Company Number: SC 001111

CLYDESDALE BANK PLC

ANNUAL REPORT AND CONSOLIDATED FINANCIAL STATEMENTS

30 SEPTEMBER 2009

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Officers and Professional Advisers

Directors	**Chairman:**	Sir Malcolm Williamson #
	Non-executive:	Jonathan Dawson* # Sir David Fell KCB* Richard Gregory OBE * # Roy Nicolson * # Elizabeth Padmore (appointed 3 November 2009) Peter Wood*
	Executive:	Lynne Peacock (Chief Executive Officer) # David Thorburn # John Hooper # (appointed 24 April 2009)
		Gavin Slater resigned as a Director of the Company on 12 March 2009
		* Member of the European Boards' Audit Committee # Member of the European Boards' Risk Committee
UK Executive Committee		Lynne Peacock, Chief Executive Officer David Thorburn, Executive Director John Hooper, Executive Director Tom Burns, Chief Risk Officer Margaret Butler, Quality and Efficiency Director Debbie Crosbie, Chief Information Officer Dean Cutbill, Products & Marketing Director Steven Martin, Head of Strategic Developments Kevin Page, Operations Director Steve Reid, Retail Director Iain Smith, Chief Financial Officer Michael Webber, Head of Legal Services and Company Secretary Arthur Willett, Human Resources Director Mike Williams, Executive General Manager iFS
Secretary		Michael Webber
Registered Office		30 St Vincent Place Glasgow, G1 2HL
Auditor		Ernst & Young LLP 1 More London Place London, SE1 2AF

CLYDESDALE BANK PLC
Chairman's Statement

Sir Malcolm Williamson, Chairman

This year, the economic environment has been particularly challenging for the UK banking sector. Throughout the turmoil Clydesdale Bank, which operates the Clydesdale Bank and Yorkshire Bank brands, has remained safe, strong and in profit. Our traditional banking model, which offers a full range of products and services to business and retail customers, has enabled the Bank to respond to the rapid deterioration in trading conditions and reflects the successful execution of a consistent and disciplined strategy that has sought, over the past few years, to build our franchise. Clydesdale is one of the few banks whose shareholders' interests have not been diluted by rescue funding.

We are continuing to reshape our balance sheet, with a substantially reduced reliance on unsecured lending in favour of more sustainable, lower risk earnings from a broader business base. We raised capital to maintain a solid capital position and maintain our solvency ratios.

In line with risk appetite, we are strengthening our business franchise and enhancing our proposition in a deliberately prudent and balanced way, reflecting risk settings that are regularly monitored and adjusted accordingly. The funding and liquidity position has been further strengthened by higher than industry average deposit growth.

Operating expenses are being firmly controlled. Furthermore, the reshaping and restructuring of our operations is continuing and investment in key infrastructure projects is being maintained, in order that the business can emerge in an excellent competitive position as markets recover and trading conditions improve.

Bad and doubtful debts have increased, reflecting the current adverse economic and market conditions. The Bank's portfolio remains well secured and diversified and asset quality measures remain under close management scrutiny. For customers who have faced financial difficulties, Clydesdale and Yorkshire Banks have continued to build on their range of initiatives to support business and personal customers.

The fundamentals of our business are strong and we are well positioned to capitalise on future growth opportunities.

Sir Malcolm Williamson
Chairman
10 December 2009

Lynne Peacock, Chief Executive Officer

Overview

The Clydesdale Bank PLC ("the Bank") together with its subsidiary undertakings (which together comprise "the Group") is the United Kingdom arm of the National Australia Bank Limited ("NAB"). In a twelve month period which has seen the near collapse and takeover of several leading names from the high street and a total figure for impairment charges reported by the leading UK banks of £67 billion, the Bank has reinforced its reputation as a conventional bank with sound management. Nevertheless, the Bank's results reflect the wider forces that have had an impact on the banking sector and economy as a whole.

Strategic Highlights & Business Developments

While facing unprecedented challenges in terms of the operating environment, the Group demonstrated a resilient performance during the 2009 year. Operating profit before impairment losses reduced by 11.6% on prior year, profit after tax for the year was £34 million. In order to build for the future, the Group's capital was protected while underlying business momentum was maintained. The Group also continued to outperform its peers on most dimensions.

Attracting and retaining a strong retail deposit base has remained a key strategic priority and, despite aggressive competition, retail deposit growth of 13.6% was achieved, over three times the industry average (as measured by the British Banking Association in September 2009). This growth has contributed to an increased Stable Funding Index of 100.6% and increased Customer Funding Index of 78.7%.

The Bank demonstrated strong support for its customers, with new lending issued through the integrated Financial Solutions (iFS) and Retail franchises of £4.1 billion during the year (£2.2 billion in the second half). During a period in which some UK lenders were criticised for low lending volumes, the Bank continued to work in partnership with customers to ensure lending is appropriately priced to reflect the inherent risk and to reduce exposure to basis risk, particularly in business lending.

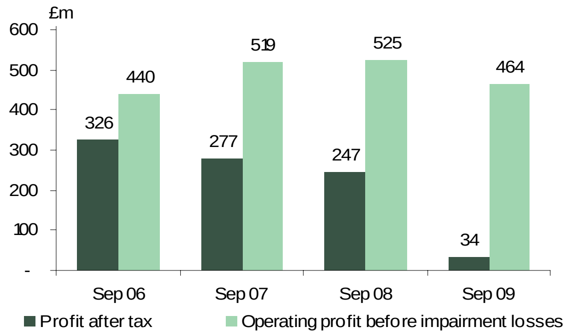
Operating expenses were firmly controlled and this resulted in a decrease in costs of £37 million (5.3%) against the prior year. The Bank has now recorded its fourth consecutive year of flat or falling costs.

The Group's portfolio remains well-secured and diversified both geographically and by lending type. Whilst issues in the commercial property portfolio reflect those experienced by the market in general, the remainder of the Group's portfolio is holding up well given the economic environment.

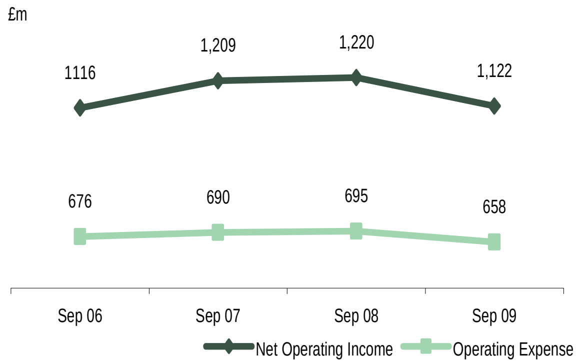
The Bank continues to support customers during the economic downturn and has maintained high levels of customer satisfaction. As a result, during a period in which key competitors saw declining satisfaction levels, the Bank's overall customer numbers have increased. The Bank continues to build on its efforts to support customers in financial difficulty through the Customer Support Unit in the Retail business and deployment of additional resources in the Business Recovery Unit.

Strategic Highlights & Business Developments (continued)

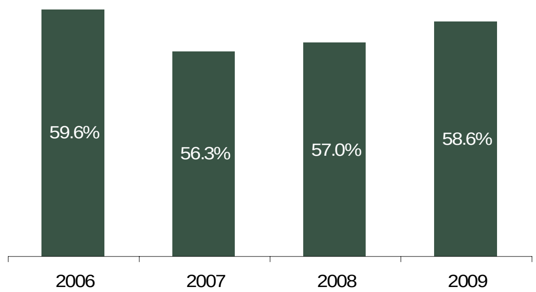
Operating Profit before Impairment Losses and Profit after Tax.



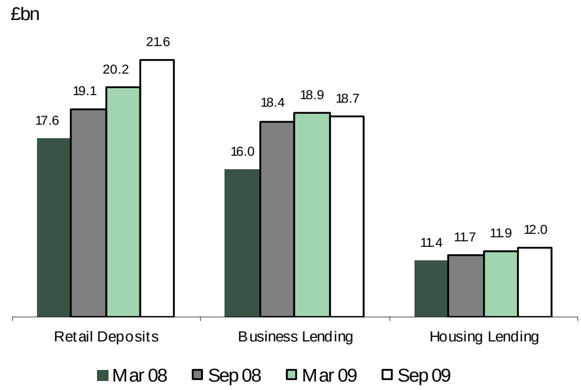
Income and Expense Trends



Cost to Income Ratios.



Loans and Deposits Half Year Average



Operating Environment

The year witnessed unprecedented changes in UK financial markets followed by the deepest recession in post war history. In response to this, the UK Government undertook a series of exceptional actions, taking substantial equity stakes in what had previously been three of the UK's top five banks and instigating a number of defensive mergers. In addition, the level to which Retail Deposits are guaranteed increased to £50,000, Base Rate was reduced to the historically low level of 0.5%, quantitative easing was undertaken and the Special Liquidity, Credit Guarantee and Asset Protection Schemes were launched.

As the year continued, regulatory initiatives focused on raising levels of bank capital and liquidity while encouraging banks to maintain an open market in lending.

The cumulative loss of output due to the recession was 5.5% by September 2009, compared with 4.9% in 1981 and 2.5% in 1992. Domestic property values declined, on average, by 20% from their peak and commercial property fell by 45%. Unemployment, which lags these measures, had climbed to 7.9% by the International Labour Organisation measure at September 2009.

The recession has affected business conditions across all sectors. Manufacturing production is down 14% from its peak, while construction output is down 15%, as both private house building and commercial construction have fallen sharply. Activity in the service sector has fallen by 4%. Total corporate insolvencies increased by over 50% in the quarter to March 2009.

The Consumer Price Index inflation has fallen from its peak of 5.2% at September 2008 to 1.1% in September 2009, below the Bank of England's 2.0% target for the first time since September 2007.

Operating Environment (continued)

The dislocation in the UK financial markets saw the average daily spread between Base Rate and three month LIBOR for the first half of the year rise to 114 basis points (90 day rolling average spread 211 basis points), which can be compared to an average of around 18 basis points from April 1997 to March 2008. This drove a substantial increase in funding and liquidity costs across the banking sector. In the second half, the spread has decreased significantly, with the average daily spread falling to 59 basis points (90 day rolling average spread of 90 basis points) which was still considerably higher than historic averages.

The outlook for 2010 is that it is not expected to worsen, but should be qualitatively different from 2009, as the consequences of the recession work their way through the economy. The Bank of England anticipates a "prolonged period of balance sheet adjustment in the financial, private and public sectors" pointing towards a slow recovery in economic activity. It anticipates GDP moving into positive territory in early 2010, thereafter returning to long-term growth rates over a period of up to two years.

In the month of September, house prices rose by 1.6% and are now rising at their fastest rate for two and a half years. In July 2009, CBRE recorded the first rise in commercial property values since 2007 (0.2%). The indices of business and consumer confidence have also picked up from the very low levels seen earlier this year. All, however, remain below long-term average rates.

Rising household and corporate distress and the decreases in property prices experienced in the last two years have driven higher mortgage arrears and asset impairment for the banking sector.

The Bank has not been immune to these forces but it has remained profitable, and strategies implemented over the last four years, including the reduced cost base and steady investment in rebuilding infrastructure, helped mitigate many of the most damaging effects of the current environment. As a result, it is well positioned for the recovery, with its reputation enhanced, while most competitors have experienced a decline in both customer and public regard.

The conservative lending policies and lower exposure to unsecured lending served to mitigate the impact of high levels of personal insolvencies and unemployment. This has resulted in mortgage arrears at one third of the industry average, overall impairment to gross loans well below the industry average, and 84 repossessions compared with 46,200 for the industry as a whole in the twelve months to 30 September 2009.

In response to the exceptional conditions in funding markets during the year, exposure to Base Rate priced assets was reduced by transferring from Base to LIBOR pricing where appropriate. In addition, a re-pricing initiative was undertaken in order to compensate for the pricing risk inherent in the book. These actions, coupled with reducing Base Rate to LIBOR spreads, resulted in a decreased cost of basis risk in the second half and a wider net interest margin.

Market issues relating to payment protection insurance claims handling and increased levies under the Financial Services Compensation Scheme are all ongoing. Further information provided in note 33 of the financial statements.

Customer, Employees and Community

Customers

The Bank continued to strengthen relationships with customers, with retention and acquisition rates improving as customer satisfaction increased in sharp contrast to the overall market, where satisfaction levels have been falling. The Bank's customer numbers continued to grow.

Employees

During the past 22 months, staff led initiatives have raised over £700,000 for Help the Hospices and over 2,600 community days have been donated by staff, in conjunction with the Bank, to support local communities and projects providing tangible help and financial support.

Community

The auction of a number of rare and collectable Clydesdale bank notes raised over £200,000 for over 70 different charities chosen by the Bank's staff, and its charity partner, 'Help the Hospices'. Coinciding with this auction, the Bank issued a completely new series of banknotes. In July, Yorkshire Bank celebrated its 150th anniversary.

Awards

During the period, the Bank achieved Data Centre Strategy of the Year at the Continuity, Insurance and Risk magazine Business Continuity Awards. Clydesdale Bank became the first UK high street bank to be awarded the Carbon Trust Standard for its efforts in tackling climate change, after it reduced its carbon footprint by 15.8% over a period of 12 months.

CLYDESDALE BANK PLC
Business Review

Financial Analysis

	Year to			Half Year to		
	Sep 09 £m	Sep 08 £m	Sep 09 v Sep 08 %	Sep 09 £m	Mar 09 £m	Sep 09 v Mar 09 %
Net interest income	**845**	896	(5.7)	**462**	383	20.6
Non interest income	**277**	324	(14.5)	**119**	158	(24.7)
Total operating income	**1,122**	1,220	(8.0)	**581**	541	7.4
Total operating expenses	**(658)**	(695)	5.3	**(340)**	(318)	(6.9)
Operating profit before impairment losses	**464**	525	(11.6)	**241**	223	8.1
Impairment losses on credit exposures	**(399)**	(179)	(122.9)	**(231)**	(168)	(37.5)
Group operating profit	**65**	346	(81.2)	**10**	55	(81.8)
Significant items (1)	**(17)**	4	(525.0)	**(5)**	(12)	58.3
Profit on ordinary activities before tax	**48**	350	(86.3)	**5**	43	(88.4)
Tax expense	**(14)**	(103)	86.4	**(1)**	(13)	92.3
Profit for the period	**34**	247	(86.2)	**4**	30	(86.7)
Average Volumes (£bn)						
Gross loans and acceptances (2)	**33.2**	31.2	6.4	**33.1**	33.3	(0.6)
Interest earning assets	**39.0**	35.4	10.2	**39.6**	38.4	3.1
Total assets	**42.1**	38.0	10.8	**42.2**	42.0	0.5
Retail deposits (3)	**20.9**	18.4	13.6	**21.6**	20.2	6.9
Performance Measures						
Profit on average assets	**0.08%**	0.65%	(57bps)	**0.02%**	0.14%	(12bps)
Net interest margin	**2.17%**	2.53%	(36bps)	**2.33%**	2.00%	33bps
Cost to income ratio	**58.6%**	57.0%	(160bps)	**58.5%**	58.8%	30bps
Profit per average FTE (£'000s)	**6**	43		**1**	10	
FTEs (spot) (4)	**5,725**	5,658		**5,725**	5,942	

(1) Included within significant items: Sep'09: £22m efficiency, quality and service initiatives, £11m profit on sale of land and buildings and £6m FSCS levy, Sep'08: £10m profit on sale of land and buildings and £6m FSCS levy. Note, that the 2009 interim accounts did not disclose efficiency, quality and service initiatives as a significant item. There were £6m of costs relating to this in the half to 31 Mar 09 which were included within total operating expenses.

(2) Gross loans and acceptances including gross loans and advances to customers, loans designated at fair value through profit and loss and due from customers on acceptances

(3) Retail deposits include current accounts, savings accounts, term deposits and business retail deposits.

(4) The FTE numbers above disclose the staff remunerated directly by the Group but exclude employees working within other National Australia Group Europe Limited subsidiaries who provide support services to the Group. The overall number of staff employed in the UK Region at 30 September 2009 was 8,295.

September 2009 v September 2008

Profit after tax at £34 million decreased by 86.2% over the prior year, reflecting the exceptionally high costs of funding, liquidity and basis risk and higher charges to provide for bad and doubtful debts. These were partially offset by re-pricing and lower expenses. Over the same period, operating profit before impairment losses totalled £464 million, a decrease of 11.6%.

Average gross loans and acceptances increased by £2 billion, or 6.4%, through the prudent pursuit of opportunities in key market segments. Within this, business lending grew by 9.3%, mortgage growth was 3.6% and exposure to credit card and personal lending fell by 9.5% in line with the Bank's strategy.

During the year the Bank continued to support customers, the iFS and Retail franchises advanced £4.1 billion of new loans, of which £2.0 billion comprised business lending and £1.8 billion were mortgage advances.

Average Retail Deposits grew by 13.6% (£2.5 billion), which is over three times the industry average growth rate of 3.7% in a highly competitive market. The flight to quality by the Bank's customers demonstrates the strength of both the Clydesdale and Yorkshire brands. iFS average deposit growth was 10.6% and Retail network growth was 17.9%.

Net interest income decreased by 5.7%. The exceptionally high costs of funding, liquidity and basis risk of £246 million were offset by a net gain of £38 million on the buy-back of Lanark Master Trust notes. These costs were driven by the Base to LIBOR spreads, which were, on average, a multiple of historic rates. In addition, the low interest rate environment reduced earnings on capital. These were partially offset by an increase in lending margins following re-pricing. Net interest income, after excluding the elevated costs of funding and liquidity, increased by 6% compared with the prior year.

September 2009 v September 2008 (continued)

The **net interest margin** decreased by 36 basis points and was primarily driven by the higher basis risk, funding and liquidity costs and reduced earnings on capital. These were partially offset by a net widening of product margins.

Non interest income decreased by 14.5%, driven by £39m cash flow hedge ineffectiveness and £10m due to an industry-wide reduction in payment protection insurance revenues, partially offset by an increase in foreign exchange derivatives. The prior year includes operating lease income up to the disposal of this business in December 2007.

Operating expenses decreased by £37 million (5.3%) on the prior year. Additional costs from investment spend and general wage inflation were more than offset by efficiency savings, including further process improvements, and lower performance related remuneration as a result of reduced profitability. The disposal of the operating lease book in December 2007 resulted in a £4 million reduction in expenses in the current year.

The **cost to income ratio** at 58.6% showed an adverse 160 basis point movement over the prior corresponding period as a result of lower income, partially offset by lower operating expenses.

The **impairment losses on credit exposures** reflects the significant deterioration in the UK environment over the last twelve months, particularly in the business sector, where there has been a first and second wave of write-downs. This has resulted in an increase in the charge of £220 million, a rise in the write-offs and a higher coverage ratio of provision to gross loans and acceptances ratio.

September 2009 v March 2009

Profit after tax decreased by £26 million on the March 2009 half. This decrease reflects the rise in charges to provide for bad and doubtful debts and an increase in expenses, which were partially offset by increased income. Operating profit before impairment losses of £241 million represents an increase of 8.1% on the first half of 2009.

Average gross loans and acceptances remained relatively flat on the March 2009 half. Gross new advances by the iFS and Retail franchises were £2.2 billion, which were offset by lower lending to sectors with a less attractive risk profile.

Average retail deposits grew by 6.9% (£1.4 billion). This was primarily driven by the continued momentum in iFS and a robust performance in the Retail network.

Net interest income increased by 20.6% due to the effects of repricing activity and lower market dislocation costs, partially offset by the higher credit spread on wholesale funding.

The **net interest margin** improved by 33 basis points. This was as a result of more judicious pricing and a reduction in market dislocation costs.

Non interest income decreased by 24.7% driven by fair value loan revaluations and lower payment protection insurance revenues.

Operating expenses increased by 6.9% on the prior half, driven partially by a property revaluation charge reflecting the downturn in the property market and an increase in the surplus lease space provision. Other cost increases have been offset through a well established culture of cost control. Notwithstanding this, investment spend has been maintained.

The **cost to income ratio** at 58.5% decreased by 30 basis points, reflecting increased income.

The **impairment losses on credit exposures** increased by £63 million over the March 2009 half. This was driven by the continuing wave of business and consumer defaults in the current economic conditions.

Other Items

Asset Quality

	As at		
	Sep-09	**Mar-09**	**Sep-08**
90+ DPD assets (£m)	284	239	154
Gross impaired assets (£m) (1)	615	403	201
90+ DPD plus gross impaired assets to gross loans and acceptances (1) (2)	2.71%	1.94%	1.07%
Specific Provision/ gross impaired assets (1)	14.6%	20.6%	30.8%
Net write-offs to gross loans and acceptances (annualised)(2)	1.03%	0.68%	0.40%
Total provision as a percentage of net write-offs (3)	130%	190%	268%
Total provision to gross loans and acceptances (2) (3)	1.34%	1.30%	1.09%
Bad and doubtful debt charge to credit risk weighted assets	1.58%	1.34%	0.72%

(1) Gross impaired assets for September 2009 includes £115 million gross impaired fair value assets. Whilst not included above, for March 2009 and September 2008 the values of gross impaired fair value assets were £54m and £28 million respectively.

(2) Gross loans and acceptances: includes gross loans and advances to customers, loans designated at fair value through profit and loss and due to customers on acceptances.

(3) Total provision to gross loans and acceptances includes the credit risk adjustments on fair value loans

Asset quality measures continue to reflect the impact of the current UK operating environment. While these measures have not yet stabilised, the Bank's performance has been mitigated by the relationship-based model and considerable proactive initiatives undertaken by management during the period. The Bank continues to compare favourably with industry averages. The portfolio remains well secured and diversified, both geographically and by lending type.

The further deterioration in asset quality continues to be driven by the business banking book, in particular the commercial property sector which represents 87% of Gross impaired Assets.

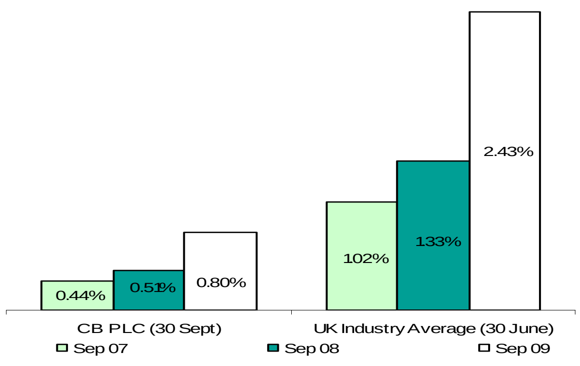
Lending on commercial property represents 24% of gross loans and acceptances (41% of the business book). Of this, approximately £6 billion is investment lending, with development lending totalling £2 billion. No one loan represents more than 1.3% of the commercial property portfolio or 0.3% of the total portfolio. The portfolio is broadly spread around the UK and therefore not concentrated in any one geographical region. The exposure to commercial property has remained stable throughout the year, with an increase in provisions raised during the second half as the economic conditions further affect developers. The arrival rate of development loans into gross impaired assets is, however, slowing.

The remainder of the business book is standing up well. In particular, the leverage portfolio has seen minimal losses.

The residential mortgages portfolio has proved resilient, with 90+ days past due arrears at 0.80% of mortgage balances. This remains significantly below the market average, as measured by the Council of Mortgage Lenders, which currently stands at 2.43% (June 2009). The mortgage book does not include any low doc (self certified) or sub prime lending. The average Loan to Value ratio (LTV) of the mortgage book is 64% on an un-indexed basis (2008 63%). Loss levels within the asset class continue to remain low as a proportion of the overall portfolio.

While keeping mortgage 90+ days past due arrears at one third of the industry average, the Bank has also continued to minimise repossessions in line with the strategy of supporting customers through this difficult period. The number of residential properties repossessed in the full year was 84, compared with 46,200 industry-wide for the same period (Council of Mortgage Lenders) and, at the end of the year, a stock of 65 properties was held.

Proportion of Mortgages in arrears by 90+ DPD



Asset Quality (continued)

As a result of the strategy to reshape the balance sheet towards secured lending over the last four years, the unsecured element of the portfolio continues to fall as a percentage of the book and now stands at 6%. The level of unsecured retail 90+ days past due in arrears has remained relatively stable during the period.

The increase in the September 2009 gross impaired asset balances over March 2009 reflects the impact of the ongoing economic and market conditions, primarily in the business banking book. It is also, in part, due to the low historical base of gross impaired assets and the lending growth experienced by the Bank in recent years.

The ratio of 90+ days past due and gross impaired assets to gross loans and acceptances increased from 1.94% to 2.71% driven by an increase in the commercial property portfolio with the remainder of the portfolio relatively flat. This was below the industry average and was mitigated by the improved management of balances in this category, including an enhanced contact programme with customers.

The coverage ratio of total provisions to gross loans and acceptances was further strengthened from 1.09% in September 2008 to 1.34% in September 2009. This reflects additional provisioning, primarily for commercial property lending, recognising the impact of the current operating environment on this segment. Such additional provisioning was partially offset by the position in the economic cycle, whereby accounts tend to be written off more quickly. Indeed, write-offs more than doubled over the last 12 months.

A number of management initiatives have been undertaken in response to the operating environment. These include increasing resourcing both in the business recovery area and the retail collections team and mobilising a Portfolio Assurance Team within iFS to work closely with customers on mitigation strategies and to identify high risk customers and sectors for closer review and monitoring.

All asset quality measures remain under close management scrutiny to ensure that the actions in place are appropriate and reflective of the current environment.

Capital & Funding Position

Clydesdale Bank PLC Consolidated Diversity of Funding

	As at		
	Sep 09	Mar 09	Sep-08
Retail deposits	**59%**	59%	53%
External short term	**15%**	14%	13%
Subordinated debt	**3%**	3%	2%
Structured finance	**3%**	3%	7%
Securitisation	**6%**	7%	8%
Parent company	**6%**	6%	11%
Medium term notes	**8%**	8%	6%
CB PLC Funding	**100%**	100%	100%

Clydesdale Bank's position as a member of the NAB Group continued to be an asset as Fitch re-affirmed the Bank's long standing AA- credit rating, while Moody's and S&P downgraded it to A1 and A+ respectively, amid downgrades to the entire UK market. The impact of the downgrades on funding has been minimal and the ratings continue to enable the Bank to attract and retain retail and wholesale funding at standard terms.

The Bank continued to improve capital ratios over the year and, as at 30 September 2009, the Tier 1 ratio was 8.2%. In December 2008, additional capital was injected into Clydesdale Bank PLC by National Australia Bank comprising £300 million of ordinary shares, £100 million of preference shares and £300 million of subordinated debt. Capital requirements are kept under regular review and are subject to external Regulatory scrutiny.

The Bank held a portfolio of liquid assets totalling £8.7 billion as at 30 September 2009. This portfolio includes UK government gilts, Bank of England Reserve Account, treasury bills and lending to other banks. The Bank's diverse funding mix of short and long-term wholesale funding, parent company funding and securitisation has enabled this strong liquidity position.

Capital & Funding Position (continued)

After receiving approval to join the Government's Credit Guarantee Scheme, the Bank took advantage of this funding source by pricing and issuing £1.25 billion of three year Government backed bonds under the scheme, enhancing an already strong medium-term funding position.

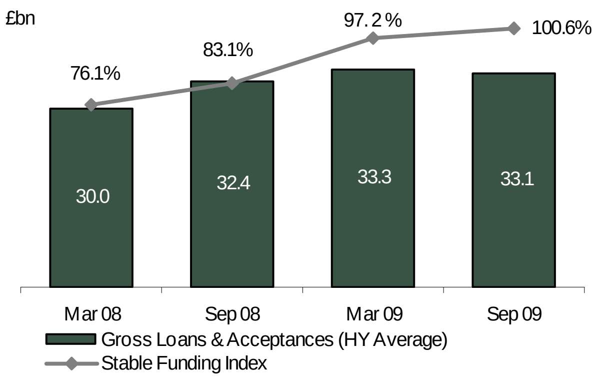
In October 2008, the Bank completed its first Covered Bond issuance under its EUR9 billion programme collateralised on retail mortgages. In January 2009, the Bank issued its second series of Covered Bonds under the existing program. Both issuances have received an AAA rating from all three rating agencies.

As existing wholesale term funding matures and is replaced with more expensive new issuance short-term and MTN funding, the overall margin paid on wholesale funding is increasing. This has been partially offset by the fall in liquidity costs as the spread between UK base and LIBOR decreases.

The Bank's strong performance in attracting retail deposits has continued and will ensure that the Bank remains well positioned to grow without increasing the refinancing risks typically associated with wholesale funding.

During the year, the Bank purchased several tranches of Lanark securitisation notes, taking advantage of price opportunities on residential mortgage backed securities. Whilst the securitisation market is currently effectively closed, Lanark remains an important element of the medium to long-term funding strategy in the UK.

UK Stable Funding Index



The Stable Funding Index (SFI) comprises of Term Funding Index (TFI) plus Customer Funding Index (CFI). TFI is defined as Term Wholesale Funding with a remaining maturity greater than 12 months, divided by Core Assets. CFI is a measure of customer deposits divided by Core Assets.

Investment Spend

During the year to September 2009 the Bank continued to invest in the business with cash spend at £87 million (£30 million operating expense) across the three categories of regulatory and compliance, efficiency and simplification, and revenue generation. This was comparable to the spend for 2008.

Within investment on regulatory and compliance, the Bank participated in the Faster Payments Service, introduced a branch based credit card origination system which avoids the need for paper forms, improved the process for opening term deposit accounts and completed straight-through processing from mortgage origination to mortgage processing.

The key investment in revenue generation was the launch of Business Internet Banking, providing a range of on-line services to business customers.

Fraud prevention and detection capability was enhanced through the deployment of new software to monitor and provide alerts on possible fraudulent Retail Internet Banking and Telephone Banking transactions. An enhanced security solution was deployed to protect information transferred to removable devices.

Distribution

As at 30 September 2009, the Bank's distribution network comprised 72 Financial Solutions Centres and 340 retail branches.

In business banking, iFS demonstrated that the Bank remained "Open for Business" throughout the period of market turbulence. There was strong growth in both domestic and offshore deposits and the corporate team was particularly successful in securing new lending opportunities. Following a detailed review of the network requirements for sustainable future growth, three Financial Solutions Centres and two satellite offices were closed.

The Retail business has focused on attracting good quality mortgage business at more attractive margins and on continuing to build the deposit base. A number of business efficiency initiatives have helped reduce costs.

CB PLC to NAB UK Region Reconciliation

The NAB Group publishes audited segmental financial results of which the UK Region forms one segment. The 2009 full year results were published by NAB on 28 October 2009. The segmentation is based on geographical lines, the exception being the nabCapital business which is treated as a global business segment in its own right. As shown in Note 3 of these financial statements, certain of the nabCapital business is written on the CB PLC balance sheet and therefore this business is not included in the UK Region result. The UK wealth management business, which operates through separate legal entities, is also included in the UK Region results but is not part of CB PLC. Additionally, the UK Region results excludes fair value and hedge ineffectiveness income in determining cash earnings. The table below sets out the reconciliation of the income statements of the two views.

Year ended 30 September 2009

	CB PLC £m	Add: Wealth Management £m	Less: nabCapital £m	Fair value and hedge ineffectiveness £m	Other * £m	NAB UK Region £m
Profit/(loss) on ordinary activities before tax/Cash earnings before tax	48	40	(37)	11	46	108
Profit/(loss) attributable to shareholders/Cash earnings after tax	34	28	(26)	8	34	78
Total assets	42,370					43,027

*Other includes Efficiency, Quality and Service initiatives and liquidity costs absorbed by NAB at Group level but not included in the NAB UK Region result.

Lynne Peacock
Chief Executive Officer
10 December 2009

CLYDESDALE BANK PLC
Report of the Directors

The Directors of Clydesdale Bank PLC (the "Bank") with its subsidiary undertakings (which together comprise the "Group") submit their report and consolidated Financial Statements for the year ended 30 September 2009.

Activities

The Bank is an "authorised person" under the Financial Services and Markets Act 2000 and is regulated by the Financial Services Authority (FSA).

The Bank and its subsidiaries offer access to a comprehensive range of banking and other related financial services through 72 Financial Solutions Centres and 340 retail branches in the UK. Developments in the Group's existing business and future prospects are discussed below.

Profits and appropriations

The Group operating profit for the year ended 30 September 2009 amounted to £65m (2008: £346m). The profit attributable to the shareholders for the year ended 30 September 2009 amounted to £34m (2008: £247m). Preference share dividends of £6m (2008: ordinary share dividends £95m) were paid during the year. The Directors do not recommend the payment of a final dividend on the ordinary shares in respect of this financial year (2008: nil). The Bank's Strategic Highlights and Business Developments are set out in the Business Review on pages 4 -12.

Financial instruments

The Group's risk management objectives and policies are discussed in Note 42 on pages 109 to 112.

Directors and Directors' interests

The current Directors are shown on page 2. Directors who are not full-time employees of the Bank or a related body corporate are appointed in accordance with the Articles of Association and may be eligible for reappointment thereafter. No Director was eligible for reappointment during the year.

Appointments

John Hooper was appointed as an Executive Director of the Company on 24 April 2009 and Elizabeth Padmore was appointed as a Non-executive Director of the Company on 3 November 2009.

Resignations

Gavin Slater resigned as an Executive Director of the Company on 12 March 2009, and has taken a new position with National Australia Bank in Australia.

Directors' interests

No Director had any interest in the shares of the Bank or its subsidiaries at any time during the year. As the Bank is a wholly-owned subsidiary of National Australia Bank (NAB), which is incorporated in Australia, any interest which the Directors may have in NAB does not need to be notified to the Bank, and thus is not disclosed in this report.

Directors' liabilities

During the year the NAB Group paid a premium for a contract insuring the Directors and Officers of National Australia Bank Limited, its subsidiaries and controlled entities against personal liabilities which may arise in the course of the performance of their duties, as well as protecting the Group itself to the extent that it is obligated to indemnify Directors and Officers for such liability.

Employee involvement

The Group carries out an information programme to keep staff informed of business objectives and results. This is achieved through regular meetings, circulars, bulletins and specially commissioned videos as well as training courses for staff.

Employee involvement (continued)

Under the UK National Share Incentive Plan, employees are entitled to purchase up to £1,500 worth of NAB shares each year. Participants contribute each month and the trustee uses the contributions to purchase shares on market which are then held in trust for the participants. Participants are entitled to receive dividends and exercise voting rights in respect of these shares and there is no risk of forfeiture. In addition, up to £3,000 of free shares per employee may be gifted per annum through the plan.

During the year, under the UK National Share Incentive Plan, the NAB gifted ordinary shares of A$1000 to eligible employees based on Group performance in respect of the 2008 Financial year. Participants are entitled to receive dividends and exercise voting rights in respect of these shares whilst they are members of the plan.

Employment of disabled persons

It is the policy of the Group to promote equality of employment opportunities by giving full and fair consideration to applications from disabled people. If existing employees become disabled, every effort is made to retain them within the workforce wherever reasonable and practicable. The Group also endeavours to provide equal opportunities in the training, promotion and general career development of disabled employees.

The Group is authorised as a "two tick" symbol user by Jobcentre Plus. The disability symbol is a recognition given by Jobcentre Plus to employers who have agreed to take action to meet five commitments regarding the employment, retention, training and career development of disabled employees, and to continually review progress and improve on what we do. Employers who wish to become a symbol user have to evidence they can achieve those commitments in their application.

Charitable and political donations

The total amount given for charitable purposes by the Bank during the year ended 30 September 2009 was £842,800 (2008: £336,000). The Bank channels its charitable donations through the Yorkshire and Clydesdale Foundation, which was established during 2008. The Foundation has made donations to many charities, including £271,000 during the year to Help the Hospices, the Bank's charity partner. During the past 22 months and together with staff led initiatives, over £700,000 has been raised and donated to Help the Hospices.

No political donations were made during the year (2008: £Nil).

Corporate governance

It is the Bank's policy not to include all of the disclosures in respect of voluntary corporate governance Codes of Practice as it is a wholly owned subsidiary of NAB. The NAB Group's Annual Financial Report details the Corporate Governance framework applicable to the Bank and its subsidiaries. These disclosures are made after consideration of authoritative pronouncements on Audit Committees and associated disclosures in Australia, the USA, and the United Kingdom.

Going concern

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future.

Events after the balance sheet date

On 25 November 2009, the Supreme Court ruled that the level of Unarranged Overdraft Charges are not assessable for fairness under the Unfair Terms in Consumer Contracts Regulations 1999. Subject to ascertaining the position of the Financial Ombudsman, all claims founded solely on unfairness or penalties will fail.

On 8 December 2009, National Australia Group Europe Limited subscribed for £160,000,000 ordinary shares in Clydesdale Bank PLC (via the holding companies of National Europe Holdings Limited and National Europe Holdings (GB) Limited).

Auditors

In accordance with section 485 of the Companies Act 2006, a resolution to reappoint Ernst & Young LLP, and to authorise the Directors to fix their remuneration, will be proposed at the next Annual General Meeting.

Directors' statement as to disclosure of information to auditors

The Directors who were members of the Board at the time of approving the Report of the Directors are listed on page 2. Having made enquiries of fellow Directors and of the Group's auditors, each of these Directors confirms that:

- to the best of each Director's knowledge and belief, there is no information relevant to the preparation of their report of which the Group's auditors are unaware; and

- each Director has taken all the steps a Director might reasonably be expected to have taken to be aware of relevant audit information and to establish that the Group's auditors are aware of that information.

By order of the Board

Michael Webber
Secretary
10 December 2009

CLYDESDALE BANK PLC
Statement of Directors' Responsibilities

The Directors are responsible for preparing the Annual Report and the Financial Statements in accordance with applicable United Kingdom law and International Financial Reporting Standards (IFRS) as adopted by the European Union.

Company Law requires the Directors to prepare Financial Statements for each financial year which give a true and fair view of the state of affairs of the Group and Bank and of the profit or loss for that financial year. In preparing the Financial Statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;

- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;

- provide additional disclosures when compliance with the specific requirements of IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and

- state that the company has complied with IFRS, subject to any material departures disclosed and explained in the Financial Statements.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and of the Bank and which enable them to ensure that the Financial Statements comply with the Companies Act 2006. They 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.

CLYDESDALE BANK PLC
Independent Auditor's Report to the members of Clydesdale Bank PLC

We have audited the Financial Statements of Clydesdale Bank PLC for the year ended 30 September 2009 which comprise the Consolidated Income Statement, the Group and Bank Statements of Recognised Income and Expense, the Group and Bank Balance Sheets, the Group and Bank Statements of Cash Flow, and the related notes 1 to 45. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Bank's members, as a body, in accordance with Sections 495 and 496 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank'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 Bank and the Bank'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

As explained more fully in the Directors' Responsibilities Statement set on page 16, the directors are responsible for the preparation of the Financial Statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the Financial Statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the Financial Statements

An audit involves obtaining evidence about the amounts and disclosures in the Financial Statements sufficient to give reasonable assurance that the Financial Statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group and Bank's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the Financial Statements.

Opinion on Financial Statements

In our opinion:

- the Financial Statements give a true and fair view of the state of the Group and Bank's affairs as at 30 September 2009 and of the Group's profit for the year then ended;
- the Group and Bank's Financial Statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006; and
- the Group and Bank's Financial Statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

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

Matters on which we are required to report by exception

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

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

Peter Wallace (Senior statutory auditor)
for and on behalf of Ernst &Young LLP, Statutory Auditor
London
11 December 2009

CLYDESDALE BANK PLC
Consolidated Income Statement
for the year ended 30 September 2009

	Note	2009 £m	2008 £m
Interest receivable and similar income		**1,722**	2,393
Interest expense and similar charges		**(877)**	(1,497)
Net interest income	4	**845**	896
Gains less losses on financial instruments at fair value		**9**	31
Other operating income		**268**	293
Non interest income	5	**277**	324
Total operating income		**1,122**	1,220
Personnel expenses		**(216)**	(211)
Depreciation expense	18	**(23)**	(26)
Other operating expenses		**(419)**	(458)
Total operating expenses before impairment	6	**(658)**	(695)
Operating profit before impairment losses		**464**	525
Impairment losses on credit exposures	15	**(399)**	(179)
Group operating profit		**65**	346
Efficiency, quality and service initiatives	6	**(22)**	-
Profit on sale of land and buildings		**11**	10
Special Financial Services Compensation Scheme levy	33	**(6)**	(6)
Profit on ordinary activities before tax		**48**	350
Tax expense	7	**(14)**	(103)
Profit for the financial year attributable to the shareholders	29	**34**	247

All material items dealt with in arriving at the profit on ordinary activities before tax for 2009 and 2008 relate to continuing activities.

CLYDESDALE BANK PLC
Statement of Recognised Income and Expense
for the year ended 30 September 2009

		Group		Bank	
	Note	**2009**	2008	**2009**	2008
		£m	£m	**£m**	£m
Income and expense recognised directly in equity					
Revaluation of land and buildings	29	**(6)**	(3)	**(6)**	(3)
Net change in available for sale investments reserve	29	**19**	3	**19**	3
Net change in cash flow hedge reserve	29	**128**	28	**84**	28
Actuarial (losses)/gains on defined benefit pension plans	25	**(591)**	5	**(591)**	5
Post retirement medical benefits	25	**-**	(7)	**-**	(7)
Total changes in items recognised directly in equity		**(450)**	26	**(494)**	26
Tax credit/(expense) on items recognised directly in equity	7	**128**	(12)	**140**	(12)
Net change in items recognised directly in equity		**(322)**	14	**(354)**	14
Profit for the year		**34**	247	**92**	143
Total recognised income and expense for the year		**(288)**	261	**(262)**	157
Attributable to:					
Ordinary shareholders		**(288)**	261	**(262)**	157

CLYDESDALE BANK PLC
Balance Sheets
at 30 September 2009

		Group		Bank	
		2009	2008	**2009**	2008
		£m	£m	**£m**	£m
	Note				As restated
Assets					
Cash and balances with central banks	9	**2,713**	5,109	**2,713**	5,109
Due from other banks	10	**340**	522	**339**	14
Derivative financial assets	11	**942**	602	**424**	270
Other financial assets at fair value	12	**5,983**	4,276	**5,983**	4,276
Investments	13	**2,180**	7	**2,486**	7
Loans and advances to customers	14	**27,147**	28,656	**22,393**	24,506
Due from customers on acceptances		**2**	3	**2**	3
Investments in controlled entities and associates	17	**2**	2	**617**	617
Property, plant and equipment	18	**167**	207	**167**	207
Investment properties	19	**44**	16	**-**	16
Current taxes		**5**	5	**54**	43
Deferred tax assets	20	**147**	-	**146**	(3)
Defined benefit pension assets	25	**-**	239	**-**	239
Due from related entities	36	**1,971**	1,153	**6,922**	1,854
Other assets	21	**727**	1,179	**403**	2,772
Total assets		**42,370**	41,976	**42,649**	39,930
Liabilities					
Due to other banks	22	**1,920**	3,962	**1,920**	3,962
Derivative financial liabilities	11	**113**	36	**113**	36
Other financial liabilities at fair value	12	**597**	553	**597**	553
Due to customers	23	**26,656**	22,334	**26,656**	22,062
Liabilities on acceptances		**2**	3	**2**	3
Deferred tax liabilities	20	**50**	24	**28**	5
Provisions	24	**14**	9	**14**	9
Defined benefit pension liabilities	25	**320**	-	**320**	-
Bonds and notes	26	**5,287**	5,451	**2,953**	2,585
Due to related entities	36	**3,321**	5,151	**6,326**	6,271
Other liabilities	27	**1,840**	2,289	**1,671**	2,507
Total liabilities		**40,120**	39,812	**40,600**	37,993
Shareholders' equity					
Share capital	28	**632**	232	**632**	232
Share premium account	29	**243**	243	**243**	243
Share option reserve	29	**2**	20	**2**	20
Asset revaluation reserve	29	**2**	7	**2**	7
Available for sale investments reserve	29	**14**	-	**14**	-
Merger reserve	29	**338**	338	**338**	338
Cash flow hedge reserve	29	**103**	11	**71**	11
Retained earnings	29	**916**	1,313	**747**	1,086
Total parent shareholders' equity		**2,250**	2,164	**2,049**	1,937
Total liabilities and shareholders' equity		**42,370**	41,976	**42,649**	39,930

These Financial Statements were approved by the Board of Directors on 10 December 2009 and were signed on its behalf by:

Sir Malcolm Williamson
Chairman

Lynne Peacock
Chief Executive Officer

CLYDESDALE BANK PLC
Cash Flow Statement
for the year ended 30 September 2009

	Note	Group		Bank	
		2009	2008	**2009**	2008
					As restated
		£m	£m	**£m**	£m
Profit on ordinary activities before tax		**48**	**350**	**55**	194
Adjustments for:					
Non cash or non operating items included in profit before tax	35	**(1,032)**	(691)	**(1,039)**	(534)
Changes in operating assets	35	**(2,887)**	(3,468)	**(900)**	(5,653)
Changes in operating liabilities	35	**2,719**	4,841	**2,508**	5,410
Interest received		**2,017**	2,052	**1,757**	1,800
Interest paid		**(758)**	(656)	**(666)**	(681)
Tax received/(paid)		**13**	(131)	**40**	(67)
Net cash provided by operating activities		**120**	2,297	**1,755**	469
Cash flows from investing activities					
Dividends received		**-**	-	**193**	-
Interest received		**45**	124	**45**	103
Purchase of available for sale investments		**(1)**	-	**(1)**	-
Purchase of property, plant and equipment		**(81)**	(78)	**(52)**	(78)
Proceeds from sale of property, plant and equipment		**66**	90	**67**	31
Purchase of shares in subsidiary		**-**	-	**-**	(580)
Proceeds from sale of subsidiary		**2**			
Sale of investments		**6**	-	**6**	-
Net cash provided by investing activities		**37**	136	**258**	(524)
Cash flows from financing activities					
Interest paid		**(319)**	(553)	**(348)**	(410)
Proceeds from ordinary shares issued		**300**	-	**300**	-
Proceeds from redeemable preference shares issued		**100**	-	**100**	-
Net (Redemption)/issue of bonds and notes		**(164)**	(20)	**368**	271
Share options settled		**(35)**	-	**(35)**	-
Net (decrease)/increase in amount due from related entities		**(818)**	176	**(5,068)**	3,675
Net (decrease)/increase in amount due to related entities		**(1,792)**	1,248	**93**	(533)
Net decrease in minority interest		**-**	(136)	**-**	-
Dividends paid		**(6)**	(95)	**(6)**	(95)
Net cash (used in)/provided by financing activities		**(2,734)**	620	**(4,596)**	2,908
Net (decrease)/increase in cash and cash equivalents		**(2,577)**	3,053	**(2,583)**	2,853
Cash and cash equivalents at beginning of the year		**5,190**	2,137	**5,190**	2,337
Cash and cash equivalents at end of the year	35	**2,613**	5,190	**2,607**	5,190

1. Authorisation of Financial Statements and statement of compliance with IFRS

In these Financial Statements Clydesdale Bank PLC is referred to as the "Bank". The "Group" consists of the Bank and its controlled entities. The principal controlled entities are listed in note 17. The consolidated Financial Statements comprise the Financial Statements of the Group.

The consolidated Financial Statements of Clydesdale Bank PLC for the year ended 30 September 2009 were authorised for issue by the Board of Directors on 10 December 2009 and the balance sheets were signed on the Board's behalf by Sir Malcolm Williamson and Lynne Peacock.

Clydesdale Bank PLC is incorporated in the UK and registered in Scotland.

Copies of the Annual Report and consolidated Financial Statements prepared in respect of the Bank may be obtained from the Corporate Affairs Department, Clydesdale Bank PLC, 20 Waterloo Street, Glasgow, G2 6DB.

The ultimate parent undertaking, and ultimate controlling party is National Australia Bank Limited ("NAB"), a company incorporated in the State of Victoria, Australia. This company also heads the largest group in which the results of the Group are consolidated. The smallest group in which the results of the Group are consolidated is that headed by National Australia Group Europe Limited ("NAGE") which is incorporated and registered in England and Wales. National Europe Holdings (GB) Limited, a company incorporated and registered in England and Wales, is the immediate holding company for the Bank.

The Group and Bank's Financial Statements have been prepared on the going concern basis, in accordance with IFRS as adopted for use in the European Union and as applied in accordance with the provisions of the Companies Act 2006. There are no differences in the accounting policies adopted by the Group and Bank. The principal accounting policies adopted by the Group are set out in note 2.

2. Accounting policies

Basis of preparation

The preparation of Financial Statements in conformity with IFRS requires the use of certain critical accounting estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosed amount of contingent liabilities. Assumptions made at each balance sheet date are based on best estimates at that date. Although the Group has internal control systems in place to ensure that estimates can be reliably measured, actual amounts may differ from those estimates. It is not anticipated that such differences would be material.

The Financial Statements have been prepared on the going concern basis under the historical cost convention, as modified by the application of fair value measurements.

As permitted by section 408 of the Companies Act 2006, no Income Statement is presented for the Bank.

Significant accounting judgements and estimates

In the process of applying the Bank's accounting policies, management has exercised judgements and estimates in determining the amounts recognised in the Financial Statements. The most significant use of judgement and estimates are as follows:

Going concern

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future.

2. Accounting policies (continued)

Going concern (continued)

The Bank's business activities, together with the factors likely to affect its future development, performance and position are set out in the Business Review on pages 4 to 12. In addition note 43 to the Financial Statements includes the Bank's objectives, policies and processes for managing its capital and note 42 to the Financial Statements includes the Bank's financial risk management objectives; details of its financial instruments and hedging activities; and its exposure to credit risk and liquidity risk.

The Bank has access to financial resources, the support of its ultimate parent NAB Group and a growing customer deposit base. As a consequence, the Directors believe that the Bank is well placed to manage its business risks successfully despite the current uncertain economic outlook.

After making enquiries, the Directors have a reasonable expectation that the Bank and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgement is required to establish fair values. The judgements include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities. The valuation of financial instruments is described in more detail in note 12.

Impairment losses on loans and advances

The Bank reviews its individually significant loans and advances at each balance sheet date to assess whether an impairment loss should be recorded in the income statement. In particular, judgement by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the Bank makes judgements about the borrower's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the impairment allowance.

Loans and advances that have been assessed individually and found not to be impaired and all not individually significant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident.

The collective assessment takes account of data from the loan portfolio (such as credit quality, levels of arrears, credit utilisation, loan to collateral ratios etc.), concentrations of risk and economic data (including levels of unemployment, real estate prices indices, country risk and the performance of different individual groups). The impairment loss on loans and advances is disclosed in more detail in note 15.

Impairment of available for sale investments

The Bank reviews its debt securities classified as available for sale investments at each balance sheet date to assess whether they are impaired. This requires similar judgement as applied to the individual assessment of loans and advances.

The Bank also records impairment charges on available for sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is 'significant' or 'prolonged' requires judgement. In making this judgement, the Bank evaluates, among other factors, historical share price movements and the duration and extent to which the fair value of an investment is less than its cost.

2. Accounting policies (continued)

Liquidity

The Bank manages its liquidity by maintaining an adequate ratio of net liquid assets to customer liabilities, which is set out in a table in the liquidity risk disclosures in note 42. The table requires judgement with respect to whether assets can be considered liquid.

Deferred tax assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies.

Retirement benefit obligations

The cost of the defined benefit pension plan is determined using an actuarial valuation. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Due to the long term nature of these plans, such estimates are subject to significant uncertainty. See note 25 for the assumptions used.

Currency of presentation

All amounts are expressed in pounds sterling and all values are rounded to the nearest million pounds unless otherwise stated.

Principles of consolidation

Controlled entities
The consolidated Financial Statements comprise the Financial Statements of the Bank and its controlled entities. Controlled entities are all entities (including special purpose entities ("SPEs")) over which the Bank has the power to govern the financial and operating policies so as to obtain economic benefits from their activities. SPEs require consolidation in circumstances such as those where the Bank has access to the majority of the residual income or is exposed to the majority of the residual risk associated with the SPE.

Controlled entities are consolidated from the date on which control is transferred to the Bank. They are deconsolidated from the date that control ceases. The purchase method of accounting is used to account for the acquisition of controlled entities.

The effects of transactions between entities within the economic entity are eliminated in full upon consolidation.

Outside interests in the equity and results of the entities that are controlled by the Bank are shown as a separate item, "minority interest", in the consolidated Financial Statements.

Associates
Associates are undertakings over which the Bank exerts significant influence but not control. Investments in associates are accounted for using the equity method. The attributable share of profit and reserves of the associated undertaking is based on the management accounts as at 30 September.

2. Accounting policies (continued)

Foreign currency translation

Functional and presentation currency
Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (functional currency). The consolidated financial report is presented in GBP, which is the Company's functional and presentation currency.

Transactions and balances
Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges. Translation differences on non-monetary items, such as equity securities held at fair value through profit or loss, are reported as part of the fair value gain or loss.

Segment reporting

A business segment is defined as a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

A geographical segment is defined as a group of assets and operations engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

Fair value measurement

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

Where the classification of a financial asset or liability requires it to be stated at fair value, the fair value is determined by reference to the quoted bid or offer price in the most advantageous active market to which the Group entity has immediate access, wherever possible. An adjustment for other credit risk is also incorporated into the fair value.

Fair value for a net open position in a financial liability that is quoted in an active market is the current offer price, and for a financial asset the bid price, multiplied by the number of units of the instrument held or issued.

Where no such active market exists for the particular asset or liability, the Group uses a valuation technique to arrive at the fair value, including the use of transaction prices obtained in recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. In doing so, fair value is estimated using a valuation technique that makes maximum use of market inputs and places minimal reliance upon entity-specific inputs.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Group recognises profits on day one.

Where a valuation technique involves little or no observable data, this should not give rise to a valuation that differs from the transaction price as in this situation the transaction price will be regarded as the best evidence of fair value.

2. Accounting policies (continued)

Assets

On initial recognition all financial assets are recorded at fair value and classified as either fair value through profit or loss, available for sale, held to maturity or loans and receivables.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and liquid assets, amounts due from other banks (to the extent less than 90 days) and short-term government securities.

Cash and cash equivalents are brought to account at the face value or the gross value of the outstanding balance where appropriate.

Due from other banks

Due from other banks includes certain loans, reverse repurchase agreements, nostro balances, and settlement account balances due from other financial institutions.

Items classified as fair value through profit or loss

Upon initial recognition financial assets may be designated as fair value through profit or loss ("FVTPL"). This classification can only be used in the following circumstances:

- Designating instruments will eliminate or significantly reduce measurement or recognition inconsistencies (eliminate an accounting mismatch) that would otherwise arise from measuring assets or liabilities on a different basis.

- Under this criterion the Group has elected to designate certain individually hedged customer loans and their underlying derivatives at FVTPL. Derivatives at FVTPL are predominantly interest rate swaps hedging fixed interest rate loans. The fair value of derivatives at FVTPL is based on current market rates. Significant terms and conditions affecting the timing and future cash flow of the loans are the principal amount, term, repayment frequency, and fluctuations in interest rates. Designating the loans at fair value minimises future volatility within the income statement as movement caused by interest rate fluctuations are largely offset by an equal and opposite movement in the underlying derivative financial instruments.

- If an embedded derivative is required to be separated from the host contract but cannot be reliably fair valued.

- Assets and liabilities are both arranged and their performance is evaluated on a fair value basis, in accordance with documented risk management and investment strategies.

Purchases and sales of financial assets classified within FVTPL are recognised on trade date, being the date that the Group is committed to purchase or sell an asset.

Once a financial instrument has been designated as FVTPL it is not possible subsequently to change the designation.

Embedded derivative

The Group assesses whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. No subsequent reassessment is permitted unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is performed. The Group determines whether a modification to cash flows is significant by considering the extent to which the expected future cash flows associated with the embedded derivative, the host contract or both have changed and whether the change is significant relative to the previously expected cash flows on the contract.

2. Accounting policies (continued)

Derivative financial instruments and hedge accounting

All derivatives are recognised in the balance sheet at fair value on trade date and are classified as trading except where they are designated as part of an effective hedge relationship. The carrying value of a derivative is measured at fair value throughout the life of the contract. Derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The method of recognising the resulting fair value gain or loss on a derivative depends on whether the derivative is designated as a hedging instrument and, if so, the nature of the item being hedged. The Group designates certain derivatives as either hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge); or hedges of highly probable future cash flows attributable to a recognised asset or liability, or a highly probable forecast transaction (cash flow hedge). Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

The Group documents, at the inception of a transaction, the relationship between hedging instruments and the hedged items, and the Group's risk management objective and strategy for undertaking these hedge transactions. The Group documents how effectiveness will be measured throughout the life of the hedge relationship and its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

Fair value hedge
The carrying value of the hedged item on initial designation is adjusted for the fair value attributable to the hedged risk. Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The movement in fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item is amortised to the income statement on an effective yield basis over the remaining period of the original hedge relationship.

Cash flow hedge
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity, while the gain or loss relating to the ineffective portion is recognised immediately in the income statement. The carrying value of the hedged item is not adjusted.

Amounts accumulated in equity are transferred to the income statement in the period in which the hedged item will affect profit or loss.

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

Derivatives that do not qualify for hedge accounting
Certain derivative instruments do not qualify for hedge accounting. This could occur for two reasons:-
- The Group has classified the derivative as a trading item; or
- The derivative does not meet the criteria for hedge accounting.

In both these cases the derivative is classified as a trading derivative. Changes in the fair value of trading derivatives are recognised immediately in the income statement.

Available for sale investments

Available for sale investments are non-derivative financial assets that are designated as available for sale and are not categorised into any of the categories of (i) fair value through profit or loss (ii) loans and receivables or (iii) held to maturity. Available for sale investments primarily comprise debt and equity securities.

2. Accounting policies (continued)

Available for sale investments (continued)

Consistent with financial assets classified as fair value through profit or loss the Group applies trade date accounting to purchases and sales of available for sale investments.

Available for sale investments are initially recognised at fair value including direct and incremental transaction costs. They are subsequently held at fair value. Gains and losses arising from changes in fair value are included as a separate component of equity until sale when the cumulative gain or loss is transferred to the income statement.

Interest income is determined using the effective interest method. Impairment losses and translation differences on monetary items are recognised in the income statement within the period in which they arise. Available for sale investments are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

Held to maturity financial assets

Held to maturity investments are non derivative financial assets with fixed or determinable payments that the Group has the intention and ability to hold to maturity. Held to maturity assets are initially recognised at fair value and subsequently recorded at amortised cost using the effective interest method.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which are not classified as 'available for sale' or designated at fair value through profit or loss. They arise when the Group provides money or services directly to a customer with no intention of trading the loan. Loans and receivables include overdrafts, credit card lending, market rate advances, bill financing, housing loans, lease finance and term lending.

Loans and receivables are recorded at amortised cost, using the effective interest method, adjusted for impairment losses and unearned income. They are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

As noted above, in certain limited circumstances the Group applies the fair value measurement option to financial assets. This option is applied to loans and advances where there is an embedded derivative within the loan contract and the Group has entered into a derivative to offset the risk introduced by the embedded derivative. The loan is designated as being carried at fair value through profit or loss to offset the movements in the fair value of the derivative within the income statement.

Repurchase and reverse repurchase agreements

Securities sold subject to repurchase agreements ("repos") are retained in their respective balance sheet categories. The counterparty liability is included in amounts due to other banks, deposits from banks, other deposits or deposits due to customers, as appropriate based upon the counterparty to the transaction.

Securities purchased under agreements to resell are accounted for as collateralised loans. The difference between the sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Such amounts are normally classified as deposits with other banks or cash and cash equivalents. Securities lent to counterparties are also retained in the Financial Statements. Securities borrowed are not recognised in the Financial Statements unless they are sold to third parties in which case the purchase and sale are recorded with the gain or loss included in trading income. The obligation to return securities borrowed is recorded at fair value as a trading liabilty.

Impairment of financial assets

The Group assesses at each balance sheet date whether there is evidence that a financial asset or a portfolio of financial assets is impaired. A financial asset or portfolio of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset and prior to the balance sheet date ('a loss event'), and that loss event or events has had an impact on the estimated future cash flows of the financial asset or the portfolio that can be reliably estimated.

2. Accounting policies (continued)

Impairment of financial assets (continued)

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

For loans and receivables and held to maturity investments, the amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The amount of the loss is recognised using an allowance account and the amount of the loss is included in the income statement.

Financial assets at fair value through the profit or loss are not assessed for impairment as their fair value reflects the credit quality of the instrument and changes in fair value are recognised in the income statement.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure and any costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar risk characteristics, taking into account asset type, industry, geographical location, collateral type, past-due status and other relevant factors. These characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the counterparty's ability to pay all amounts due according to the contractual terms of the assets being evaluated.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist. In addition, the Group uses its experienced judgement to estimate the amount of an impairment loss. This incorporates amounts calculated to overcome model deficiencies and systemic risks where appropriate and supported by historic loss experience data. The use of such judgements and reasonable estimates is considered by management to be an essential part of the process and does not impact reliability.

The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Following impairment, interest income is recognised using the original effective rate of interest which was used to discount the future cash flows for the purpose of measuring the impairment loss.

When a loan is uncollectible, it is written off against the related provision. Such loans are written off after 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 provision for loan impairment in the balance sheet.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

2. Accounting policies (continued)

Impairment of financial assets (continued)

Renegotiated loans
The bank's objective in restructuring a loan will primarily be to maximise the potential recovery of its outstanding debt. A loan restructuring is the modification or elimination of a loan prior to or at its maturity date by means other than those prescribed under the contractual terms of the loan agreement. This may involve extending the payment arrangements and the agreement of new loan conditions. When the terms of the loan have been renegotiated, the loan is no longer considered past due. The bank continually reviews renegotiated loans to ensure that all criteria are met and future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Equity and debt instruments
In the case of equity instruments classified as available for sale, the Group seeks evidence of a significant or prolonged decline in the fair value of the security below its cost to determine whether impairment exists. Where such evidence exists, the cumulative net loss that has been previously recognised directly in equity is removed from equity and recognised in the income statement. In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as all other financial assets. Reversals of impairment of debt securities classified as available for sale are recognised in the income statement. Reversals of impairment of equity shares classified as available for sale are not recognised in the income statement. Increases in the fair value of equity shares classified as available for sale after impairment are recognised directly in equity.

Investments in controlled entities and associates

The Bank's investments in controlled entities and associates are valued at cost or valuation less any provision for impairment. Such investments are reviewed annually for impairment, or more frequently when there are indications that impairment may have occurred. Losses relating to impairment in the value of shares in controlled entities and associates are recognised in the income statement.

Property, plant and equipment

All freehold and long-term leasehold land and buildings are revalued annually on an open market basis by the Directors to reflect current market values, based on advice received from independent valuers. In addition, full independent valuations are carried out on a three year cycle on an open market basis, including directly attributable acquisition costs but without deducting expected selling costs. For properties that are vacant, valuations are carried out on an open market basis. Revaluation increments are credited to the asset revaluation reserve, unless these reverse deficits on revaluations charged to the income statement in prior years. To the extent that they reverse previous revaluation gains, revaluation losses are charged against the asset revaluation reserve. This policy is applied to assets individually. Revaluation increases and decreases are not offset, even within a class of assets, unless they relate to the same asset.

All other items of property, plant and equipment are carried at cost, less accumulated depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to acquisition.

Property, plant and equipment is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of (i) the asset's fair value less costs to sell and (ii) the asset's value in use.

Where a group of assets working together supports the generation of cash inflows largely independent of cash inflows from other assets or groups of assets, recoverable amount is assessed in relation to that group of assets (cash-generating unit).

2. Accounting policies (continued)

Property, plant and equipment (continued)

With the exception of land, all items of property, plant and equipment are depreciated using the straight-line method, at rates appropriate to their estimated useful lives to the Group. Buildings and leasehold properties with more than thirty years to the expiry of the lease, are depreciated over the term of the lease to a maximum of fifty years. Leasehold properties with less than thirty years to the expiry of the lease are depreciated over ten years or the period of the lease, whichever is the shorter. Motor vehicles, fixtures and equipment are depreciated over their estimated useful lives, which range from three to ten years. Residual values are determined on the dates of acquisition and revaluation of assets, based on estimated realisable values, net of any realisation costs.

Gains or losses on the disposal of property, plant and equipment, which is determined as the difference between the net sale proceeds and the carrying amount at the time of sale are included in the income statement.

Any realised amounts in the asset revaluation reserve are transferred directly to retained earnings.

Investment property assets

Investment property assets are carried at fair value, with fair value increments and decrements taken to the income statement in the period in which they arise. Investment property assets are revalued annually by directors to reflect fair values. Directors' valuations are based on advice received from independent valuers. Such valuations are performed on an open market basis being the amounts for which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable willing seller in an arm's length transaction at the valuation date. Newly acquired investment property assets are held at cost (i.e. equivalent to fair value due to their recent acquisition) until the time of the next annual review, a period not exceeding twelve months.

Leases

The determination of whether an arrangement is, or contains, a lease is based on the substance of the arrangement and requires an assessment of whether:

- fulfilment of the arrangement is dependent on the use of a specific asset or assets; and
- the arrangement conveys a right to use the asset.

As lessee

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

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

Sale and leaseback leases entered into by the Group as lessee are primarily operating leases. If a sale and leaseback transaction results in a finance lease, any excess of sales proceeds over the carrying amount is deferred and amortised over the lease term. If it results in an operating lease, and the transaction is established at fair value, any excess of sales proceeds over the carrying amount is recognised immediately in the income statement.

2. Accounting policies (continued)

Leases (continued)

As lessor
Leases entered into by the Group as lessor, where the Group transfers substantially all the risks and rewards of ownership to the lessee, are classified as finance leases. The net investment in the lease, which is comprised of the present value of the lease payments including any guaranteed residual value and initial direct costs, is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is unearned income. Income is recognised over the term of the lease using the net investment method (before tax) reflecting a constant periodic rate of return.

Assets under operating leases are included within property, plant and equipment at cost and depreciated over the useful life of the lease after taking into account anticipated residual values. Operating lease rental income is recognised within 'Other operating income' in the income statement on a straight line basis over the life of the lease. Depreciation is recognised within 'Depreciation expense' in the income statement consistent with the nature of the asset (refer to note 18, Property plant and equipment).

Liabilities

Financial liabilities

Financial liabilities comprise items such as due to other banks, due to customers, liabilities on acceptances, trading liabilities and deposits and other borrowings.

Financial liabilities may be held at fair value through profit or loss or at amortised cost. Items held at fair value through profit or loss comprise both items held for trading and items specifically designated as fair value through profit or loss at initial recognition.

Financial liabilities held at fair value through profit or loss are initially recognised at fair value with transaction costs being recognised immediately in the income statement. Subsequently they are measured at fair value and any gains and losses are recognised in the income statement as they arise.

Liabilities may be designated as fair value through profit or loss if they meet the following criteria:

- If a host contract contains one or more embedded derivative the Group may designate the entire contract as being held at fair value; or

- Designating instruments will eliminate or significantly reduce measurement or recognition inconsistencies (eliminate an accounting mismatch) that would otherwise arise from measuring assets or liabilities on a different basis; or

- Assets and liabilities are both arranged and their performance evaluated on a fair value basis in accordance with documented risk management and investment strategies.

2. Accounting policies (continued)

Financial liabilities (continued)

A financial liability is classified as held-for-trading if it is incurred principally for the purpose of selling in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative (not in a qualifying hedge relationship).

All other financial liabilities are measured at amortised cost using the effective interest method. A financial liability is derecognised from the balance sheet when the Group has discharged its obligation, the contract is cancelled or expires.

Provisions

Provisions are recognised when a legal or constructive obligation exists as a result of past events and it is probable that an outflow of economic benefit will be necessary to settle the obligation, and it can be reliably estimated. Provisions are not discounted to the present value of their expected net future cash flows except where the time value of money is considered material.

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised in the balance sheet but are disclosed unless they are remote.

Non-lending losses

Provision for non-lending losses is raised for losses to be incurred by the Group, which do not relate directly to amounts in respect of principal and interest outstanding for loans and advances.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation as at the reporting date, taking into account the risks and uncertainties that surround the events and circumstances that affect the provision.

Restructuring costs

Provisions for restructuring costs include provisions for expenses incurred but not yet paid and future expenses that will arise as a direct consequence of decisions already made. A provision for restructuring costs is only made where the Group has made a commitment and entered into an obligation such that it has no realistic alternative but to carry out the restructure and make future payments to settle the obligation. Provision for restructuring costs is only recognised when a detailed plan has been approved and the restructuring has either commenced or has been publicly announced. This includes the cost of staff termination benefits and surplus leased space. Costs related to ongoing activities are not provided for.

Surplus leased space

Surplus leased space is an onerous contract and a provision is recognised when the expected benefits to be derived from the contract are less than the costs that are unavoidable under the contract. This arises where premises are currently leased under non-cancellable operating leases and either the premises are not occupied, or are being sub-leased for lower rentals than the Group pays, or there are no substantive benefits beyond a known future date. The provision is determined on the basis of the present value of net future cash flows.

Dividends

Dividends are recognised as a liability at the time the dividend is approved. Dividends that are approved after the balance sheet date are disclosed as a post balance sheet event.

2. Accounting policies (continued)

Financial guarantees

The Group provides guarantees in the normal course of business on behalf of its customers. Guarantees written are conditional commitments issued by the Group to guarantee the performance of a customer to a third party. Guarantees are primarily issued to support direct financial obligations such as commercial bills or other debt instruments issued by a counterparty. It is the rating of the Group as a guarantee provider that enhances the marketability of the paper issued by the counterparty in these circumstances.

Financial guarantees are recognised at the greater of the unearned revenue or any provision that arises when a claim obligation is probable.

Pension and post retirement costs

Employees of the Group are entitled to benefits on retirement, disability or death from the Group's superannuation plans. The Group operates both defined benefit and defined contribution pension schemes.

The defined contribution scheme receives fixed contributions from Group companies and the Group's obligation for contributions to these plans are recognised as an expense in the income statement as incurred. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payment is available.

The defined benefit schemes provide defined benefits based on years of service and career averaged revalued earnings. A liability or asset in respect of defined benefit pension plans is recognised in the balance sheet and is measured as the present value of the defined benefit obligation at the reporting date less the fair value of the superannuation fund's assets at that date and any unrecognised past service cost.

The present value of the defined benefit obligations for each scheme is discounted by the AA corporate bond rates for bonds that have maturity dates approximating to the terms of the Group's obligations.

Where pension schemes from outside the Group are merged, the net fair value of assets and liabilities of the scheme transferred is recognised in the income statement.

Pension expense attributable to the Group's defined benefit plans comprises current service cost, interest cost, expected return on plan assets, curtailment gains and past service cost. The Group's policy where actuarial gains and losses arise as a result of actual experience is to fully recognise such amounts directly into retained earnings.

The Group also provides post retirement health care for certain retired employees. The calculation of the post retirement health care liability is calculated in the same manner as the defined benefit pension obligation.

Securitisation

Through its loan securitisation programme, the Group packages and sells loans (principally housing mortgage loans) as securities to investors through a securitisation vehicle.

All such financial instruments continue to be held on the Group balance sheet, and a liability recognised for the proceeds of the funding transaction, unless:

- a full or proportional share of all or specifically identified cash flows are transferred to the lender, in which case, the full amount or that proportion of the asset is derecognised; or

- substantially all the risks and returns associated with the financial instruments have been transferred, in which case, the assets are derecognised in full; or

- if a significant portion, but not all, of the risks and rewards have been transferred, the asset is derecognised entirely if the transferee has the practical ability to sell the financial asset or recognised only to the extent of the Group's continuing involvement in the asset.

2. Accounting policies (continued)

Income tax

Income tax expense or revenue is the tax payable (or receivable) on the current period's taxable income based on the applicable tax rate adjusted by changes in deferred tax assets and liabilities.

Deferred tax assets and liabilities are recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated Financial Statements. Deferred income tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled. A deferred tax asset or liability is not recognised if it arises from initial recognition of an asset or liability (in a transaction other than a business combination) that at the time of the transaction affects neither accounting profit nor taxable profit or loss.

Deferred tax assets are only recognised for temporary differences, unused tax losses and unused tax credits if it is probable that future taxable amounts will arise to utilise those temporary differences and losses.

Deferred liabilities are not recognised for temporary differences arising from investments in subsidiaries and associates where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the difference will not reverse in the foreseeable future. Deferred tax assets are not recognised for temporary differences arising from investments in subsidiaries and associates where it is probable that the difference will not reverse in the foreseeable future, and it is not probable that taxable profit will be available against which the temporary difference can be utilised.

The effects of income taxes arising from asset revaluation adjustments are recognised directly in the asset revaluation reserve where relevant.

Deferred tax assets and liabilities related to fair value re-measurement of cash flow hedges, which are charged or credited directly to equity, are also credited or charged directly to equity. The tax associated with these transactions will be recognised in the income statement at the same time as the underlying transaction.

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it is related to items recognised in equity, in which case the tax is also recognised in equity.

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

Subordinated debt and related entity balances

Subordinated debt and related entity balances are recorded at amortised cost.

Debt issues

Debt issues are short and long term debt issued by the Group including commercial paper, notes, term loans, medium term notes and residential mortgage backed securities. Debt issues are typically recorded at amortised cost using the effective interest method. Premiums, discounts and associated issue expenses are recognised using the effective interest method through the income statement from the date of issue to accrete the carrying value of securities to redemption values by maturity date. Interest is charged to the income statement using the effective interest method. Embedded derivatives within debt instruments must also be separately accounted for where not closely related to the terms of the host debt instrument. These embedded derivative instruments are recorded at fair value with gains and losses on the embedded derivative recorded in the income statement.

Where debt issues are classified as held at fair value through profit or loss they are initially recognised at fair value with transaction costs being recognised immediately in the income statement. Subsequently, they are measured at fair value and any gains and losses are recognised in the income statement as they arise.

2. Accounting policies (continued)

Netting

A financial asset and a financial liability shall be offset and the net amount presented in the balance sheet when, and only when, the Bank currently has a legally enforceable right to set off the recognised amounts and it intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Revenue and expense recognition

Net interest income

Interest income is reflected in the income statement using the effective interest method.

The effective interest method is a method of calculating amortisation using the effective interest rate of a financial asset or financial liability. The effective interest rate is the rate that exactly discounts the estimated stream of future cash payments or receipts over the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or liability.

When calculating the effective interest rate, the cash flows are estimated considering all contractual terms of the financial instrument (e.g. prepayment, call and similar options) excluding future credit losses.

The calculation of the effective interest rate includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts. Where it is not possible to estimate reliably the cash flows or the expected life of a financial instrument (or group of financial instruments), the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments) are used.

Loan origination fees are recognised as revenue over the life of the loan as an adjustment of yield. Commitment fees are deferred, and recognised over the life of the loan as an adjustment of yield, or if unexercised, recognised as revenue upon expiration of the commitment. Where commitment fees are retrospectively determined and nominal in relation to market interest rates on related loans, commitment fees are recognised as revenue when charged. Where the likelihood of exercise of the commitment is remote, commitment fees are recognised as revenue over the commitment period. Loan related administration and service fees are recognised as revenue over the period of service.

Direct loan origination costs are netted against loan origination fees and the net amount recognised as revenue over the life of the loan as an adjustment of yield. All other loan related costs are expensed as incurred.

Fees and commissions

Unless included in the effective interest calculation, fees and commissions are recognised on an accruals basis when the service has been provided. Fees and commissions not integral to the effective interest rate arising from services provided to customers and third parties are recognised once the service has been provided.

Commitment fees, together with related direct costs, for loan facilities where draw down is probable are deferred and recognised as an adjustment to the effective yield on the loan once drawn. Commitment fees in relation to facilities where draw down is not probable are recognised over the term of the commitment.

2. Accounting policies (continued)

Gains less losses on financial instruments at fair value through profit or loss

Gains less losses on financial instruments at fair value through profit or loss comprises fair value gains and losses from three distinct activities:

- trading financial instruments;
- hedging assets, liabilities and derivatives designated in hedge relationships; and
- financial assets and liabilities designated at fair value through profit or loss.

Trading financial instruments recognises fair value movements on all trading financial instruments. For trading derivatives a full fair value is determined inclusive of interest income and expense arising on those derivatives. Interest income and expense on trading securities is reported within interest income and not included in the fair value movement on these instruments.

Hedging assets, liabilities and derivatives designated in hedge relationships recognises fair value movements on both the hedged item and hedging derivative in a fair value hedge relationship, and hedge ineffectiveness for both fair value and cash flow hedge relationships.

Financial instruments designated at fair value through profit or loss recognises fair value movements (excluding interest) on those items designated as fair value through profit or loss at inception.

Interest income and interest expense on hedging assets, liabilities and derivatives and financial assets and liabilities designated as fair value through profit or loss at initial recognition are recognised in net interest income.

Equity based compensation

The Group engages in share-based payment transactions in respect of services received from certain of its employees. The fair value of the services received is measured by reference to the fair value of the shares or share options of NAB granted, on the date of the grant. The cost of the employee service received is measured by reference to the fair value of the shares or share options of NAB granted, on the date of the grant. The cost of the employee service received in respect of the shares or share options granted is recognised in the income statement over the period that the services are received by the Group, which is the vesting period, with a consequent increase in equity. The increase in share option reserve is reduced on repayment to the ultimate parent company.

The fair value of the options granted is determined using option pricing models, which take into account the exercise price of the option, the current share price, the risk free interest rate, the expected volatility of the NAB share price over the life of the option and other relevant factors. In the absence of market prices, the fair value of the instruments at the date of the grant is estimated using an appropriate valuation technique.

Except for those which include terms related to market conditions, vesting conditions included in the terms of the grant are not taken into account in estimating fair value.

Non market vesting conditions are taken into account by adjusting the number of share or share options included in the measurement of the cost of employee services so that ultimately, the amount recognised in the income statement reflects the number of vested shares or share options. Where vesting conditions are related to market conditions, the charges for the services received are recognised regardless of whether or not the market related vesting condition is met, provided that the non market vesting conditions are met.

2. Accounting policies (continued)

Accounting developments

During the year the International Accounting Standards Board and International Financial Reporting Interpretations Committee issued the following standards and interpretations with an effective date after the date of these Financial Statements:

International Financial Reporting Standards (IAS/IFRS)		***Effective Date: Annual periods beginning on or after***
Various	Improvements to IFRS (Issued 22 May 2008)	Various, earliest is 1 January 2009
Various	Improvements to IFRS (Issued 16 April 2009) (i)	Various, earliest is 1 July 2009
IFRS 1	Amendment - Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate	1 January 2009
IFRS 1	Amendment - Additional Exemptions for First-time Adopters (i)	1 January 2009
IFRS 1	Revised - First Time Adoption of IFRS	1 July 2009
IFRS 2	Amendment - Vesting Conditions and Cancellations (i)	1 January 2009
IFRS 2	Amendment - Group Cash-settled Share-based Payment Transactions (i)	1 January 2010
IFRS 3	Revised - Business Combinations	1 July 2009
IFRS 7	Amendment - Improving Disclosures about Financial Instruments (i)	1 July 2008
IFRS 8	Operating Segments	1 January 2009
IFRS 9	Financial Instruments (i)	1 January 2013
IAS 1	Revised - Presentation of Financial Statements	1 January 2009
IAS 1	Amendment - Puttable Financial Instruments and Obligations Arising on Liquidation	1 January 2009
IAS 23	Revised - Borrowing costs	1 January 2009
IAS 24	Revised - Related Party Disclosures (i)	1 January 2011
IAS 27	Amendment - Consolidated and Separate Financial Statements	1 July 2009
IAS 27	Amendment - Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate	1 January 2009
IAS 32	Amendment - Puttable Financial Instruments and Obligations Arising on Liquidation	1 January 2009
IAS 32	Classification of Rights Issues (i)	1 February 2010
IAS 39	Amendment - Eligible Hedged Items	1 July 2009
IAS 39	Amendment - Embedded Derivatives	30 June 2009

2. Accounting policies (continued)

Accounting developments (continued)		***Effective Date: Annual periods beginning on or after***
International Financial Reporting Interpretations Committee (IFRIC)		
IFRIC 9	Amendment - Embedded Derivatives (i)	30 June 2009
IFRIC 14	Amendment - Prepayment of a Minimum Funding Requirement (i)	1 January 2011
IFRIC 15	Agreements for the Construction of Real Estate	1 January 2009
IFRIC 17	Distributions of Non-Cash Assets to Owners (i)	1 July 2009
IFRIC 18	Transfer of Assets from Customers (i)	1 July 2009
IFRIC 19	Extinguishing Financial Liabilities with Equity Instruments (i)	1 July 2010

(i) This standard/interpretation has not yet been adopted by the European Union.

The Bank has not early adopted these standards and interpretations. The Directors do not anticipate any material impacts as a result of adoption of these standards and interpretations.

3. Nature of business and segmental reporting

For the purposes of this note a business segment is a distinguishable component of the entity that is engaged in providing groups of related products and services and that is subject to risks and returns that are different from those of other business segments. Separate financial information for each segment is reported to the UK Executive Committee for the purposes of evaluating performance.

The Group's business is organised into two main operating segments: Financial Services UK and nabCapital. Financial Services UK is the retailing arm of the Group, providing a full range of financial services to customers. nabCapital is responsible for the Group's relationships with large corporations and institutions. However, corporate lending is to be integrated with the regional business banking operations going forward as part of the new National Australia Bank ("NAB") strategy. The Group will report on this basis for the 2010 financial year.

Revenue and expenses directly associated with each business segment are included in determining their result. Segment revenue represents revenue directly attributable to a segment and a portion of the Group's revenue that can be allocated to a segment on a reasonable basis. Segment result represents segment revenue less segment expenses and impairment losses on credit exposures and after income taxes. The Group allocates all of its assets and liabilities to business segments.

2009	Financial Services UK £m	nabCapital £m	Total £m
Net interest income	842	3	845
Non interest income	237	40	277
Segment revenue	1,079	43	1,122
Segment result	11	37	48
Tax expense			(14)
Profit for the financial year			34
Total assets	42,038	332	42,370
Total liabilities	40,104	16	40,120
Other segment items			
Acquisition of property, plant & equipment	52	-	52
Depreciation of property plant & equipment	23	-	23
Share based payments	15	-	15
Impairment losses:			
Recognised in income statement	396	3	399
Amounts written off	395	-	395
Recoveries of amounts written off in previous years	52	-	52

The Clydesdale Bank Money Market desk, which issues Commercial Paper and Certificates of Deposits and raises interbank and corporate deposits, was transferred from nabCapital to UK Treasury; also part of Financial Services UK. UK Treasury is responsible for wholesale funding and liquidity management within Clydesdale and the transfer is therefore consistent with these objectives.

3. Nature of business and segmental reporting (continued)

2008	**Financial Services UK**	**nabCapital**	**Total**
Net interest income	**£m**	**£m**	**£m**
Non interest income			
Net significant revenue	868	28	896
Segment revenue	296	28	324
	4	-	4
Segment result	1,168	56	1,224
Tax expense	303	47	350
Profit for the financial year			(103)
			247
Total assets	40,334	1,642	41,976
Total liabilities	32,557	7,255	39,812
Other segment items			
Acquisition of property, plant & equipment	78	-	78
Depreciation of property plant & equipment	26	-	26
Share based payments	12	-	12
Impairment losses:			
Recognised in income statement	174	5	179
Amounts written off	190	-	190
Recoveries of amounts written off in previous years	56	-	56

The outcome of a Group strategic review during 2008 resulted in a number of nabCapital regional client portfolios being transferred to Clydesdale's Corporate & Acquisition Finance business, which is an integral part of Financial Services UK, under Clydesdale/Yorkshire branding.

Geographical segments

The Group has no material segments outwith the UK and thus no secondary geographical segment information is presented.

4. Net interest income

	2009 £m	2008 £m
Interest income		
Loans and advances to other banks	**94**	97
Investments	**30**	55
Loans and advances to customers	**1,359**	1,844
Due from related entities	**15**	69
Financial assets at fair value through profit or loss	**224**	328
Total interest income	**1,722**	2,393
Interest expense		
Due to other banks	**61**	129
Due to customers	**494**	805
Bonds and notes	**195**	322
Due to related entities	**124**	231
	874	1,487
Financial liabilities at fair value through profit or loss	**3**	10
Total interest expense	**877**	1,497
Net interest income	**845**	896

Included within interest income is a net gain of £38m recognised on the purchase by Clydesdale Bank PLC of notes issued by Lanark Master Trust (the Bank's own securitisation vehicle - refer note 16).

5. Non interest income

	2009 £m	2008 £m
Gains less losses on financial instruments at fair value through profit or loss		
Foreign exchange derivatives	**23**	9
Interest rate derivatives	**(248)**	(84)
Other derivatives	**4**	-
Movement in fair value of assets and liabilities	**245**	80
Ineffectiveness arising from fair value hedges	**2**	4
Ineffectiveness arising from cash flow hedges	**(17)**	22
	9	31
Other operating income		
Fee and commission income	**261**	268
Operating lease income	**-**	4
Other income	**7**	21
	268	293
Total non interest income	**277**	324

Certain financial assets are designated at inception as fair value through profit or loss. These assets are predominantly fixed interest rate loans which are individually hedged. The fair value of these fixed rate loans will increase as interest rates fall and decrease as interest rates rise. Corresponding opposite movements in the underlying derivatives are shown in the interest rate derivatives line.

On 22 October 2008, Kerala Investments Limited (a subsidiary of CB Group Investments Limited) was disposed to Morgan Stanley & Co International plc. The net proceeds received were £2m resulting in a net gain on disposal of £2m. This gain is included in Other income.

6. Operating expenses

	2009 £m	2008 £m
Personnel expenses		
Salaries, wages and non cash benefits	**169**	186
Related personnel expenses	**17**	17
Defined contribution pension expense	**6**	5
Defined benefit pension expense/(credit)	**1**	(21)
Employee share compensation	**15**	12
Other personnel expenses	**8**	12
	216	211
Depreciation expense		
Depreciation of property, plant & equipment (note 18)	**23**	26
Other operating expenses		
Operating lease rental	**36**	31
Other occupancy expenses	**33**	34
Related entity recharges	**249**	304
Other operating expenses	**101**	89
Total operating expenses	**658**	695

Auditors' remuneration

The Group paid the following amounts to its auditors in respect of the audit of the Financial Statements and for other services provided to the Group.

	2009 £'000	2008 £'000
Audit of the Financial Statements	**812**	790
Other fees to auditors:		
Audit of the Group pension schemes	**64**	50
Local statutory audits for subsidiaries	**138**	126
Other assurance	**53**	229
	1,067	1,195

Efficiency, quality and service initiative costs

The following expenses have been disclosed as a separate line item on the income statement.

	2009 £m
Other personnel expenses	**12**
Other occupancy expenses	**3**
Other expense	**7**
	22

7. Tax expense

a) Analysis of charge in the period

Tax charged in the income statement

The charge for taxation comprises:	**2009 £m**	2008 £m
Current tax		
United Kingdom corporation tax at 28% (2008: 29%)		
- current year	**(12)**	47
Other overseas taxation	**16**	28
Total current tax	**4**	75
Deferred tax		
Origination and reversal of temporary differences		
- current year	**11**	25
- prior year	**(1)**	3
Total deferred income tax	**10**	28
Income tax expense reported in income statement	**14**	103

Tax relating to items charged or credited to equity

	2009 £m	2008 £m
Current tax		
Available for sale investments	**5**	-
Release of transitional deferred tax	**(8)**	(6)
Deferred tax asset		
Actuarial gains and losses on post retirement benefits	**(165)**	-
Employee share compensation	**(2)**	4
Release of transitional deferred tax	**8**	6
Deferred tax liability		
Net gain on revaluation of cash flow hedges	**36**	8
Asset revaluation reserve	**(2)**	-
Tax (credit)/charge in the statement of recognised income and expense	**(128)**	12

7. Tax expense (continued)

b) Factors affecting tax charge for the period

The tax assessed for the period reflects the standard rate of corporation tax in the UK (28%). The factors are explained below:

	2009	2008
	£m	£m
Profit on ordinary activities before tax	**48**	350
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK of 28% (2008: 29%)	**13**	101
Effects of:		
Expenses not deductible for tax purposes	**5**	4
Amounts not subject to UK tax	**(5)**	(3)
Rate differences	**-**	(1)
Adjustments to tax charge in respect of previous periods	**(1)**	3
Other	**2**	(1)
Total income tax charge for period	**14**	103

On 1 April 2008, the UK tax rate was reduced from 30% to 28%. The rate differences adjustment reflects the impact on the deferred tax balances held.

8. Dividends paid

	2009	2008
	£m	£m
2009 interim preference dividend paid - 12% per annum payable semi-annually (6p per share)	**6**	-
2007 final ordinary dividends paid - 40.95p per share	**-**	95
	6	95

9. Cash and balances with central banks

	Group		**Bank**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Cash assets	**82**	153	**82**	153
Balances with central banks	**2,631**	4,956	**2,631**	4,956
	2,713	5,109	**2,713**	5,109

Balances with central banks include mandatory deposits of £27m (2008: £26m) which are not available for use in the Group's day to day business.

9. Cash and balances with central banks (continued)

Cash collateral on securities borrowed and reverse repurchase agreements

Group and Bank	**2009**	2008
	£m	£m
Cash collateral on reverse repo agreements	**1,582**	802
Other assets used as collateral:		
For loans at fair value through profit or loss	**55**	39
	1,637	841

As part of the reverse repurchase and securities borrowing agreements, the Group has received securities that it is allowed to sell or repledge. No securities held under the reverse repurchase agreements have been sold or re-pledged to third parties in connection with financing activities or to comply with commitments under short sale transactions.

The Group is obliged to return equivalent securities on maturity of the transaction. The associated liability to return these securities is included in derivative financial liabilities. These transactions are conducted under terms that are usual and customary to standard lending, securities borrowing and lending activities.

10. Due from other banks

	Group		**Bank**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Transaction balances with other banks	**16**	20	**15**	13
Loans and advances	**-**	500	**-**	-
Placements with other banks	**324**	2	**324**	1
	340	522	**339**	14

The Bank has increased its placements with other banks in the current year as part of the growth of its liquid asset portfolio.

11. Derivative financial instruments

Use of derivatives

The Group uses derivatives to hedge its balance sheet. The Group's principal objective in holding or issuing derivatives is asset and liability management.

The operations of the Group are subject to the risk of interest rate fluctuations, to the extent that there is a difference between the amount of the interest-earning assets and the amount of interest-bearing liabilities that mature or reprice in specified periods. One of the objectives of asset and liability management is to protect levels of net interest income, while maintaining acceptable levels of liquidity to meet the Group obligations as they fall due.

To achieve these objectives, the Group uses a combination of derivative financial instruments, including foreign exchange forward rate agreements, swaps, options, caps, floors, and other contingent contracts. The hedges transacted within the Group are entered into with NAB. Provided IAS 39 cash flow hedging criteria are met, the fair value changes on the related hedging instruments that are deemed effective are deferred in the cash flow reserve and transferred to the income statement at the time the hedged item affects income. Hedge effectiveness is monitored, and any hedge ineffectiveness is recognised in the income statement immediately.

Subsequent to initial designation, changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The movement in fair value of the hedged item attributable to the hedged risk is made as an adjustment to the carrying value of the hedged asset or liability.

The Group does not have a trading book. However, certain historical derivatives do not meet the IAS39 hedging criteria and are accounted for as trading derivatives. The residual volume of these derivatives is gradually reducing over time as deals mature and their mark to market directly impacts income.

Derivatives

A derivative financial instrument is a contract or agreement whose value is related to the value of an underlying instrument, reference rate or index. Derivatives are usually separated into three generic classes: forward and futures contracts, options, and swaps, although individual products may combine the features of more than one class. The principal features of each of these classes, for derivatives that the Group enters into, are summarised below.

Forward and futures contracts

Forward and futures contracts are contracts for delayed delivery of a specific underlying asset in which the seller agrees to settle at a specified future date at a specified price or yield. A forward rate agreement is a confirmed agreement between two parties to exchange an interest rate differential on a notional principal amount at a given future date.

Options

Options are contracts that allow the holder of the option the right, but not the obligation, to purchase or sell a financial instrument at a specified price and within a specified period. Interest rate caps and floors are option contracts and are included as such in the disclosures below. They require the seller to pay the purchaser at specified future dates the amount, if any, by which a specified market interest rate exceeds the fixed cap rate or falls below the fixed floor rate, applied to the notional principal amount.

Swaps

Interest rate swap transactions generally involve the exchange of fixed and floating interest payment obligations without the exchange of the underlying notional principal amount. A vanilla cross currency swap takes the form of an agreement to exchange one currency for another and to re-exchange the currencies at the maturity of the swap, using the same exchange rate, with the exchange of interest payments throughout the swap period. A balance guarantee cross currency swap protects the Group if securitisation amortisation payment frequencies change.

11. Derivative financial instruments (continued)

Use of derivatives (continued)

Other financial instruments
In addition to derivatives, various financial instruments, for example loans and advances, deposits, debt securities, trade debtors and creditors and accruals, arise directly from the Group's operations. Where the fair value of these differ from the book value details are given in note 39 to the Financial Statements. The disclosures in these notes include all short-term debtors and creditors.

Risk Management
The Group's management of certain key risk factors that may impact the future results is discussed in note 42 on pages 109 to 112. The factors discussed should not be considered to be the complete list of all potential risks.

Derivative contracts are disclosed as follows:

Group

	Fair Value		Fair Value	
	Assets	**Liabilities**	Assets	Liabilities
	2009	**2009**	2008	2008
	£m	**£m**	£m	£m
Derivative financial assets and liabilities	**942**	**113**	602	36
Other derivative financial assets and liabilities at fair value through profit or loss (note 12)	**271**	**1**	136	165
Derivative financial assets and liabilities at fair value - related entities (note 12)	**183**	**535**	169	214
	1,396	**649**	907	415

Bank

	Fair Value		Fair Value	
	Assets	**Liabilities**	Assets	Liabilities
	2009	**2009**	2008	2008
	£m	**£m**	£m	£m
Derivative financial assets and liabilities	**424**	**113**	270	36
Other derivative financial assets and liabilities at fair value through profit or loss (note 12)	**271**	**1**	136	165
Derivative financial assets and liabilities at fair value - related entities (note 12)	**183**	**535**	169	214
	878	**649**	575	415

Certain derivative financial assets and liabilities have been booked in consolidated special purpose vehicles.

Derivative financial assets and liabilities held at fair value through profit or loss (FVTPL) include the hedges for the Group Securitisation programme, Medium Term Note ("MTNs") programmes and Cash flow hedges.

The carrying value of the currency liabilities issued through securitisation and MTN programmes has increased as a result of foreign exchange movements. There is a corresponding increase in the value of the hedging derivative.

The carrying value of the Cash flow hedge derivatives has increased as LIBOR yield curves used to discount the future cashflow have reduced. There is a corresponding increase (after tax) in the Cashflow hedge reserve.

Derivative financial assets and liabilities that cannot be held in a hedge relationship are deemed to be held for trading.

11. Derivative financial instruments (continued)

Group

	Contract Amount 2009 £m	**Fair Value Assets 2009 £m**	**Fair Value Liabilities 2009 £m**	Contract Amount 2008 £m	Fair Value Assets 2008 £m	Fair Value Liabilities 2008 £m
Total derivatives held						
Foreign exchange rate related contracts						
Spot, forwards and futures	**4,352**	**115**	**35**	3,160	28	-
Currency swaps	**2,818**	**640**	**4**	2,967	449	1
Options	**276**	**6**	**6**	324	4	4
Total	**7,446**	**761**	**45**	6,451	481	5
Interest rate related contracts						
Forward rate agreements	**-**	**-**	**-**	111	-	-
Swaps	**26,995**	**604**	**532**	28,004	405	370
Swaptions	**1,276**	**22**	**9**	532	6	7
Options	**1,718**	**7**	**59**	2,661	14	29
Total	**29,989**	**633**	**600**	31,308	425	406
Credit derivatives	**200**	**-**	**2**	200	-	3
Commodity derivatives	**26**	**2**	**2**	14	1	1
	226	**2**	**4**	214	1	4
Total derivative contracts	**37,661**	**1,396**	**649**	37,973	907	415

Bank

	Contract Amount 2009 £m	**Fair Value Assets 2009 £m**	**Fair Value Liabilities 2009 £m**	Contract Amount 2008 £m	Fair Value Assets 2008 £m	Fair Value Liabilities 2008 £m
Total derivatives held						
Foreign exchange rate related contracts						
Spot, forwards and futures	**4,352**	**115**	**35**	3,160	28	-
Currency swaps	**1,108**	**166**	**4**	1,146	163	1
Options	**276**	**6**	**6**	324	4	4
Total	**5,736**	**287**	**45**	4,630	195	5
Interest rate related contracts						
Forward rate agreements	**-**	**-**	**-**	111	-	-
Swaps	**26,495**	**560**	**532**	25,854	359	370
Swaptions	**1,276**	**22**	**9**	532	6	7
Options	**1,718**	**7**	**59**	2,661	14	29
Total	**29,489**	**589**	**600**	29,158	379	406
Credit derivatives	**200**	**-**	**2**	200	-	3
Commodity derivatives	**26**	**2**	**2**	14	1	1
	226	**2**	**4**	214	1	4
Total derivative contracts	**35,451**	**878**	**649**	34,002	575	415

11. Derivative financial instruments (continued)

Cash flow hedges

Included in the derivative tables on the previous page are the following cash flow hedge derivatives:

	Contract Amount 2009 £m	**Fair Value Assets 2009 £m**	**Fair Value Liabilities 2009 £m**	Contract Amount 2008 £m	Fair Value Assets 2008 £m	Fair Value Liabilities 2008 £m
Interest rate-related contracts	**15,420**	**259**	**113**	17,086	193	156

The Group macro hedges its interest rate exposure using cash flow hedges. These are vanilla fixed rate interest rate swaps for which the Group has the following commitments in the time bands noted:

Nominal values per time period	**2009 £m**	2008 £m
0 to 6 months	**6,070**	4,571
6 to 12 months	**2,713**	1,320
1 to 2 years	**4,077**	3,783
2 to 5 years	**2,560**	7,412
	15,420	17,086

The Group has hedged the following forecast cash flows, which primarily vary with interest rates. These cash flows are expected to impact the income statement in the following periods, excluding any hedge adjustments that may be applied:

	Forecast receivable cash flows 2009 £m	**Forecast payable cash flows 2009 £m**	Forecast receivable cash flows 2008 £m	Forecast payable cash flows 2008 £m
- within one year	**14**	**259**	110	283
- between one and two years	**30**	**148**	71	135
- between two and three years	**17**	**79**	64	123
- between three and four years	**1**	**30**	22	55
- between four and five years	**-**	**9**	1	11
	62	**525**	268	607

	2009 £m	2008 £m
(Loss)/Gain from cash flow hedges recognised in the income statement due to hedge ineffectiveness	**(17)**	22

11. Derivative financial instruments (continued)

Fair value hedges

In addition the Group has the following fair value hedges that are designated as sterling interest rate related swaps:

Nominal values per time period	**2009 £m**	2008 £m
0 to 6 months	**-**	200
6 to 12 months	**-**	-
1 to 2 years	**250**	-
2 to 5 years	**1,650**	2,450
	1,900	2,650

The 30 September 2008 comparatives has been restated to accord with the 2009 balances reported. The analysis is provided based on expected maturity.

Finally the Group has the following fair value hedges that are designated as cross currency related swaps:

		2009 £m	2008 £m
Nominal values per time period			
0 to 6 months	Exchange rate £/Euro = 1.0972	**175**	-
0 to 6 months	Exchange rate £/USD = 1.6044	**387**	-
6 to 12 months	Exchange rate £/Euro = 1.0972	**-**	493
6 to 12 months	Exchange rate £/USD = 1.6044	**-**	142
6 to 12 months	Exchange rate £/JPY = 144.0523	**-**	53
2 to 5 years	Exchange rate £/Euro = 1.0972	**1,301**	1,299
2 to 5 years	Exchange rate £/USD = 1.6044	**612**	947
		2,475	2,934

Gains or (losses) arising from fair value hedges	**2009 £m**	2008 £m
Hedging instrument	**267**	429
Hedged item attributable to the hedged risk	**(265)**	(425)
	2	4

The 30 September 2008 comparative figures were incorrectly presented between the hedging instrument and the hedged item attributable to the hedged risk. There is no change to the overall gain arising from the fair value hedges.

12. Other financial assets and liabilities at fair value

Group and Bank	2009 £m	2008 £m
Financial assets at fair value through profit or loss		
Loans and advances	**5,327**	3,772
Securities	**202**	199
	5,529	3,971
Hedging derivatives		
Other derivative financial assets (note 11)	**271**	136
Derivative financial assets - related entities (note 11)	**183**	169
	454	305
	5,983	4,276
Financial liabilities at fair value through profit or loss		
Due to customers - term deposits	**61**	174
Hedging derivatives		
Other derivative financial liabilities (note 11)	**1**	165
Derivative financial liabilities - related entities (note 11)	**535**	214
	536	379
	597	553

Loans and advances to customers

Included in other financial assets at fair value is a portfolio of loans which have embedded derivative characteristics. These loans are hedged with interest rate derivative contracts with matching cash flows. The hedges do not achieve the criteria for hedge accounting and the loans are recorded at fair value to avoid an accounting mismatch. The maximum credit exposure of the loans is £5,327m (2008: £3,772m). The cumulative movement in fair value of the loans attributable to changes in credit risk amounts to £110m (2008: £80m) and the change for the current year is £30m (2008: £30m).

The changes in fair value of the designated loans attributable to credit risk have been calculated by determining the changes in credit spreads above the market interest rates, established through a statistical based calculation used to estimate expected losses attributable to adverse movements in credit risk.

Due to customers - Term deposits

Included in other financial liabilities at fair value are fixed rate defeasance deposits which have been hedged with interest rate derivative contracts with matching cash flows.

The change in fair value attributable to changes in the Bank credit risk is £Nil (2008:£Nil). The Bank is contractually obligated to pay £6m (2008: £1m) less than the carrying amount at maturity to the deposit holder.

13. Investments

	Group		Bank	
	2009 £m	2008 £m	**2009 £m**	2008 £m
Available for sale - listed	**1,531**	-	**1,531**	-
Available for sale - unlisted	**10**	6	**10**	6
Held to maturity - listed	**639**	1	**945**	1
	2,180	7	**2,486**	7

Included in the Available for sale ("AFS") listed securities at 30 September 2009 are £1.4bn investments in other banks' debt securities, which are subject to a UK Government backed guarantee. These are held as AFS investments as part of the Bank's liquid asset portfolio.

14. Loans and advances to customers

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Overdrafts	**4,236**	4,779	**4,236**	5,258
Credit cards	**521**	543	**521**	543
Lease finance	**1,248**	1,533	**591**	757
Housing loans	**12,327**	11,868	**8,208**	8,002
Other term lending - non retail	**8,226**	9,104	**8,226**	9,104
Other term lending - retail	**1,247**	1,489	**1,247**	1,489
Other lending	**11**	2	**11**	3
Gross loans and advances to customers	**27,816**	29,318	**23,040**	25,156
Unearned income	**(290)**	(330)	**(290)**	(330)
Deferred and unamortised fee income	**(43)**	(52)	**(37)**	(47)
Impairment provisions on credit exposures (note 15)	**(336)**	(280)	**(320)**	(273)
	27,147	28,656	**22,393**	24,506

The Group and Bank have transferred £2,446m and £1,420m respectively (2008: £2,910m and £1,640m respectively) of housing loans through securitisation arrangements that do not qualify for derecognition from the balance sheet (note 16).
The housing loans do not qualify for derecognition because the Group and Bank remain exposed to the risks and rewards of ownership on an ongoing basis. The Group and Bank continue to be exposed primarily to the liquidity risk, interest rate risk and credit risk of the housing loans. The Group is also exposed to the residual rewards of the housing loans as a result of its ability to benefit from the future performance of the housing loans through the receipt of deferred consideration.

The carrying amount of the associated liability is £2,343m (2008: £2,867m).

Included within Group and Bank loans and advances to customers are £2,614m and £1,763m respectively (2008: nil) of housing loans assigned to a bankruptcy remote special purpose entity, Clydesdale Covered Bonds LLP. These loans provide security for issues of covered bonds made by Clydesdale Bank PLC. These transactions do not qualify for derecognition from the balance sheet. During the period, Clydesdale Bank PLC issued £2,450m of covered bonds, under its covered bond programme, which were held by Clydesdale Bank PLC at 30 September 2009. Accordingly no accounting entries are required in these Financial Statements.

Lease Finance
The bank leases a variety of assets to third parties under operating and finance lease arrangements, including vehicles and general plant and machinery.

The costs of assets acquired by the Group during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £7m (2008: £28m) and £510m (2008: £1,013m) respectively. The total closing balances of finance leases and hire purchase contracts were £37m (2008: £47m) and £1,116m (2008: £1,335m) respectively.

Loans and advances to customers include finance lease receivables, which may be analysed as follows:

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Gross investment in finance lease receivables:				
Due within one year	**518**	657	**269**	324
Due within one to five years	**685**	853	**312**	422
Due after more than five years	**45**	23	**10**	11
Total gross investment in lease finance receivables	**1,248**	1,533	**591**	757
Deduct: Unearned future finance income on lease receivables	**(90)**	(99)	**(90)**	(99)
Net investment in lease finance	**1,158**	1,434	**501**	658

14. Loans and advances to customers (continued)

There are specific provisions of £7.6m (2008: £2.9m) in relation to finance lease receivables, with a collective provision of £3.1m (2008: £2.5m) as at 30 September 2009.

Maximum exposure to credit risk
The amounts disclosed are the maximum exposure to credit risk of “Loans and advances”, before taking account of any collateral held or other credit enhancements unless such credit enhancements meet offsetting requirements set out in note 40. For financial assets recognised on the balance sheet, the exposure to credit risk equals their carrying amount.

For financial guarantees granted, the maximum exposure to credit risk is the maximum amount that the Group would have to pay if the guarantees are called upon. For loan commitments and other credit related commitments that are irrevocable over the life of the respective facilities, the maximum exposure to credit risk is the full amount of the committed facilities.

Description of collateral held as security and other credit enhancements
The Group evaluates each customer’s creditworthiness on a case by case basis. The amount of collateral obtained, if deemed necessary by the Group upon extension of credit, is based on management’s credit evaluation of the counterparty. Collateral held varies, but may include:
- a floating charge over all assets and undertakings of an entity, including uncalled capital and called but unpaid capital;
- specific or interlocking guarantees;
- specific charges over defined assets of the counterparty; and
- loan agreements which include affirmative and negative covenants and in some instances guarantees of counterparty obligations.

Distribution of loans and advances by credit quality	**Non retail**		**Retail**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Group				
Gross loans and advances:				
Neither past due nor impaired	**12,672**	14,593	**13,634**	13,448
Past due but not impaired	**562**	638	**448**	438
Impaired	**487**	187	**13**	14
	13,721	15,418	**14,095**	13,900
Bank				
Gross loans and advances:				
Neither past due nor impaired	**12,119**	14,423	**9,686**	9,602
Past due but not impaired	**487**	548	**285**	418
Impaired	**458**	155	**5**	10
	13,064	15,126	**9,976**	10,030

Restructured/renegotiated loans
There has been one loan of £0.5m (2008: none) that has had its terms renegotiated that would otherwise have been past due or impaired .

Credit quality of loans and advances
The Group has an internally developed credit rating system that uses data drawn from a number of sources to assess the potential risk in lending to the Bank's customers. The Group has a single common masterscale across all non-retail counterparties for Probability of Default. This probability of default masterscale can be broadly mapped to external rating agencies and has performing (pre-default) and non performing (post-default) grades. Impaired assets consist of non-retail loans (excludes credit card loans and portfolio managed facilities) which have been individually assessed and there is sufficient doubt about the ultimate collectability of principal and interest with security insufficient to cover principal and interest.

Unsecured portfolio managed facilities are classified as impaired when they become 180 days past due (if not written off).

14. Loans and advances to customers (continued)

Distribution of loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the Group's standard credit rating system. The credit rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy.

The table below presents the analysis of non retail credit quality of loans and advances that are neither past due nor impaired:

	Non retail	
	2009	2008
	£m	£m
Group		
Senior investment grade	**1,211**	987
Investment grade	**1,884**	2,629
Sub investment grade	**9,577**	10,977
	12,672	14,593
Bank		
Senior investment grade	**1,153**	944
Investment grade	**1,847**	2,517
Sub investment grade	**9,119**	10,962
	12,119	14,423

For the non-retail analysis, Investment Grades are determined by the Customer Rating System (eCRS) as defined under the Credit Risk Management Policy.

- Senior Investment Grade is eCRS Ratings 1 to 5.
- Investment Grade is eCRS Ratings 6 to 11.
- Sub-investment Grade is eCRS Ratings 12 to 23.

These ratings were applied based on the Group determined eCRS distribution curve utilising UK sourced data. The results of this are then applied to the Loans and Advances to determine the allocation between investment grades.

There are no eCRS ratings available for Retail loans and advances as these loans and advances are not risk rated on this basis, rather an overall portfolio profile basis is applied.

Loans and advances which were past due but not impaired	**Non retail**		**Retail**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Group				
1 to 29 days past due	**401**	501	**146**	171
30 to 59 days past due	**15**	57	**104**	120
60 to 89 days past due	**4**	22	**56**	51
Past due over 90 days	**142**	58	**142**	96
	562	638	**448**	438
Bank				
1 to 29 days past due	**347**	420	**90**	171
30 to 59 days past due	**13**	50	**64**	120
60 to 89 days past due	**2**	22	**36**	51
Past due over 90 days	**125**	56	**95**	76
	487	548	**285**	418

Loans and advances that are past due but are not impaired are classified as such where the net current market value of supporting security is sufficient to cover all principal, interest and other amounts (including legal, enforcement, realisation costs etc.) due on the facility.

15. Impairment provisions on credit exposures

	Non retail		Retail		
Group	**Specific**	**Collective**	**Specific**	**Collective**	**Total**
2009	**£m**	**£m**	**£m**	**£m**	**£m**
Opening balance	41	164	5	70	280
Transfer to/from specific provision	258	(258)	103	(103)	-
Charge for the year	-	284	-	115	399
Amounts written off	(245)	-	(150)	-	(395)
Recoveries of amounts written off in previous years	-	-	52	-	52
Closing balance	54	190	10	82	336
Group					
2008					
Opening balance	18	150	-	72	240
Transfer to/from specific provision	45	(45)	122	(122)	-
Charge for the year	-	59	-	120	179
Amounts written off	(17)	-	(173)	-	(190)
Recoveries of amounts written off in previous years	-	-	56	-	56
Other	(5)	-	-	-	(5)
Closing balance	41	164	5	70	280

15. Impairment provisions on credit exposures (continued)

	Non retail		Retail		
Bank	**Specific**	**Collective**	**Specific**	**Collective**	**Total**
2009	**£m**	**£m**	**£m**	**£m**	**£m**
Opening balance	40	158	5	70	273
Transfer to/from specific provision	239	(239)	98	(98)	-
Charge for the year	-	273	-	110	383
Amounts written off	(239)	-	(149)	-	(388)
Recoveries of amounts written off in previous years	-	-	52	-	52
Closing balance	40	192	6	82	320

	Non retail		Retail		
Bank	**Specific**	**Collective**	**Specific**	**Collective**	**Total**
2008	**£m**	**£m**	**£m**	**£m**	**£m**
Opening balance	17	144	-	72	233
Transfer to/from specific provision	44	(44)	122	(122)	-
Charge for the year	-	58	-	120	178
Amounts written off	(16)	-	(173)	-	(189)
Recoveries of amounts written off in previous years	-	-	56	-	56
Other	(5)	-	-	-	(5)
Closing balance	40	158	5	70	273

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Amounts included in				
Loans and advances to customers (note 14)	**336**	280	**320**	273
Non accrual loans				
Loans and advances to customers	**500**	201	**492**	198
Provisions	**(64)**	(46)	**(51)**	(44)
Total	**436**	155	**441**	154

16. Securitisation

Securitised advances are subject to non-recourse finance arrangements. These loans have been transferred at principal value to an special purpose entity (SPE) from Clydesdale Bank PLC, and have been funded through the issue of amortising mortgage backed securities to wholesale market investors. The transfer did not meet the derecognition tests in IAS39. The Group's and Bank's balance sheets include the results, assets and liabilities of securitisation SPEs on a line by line basis.

The balance of assets and liabilities in relation to securitisation notes in issue at 30 September 2009 within the Group's balance sheet are as follows:-

	2009	2008
	£m	£m
Assets		
Cross currency swaps on bonds and notes	**475**	286
Loans & advances to customers (note 14)	**2,446**	2,910
Accrued interest receivable	**15**	40
	2,936	3,236
Liabilities		
Bonds and notes	**2,343**	2,867
Accrued interest payable	**7**	24
	2,350	2,891

The balance of assets and liabilities in relation to securitisation notes in issue at 30 September 2009 within the Bank's balance sheet are as follows:-

	2009	2008
	£m	£m
Assets		
Loans & advances to customers (note 14)	**1,420**	1,640
Accrued interest receivable	**3**	6
Other assets	**907**	1,187
	2,330	2,833
Liabilities		
Due to related entities	**2,204**	2,586

At 30 September 2009 the SPEs had cash deposits with Clydesdale Bank PLC amounting to £53m (2008: £150m). This balance is restricted in use to the repayment of the debt securities issued by the SPEs and other legal obligations.

The 30 September 2008 comparative figure for Bank other assets has been restated from £144m to £1,187m and the Bank due to related entities figure has been restated from £1,337m to £2,586m following the adoption of a revised approach to the disclosure.

The Bank initiated two public tender offer processes during 2009 to purchase Lanark notes: one in March 2009 (where £20m and €94m and US $99m were tendered) and one in June 2009 (where €85m and £40m were tendered). These securities are all Triple A rated and attract a 20% risk weighting on a Standardised capital basis. In September 2009 CB plc undertook a private market purchase to acquire Lanark subordinate RMBS of which £100,000 (GBP) of class Single-A rated notes, €16m (EUR) Triple-B rated notes and a further £46m (GBP) Triple-B rated notes were successfully purchased. The Single-A rated notes attract a 50% risk weighting and the Triple-B rated notes attract a 100% risk weighting on a standardised capital basis.

17. Investments in controlled entities and associates

	Group		Bank	
	2009	2008	**2009**	2008 As restated
	£m	£m	**£m**	£m
At 30 September	**2**	2	**617**	617

The associated undertaking is The Scottish Agricultural Securities Corporation PLC, its country of registration and operations being Scotland. The associated undertaking's principal activity is in the provision of finance and the Group's interest of 33.33% in the issued equity capital of £2,000,000 is held by the Bank. The associated undertaking has a 31 March year end. The investment is equity accounted.

The 30 September 2008 comparative figure for investments in controlled entities and associates has been restated from £37m to £617m following a £580m reallocation of the investment in Yorkshire Bank Investments Limited. This was previously included within amounts due from controlled entities.

Principal controlled entities at 30 September 2009	**Nature of business**	**Country of incorporation and principal operations**
Clydesdale Bank Asset Finance Limited	Leasing and hire purchase	Scotland
Yorkshire Bank Home Loans Limited	Mortgage finance	England
Yorkshire Bank Investments Limited	Investment holding	England

All the principal subsidiary undertakings are wholly owned by the Bank. Details of all subsidiary undertakings will be annexed to the next Annual Return of the Bank.

The following companies are SPEs established in connection with the Bank's and Group's securitisation programme (see note 16). Although the Bank has no direct or indirect ownership interest in these companies, they are regarded as controlled entities as described in note 2.

	Nature of business	**Country of incorporation**
Lanark Trustees Limited	Mortgages trustee	Jersey
Lanark Funding Limited	Funding company	England
Lanark Master Issuer PLC	Issuer of securitised notes	England

All of the above controlled entities have a 30 September financial year end. Where a controlled entity has a financial year end other than 30 September, the consolidated Financial Statements include interim management accounts prepared to 30 September.

18. Property, plant and equipment

Movements on property, plant and equipment

Group	Freehold land and buildings £m	Leases of 50 years and over unexpired £m	Leases of under 50 years unexpired £m	Motor vehicles, fixtures and equipment £m	Operating lease assets £m	Total £m
Cost or valuation						
At 1 October 2008	60	11	118	181	2	372
Additions	11	-	21	20	-	52
Disposals	(18)	(6)	(10)	(58)	(2)	(94)
Deficit on revaluation	(12)	(2)	-	-	-	(14)
At 30 September 2009	**41**	**3**	**129**	**143**	**-**	**316**
Accumulated depreciation						
At 1 October 2008	(1)	1	53	110	2	165
Charge for the year	1	1	11	10	-	23
Disposals	-	-	(3)	(34)	(2)	(39)
At 30 September 2009	**-**	**2**	**61**	**86**	**-**	**149**
Net book value						
At 30 September 2009	**41**	**1**	**68**	**57**	**-**	**167**
At 30 September 2008	61	10	65	71	-	207

Bank	Freehold land and buildings £m	Leases of 50 years and over unexpired £m	Leases of under 50 years unexpired £m	Motor vehicles, fixtures and equipment £m	Total £m
Cost or valuation					
At 1 October 2008	60	11	118	181	370
Additions	11	-	21	20	52
Disposals	(18)	(6)	(10)	(58)	(92)
Deficit on revaluation	(12)	(2)	-	-	(14)
At 30 September 2009	**41**	**3**	**129**	**143**	**316**
Accumulated depreciation					
At 1 October 2008	(1)	1	53	110	163
Charge for the year	1	1	11	10	23
Disposals	-	-	(3)	(34)	(37)
At 30 September 2009	**-**	**2**	**61**	**86**	**149**
Net book value					
At 30 September 2009	**41**	**1**	**68**	**57**	**167**
At 30 September 2008	61	10	65	71	207

18. Property, plant and equipment (continued)

Included in freehold land and buildings are properties under construction with a carrying value of £13.7m.

The 2008 closing cost balances in freehold land and buildings and leases of 50 years included investment properties of £16m. Investment properties are now disclosed separately in Note 19 therefore the opening cost balances have been revised accordingly.

Valuations

Cost and valuation of freehold and leasehold land and buildings at 30 September comprises:

	2009	2008
	£m	£m
At current year valuation	**37**	45
At cost	**136**	160
	173	205

The Bank's properties are carried at their fair value as determined by independent surveyors. Fair values were determined in accordance with guidance published by the Royal Institution of Chartered Surveyors. Valuations are performed annually in July.

On the historical cost basis, freehold and leasehold land and buildings would have been included as follows:

	2009	2008
	£m	£m
Cost	**221**	239
Accumulated depreciation	**(96)**	(96)
Net book value	**125**	143

Land and buildings occupied for own activities

	2009	2008
	£m	£m
Net book value	**136**	**137**

Included are freehold and leasehold properties and fixtures and fittings.

19. Investment properties

	2009	2008
Group	**£m**	£m
At 1 October 2008	**16**	-
Additions	**29**	16
Deficit on revaluation	**(1)**	-
	44	16

Investment properties are stated at fair value, which has been determined based on valuations performed by an independent valuer, as at 30 September 2009. Fair values were determined in accordance with guidance published by the Royal Institution of Chartered Surveyors.

20. Deferred tax

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Deferred tax asset				
Opening balance	**-**	45	**(3)**	40
Tax expense recognised in income statement	**(10)**	(31)	**(10)**	(31)
Deferred taxation recognised in equity	**159**	(10)	**159**	(11)
Other	**(2)**	(4)	**-**	(1)
Closing balance	**147**	-	**146**	(3)

The deferred tax asset is attributable to the following items:

Defined benefit pension liability/(asset)	**87**	(66)	**87**	(66)
Impairment reserve on credit exposures	**37**	42	**37**	42
Employee share based payments	**10**	6	**10**	6
Other	**13**	18	**12**	15
	147	-	**146**	(3)

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Deferred tax liability				
Opening balance	**24**	18	**5**	-
Tax (credit)/expense recognised in income statement	**-**	(3)	**-**	(3)
Deferred taxation recognised in equity	**34**	8	**23**	8
Transfers to deferred tax asset	**-**		**-**	
Other	**(8)**	1	**-**	-
Closing balance	**50**	24	**28**	5

The deferred tax liability is attributable to the following items:

Accelerated capital allowances	**7**	15	**(3)**	(3)
Net gain on revaluation of properties	**3**	3	**3**	3
Cash flow hedge reserve	**40**	6	**28**	5
	50	24	**28**	5

21. Other assets

	Group		Bank	
				As restated
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Prepayments and accrued income	**415**	733	**246**	481
Other	**312**	446	**157**	2,291
	727	1,179	**403**	2,772

22. Due to other banks

	2009	2008
Group and Bank	**£m**	£m
Transaction balances with other banks	**5**	6
Securities sold under agreements to repurchase	**584**	2,087
Deposits with other banks	**1,331**	1,869
	1,920	3,962

23. Due to customers

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Non interest bearing demand deposits	**984**	873	**984**	873
Interest bearing demand deposits	**15,395**	13,403	**15,395**	13,131
Term deposits	**7,176**	6,138	**7,176**	6,138
Other wholesale deposits	**3,101**	1,920	**3,101**	1,920
	26,656	22,334	**26,656**	22,062

24. Provisions

Group and Bank	**2009**	2008
	£m	£m
Refund of current account fees & associated costs		
At 1 October	**3**	7
Charge to income statement	**2**	1
Provisions utilised	**(1)**	(5)
At 30 September	**4**	3
Efficiency, quality and service initiatives		
At 1 October	**-**	-
Charge to income statement	**3**	-
Provisions utilised	**(3)**	-
At 30 September	**-**	-
Other provisions		
At 1 October	**6**	6
Provisions transferred (note 25)	**-**	(3)
Charge to income statement	**6**	4
Provisions utilised	**(2)**	(1)
At 30 September	**10**	6
Total provisions	**14**	9

Refund of current account fees & associated costs

A test case involving a number of current account providers (including the Bank) recently ended. The Supreme Court ruled that the level of charges incurred by customers when an unauthorised overdraft occurred could not be assessed for fairness. The High Court had previously ruled that such charges were not penalties at common law. Subject to ascertaining the position of the Financial Ombudsman, all claims founded solely on unfairness or penalties will fail.

In relation to business accounts, the High Court had ruled that none of the banks' contracts contain penalties at common law.

As at 30 September 2009 a provision of £4m remains to cover projected legal costs and further settlement of hardship cases and is considered adequate.

Efficiency, quality and service initiatives

A provision of £3m was created during the year for the Efficiency, quality and service initiatives. This provision was fully utilised during the year for severance payments and related to employees already displaced and who left the Bank before 30 September.

Other
This category includes:
- Provision for costs arising in respect of a number of legal actions and claims arising in the ordinary course of the Bank's business
- Provision for future employer related taxes in relation to share based remuneration
- Provision for mis-selling of Payment Protection Insurance which is under review by Regulators, specifically the FSA and Competition Commission

25. Retirement benefit obligations

At the start of the year the Group was sponsoring employer in two funded defined benefit schemes, the Clydesdale Bank Pension Scheme and the Yorkshire Bank Pension Fund. The assets of the two schemes were held in separate trustee administered funds.

On the 30th September 2009, all the assets and liabilities of the Yorkshire Bank Pension Fund were transferred to the Clydesdale Bank Pension Scheme, and the remaining scheme was renamed the Yorkshire and Clydesdale Bank Pension Scheme. This remaining Scheme is a fully sectionalised arrangement where the discrete assets and liabilities of the two sections are independently calculated in accordance with the previously existing scheme structures.

The Group closed the defined benefit schemes to new members in 2004. Since that time the principal scheme available to new members is the defined contribution scheme, "Total Pension". In relation to this scheme, the pension charge for the year for the Group is disclosed in note 6.

In April 2006, the Group implemented a number of reforms in relation to the Schemes. Defined benefits accruing after April 2006 are determined on a "career average revalued earnings" basis. Benefits for active members which have built up to April 2006 revalue in the future in line with price inflation. Pensions in payment which built up after April 2006 increase in line with price inflation subject to a maximum annual increase of 2.5%.

The Bank also provides post-retirement health care under a defined benefit scheme for pensioners and their dependant relatives for which provision has been made. This is a closed scheme and the provision will be utilised over the life of the remaining scheme members. A one percentage point change in the assumed rate of increase in healthcare costs would change the defined benefit pension obligation by £0.8m (2008: £0.9m) and would have no material impact upon service costs and interest costs.

The last full valuations of the Schemes were carried out at 30 September 2007 and have been updated to 30 September 2009 by qualified independent actuaries. The effective date of the next triennial valuation is expected to be 30 September 2010.

The principal financial assumptions used in the Schemes' valuations at 30 September 2009 were as follows:

	2009	2008	2007
	% p.a.	% p.a.	% p.a.
Inflation	**3.10**	3.60	3.25
Rate of increase for pensions in payment:			
pre 5 April 1997 benefits (Clydesdale Bank Pension Scheme)	**2.20**	2.50	2.50
pre 5 April 1997 benefits (Yorkshire Bank Pension Fund)	**3.00**	3.50	3.25
post April 1997 (both Schemes)	**3.00**	3.50	3.25
post April 2006 (both Schemes)	**2.20**	2.50	2.50
Rate of increase for pensions in deferment	**3.10**	3.60	3.25
Discount rate	**5.50**	7.20	5.95
Post-retirement mortality:			
Current pensioners at 60 - male	**25.5 years**	25.5 years	25.2 years
Current pensioners at 60 - female	**27.3 years**	27.3 years	28.2 years
Future pensioners at 60 - male	**26.5 years**	26.5 years	26.1 years
Future pensioners at 60 - female	**28.2 years**	28.2 years	29.1 years

25. Retirement benefit obligations (continued)

Total contributions made to the Scheme during the year were £32m (2008: £80m).

The Group prepaid contributions of £41m on 1 October 2009 in respect of the year ending 30 September 2010.

The fair value of the Schemes' assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the Schemes' liabilities, which are derived from cash flow projections over long periods and thus inherently uncertain, were:

Summary

	2009	2008	2007	2006	2005
	£m	£m	£m	£m	£m
Clydesdale Bank Pension Scheme					
Total market value of scheme assets	**1,037**	1,036	1,123	889	759
Present value of scheme liabilities	**(1,242)**	(926)	(1,060)	(978)	(1,030)
Net pension (liability)/asset	**(205)**	110	63	(89)	(271)
Yorkshire Bank Pension Fund					
Total market value of scheme assets	**791**	806	885	815	713
Present value of scheme liabilities	**(896)**	(667)	(789)	(838)	(824)
Net pension (liability)/asset	**(105)**	139	96	(23)	(111)

Clydesdale Bank Pension Scheme

	2009		2008	
	£m	**% of fair value of scheme assets**	£m	% of fair value of scheme assets
Assets				
Equities	**543**	**52.36**	498	48.07
Property	**60**	**5.79**	44	4.25
Government bonds	**196**	**18.90**	451	43.53
Corporate bonds	**233**	**22.47**	29	2.80
Cash	**5**	**0.48**	14	1.35
Total market value of scheme assets	**1,037**	**100.00**	1,036	100.00
Present value of scheme liabilities	**(1,242)**		(926)	
Net pension (liability)/asset	**(205)**		110	

The Clydesdale Section of the Scheme includes certain property investments leased by the Group. However these investments are within the 5% self-investment limit.

25. Retirement benefit obligations (continued)

Yorkshire Bank Pension Fund

	2009 £m	**2009 % of fair value of scheme assets**	2008 £m	2008 % of fair value of scheme assets
Assets				
Equities	**423**	**53.48**	388	48.14
Property	**28**	**3.54**	34	4.22
Government bonds	**154**	**19.47**	350	43.43
Corporate bonds	**183**	**23.14**	23	2.85
Cash	**3**	**0.37**	11	1.36
Total market value of scheme assets	**791**	**100.00**	806	100.00
Present value of scheme liabilities	**(896)**		(667)	
Net pension (liability)/asset	**(105)**		139	

The Schemes have not invested in any of the Group's own financial instruments nor in other assets used by the Group apart from the property investments leased by the Group disclosed previously.

Expected rate of return on plan assets

The expected return on assets assumption has been determined by looking at the assets expected to be held over the following year and considering the expected returns for each asset class.

	2009 % p.a.	2008 % p.a.	2007 % p.a.	2006 % p.a.	2005 % p.a.
Equities	**8.15**	8.70	8.35	8.20	8.10
Property	**6.80**	8.00	7.15	6.60	6.55
Government bonds	**3.95**	4.70	5.00	4.40	4.30
Corporate bonds	**5.35**	7.00	5.95	5.05	5.00
Cash	**3.95**	5.00	5.75	4.75	4.50

Reconciliation of fair value of scheme assets

	Clydesdale Bank		**Yorkshire Bank**		**Total**	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
Fair value of scheme assets at 1 October	**1,036**	1,123	**806**	885	**1,842**	2,008
Actual return on scheme assets	**15**	(100)	**11**	(80)	**26**	(180)
Employer contributions	**29**	53	**3**	27	**32**	80
Benefits paid	**(43)**	(40)	**(29)**	(26)	**(72)**	(66)
Fair value of scheme assets at 30 September	**1,037**	1,036	**791**	806	**1,828**	1,842

25. Retirement benefit obligations (continued)

Reconciliation of defined benefit obligation

	Clydesdale Bank		Yorkshire Bank		Total	
	2009	2008	**2009**	2008	**2009**	2008
	£m	£m	**£m**	£m	**£m**	£m
Defined benefit obligation at 1 October	**926**	1,060	**667**	789	**1,593**	1,849
Interest cost	**65**	62	**47**	46	**112**	108
Current service cost	**15**	16	**10**	11	**25**	27
Benefits paid	**(44)**	(40)	**(29)**	(26)	**(73)**	(66)
Actuarial loss/(gain)	**279**	(172)	**199**	(153)	**478**	(325)
Past service cost	**1**	-	**2**	-	**3**	-
Defined benefit obligation at 30 September	**1,242**	926	**896**	667	**2,138**	1,593

Reconciliation of balance sheet (liability)/asset

	Clydesdale Bank		Yorkshire Bank		Total	
	2009	2008	**2009**	2008	**2009**	2008
	£m	£m	**£m**	£m	**£m**	£m
Balance sheet asset/(liability) at 1 October	**110**	63	**139**	96	**249**	159
Employer contributions	**29**	53	**3**	27	**32**	80
Total pension expense	**-**	-	**-**	5	**-**	5
Statement of recognised income and expense	**(344)**	(6)	**(247)**	11	**(591)**	5
Balance sheet (liability)/asset at 30 September	**(205)**	110	**(105)**	139	**(310)**	249
Post Retirement Healthcare Schemes						
Balance sheet liability at 1 October					**(10)**	-
Transferred from provisions (note 24)					**-**	(3)
Statement of recognised income and expense					**-**	(7)
Balance sheet liability at 30 September 2009					**(10)**	(10)
Balance sheet (liability)/asset at 30 September 2009					**(320)**	239

25. Retirement benefit obligations (continued)

Pension expense for the year

	Clydesdale Bank		Yorkshire Bank		Total	
	2009	2008	**2009**	2008	**2009**	2008
	£m	£m	**£m**	£m	**£m**	£m
Current service cost	**15**	16	**10**	11	**25**	27
Past service costs	**1**	-	**3**	-	**4**	-
Interest cost	**65**	62	**47**	46	**112**	108
Expected return on assets	**(78)**	(78)	**(61)**	(61)	**(139)**	(139)
Effect of transfer of DC scheme	**(1)**	-	**-**	-	**(1)**	-
Total pension expense/(credit)	**2**	-	**(1)**	(4)	**1**	(4)

25. Retirement benefit obligations (continued)

Statement of recognised income and expense (SORIE)

	Clydesdale Bank		Yorkshire Bank		Total	
	2009	2008	**2009**	2008	**2009**	2008
	£m	£m	**£m**	£m	**£m**	£m
Loss on scheme assets	**(63)**	(178)	**(49)**	(141)	**(112)**	(319)
Experience losses on scheme liabilities	**(4)**	(16)	**2**	20	**(2)**	4
(Loss)/gain from change in actuarial assumptions - Defined benefit plans	**(277)**	188	**(200)**	132	**(477)**	320
Total amount recognised in SORIE	**(344)**	(6)	**(247)**	11	**(591)**	5
Cumulative amount recognised in SORIE	**(242)**	100	**(93)**	156	**(335)**	256

History of experience gains and losses
Clydesdale Bank

	2009	2008	2007	2006
Difference between the expected and actual return on scheme assets				
Amount (£m)	**(63)**	(178)	27	24
Percentage of scheme assets	**-6.08%**	-17.18%	2.40%	2.70%
Experience gains and (losses) on scheme liabilities				
Amount (£m)	**(4)**	(16)	1	-
Percentage of the present value of the scheme liabilities	**-0.32%**	-1.73%	0.10%	0.00%
Total amount recognised in SORIE				
Amount (£m)	**(344)**	(6)	119	8
Percentage of the present value of the scheme liabilities	**-27.68%**	-0.65%	11.23%	0.82%

25. Retirement benefit obligations (continued)

History of experience gains and losses
Yorkshire Bank

	2009	2008	2007	2006
Difference between the expected and actual return on scheme assets				
Amount (£m)	**(49)**	(141)	22	22
Percentage of scheme assets	**-6.19%**	-17.49%	2.49%	2.70%
Experience gains and (losses) on scheme liabilities				
Amount (£m)	**2**	20	-	-
Percentage of the present value of the scheme liabilities	**0.22%**	3.00%	0.00%	0.00%
Total amount recognised in SORIE				
Amount (£m)	**(247)**	11	103	11
Percentage of the present value of the scheme liabilities	**-27.57%**	1.65%	13.05%	1.31%

26. Bonds and notes

	Group		**Bank**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Medium term notes	**2,465**	2,133	**2,465**	2,133
Subordinated medium term notes	**450**	450	**450**	450
Residential mortgage backed securities	**2,343**	2,860	**-**	-
Total bonds, notes and subordinated debt	**5,258**	5,443	**2,915**	2,583
Hedge adjustments	**29**	9	**38**	3
Net discounts	**-**	(1)	**-**	(1)
	5,287	5,451	**2,953**	2,585
Total bonds and notes were recorded as:				
At amortised cost	**1,666**	1,781	**1,029**	1,781
Designated as fair value hedges	**3,621**	3,670	**1,924**	804
	5,287	5,451	**2,953**	2,585

26. Bonds and notes (continued)

Details of the terms and conditions of the medium term notes issued by Clydesdale Bank PLC as at 30 September 2009 were as follows:

Issue date	Issue currency	Carrying value £m	Coupon rate %	Maturity date
Medium term notes				
29 June 2006	GBP	350	0.64000%	29 June 2011
30 May 2007	EUR	686	0.90900%	30 May 2012
09 June 2008	GBP	29	1.78688%	9 December 2009
31 July 2008	GBP	150	1.95188%	30 October 2009
09 December 2008	GBP	750	3.37500%	9 December 2011
11 December 2008	GBP	500	1.42813%	11 November 2011
		2,465		
Subordinated medium term notes				
16 February 2006	GBP	250	4.87500%	17 February 2016
30 March 2007	GBP	200	5.70313%	30 March 2017
		450		

Details of the terms and conditions of the residential mortgage backed securities issued by Lanark Master Issuer PLC as at 30 September 2009 were as follows:

Class A residential mortgage backed securities				
06 August 2007	GBP	590	0.86000%	22 May 2013
06 August 2007	USD	387	0.50688%	22 August 2012
06 August 2007	USD	531	0.54688%	22 August 2012
06 August 2007	EUR	614	0.99100%	22 August 2012
Class B residential mortgage backed securities				
06 August 2007	EUR	124	1.07100%	22 February 2010
Class C residential mortgage backed securities				
06 August 2007	GBP	24	1.13000%	22 February 2010
06 August 2007	EUR	24	1.27100%	22 February 2010
Class D residential mortgage backed securities				
06 August 2007	GBP	23	1.46000%	22 February 2010
06 August 2007	EUR	26	1.60100%	22 February 2010
		2,343		

27. Other liabilities

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Accruals and deferred income	**47**	95	**47**	83
Notes in circulation	**1,163**	1,211	**1,163**	1,211
Accrued interest payable	**519**	719	**353**	467
Other liabilities	**111**	264	**108**	746
	1,840	2,289	**1,671**	2,507

28. Called up share capital

	2009	2008
	Number	Number
Authorised		
Ordinary shares of £1 each - equity	**554,785,000**	254,785,000
12% Non-cumulative redeemable preference shares of £1 each - equity	**100,000,000**	-

During the year the authorised share capital was increased by £400,000,000 with the creation of 300,000,000 ordinary shares of £1 each and 100,000,000 12% non-cumulative redeemable preference shares of £1 each.

	2009	2008
	£m	£m
Allotted, called up and fully paid		
Ordinary shares of £1 each - equity		
At 1 October	**232**	232
Issued during the period	**300**	-
At 30 September 2009 and 2008	**532**	232
Preference Shares		
Preference shares of £1 each - equity		
Issued during the period	**100**	-
At 30 September 2009 and 2008	**100**	-
Share Capital	**632**	232

On 17 December 2008, 300,000,000 ordinary shares of £1 each were issued at par, resulting in an increase of £300,000,000 in the allotted, called up and fully paid share capital. On the same day 100,000,000 preference shares of £1 each were issued at par, resulting in an increase of £100,000,000 in the preference share capital.

The preference shares entitle the holder to a discretionary fixed non-cumulative dividend of 12% per annum, payable semi-annually in arrears commencing on 17 June 2009, until the first redemption date, and thereafter semi-annually in arrears, at 12% per annum. The preference shares are redeemable, in whole only, at the option of CB PLC on the day following the 5th anniversary of the date of issue. No such redemption may be made without the consent of the FSA. Accordingly, the preference shares have been classified as issued share capital rather than as a financial liability.

29. Reserves

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Share premium account	**243**	243	**243**	243
Share option reserve	**2**	20	**2**	20
Asset revaluation reserve	**2**	7	**2**	7
Available for sale investments reserve	**14**	-	**14**	-
Merger reserve	**338**	338	**338**	338
Cash flow hedge reserve	**103**	11	**71**	11
Retained earnings	**916**	1,313	**747**	1,086
	1,618	1,932	**1,417**	1,705

Share option reserve
The share option reserve records the value of equity benefits provided to employees and directors as part of their remuneration.

Asset revaluation reserve
The asset revaluation reserve includes the gross revaluation increments and decrements arising from the revaluation of land and buildings.

Merger reserve
The merger reserve arose as a result of the transfer of the entire business and undertakings of Yorkshire Bank PLC to Clydesdale Bank PLC on 1 December 2004. As no consideration was paid in relation to the transfer the only impact arising was the crystallisation of the Yorkshire Bank PLC Share Capital and Share Premium into a Merger Reserve in the combined entity.

Cash flow hedge reserve
The cash flow hedge reserve records fair value revaluations of derivatives designated as cash flow hedging instruments.

29. Reserves (continued)

Movements in reserves **Group**	**Share premium account £m**	**Share option reserve £m**	**Asset revaluation reserve £m**	**Available for sale investments reserve £m**	**Cash flow hedge reserve £m**	**Retained earnings £m**
At 1 October 2007	243	12	13	(3)	(9)	1,160
Profit for the year ended 30 September 2008	-	-	-	-	-	247
Actuarial gains on defined benefit pension schemes	-	-	-	-	-	5
Post retirement medical benefits	-	-	-	-	-	(7)
Share options granted	-	12	-	-	-	-
Share options settled	-	-	-	-	-	-
Revaluation of land and buildings	-	-	(3)	-	-	-
Net change in available for sale investments reserve	-	-	-	3	-	-
Fair value gains on cash flow hedge reserve	-	-	-	-	6	-
Transferred to income statement	-	-	-	-	22	-
Transfers from/to asset revaluation reserve	-	-	(3)	-	-	3
Tax on items recognised directly in equity	-	(4)	-	-	(8)	-
Dividends paid	-	-	-	-	-	(95)
At 30 September 2008	**243**	**20**	**7**	**-**	**11**	**1,313**
Profit for the year ended 30 September 2009	-	-	-	-	-	34
Actuarial gains on defined benefit pension schemes	-	-	-	-	-	(591)
Share options granted	-	15	-	-	-	-
Share options settled	-	(35)	-	-	-	-
Revaluation of land and buildings	-	-	(6)	-	-	-
Movement in available for sale investments	-	-	-	23	-	-
Transferred to income statement	-	-	-	(4)	-	-
Fair value gains on cash flow hedge reserve	-	-	-	-	145	-
Transferred to income statement	-	-	-	-	(17)	-
Transfers from/to asset revaluation reserve	-	-	(1)	-	-	1
Tax on items recognised directly in equity	-	2	2	(5)	(36)	165
Dividends paid	-	-	-	-	-	(6)
At 30 September 2009	**243**	**2**	**2**	**14**	**103**	**916**

29. Reserves (continued)

Movements in reserves

Bank	**Share premium account £m**	**Share option reserve £m**	**Asset revaluation reserve £m**	**Available for sale investments reserve £m**	**Cash flow hedge reserve £m**	**Retained earnings £m**
At 1 October 2007	243	12	13	(3)	(9)	1,037
Profit for the year ended 30 September 2008	-	-	-	-	-	143
Actuarial gains on defined benefit pension schemes	-	-	-	-	-	5
Share options granted	-	12	-	-	-	(7)
Share options settled	-	-	-	-	-	-
Revaluation of land and buildings	-	-	(3)	-	-	-
Net change in available for sale investments reserve	-	-	-	3	-	-
Fair value gains on cash flow hedge reserve	-	-	-	-	6	-
Transferred to income statement	-	-	-	-	22	-
Transfers (from)/to asset revaluation reserve	-	-	(3)	-	-	3
Tax on items recognised directly in equity	-	(4)	-	-	(8)	-
Dividends paid	-	-	-	-	-	(95)
At 30 September 2008	**243**	**20**	**7**	**-**	**11**	**1,086**
Profit for the year ended 30 September 2009	-	-	-	-	-	92
Actuarial gains on defined benefit pension schemes	-	-	-	-	-	(591)
Share options granted	-	15	-	-	-	-
Share options settled	-	(35)	-	-	-	-
Revaluation of land and buildings	-	-	(6)	-	-	-
Movement in available for sale investments	-	-	-	23	-	-
Transferred to income statement	-	-	-	(4)	-	-
Fair value gains on cash flow hedge reserve	-	-	-	-	101	-
Transferred to income statement	-	-	-	-	(17)	-
Transfers from/to asset revaluation reserve	-	-	(1)	-		1
Cash flow hedge reserve						
Tax on items recognised directly in equity	-	2	2	(5)	(24)	165
Dividends paid	-	-	-	-	-	(6)
At 30 September 2009	**243**	**2**	**2**	**14**	**71**	**747**

30. Memorandum items

	Contract amount 2009 £m	**Risk weighted amount 2009 £m**	Contract amount 2008 £m	Risk weighted amount 2008 £m
Contingent liabilities				
Group and Bank				
Guarantees and assets pledged as collateral security				
- guarantees and irrevocable letters of credit	**673**	**177**	828	189
- At call	**1**		70	
- Due in less than three months	**29**		46	
- Due after 3 months through to 1 year	**196**		440	
- Due after 1 year through to 3 years	**274**		18	
- Due after 3 years through to 5 years	**6**		8	
- Due after 5 years	**128**		116	
- No specified maturity	**39**		130	
	673		828	
Commitments				
Group				
Sale and option to repurchase transactions	**750**	**-**	2,000	-
- At call	**-**		-	
- Due in less than three months	**-**		1,000	
- Due after 3 months through to 1 year	**250**		-	
- Due after 1 year through to 3 years	**500**		-	
- Due after 3 years through to 5 years	**-**		1,000	
	750		2,000	
Group and Bank				
Other commitments				
- undrawn formal standby facilities, credit lines and other commitments to lend	**8,595**	**562**	10,420	373
- At call	**8,595**		10,420	

The 30 September 2008 comparative figure for other commitments has been restated from £11,940m to £10,420m to remove an overstatement in the previously reported figure.

The tables above give the contract amounts and risk-weighted amounts of off balance sheet transactions for the Group and Bank. The contract amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The risk weighted amounts have been calculated in accordance with the FSA guidelines.

30. Memorandum items (continued)

Contingent liabilities and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. Since a significant portion of guarantees and commitments are expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

31. Capital commitments

The Group and Bank had future capital expenditure which had been contracted for but not provided for in the financial statements of £2m (2008: £9m) at 30 September 2009.

32. Lease commitments

Group and Bank **Operating lease commitments**	**Land and buildings 2009 £m**	Land and buildings 2008 £m
Payments committed to be made during the next year under non-cancellable operating leases which expire:		
- within 1 year	**2**	2
- between 1 and 5 years	**3**	4
- over 5 years	**2**	3
	7	9
Where the Group is the lessee the future minimum lease payments under non-cancellable operating leases are:		
- within 1 year	**1**	23
- within 1 and 5 years	**20**	81
- over 5 years	**372**	206
	393	310

33. Other contingent liabilities

United Kingdom Financial Services Compensation Scheme

The UK Financial Services Compensation Scheme (FSCS) provides compensation to depositors in the event that a financial institution is unable to repay amounts due. Following the failure of a number of financial institutions, claims have been triggered against the FSCS, initially to pay interest on borrowing which the FSCS has raised from the UK Government to support the protected deposits. These borrowings are anticipated to be repaid from the realisation of the assets of the institutions, and in the interim the FSCS has estimated levies due to 31 March 2010 and a charge of £6 million has been recognised in the period for the Group's calculated liability. If the assets of the failed institutions are insufficient to repay the Government loan, additional levies will become payable in future periods.

Claims for potential mis-selling of Payment Protection Insurance (PPI)

Following the investigation by the UK Competition Commission into the sale of Payment Protection Insurance, a report was published on 29th January 2009 concluding a lack of competition in the UK market as a result of various factors including lack of transparency and barriers to entry for stand alone providers. A range of remedies to address the issue have been imposed and further to the investigation, the FSA announced proposals on 30th September 2009 to require banks to re-open previously rejected complaints and to re-assess them in light of new guidance. Provision has been made for costs arising from expected claims, although at this stage there remains some uncertainty surrounding regulatory guidance and its potential impact. It is expected that the final version of the regulatory guidance will be published at the end of January 2010.

Other

The Bank is named in and defending a number of legal claims arising in the ordinary course of business. No material adverse impact on the financial position of the Group or the Bank is expected to arise from the ultimate resolution of these legal actions.

34. Employees

The average number of full time equivalent employees of the Group during the year was made up as follows:

	2009	2008
	Number	Number
Managers	**1,570**	1,545
Clerical staff	**4,313**	4,191
	5,883	5,736

All staff are contracted employees of National Australia Group Europe Limited ("NAGE") (the intermediate parent company of the Bank) The numbers above disclose the staff remunerated directly by the Group but exclude employees working within other NAGE subsidiaries who provide support services to the Group. The average number of staff employed in the UK Region in the year to 30 September 2009 was 8,295 (2008: 8,758).

35. Notes to the statement of cash flows

	Group		Bank	
	2009	2008	**2009**	2008
Non cash and non-operating items				As restated
included in profit before tax	**£m**	£m	**£m**	£m
Interest receivable	**(1,722)**	(2,393)	**(1,547)**	(2,042)
Interest payable	**877**	1,497	**900**	1,307
Depreciation (note 6)	**23**	26	**23**	23
Actuarial (losses)/gains on defined benefit pension plans	**(591)**	5	**(591)**	5
Post retirement medical benefit	**-**	(7)	**-**	(7)
Profit on sale of land & buildings	**(11)**	(10)	**(11)**	(10)
Loss on devaluation of land and buildings	**9**	-	**9**	-
Profit on disposal of available for sale investments	**(6)**	-	**(6)**	-
Transfer from available for sale reserve (note 29)	**(4)**	-	**(4)**	-
Transfer from cash flow hedge reserve (note 29)	**(17)**	-	**(17)**	-
Impairment losses on credit exposures (note 15)	**399**	179	**383**	178
Share of operating profit in associated undertaking	**(2)**	-	**-**	-
Dividends received from subsidiaries	**-**	-	**(193)**	-
Profit on disposal of subsidiary (note 5)	**(2)**	-	**-**	-
Equity based compensation expense	**15**	12	**15**	12
	(1,032)	(691)	**(1,039)**	(534)
Changes in operating assets				
Net (increase)/decrease in:				
Balances with supervisory central banks	**(1)**	8	**(1)**	8
Due from other banks	**182**	163	**(325)**	151
Derivative financial assets	**(340)**	(476)	**(154)**	(190)
Financial assets at fair value through profit or loss	**(1,562)**	(1,223)	**(1,606)**	(1,223)
Investments	**(2,145)**	1,707	**(2,453)**	1,307
Loans and advances to customers	**1,110**	(3,780)	**1,730**	(3,878)
Due from customers on acceptances	**1**	-	**1**	-
Other assets	**(132)**	133	**1,908**	(1,828)
	(2,887)	(3,468)	**(900)**	(5,653)
Changes in operating liabilities				
Net increase/(decrease) in:				
Due to other banks	**(2,039)**	1,671	**(2,039)**	1,671
Derivative financial liabilities	**77**	14	**77**	14
Financial liabilities at fair value through profit or loss	**44**	111	**44**	111
Due to customers	**4,322**	3,015	**4,594**	3,161
Liabilities on acceptances	**(1)**	-	**(1)**	-
Provisions	**5**	(4)	**5**	(4)
Defined benefit pension obligations	**559**	(80)	**559**	(80)
Other liabilities	**(248)**	114	**(731)**	537
	2,719	4,841	**2,508**	5,410

35. Notes to the statement of cash flows (continued)

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises the following balances with less than three months maturity from the date of acquisition.

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Cash assets (excluding mandatory deposits with central banks - note 9)	**2,686**	5,083	**2,686**	5,083
Other assets	**131**	343	**125**	343
Due to other banks	**(5)**	(8)	**(5)**	(8)
Due to related entities	**(123)**	(161)	**(123)**	(161)
Other liabilities	**(76)**	(67)	**(76)**	(67)
	2,613	5,190	**2,607**	5,190

36. Related party transactions

The Bank is a wholly owned controlled entity of National Australia Group Europe Limited. The ultimate parent entity of the Bank is National Australia Bank Limited.

During the year there have been transactions between the Bank, its ultimate parent, controlled entities of the ultimate parent, controlled entities of the Bank, and other related parties.

The Bank provides a range of services to related parties, including the provision of banking facilities and standby financing arrangements. Other dealings include granting loans and accepting deposits, and the provision of finance, forward exchange and interest cover. Those transactions are normally subject to commercial terms and conditions.

The Bank and Group receives a range of services from the parent and related parties, including loans and deposits, forward exchange and interest rate cover and various administrative services. Fees may be charged for these services.

Amounts due from related entities	Group		Bank	
	2009	2008	**2009**	2008 As restated
	£m	£m	**£m**	£m
Loans				
Ultimate parent	**1,947**	1,140	**1,947**	1,140
Controlled entities of the Bank	**-**	-	**4,951**	701
	1,947	1,140	**6,898**	1,841
Other receivables				
Ultimate parent	**5**	1	**5**	1
Controlled entities of the ultimate parent	**19**	12	**19**	12
	24	13	**24**	13
Total amounts due from related entities	**1,971**	1,153	**6,922**	1,854
Interest income on the above amounts was as follows:				
Ultimate parent	**15**	69	**15**	69
Controlled entities of the Bank	**-**	-	**75**	109
Total interest income on amounts due from related entities	**15**	69	**90**	178

The 30 September 2008 comparative figure for amounts due from related entities has been restated from £1,281m to £701m following a £580m reallocation of the investment in Yorkshire Bank Investments Limited. This investment is now included in Note 17.

36. Related party transactions (continued)

Amounts due to related entities	**Group**		**Bank**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Deposits				
Ultimate parent	**2,435**	4,486	**2,435**	4,486
Controlled entities of the ultimate parent	**-**	158	**-**	158
Controlled entities of the Bank	**-**	-	**3,005**	1,120
	2,435	4,644	**5,440**	5,764
Subordinated liabilities				
Ultimate parent	**300**	-	**300**	-
Controlled entities of the ultimate parent	**426**	426	**426**	426
Other payables				
Ultimate parent	**7**	21	**7**	21
Controlled entities of the ultimate parent	**153**	60	**153**	60
	160	81	**160**	81
Total amounts due to related parties	**3,321**	5,151	**6,326**	6,271
Interest expense on the above amounts was as follows:				
Ultimate parent	**106**	195	**106**	195
Controlled entities of the ultimate parent	**18**	36	**18**	36
Controlled entities of the Bank	**-**	-	**223**	1
Total interest expense on amounts due to related entities	**124**	231	**347**	232

Subordinated liabilities

Subordinated liabilities comprises of undated and dated loan capital which is provided to the Bank by NAGE and NAB. Interest on the loans is payable at rates related to the London Interbank Offered Rate ("LIBOR"). The undated loans are subject to five years and one day's notice of redemption by the lenders and are repayable at par. Early repayment is at the option of the borrower, subject to the prior consent of the Financial Services Authority. The loans are subordinated to the claims of other creditors and are unsecured. The loans are employed in the general business of the Bank.

Details of subordinated liabilities in excess of 10% of the total balance (based on the 2008 financial year) are disclosed below:

	2009	2008
	£m	£m
6.45750% 10-year, non-call five years with a final maturity of 17 February 2019	**300**	-
1.95500% (2008: 6.27125%) Undated subordinated notes	**100**	100
1.84875% (2008: 6.59563%) Undated subordinated notes	**50**	50
1.72688% (2008: 6.47375%) Undated subordinated notes	**50**	50
1.93875% (2008: 6.68563%) Undated subordinated notes	**50**	50
	550	250
Other undated subordinated notes	**176**	176
Total subordinated debt	**726**	426

The rates of interest stated above apply at 30 September 2009.

Securitisation

The Bank has securitised part of its residential mortgage portfolio and the cash raised via the issue of Residential Mortgaged Backed Securities (RMBS) through SPEs forms part of the Banks medium term funding. The value of the RMBS issued as at 30 September 2009 was £2,215m (2008: £2,548m).

36. Related party transactions (continued)

Other transactions with related entities

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Non interest income received				
Controlled entities of the ultimate parent	**14**	25	**14**	**25**
Administrative expenses				
Ultimate parent	**4**	4	**4**	**4**
Controlled entities of the ultimate parent	**245**	300	**245**	**300**
	249	304	**249**	**304**

Other related party transactions

Compensation of key management personnel (including directors)

	Group	
	2009	2008
	£m	£m
Salaries and other short-term benefits	**9**	8
Share based payments	**4**	4
	13	12

Transactions with key management personnel (KMP)

For the purposes of IAS24 "Related Party Disclosures" key management personnel comprise Directors of the Bank, members of the UK Executive Committee and FSA approved persons with a control function of 1 to 20.

KMP, their close family members and any entity KMP have undertaken the following transactions with the Group in the normal course of business. The transactions were made on the same terms and conditions as applicable to other Group employees, or on normal commercial terms.

	2009	2008
	£m	£m
Loans and advances	**4**	4
Deposits	**8**	9

No provisions have been recognised in respect of loans provided to key management personnel. There were no debts written off or forgiven during the year ended 30 September 2009 (2008: £Nil).

Included in the above are eight (2008: six) loans totalling £0.7m (2008: £1.3m) made to directors.

36. Related party transactions (continued)

Other related party transactions

The Group incurred costs in relation to pension scheme administration. These costs, which amounted to £0.4m in the year ended 30 September 2009 (2008: £0.6m) were charged to the Group sponsored Schemes. The Group has deposits of £4.8m (2008: £3.6m) at the year end placed by the Schemes at market rates.

The following payments were made to superannuation funds sponsored by the Bank:	**Bank**	
	2009	2008
	£m	£m
Clydesdale Bank Pension Scheme	**29**	**41**
Yorkshire Bank Pension Scheme	**3**	**23**
	32	**64**

37. Share based payments

Share incentive plans, share offers, performance options and performance rights in NAB, the Group's ultimate parent company, are used to provide short-term and long-term incentives to employees. These incentives are an integral part of the Group's remuneration strategy in rewarding employees' current and future contribution to the Group's performance.

The plans described below involve the provision of shares in NAB to employees of the Group and to directors of the Company, and performance options and performance rights to senior employees of the Group. The Group reimburses NAB for the cost of these shares and the value of the performance options and performance rights.

Above Target Short Term Incentive (STI)

Employees are required to take any awards in excess of A$500 above their STI target in the form of NAB shares (with a minimum one year restriction period). During the first year after allocation the shares are forfeited if the employee resigns (or upon termination for serious misconduct), or if the employee fails to pass both quality gates (behaviour and compliance) in respect of their performance review at the end of the following financial year.

Recognition Shares

These shares enable retention and recognition awards to be provided in the form of shares, rather than in cash. Such awards are made on a very limited basis with NAB Group executive general manager approval, to individuals in significant key roles where retention is critical over a medium-term timeframe (two to three years). Awards under the program may also be provided to individuals accepting significant project leadership or additional responsibilities for a limited period of time with no related increase in their fixed remuneration. The provision of shares under this plan is desired over the use of cash payments as it provides a stronger retention and shareholder value link to the reward. The shares are subject to forfeiture if the participant resigns or retires before specified key dates and/or milestones are not met, if the participant’s performance falls below specified levels, for conduct in breach of the Company’s Code of Conduct or other applicable standards set from time to time, and on termination for serious misconduct. The minimum restriction period is until the final key date or milestone has been achieved, with the employee able to choose a longer holding period of up to 10 years.

Commencement Shares

These shares enable 'buy-out' of evidenced equity from previous employment for significant new hires. Shares are provided under this program or Commencement performance options and performance rights if more appropriate. The shares are subject to forfeiture if the participant resigns before specified key dates, for conduct in breach of the Company's Code of Conduct or other applicable standards set from time to time or in the event of termination for serious misconduct.

UK National Share Incentive Plan

Under the UK National Share Incentive Plan, employees are entitled to purchase up to £1,500 worth of NAB shares each year through the National Partnership Share Plan. Participants contribute each month and the trustee uses the contributions to purchase shares on market which are then held in trust for the participants. Participants are entitled to receive dividends and exercise voting rights in respect of these shares and there is no risk of forfeiture. In addition, up to £3,000 of free shares per employee may be gifted per annum through the plan.

37. Share based payments (continued)

Mid Year and Year End Share Offers
Under the UK National Share Incentive Plan, the National EVA ® Share Offer gifts up to A$1,000 of ordinary shares to each employee when the Group's performance is on target.

In 2008 an employee share offer valued at approximately A$1,000 per employee was made, based on the Group's achievements as measured against a scorecard of objectives for the Group. Shares under the year end offer were allocated on 19 December 2008. These shares are held by the trustees for three years, or until the employee ceases their 'relevant employment', i.e. ceases employment with either a company in the Group or a company that was in the Group when the shares were allocated to the employee.

The shares are registered in the name of the trustee who holds them on behalf of the participating employee for the duration of the restriction period. Participating employees receive dividends and may exercise, through the trustee, voting rights (which are the equivalent to those for other ordinary NAB shares) in respect of the shares, but otherwise cannot deal with the shares until the restriction period concludes. If a participating employee leaves the Group prior to the end of the three year restriction period due to voluntary resignation the shares may be transferred to the employee or sold. If employment is terminated during the restriction period for a reason justifying dismissal the shares are forfeited.

Executive Share Option Plan and Performance Rights Plan
The Group operates a long term incentive programme primarily targeted at key executive positions, delivering performance options and performance rights, linked to the share price of NAB.

The plans provide for the Board of NAB to grant performance options and performance rights to executives of the Group to subscribe for fully paid ordinary shares in NAB. Each performance option or performance right is exchanged for one fully paid ordinary share in NAB upon exercise. The performance options and performance rights cannot be transferred and are not quoted on a recognised stock market. No payment is required from executives at the time of the grant. There are no voting rights or dividends associated with the performance options or performance rights.

The exercise price per performance option is the market price of NAB fully paid ordinary shares as at the date the performance option was granted or such other relevant date determined by the Board of NAB.

The holder of performance rights must pay a nominal exercise price in order to exercise those rights. The total exercise price payable on the exercise of any performance rights on a particular day is A$1, irrespective of the number of rights exercised that day.

The fair value of the options granted is determined using option pricing models, which take into account the exercise price of the option, the current share price, the risk free interest rate, the expected volatility of the NAB share price over the life of the option and other relevant factors. In the absence of market prices, the fair value of the instruments at the date the grant is estimated using an appropriate valuation technique.

Except for those which include terms related to market conditions, vesting conditions included in the terms of the grant are not taken into account in estimating fair value.

The following significant assumptions were adopted to determine the fair value of options and performance rights at each issue date:

Grant date	16-Jan-09	28-Feb-08	14-Feb-08	28-Aug-07
Risk-free interest rate (per annum)	3.47%	6.54%	6.54%	6.10%
Life of options	4 years	3.5 years	4 years	5 years
Volatility of share price	36.00%	19.00%	19.00%	15.00%
Dividend rate (per annum)	5.30%	4.50%	4.50%	4.40%
Exercise price of options	A$19.89	-	A$31.70	A$43.43
Fair value of performance options	A$3.54	-	A$3.73	A$2.69
Fair value of performance rights	-	A$26.18	-	-

37. Share based payments (continued)

Grant date	03-Aug-07	07-Feb-07	31-Oct-06	31-Jul-06
Risk-free interest rate (per annum)	6.19%	5.90%	5.80%	5.90%
Life of options	5 years	5.5 years	4.75 years	5.5 years
Volatility of share price	15.00%	15.00%	15.00%	15.50%
Dividend rate (per annum)	4.40%	4.70%	4.90%	5.00%
Exercise price of options	A$40.91	A$40.91	A$38.29	A$35.50
Fair value of performance options	A$2.68	A$4.20	A$3.73	A$3.98
Fair value of performance rights	A$13.57	A$18.67	A$19.59	A$20.11

Grant date	03-May-06	03-May-06	06-Feb-06	06-Feb-06
Risk-free interest rate (per annum)	5.70%	5.70%	5.20%	5.20%
Life of options	5.5 years	5.5 years	5.5 years	5 years
Volatility of share price	15.00%	15.00%	15.00%	15.00%
Dividend rate (per annum)	5.00%	5.00%	5.30%	5.30%
Exercise price of options	A$37.55	A$34.53	A$34.53	A$34.53
Fair value of performance options	A$3.75	A$4.65	A$3.39	A$3.23
Fair value of performance rights	A$19.51	A$19.51	A$18.23	-

Grant date	19-Dec-05	08-Jul-05	22-Feb-05	07-Feb-05
Risk-free interest rate (per annum)	5.20%	5.10%	5.40%	5.30%
Life of options	5 years	5 years	5 years	5 years
Volatility of share price	15.00%	16.00%	16.00%	16.00%
Dividend rate (per annum)	5.30%	5.80%	5.80%	5.80%
Exercise price of options	A$31.78	A$29.93	A$30.41	A$29.93
Fair value of performance options	A$2.74	A$2.80	A$1.54	A$2.80
Fair value of performance rights	A$17.11	A$18.31	A$7.37	A$17.15

The movement in share options and performance rights granted since March 2003 and exercised during the year was as follows:

Share options	**2009**		2008	
	Number	**Weighted Average Exercise Price A$**	Number	Weighted Average Exercise Price A$
Outstanding at 1 October	**7,341,460**	**34.81**	7,169,809	34.89
Granted during the year	**190,338**	**19.89**	171,651	31.70
Forfeited during the year	**(1,083,795)**	**33.92**	-	-
Outstanding at 30 September	**6,448,003**	**34.52**	7,341,460	34.81
Exercisable at 30 September	**2,854,300**		3,612,109	

No share options were exercised during the year (2008: Nil). For share options outstanding at 30 September 2009, the weighted average remaining contractual life is 3.58 years (2008: 3.05 years). The range of exercise prices for options outstanding at the end of the year were A$19.89 to A$43.43 (2008: $26.59 - $43.43).

37. Share based payments (continued)

Performance rights	**2009 Number**	**2009 Weighted Average Exercise Price A$**	2008 Number	2008 Weighted Average Exercise Price A$
Outstanding at 1 October	**1,523,791**	**1.00**	1,522,101	1.00
Granted during the year	**-**	**1.00**	1,690	1.00
Forfeited during the year	**(2,906)**		-	
Outstanding at 30 September	**1,520,885**	**1.00**	1,523,791	1.00
Exercisable at 30 September	**782,137**		633,151	

No performance rights were exercised during the year (2008: Nil). For performance rights outstanding at 30 September 2009, the weighted average remaining contractual life is 3.59 years (2008: 3.59 years). The range of exercise prices for options outstanding at the end of the year were A$1.00 to A$35.50 (2008: $1.00 to $35.50).

38. Directors' emoluments

	(1) Salary and fees £'000	(2) Benefits and allowances £'000	Performance Related Pay: Short Term (3) Annual (cash) £'000	Performance Related Pay: Short Term (3) Deferred (shares) £'000	Performance Related Pay: Total Short Term PRP £'000	Performance Related Pay: Long Term Incentive Scheme (4) Shares £'000	Total Emoluments £'000
2009							
Total	**1,731**	**379**	**625**	**156**	**781**	**1,015**	**3,906**
Highest Paid Director	**436**	**205**	**114**	**114**	**228**	**790**	**1,659**
2008							
Total	1,579	424	1,103	354	1,457	1,763	5,223
Highest Paid Director (5)	421	190	495	99	594	809	2,014

In addition to amounts shown in the above table, social security costs were payable in respect of emoluments for directors amounting to £444,000 (2008: £716,000) and in respect of emoluments for the Highest Paid Director of £205,000 (2008: £298,000).

Notes

(1) Salary costs include salaries paid to executive directors and fees paid to non-executive directors.
(2) Benefits and allowances include cash payments in lieu of pension contributions and other taxable allowances and benefits. Retirement benefits accrued to one director under a defined benefit pension plan. Pension contributions amounting to £26,000 (2008: £32,000) were paid during the year of which contributions for the Highest Paid Director amounts to £Nil (2008: £Nil).
(3) Performance related pay relates to the respective financial year. The cash element will be paid in the forthcoming year and deferred amount represents shares deferred for one year.
(4) The long term incentive scheme amounts represents share options, share rights and deferred shares for services rendered during the year which require the achievement of performance hurdles and/or milestones before they vest. Typical, the performance period is three years. The value attributed is the fair value of the shares at the date of granting. No director exercised share options during the year (2008:Nil). Three directors (2008: Three) were entitled under a long term incentive scheme.
(5) The 2008 Total Emoluments for the Highest Paid Director exclude social security costs which are separately disclosed above.

39. Fair values of financial instruments

Financial instruments include both financial assets and financial liabilities and also derivatives. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. For the purposes of this note, carrying value refers to amounts reflected in the Consolidated Balance Sheet.

Group	Footnote	**2009** Carrying Value £m	**2009** Fair value £m	2008 Carrying Value £m	2008 Fair value £m
Financial assets					
Cash and balances with supervisory central banks	(a)	**2,713**	**2,713**	5,109	5,109
Loans and advances to other banks	(b)	**340**	**340**	522	522
Derivative financial assets (on balance sheet)	(c)	**942**	**942**	602	602
Other financial assets at fair value	(d)	**5,983**	**5,983**	4,276	4,276
Investments	(e)	**2,180**	**2,186**	7	7
Loans and advances to customers	(e)	**27,147**	**28,091**	28,656	28,656
Due from customers on acceptances	(a)	**2**	**2**	3	3
Due from related entities	(f)	**1,971**	**1,971**	1,153	1,153
Other assets	(g)	**368**	**368**	708	708
Financial liabilities					
Due to other banks	(e)	**1,920**	**1,963**	3,962	3,962
Derivative financial liabilities (on balance sheet)	(c)	**113**	**113**	36	36
Other financial liabilities at fair value	(d)	**597**	**597**	553	553
Due to customers	(e)	**26,656**	**26,755**	22,334	22,334
Liabilities on acceptances	(a)	**2**	**2**	3	3
Bonds and notes	(e)	**5,287**	**5,375**	5,451	5,451
Due to related entities	(f)	**3,321**	**3,321**	5,151	5,151
Other liabilities	(h)	**1,682**	**1,682**	1,930	1,930

The fair value estimates are based on the following methodologies and assumptions:

(a) The carrying amounts of these financial assets and financial liabilities approximate fair value.

(b) The carrying value of loans and advances is net of allowance for impairment losses and unearned income. The fair values of loans and advances equate to the carrying value at 30 September.

(c) The fair value of derivatives, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from quoted closing market prices as at the balance sheet date, discounted cash flow models or option pricing models as appropriate.

(d) The fair value of assets and liabilities designated as being carried at fair value through profit or loss are based on quoted market prices and data or valuation techniques based upon observable market data as appropriate to the nature and type of the underlying instrument.

(e) The fair value of these financial assets and financial liabilities are obtained from discounted cash flow models. This information was not available for 2008.

(f) The carrying amount of amounts due from and due to related entities is considered to approximate fair value as they are repayable on demand.

(g) Other financial assets include accrued interest receivable.

(h) Other financial liabilities include accrued interest payable and notes in circulation.

40. Financial risk management

Strategy in using financial instruments

By their nature, the Group's activities are principally related to the use of financial instruments including derivatives. The Group accepts deposits from customers at both fixed and floating rates for various periods, and seeks to earn above-average interest margins by investing these funds in high-quality assets. The Group seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due.

The Group also seeks to raise its interest margins by obtaining above-average margins, net of allowances, through lending to commercial and retail borrowers with a range of credit standing. Such exposures involve not just on-balance sheet loans and advances, but the Group also enters into guarantees and other commitments such as letters of credit and performance, and other bonds.

Fair value hedges
The Group hedges part of its existing interest rate and foreign currency risk resulting from any potential decrease in the fair value of fixed rate assets or increase in fair value of fixed rate liabilities attributable to both interest rate and foreign currency risk denominated both in local and foreign currencies using interest rate, cross currency interest rate and cross currency swaps. The net fair value of these swaps is disclosed in note 11.

Cash flow hedges
The Group hedges a portion of the variability in future cash flows attributable to interest rate risk of variable interest rate assets and liabilities, using interest rate swaps, forward rate agreements and futures contracts.

There were no transactions for which cash flow hedge accounting had to be ceased in 2009 as a result of the highly probable cash flows no longer expected to occur. The fair value of derivatives entered into is disclosed in note 11. The movement in fair value of derivatives deferred within the cash flow hedge reserve to hedge forecast future cash flows is disclosed in note 29.

Credit risk

Credit is defined as any transaction that creates an actual or potential obligation for a borrower to pay the Group. Credit risk is the potential that a borrower will fail to meet its obligations to the Group in accordance with agreed terms.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees, but a significant portion is personal lending where no such collateral can be obtained. The process for valuing collateral and other credit enhancements is described in note 14.

Derivatives
The Group maintains control limits on net open derivative positions (i.e. the difference between purchase and sale contracts), by both amount and term. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Group (i.e. assets where their fair value is positive), which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding. This credit risk exposure is managed as part of the overall lending limits with customers, together with potential exposures from market movements.

Credit-related commitments
Credit-related commitments are facilities where the Group is under a legal obligation to extend credit unless some event occurs, which gives the Group the right, in terms of the commitment letter of offer or other documentation to withdraw or suspend the facilities.
The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Group on behalf of a customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions, are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing.

40. Financial risk management (continued)

Credit-related commitments (continued)

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss of an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

Maximum exposure to credit risk

The Group's credit exposure has been determined in accordance with capital adequacy guidelines. The Group has comprehensive credit risk management policies that restrict the level of exposure to any one borrower or group of borrowers, industries and countries.
Unless otherwise noted, the amount that best represents the maximum credit exposure at reporting date is the carrying value of the financial asset.

The table below shows the maximum exposure to credit risk for the components of the balance sheet, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through use of master netting and collateral agreements.

	Group		Bank	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Cash and balances with central banks	**2,713**	5,109	**2,713**	5,109
Loans and advances to other banks	**340**	522	**339**	14
Derivative financial assets	**942**	602	**424**	270
Other financial assets at fair value	**5,983**	4,276	**5,983**	4,276
Investments	**2,180**	7	**2,486**	7
Loans and advances to customers	**27,147**	28,656	**22,393**	24,506
Due from customers on acceptances	**2**	3	**2**	3
	39,307	39,175	**34,340**	34,185
Contingent liabilities (note 30)	**673**	828	**673**	828
Commitments (note 30)	**9,345**	12,420	**8,595**	10,420
Total credit risk exposure	**49,325**	52,423	**43,608**	45,433

The credit quality of financial assets other than loans and advances to customers, that are neither past due nor impaired, are as follows:

		Investments		
	Due from other banks	**Available for sale**	**Held to maturity**	**Acceptances**
	£m	**£m**	**£m**	**£m**
Group				
2009				
Senior investment grade	340	1,531	639	-
Investment grade	-	9	-	2
Sub investment grade	-	1	-	-
	340	**1,541**	**639**	**2**

40. Financial risk management (continued)

Maximum exposure to credit risk (continued)

	Due from other banks	Investments Available for sale	Investments Held to maturity	Acceptances
	£m	£m	£m	£m
Group				
2008				
Senior investment grade	519	-	-	-
Investment grade	3	7	-	3
Sub investment grade	-	-	-	-
	522	7	-	3
Bank				
2009				
Senior investment grade	339	1,531	884	-
Investment grade	-	9	61	2
Sub investment grade	-	1	-	-
	339	**1,541**	**945**	**2**
Bank				
2008				
Senior investment grade	14	-	-	-
Investment grade	-	7	-	3
Sub investment grade	-	-	-	-
	14	7	-	3

See note 14 for information about the credit quality of loans and advances to customers that are neither past due nor impaired.

Market risk

The focus of the Bank's activity is to provide high quality banking services to its customers. This focus is relationship in nature. As a consequence, the Bank's participation in wholesale markets, along with its use of financial instruments, is to fund its banking activities and to manage the liquidity and interest rate risks arising from these activities. As a result of these activities the Group may be exposed to market risk. These risks are subsequently managed to a *de minimus* risk position in accordance with the Group's trading policy statement.

Prepayment Risk

The level of prepayment risk is not considered material at present. Early repayment charges on fixed rate business loans are calculated on an economic cost basis, fully recompensing the Bank for any loss on the unwinding of the underlying hedge. Early repayment charges on fixed rate mortgages are calculated on a sliding scale basis, whereby an agreed percentage of the balance is charged dependant upon the residual time to maturity of the loan. Although interest rates have fallen during the year the level of prepayments has been lower than otherwise may have been expected due to reduced availability of credit across the market.

40. Financial risk management (continued)

Market risk - Non-trading / Banking positions

Interest rate risk in the banking book (IRRBB)
IRRBB is measured, monitored, and managed from both an internal management and regulatory perspective. The risk management framework incorporates both market valuation and earnings based approaches in accordance with the Group IRRBB policy.
Risk measurement techniques include: Value at Risk (VaR), Earnings at Risk (EaR), interest rate risk stress testing, repricing analysis, cash flow analysis and scenario analysis.

Key features of the internal interest rate risk management model:

- Historical simulation approach utilising instantaneous interest rate shocks.
- Static balance sheet (i.e. any new business is assumed to be matched, hedged or subject to immediate repricing).
- VaR and EaR are measured on a consistent basis.
- 99% confidence level.
- Three month holding period.
- EaR utilises a twelve month forecast period.
- 8 years of business day historical data.
- Rate changes are proportional rather than absolute.
- Investment term for capital is modelled with an established benchmark term of between 1 and 5 years.
- Investment term for core "non-interest bearing" (non-interest rate bearing assets and liabilities) is modelled on a behavioural basis with a term that is consistent with sound statistical analysis.

Model parameters and assumptions are reviewed and updated on at least an annual basis by Non-Traded Market Risk, in consultation with Treasury. Material changes require the approval of the Asset and Liability Committee.

	As at 30 September		**Average value during reporting period**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Value at risk				
Interest Rate Risk	**3**	14	**7**	11
Earnings at risk				
Interest Rate Risk	**13**	4	**7**	3

	Minimum value during reporting period		**Maximum value during reporting period**	
	2009	2008	**2009**	2008
	£m	£m	**£m**	£m
Value at risk				
Interest Rate Risk	**2**	4	**13**	23
Earnings at risk				
Interest Rate Risk	**3**	1	**14**	5

Risk concentration
Concentration of risk is managed by client/ counterparty, by geographical region and by industry sector. In addition single name exposures exist to limit exposure to single entity/counterparty.

40. Financial risk management (continued)

Industry concentration of assets

The following table shows the levels of industry concentration of assets at 30 September:

Group 2009	**Loans designated at fair value through profit or loss £m**	**Loans at amortised cost £m**	**Contingent liabilities and credit related commitments £m**
Government and public authorities	12	24	-
Agriculture, forestry, fishing and mining	527	1,065	395
Financial, investment and insurance	73	276	1,489
Real estate - construction	97	742	314
Manufacturing	140	703	109
Instalment loans to individuals and other personal lending (including credit cards)	120	2,847	5,066
Real estate - mortgage	-	12,327	-
Asset and lease financing	-	1,248	-
Other commercial and industrial	4,358	8,584	2,645
	5,327	**27,816**	**10,018**

	Due from other banks £m	**Investments Available for sale £m**	**Investments Held to maturity £m**	**Acceptances £m**
Government and public authorities	-	-	-	-
Agriculture, forestry, fishing and mining	-	-	-	-
Financial, investment and insurance	340	1,541	639	-
Real estate - construction	-	-	-	-
Manufacturing	-	-	-	2
Instalment loans to individuals and other personal lending (including credit cards)	-	-	-	-
Real estate - mortgage	-	-	-	-
Asset and lease financing	-	-	-	-
Other commercial and industrial	-	-	-	-
	340	**1,541**	**639**	**2**

40. Financial risk management (continued)

Industry concentration of assets (continued)

Group 2008	Loans designated at fair value through profit or loss £m	Loans at amortised cost £m	Contingent liabilities and credit related commitments £m
Government and public authorities	10	31	35
Agriculture, forestry, fishing and mining	327	901	251
Financial, investment and insurance	57	471	2,414
Real estate - construction	44	1,157	267
Manufacturing	99	673	245
Instalment loans to individuals and other personal lending (including credit cards)	95	2,864	4,822
Real estate - mortgage	-	11,868	1,232
Asset and lease financing	-	1,533	-
Other commercial and industrial	3,140	9,820	3,982
	3,772	29,318	13,248

	Due from other banks £m	Investments Available for sale £m	Investments Held to maturity £m	Acceptances £m
Government and public authorities	-	-	-	-
Agriculture, forestry, fishing and mining	-	-	-	-
Financial, investment and insurance	522	7	-	-
Real estate - construction	-	-	-	-
Manufacturing	-	-	-	3
Instalment loans to individuals and other personal lending (including credit cards)	-	-	-	-
Real estate - mortgage	-	-	-	-
Asset and lease financing	-	-	-	-
Other commercial and industrial	-	-	-	-
	522	7	-	3

40. Financial risk management (continued)

Industry concentration of assets (continued)

Bank 2009	**Loans designated at fair value through profit or loss £m**	**Loans at amortised cost £m**	**Contingent liabilities and credit related commitments £m**
Government and public authorities	12	24	-
Agriculture, forestry, fishing and mining	527	1,065	395
Financial, investment and insurance	73	276	739
Real estate - construction	97	742	314
Manufacturing	140	703	109
Instalment loans to individuals and other personal lending (including credit cards)	120	2,847	5,066
Real estate - mortgage	-	8,208	-
Asset and lease financing	-	591	-
Other commercial and industrial	4,358	8,584	2,645
	5,327	**23,040**	**9,268**

		Investments		
	Due from other banks £m	**Available for sale £m**	**Held to maturity £m**	**Acceptances £m**
Government and public authorities	-	-	-	-
Agriculture, forestry, fishing and mining	-	-	-	-
Financial, investment and insurance	339	1,541	945	-
Real estate - construction	-	-	-	-
Manufacturing	-	-	-	2
Instalment loans to individuals and other personal lending (including credit cards)	-	-	-	-
Real estate - mortgage	-	-	-	-
Asset and lease financing	-	-	-	-
Other commercial and industrial	-	-	-	-
	339	**1,541**	**945**	**2**

40. Financial risk management (continued)

Industry concentration of assets (continued)

Bank 2008	Loans designated at fair value through profit or loss £m	Loans at amortised cost £m	Contingent liabilities and credit related commitments £m
Government and public authorities	10	31	35
Agriculture, forestry, fishing and mining	327	901	251
Financial, investment and insurance	57	473	414
Real estate - construction	44	1,157	-
Manufacturing	99	673	245
Instalment loans to individuals and other personal lending (including credit cards)	95	3,343	4,822
Real estate - mortgage	-	8,002	1,232
Asset and lease financing	-	757	-
Other commercial and industrial	3,140	9,819	4,249
	3,772	25,156	11,248

	Due from other banks £m	Investments Available for sale £m	Investments Held to maturity £m	Acceptances £m
Government and public authorities	-	-	-	-
Agriculture, forestry, fishing and mining	-	-	-	-
Financial, investment and insurance	14	7	-	-
Real estate - construction	-	-	-	-
Manufacturing	-	-	-	3
Instalment loans to individuals and other personal lending (including credit cards)	-	-	-	-
Real estate - mortgage	-	-	-	-
Asset and lease financing	-	-	-	-
Other commercial and industrial	-	-	-	-
	14	7	-	3

40. Financial risk management (continued)

Maturity analysis of assets and liabilities

The following tables represent a breakdown of the Group's balance sheet for the last two years as at 30 September according to when the assets and liabilities are expected to be recovered or settled. Many of the longer-term monetary assets are variable rate products, with actual maturities shorter than the contractual terms. Accordingly, this information is not relied upon by the Group in its management of interest rate risk (refer to note 41 for information on interest rate sensitivity). See "Cash flows payable under financial liabilities by contractual maturities" for the Group's contractual undiscounted repayment obligations.

Group 2009	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	2,713	-	-	-	-	-	2,713
Due from other banks	15	325	-	-	-	-	340
Derivative financial assets	-	10	178	727	27	-	942
Other financial assets at fair value	698	374	421	2,208	2,282	-	5,983
Investments	-	639	-	1,541	-	-	2,180
Loans and advances to customers	3,856	-	4,486	3,104	15,701	-	27,147
Due from customers on acceptances	-	2	-	-	-	-	2
Due from related entities	433	1	1,506	6	25		1,971
All other assets	131	-	-	-	-	961	1,092
Total assets	7,846	1,351	6,591	7,586	18,035	961	42,370
Liabilities							
Due to other banks	165	580	623	552	-	-	1,920
Derivative financial liabilities	-	2	13	98	-	-	113
Other financial liabilities at fair value	61	19	36	221	260	-	597
Due to customers	16,223	5,402	3,612	1,419	-	-	26,656
Liabilities on acceptances	-	2	-	-	-	-	2
Bonds and notes	-	179	222	4,436	450	-	5,287
Due to related entities	228	348	1,256	634	855		3,321
All other liabilities	76	-	-	-	-	2,148	2,224
Total liabilities	16,753	6,532	5,762	7,360	1,565	2,148	40,120

40. Financial risk management (continued)

Maturity analysis of assets and liabilities (continued)

Group 2008	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	5,109	-	-	-	-	-	5,109
Due from other banks	-	522	-	-	-	-	522
Derivative financial assets	602	-	-	-	-	-	602
Other financial assets at fair value	378	238	121	1,649	1,890	-	4,276
Investments	-	6	-	-	1	-	7
Loans and advances to customers	5,138	-	4,900	3,263	15,355	-	28,656
Due from customers on acceptances	-	3	-	-	-	-	3
Due from related entities	349	804	-	-	-	-	1,153
All other assets	343	-	-	-	-	1,305	1,648
Total assets	11,919	1,573	5,021	4,912	17,246	1,305	41,976
Liabilities							
Due to other banks	101	2,549	312	1,000	-	-	3,962
Derivative financial liabilities	36	-	-	-	-	-	36
Other financial liabilities at fair value	553	-	-	-	-	-	553
Due to customers	14,006	5,070	2,603	651	4	-	22,334
Liabilities on acceptances	-	3	-	-	-	-	3
Bonds and notes	(4)	450	564	3,991	450	-	5,451
Due to related entities	1,427	784	1,042	50	1,848	-	5,151
All other liabilities	67	-	-	-	-	2,255	2,322
Total liabilities	16,186	8,856	4,521	5,692	2,302	2,255	39,812

The 30 September 2008 All other assets and liabilities balances have been reallocated between call and no specified maturity.

40. Financial risk management (continued)

Maturity analysis of assets and liabilities (continued)

Bank 2009	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Assets							
Cash and balances with central banks	2,713	-	-	-	-	-	2,713
Due from other banks	14	325	-	-	-	-	339
Derivative financial assets	-	10	43	344	27	-	424
Other financial assets at fair value	698	374	421	2,208	2,282	-	5,983
Investments	-	639	-	1,847	-	-	2,486
Loans and advances to customers	3,873	-	4,227	2,592	11,701	-	22,393
Due from customers on acceptances	-	2	-	-	-	-	2
Due from related entities	5,187	198	1,506	6	25	-	6,922
All other assets	125	-	-	-	-	1,262	1,387
Total assets	12,610	1,548	6,197	6,997	14,035	1,262	42,649
Liabilities							
Due to other banks	165	580	623	552	-	-	1,920
Derivative financial liabilities	-	2	13	98	-	-	113
Other financial liabilities at fair value	61	19	36	221	260	-	597
Due to customers	16,223	5,402	3,612	1,419	-	-	26,656
Liabilities on acceptances	-	2	-	-	-	-	2
Bonds and notes	-	179	-	2,324	450	-	2,953
Due to related entities	229	874	1,404	2,964	855	-	6,326
All other liabilities	76	-	-	-	-	1,957	2,033
Total liabilities	16,754	7,058	5,688	7,578	1,565	1,957	40,600

40. Financial risk management (continued)

Maturity analysis of assets and liabilities (continued)

Bank 2008	**Call £m**	**3 months or less £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**No specified maturity £m**	**Total £m As restated**
Assets							
Cash and balances with central banks	5,109	-	-	-	-	-	5,109
Due from other banks	-	14	-	-	-	-	14
Derivative financial assets	270	-	-	-	-	-	270
Other financial assets at fair value	378	238	121	1,649	1,890	-	4,276
Investments	-	6	-	-	1	-	7
Loans and advances to customers	5,617	-	4,572	2,840	11,477	-	24,506
Due from customers on acceptances	-	3	-	-	-	-	3
Due from related entities	349	804	-	-	-	701	1,854
All other assets	343	-	-	-	-	3,548	3,891
Total assets	12,066	1,065	4,693	4,489	13,368	4,249	39,930
Liabilities							
Due to other banks	101	2,549	312	1,000	-	-	3,962
Derivative financial liabilities	36	-	-	-	-	-	36
Other financial liabilities at fair value	553	-	-	-	-	-	553
Due to customers	13,734	5,070	2,603	651	4	-	22,062
Liabilities on acceptances	-	3	-	-	-	-	3
Bonds and notes	(4)	450	564	1,125	450	-	2,585
Due to related entities	1,427	784	1,042	50	1,848	1,120	6,271
All other liabilities	67	-	-	-	-	2,454	2,521
Total liabilities	15,914	8,856	4,521	2,826	2,302	3,574	37,993

The 30 September 2008 All other assets and liabilities balances have been reallocated between call and no specified maturity.

40. Financial risk management (continued)

Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities when they fall due. Liquidity risk arises from the possibility that market conditions prevailing at some point in the future will require the Group to sell positions at a value which is below their underlying worth, or may result in the inability to exit from the positions. The liquidity of a derivative, or an entire market, can be reduced substantially as a result of external economic or market events, market size or the actions of individual participants.

The Group manages liquidity and funding risk through a combination of positive cash flow management, the maintenance of portfolios containing high quality liquid assets, maintenance of a prudent funding strategy and diversification of its funding base. The Group undertakes a conservative approach by imposing internal limits, including stress and scenario testing that are in addition to regulatory requirements.

Cash flows payable under financial liabilities by contractual maturities

Group 2009	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m
Due to other banks	-	711	680	595	-	-	1,986
Derivative financial liabilities	2	-	-	-	-	-	2
Other financial liabilities at fair value	-	1	2	24	52	-	79
Deposits and other borrowings	16,038	6,007	3,512	1,227	-	-	26,784
Liability on acceptances	-	2	-	-	-	-	2
Bonds and notes	-	225	283	4,590	495	-	5,593
All other liabilities	-	-	-	-	-	1,163	1,163
Hedging derivatives							
- contractual amounts payable	-	30	63	122	-	-	215
- contractual amounts receivable	-	(4)	(16)	(73)	-	-	(93)
	16,040	6,972	4,524	6,485	547	1,163	35,731

Group 2008	Call £m	3 months or less £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specified maturity £m	Total £m As restated
Due to other banks	-	1,539	420	2,397	-	-	4,356
Derivative financial liabilities	36	-	-	-	-	-	36
Other financial liabilities at fair value	379	8	20	26	201	-	634
Deposits and other borrowings	14,007	5,124	2,659	700	5	-	22,495
Liability on acceptances	-	3	-	-	-	-	3
Bonds and notes	-	648	830	4,367	511	-	6,356
All other liabilities	-	-	-	-	-	1,211	1,211
Hedging derivatives							
- contractual amounts payable	-	60	119	165	-	-	344
- contractual amounts receivable	-	(56)	(89)	(145)	-	-	(290)
	14,422	7,326	3,959	7,510	717	1,211	35,145

Refer to note 30 for off-balance sheet items disclosed by cashflow maturity.

40. Financial risk management (continued)

Cash flows payable under financial liabilities by contractual maturities (continued)

Bank 2009	**Call £m**	**3 months or less £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**No specified maturity £m**	**Total £m**
Due to other banks	-	711	680	595	-	-	1,986
Derivative financial liabilities	2	-	-	-	-	-	2
Other financial liabilities at fair value	-	1	2	24	52	-	79
Deposits and other borrowings	16,038	6,007	3,512	1,227	-	-	26,784
Liability on acceptances	-	2	-	-	-	-	2
Bonds and notes	-	196	49	2,431	495	-	3,171
All other liabilities	-	-	-	-	-	1,163	1,163
Hedging derivatives							
- contractual amounts payable	-	30	63	122	-	-	215
- contractual amounts receivable	-	(4)	(16)	(73)	-	-	(93)
	16,040	6,943	4,290	4,326	547	1,163	33,309

Bank 2008	**Call £m**	**3 months or less £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**No specified maturity £m**	**Total £m As restated**
Due to other banks	-	1,539	420	2,397	-	-	4,356
Derivative financial liabilities	36	-	-	-	-	-	36
Other financial liabilities at fair value	379	8	20	26	201	-	634
Deposits and other borrowings	13,735	5,124	2,659	700	5	-	22,223
Liability on acceptances	-	3	-	-	-	-	3
Bonds and notes	-	648	830	1,501	511	-	3,490
All other liabilities	-	-	-	-	-	1,211	1,211
Hedging derivatives							
- contractual amounts payable	-	60	119	165	-	-	344
- contractual amounts receivable	-	(56)	(89)	(145)	-	-	(290)
	14,150	7,326	3,959	4,644	717	1,211	32,007

The balances in the cashflow tables above will not agree directly to the balances in the consolidated balance sheet as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments.

The 30 September 2008 comparatives for Group and Bank Hedging derivatives have been restated. The previously reported figures were the notional principal amounts. These amounts now disclosed are the undiscounted cashflow amounts.

41. Interest rate risk

Interest rate sensitivity gap analysis

Part of the Group's return on financial instruments is obtained from controlled mismatching of the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rates or, if earlier, the dates on which the instruments mature. The tables below summarise these repricing mismatches on the Group's non-trading book as at 30 September 2009 and 30 September 2008. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date or the maturity date.

Group 2009	**Weighted average effective interest rate %**	**0 to 3 months £m**	**3 to 12 months £m**	**1 to 2 years £m**	**2 to 3 years £m**	**3 to 4 years £m**	**4 to 5 years £m**	**Over 5 years £m**	**Non interest bearing £m**	**Total £m**
Assets										
Cash assets	2.56	2,631	-	-	-	-	-	-	82	2,713
Balances with supervisory central banks		-	-	-	-	-	-	-	27	27
Due from other banks	6.36	307	6	-	-	-	-	-	-	313
Derivative financial assets		-	-	-	-	-	-	-	942	942
Other financial assets at fair value	3.35	374	412	642	591	602	471	2,001	890	5,983
Investments										
-Available for sale	2.11	1,100	-	125	268	-	48	-	-	1,541
-Held to maturity	2.14	639	-	-	-	-	-	-		639
Loans and advances to customers	5.19	22,753	1,176	1,534	1,016	328	251	89	-	27,147
Due from customers on acceptances		-	-	-	-	-	-	-	2	2
Due from related entities		1,947	-	-	-	-	-	-	24	1,971
All other assets		-	-	-	-	-	-	-	1,092	1,092
Total assets		29,751	1,594	2,301	1,875	930	770	2,090	3,059	42,370
Liabilities										
Due to other banks	2.78	761	659	-	500	-	-	-	-	1,920
Derivative financial liabilities		-	-	-	-	-	-	-	113	113
Other financial liabilities at fair value	4.16	-	5	6	6	10	15	18	537	597
Due to customers	2.06	21,027	3,461	545	540	7	91	-	985	26,656
Liabilities on acceptances		-	-	-	-	-	-	-	2	2
Bonds and notes	3.16	4,087	-	250	950	-	-	-	-	5,287
Due to related entities		2,643	450	-	200	-	-	-	28	3,321
All other liabilities		-	-	-	-	-	-	-	2,224	2,224
Shareholders' equity		-	-	-	-	-	-	-	2,250	2,250
Total liabilities and shareholders' equity		28,518	4,575	801	2,196	17	106	18	6,139	42,370
Off balance sheet items		(2,878)	2,334	979	1,517	(252)	36	(1,736)	-	-
Interest rate sensitivity gap		(1,645)	(647)	2,479	1,196	661	700	336	(3,080)	-
Cumulative gap		(1,645)	(2,292)	187	1,383	2,044	2,744	3,080	-	-

41. Interest rate risk (continued)

Interest rate sensitivity gap analysis (continued)

Group 2008	Weighted average effective interest rate %	0 to 3 months £m	3 to 12 months £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	Over 5 years £m	Non interest bearing £m	Total £m
Assets										
Cash assets	5.10	4,930	-	-	-	-	-	-	153	5,083
Balances with supervisory central banks		-	-	-	-	-	-	-	26	26
Due from other banks	2.95	522	-	-	-	-	-	-	-	522
Derivative financial assets		-	-	-	-	-	-	-	602	602
Other financial assets at fair value	6.84	554	104	276	426	388	542	1,680	306	4,276
Investments										
-Available for sale	5.73	-	-	-	-	-	-	-	7	7
-Held to maturity		-	-	-	-	-	-	-		-
Loans and advances to customers	6.94	23,091	1,567	1,502	1,061	820	372	243	-	28,656
Due from customers on acceptances		-	-	-	-	-	-	-	3	3
Due from related entities		1,140	-	-	-	-	-	-	13	1,153
All other assets		-	-	-	-	-	-	-	1,648	1,648
Total assets		30,237	1,671	1,778	1,487	1,208	914	1,923	2,758	41,976
Liabilities										
Due to other banks	4.11	3,650	312	-	-	-	-	-	-	3,962
Derivative financial liabilities		-	-	-	-	-	-	-	36	36
Other financial liabilities at fair value	3.78	-	8	10	11	13	18	114	379	553
Due to customers	3.79	18,702	2,335	224	189	4	3	4	873	22,334
Liabilities on acceptances		-	-	-	-	-	-	-	3	3
Bonds and notes	5.93	5,001	-	-	250	200	-	-	-	5,451
Due to related entities		5,095	-	-	-	-	-	-	56	5,151
All other liabilities		-	-	-	-	-	-	-	2,322	2,322
Shareholders' equity		-	-	-	-	-	-	-	2,164	2,164
Total liabilities and shareholders' equity		32,448	2,655	234	450	217	21	118	5,833	41,976
Off balance sheet items		(2,602)	1,872	143	1,122	1,061	(187)	(1,409)	-	-
Interest rate sensitivity gap		(4,813)	888	1,687	2,159	2,052	706	396	(3,075)	-
Cumulative gap		(4,813)	(3,925)	(2,238)	(79)	1,973	2,679	3,075	-	-

A negative interest rate sensitivity gap exists when more liabilities than assets reprice during a given period. Although a negative gap position tends to benefit net interest income in a declining interest rate environment, the actual effect will depend on a number of factors, including the extent to which repayments are made earlier or later than the contracted date and variations in interest rate sensitivity within repricing periods and among currencies.

41. Interest rate risk (continued)

Interest rate sensitivity gap analysis (continued)

Bank 2009	Weighted average effective interest rate %	0 to 3 months £m	3 to 12 months £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	Over 5 years £m	Non interest bearing £m	Total £m
Assets										
Cash assets	2.56	2,631	-	-	-	-	-	-	82	2,713
Balances with supervisory central banks		-	-	-	-	-	-	-	26	26
Due from other banks	6.36	307	6	-	-	-	-	-	-	313
Derivative financial assets		-	-	-	-	-	-	-	424	424
Other financial assets at fair value	3.35	374	412	642	591	602	471	2,001	890	5,983
Investments										
-Available for sale	2.11	1,100	-	125	268	-	48	-	-	1,541
-Held to maturity	2.14	945	-	-	-	-	-	-	-	945
Loans and advances to customers	5.19	19,650	754	1,030	651	133	113	62	-	22,393
Due from customers on acceptances		-	-	-	-	-	-	-	2	2
Due from related entities		6,898	-	-	-	-	-	-	24	6,922
All other assets		-	-	-	-	-	-	-	1,387	1,387
Total assets		31,905	1,172	1,797	1,510	735	632	2,063	2,835	42,649
Liabilities										
Due to other banks	2.78	761	659	-	500	-	-	-	-	1,920
Derivative financial liabilities		-	-	-	-	-	-	-	113	113
Other financial liabilities at fair value	4.16	-	5	6	6	10	15	18	537	597
Due to customers	2.06	21,027	3,461	545	540	7	91	-	985	26,656
Liabilities on acceptances		-	-	-	-	-	-	-	2	2
Bonds and notes	3.16	1,753	-	250	950	-	-	-	-	2,953
Due to related entities		5,648	450	-	200	-	-	-	28	6,326
All other liabilities		-	-	-	-	-	-	-	2,033	2,033
Shareholders' equity		-	-	-	-	-	-	-	2,049	2,049
Total liabilities and shareholders' equity		29,189	4,575	801	2,196	17	106	18	5,747	42,649
Off balance sheet items		(2,878)	2,334	979	1,517	(252)	36	(1,736)	-	-
Interest rate sensitivity gap		(162)	(1,069)	1,975	831	466	562	309	(2,912)	-
Cumulative gap		(162)	(1,231)	744	1,575	2,041	2,603	2,912	-	-

41. Interest rate risk (continued)

Interest rate sensitivity gap analysis (continued)

Bank 2008	Weighted average effective interest rate %	0 to 3 months £m	3 to 12 months £m	1 to 2 years £m	2 to 3 years £m	3 to 4 years £m	4 to 5 years £m	Over 5 years £m	Non interest bearing £m	Total £m As restated
Assets										
Cash assets	5.10	4,930	-	-	-	-	-	-	153	5,083
Balances with supervisory central banks		-	-	-	-	-	-	-	26	26
Due from other banks	2.95	14	-	-	-	-	-	-	-	14
Derivative financial assets		-	-	-	-	-	-	-	270	270
Other financial assets at fair value	6.84	554	104	276	426	388	542	1,680	306	4,276
Investments		-	-	-	-	-	-	-	7	7
Loans and advances to customers	5.73	19,747	1,340	1,284	907	701	318	208	1	24,506
Due from customers on acceptances	6.94	-	-	-	-	-	-	-	3	3
Due from related entities		622	-	-	-	-	-	-	1,232	1,854
All other assets		-	-	-	-	-	-	-	3,891	3,891
Total assets		25,867	1,444	1,560	1,333	1,089	860	1,888	5,889	39,930
Liabilities										
Due to other banks	4.11	3,650	312	-	-	-	-	-	-	3,962
Derivative financial liabilities		-	-	-	-	-	-	-	36	36
Other financial liabilities at fair value	3.78	-	8	10	11	13	18	114	379	553
Due to customers	3.79	18,430	2,335	224	189	4	3	4	873	22,062
Liabilities on acceptances		-	-	-	-	-	-	-	3	3
Bonds and notes	5.93	2,135	-	-	250	200	-	-	-	2,585
Due to related entities		5,892	-	-	-	-	-	-	379	6,271
All other liabilities		-	-	-	-	-	-	-	2,521	2,521
Shareholders' equity		-	-	-	-	-	-	-	1,937	1,937
Total liabilities and shareholders' equity		30,107	2,655	234	450	217	21	118	6,128	39,930
Off balance sheet items		(2,602)	1,872	143	1,122	1,061	(187)	(1,409)	-	-
Interest rate sensitivity gap		(6,842)	661	1,469	2,005	1,933	652	361	(239)	-
Cumulative gap		(6,842)	(6,181)	(4,712)	(2,707)	(774)	(122)	239	-	-

42. Management of risk

Effective management of risk is a key capability for a successful financial services provider, and is fundamental to the Clydesdale Bank Group's ("CB Group") strategy, as well as that of its ultimate parent entity National Australia Bank Limited ("NAB Group"). A key component of the NAB Group's risk management strategy is the establishment by the Board of a formal 'risk appetite statement' for the NAB Group and all major subsidiaries.

This places an overall limit on the total amount of risk that the NAB Group is prepared to take. This position is set with respect to the returns that the NAB Group is seeking to provide to shareholders, the credit rating that the NAB Group is seeking to maintain, and the NAB Group's capital position and desired capital ratios.

This position informs the CB Group's risk, capital and business management limits and policies. It is periodically reviewed by the Boards as a part of the strategic planning process, or as the commercial circumstances of the CB Group change.

In line with the NAB Group Risk Charter, the CB Group's approach to risk management is based on an overriding principle that risk management capability must be embedded within the business' front-line teams to be effective. This overriding principle embodies the following concepts:

- all business decisions proactively consider risk;
- business managers use the risk management framework which assists in the appropriate balancing of both risk and reward components;
- all employees are responsible for risk management in their day-to-day activities; and
- risk management is a core competency area for all employees.

The CB Group manages risk within an established 'three lines of defence' framework. Control is exercised through clearly defined delegation of authority, with clear and rapid communication and escalation channels throughout the organisation. The first line of defence comprises the business units managing the risks associated with their activities. The second line encompasses dedicated risk functions who are accountable for independent monitoring and oversight. The third line of defence relates to Internal Audit independently reviewing, monitoring, and testing business unit compliance with risk policies and procedures, and regularly assessing the overall effectiveness of the risk management framework.

The NAB Group Risk Management Committee, chaired by the Group Chief Executive Officer, serves as the principal risk strategy and policy decision making body within the NAB Group, and provides the Principal Board with assurance in the performance of the overall risk management framework. This committee is supported by three sub-committees - NAB Group Credit and Concentrations Limits Committee, NAB Group Asset and Liability Committee, and NAB Group Capital Committee - each with a specialised focus.

Within the UK there is a regional Risk Management Committee comprised of senior regional executives, which serves to provide a leadership focus on key risk issues from a regional perspective. In addition, the European Boards' Risk Committee provides review and oversight of the risk profile and risk appetite of the UK.

The UK risk management team independently monitors and systematically assesses the risk profile within the region against established risk appetite parameters. They also assist the front line businesses in the design and implementation of appropriate risk management policies/strategies, and work with the businesses to promote awareness of the need to manage risk. Together with the NAB Group Risk Management function, efforts continue to evolve the organisational culture and staff behaviour.

Operational risk and compliance

Operational risk is the risk of loss resulting from inadequate or failed processes, people or systems, or from external events. This includes risk relating to the management of ongoing activities, as well as to organisational changes such as project and change initiatives.

42. Management of risk (continued)

Operational risk and compliance (continued)

Various reports are produced at management, Board sub-committee and Board level to assist with their oversight and monitoring obligations. This incorporates regional reporting of risk profiles, key operational risk and events, as well as consideration of external events and their relevance to the NAB Group. This process generates visibility and understanding of the NAB Group's overall operational risk profile.

The Operational Risk Framework ("ORF") is based on a set of core principles and defines the NAB Group's standards for operational risk management and compliance. Its design recognises the importance of embedding operational risk into "business-as-usual" activities. It has particular focus on defining and implementing the right behaviour and incorporating risk considerations into the NAB Group's systems and processes.

The ORF is an essential element of the business strategy, which underpins all operational risk management activities. It includes:
- an established governance structure that is used to ensure consistent application, management and reporting of the operational risk management process. This element also includes the establishment and communication of the NAB Group's operational risk appetite;
- a structured risk management process to facilitate the identification, quantification and management of risks.

Credit risk

Credit risk is the potential that a borrower or a counterparty will fail to meet its obligations in accordance with agreed terms. The NAB Group's credit risk management infrastructure is framed to provide sound management principles and practices for the maintenance of appropriate asset quality across the NAB Group. These principles and practices are followed by the CB Group. Group Credit Policy & Counterparty Credit and Group Portfolio & Models, divisions of NAB Group Risk Management, are responsible for the development and maintenance of credit policies and key credit risk systems.

The management of credit risk within the CB Group is achieved through both the traditional focuses on approval and monitoring of individual transactions and asset quality, analysis of the performance of the various credit risk portfolios and the independent oversight of credit portfolios across the CB Group. Portfolio monitoring techniques cover such areas as industry or geographic concentrations and delinquency trends. Roles and responsibilities between NAB Group Credit Policy & Counterparty Credit and Group Portfolio & Models and the regional Risk Management teams are clearly defined.

Significant credit risk strategies and policies are approved, and reviewed annually, by the NAB Board, and the NAB Risk Committee. Through such policies the NAB Board establishes the NAB Group's tolerance for risk. These policies are delegated to, and disseminated under the guidance and control of, executive management within the UK.

The NAB Group's credit policies, which are subject to ongoing review, are documented and disseminated in a form that provides a consistent view of all major credit policies supporting the credit operations of the NAB Group.

For complex credit products and services, NAB Group Credit Policy & Counterparty Credit and Group Portfolio & Models provide a policy framework that identifies and quantifies risks and establishes the means of mitigating such risks.

Single large exposure policies are in place within the CB Group. Overall composition and quality of credit portfolio exposures are monitored and periodically reported to the CB Board, and, where required, to the relevant regional supervisory authorities.

A key factor in the introduction of new products and services is the identification of credit risk inherent in such products and services. For high risks, this is managed through a process requiring acceptance by all impacted areas of the business and approval by Risk Management Committees prior to implementation.

Non-traded market risk

Non-traded market risk includes liquidity and funding risk, structural interest rate risk and foreign exchange risk.
The primary objective for the management and oversight of non-traded market risk is to maintain the risk profile within approved risk appetite and limits, while implementing strategies that protect current and future earnings from the impact of market volatility.

42. Management of risk (continued)

Non-traded market risk (continued)

Policies, inclusive of risk appetite and limits, are approved by the NAB Board, with Group authority delegated to the NAB Group Asset and Liability Management Committee (Group ALCO) and UK Asset and Liability Management Committee (UK ALCO) for their subsequent implementation and monitoring.

UK ALCO oversees the management of non traded market risks. UK ALCO meets monthly and reports to the UK Risk Committee and the European Board Risk Committee. Treasury is responsible for the development and execution of strategy subject to oversight from Non Traded Market Risk.

Liquidity and funding risk

Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due at acceptable cost. These obligations include the repayment of deposits on-demand or at their contractual maturity dates, the repayment of borrowings and loan capital as they mature, the payment of operating expenses and tax, the payment of dividends and the ability to fund new and existing loan commitments.

Liquidity within the CB Group is managed in accordance with the regulatory requirements of the FSA and with policies approved by the NAB Board, with oversight from UK ALCO and Group ALCO.

To meet the requirements of local regulatory authorities the liquidity of the regional bank is managed on a daily basis as a stand-alone undertaking. UK ALCO delegates daily management responsibilities to the regional treasury operating divisions.

NAB Group policies are applied over and above the requirements of local regulatory authorities, when these supplement local regulatory policy. The combination of regulatory and NAB Group policy requirements results in liquidity being managed through a combination of positive cash flow management, including under a series of assumptions to simulate stressed market conditions, the maintenance of portfolios of high quality liquid assets, and diversification of the funding base. NAB Group Policy uses liquidity scenarios to monitor both 'going concern' and 'name crisis' events. Cash flow mismatch limits have been established to limit the CB Group's liquidity exposure. In addition, regional banks are required to hold liquid asset portfolios to meet unexpected cash flow requirements.

A three-level contingency plan has also been established for management of an escalated liquidity requirement where the CB Group experiences either restricted access to wholesale funding, or a large increase in the withdrawal of funds. The plan identifies triggers on each level, details the action required, allocates the key tasks to individuals, provides a timeframe and defines a management committee to manage the action plan.

Structural interest rate risk

Structural interest rate risk comprises the sensitivity of the CB Group's current and future net interest income to movements in market interest rates.

These are three major contributors to interest rate risk:
- the investment of non-interest bearing deposits and equity into interest-bearing assets;
- the mismatch between repricing dates of interest-bearing assets and liabilities; and
- the inability of the pricing 'basis' for customer asset and liability products to be replicated in the financial markets.

Within the objective to secure stable and optimal net interest income over both a 12-month period and over the long term, mismatch risk can be minimised with the investment of equity and non-interest-bearing deposits targeting the stability of net interest income.

Interest rate risk is principally managed through the use of interest rate swaps and caps/floors. All products are used within approved mandates, with strategies subject to monthly reporting to UK ALCO and Group ALCO.

Interest rate risk management across the NAB Group is directed by NAB Group Treasury, with execution on a UK business basis via CB Group Treasury. UK Risk Committee, through UK ALCO oversight, monitors risk to ensure it remains within approved policy and limits set by the NAB Board.

42. Management of risk (continued)

Structural interest rate risk (continued)

Basis risk is more difficult to manage, given limited market liquidity in basis risk products. To mitigate this risk, CB Group Treasury and the Non-Traded Market Risk team closely monitor pricing strategies, product innovation and marketing, since these play an important role in reducing the mismatch attributable to repricing characteristics of customer assets and liabilities.

A key feature of the risk management and oversight framework in the NAB Group is the use of Value at Risk (VaR) as one of its principal measures for interest rate risk, along with an Earnings at Risk (EaR) measure that calculates the impact on future net interest income over the next 12 months. These limit measures are complemented by sensitivity and scenario analysis.

These risk measures and the independence of NAB Group Treasury and NAB Non-Traded Market Risk management structures have contributed to a transparent interest rate risk management framework within NAB Board approved risk appetite and limits.

Foreign exchange risk

Real foreign exchange exposures arise independently of the accounting process. Such transaction exposures arise from the risk that future cash flows will be converted to Sterling at less favourable rates than at present. The policy of NAB Group is to fully hedge these exposures at the time of commitment, if they are of a material nature. Such hedging of transaction exposures is assessed on a case-by-case basis.

The transactional currency exposures principally arise from dealings with customers and the CB Group maintains a matched position through transactions with NAB Group in order to comply with CB Group's trading policy statement.

43. Capital Management Overview

The Bank is governed by NAB Group's capital management policy. The objectives of the NAB Group's capital management policy are to efficiently manage the capital base to optimise shareholder returns whilst maintaining capital adequacy and satisfying key stakeholders such as regulators and ratings agencies.

The Bank's prime objectives in relation to the management of capital are to comply with the requirements set out by the Financial Services Authority (FSA), the Bank's primary prudential supervisor, to provide a sufficient capital base to cover business risks, maintain a targeted credit rating and to support future business development.

The Bank implemented Basel II requirements from 1 January 2008 in measuring operational and credit risks under the standardised approach. Under Pillar I of Basel II, the Bank calculates its minimum capital requirements based on 8% of RWAs. The FSA then applies a multiplier to this amount to cover risks under Pillar II of Basel II and generate an Individual Capital Guidance (ICG).

The ultimate responsibility for capital adequacy rests with the Board of Directors. The Bank's Asset and Liabilties Committee (UK ALCO), which consists of an Executive Director, Chief Financial Officer and other senior executives, is responsible for the management of the capital process including approving policy, overseeing internal controls and setting internal limits over capital ratios.

The Bank actively manages its capital position and reports this on a regular basis to senior management via UK ALCO and other governance committees. Capital requirements are included within an annual capital management plan with initiatives being executed against this plan.

The Clydesdale Bank Group has fully complied with the FSA's capital requirements throughout the year, and the Group's consolidated capital ratios are as follows:

Regulatory capital

	2009	2008
	£m	£m
Actual capital		
Core Tier 1 capital (less deductions)	**2,187**	2,048
Preference shares	**100**	-
Tier 1 capital (less deductions)	**2,287**	2,048
Tier 2 capital (less deductions)	**1,398**	1,091
Total capital held	**3,685**	3,139
Risk weighted assets	**28,049**	27,687

	2009	2008
	%	%
Tier 1 ratio	**8.2%**	7.4%
Total capital ratio	**13.1%**	11.3%

Regulatory capital consists of Tier 1 capital, which includes share capital, share premium and retained earnings and includes profits up to 30 September 2009. The other component of regulatory capital is Tier 2 capital, which includes subordinated long term debt, provisions and revaluation reserves. FSA adjustments have been included in both Tier 1 and Tier 2 capital.

44. Basel II Capital Requirements Directive Pillar 3 Disclosure

The Financial Services Authority ("FSA") has granted the Bank a waiver direction under BIPRU 11.2.6: (Waiver: Comparable disclosures provided on a consolidated basis by a parent undertaking established in a third country).

The waiver direction can be found on the FSA website. http://www.fsa.gov.uk/pubs/waivers/bipru_waivers.pdf

In line with the FSA waiver direction, the Bank will rely on the following references to comparable National Australia Bank Limited consolidated disclosure to satisfy its Pillar 3 disclosure obligations:

National Australia Bank Limited 2009 Full Year Risk and Capital Report: http://www.nabgroup.com/0,,96819,00.html
National Australia Bank Limited 2009 Full Year Financial Results, Note 1, Section 6 (Supplementary Information) : http://www.nabgroup.com/0,,32863,00.html
National Australia Bank Limited 2009 Annual Financial Report :http://www.nabgroup.com/0,,32863,00.html

With specific reference to securitisation policy, disclosure is made on pages 60 and 153-158 of the National Australia Bank Limited 2009 Annual Financial Report.

The first published disclosure is based on the financial position of CB PLC and NAB as at 30 September 2008. After due consideration by the CB PLC Directors, subsequent Pillar 3 disclosures will be made annually by way of the National Australia Bank Limited Risk and Capital Report. These disclosures will be in line with the FSA Waiver direction as outlined above.

The information contained in these qualitative disclosures has not been audited by the Group's external auditors except to the extent that they are equivalent to those made under accounting requirements and is limited to those required by BIPRU 11.

45. Events after the balance sheet date

On 25 November 2009, the Supreme Court ruled that the level of Unarranged Overdraft Charges are not assessable for fairness under the Unfair Terms in Consumer Contracts Regulations 1999. Subject to ascertaining the position of the Financial Ombudsman, all claims founded solely on unfairness or penalties will fail.

On 8 December 2009, National Australia Group Europe Limited subscribed for £160,000,000 ordinary shares in Clydesdale Bank PLC (via the holding companies of National Europe Holdings Limited and National Europe Holdings (GB) Limited).

There have been no other subsequent events which have occurred post 30 September 2009 that would require disclosure in the Financial Statements of Clydesdale Bank PLC.