flow hedges	5.5	5.5	(33.6)	(33.6)	717.8
Other derivatives and embedded derivatives	67.3	67.3	(59.7)	(59.7)	5,011.4
	13,240.9	13,169.5	(12,733.7)	(12,451.7)	

33. Financial instruments (continued)

Society	2009				
	Positive book value £m	Positive fair value £m	Negative book value £m	Negative fair value £m	Notional value / principal £m
Cash and cash equivalents	1,272.0	1,272.0	-	-	1,272.0
Debt securities	2,273.6	2,243.1	-	-	2,298.5
Loans and advances to customers	8,273.1	8,470.5	-	-	8,273.1
Loans and advances to credit institutions	309.1	309.1	-	-	308.5
Trade receivables	0.5	0.5	-	-	0.5
Shares	-	-	(10,470.2)	(10,461.5)	10,342.2
Amounts owed to credit institutions	-	-	(1,371.5)	(1,371.5)	1,370.1
Amounts owed to other customers	-	-	(1,339.9)	(1,220.7)	1,335.1
Debt securities in issue	-	-	(1,405.6)	(1,299.5)	1,303.2
Subordinated liabilities and subscribed capital	-	-	(307.9)	(258.5)	312.5
Trade payables	-	-	(0.3)	(0.3)	0.3
Derivatives designated as fair value hedges	233.9	233.9	(154.6)	(154.6)	6,216.8
Derivatives designated as cash flow hedges	2.0	2.0	(25.3)	(25.3)	1,442.3
Other derivatives and embedded derivatives	79.5	79.5	(71.2)	(71.2)	3,519.4
	12,443.7	**12,610.6**	**(15,146.5)**	**(14,863.1)**	

Society	2008				
	Positive book value £m	Positive fair value £m	Negative book value £m	Negative fair value £m	Notional value / principal £m
Cash and cash equivalents	359.4	359.4	-	-	359.4
Debt securities	1,734.6	1,721.4	-	-	1,757.7
Loans and advances to customers	7,740.6	7,712.5	-	-	7,590.5
Loans and advances to credit institutions	1,041.5	1,041.5	-	-	1,036.6
Shares	-	-	(8,158.2)	(8,119.9)	7,963.8
Amounts owed to credit institutions	-	-	(822.4)	(822.4)	817.4
Amounts owed to other customers	-	-	(2,622.6)	(2,522.9)	2,589.1
Debt securities in issue	-	-	(1,375.0)	(1,227.5)	1,224.7
Subordinated liabilities and subscribed capital	-	-	(210.0)	(209.9)	205.0
Trade payables	-	-	(0.4)	(0.4)	0.4
Derivatives designated as fair value hedges	357.1	357.1	(154.2)	(154.2)	5,542.3
Derivatives designated as cash flow hedges	5.5	5.5	(33.6)	(33.6)	717.8
Other derivatives and embedded derivatives	137.8	137.8	(59.5)	(59.5)	5,961.1
	11,376.5	11,335.2	(13,435.9)	(13,150.3)	

The fair value of mortgages has been determined at a unit of account level of the individual mortgage and is based on the present value of future cash flows. These cash flows represent the best estimate of future interest flows adjusted for credit risk. However, were the Society to dispose of portfolio mortgages, it is likely that the fair value would be lower than that shown above, as there is currently no market for the sale of mortgage books.

33. Financial instruments (continued)

The table below summarises the Group's main financial instruments by financial asset type.

	2009			
	Amortised cost £m	**Held at fair value as available-for-sale assets £m**	**Fair value through profit or loss £m**	**Total £m**
Cash and cash equivalents	1,272.1	-	-	1,272.1
Trade receivables	61.2	-	-	61.2
Loans and advances to credit institutions	447.5	-	-	447.5
Loans and advances to customers	10,813.3	-	-	10,813.3
Debt securities	314.1	2,025.2	-	2,339.3
Derivative financial instruments	-	-	265.5	265.5
Shares	(10,470.2)	-	-	(10,470.2)
Amounts owed to credit institutions and other customers	(2,146.1)	-	-	(2,146.1)
Trade payables	(7.0)	-	-	(7.0)
Debt securities in issue	(1,405.6)	-	-	(1,405.6)
Subordinated liabilities	(213.0)	-	-	(213.0)
Derivative financial instruments	-	-	(263.7)	(263.7)
	(1,333.7)	**2,025.2**	**1.8**	

	2008			
	Amortised cost £m	Held at fair value as available-for-sale assets £m	Fair value through profit or loss £m	Total £m
Cash and cash equivalents	359.4	-	-	359.4
Trade receivables	65.0	-	-	65.0
Loans and advances to credit institutions	1,084.3	-	-	1,084.3
Loans and advances to customers	9,567.7	-	-	9,567.7
Debt securities	303.4	1,431.2	-	1,734.6
Derivative financial instruments	-	-	429.9	429.9
Shares	(8,158.2)	-	-	(8,158.2)
Amounts owed to credit institutions and other customers	(2,702.8)	-	-	(2,702.8)
Trade payables	(7.4)	-	-	(7.4)
Debt securities in issue	(1,375.0)	-	-	(1,375.0)
Subordinated liabilities	(183.7)	-	-	(183.7)
Derivative financial instruments	-	-	(280.3)	(280.3)
	(1,047.3)	1,431.2	149.6	

33. Financial instruments (continued)

The table below summarises the Society's main financial instruments by financial asset type.

	2009			
	Amortised cost £m	**Held at fair value as available-for-sale assets £m**	**Fair value through profit or loss £m**	**Total £m**
Cash and cash equivalents	1,272.0	-	-	1,272.0
Trade receivables	0.5	-	-	0.5
Loans and advances to credit institutions	309.1	-	-	309.1
Loans and advances to customers	8,273.1	-	-	8,273.1
Debt securities	314.1	1,959.5	-	2,273.6
Derivative financial instruments	-	-	315.4	315.4
Shares	(10,470.2)	-	-	(10,470.2)
Amounts owed to credit institutions and other customers	(1,718.5)	-	(992.9)	(2,711.4)
Trade payables	(0.3)	-	-	(0.3)
Debt securities in issue	(1,405.6)	-	-	(1,405.6)
Subordinated liabilities	(224.3)	-	-	(224.3)
Derivative financial instruments	-	-	(251.1)	(251.1)
	(3,650.1)	**1,959.5**	**(928.6)**	

	2008			
	Amortised cost £m	Held at fair value as available-for-sale assets £m	Fair value through profit or loss £m	Total £m
Cash and cash equivalents	359.4	-	-	359.4
Trade receivables	-	-	-	-
Loans and advances to credit institutions	1,041.5	-	-	1,041.5
Loans and advances to customers	7,740.6	-	-	7,740.6
Debt securities	303.4	1,431.2	-	1,734.6
Derivative financial instruments	-	-	500.4	500.4
Shares	(8,158.2)	-	-	(8,158.2)
Amounts owed to credit institutions and other customers	(2,476.1)	-	(968.9)	(3,445.0)
Trade payables	(0.4)	-	-	(0.4)
Debt securities in issue	(1,375.0)	-	-	(1,375.0)
Subordinated liabilities	(183.7)	-	-	(183.7)
Derivative financial instruments	-	-	(247.3)	(247.3)
	(2,748.5)	1,431.2	(715.8)	

33. Financial instruments (continued)

The tables below summarise the fair value measurement basis used for assets and liabilities held at fair value.

Group

	2009			
	Quoted prices in active markets (Level 1) £m	Valuation techniques using observable inputs (Level 2) £m	Valuation techniques using significant unobservable inputs (Level 3) £m	Total £m
Financial assets				
Financial assets held at fair value as available-for-sale:				
Debt securities	1,121.6	903.6	-	2,025.2
Financial assets at fair value through profit and loss:				
Derivative financial instruments	-	265.5	-	265.5
	1,121.6	1,169.1	-	2,290.7
Financial liabilities				
Financial liabilities at fair value through profit and loss:				
Derivative financial instruments	-	263.7	-	263.7
	-	263.7	-	263.7

Society

	2009			
	Quoted prices in active markets (Level 1) £m	Valuation techniques using observable inputs (Level 2) £m	Valuation techniques using significant unobservable inputs (Level 3) £m	Total £m
Financial assets				
Financial assets held at fair value as available-for-sale:				
Debt securities	1,055.9	903.6	-	1,959.5
Financial assets at fair value through profit and loss:				
Derivative financial instruments	-	315.4	-	315.4
	1,055.9	1,219.0	-	2,274.9
Financial liabilities				
Financial liabilities at fair value through profit and loss:				
Derivative financial instruments	-	251.1	-	251.1
Amounts owed to credit institutions and other customers	-	992.9	-	992.9
	-	1,244.0	-	1,244.0

33. Financial instruments (continued)

Valuation techniques

Fair values are determined using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1

The most reliable fair values of derivative financial instruments and available-for-sale assets are quoted market prices in an actively traded market.

Level 2

These are valuation techniques for which all significant inputs are taken from observable market data. These include valuation models used to calculate the present value of expected future cash flows and may be employed either when no active market exists or when there are quoted prices available for similar instruments in active markets.

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

Level 3

These are valuation techniques for which any one or more significant input is not based on observable market data.

Valuation techniques include net present value and discounted cashflow models, comparison to similar instruments for which market observable prices exist, Black-Scholes and other valuation models. Assumptions and market observable inputs used in valuation techniques include risk-free and benchmark interest rates, foreign currency exchange 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.

34. Group segmental reporting

	2009								
	Mortgages and Savings £m	Mortgage Services £m	Estate Agency £m	Financial Advice £m	Investment Portfolio £m	Inter-company adjustments £m	Continuing operations £m	Discontinued operation £m	Total £m
Income									
Interest receivable and similar income	550.6	0.2	1.1	0.2	2.4	(132.7)	421.8	-	421.8
Interest payable and similar charges	(498.1)	-	(0.2)	(0.3)	(2.8)	132.9	(368.5)	(0.3)	(368.8)
Fair value losses on financial instruments	3.9	-	-	-	-	-	3.9	-	3.9
Fees and commissions receivable	13.1	84.2	214.8	43.1	44.1	(10.3)	389.0	48.7	437.7
Fees and commissions payable	(2.6)	-	(2.2)	(5.4)	(13.9)	4.7	(19.4)	-	(19.4)
Profit on disposal of subsidiary undertakings	-	-	-	-	-	-	-	39.7	39.7
Share of profits from joint ventures	-	-	0.2	-	-	-	0.2	-	0.2
Profit on disposal of associate	-	-	-	-	-	-	-	-	-
Other income	7.6	2.2	0.4	0.1	8.6	(5.9)	13.0	-	13.0
Total income	74.5	86.6	214.1	37.7	38.4	(11.3)	440.0	88.1	528.1
Employee and pension costs	29.3	50.1	100.2	25.4	25.6	-	230.6	22.6	253.2
Depreciation and amortisation	4.6	5.4	4.2	1.3	3.8	-	19.3	4.0	23.3
Impairment losses / provisions for liabilities	37.6	-	0.2	-	0.5	-	38.3	-	38.3
Other admin expenses	36.3	27.8	55.4	9.9	25.2	(20.8)	133.8	16.0	149.8
Total expenses	107.8	83.3	160.0	36.6	55.1	(20.8)	422.0	42.6	464.6
Profit before tax	(33.3)	3.3	54.1	1.1	(16.7)	9.5	18.0	45.5	63.5
Taxation	12.3	(1.3)	(15.8)	(0.5)	1.0	-	(4.3)	(1.6)	(5.9)
Profit after tax	(21.0)	2.0	38.3	0.6	(15.7)	9.5	13.7	43.9	57.6
Total assets	18,588.4	33.1	139.1	25.2	253.8	(3,470.8)	15,568.8	-	15,568.8
Total liabilities	17,828.4	9.7	58.6	1.1	154.9	(3,250.3)	14,802.4	-	14,802.4
Capital expenditure	18.9	6.1	1.6	1.1	4.0	-	31.7	3.9	35.6

34. Group segmental reporting (continued)

Performance by segment is reported to the chief operating decision maker based on the Group's interpretation of items which are routine and non-routine as follows:

2009	Mortgages and Savings £m	Mortgage Services £m	Estate Agency £m	Financial Advice £m	Investment Portfolio £m	Inter-company adjustments £m	Continuing operations £m	Discontinued operation £m	Total £m
Reported profit before tax	(33.3)	3.3	54.1	1.1	(16.7)	9.5	18.0	45.5	63.5
Non-routine items:									
Profit on sale of subsidiary companies	-	-	-	-	-	-	-	(39.7)	(39.7)
Financial Services Compensation Scheme Levy	(4.3)	-	-	-	-	-	(4.3)	-	(4.3)
Recovery of investment securities	(1.3)	-	-	-	-	-	(1.3)	-	(1.3)
Curtailment gain on closure of pension schemes	(10.4)	-	-	-	-	-	(10.4)	-	(10.4)
Provisions against loans and investment in subsidiary undertakings	5.3	0.5	-	-	12.5	(18.3)	-	-	-
Impairment of goodwill	-	-	-	0.8	1.3	9.9	12.0	-	12.0
Net losses from fair value volatility	(3.9)	-	-	-	-	-	(3.9)	-	(3.9)
Merger expenses	3.9	0.9	-	-	-	-	4.8	-	4.8
Profit before tax after adjusting for non-routine items	(44.0)	4.7	54.1	1.9	(2.9)	1.1	14.9	5.8	20.7

Total income can be analysed as follows:

2009	Mortgages and Savings £m	Mortgage Services £m	Estate Agency £m	Financial Advice £m	Investment Portfolio £m	Inter-company adjustments £m	Continuing operations £m	Discontinued operation £m	Total £m
Income from other segments	7.0	5.5	1.5	(2.1)	1.9	(13.8)	-	-	-
External income	67.5	81.1	212.6	39.8	36.5	2.5	440.0	88.1	528.1
Total income	74.5	86.6	214.1	37.7	38.4	(11.3)	440.0	88.1	528.1

34. Group segmental reporting (continued)

2008	Mortgages and Savings £m	Mortgage Services £m	Estate Agency £m	Financial Advice £m	Investment Portfolio £m	Inter-company adjustments £m	Continuing operations £m	Discontinued operation £m	Total £m
Income									
Interest receivable and similar income	891.2	0.3	1.9	0.9	6.9	(129.8)	771.4	-	771.4
Interest payable and similar charges	(801.9)	(0.2)	(1.3)	(0.5)	(10.3)	130.3	(683.9)	(1.5)	(685.4)
Fair value losses on financial instruments	(3.3)	-	-	-	-	-	(3.3)	-	(3.3)
Fees and commissions receivable	14.6	85.9	178.0	40.4	59.0	(6.3)	371.6	49.3	420.9
Fees and commissions payable	(2.1)	-	(1.6)	(5.3)	(21.1)	3.1	(27.0)	-	(27.0)
Profit on disposal of subsidiary undertakings	-	-	-	-	9.1	-	9.1	-	9.1
Share of profits from joint ventures	-	-	3.9	-	-	-	3.9	-	3.9
Profit on disposal of associate	-	-	22.3	-	-	-	22.3	-	22.3
Other income	3.3	2.8	1.7	-	11.9	(9.3)	10.4	0.1	10.5
Total income	101.8	88.8	204.9	35.5	55.5	(12.0)	474.5	47.9	522.4
Employee and pension costs	38.3	47.3	96.4	25.0	27.2	-	234.2	21.4	255.6
Depreciation and amortisation	3.2	5.3	5.0	1.9	3.6	(0.1)	18.9	3.9	22.8
Impairment losses / provisions for liabilities	61.0	-	5.5	-	0.4	-	66.9	-	66.9
Other admin expenses	27.5	27.9	61.8	9.6	19.6	(9.8)	136.6	18.0	154.6
Total expenses	130.0	80.5	168.7	36.5	50.8	(9.9)	456.6	43.3	499.9
Profit before tax	(28.2)	8.3	36.2	(1.0)	4.7	(2.1)	17.9	4.6	22.5
Taxation	7.1	(2.5)	(3.2)	0.3	1.1	-	2.8	(1.5)	1.3
Profit after tax	(21.1)	5.8	33.0	(0.7)	5.8	(2.1)	20.7	3.1	23.8
Total assets	15,913.7	30.4	154.7	25.9	299.9	(2,840.1)	13,584.5	62.5	13,647.0
Total liabilities	15,264.7	5.4	71.1	1.9	211.4	(2,649.6)	12,904.9	34.6	12,939.5
Capital expenditure	9.4	5.1	3.4	1.9	3.2	-	23.0	5.4	28.4

34. Group segmental reporting (continued)

Performance by segment is reported to the chief operating decision maker based on the Group's interpretation of items which are routine and non-routine as follows:

2008	Mortgages and Savings £m	Mortgage Services £m	Estate Agency £m	Financial Advice £m	Investment Portfolio £m	Inter-company adjustments £m	Continuing operations £m	Discontinued operation £m	Total £m
Reported profit before tax	(28.2)	8.3	36.2	(1.0)	4.7	(2.1)	17.9	4.6	22.5
Non-routine items:									
Profit on sale of subsidiary companies	-	-	-	-	(9. 1)	-	(9.1)	-	(9.1)
Profit on sale of investment in associate	-	-	(22.3)	-	-	-	(22.3)	-	(22.3)
Financial Services Compensation Scheme Levy	16.3	-	-	-	-	-	16.3	-	16.3
Impairment of investment securities	11.5	-	-	-	-	-	11.5	-	11.5
Curtailment gain on closure of pension schemes	-	-	(6.3)	-	-	-	(6.3)	-	(6.3)
Impairment of goodwill	-	-	2.8	-	3.0	-	5.8	0.1	5.9
Net losses from fair value volatility	3.3	-	-	-	-	-	3.3	-	3.3
Merger expenses	0.7	-	-	-	-	-	0.7	-	0.7
Profit before tax after adjusting for non-routine items	3.6	8.3	10.4	(1.0)	(1.4)	(2.1)	17.8	4.7	22.5

Total income can be analysed as follows:

2008	Mortgages and Savings £m	Mortgage Services £m	Estate Agency £m	Financial Advice £m	Investment Portfolio £m	Inter-company adjustments £m	Continuing operations £m	Discontinued operation £m	Total £m
Income from other segments	13.5	4.6	1.3	(2.1)	(3.6)	(12.7)	1.0	(1.0)	-
External income	88.3	84.2	203.6	37.6	59.1	0.7	473.5	48.9	522.4
Total income	101.8	88.8	204.9	35.5	55.5	(12.0)	474.5	47.9	522.4

34. Group segmental reporting (continued)

The Group's operating results are regularly reviewed by the chief operating decision maker in the following reportable segments. Each segment offers different products and services and is managed separately based on the Group's management and internal reporting structure.

- Mortgages and Savings – principally the Society, but also includes specialist mortgage businesses Amber Homeloans and North Yorkshire Mortgages, and deposit taking and lending in Jersey and Guernsey through Skipton International.
- Mortgage Services – mortgage administration services, principally Homeloan Management, also includes Specialist Mortgage Services and Baseline Capital.
- Estate Agency – including survey and valuations, conveyancing, lettings, asset management and mortgage broking carried out through Connells.
- Financial Advice – provision of financial advice and broking services through five separate financial advice companies.
- Credit & Marketing Solutions – provision of credit reference agency and database services by Callcredit Information Group, which became a discontinued operation from 7 December 2009 on disposal.
- Investment Portfolio – includes holding companies and a number of other small trading companies that do not fall within the core operating segments.

These segments reflect how internal reporting is provided to management and how management allocate resources and assess performance.

Transactions between the segments are on normal commercial terms and conditions. The accounting policies of the reportable segments are consistent with the Group's accounting policies.

No geographical analysis is presented because substantially all of the Group's activities are conducted within the UK. Of the total external income, £11.9m (2008: £9.2m) was generated outside of the UK.

Following a review of the segments in which the Group operated, each segment was renamed in 2009, however, whilst the segment headings have been renamed, the actual segments themselves are the same as those reported under IAS 14.

A more detailed breakdown of the allocation of goodwill to each segmental area is given within note 18.

35. Pensions

Defined contribution schemes

The amount charged to the Income Statement in respect of contributions to the Group's defined contribution and stakeholder pension arrangements is the contribution payable in the year. The total pension cost charged to the Income Statement amounted to Group: £6.5m (2008: £5.8m) and Society: £2.0m (2008: £1.7m).

Defined benefit schemes

The Group has five funded defined benefit arrangements, all of which are now closed to new members:

- The Skipton Building Society Pension & Life Assurance Scheme ('the Skipton Scheme')
- The Connells Limited Pension & Life Assurance Scheme ('the Connells Scheme')
- The Sequence (UK) Limited (1997) Pension & Life Assurance Scheme ('the Sequence 1997 Scheme')
- The Sequence (UK) Limited (South) Staff Pension Scheme ('the Sequence Staff Scheme')
- The Scarborough Building Society Group Pension and Death Benefits Scheme ('the Scarborough Scheme'), which became part of the Skipton Group from 29 March following the merger of the Scarborough Building Society with Skipton Building Society.

The Schemes provide benefits based on final salary for employees. The Scarborough Scheme closed to future accrual of benefits on 1 May 2007, the Connells Scheme, Sequence 1997 Scheme and Sequence Staff Scheme all closed to future accrual of benefits on 1 January 2009, and the Skipton Scheme closed to future accrual of benefits on 1 January 2010, at which point all active members left pensionable service and became entitled to deferred benefits. The assets of the Schemes are held in separate trustee-administered funds.

Contributions to the Schemes are assessed in accordance with the advice of an independent qualified actuary using the projected unit method.

The Group's policy for recognising actuarial gains and losses is to recognise them immediately on the Statement of Financial Position through the Statement of Recognised Income and Expense.

The aggregate costs of the five schemes are recognised in accordance with IAS 19 (Amended). The Skipton Scheme is operated by a number of Group companies. Each of the participating entities, except for the Society, accounts on the basis of contributions paid by that company. The Society accounts for the difference between the aggregate IAS 19 (Amended) costs of the scheme and the aggregate contributions paid by the other entities.

A qualified independent actuary carried out the last full actuarial valuations of the schemes as at the following dates:

- 1 April 2008 for the Skipton Scheme.
- 30 April 2008 for the Connells Scheme.
- 5 April 2008 for the Sequence 1997 Scheme.
- 1 April 2007 for the Sequence Staff Scheme.
- 31 December 2007 for the Scarborough Scheme.

35. Pensions (continued)

The main financial assumptions used in the actuarial valuation are as follows:

	Group and Society 2009 %	Group and Society 2008 %
Inflation rate	**3.50**	3.00
Discount rate	**5.75**	6.20
Expected return on assets	**6.81-7.75**	6.90-7.37
Rate of increase in pay	**N/A***	5.00
Rate of increase of pensions in payment:		
increasing in line with LPI (Limited Price Inflation)	**3.40**	2.90
increasing in line with LPI, subject to a minimum of 3% pa	**3.80**	3.60
increasing in line with LPI, subject to a maximum of 2.5% pa	**2.40**	2.30
Rate of increase deferred pensions	**3.50**	3.00

*Note – The one exception to this is for the Scarborough Scheme, where a salary link applies in respect of accrued benefits for those members who have remained in employment since the scheme closed to future accrual on 1 May 2007. The real earnings inflation assumption adopted as at 29 March 2009 (the date of the business combination) to reflect this was 2% per annum and this assumption has been retained as at 31 December 2009.

The most significant non-financial assumption is the assumed rate of longevity. For the year-ending 31 December 2009, this has been based on mortality rates that are 105% of the PNMA00 tables for males (or PNFA00 tables for females) with an allowance for projected improvements in mortality in line with long cohort improvements. This is the same mortality assumption used as at 31 December 2008. The tables adopted assume that, when a member who is fifteen years from retirement reaches age 65, the life expectancy from age 65 is as follows:

Non-retired members	2009	2008
Males	**24.0**	24.0
Females	**26.3**	26.2

The table below shows the net pension liability which is recognised in the Statement of Financial Position:

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
Fair value of plan assets	**148.8**	115.7	**76.4**	54.2
Present value of defined benefit obligations	**(196.2)**	(153.6)	**(95.9)**	(72.3)
Total amount of surplus not recoverable	**-**	-	**-**	-
Net pension liability	**(47.4)**	(37.9)	**(19.5)**	(18.1)

As all actuarial gains and assets are recognised, the deficits shown above are those recognised in the Statement of Financial Position.

The table below sets out the reconciliation of the fair value of scheme assets for the year:

	Group 2009 £m	Group 2008 £m	Society 2009 £m	Society 2008 £m
At 1 January	**115.7**	140.2	**54.2**	63.7
Expected return on assets	**8.8**	9.9	**4.3**	4.4
Actuarial gains / (losses)	**13.6**	(37.5)	**6.8**	(16.0)
Contributions by employer	**6.0**	4.2	**4.9**	2.5
Contributions by employees	**0.5**	1.4	**0.4**	0.4
Benefits paid	**(5.4)**	(2.5)	**(3.8)**	(0.8)
Assets acquired on transfer of engagements	**9.6**	-	**9.6**	-
At 31 December	**148.8**	115.7	**76.4**	54.2

35. Pensions (continued)

The table below sets out a reconciliation of the present value of the defined benefit obligation for the year:

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
At 1 January	**153.6**	161.0	**72.3**	71.5
Current service cost	**0.8**	2.1	**0.8**	1.0
Past service costs	**-**	0.2	**-**	0.2
Curtailments	**(10.4)**	(6.3)	**(10.4)**	-
Interest cost	**10.2**	9.7	**5.2**	4.3
Contributions by employees	**0.5**	1.4	**0.4**	0.4
Actuarial gains / (losses)	**31.5**	(12.0)	**16.0**	(4.3)
Actual benefit payments	**(5.4)**	(2.5)	**(3.8)**	(0.8)
Liabilities assumed on transfer of engagements	**15.4**	-	**15.4**	-
At 31 December	**196.2**	153.6	**95.9**	72.3

The difference between the expected return and the actual return on scheme assets is recognised in the Statement of Comprehensive Income and is reconciled below:

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Actual return on assets	**22.4**	(27.6)	**11.1**	(11.6)
Expected return on assets	**(8.8)**	(9.9)	**(4.3)**	(4.4)
Actuarial (loss) / gain on assets	**13.6**	(37.5)	**6.8**	(16.0)

The expected return on assets has been derived as the weighted average of the expected returns from each of the main asset classes. The expected return for each asset class, which is provided in the next table, reflects a combination of historical performance analysis, the forward looking views of the financial markets (as suggested by the yields available), and the views of investment organisations. The table also sets out the fair value of the scheme assets by each major category.

Group	**2009**		2008	
	£m	**% pa**	£m	% pa
Equities	**96.2**	**8.25**	70.2	8.50
Property	**5.3**	**6.55**	6.2	6.80
Corporate bonds	**17.3**	**5.75**	15.0	6.20
Government bonds	**26.7**	**4.50**	22.8	3.70
Cash	**3.3**	**3.00**	1.5	2.00
	148.8	**7.11**	115.7	7.08

The actual return on the scheme assets over the year ended 31 December 2009 was estimated as 19%.

Society	**2009**		2008	
	£m	**% pa**	£m	% pa
Equities	**45.7**	**8.25**	29.7	8.50
Property	**2.8**	**6.55**	3.3	6.80
Corporate bonds	**10.2**	**5.75**	8.4	6.20
Government bonds	**15.1**	**4.50**	12.5	3.70
Cash	**2.6**	**3.00**	0.3	2.00
	76.4	**6.94**	54.2	6.90

The actual return on the scheme assets over the year ended 31 December 2009 was estimated as 16%.

35. Pensions (continued)

The service costs and curtailments for the year are recognised in 'Administrative expenses', whilst the interest cost and expected return on assets are recognised within 'Other income'. An analysis of the charge is set out below:

	Group 2009 £m	Group 2008 £m	**Society 2009 £m**	Society 2008 £m
Current service cost	**0.8**	2.1	**0.8**	1.0
Past service cost	**-**	0.2	**-**	0.2
Curtailments	**(10.4)**	(6.3)	**(10.4)**	-
Interest on liabilities	**10.2**	9.7	**5.2**	4.3
Expected return on assets	**(8.8)**	(9.9)	**(4.3)**	(4.4)
Total pension (income) / expense	**(8.2)**	(4.2)	**(8.7)**	1.1

The tables below sets out the actuarial gains and losses which have been recognised within the Statement of Comprehensive Income.

Group	**2009 £m**	2008 £m	2007 £m	2006 £m	2005 £m
Experience (losses) / gains on scheme assets	**13.6**	(37.5)	(1.3)	2.7	10.5
Experience gains / (losses) on defined benefit obligation	**(0.7)**	(1.6)	(4.4)	5.3	(2.1)
Gains / (losses) from change in assumptions	**(30.8)**	13.5	15.9	6.0	(25.2)
Total amount of surplus not recoverable	**-**	1.5	(1.5)	-	-
Total gains / (losses) recognised in Statement of Comprehensive Income during the year	**(17.9)**	(24.1)	8.7	14.0	(16.8)
Cumulative actuarial (losses) / gains recognised at end of year	**(38.4)**	(20.5)	3.6	(5.1)	(19.1)

Society	**2009 £m**	2008 £m	2007 £m	2006 £m	2005 £m
Experience (losses) / gains on scheme assets	**6.8**	(16.0)	(0.6)	1.3	4.1
Experience gains / (losses) on defined benefit obligation	**(0.1)**	(1.5)	(3.6)	5.1	(0.6)
Gains / (losses) from change in assumptions	**(16.0)**	5.8	5.4	2.7	(11.8)
Total gains / (losses) recognised in Statement of Comprehensive Income during the year	**(9.3)**	(11.7)	1.2	9.1	(8.3)
Cumulative actuarial (losses) / gains recognised at end of year	**(19.4)**	(10.1)	1.6	0.4	(8.7)

The present value of the defined benefit obligation and the fair value of the scheme assets are as follows:

Group	**2009 £m**	2008 £m	2007 £m	2006 £m	2005 £m
Fair value of plan assets	**148.8**	115.7	140.2	120.4	96.0
Present value of defined benefit obligations	**(196.2)**	(153.6)	(161.0)	(163.8)	(164.8)
Total amount of surplus not recoverable	**-**	-	(1.5)	-	-
Net pension liability	**(47.4)**	(37.9)	(22.3)	(43.4)	(68.8)

35. Pensions (continued)

Society	2009 £m	2008 £m	2007 £m	2006 £m	2005 £m
Fair value of plan assets	**76.4**	54.2	63.7	48.1	38.4
Present value of defined benefit obligations	**(95.9)**	(72.3)	(71.5)	(69.4)	(73.1)
Net pension liability	**(19.5)**	(18.1)	(7.8)	(21.3)	(34.7)

The table below sets out our best estimate, of the aggregate contributions expected to be paid to the schemes during the year ending 31 December 2010.

	Group 2010 £m	Society 2010 £m
Estimated employer contributions	**6.2**	**5.2**
Estimated employee contributions	**-**	**-**
Estimated total contributions	**6.2**	**5.2**

36. Adoption of new and revised International Financial Reporting Standards

Disclosed below are new standards and interpretations which have been adopted during the year.

- IAS 1, *Presentation of Financial Statements (2007)*. This standard replaces the current IAS 1, *Presentation of Financial Statements* and is effective from 1 January 2009. In summary, IAS 1 sets overall requirements for the presentation of financial statements, guidelines for their structure and minimum requirements for their content. This standard has impacted the presentation of the financial performance of the Group, in line with other financial institutions. However, it has not changed the recognition, measurement or disclosure of specific transactions and other events required by other IFRSs.
- IAS 23, *Borrowing Costs (Revised)*. This revised standard relates to interest costs on assets that take a substantial time to get ready for intended use or sale. The option to recognise all borrowing costs immediately as an expense is eliminated, such costs must be capitalised. All other borrowing costs should be expensed as incurred.
- Amendment to IFRS 7, *Financial Instruments: Disclosures*. The amendments to this standard were endorsed on 1 December 2009 and are effective from 1 January 2009. The amendment requires enhanced disclosures about fair value measurements and liquidity risk.
- IFRS 8, *Operating Segments*. This new standard was issued on 30 November 2006 and replaces IAS 14, *Segment Reporting*. In summary, this standard 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.

Disclosed below are the new IFRS, interpretations and amendments, which are likely to have an impact on the Group, which as at 31 December 2009 have been issued but have not yet been adopted by the Group (although early adoption is permitted):

- IAS 27, *Consolidated and Separate Financial Statements (2008)*. The changes to this standard require the effects of all transactions with non-controlling interests to be recorded in equity if there has been no change in control. The changes also specify the accounting where control of an entity is lost. The amendment will impact the accounting for the future exercises of put options by minority shareholders within our subsidiary companies.
- IFRS 3, *Business Combinations (Revised)*. The main changes in this standard in addition to the inclusion of mutual entities, are that the cost of investment will comprise the consideration paid to the vendors for equity with acquisition costs being expensed immediately; goodwill will be accounted for only upon the acquisition of a subsidiary undertaking as subsequent changes in interest will be recognised in equity and only upon the loss of control will any profit or loss be recognised in the Income Statement. Further, any pre-existing holding within the acquired entity will, where control is subsequently gained, be revalued with any profit or loss arising being credited / charged through the Income Statement.

37. Subsequent events

On 24 February 2010 the Society announced its intention to merge with Chesham Building Society. If the proposal is approved by the Chesham Building Society's members and subsequently confirmed by the FSA the merger is expected to become effective through the transfer of all of the Chesham Building Society's engagements to Skipton on 1 June 2010.

There have been no other material subsequent events between 31 December 2009 and the approval of this Report & Accounts by the Board.

38. Transfer of engagements

On 30 March 2009 the Society merged with the Scarborough Building Society ('Scarborough') under section 42B(3)(b) of the Building Societies Act on the basis of a Board resolution of Scarborough as permitted by a direction given by the Financial Services Authority.

The Board of Scarborough independently reached a conclusion that merging with Skipton was in the best interests of its members, given the current uncertain economic environment and following the identification of financial issues faced by their Society. From Skipton's perspective, the merger provided an opportunity to build on our strong position within the financial services sector by adding attractive customer franchises to our existing operations.

The assets and liabilities acquired and the associated accounting adjustments are set out below:

	Notes	Cessation accounts Audited £m	Fair value adjustments £m	**Take-on balances £m**
Assets				
Cash in hand and balances with the Bank of England		1.8	-	**1.8**
Loans and advances to credit institutions		143.4	-	**143.4**
Debt securities	e	356.5	(31.3)	**325.2**
Derivative financial instruments		29.2	-	**29.2**
Loans and advances to customers	f	2,104.4	3.8	**2,108.2**
Corporation tax asset		0.9	-	**0.9**
Deferred tax asset	g	7.4	9.6	**17.0**
Intangible assets	h	23.6	(20.4)	**3.2**
Property, plant and equipment	i	12.5	(6.5)	**6.0**
Investment property		1.1	-	**1.1**
Other assets		1.9	-	**1.9**
Total assets		2,682.7	(44.8)	**2,637.9**
Liabilities				
Shares	j	1,771.9	3.3	**1,775.2**
Amounts owed to credit institutions		51.3	-	**51.3**
Amounts owed to other customers	k	593.2	1.1	**594.3**
Debt securities in issue		42.7	-	**42.7**
Derivative financial instruments		60.7	-	**60.7**
Other liabilities		6.5	-	**6.5**
Deferred tax liability		5.1	-	**5.1**
Provisions for liabilities	l	1.5	2.0	**3.5**
Retirement benefit obligations		5.8	-	**5.8**
Subordinated liabilities	m	31.0	(1.7)	**29.3**
Subscribed capital	m	72.5	(9.0)	**63.5**
Total liabilities		2,642.2	(4.3)	**2,637.9**
Reserves		40.5	(40.5)	**-**
Total members' interests and liabilities		2,682.7	(44.8)	**2,637.9**
Goodwill				
Fair value of net assets				**-**
Purchase consideration	n			**-**
Goodwill				**-**

38. Transfer of engagements (continued)

Notes and adjustments

a. The income and expenditure account for the Scarborough for the period to 29 March 2009 is reported in the table below for information only and is not included in these financial statements.

b. The cessation accounts of the Scarborough have been prepared in accordance with International Financial Reporting Standards as endorsed by the EU. Balances have been adjusted in line with the principles of IFRS 3, *Business Combinations (Revised)* (note 1b).

c. The assets and liabilities of the Scarborough Building Society have been included within the accounts of the Skipton Building Society at fair value. Financial assets and liabilities which, following the Group's accounting policies, would be carried at amortised cost, are brought on to the balance sheet at their fair value at acquisition and are subsequently carried at amortised cost using the effective interest rate method.

d. The policies used in drawing up the cessation accounts of the Scarborough have been reclassified in line with the Skipton Group accounting policies in arriving at the fair value adjustments.

e. The debt securities fair value adjustment has been calculated by applying the latest mark-to-market valuation. The methodology used is fully consistent with that used by the Group.

f. The entry method of mortgage valuation has been used. This method considers the rates at which new lending would be made in the market by comparison to the rates applied at the origination of the mortgage book. The acquisition fair value adjustment reflects both the credit and interest rate risk associated with these assets.

g. Deferred tax has been provided where subsequent tax benefits or charges will arise from the fair value adjustments.

h. The write-down of intangible assets comprises; £14.1m write down of goodwill relating to an historical acquisition by the Scarborough; £9.1m of software intangibles were written-down. A £2.8m core deposit intangible has been recognised representing the intrinsic value of the retail savings book, that is, its fair value.

i. The fair value of property, plant and equipment has been valued down by £6.5m based on an independent valuation, assessing current market value rather than value in use.

j. The fair value adjustments for shares and deposits from banks reflect the interest rate risk associated with these liabilities. Under IFRS these liabilities were previously carried at amortised cost.

k. The £1.1m write-off relates to an historical core deposit intangible.

l. The fair value adjustment within provisions for liabilities includes £1.2m for the FSCS charge relating to the Scarborough savings balances transferred to the Group. In addition, a £800k dead rent provision has been provided for vacant properties.

m. The fair value adjustment for subscribed capital and subordinated liabilities reflect both credit and interest rate risk associated with these liabilities.

n. Imputed consideration represents the fair value of members' interests transferred. The combination of the two societies did not involve the transfer of any cash consideration. The value of the consideration has been calculated by measuring the fair value of the business of the Scarborough. The calculation was made with reference to publicly available valuations of quoted financial services organisations, adjusted to reflect the financial status, unquoted nature, relative size and economic diversification of the business. This resulted in a value of £Nil attributed to the imputed consideration.

38. Transfer of engagements (continued)

Income and expenditure account of the Scarborough Building Society
For the period 1 May 2008 to 29 March 2009

	£m
Net interest receivable	11.3
Other income and charges	7.7
Fair value losses	(4.3)
Administrative expenses	(20.2)
Impairment losses	(10.8)
Loss for the period before taxation	(16.3)
Taxation	2.8
Loss for the period	(13.5)

The above income and expenditure relates to the cessation accounts of the Scarborough and these amounts have not been included in the Income Statements of the Society or the Group. They are reported here for information only.

If we had transferred the engagements of the Scarborough Building Society from the start of the year up until the end of March, the Scarborough would have contributed £1.9m to income and a loss before tax of £9.1m.

The merger also brought the following subsidiaries into the Group.

Name of subsidiary undertaking	Principal business activity	Percentage of ownership interest
North Yorkshire Mortgages Limited	Lending body	100.0
Scarborough Channel Islands Limited	Offshore deposit taker and lender	100.0
Scarborough Investment Services Limited	Intermediate holding company	100.0
Scarborough Properties Limited	Property developer	100.0
Specialist Mortgage Services Limited	Provider of mortgage services	100.0

Subsequent to the merger, Scarborough Channel Islands Limited was amalgamated into Skipton International Limited, together with an existing subsidiary Skipton Guernsey Limited, and Specialist Mortgage Services Limited was purchased by Homeloan Management Limited (a fellow subsidiary).

Following the merger, the Scarborough ceased to exist, being subsumed by Skipton Building Society. It is therefore not possible to separate its results post the transfer of engagements.

1. Statutory percentages

	As at 31 December 2009 %	Statutory limit %
Lending limit	**10.64**	25.00
Funding limit	**20.58**	50.00

These percentages form part of the audited accounts.

Explanation

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 fully secured on residential property. Business assets are defined as the total assets of the Group plus provisions for impairment losses on loans and receivables less liquid assets, intangible assets, property, plant and equipment and investment properties 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. We have taken advantage of the relief set out in SI 2007/No 860, effective from April 2007, to exclude retail offshore deposits from the total of wholesale funds.

The statutory limits are as laid down under the Building Societies Act 1986 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

	2009 %	2008 %
As a percentage of shares and borrowings:		
(i) Gross capital	**7.58**	7.50
(ii) Free capital	**5.79**	4.95
(iii) Liquid assets	**28.95**	28.84
As a percentage of mean total assets:		
(i) Group profit after taxation	**0.39**	0.18
(ii) Group management expenses	**2.63**	2.98
(iii) Society management expenses	**0.35**	0.47

These percentages form part of the audited accounts.

Explanation

The above percentages have been calculated from the Group and Society Statements of Financial Position.

Shares and borrowings represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue, including accrued interest and the fair value adjustment for hedged risk.

Gross capital represents the general reserve together with the available-for-sale reserve, cash flow reserve, translation reserve, subordinated liabilities, subscribed capital and non-controlling interests, as shown in the Group Statement of Financial Position.

Free capital represents gross capital and provisions for collective impairment losses on loans and advances to customers less property, plant and equipment, investment properties and intangible assets as shown in the Group Statement of Financial Position.

Liquid assets represent the total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.

Mean total assets are the average of the 2009 and 2008 total assets.

Management expenses represent the aggregate of administrative expenses, depreciation and amortisation of continuing operations.

3. Information relating to Directors and other officers at 31 December 2009

The Board of Directors at 31 December 2009, their dates of birth and dates of appointment as Director were:

	Date of Birth	Date of Appointment
D J Cutter	1 January 1962	1 January 2000
A I Findlay	1 April 1952	12 June 2006
P R Hales	21 October 1946	29 May 2007
P M Hay-Plumb	18 March 1960	12 June 2006
C N Hutton	4 November 1949	28 June 2004
A B E Kinney	30 May 1958	15 July 2003
J B Rawlings	10 February 1947	1 June 1995
J Spence	30 January 1951	25 June 2009
P J S Thompson	28 September 1946	1 April 2009
R J Twigg	12 February 1965	1 March 2002
T F Wood	14 April 1972	7 September 2009
W R Worsley	12 September 1956	24 April 2009

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

The Society's officers at 31 December 2009 and their business occupations were:

S E Aldous	General Manager, Customer Engagement
S P Barker	Head of Group Tax
E A Blythe	General Manager, Audit Services
P M Craddock	Director of Financial Services
G M Davidson	Group Secretary
T Fletcher	General Manager, Products and Marketing
S H Galletley	General Manager, Finance
J J Gibson	Director of Group Risk
G Jolly	General Manager, Credit and Lending
E N Law	Commercial Director
R S P Litten	Commercial Director
C J A Mack	General Manager, Capital Markets and Planning
B Ndawula	Head of Group Finance
A C Robinson	Commercial Director
H Varney	General Manager, Business Infrastructure
C Worts	Head of Human Resources
V Wright	Head of Group Procurement

The Directors' business occupations and other Directorships at 31 December 2009 were:

D J Cutter	Building Society Group Chief Executive	Advance Mortgage Funding Limited
		Amber Homeloans Limited
		Bailey Computer Services Limited
		Baseline Capital Limited
		BDS Mortgage Group Limited
		Connells Limited
		Enable Mortgage & Insurance Adviser Network Limited
		Heriotbell Limited
		Homeloan Management Limited
		Incresco Limited
		KB Analytics Limited
		Leeds Share Shop Limited
		Life Policies Direct Limited

D J Cutter (continued)		Malsis School Trust Mortgage Systems Limited North East Trustees Limited North West Investments NZ Limited North Yorkshire Mortgages Limited Pace Financial Solutions Limited Pace Mortgage Solutions Limited Parnell Fisher Child & Co. Limited Parnell Fisher Child Holdings Limited Pearson Jones Plc PS Employee Benefits Limited Red Arc Assured Ltd Savings Management Limited Sequence (UK) Limited Scarborough Commercial Mortgages Limited Scarborough Computer Services Limited Scarborough Finance Limited Scarborough Insurance Services Limited Scarborough Properties Limited Scarborough Residential Mortgages Limited Skipton Business Finance Limited Skipton Financial Services Limited Skipton Group Holdings Limited Skipton Group Limited Skipton Investments Limited Skipton Limited Skipton Mortgages Limited Skipton Mortgages Corporation Limited Skipton Premier Mortgages Limited Skipton Premises Limited Skipton Share Dealing Services Limited Skipton Trustees Limited Specialist Investment Services Limited Specialist Mortgage Services Limited Symington Glass (2) Limited The Independent Mortgage Shop Limited The Private Health Partnership Limited Thomson Shepherd Limited Thomson Shepherd Holdings Limited Torquil Clark Holdings Limited Torquil Clark Limited Torquil Clark Pension Trustees Limited Torquil Clark Professional Connections Limited TQ Management Services Limited Yorkshire Factors Limited
A I Findlay	Company Director	Amec Executive Pensions Trustee Limited Amec Staff Pensions Trustee Limited Countess of Chester Hospital NHS Foundation Trust Skipton Group Holdings Limited

P R Hales	Chartered Insurer	Just Retirement (Holdings) Plc Just Retirement Limited Just Retirement Solutions Limited Skipton Group Holdings Limited UNUM Limited
P M Hay-Plumb	Company Director	Forensic Science Service Limited National Australia Group CIF Trustee Limited Skipton Group Holdings Limited
C N Hutton	Retired Solicitor	Ben Rhydding Sports Club Limited Skipton Group Holdings Limited
A B E Kinney	Retired Partner of a Leading Firm of Chartered Accountants and Consultants	Financial Services Compensation Scheme Limited Gradient Finance Limited Skipton Group Holdings Limited
J B Rawlings	Banker	Ansbacher & Co Limited Ansbacher Group Holdings Limited Sarl Ansbacher Pension Trust Limited Ansbacher UK Group Limited QNB International Holdings Limited Sarl Skipton Group Holdings Limited
J A Spence	Banker	Action for Blind People Business in the Community Capital for Enterprise Limited Capital for Enterprise Fund Managers Limited Chelmsford Diocesan Board of Finance Essex Community Foundation Harlow Renaissance Limited H M Revenue and Customs Skipton Group Holdings Limited St Paul's Cathedral Foundation Vitalise Limited
P J S Thompson	Non-Practising Solicitor	Bailey Electrical Limited Denney O'Hara Limited Denney O'Hara (Life & Pensions) Limited Giggleswick School Judicium Business Services Limited Judicium Consulting Limited Judicium PLC NG Bailey Limited NG Bailey and Company (Overseas) Limited Rushbond Plc Skipton Group Holdings Limited TEP Electrical Distributors Limited
R J Twigg	Building Society Group Commercial Director	Advance Mortgage Funding Limited Amber Homeloans Limited Bailey Computer Services Limited Baseline Capital Limited Connells Limited Connell Financial Services Limited

R J Twigg (continued)		Enable Mortgage & Insurance Adviser Network Limited Homeloan Management Limited KB Analytics Limited Leeds Share Shop Limited MBO 1994 Limited Mortgage Systems Limited North West Investments NZ Limited North Yorkshire Mortgages Limited Savings Management Limited Sequence (UK) Limited Scarborough Commercial Mortgages Limited Scarborough Computer Systems Limited Scarborough Finance Limited Scarborough Insurance Services Limited Scarborough Properties Limited Scarborough Residential Mortgages Limited Skipton Limited Skipton Building Society Charitable Foundation Skipton Covered Bonds Finance (Holdings) Limited Skipton Covered Bonds LLP Skipton Financial Services Limited Skipton International Limited Skipton Group Limited Skipton Group Holdings Limited Skipton Investments Limited Skipton Mortgage Corporation Limited Skipton Mortgages Limited Skipton Premier Mortgages Limited Skipton Premises Limited Skipton Share Dealing Services Limited Skipton Trustees Limited Specialist Mortgage Services Limited Specialist Investment Services Limited Sterling Brokers Limited Sterling International Brokers Limited Yorkshire Factors Limited
T F Wood	Building Society Group Finance Director	Connells Limited Sequence (UK) Limited Skipton Business Finance Limited Skipton Group Holdings Limited TFW Associates Limited
W R Worsley	Chartered Surveyor	Copefringe Limited Country Land & Business Association Limited Skipton Group Holdings Limited The Brunner Investment Trust Plc 61 Cadogan Square Tenants Limited

Messrs Cutter, Twigg and Wood have service contracts entered into on 1 January 2000, 1 March 2002 and 7 September 2009 respectively which may be terminated by either party giving one year's notice.

Directorships of the Society's officers at 31 December 2009 were as follows:

S E Aldous	Skipton Premises Limited
P M Craddock	HE Grant (Holdings) Limited HE Grant Limited Heriotbell Limited Incresco Limited Life Policies Direct Limited North East Trustees Limited Pace Financial Solutions Limited Pace Mortgage Solutions Limited Parnell Fisher Child & Co. Limited Parnell Fisher Child Holdings Limited Pearson Jones Plc PS Employee Benefits Limited Skipton Financial Services Limited Skipton Group Holdings Limited Symington Glass (2) Limited The Independent Mortgage Shop Limited Thomson Shepherd Limited Thompson Shepherd Holdings Limited Torquil Clark Holdings Limited Torquil Clark Limited Torquil Clark Pension Trustees Limited Torquil Clark Professional Connections Limited TQ Management Services Limited
G M Davidson	Skipton Trustees Limited Skipton Premises Limited Skipton Pension Trustees Limited Mutual One Limited
J J Gibson	Connell Financial Services Limited Skipton Pension Trustees Limited
E N Law	MBO 1994 Limited Parnell Fisher Child & Co Limited Parnell Fisher Child Holdings Limited Skipton Group Holdings Limited Sterling International Brokers Limited Thomson Shepherd Holdings Limited Thomson Shepherd Limited
R S P Litten	Amber Homeloans Limited North Yorkshire Mortgages Limited Skipton International Limited
C J A Mack	Skipton Covered Bonds Finance Limited
A C Robinson	Admiral Mortgage Company Limited Advance Mortgage Funding Limited Alegra Fine Products Limited Alegra Limited Bailey Computer Services Limited BDS Mortgage Group Limited

A C Robinson (continued)	BDS Mortgage Solutions Limited MBO 1994 Limited Medical Care Direct Limited Mutual One Limited Pearson Jones Plc Red Arc Assured Limited Skipton Business Finance Limited Skipton Group Holdings Limited Sterling Brokers Limited Sterling International Brokers Limited The Mortgage Helper Limited The Private Health Partnership Limited Torquil Clark Holdings Limited

No other officers held any Directorships.

Stock code 10-8419/02/03/10/APS

Skipton Building Society
Principal Office, The Bailey, Skipton, North Yorkshire BD23 1DN
Telephone: 08458 501700*
skipton.co.uk

mutualmatters

SKIPTON BUILDING SOCIETY