ANNUAL REPORT AND ACCOUNTS 2004

‘Our members are at the heart of our business’

Philip Williamson, Chief Executive

Nationwide

We're different because we're a building society. We're run for the benefit of our members, and take pride in championing the rights of consumers.

Our principles of fairness, honesty and openness enable us to offer better rates, fewer charges and an excellent level of service.

We're committed to remaining a building society so that we can continue to offer these benefits to members now and in the future.

Contents

We are the **fourth largest** provider of mortgages in the UK.

We are the **third largest** home for people's savings in the UK.

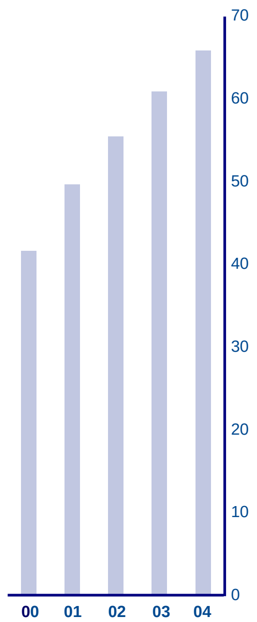
Total assets passed the **£100 billion** mark in February 2004.

As a modern building society we deliver **valuable benefits** to our members.

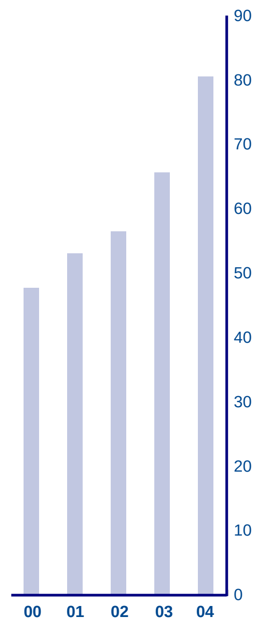
Total pricing benefits delivered since 1996 of nearly **£3 billion.**

The **top financial services provider** in the PressWatch Company Rankings survey for the **third consecutive year.**

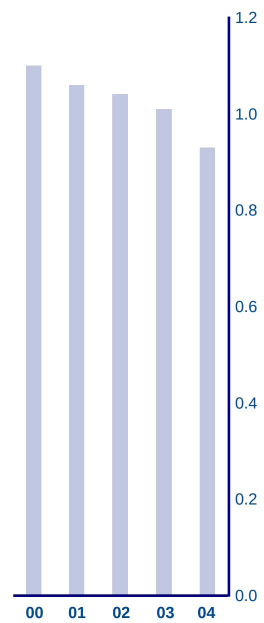
Nationwide. Proud to be different



Member savings balances (£bn)



Loans and advances to customers (£bn)



Cost as a percentage of mean total assets (%)

Total assets over **£100bn**

Profit before tax **£426.8m**

Pricing benefits of **£588m**

Efficiency improved for the **15th** consecutive year

12.8% share of net residential mortgage advances

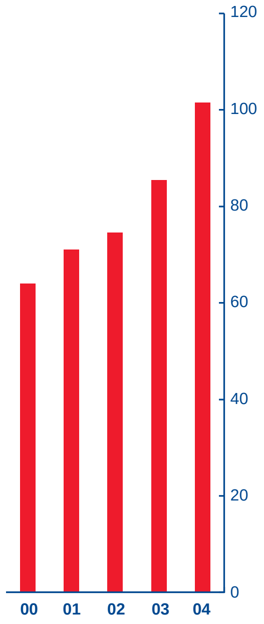
Over **2.7m** current accounts

Member savings increased by **8%**

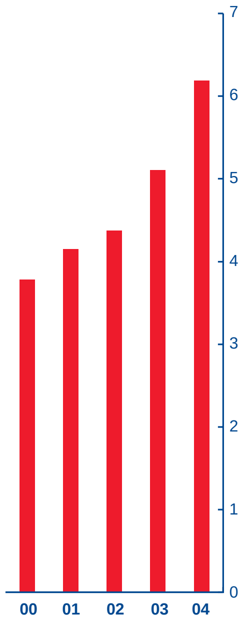
Financial Highlights

	2000	2001	2002	2003	**2004**
Total assets (£m)	64,010.0	71,075.5	74,454.9	85,417.7	**101,428.4**
Loans and advances to customers (£m)	47,818.4	53,124.4	56,664.7	65,733.4	**80,706.2**
Total reserves (£m)	3,256.8	3,636.2	3,888.6	4,186.1	**4,553.0**
Costs as a percentage of mean total assets (%)	1.10	1.06	1.04	1.01	**0.93**
Member savings balances (£m)	41,646.4	49,672.7	55,460.8	60,952.2	**65,943.9**
Total capital (£m)	3,774.2	4,154.8	4,377.2	5,102.2	**6,186.4**

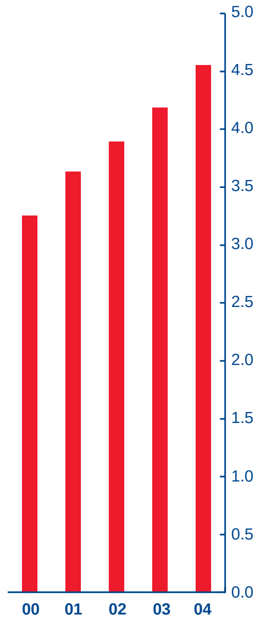
- Total assets up 19% from £85.4 billion to £101.4 billion.
- Costs as a percentage of mean total assets down for the 15th consecutive year to 0.93%.
- Gross capital rose to £6.2 billion from £5.1 billion.
- Loans and advances to customers up 23% from £65.7 billion to £80.7 billion.
- Retained £317.9 million of profit during the year to support the growth of the business.



Total assets (£bn)



Total capital (£bn)



Total reserves (£bn)

Chairman's Statement

Our total assets now exceed £101 billion and our solvency ratio remains strong at 11.7%.

Jonathan Agnew, Chairman

Last year the Society delivered £588 million of pricing benefits to members and achieved post tax profits of £317.9 million, a record total of £906 million of member value. Our total assets now exceed £101 billion and our solvency ratio remains strong at 11.7%. We are the second largest high street taker of retail savings in an highly competitive market. By retaining existing customers and attracting good quality new business, we achieved a market share of net mortgage lending of 12.8%, compared with an historic market share of 7.9%, and are now the fourth largest mortgage provider. We aim to provide very competitive pricing on our products, during the last twelve months, our products appeared in 'best buy' tables in newspapers over 1,500 times.

We achieved a market share of net mortgage lending of 12.8%, compared with an historic market share of 7.9%.

As a mutual, we not only deliver financial value to our members; we also seek to provide them with a high level of service. Independent surveys show that in most areas we achieve this. We continue, however, to look for improvements in service and, when we receive complaints, we try to deal with them in a fair and sympathetic way.

We intend to continue to deliver value to our members and have resolved to improve the efficiency of our business over the next five years through a challenging plan to contain the increase in the Society's costs to a significantly lower growth rate than that of its income. During the year, we have done, and we continue to do, a considerable amount of work to control and reduce risk in the business.

Our successes in the year are attributable to the commitment and professionalism of our employees, led by our management, in meeting the needs of members. The Board thanks them, on your behalf, for their contribution and congratulates them on the results.

Jonathan Agnew

Jonathan Agnew
Chairman

19 May 2004

Chief Executive's Review

As a modern mutual we can achieve a strong financial performance while still being able to deliver consistently good value products and services.

It has been another outstanding year at Nationwide, with members coming to, and staying with us in record numbers. We have demonstrated that as a modern mutual we can achieve a strong financial performance while still being able to deliver consistently good value products and services to our members.

Philip Williamson, Chief Executive

Great value products

During the year, we have continued to expand our range of products and services. We launched two fixed rate bonds – both of which offered exceptional value and were exclusively available to those who have been members for three years or more. In the summer, we celebrated 50 years since the Coronation with the launch of our Members' Coronation Bond. It was followed later in the year with our Members' Christmas Bond. Both bonds offered market-leading rates.

We have improved our hugely popular internet savings account – e-Savings – by adding a guarantee that the interest rate will match or better the Bank of England base rate until the end of March 2005. In response to feedback from our members, we've also increased the maximum amount that can be invested in e-Savings from £50,000 to £2 million.

The value we can offer as a mutual has been recognised again this year by industry experts. Over the past 12 months, we have picked up a string of awards, including 'Best Building Society' from *Your Mortgage* magazine, 'Best Remortgage Lender' from *Mortgage* magazine, and 'Best Direct ISA Provider', 'Best Direct Credit Card' and 'Best Direct Travel Insurance Provider (family)' from *Your Money*.

Fairness and transparency

As well as delivering long-term good value, we have continued to champion the cause of our members. Our approach to mortgage pricing is a prime example of how we've led by example – making our full range of mortgage products equally available to all borrowers. Recently, the Miles report highlighted the iniquity that is common practice in the mortgage market of loyal borrowers subsidising new customers – confirming what we concluded three years ago.

The value we can offer as a mutual has been recognised again this year by industry experts.

As the number of 'convenience' cash machines in corner shops and other retail outlets has continued to grow, our campaign on behalf of consumers generally means that all such cash machines must now display an early warning message when people use them.

Chief Executive's Review (continued)

In October, we became the first financial services organisation in the UK to publish a Summary Box on all of our credit card literature. The new table outlines key rates and charges, making it easier for consumers to compare credit cards from different providers.

One **in five** of our sales is now online or over the telephone, and a quarter of our current account holders use our internet banking service.

World-class service

Our reputation for providing good service was underlined when we were ranked top by the National Complaints Culture Survey, a report endorsed by the Institute of Customer Service. Furthermore, we were ranked as 'world class' in 10 out of 15 separate categories. The survey canvassed the opinion of customers throughout the UK and employees from over 40 organisations.

We handle in excess of 50 million transactions each month, and regrettably there are occasions when we don't get things right, and sometimes complaints arise. Even then, our continuing commitment to delivering exceptional service and our attitude towards complaints are such that we were able to resolve over three quarters of them without involving the Financial Ombudsman Service.

Improving access

We continue to believe that our members should be able to choose how they do business with us – whether it's by phone or post, online or in one of our branches. One in five of our sales is now online or over the telephone, and a quarter of our current account holders use our internet banking service. However, we remain committed to maintaining our branch network and have invested £8.5 million in refurbishing 19 branches and opening a new branch in Halesowen. We've also opened nine new local agencies in small towns and villages where a full branch wouldn't be financially viable, taking our total number of agencies to 198.

To make it easier for people to move their current account to Nationwide, we launched our 'Switcher Pack'. Branded 'the 10-minute current account cure' – it only takes a few minutes to complete the simple application form. From then on, we do the rest, including contacting our member's existing bank, setting up standing orders and informing the Direct Debit companies.

We've worked hard to make sure it's as easy as possible for our members to do business with us, whatever their needs as an individual. Subject to planning permission and where reasonably practicable, all our branches will have level access by October this year, when the Disability Discrimination Act comes fully into force. Every time we refurbish a branch we make sure it has a ground floor interview room accessible for wheelchair users and that the signage is suitable for partially sighted members. To meet the needs of our members whose first language is not English, our branches in west London will soon be trialling a number of initiatives, including wearing name badges and displaying posters in languages that reflect their local communities.

Member involvement

We have continued to listen to our members and, where possible, make improvements based upon their views and opinions. Last year alone, over 120,000 members were personally invited to attend a series of Member TalkBack events, at which they could discuss the issues that affect the running of their Society with our executive and divisional directors. For the benefit of the increasing number of members who do business with us over the internet, we also held two live debates online.

We now contact over 34,000 members every month to ask them about the service and products they receive from us, and their general perceptions of Nationwide. In addition, our employees have recorded over 120,000 pieces of member feedback – from casual remarks to formal complaints – at the point of engagement, helping us to understand and respond to their views. For example, we have improved our Bonus Saver account to allow members to withdraw the annual bonus in the month that it is paid, without affecting the following year's bonus.

In the National Complaints Culture Survey, we were ranked as ‘world class’ in 10 out of 15 separate categories.

Our Annual General Meeting is another example of how we have reacted to our members’ views. Many of them told us that they would like to see the meeting moved away from London to a more central location, and therefore we will be holding this year’s meeting in Birmingham.

Social and environmental responsibility

Following the publication last summer of our first Sustainability Report, we have made good progress in managing our impact on the environment and the communities in which we serve. We now print almost 80% of our marketing literature on recycled paper and are piloting Fairtrade coffee at our main administration centres. We have also significantly reduced our carbon emissions by buying, supply permitting, electricity from renewable sources. We will be publishing our second Sustainability Report on our website – www.nationwide.co.uk – this summer.

We have continued to support many worthy causes, including our flagship charity – Macmillan. Through events such as ‘The World’s Biggest Coffee Morning’ and ‘The Big Hush’, employees and members have raised more than £3 million for the cancer charity since 1993. Our partnership with the Local Heritage Initiative is now helping over 800 groups investigate, explain and care for their local landscape, landmarks and traditions. Most of the projects bring together over 100 members in each community, and three quarters of them involve young people.

Since the inception of our associated charity, The Nationwide Foundation, six years ago, it has supported charities and ‘not for profit’ groups with donations of more than £15 million. In particular, it has continued to support the New Generation Initiative, a collaborative project involving five national charities that seeks to address many of the difficult issues of parenting.

Our people

We are particularly pleased with the development of our culture at Nationwide and that, having continued to invest in our employees, we moved up to 18th in the list of the ‘100 Best Companies to Work For’, published in *The Sunday Times*. We were the highest placed financial services provider for the third year running – an achievement that was particularly satisfying because 80% of our total score was based on what our employees said about what it is like to work for Nationwide. We will publish further details about our performance as an employer in our Sustainability Report.

We moved up to 18th in the list of the ‘100 Best Companies to Work For’, published in *The Sunday Times.*

In contrast to the current trend for relocating call centres abroad, we remain committed to keeping Nationwide’s in the UK. Our call centres in Swindon, Northampton and Swansea employ around 800 people between them, reinforcing our links with the communities from which we have grown. Such is our commitment to safeguarding jobs in this country that we are opening another call centre in Sheffield this summer.

Finally, I would like to add my thanks to those expressed by the Chairman and the Board to our employees. It is their energy, enthusiasm and desire to deliver best value for the benefit of all our members that are at the heart of our continued success. I consider myself very fortunate to work with such a great group of people.

Philip Williamson
Chief Executive

19 May 2004

Operating and Financial Review

Operating Review

Our success in delivering a broad range of financial services products enabled us to increase total assets by 19% from £85.4 billion last year to £101.4 billion.

Graham Beale, Group Finance Director

Nationwide achieved its strategic goals of delivering value to its membership, combined with a healthy profit to support continued investment in the Society and the future growth of the balance sheet. Our success in delivering a broad range of financial services products enabled us to increase total assets by 19% from £85.4 billion last year to £101.4 billion and generated a Profit Before Tax of £426.8 million (2003 – £353.3 million).

During the year we generated over £588 million in the form of pricing benefit to our members by offering better rates and by charging lower fees and charges than our competitors. Over the medium term we aim to fund our growth through retained profits. This year we retained £317.9 million, an increase of 21% on last year, to support the strong 19% growth in our assets over the year. We also invested in our infrastructure and in our people to develop a modern business.

Our member base grew by 370,000 during the year to 11 million. Our members' crossholdings of product groups improved from 1.64 last year to 1.70.

We have continued to develop our distribution channels and this has been a major factor in increasing our market share of net mortgage lending. During the year we refurbished 19 branches (2003 – 17) and opened a new branch office in Halesowen. The strength of Nationwide's retail franchise is key to our strategy and enabled us to continue to increase our level of retail funding.

Mortgages

The Nationwide Group achieved an exceptional £13.2 billion of net lending in 2003/04, representing a market share of 12.8% against a par market share of 7.9%. During the year we overtook Barclays to become the fourth largest lender in the UK.

- The UK experienced a strong mortgage market driven by an increase in re-mortgaging by existing homeowners. Over £285 billion was lent to borrowers with re-mortgaging accounting for nearly 45%. The growth in re-mortgaging reflected the intense competition in the market, with consumers being more willing to move providers in search of a better deal.

- The Society's gross lending was £22.5 billion, an estimated market share of 7.9%. The Society was particularly successful in attracting re-mortgage business, gaining an estimated share of 9.5% of the re-mortgage market.

- We were highly successful in retaining borrowers. This excellent performance was partly driven by our policy of charging between 0.75% to 1.00% less interest on our standard variable rate mortgage compared with our competitors. Good service and an active policy of customer contact also helped us to retain borrowers with maturing fixed rate and tracker rate mortgage products. Our 6.1% market share of principal repaid in the Group was well below our mortgage par share of 7.9%. We estimate this excellent retention performance contributed £4.5 billion to our total net mortgage lending.

The Nationwide Group achieved an exceptional **£13.2 billion** of **net lending** in 2003/04, representing a market share of **12.8%** against a par market share of 7.9%.

- UCB Home Loans, the Society's specialist mortgage lender, also recorded a strong performance with gross mortgage advances of £1.9 billion (2003 – £1.6 billion). UCBHL deals mainly with self certified mortgages, for borrowers who find it difficult to obtain loans from mainstream lenders, and with Buy to Let applications.

We provide a comprehensive range of very competitive mortgage products both directly, through branches, over the phone, via the internet, and through intermediaries. Unlike the majority of other lenders all of our mortgage products are available to both existing and to new customers. We believe it is unfair to offer attractive deals to new customers which are not available to long standing existing customers, a view recently endorsed by Professor David Miles.

Asset quality remains very strong. Our responsible approach to lending has ensured that our arrears levels are better than industry averages.

The average loan to value (LTV) of new residential mortgage lending was 52%, while the estimated LTV of our total book is 38%.

LTV Band	% of book	Cumulative
0%-50%	57.5%	57.5%
51%-75%	32.8%	90.3%
76%-90%	9.0%	99.3%
91%-95%	0.7%	100.0%
96%-100%	0.0%	
Total	**100.0%**	

Mortgage arrears (3 months or more) reduced by 28% from £10.5 million to £7.6 million over the past twelve months. The analysis of the residential mortgage book by arrears time band is:

Number of cases	2003/04	2002/03
No arrears	**97.7%**	96.8%
0 – 3 months arrears	**2.0%**	2.7%
3 – 6 months arrears	**0.2%**	0.3%
6+ months arrears	**0.1%**	0.2%
Total	**100.0%**	100.0%

At 4 April 2004 we had only 56 properties in possession (2003 – 139) out of a total of 1,145,000 mortgage cases.

Savings

The competition for retail funds intensified during the year amongst savings providers, including National Savings. Despite this increased competition, we achieved a 6.9% share of the overall increase in UK retail savings (2003 – 10.4%), representing £5.0 billion (2003 – £5.5 billion) with total retail member deposits as at 4 April 2004 amounting to £65.9 billion (2003 – £60.9 billion).

The great majority of our retail funding is in the form of UK retail member deposits. In addition, we accept offshore deposits and deposits which do not convey member status. We are the third largest deposit taker in the UK (second largest high street provider), and our savings accounts were, on average, 0.43% better priced that those of our competitors.

Strong savings flows were primarily driven by our e-Savings and fixed rate bond products. We also launched two special bonds available only to existing members: a Coronation Bond at a fixed rate of 4.50% and a Christmas Bond at a fixed rate of 5.25%.

Asset quality remains very strong. Our responsible approach to lending has ensured that our arrears levels are better than industry averages.

Banking & Consumer Lending – Personal Loans

Personal loans are offered through the Society's personal loans subsidiary, Nationwide Trust Limited. Gross advances amounted to £929 million (2003 – £763 million), driven by our strategy of offering keener pricing combined in a single rate available to all borrowers irrespective of the amount borrowed. Loans are sold through our retail network, over the telephone and through the internet. Nationwide Trust has in excess of 230,000 unsecured personal loan customers.

A national trend during 2003/04 was the continued growth in unsecured debt, which is at record levels. While the low interest rate, low unemployment environment means that the debt service burden is currently very manageable, the rate at which debt is being accumulated is less sustainable. There is clearly

Operating and Financial Review (continued)

a responsibility on lenders to apply prudent criteria and make sensible lending decisions, but individuals need to be realistic too. We adopt a cautious approach to all of our lending activities, particularly unsecured lending. Last year we rejected one in every two unsecured loan applications received and our credit assessment process looks at the impact of an assumed increase in interest rates to determine a borrower's ability to service their debt in more difficult economic conditions.

Nationwide was the first UK card provider to publish a credit card comparison table to help consumers make an informed choice and successfully lobbied for it to be adopted by all card providers.

Banking & Consumer Lending – Credit Cards

We issued 222,000 new credit card accounts (2003 – 178,000) taking total cards in issue to 868,000 (2003 – 631,000). Balances outstanding on credit cards as at 4 April 2004 amounted to £472 million (2003 – £392 million).

With over 1,300 brands available in the UK, offering a variety of rates, fees, terms and conditions, the credit card market is complex. As part of our drive for greater transparency, Nationwide was the first UK card provider to publish a credit card comparison table to help consumers make an informed choice and successfully lobbied for it to be adopted by all card providers.

Banking & Consumer Lending – Current Accounts

The Society's current account, FlexAccount, is a key product in developing and retaining customer relationships. We offer a highly competitive account with a range of good value features including up to 2.25% credit interest. More than 23% of FlexAccount customers now regularly use our internet banking service and over 1.7 million members are registered to use Nationwide's online banking service.

The Society opened over 508,000 new FlexAccounts during the year (2003 – 382,000) taking the total number of accounts held to 2.7 million, an increase in the year of 17%.

General Insurance

During the year over 529,000 general insurance covers were sold and our general insurance book stood at over 1.6 million covers as at 4 April 2004. The primary general insurance products we sell are:

- buildings and contents insurance;
- travel insurance;
- payment protection policies;
- motor and personal accident insurance.

We typically use leading insurers as third-party underwriters. This provides us with an important source of non-interest income and in 2003/04 we earned £75.5 million (2003 – £71.6 million) from commission and profit share.

Life Insurance

We underwrite two types of insurance product; term life assurance and critical illness cover. Over 96,000 life products were sold during the year representing a 14% increase over last year (2003 – 84,000 products).

We also provide our customers with a range of personal investment products, including, unit trusts, pension contracts, guaranteed equity bonds and equity individual savings accounts (ISAs). At 4 April 2004 our range of unit trust investment products held by our customers had a market value of approximately £1.7 billion (2003 – £1.2 billion).

Our life insurance subsidiary is consolidated in the Group using the embedded value method. The change in the value of the long term life assurance business is included within other operating income and was similar to last year at £44.8 million (2003 – £43.7 million).

As a mutual organisation our strategy and policies are designed to **put our members first**, to maintain our financial strength and to safeguard our assets.

Commercial Lending

Commercial mortgage lending accounted for 14% of our total lending as at 4 April 2004, with balances outstanding of £12.1 billion (2003 – £10.6 billion). Gross advances of £4.1 billion reflected a record year in all three business units which deal with loans:

- to U.K. registered social landlords secured on residential property;
- secured on commercial property; and
- to support Private Finance Initiatives.

Asset quality remains strong. Commercial lending arrears levels of three months or more have improved year on year from 167 to 87 cases. Arrears balances were £3.8 million (2003 – £4.5 million) representing a 16% decrease, equivalent to 0.03% of the total book (2003 – 0.04%).

We are one of the largest lenders to U.K. registered social landlords by amount of assets lent. The number of registered social landlords continued to increase during the year, as local government transfer their municipal housing stocks to private organisations.

Private Finance Initiative (PFI) schemes are being used to fund improvements to local authority housing stock and the development of new social housing, as well as for other initiatives such as the development of new schools and hospitals. We saw an increase in PFI business during the year and this is expected to grow further next year. Advances on PFI loans amounted to £251 million (2003 – £143 million) as Nationwide establishes itself as a major player in this emerging market.

Treasury

Total wholesale funding was increased by £9.4 billion, mainly in support of lending growth. At 4 April 2004, wholesale balances stood at £26.8 billion (2003 – £17.4 billion) representing a funding ratio of 28.9%. During the year the Society has enjoyed a strong appetite from wholesale funding investors and has operated successful Medium Term Note (MTN) programmes in the Dollar, Euro and Sterling markets.

In addition to raising wholesale funds we also raised capital in the year:

- £341.9 million of subordinated debt (within the US MTN programme);
- £400 million of Permanent Interest Bearing Shares (PIBS).

Liquidity balances totalled £17.4 billion at 4 April 2004 (2003 – £17 billion) representing 18.8% of shares and borrowings (2003 – 21.7%).

Pricing Benefit

The Pricing Benefit we generate for our members is calculated by comparing the price of each of our products (including interest rates, fees and charges) against the equivalent products of our main competitors.

Pricing Benefit distributed to members	**2003/04**	2002/03
	£m	£m
Benefit to borrowers	**223**	220
Benefit to savers	**236**	200
Benefit to members with other products	**129**	90
Total	**588**	510

The measurement of the pricing benefit includes the benefits arising from fixed and tracker rate mortgage and fixed interest savings products. This reflects the growing popularity and importance of these products to our savers and borrowers. In 2002/03 and previous years we have excluded the pricing benefits attaching to these products.

Operating and Financial Review (continued)

Regulation

As a mutual organisation our strategy and policies are designed to put our members first, to maintain our financial strength and to safeguard our assets. We aim to maintain a relatively low risk profile and to comply fully with all relevant rules and regulations.

A key theme of our regulator is ‘treating customers fairly’ and we strive to ensure that we remain ahead of our competitors in this regard.

A key theme of our regulator is ‘treating customers fairly’ and we strive to ensure that we remain ahead of our competitors in this regard. In particular, we welcome the introduction of new regulation of mortgages later in 2004 and general insurance early in 2005 and we are actively preparing for the necessary changes that this will entail.

International Accounting Standards (IAS)

The Group, in common with other listed institutions in the European Union, is required to prepare its Annual Report and Accounts under International Financial Reporting Standards (also referred to as International Accounting Standards) for accounting periods commencing on or after 1 January 2005.

We are making good progress in our preparation to produce IAS compliant Annual Accounts. Necessary systems changes are being implemented and revised accounting policies under IAS are currently being drafted.

Basel 2

We have made significant investment to ensure we are compliant with the Basel 2 Capital Accord when it is introduced in 2007. Ongoing work includes the development of risk management systems that will form the core element of our future management information systems and reporting. We believe the composition of our business and the quality of our asset base will lead to Nationwide potentially benefiting from a lower regulatory capital requirement under the new regime.

Profit before tax amounted to £426.8 million an increase of 21%.

Financial Review

The increase in profit was consistent with the Society's strategy of moving to a level of retained earnings that supports the growth in the Balance Sheet.

Overview of the Group's results by Income and Expenditure category

Consolidated Income and Expenditure Statement

	2004 £m	2003 £m
Net interest receivable	**1,098.7**	1,031.1
Other income	**251.0**	227.9
Total income	**1,349.7**	1,259.0
Administrative expenses	**756.8**	715.6
Depreciation and amortisation	**108.8**	91.5
Total administrative expenses and depreciation	**865.6**	807.1
Operating profit before provisions	**484.1**	451.9
Provisions for bad and doubtful debts	**43.6**	49.4
Provisions for contingent liabilities and commitments	**39.9**	11.0
Amounts (released)/written off fixed asset investments	**(26.2)**	38.2
Total provisions	**57.3**	98.6
Profit on ordinary activities before tax	**426.8**	353.3
Tax on profit on ordinary activities	**108.9**	90.6
Profit for the financial year	**317.9**	262.7

Profit

Profit before tax amounted to £426.8 million (2003 – £353.3 million) an increase of 21%. Profit after tax was £317.9 million (2003 – £262.7 million) an increase of 21%. The increase in profit was consistent with the Society's strategy of moving to a level of retained earnings that supports the growth in the Balance Sheet. During the year retained earnings were supplemented with subscribed capital to maintain a strong Solvency Ratio of 11.7% (2003 – 11.7%).

Operating and Financial Review (continued)

Group Net Interest Income

	2004	2003
	£m	£m
Net interest income	**1,098.7**	1,031.1
Average balances:		
• Interest-earning assets	**90,264.0**	74,278.9
• Interest-bearing liabilities	**86,230.9**	70,313.6
Average rates	**%**	%
Average yield on interest-earning assets	**4.29**	4.78
Average rate on interest-bearing liabilities	**3.21**	3.58
Average bank base rate	**3.71**	3.96
Average 3-month Libor	**3.81**	3.98

Group net interest income of £1,098.7 million was £67.6 million or 7% higher than in 2002/03. The net interest margin fell to 1.18% from 1.29% in 2003. This was the consequence of increasing competition causing downward pressure on the spread between savings and lending rates, the continuing fall in the proportion of mortgage balances paying standard variable rates and an increase in the cost of funds compared with base rate. This was partially offset by the rise in base rate and Libor over the year which had a beneficial impact on interest income from interest-free liabilities.

Non-Interest Income

	2004	2003
	£m	£m
Income from investments	**0.4**	0.2
Fees and commissions receivable	**292.8**	247.1
Fees and commissions payable	**(111.1)**	(87.4)
Other operating income	**68.9**	68.0
Total income	**251.0**	227.9

Group non-interest income increased by £23.1 million, or 10% to £251.0 million (2003 – £227.9 million). Fees receivable from lending activity increased by £13 million mainly from higher mortgage volumes. Increased lending also contributed to an increase in commissions receivable from cross-sales of products such as general insurance.

The proportion of lending business introduced through intermediaries increased from 48% in 2002/03 to 57%. As a result, fees and commissions payable increased by £23.7 million to £111.1 million (2003 – £87.4 million).

Other operating income increased 1% or £0.9 million principally due to enhanced income from our long-term life assurance business.

Administrative Expenses and Depreciation

	2004 £m	2003 £m
Staff related expenditure	**388.0**	359.4
Premises, equipment and other	**368.8**	356.2
Total core administrative expenses	**756.8**	715.6
Depreciation	**108.8**	91.5
Total operating expenses	**865.6**	807.1

Total administrative expenses and depreciation increased by £58.5 million, or 7%, to £865.6 million (2003 – £807.1 million). This was against a background of a strong growth in new business with total assets increasing by 19%. As a result, the costs to mean total assets ratio, one of our principal measures of efficiency, improved from 1.01% last year to 0.93% this year. Despite the increase in administration and depreciation costs the cost income ratio remained stable at 64.1%. This will become a key measure of Nationwide's performance over future years.

Employee cost increases are driven by headcount growth and salary and other employee cost inflation, including pension costs. During the year headcount increased by 152 (Full Time Equivalent employees) but is planned to remain flat going forward. The total charge in respect of pensions was £46.1 million (2003 – £47.0 million). As at 4 April 2004 the net retirement benefits liability was £302 million (4 April 2003 – £342 million) as measured under the assumptions contained in Financial Reporting Standard 17 – Retirement Benefits (FRS 17).

In relative terms other costs have been contained, particularly taking into account the additional cost of processing much higher volumes of business.

The increase in depreciation reflects an underlying increase in investment in the infrastructure – additions to fixed assets totalled £130.7 million (2003 - £108.7 million). In addition depreciation on certain insurance system developments was accelerated, giving rise to a one-off charge of £7.8 million, resulting from a change in strategy to comply with the forthcoming regulation of general insurance.

Operating and Financial Review (continued)

Provisions for Bad and Doubtful Debts

	2004 £m	2003 £m
Provisions charge/(credit) for the year:		
Specific - loans fully secured on residential property	**(4.9)**	(4.2)
- loans fully secured on land	**0.5**	6.4
- other loans	**39.0**	29.4
	34.6	31.6
General - loans fully secured on residential property	**8.1**	13.9
- loans fully secured on land	**5.4**	3.6
- other loans	**(4.5)**	0.3
	9.0	17.8
	43.6	49.4

The total charge for bad and doubtful debts fell by £5.8 million to £43.6 million. The combination of high quality lending, low interest rates and high house price inflation all contributed to this reduction. In the two principal loan portfolios, residential and commercial, the accounts 3 months or more in arrears fell by 27% and 48% respectively.

Provisions for Contingent Liabilities and Commitments

Like many other distributors of savings and investment products, Nationwide is facing an increasing level of concern on the part of current and former members and customers about the value of some of their life assurance products and investment policies, particularly endowment policies sold principally before 1990 by the Society, intended as repayment vehicles for mortgage borrowings. Against a background of falling investment returns it is possible that the value of some investment policies will not be sufficient to fully repay mortgages on maturity. Complaints from members, who claim they did not appreciate this risk, are reviewed on an individual basis and with reference to the circumstances prevailing at the date the policies were sold. In some cases this gives rise to the payment of compensation to put the borrower in the equivalent position as if the mortgage had been written on capital repayment terms.

Provisions raised of £39.9 million (2003 – £11.0 million) include £34.1 million (2003 – £11.0 million) for the cost of customer redress relating to all current and potential future endowment review claims based on current trends and investment performance.

Provision has also been made for the cost of loyalty benefits accruing to investors in certain unit trust products that will crystallise on the 10th anniversaries of the sale of the products from 2006 onwards.

Amounts (Released)/Written Off Fixed Asset Investments

	2004 £m	2003 £m
Specific	**(16.3)**	29.1
General	**(9.9)**	9.1
Movement in provision (released)/increase	**(26.2)**	38.2
As a % of investment assets	**(1.6)%**	2.1%

Provisions of £26.2 million were released during the year (2003 – £38.2 million raised) against an investment asset portfolio of £1.6 billion (2003 – £1.8 billion), primarily comprising asset backed securities and corporate bonds. The reduction in the provision reflects an improvement in the underlying value of these assets.

Taxation

The effective rate of tax was 25.5% (2003 – 25.6%), compared with the standard rate of corporation tax of 30%. Nationwide carries out its commercial activities and structures its business in a tax efficient manner and this is reflected in the Group tax charge.

Business Segment Contribution Statement

Nationwide operates three main business segments, Retail, Commercial and Group. The Group segment contains Treasury, Capital and items classified as being non-attributable to our core business areas.

Results by Business Segment

	2004 £m	2003 £m
Residential mortgages	**183.1**	162.4
Consumer lending	**19.8**	28.2
General insurance & life products	**96.1**	97.0
Retail	**299.0**	287.6
Commercial	**174.1**	165.6
Group	**(46.3)**	(99.9)
Profit before tax	**426.8**	353.3

Retail lending is predominantly funded using the retail savings inflows. Wholesale funding and liquidity are used to offset any surplus or shortfall in retail funds.

Operating and Financial Review (continued)

Retail Contribution by Income and Expenditure Category

	2004 £m	2003 £m
Net interest income	**931.7**	858.7
Non-interest income	**195.0**	173.6
Total income	**1,126.7**	1,032.3
Operating expenses	**(749.9)**	(693.8)
Bad debt provisions	**(37.9)**	(39.9)
Provisions for contingent liabilities and commitments	**(39.9)**	(11.0)
Profit before tax	**299.0**	287.6

Retail contribution has increased 4% from £287.6 million to £299.0 million. Residential mortgage contribution has increased by 13% driven by the strong growth in mortgage lending of 15% offset by increased wholesale funding costs. The contribution of our mortgage business was enhanced by containing the costs of securing new business and by strong retention of customers coming to the end of fixed rate and tracker deals. The high quality asset base, low arrears and falling provisions have also enhanced contribution.

The contribution of our mortgage business was enhanced by containing the costs of securing new business and by strong retention of customers coming to the end of fixed rate and tracker deals.

Consumer lending performance has been strong with high levels of business in the year. Contribution has fallen primarily due to keener pricing on personal loans where the rate on unsecured lending fell from 7.9% at the start of the year to 6.7%. We also improved our credit card pricing with a 0% introductory rate on purchases and balance transfers for new credit cards.

General insurance and life business performance was supported by the strong mortgage business although contribution from the life business reduced due to provisions made for the cost of loyalty benefits accruing to investors in certain unit trust products.

Nationwide Building Society has established a high quality portfolio of commercial and Housing Association loans totalling in excess of £12 billion by the year end.

Commercial Contribution by Income and Expenditure Category

	2004	2003
	£m	£m
Net interest margin	**174.6**	170.9
Non-interest income	**46.0**	47.1
Total income	**220.6**	218.0
Administrative expenses	**(40.8)**	(42.9)
Provisions for bad debts	**(5.7)**	(9.5)
Profit before tax	**174.1**	165.6

Nationwide Building Society has been active in commercial lending since the 1980s and has established a high quality portfolio of commercial and Housing Association loans totalling in excess of £12 billion by the year end. The contribution from this activity is used to supplement our mutual agenda.

During the year the margin narrowed due to a combination of competitive pressures in the market place and borrowers refinancing at lower rates. However, the increased volumes of new business bolstered net income. Costs and provisions have been contained below last year's level to give an overall improvement in contribution from £165.6 million to £174.1 million.

The commercial contribution includes at.home nationwide, a wholly owned subsidiary that specialises in high quality residential property rental. The income from at.home nationwide is included in the non-interest income element (2004 £16.8 million; 2003 £17.4 million).

Operating and Financial Review (continued)

Group Contribution by Income and Expenditure Category

	2004	2003
	£m	£m
Net interest income	**(7.6)**	1.4
Non-interest income	**10.0**	7.2
Total income	**2.4**	8.6
Operating expenses	**(74.9)**	(70.3)
Amounts released/(written off) fixed asset investments	**26.2**	(38.2)
Net cost before tax	**(46.3)**	(99.9)

Net interest income has reduced due to the requirement to increase wholesale and capital funding to support the strong growth in lending volumes.

Non-interest income includes income not core to the Group, for example, rental income from residential property associated with retail premises.

Operating expenses includes costs which are not appropriate to allocate to the business segments, for example brand advertising.

The amounts released from provisions against fixed asset investments have supported Group contribution.

Capital Structure

Total capital stood at £6.2 billion (2003 – £5.1 billion) with the Group's total solvency ratio remaining strong at 11.7% (2003 – 11.7%). The Tier 1 solvency ratio stood at 9.3% (2003 – 9.6%). Both ratios remain well in excess of the minimum established by the Society's regulator.

	2004	2003
	£m	£m
Capital: Tier 1	**4,905.8**	4,217.0
Tier 2	**1,308.5**	914.2
Deductions	**(27.9)**	(29.0)
Total capital	**6,186.4**	5,102.2
Total risk weighted assets	**52,765.1**	43,694.9
Risk asset ratios:		
Total capital	**11.7%**	11.7%
Tier 1	**9.3%**	9.6%

We will work hard to deliver another set of excellent results with good growth in all of our key markets, further improvement in our efficiency and stringent control over asset quality.

Group's Profit Ratios

	2004	2003
	%	%
Post tax return on capital	**5.63**	5.55
Post tax return on mean assets	**0.34**	0.33
Post tax return on mean risk weighted assets	**0.66**	0.64

We were very successful in raising both Tier 1 (£400 million of PIBS) and Tier 2 (£341.9 million) capital in the year. The capital was raised to fund the strong growth in the Balance Sheet. There was, and remains, substantial appetite for our credit in the European and US markets. The work undertaken in recent years in developing these sources of funds has proved highly beneficial in enabling the Group to raise the required wholesale funding and additional capital at an attractive rate.

Outlook

We expect higher interest rates to dampen house price and mortgage lending growth over the next year. Equity withdrawal will also become more subdued, although remortgage activity will remain strong. Overall UK net mortgage lending is expected to reduce modestly compared with 2003. Our target is to exceed our par share of net lending for the second consecutive year.

The savings market will remain strong with continuing uncertainty over the strength of the recovery in equity prices. Competition will also remain strong both from National Savings and from a number of lenders who need to raise their share of retail funding to support their net mortgage lending.

The combined competition in the mortgage and savings markets will continue to put downward pressure on interest margins. We expect a number of increases in the Bank of England Base Rate throughout the year, taking it to 4.75-5.00% by the year end. The current position of Libor relative to Base Rate will help mitigate some of the margin squeeze.

We will work hard to deliver another set of excellent results with good growth in all of our key markets, further improvement in our efficiency and stringent control over asset quality. This should lead to the delivery of increased profits while maintaining the distribution of substantial pricing benefits to our members.

Operating and Financial Review (continued)

Risk Management and Control

Overview

The purpose of risk management is to monitor and control the size and concentration of risks arising from our activities. The principal categories of financial risk inherent to our business are:

- liquidity risk;
- market risk, including interest rate risk and foreign currency risk;
- credit risk, including settlement risk; and
- operational risk.

We designed our risk management policy to analyse these risks and set appropriate limits that are consistent with the strengths of our organisation, and we continually monitor these risks and limits by using developed risk management systems.

Management of financial risk is fundamental to our business. We have a formal structure for managing risk, including a risk assessment methodology, established risk limits, reporting lines, mandates, a new product approval process and other control procedures. The Board has delegated specific risk monitoring and control responsibilities to the Audit Committee, the Assets and Liabilities Committee (ALCO), the Credit Committee (Retail) and the Credit Committee (Commercial & Treasury).

The Treasury Division is responsible for the day-to-day management and control of a significant portion of our financial risks and of the risks relating to the Treasury Division's activities, ensuring that those risks and activities are within the parameters set by our Board of Directors, ALCO and the Credit Committees. The Treasury Division reports and makes recommendations to ALCO and the Credit Committees.

Liquidity Risk

The objective of our liquidity policy is to enable us to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding, to maintain full public confidence in our business and to enable us to meet our financial obligations. The development and implementation of policy is the responsibility of ALCO.

The day-to-day management of liquidity is the responsibility of Treasury, which provides funding to, and takes surplus funds from each of the Group's businesses as required. Liquidity policy is approved by the Board and agreed within a framework established by the Financial Services Authority. Regulatory guidelines drive the scope and nature of the Group's holdings of readily realisable liquid assets.

Credit Risk

Credit risk is the risk that a customer or counterparty will not be able to meet its obligations to us as they become due. Credit risk primarily occurs in loans, investment assets and derivative contracts.

The Credit Committee (Commercial & Treasury) and the Credit Committee (Retail) set our credit risk management policy, and the Risk Management Division manages it. Generally, we have distanced the credit decision from our sales force and now make these decisions centrally. We accomplish this by developing, maintaining and using automated credit scoring systems that differentiate credit risks for residential mortgage loans and other consumer products and services. The Risk Management Division assesses the risk profile of large loans. Loans above certain levels also require approval from the relevant Credit Committee or our Board of Directors.

The Risk Management Division also approves and monitors counterparty, industry and country credit limits for all transactions undertaken by the Treasury Division. We constantly monitor and manage our credit exposure to ensure that it remains within authorised credit limits. Breaches of credit limits are reported to the relevant Credit Committee.

We designed our credit risk management policy to control the quality of our loan and investment portfolios. We review several key risks in managing the portfolios to ensure that credit quality is, and remains, acceptable. All credit policies covering lending and counterparty exposure limits are reviewed and approved annually by the Board.

Market Risk

Market risk is the risk that changes in the level of interest rates, foreign currency rates, asset prices or other financial contracts, including derivatives, will adversely impact the result of our operations or our financial condition. Our general activities expose us to market risk, primarily interest rate risk.

We offer numerous mortgage, savings and other financial services products with varying interest rate features and maturities which create interest rate risk exposures. Interest rate risk arises as a result of timing differences on the re-pricing of assets and liabilities and imperfect correlation of interest rates between different financial instruments. Treasury is responsible for managing this exposure within the operational limits set out in the Group's policies.

Currency Risk

We encounter currency risk as a result of activity undertaken by the Group in order to manage borrowing costs and investment returns. The Group raises and invests funds in currencies other than Sterling. As with interest rate risk, Treasury is responsible for managing this exposure within the limits as set out in the Group's policies.

Currency risk is managed primarily through the use of currency swaps and forward foreign exchange contracts. The risk is also managed, when appropriate, by foreign exchange currency liabilities being matched with assets denominated in the same foreign currency.

Equity Risk

We offer certain investment products where we guarantee customers' principal investment, and their return depends on the performance of stock market indices. Our policy is to hedge this risk fully through derivatives.

Operational Risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed internal processes or systems, human error or external events.

The Group's business units manage this risk through appropriate controls and loss mitigation actions, including insurance. These actions include a balance of policies, appropriate procedures and internal controls to ensure compliance with laws and regulations.

Derivatives

We only use derivative instruments, in accordance with the Building Societies Act, to limit the extent to which we will be affected by changes in interest rates, exchange rates or other factors defined by the Building Societies Act. In addition we do not use derivatives for speculative purposes.

Graham Beale

Graham Beale
Group Finance Director

19 May 2004

Board of Directors

For the year ended 4 April 2004

Jonathan Agnew

Philip Williamson

Graham Beale

Brian Walsh

Bernard Simpson

Stuart Bernau

Jonathan Agnew (62)

Chairman

Jonathan Agnew was appointed to the Board in 1997 and became Chairman in 2002. During his career he has been a Managing Director of Morgan Stanley, Group Chief Executive of Kleinwort Benson and Chairman of Limit and of Gerrard Group. He is now Chairman of Beazley Group and, since November of last year, a non-executive Director of Jarvis.

Brian Walsh (59)

Deputy Chairman

Brian Walsh joined the Board in 1999 and became Deputy Chairman in 2002. He is also Chairman of the Society's Audit Committee. His background is in industry and finance, most recently as Vice-Chairman and Finance Director of TI Group plc. Previous positions include Finance Director, GKN plc and executive Director, Credit Suisse First Boston.

Philip Williamson (56)

Chief Executive

Philip Williamson was appointed to the Board in April 1996 and was appointed Chief Executive on 1 January 2002. Prior to his appointment as Chief Executive, he held roles as Retail Operations Director and as Marketing & Commercial Director. Before joining Nationwide he held senior appointments within the banking and property industries.

Bernard Simpson (56)

Deputy Chief Executive & Chief Operating Officer

Bernard Simpson joined the Society in 1989. He was appointed a Director in 1994, Deputy Chief Executive in December 1999 and additionally Chief Operating Officer in 2002. His responsibilities include technology, retail and marketing as well as central administration of all savings, mortgages and insurance.

Graham Beale (45)

Group Finance Director

Graham Beale joined the Society in 1985 and has worked extensively in the finance function and other parts of the Group. He was appointed to the Board on 5 April 2003 with executive responsibility for finance and planning, risk management, legal compliance, internal audit and lending control.

Stuart Bernau (52)

Commercial & Treasury Director

Stuart Bernau joined the Society in 1990 and was appointed a Director in 1996. His current responsibilities include treasury operations, commercial lending, personnel and development and communications. He is also Chairman of the Society's life insurance and unit trust subsidiaries.


Stella David


Ruth Evans


Robert Walther


John Engestrom


Richard Handover


Jim Willens

Stella David (41)

Non-executive Director

Stella David joined the Board on 16 April 2003. Her expertise is in marketing and she is Managing Director of Bacardi-Martini Limited having joined its Board in 1996. She is also President of the Supervisory Board of Bacardi Netherlands NV. Before joining Bacardi she held senior appointments at Golden Wonder.

John Engestrom (62)

Non-executive Director

John Engestrom was appointed a Director in 1997. He is also a Director of the Society's life insurance and unit trust subsidiaries. He is Chairman of the Society's Remuneration Committee. He was previously Group Chief Executive of Mercantile & General Reinsurance, Chief Executive of Liberty Re and ACE Tempest Reinsurance Ltd. He is currently a Director of Wellington Underwriting plc.

Ruth Evans (46)

Non-executive Director

Ruth Evans joined the Board as a non-executive Director on 1 April 2002. She is a lay member of the General Medical Council and Chair of the Standards Committee. Prior to this she was a Director of the National Consumer Council. She also chairs the Independent Inquiry into Drug Testing at Work, is Deputy Chair of the Consumer Panel of Ofcom and holds a number of other public appointments.

Richard Handover (57)

Non-executive Director

Richard Handover was appointed to the Board in 2000. He is Chairman of WHSmith plc, having previously been Chief Executive. He is also Vice-Chairman of Business in the Community, Chairman of the Adult Learning Inspectorate and a non-executive Director of the Royal Mail.

Robert Walther (60)

Non-executive Director

Robert Walther joined the Board as a non-executive Director on 1 July 2002. He was Chief Executive of Clerical Medical from 1995 to 2001, which he joined in 1965. He is currently Chairman of JP Morgan Fleming Claverhouse Investment Trust plc and Fidelity European Values plc.

Jim Willens (47)

Retail Operations Director

Jim Willens joined the Society in 1978 and became a Director on 1 January 2002. He has executive responsibility for our branches, call centres, online internet services and intermediary business. He is also a Director of the Society's life insurance and unit trust subsidiaries and its specialist lending business, UCB Home Loans. Before joining Nationwide, he worked for two major banks.

Directors' Report

For the year ended 4 April 2004

The Directors have pleasure in presenting their Annual Report and Accounts for the year ended 4 April 2004.

Business objectives

The main aim of the Society and its subsidiaries (the 'Group') is to provide a full range of top value, quality financial services that are widely available and delivered with speed, courtesy and reliability. This aim is backed by the key values of fairness, honesty, employee importance and corporate responsibility.

Business review and future developments

The Group's business and future plans are reviewed by the Chairman and Chief Executive on pages 2 to 5 and the Operating and Financial Review on pages 6 to 21.

Profits and capital

Profit before tax was £426.8 million (2003 – £353.3 million). The profit after tax transferred to the general reserve was £317.9 million (2003 – £262.7 million).

Total Group reserves at 4 April 2004 were £4,553.0 million (2003 – £4,186.1 million) after taking into account the revaluation reserve of £211.9 million (2003 – £165.1 million).

Gross capital at 4 April 2004 was £6,170.3 million (2003 – £5,076.5 million) including £925.6 million (2003 – £594.0 million) of subordinated debt and £691.7 million (2003 – £296.4 million) of subscribed capital. The ratio of gross capital as a percentage of shares and borrowings at 4 April 2004 was 6.7% (2003 – 6.5%) and the free capital ratio was 5.9% (2003 – 5.7%). The total solvency ratio at 4 April 2004 was 11.7% (2003 – 11.7%) and the Tier 1 solvency ratio was 9.3% (2003 – 9.6%).

Mortgage arrears

The mortgage portfolio at 4 April 2004 included 571 mortgage accounts (2003 – 798), including those in possession, where payments were more than 12 months in arrears. The total amount of principal loans outstanding in these cases was £32.1 million (2003 – £47.2 million). The total amount of arrears in these cases was £5.4 million (2003 – £8.9 million) or 0.01% (2003 – 0.01%) of total mortgage balances.

Charitable and political donations

During the year the Group made charitable donations of £1,296,965 (2003 – £2,645,239) including £1,000,000 (2003 - £2,100,000) to The Nationwide Foundation. No contributions were made for political purposes. However, as a result of the Political Parties, Elections and Referendums Act 2000 time allowed to employees to carry out civic duties can amount to a donation. The Group supports a very small number of employees in this way.

Creditor payment policy

The Group's policy is to agree the terms of payment with suppliers at the start of trading, ensure that suppliers are aware of the terms of payment and pay in accordance with its contractual and other legal obligations.The Group's policy is to settle the supplier's invoice for the complete provision of goods and services (unless there is an express provision for stage payments), when in full conformity with the terms and conditions of the purchase, within the agreed payment terms.

The Society's creditor days were 24 days at 4 April 2004 (2003 – 19 days).

Employees

During the financial year the Society has maintained and developed systems for the provision of information to employees. The Society has continued to consult actively with the Nationwide Group Staff Union. In addition, meetings, team briefings, circulars, newsletters and the Society's intranet ensure employees are aware of the Society's performance and objectives and the business environment in which it operates.

It is the Society's policy to afford access to training, career development and promotion opportunities equally to all employees regardless of their race, creed, sex, marital status, age, physical or mental disability. Should employees become disabled, it is the Society's policy to continue their employment where possible with appropriate training and redeployment where necessary.

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

This statement which should be read in conjunction with the statement of the auditors on page 35, is made by the Directors to explain their responsibilities in relation to the preparation of the Annual Accounts, the Directors' Emoluments disclosures within the Report of the Directors on Remuneration, the Annual Business Statement and the Directors' Report.

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

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

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

Directors' responsibilities in respect of Accounting Records and Internal Control

The Directors are responsible for ensuring that the Society and its connected undertakings:

- keep accounting records which disclose with reasonable accuracy the financial position of the Society and the Group and which enable them to ensure that the Annual Accounts comply with the Act; and
- establish and maintain systems of control of its business and records, and of inspection and report.

The Directors have general responsibility for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Going concern

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

Directors

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

J G W Agnew MA (Chairman)

B A Walsh MSc (Econ), FCMA, CIMgt (Deputy Chairman)

P F Williamson BA (Econ), FCIB (Chief Executive)

B K Simpson MIMIS, FRSA (Deputy Chief Executive and Chief Operating Officer)

S D M Bernau BSc (Econ), FCIB, MCT (Commercial and Treasury Director)

G J Beale BSc, ACA (Group Finance Director)

J H Willens MBA, DMS, ACIB (Retail Operations Director)

Mrs S J David MA Cantab

J Engestrom MBA

Ms R E Evans MA

R G Handover

R P Walther MA, FIA

Mrs A J Carnwath BA, ACA

G J Beale was appointed Group Finance Director on 5 April 2003 and Mrs S J David was appointed a non-executive Director on 16 April 2003.

Mrs A J Carnwath retired on 24 July 2003.

G J Beale, Mrs S J David, R G Handover and B K Simpson, will retire at the Annual General Meeting on 22 July 2004, and they will all stand for election.

None of the Directors has any beneficial interest in shares in, or debentures of, any connected undertaking of the Society.

The auditors

A resolution to reappoint PricewaterhouseCoopers LLP as auditors will be proposed at the Annual General Meeting.

J G W Agnew
Chairman

19 May 2004

Report of the Directors on Corporate Governance

For the year ended 4 April 2004

The Board of Directors is committed to best practice in corporate governance. This Report on Corporate Governance explains how the Society applies the principles in the Combined Code (the 'Code') on Corporate Governance issued by the Financial Reporting Council in 2003 as well as meeting guidance for building societies issued by the Financial Services Authority (the 'FSA'). Although the Code is intended to apply to listed companies' reporting years beginning on or after 1 November 2003, following a thorough review and the introduction of some changes in its corporate governance arrangements during the year the Board considers that the Society now complies with all the Code provisions unless the contrary is stated.

Directors

The Board

Code Principle: Every company should be headed by an effective Board, which is collectively responsible for the success of the company.

Board comment: The Board's terms of reference are published on the Society's website. The principal functions of the Board are to determine the strategy and policies of the Group, to set out the guidelines within which the business is managed and to review business performance. The Board has a general duty to ensure that the Group operates within the Society's constitution and relevant legislation and regulation and that proper accounting records and effective systems of business control are established, maintained, documented and audited. The Board's terms of reference include a list of specific matters reserved to the Board and a High Level Business Control Manual sets out the structure of delegation of authority by the Board to management.

The Board has three main Committees. These are the Audit Committee, the Nomination Committee and the Remuneration Committee (the latter two Committees having been established with effect from January 2004 in succession to the former combined Senior Appointments & Remuneration Committee (the 'SARC') which has ceased to exist). Each Committee comprises only non-executive Directors and each Committee has a different Chairman. The terms of reference of each Committee are published on the Society's website. The composition of the Committees is shown in the Annexe to this Report. The Deputy Chairman is the Senior Independent Director.

The Board meets as often as necessary for the proper conduct of business, and there are usually at least ten formal Board meetings each year. In addition the non-executive Directors meet without executive Directors present, at least once a year. The attendance record during the year of members at formal meetings of the Board and its Committees is shown in the Annexe.

All Board members have the benefit of appropriate liability insurance at the Society's expense. All Board members have access to independent legal advice if required.

Chairman and Chief Executive

Code Principle: There should be a clear division of responsibilities at the head of the company between the running of the Board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision.

Board comment: The offices of Chairman and Chief Executive are distinct and held by different people. The role of each is set out in their terms of appointment or contract respectively and in their individual performance agreement. The Chairman is responsible for leading the Board and communicating with the Society's members on behalf of the Board. The Chief Executive is responsible for managing the Society's business within the parameters set by the Board.

Board Balance and Independence

Code Principle: The Board should include a balance of executive and non-executive Directors (and in particular independent non-executive Directors) such that no individual or small group of individuals can dominate the Board's decision taking.

Board comment: The Board comprises five executives and seven non-executives (including the Chairman). Apart from the Chairman, for whom the test of independence is considered inappropriate, all non-executive Directors are considered by the Board to be independent in character and judgement and free of any relationship or circumstances which could materially interfere with the exercise of their judgement.

Appointment to the Board

Code Principle: There should be a formal, rigorous and transparent procedure for the appointment of new Directors to the Board.

Board comment: Prior to its dissolution the SARC considered, and following its establishment the Nomination Committee now considers, the balance of skills and experience on the Board and the requirements of the business. The Board has an agreed Board Composition and Succession Plan which is published on the Society's website. Appointments to the Board are made on merit and against objective criteria. Candidates for non-executive Directorship are identified in a variety of ways, including the use of external search consultants by the Board, and in addition members of the Society have the right under the Society's Rules to nominate candidates for election to the Board. All Directors must meet the tests of fitness and propriety laid down by the FSA and all Directors are required to be registered with the FSA as an Approved Person in order to fulfil their Controlled Function as a Director.

The service contracts of executive Directors and the letters of appointment of non-executives are available for inspection on request from the Secretary.

Information and Professional Development

Code Principle: The Board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties. All Directors should receive induction on joining the Board and should regularly update and refresh their skills and knowledge.

Board comment: The Chairman ensures that the Board receives information sufficient to enable it to fulfil its responsibilities. All new Directors undergo formal induction and any training or development needs are identified during this process and in the course of subsequent annual evaluations of the Board's and individual Directors' performance and effectiveness.

Performance Evaluation

Code Principle: The Board should undertake a formal and rigorous annual evaluation of its own performance and that of its Committees and individual Directors.

Board comment: During the year the Board has adopted new methodology to evaluate the performance and effectiveness of individual Directors and of the Board as a whole. Each Director has a Performance Agreement and Personal Development Plan tailored to their individual circumstances (e.g. as Chairman, other non-executive Director, or executive Director). The non-executive Directors are evaluated by the Chairman, taking into account the views of other Directors; the Chairman is evaluated by the non-executive Directors facilitated by the senior independent Director and taking into account the views of the executive Directors; and the Board evaluates its own overall performance. Executive Directors are evaluated within the performance evaluation framework for employees generally and by the Remuneration Committee in context of their remuneration.

Re-election

Code Principle: All Directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance. The Board should ensure planned and progressive refreshing of the Board.

Board comment: The Society's Rules require that all Directors are submitted for election at the Annual General Meeting (the 'AGM') following their first appointment to the Board, except where their appointment occurs in the period between the end of the Society's financial year and the AGM itself, in which case they must seek election at the AGM in the following year, and all Directors are required to seek re-election every three years after first being elected.

The Board's general policy is that non-executive Directors should not expect to serve more than two full three year terms. The Nomination Committee considers and recommends to the Board whether a non-executive Director should be submitted for re-election. Any term lasting beyond the normal six years will be subject to particularly rigorous review and any term lasting beyond nine years will be approved by the Board only in exceptional circumstances and then only on the basis of annual re-election. Currently, two non-executive Directors have served more than two full three year terms; they are Jonathan Agnew (Chairman) and John Engestrom (Chairman of the Remuneration Committee). Mr Engestrom does not expect to stand for re-election for a further term. Mr Agnew expects to retire about the time of the AGM in 2007 by which time he will have served for five years as Chairman as envisaged at the time of his appointment by the Board as Chairman.

Report of the Directors on Corporate Governance

(continued) For the year ended 4 April 2004

Remuneration

The Report of the Directors on Remuneration (on pages 31 to 34) explains how the Society applies the Code principles and its compliance with the Code provisions relating to remuneration.

Accountability and audit

Financial Reporting

Code Principle: The Board should present a balanced and understandable assessment of the company's position and prospects.

Board comment: The responsibilities of the Directors in relation to the preparation of the Society's accounts and a statement that the Society's business is a going concern are to be found within the Directors' Report (on pages 24 and 25).

Internal Control

Code Principle: The Board should maintain a sound system of internal control to safeguard shareholders' investment and the company's assets.

Board comment: The Board is responsible for determining strategies for risk management and control. Senior management are responsible for designing, operating and monitoring risk management and internal control processes, and the Audit Committee, on behalf of the Board, is responsible for reviewing the adequacy of these processes. The Society has a strong compliance culture. The system of internal control is designed to enable the Society to achieve its corporate objectives within a managed risk profile, not to eliminate risk. The Risk Management Division ensures that appropriate risk management systems exist across the spectrum of the Group's operations, and that in particular there is an ongoing process for identifying, evaluating and managing significant risks faced by the Group. This process has operated throughout the year and the process is regularly reviewed at Board level. The Group Internal Audit function provides independent and objective assurance that these processes are appropriate and effectively applied.

The Board has approved a Group Risk Appetite Statement and both the Board and the Audit Committee regularly review the Group Risk Profile in the context of the Group's risk appetite. The Group Risk Profile is compiled by the Risk Management Division based on risk assessment submissions from divisional directors and other senior executives throughout the Group in relation to the areas of the Group's business for which they are responsible. The key risk categories are identified together with the ongoing status in relation to each risk and any actions deemed necessary being taken or planned to mitigate such risks. In particular, the principal categories of financial risk inherent in the Group's business are described in greater detail in the Operating and Financial Review under the heading Risk Management and Control (on pages 20 and 21) together with an explanation of the structure adopted within the Group for managing financial risk (including the roles of the Credit Committees and the Assets and Liabilities Committee). The Chief Executive's Committee, which comprises all executive Directors and all divisional directors, is the principal risk management committee. It reviews the Group Risk Profile on a regular monthly basis and facilitates an integrated approach to risk management across the business as a whole.

The Board has ultimate responsibility for ensuring the effectiveness of the Society's systems of risk management and internal control, and following review by the Audit Committee it is satisfied that the Society's systems are effective and meet the requirements of the Code and the supplementary Turnbull guidance.

Audit Committee and auditors

Code Principle: The Board should establish formal and transparent arrangements for considering how they should apply the financial reporting and internal control principles and for maintaining an appropriate relationship with the company's auditors.

Board comment: The Board has an Audit Committee comprising four non-executive Directors chaired by the Deputy Chairman, all of whom are independent. The Chairman of the Board is not a member of the Committee although he is usually invited to attend meetings of the Committee. The Board is satisfied that at least one member of the Committee has recent and relevant financial experience. The Chairman and all members of the Committee receive supplementary fees in recognition of their additional responsibilities. The terms of reference of the Audit Committee are available on request from the Secretary and are published on the Society's website.

The role of the Audit Committee is to review the integrity of the financial statements, to review the effectiveness of internal controls and risk management systems, to monitor and review the effectiveness of the internal audit function, to consider and recommend to the Board (for approval by the members) the appointment or reappointment of the external auditors and to oversee the relationship with the external auditors, including the development of policy on the engagement of the external auditors for non-audit services.

The policy developed by the Committee on the engagement of the external auditors for non-audit work includes a requirement that the engagement of the auditors for non-audit services requires prior approval of the Committee where the level of fees payable for non-audit services would exceed set threshold proportions of the audit fee, differentiating between non-discretionary services (i.e. those required by external rules to be carried out by the auditors) and discretionary services (i.e. any other services). The Committee is unlikely to sanction any engagement of the auditors for non-audit services where the aggregate fees for all non-audit services would exceed a limit set as a proportion of the audit fee.

The Committee is also responsible for ensuring that there are effective whistleblowing arrangements to enable employees to raise, in confidence, any concerns about possible improprieties in matters of financial reporting or other matters and effective arrangements for investigation of any such concerns raised.

The Audit Committee usually meets six times a year. The Committee usually excludes all executives from part of its meetings and the Committee periodically meets with only the external auditors. By invitation of the Committee, executives and others regularly attending part of its meetings include the Head of Group Audit, the Deputy Chief Executive and Chief Operating Officer, the Group Finance Director, the Divisional Director Risk Management and the external auditors. Minutes of the Committee's meetings are routinely distributed to all Board members and the Chairman of the Committee reports to the Board at each regular meeting of the Board following a meeting of the Committee.

During the past year the Audit Committee has adopted new methodology to evaluate annually the performance and effectiveness of the Committee and its compliance with the requirements of the Code and the supplementary Smith guidance, although the new methodology has not yet completed its first annual cycle. The evaluation process includes the completion of a standard review proforma by members of the Committee and by the Head of Group Audit and a report for agreement by the Committee and submission to the Board.

Relations with shareholders

Dialogue with Institutional Shareholders

Code Principle: There should be a dialogue with shareholders based on the mutual understanding of objectives. The Board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place.

Board comment: As a mutual body, the Society has a membership composed almost exclusively of (currently over 11 million) individuals (rather than institutions), all of whom are the Society's customers. The Society proactively seeks the views of members in a variety of ways. Every month the Society invites 30,000 members to complete a Member Perception Questionnaire and comment on the service they receive. Member TalkBack events (both face to face and via the internet) give members an opportunity to put questions or points to a Director or senior executive. The Member Suggestion Scheme enables members to express their views on an ongoing basis, and a Feedback Log allows employees to record immediately any ad hoc comments from members on any aspect of its business.

The Society conducts market research on a regular basis via telephone surveys, group discussions and conversations, in order to elicit feedback on a wide range of issues. In addition, members' participation in its Usability Centre enables the Society to obtain members' comments on a range of practical measures and initiatives.

Constructive Use of the AGM

Code Principle: The Board should use the AGM to communicate with investors and to encourage their participation.

Board comment: Each year the Society sends details of the AGM and the Postal Ballot for the election of Directors to (currently over 6 million) members who are eligible to vote. Members are sent Voting Forms and are encouraged to vote in the Postal Ballot and to appoint a proxy to vote for them at the AGM if they cannot, or choose not to, attend the AGM. All postal ballot votes and all proxy votes are counted under independent scrutiny. A poll is called in relation to each resolution at the AGM and all proxy votes cast are included in the published results of voting.

All members of the Board are present at the AGM each year (unless exceptionally their absence is unavoidable) and the Chairmen of the Audit and the Remuneration Committees are therefore available to answer questions.

Report of the Directors on Corporate Governance

(continued) For the year ended 4 April 2004

ANNEXE

Board and Committee membership attendance record

Against each Director's name is shown the number of meetings of the Board and its Committees at which the Director was present and in brackets the number of such meetings that the Director was eligible as a member of the Board or Committee to attend during the year.

Director	Board	Audit Committee	SARC	Nomination Committee	Remuneration Committee
J G W Agnew Chairman of Board and the Nomination Committee	10 (10)	–	2 (2)	1 (1)	1 (1)
G J Beale	10 (10)	–	–	–	–
S D M Bernau	10 (10)	–	–	–	–
Mrs A J Carnwath	3 (4)	2 (3)	1 (1)	–	–
Mrs S J David	10 (10)	–	2 (2)	1 (1)	1 (1)
J Engestrom Chairman of the Remuneration Committee	9 (10)	7 (7)	2 (2)	1 (1)	1 (1)
Ms R E Evans	9 (10)	–	2 (2)	–	1 (1)
R G Handover	7 (10)	1 (2)	1 (2)	–	1 (1)
B K Simpson	10 (10)	–	–	–	–
R P Walther	8 (10)	6 (7)	2 (2)	–	1 (1)
B A Walsh Deputy Chairman, Chairman of the Audit Committee and Senior Independent Director	10 (10)	7 (7)	2 (2)	1 (1)	1 (1)
J H Willens	10 (10)	–	–	–	–
P F Williamson	10 (10)	–	–	–	–

J G W Agnew
Chairman

19 May 2004

Report of the Directors on Remuneration

For the year ended 4 April 2004

The Board is committed to best practice in its remuneration policy for Directors. This Report of the Directors on Remuneration explains how the Society applies the principles in the Combined Code on Corporate Governance relating to remuneration. The Society complies with all the Code provisions unless the contrary is stated. In addition, insofar as it is possible for the Society as a mutual organisation without equity share capital to comply with such requirements, this Report addresses the statutory disclosure requirements for listed companies in relation to Directors' remuneration.

The Level and Make-up of Remuneration

Code Principle: Levels of remuneration should be sufficient to attract, retain and motivate Directors of the quality to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive Directors' remuneration should be structured so as to link rewards to corporate and individual performance.

Board Comment: The Society's remuneration policy is to reward Directors through salaries which are regularly compared with salaries for jobs carrying similar responsibilities in comparable organisations, and through other benefits including a bonus scheme designed to recognise corporate and personal performance on an annual basis and an additional incentive plan designed to recognise medium-term corporate performance.

Executive Directors' Emoluments

- The remuneration arrangements for executive Directors, in force during the period covered by the Annual Report and Accounts, are as described in this Report (and where any change in arrangements is envisaged this is stated). Details of executive Directors' emoluments for the year are set out in Table 1.

- Remuneration is assessed by reference to jobs carrying similar responsibilities in comparable organisations. The principal comparator group consists of financial organisations with a similar level of complexity and diversity to the Society. A secondary comparator group including organisations outside financial services is also taken into account.

- Rewards are in three parts and are based on market data from comparator groups. These are basic salary, an annual cash bonus scheme to reward success at the end of the financial year and a medium-term cash incentive scheme by which reward for business success is paid over rolling three-year periods. Payments made as a result of the annual bonus scheme or the medium-term incentive scheme are not pensionable. The Society has no share option scheme and none of the Directors has any beneficial interest in, or any rights to subscribe for, shares in or debentures of any connected undertaking of the Society.

- Basic salaries are normally reviewed annually by reference to jobs carrying similar responsibilities in comparable organisations and in the light of market conditions generally.

- The annual bonus scheme is based on achievement against key corporate performance measures, such as the achievement of financial targets (e.g. in relation to costs, net mortgage lending and profit) and the achievement of operational targets (e.g. in relation to growth in product holdings per member).

  For 2003/04, the scheme was designed to deliver a basic bonus award of 14% of basic salary for executive Directors (17.5% in the case of the Chief Executive) for on-target performance up to a possible maximum of 32% (40% in the case of the Chief Executive) and a possible further payment of up to 25% based on personal performance. For 2004/05, the scheme has been designed to deliver a basic bonus award of 16% of basic salary for executive Directors (20% in the case of the Chief Executive) for on-target performance, with a possible maximum of 40% (49% in the case of the Chief Executive), and a possible further payment of up to 25% (30% in the case of the Chief Executive) based on personal performance.

- The purpose of the medium-term incentive plan is to reward success in achieving corporate performance targets over a longer time scale.

  The plan was redesigned with effect from 2003/04 onwards so that performance is rewarded according to the cumulative increase in total member value, comprising retained post-tax profit and aggregate pricing benefits delivered to members, and also (as a result of a recent change) improvement in the Society's cost:income ratio, over rolling three-year periods. The target bonus for the first three year period (2003/06) is 30% of basic salary (36% in the case of the Chief Executive) with a maximum for exceptional performance of 50% (60% in the case of the Chief Executive). The target bonus for the second three year period (2004/07) is 35% of basic salary (40% in the case of the Chief Executive) with a maximum for exceptional performance of 58% (67% in the case of the Chief Executive).

  During the three-year transitional period, any bonus awards payable under the plan in 2004/05 and 2005/06 will be based on the previous deferred bonus formula which was designed to pay a total bonus in any one year (consisting of instalments from the previous three years) in the region of 24% of basic salary for successful performance with payments of around 40% for exceptional performance.

- Executive Directors are members of the Nationwide Pension Fund, details of which are set out in the Notes to the

Report of the Directors on Remuneration (continued)

For the year ended 4 April 2004

Accounts, and the Nationwide Executive Pension Scheme ('the Executive Scheme'). The Executive Scheme is a funded approved scheme, the purpose of which is to provide an accelerated pension accrual, subject to a maximum of two-thirds of basic salary. The Society's contribution rate to the Executive Scheme is 15%. The Group also has a funded unapproved pension scheme for executive Directors, the purpose of which is to provide that part (if any) of an executive Director's pension which cannot be provided by approved pension arrangements due to Inland Revenue restrictions. The contributions to this scheme are recommended by the scheme's independent actuaries. Table 2 shows the value of executive Directors' pension benefits, including those arising from unapproved schemes.

- Executive Directors receive other taxable benefits including a car or car allowance, healthcare provision and a mortgage allowance. The aggregate amount of these benefits is included in Table 1.

Executive Directors' Contractual Terms

- The standard terms for new executive Director appointments include a contractual notice period of 12 months. Four executive Directors have contracts on this basis; they are (with the date of their contract) P F Williamson (5 April 1996), S D M Bernau (1 November 1996), J H Willens (1 January 2002) and G J Beale (3 March 2003). Any contractual termination payment will not exceed 12 months' salary and accrued benefits. One executive Director, B K Simpson, has a contract which was entered into on 16 April 1992, before the current standard terms were introduced, which is terminable by him on three months' notice or by the Society on payment of an amount equivalent to two years' basic salary.

Non-executive Directors

- The level of fees payable to non-executive Directors is assessed using benchmarks from a comparator group comprising converted and continuing building societies and a secondary group of public limited companies providing comparable services to the Society, including banks and retailers. Details of non-executive Directors' emoluments are set out in Table 1.

- There are no bonus schemes for the Chairman and other non-executive Directors and non-executive Directors do not qualify for pension entitlement.

The Procedure for Determining Remuneration

Code Principle: There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual Directors. No Director should be involved in deciding his or her own remuneration.

- *Board Comment:* The Board established a Remuneration Committee (the 'RemCo') and a Nomination Committee in January 2004 to replace the former combined Senior Appointments & Remuneration Committee (the 'SARC') which has now ceased to exist. The RemCo comprises all the non-executive Directors (identified in Table 1) and is chaired by Mr Engestrom. The SARC also comprised all non-executive Directors and was chaired by the Chairman of the Board. The terms of reference of the RemCo are available on request from the Secretary and are published on the Society's website.

- The RemCo has taken over responsibility from the SARC for the Society's policy on the remuneration of Directors and the top layer of management beneath the Board. By invitation of the Committee, executives and others regularly attending all or part of its meetings include the Chief Executive, the Divisional Director Personnel and Development and an adviser from the Committee's external remuneration consultant Hay Group Ltd (which also advises the Society's management in relation to remuneration matters generally). Minutes of the Committee's meeting are routinely distributed to all Board members and the Chairman of the Committee reports at each Board meeting following a meeting of the Committee.

- The RemCo is responsible for setting the remuneration of the executive Directors, the Chairman and the divisional directors (who principally comprise the top layer of management below the Board). The Chairman of the Board is not present during any discussion of his own remuneration. During the year, the SARC reviewed with Hay Group Ltd the results of recent surveys of comparator groups of financial organisations and public limited companies providing similar services to the Society and was satisfied with the approach and the data. Similar reviews are carried out annually and the process is reviewed every two years.

- The RemCo is not responsible for the remuneration of non-executive Directors (other than the Chairman). Instead, with effect from January 2004, a panel comprising the executive Directors and the Chairman now determines the level of fees for non-executive Directors, with advice from Hay Group Ltd. The panel uses benchmarks from similar comparator groups as used by the RemCo. Until December 2003 the panel comprised the Chief Executive, the Divisional Director Personnel & Development and the Secretary, with advice from an independent consultant, Sir Leonard Peach, and recommended the level of fees for non-executive Directors to the Board for decision.

TABLE 1 Directors' emoluments

Audited information

Non-executive Directors	2004 Fees	2004 Total	2003 Fees	2003 Total
	£000	£000	£000	£000
J G W Agnew (Chairman)	**160**	**160**	119	119
Mrs A J Carnwath (Retired 24 July 2003)	**14**	**14**	43	43
Mrs S J David (Appointed 16 April 2003)	**34**	**34**	–	–
J Engestrom	**55**	**55**	45	45
Ms R E Evans	**35**	**35**	30	30
R G Handover	**37**	**37**	30	30
B A Walsh	**70**	**70**	55	55
R P Walther	**45**	**45**	26	26
	450	**450**	348	348
Pension payments to past Directors in respect of services as Directors		**456**		459

Executive Directors	Salary	Annual bonus	Benefits	Other payments	3-year medium term bonus	Sub-total	Increase in accrued pension	Total
	£000	£000	£000	£000	£000	£000	£000	£000
2004								
P F Williamson (Chief Executive)	**476**	**267**	**28**	**–**	**188**	**959**	**34**	**993**
B K Simpson	**394**	**187**	**26**	**–**	**152**	**759**	**22**	**781**
G J Beale	**245**	**117**	**24**	**–**	**96**	**482**	**56**	**538**
S D M Bernau	**317**	**154**	**25**	**–**	**126**	**622**	**18**	**640**
J H Willens	**245**	**118**	**24**	**–**	**97**	**484**	**15**	**499**
	1,677	**843**	**127**	**–**	**659**	**3,306**	**145**	**3,451**
2003								
P F Williamson (Chief Executive)	425	179	8	–	163	775	63	838
B K Simpson	365	146	26	–	140	677	41	718
A R H Dales (Retired 4 April 2003)	301	96	15	889	116	1,417	18	1,435
S D M Bernau	301	123	25	–	116	565	29	594
J H Willens	203	79	24	–	78	384	28	412
	1,595	623	98	889	613	3,818	179	3,997

Note: £889,457 included in other payments represents the amount Mr Dales received as compensation for his agreed early retirement from office on 4 April 2003. This comprised two year's salary totalling £602,400 and an accrued bonus award of £287,057.

Report of the Directors on Remuneration (continued)

For the year ended 4 April 2004

TABLE 2 Directors' pension benefits

	Accrued pension at 4.4.04	Accrued pension at 4.4.03	**Transfer value at 4.4.04**	Transfer value at 4.4.03	Change in transfer value	Additional pension earned in a year	Transfer value of the increase	Directors' contri-butions in a year
	£000	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**
	(a)	(b)	(c)	(d)	(c – d)	(e)	(f)	
Executive Directors								
P F Williamson (Chief Executive)	**194**	160	**2,948**	2,125	823	30	458	15
B K Simpson	**211**	189	**3,185**	2,493	692	17	262	15
G J Beale	**100**	44	**952**	339	613	55	520	14
S D M Bernau	**167**	149	**2,195**	1,627	568	14	187	15
J H Willens	**116**	101	**1,246**	877	369	12	130	14

Notes:

(a) and (b) show deferred pension entitlements at 4 April 2004 and 2003 respectively.

(c) is the transfer value of the deferred pension in (a) calculated at 4 April 2004.

(d) is the equivalent transfer value at 4 April 2003 of the deferred pension in (b) on the assumption that the Director left service at that date.

(e) is the increase in pension built up during the year recognising the additional service completed and the effect of pay changes in 'real' (inflation adjusted) terms on the pension already earned at the start of the year.

(f) is the capital value of the pension in (e).

J Engestrom
Chairman of the Remuneration Committee

19 May 2004

Independent Auditors' Report

To the members of Nationwide Building Society

We have audited the Annual Accounts which comprise the income and expenditure accounts, the balance sheets, the cash flow statement, the statements of total recognised gains and losses and the related notes which have been prepared under the historical cost convention (as modified by the revaluation of certain fixed assets and investment properties and the valuation of the long term life assurance business), and the accounting policies set out in the statement of accounting policies. We have also audited the disclosures required by the applicable requirements of Part VIII of the Building Societies Act 1986 and regulations made under it contained in the Report of the Directors on Remuneration ('the auditable part').

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

Respective responsibilities of Directors and Auditors

The Directors' responsibilities for the preparation of the Annual Report include responsibilities for the Annual Accounts, the Report of the Directors on Remuneration, the Annual Business Statement and the Directors' Report and are set out in the Directors' Report on pages 24 to 25.

Our responsibility is to audit the Annual Accounts in accordance with relevant legal and regulatory requirements and United Kingdom Auditing Standards issued by the Auditing Practices Board. This report, including the opinion, has been prepared for and only for the Society's members as a body in accordance with Section 78 of the Building Societies Act 1986 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or in to whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the Annual Accounts give a true and fair view, whether the Annual Accounts and the auditable part of the Report of the Directors on Remuneration have been properly prepared in accordance with the applicable requirements of Part VIII of the Building Societies Act 1986 and regulations made under it, on certain information included within the Annual Business Statement, and on whether the Directors' Report is consistent with the accounting records and the Annual Accounts. We also report to you if in our opinion we have not received all the information and explanations we require for our audit, or if the Annual Accounts are not in agreement with the accounting records.

We read the other information contained in the Annual Report and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the Annual Accounts, the Annual Business Statement or the Directors' Report. The other information contained in the Annual Report comprises Financial Highlights, the Chairman's Statement, the Chief Executive's Review, the Operating and Financial Review, the remainder of the Report of the Directors on Remuneration and the Report of the Directors on Corporate Governance.

Basis of audit opinion

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

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

Opinion

In our opinion:

- the Annual Accounts give a true and fair view of the state of affairs of the Society and of the Group as at 4 April 2004 and of the income and expenditure of the Society and the income and expenditure and cash flows of the Group for the year then ended;
- the information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given;
- the information given in the Directors' Report is consistent with the accounting records and the Annual Accounts; and
- the Annual Accounts, the Annual Business Statement, the Directors' Report and the auditable part of the Report of the Directors on Remuneration have each been prepared in accordance with the applicable requirements of Part VIII of the Building Societies Act 1986 and regulations made under it.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
19 May 2004

Income and Expenditure Accounts

For the year ended 4 April 2004

	Notes	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Interest receivable and similar income	1	**3,870.8**	3,547.0	**3,722.2**	3,377.9
Interest payable and similar charges	2	**2,772.1**	2,515.9	**2,761.9**	2,514.7
Net interest receivable		**1,098.7**	1,031.1	**960.3**	863.2
Income from investments	3	**0.4**	0.2	**69.8**	44.0
Fees and commissions receivable		**292.8**	247.1	**245.0**	197.3
Fees and commissions payable		**(111.1)**	(87.4)	**(99.4)**	(71.9)
Other operating income	4	**68.9**	68.0	**6.6**	7.7
Total income		**1,349.7**	1,259.0	**1,182.3**	1,040.3
Administrative expenses	5	**756.8**	715.6	**729.7**	694.9
Depreciation and amortisation	17	**108.8**	91.5	**106.2**	88.8
Operating profit before provisions		**484.1**	451.9	**346.4**	256.6
Provisions for bad and doubtful debts	15	**43.6**	49.4	**36.7**	38.6
Provisions for contingent liabilities and commitments	27	**39.9**	11.0	**34.1**	11.0
Amounts (released)/written off fixed asset investments	13	**(26.2)**	38.2	**(26.2)**	38.2
Profit on ordinary activities before tax		**426.8**	353.3	**301.8**	168.8
Tax on profit on ordinary activities	9	**108.9**	90.6	**83.8**	44.7
Profit for the financial year	31	**317.9**	262.7	**218.0**	124.1

All profits arise from continuing operations.

The accounting policies and notes on pages 41 to 78 form part of these Accounts.

Statements of Total Recognised Gains and Losses

For the year ended 4 April 2004

	Notes	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Profit for the financial year		**317.9**	262.7	**218.0**	124.1
Unrealised surplus on revaluation of properties	30	**49.0**	34.8	**24.4**	16.1
		366.9	297.5	**242.4**	140.2
Translation difference on foreign currency investment		**(7.9)**	2.7	**–**	0.6
Translation difference on foreign currency hedge		**11.3**	(3.8)	**–**	(0.8)
Taxation on translation difference on foreign currency hedge		**(3.4)**	1.1	**–**	0.2
Total gains and losses recognised relating to the year		**366.9**	297.5	**242.4**	140.2

Note of Historical Cost Profits and Losses

For the year ended 4 April 2004

	Group 2004 £m	Group 2003 £m	Society 2004 £m	Society 2003 £m
Reported profit on ordinary activities before tax	**426.8**	353.3	**301.8**	168.8
Unrealised (increase) in valuation of long term life assurance business	**(34.7)**	(3.8)	**–**	–
Realisation of net property revaluation gains of previous year	**2.2**	3.6	**–**	–
Historical cost profit on ordinary activities before tax	**394.3**	353.1	**301.8**	168.8
Historical cost profit for the financial year	**285.4**	262.9	**218.0**	124.1

The accounting policies and notes on pages 41 to 78 form part of these Accounts.

Group Balance Sheet

At 4 April 2004

	Notes	2004	2003
		£m	£m
ASSETS			
Liquid assets			
Cash in hand and balances with the Bank of England		**310.5**	348.4
Loans and advances to credit institutions	11	**1,464.1**	975.8
Debt securities	12	**15,650.8**	15,661.0
Loans and advances to customers			
Loans fully secured on residential property	14	**70,762.2**	57,212.4
Other loans	14	**9,944.0**	8,521.0
Investments			
Equity shares	16	**9.0**	6.6
Tangible fixed assets	17	**857.6**	798.4
Other assets	18	**409.9**	301.4
Prepayments and accrued income	19	**237.4**	121.0
		99,645.5	83,946.0
Long term life assurance business assets	20	**1,782.9**	1,471.7
Total assets		**101,428.4**	85,417.7
LIABILITIES			
Shares	21	**65,943.9**	60,952.2
Amounts owed to credit institutions	22	**2,229.3**	1,758.8
Amounts owed to other customers	23	**4,836.5**	4,539.5
Debt securities in issue	24	**19,706.5**	11,088.1
Other liabilities	25	**419.0**	250.0
Accruals and deferred income	26	**284.6**	259.0
Provisions for liabilities and charges	27	**55.4**	21.9
Subordinated liabilities	28	**925.6**	594.0
Subscribed capital	29	**691.7**	296.4
		95,092.5	79,759.9
Revaluation reserve	30	**211.9**	165.1
General reserve	31	**4,341.1**	4,021.0
		99,645.5	83,946.0
Long term life assurance business liabilities	20	**1,782.9**	1,471.7
Total liabilities		**101,428.4**	85,417.7
MEMORANDUM ITEMS			
Commitments	32	**2,930.6**	3,561.5

Other loans include £849.8 million (2003 – £932.6 million) of loans which are fully secured on residential property but are classified as ‘other loans’ in accordance with the requirements of the Building Societies Act 1997 (Note 14).

The accounting policies and notes on pages 41 to 78 form part of these Accounts.

Approved by the Board of Directors on 19 May 2004.

J G W Agnew, Chairman
B A Walsh, Deputy Chairman
P F Williamson, Director and Chief Executive
G J Beale, Group Finance Director

Society Balance Sheet

At 4 April 2004

	Notes	2004	2003
		£m	£m
ASSETS			
Liquid assets			
Cash in hand and balances with the Bank of England		**306.8**	347.8
Loans and advances to credit institutions	11	**1,332.9**	741.5
Debt securities	12	**14,969.1**	15,115.1
Loans and advances to customers			
Loans fully secured on residential property	14	**64,996.2**	51,994.3
Other loans	14	**8,169.7**	6,946.5
Investments			
Equity shares	16	**1.7**	1.6
Investments in subsidiary undertakings	16	**7,884.4**	7,263.3
Tangible fixed assets	17	**602.5**	572.3
Other assets	18	**110.5**	47.9
Prepayments and accrued income	19	**354.5**	253.2
Total assets		**98,728.3**	83,283.5
LIABILITIES			
Shares	21	**65,943.9**	60,952.2
Amounts owed to credit institutions	22	**2,181.6**	1,758.2
Amounts owed to other customers	23	**5,271.0**	4,830.6
Debt securities in issue	24	**19,399.8**	11,006.7
Other liabilities	25	**307.1**	133.1
Accruals and deferred income	26	**276.4**	252.2
Provisions for liabilities and charges	27	**49.5**	20.8
Subordinated liabilities	28	**925.6**	594.0
Subscribed capital	29	**691.7**	296.4
		95,046.6	79,844.2
Revaluation reserve	30	**110.7**	86.3
General reserve	31	**3,571.0**	3,353.0
Total liabilities		**98,728.3**	83,283.5
MEMORANDUM ITEMS			
Commitments	32	**2,288.0**	3,103.2

Other loans include £260.0 million (2003 – £361.0 million) of loans which are fully secured on residential property but are classified as ‘other loans’ in accordance with the requirements of the Building Societies Act 1997 (Note 14).

The accounting policies and notes on pages 41 to 78 form part of these Accounts.

Approved by the Board of Directors on 19 May 2004.

J G W Agnew, Chairman
B A Walsh, Deputy Chairman
P F Williamson, Director and Chief Executive
G J Beale, Group Finance Director

Consolidated Cash Flow Statement

For the year ended 4 April 2004

	Notes	2004	2003
		£m	£m
Net cash (outflow)/inflow from operating activities	34	**(177.1)**	1,753.0
Returns on investments and servicing of finance			
Interest paid on subordinated liabilities		**(35.2)**	(16.0)
Interest paid on subscribed capital		**(23.8)**	(23.8)
		(59.0)	(39.8)
Taxation		**(95.2)**	(59.2)
Capital expenditure and financial investment			
Purchase of investment securities		**(27,249.5)**	(27,372.9)
Sale and maturity of investment securities		**26,943.9**	25,363.1
Purchase of tangible fixed assets		**(126.8)**	(110.9)
Sale of tangible fixed assets		**13.8**	13.4
		(418.6)	(2,107.3)
		(749.9)	(453.3)
Financing			
Issue of subscribed capital	29	**400.0**	–
Issue of subordinated liabilities	28	**341.9**	473.8
Maturity of subordinated liabilities	28	**–**	(27.1)
(Decrease) in cash	34	**(8.0)**	(6.6)

Statement of Accounting Policies

Accounting convention

The Accounts have been prepared under the historical cost convention as modified by the revaluation of certain freehold and long leasehold premises and investment properties and the valuation of the long term life assurance business, in accordance with the Building Societies (Accounts and Related Provisions) Regulations 1998 (the 'Regulations') with applicable accounting standards issued by the Accounting Standards Board and pronouncements of its Urgent Issues Task Force and with the Statements of Recommended Practice (SORPs) issued by the British Bankers' Association.

The Association of British Insurers (ABI) has issued a SORP addressing the accounting and disclosure of insurance business for insurance undertakings. Nationwide is not an insurance undertaking and the ABI SORP does not specifically address the accounting for long term life assurance business for predominantly retail banking institutions. In line with other retail banking groups, Nationwide uses the embedded value method to measure its interest in the long term life assurance business.

Although the Group has continued to account for pensions under SSAP 24, the additional transitional disclosures required under Financial Reporting Standard ('FRS') 17 'Retirement Benefits' are set out in Note 8 to the Accounts.

An analysis of results by business segment is provided in Note 10. A business segment is defined as one providing products with different risks and returns from other business segments. No segmental analysis is presented on geographical lines because substantially all of the Group's activities are in the United Kingdom and the Isle of Man.

Basis of consolidation

The Group Accounts consolidate the assets, liabilities and results of the Society, its subsidiary and associate undertakings. Companies that do not meet the legal definition of a subsidiary but which give rise to benefits that are in substance no different to those that would arise from subsidiaries are considered to be quasi-subsidiaries and are also consolidated. Investments in subsidiary undertakings are stated in the Society Accounts at cost less provisions for any impairment in value. The Directors consider it appropriate for administrative and commercial reasons that subsidiary undertakings have financial years ending on 31 March. Adjustment is made for any individually significant transactions arising between 31 March and the Society's year end. Certain quasi-subsidiaries have year ends other than 31 March and are consolidated using internal management accounts prepared to that date.

As the consolidated accounts include partnerships where a Group member is a partner, advantage has been taken of the exemption given by Regulation 7 of the Partnerships and Unlimited Companies (Accounts) Regulations 1993 with regard to the preparation and filing of individual partnership accounts.

In order to aid comparability certain comparatives have been re-classified.

Income recognition

Interest is recognised in the Income and Expenditure Account on an accruals basis with the exception of accounts where interest has been suspended in accordance with the provisioning policy for bad and doubtful debts as set out below.

Fees received by the Group relating to the risk borne for a customer are offset against Loans to Customers on the balance sheet and are then taken to interest receivable and similar income so as to achieve a constant yield over the expected life of the underlying loan. Other fees and commissions are recognised on an accruals basis in the period during which they are earned or incurred.

Mortgage incentives

The costs of mortgage cashbacks and discounts are charged as incurred to the Income and Expenditure Account.

Goodwill

Goodwill arising on the acquisition of subsidiary undertakings represents the excess of cost over the fair value of net tangible assets acquired. Goodwill arising on each acquisition is capitalised and amortised on a straight line basis over its useful economic life which does not exceed 20 years. Useful economic life is determined at the time of acquisition by considering the nature of the acquired business, the economic environment in which it operates and the period over which the value of the business is expected to exceed the values of the net tangible assets.

Deferred taxation

Full provision is made for deferred tax on all timing differences between the recognition of gains and losses in the accounts and their recognition in a tax computation. Deferred taxation is provided at tax rates expected to be applicable when a liability or asset crystallises, on a non-discounted basis. Deferred tax assets are recognised to the extent that it is regarded that there will be sufficient taxable profits available against which they can be offset in the future.

Statement of Accounting Policies (continued)

Tangible fixed assets and depreciation

Freehold and long leasehold premises (excluding specialised administration buildings) are revalued at open market valuation for existing use. Movements in freehold and long leasehold valuations are taken to the revaluation reserve except where a deficit is deemed permanent, when it is charged to the Income and Expenditure Account.

The directly attributable costs of additions, major alterations and refurbishments to premises and directly attributable borrowing costs incurred in the construction of qualifying assets are added to fixed assets.

Depreciation is not charged on freehold land and freehold and long leasehold premises where the assets are continually maintained to a high state of repair and improved or extended from time to time such that their useful economic lives are so long and residual values, based on latest valuations, so high that any depreciation is immaterial, such assets being subject to annual impairment reviews as required by FRS 15.

Other fixed assets are included at cost less depreciation. Depreciation, where applicable, is provided against cost or valuation to write down the assets to their residual values by equal annual instalments over the following estimated useful lives.

Specialised administration buildings	25 to 43 years
Short leasehold premises	the period of the lease
Fixtures and fittings	7 to10 years
Plant and machinery	5 to10 years
Office equipment	5 to 7 years
Computer equipment	3 to 5 years
Motor vehicles	3 to 5 years

Estimated useful lives are reviewed regularly in the light of technological developments, usage and other relevant factors.

Leases

Operating lease costs are charged to the Income and Expenditure Account in equal annual instalments over the life of the lease.

Debt securities and other eligible bills

Debt securities and other eligible bills are stated at cost adjusted over the period to maturity to allow for the amortisation of premiums or discounts arising on acquisition, whch are amortised from purchase to maturity in equal annual instalments less provision for any impairment in value.

Sale and repurchase transactions

Securities which have been sold with an agreement to repurchase continue to be shown on the balance sheet and the sale proceeds are recorded as a deposit. Securities acquired in reverse sale and repurchase transactions are not recognised on the balance sheet and the purchase price is treated as a loan. The difference between the sale price and repurchase price is accrued evenly over the life of the transaction and taken to the Income and Expenditure Account as interest payable and similar charges, or interest receivable and similar income as appropriate.

Derivatives

In accordance with the Building Societies Act 1986, derivatives are used purely to hedge risk exposure and are not used for speculative purposes. Derivatives are taken out to reduce exposures to fluctuations in interest rates, exchange rates, market indices and credit risk.

Derivatives are initially recorded at cost and are accounted for on an accruals basis in the same way as the underlying items which they are hedging. Interest receipts and payments on hedging instruments are included as net income or expense on financial instruments within interest receivable and similar income or interest payable and similar charges. In order to achieve a consistent timing of income recognition on the items being hedged, deferred gains and losses are included in the balance sheet within accruals and deferred income or prepayments and accrued income.

Where a hedge is terminated early, the resulting gain or loss is amortised over the remaining life of the item being hedged. If the underlying item is redeemed, the unamortised amounts are recognised immediately in the Income and Expenditure Account.

Statement of Accounting Policies (continued)

Foreign currency translation

Foreign currency income and expenditure are included in the Income and Expenditure Account at the rate of exchange current at the date the transaction took place, unless the transaction is hedged, when it is translated at the underlying rate of exchange inherent in the associated hedge contract. Amounts due or receivable under foreign currency swap contracts are translated at the exchange rate inherent in those contracts and are included within accruals and deferred income or prepayments and accrued income. All other non-Sterling assets and liabilities are translated at the rates of exchange ruling at the balance sheet date.

Exchange differences on the translation of the opening net assets of overseas Group undertakings are taken to reserves. Exchange differences arising from the translation of funding and hedge transactions relating to investments in such undertakings are also taken to reserves to offset the exchange differences arising from the translation of these investments.

Debt securities in issue and subordinated liabilities

Premiums and discounts, together with costs associated with the issue of debt securities and subordinated liabilities, are accounted for as an adjustment to the amount of the liability and amortised in equal annual instalments to interest payable and similar charges over the term of the instrument.

Provisions for bad and doubtful debts

Provisions are made to reduce the value of loans and advances to the amount that the Directors consider likely to be recovered.

Specific provisions

Specific provisions are raised against defaulted loans where, in the opinion of the Directors, it is likely that some of the capital will not be repaid or, where the loan is secured, recovered through enforcement of security. No specific provision is made where the estimated value of the security is in excess of the secured debt.

The specific provisions established against the Group's high volume homogeneous loans such as the residential mortgage, personal lending and credit card portfolios are calculated using statistical techniques. These techniques apply a propensity factor against each portfolio based on recent experience and other relevant risk considerations to determine the appropriate provision. Specific provisions are calculated as the difference between the outstanding loan balance and, where applicable, the estimated market value (net of costs) of the security.

For residential mortgages, the estimated value of security is derived by applying Nationwide's regional house price index less a forced sale discount to the purchase value for each property.

For the Group's non-retail lending portfolios, the specific provision is determined on a case by case basis from a review of the financial condition of the counterparty and any guarantor and takes into account the nature and value of any security held.

General provisions

General provisions are made to cover latent losses which, although not yet specifically identified, are known from experience to exist in the Group's loan portfolios. General provisions are determined using management judgement based on a combination of past loss experience, lending quality and other relevant risk considerations.

Specific and general provisions are deducted from loans and advances. The charge to the Income and Expenditure Account represents new or additional provisions made less any reduction in provisions or recoveries of amounts previously written off.

Loans on which interest is being placed in suspense

When the collection of interest is in doubt it is credited to a suspense account, excluded from interest income and netted off loans and advances. However, interest continues to be charged to the customer's account. This interest is subsequently written off if there is deemed to be no realistic prospect of recovery.

Investment properties

Investment properties, which comprise properties held for rental, are revalued annually to open market value. The changes in market value are reflected in the revaluation reserve except where any impairment is deemed permanent, when it is taken to the Income and Expenditure Account. No provision is made for depreciation of investment properties. This is a departure from the requirements of accounting legislation which requires all properties to be depreciated. The Directors consider that these properties are held for investment and that to depreciate them would not give a true and fair view. The depreciation charge is only one of the factors reflected in the annual valuation and therefore the amount of depreciation which might otherwise have been charged cannot be readily quantified.

Statement of Accounting Policies (continued)

Pension costs

The expected cost, including variations from the regular cost, of pensions in respect of the Group's pension schemes is charged to the Income and Expenditure Account so as to spread the cost of pensions over the expected service lives of employees in the schemes. The pension cost is assessed in accordance with the advice of independent actuaries. A formal actuarial valuation of the Society's pension scheme is undertaken on a triennial basis.

Long term life assurance business

Nationwide uses the embedded value method of accounting to measure its interest in the long term life assurance business. In order to reflect the different nature of the shareholder's and policyholders' interests in the long term life assurance business, the value of the long term life assurance business attributable to the shareholder and the assets and liabilities attributable to policyholders are disclosed separately in the Group balance sheet.

The value of the shareholder's interest in the long term life assurance business ('the embedded value') is included in other assets in the balance sheet. This represents the present value of future earnings of in-force business, together with the net tangible assets and the surplus retained within the long term life assurance fund. The value of in-force business is determined annually using assumed economic parameters (future investment returns, expense inflation and risk discount rate) and taxation, mortality, persistency and expense assumptions. Changes in the value of the long term life assurance business, which are determined on a post-tax basis, are included in other operating income and are grossed up at the effective rate of tax for the purpose of presentation.

Long term life assurance funds comprising the assets and liabilities relating to the policyholders of the long term life assurance business are of a different nature to the assets and liabilities of the rest of the Group. Accordingly the Directors have separately classified the long term life assurance business assets and liabilities on the face of the Group balance sheet. An analysis of these assets and liabilities is shown separately in Note 20 to the Accounts.

Notes to the Accounts

1 Interest receivable and similar income

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
On loans fully secured on residential property	**3,065.3**	2,641.5	**2,751.2**	2,350.4
On other loans				
• Connected undertakings	**–**	–	**300.7**	296.3
• Other	**575.8**	555.3	**464.9**	431.9
On debt securities				
• Interest and other income	**534.4**	622.9	**499.7**	574.2
• Net gains arising on realisation	**–**	5.4	**–**	5.4
On other liquid assets				
• Interest and other income	**14.5**	18.9	**25.9**	17.6
Other interest receivable	**1.0**	0.9	**–**	–
Net expense on financial instruments hedging assets	**(320.2)**	(297.9)	**(320.2)**	(297.9)
	3,870.8	3,547.0	**3,722.2**	3,377.9
Interest receivable on loans fully secured on residential property includes:				
Discounts provided to customers charged to interest receivable	**23.3**	78.6	**17.5**	66.5

Interest receivable on 'other loans' includes Group £48.9 million (2003 – £59.6 million) and Society £19.1 million (2003 – £22.7 million), in respect of loans to corporate bodies, such as Registered Social Landlords, which are fully secured on residential property where the commitment was made prior to 2 January 1998. The classification adopted for such amounts is consistent with the balance sheet classification of the related loan in accordance with the Building Societies Act 1997 (Note 14).

Interest and other income on debt securities includes Group and Society £107.9 million (2003 – £64.5 million) of income from fixed income securities.

Interest which is considered irrecoverable, where the property has been taken into possession or the normal lending relationship has ceased, has been suspended and debited to the borrower. Movements in the suspended interest accounts are as follows:

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
Balance brought forward	**9.1**	8.9	**6.3**	7.3
Interest written off during the year	**(2.2)**	(1.4)	**(2.4)**	(1.3)
Interest suspended in the year	**1.6**	1.6	**0.6**	0.3
Balance carried forward	**8.5**	9.1	**4.5**	6.3

Notes to the Accounts (continued)

2 Interest payable and similar charges

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
On shares held by individuals	**2,031.3**	1,993.7	**2,031.3**	1,993.7
On other shares	**0.5**	0.4	**0.5**	0.4
On subscribed capital	**27.8**	24.0	**27.8**	24.0
On deposits and other borrowings				
• Subordinated liabilities	**40.0**	13.6	**40.0**	13.6
• Connected undertakings	**–**	–	**32.5**	30.7
• Other	**684.4**	536.8	**641.7**	504.9
Net income on financial instruments hedging liabilities	**(11.9)**	(52.6)	**(11.9)**	(52.6)
	2,772.1	2,515.9	**2,761.9**	2,514.7

3 Income from investments

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
Income from equity shares	**0.4**	0.2	**0.4**	0.2
Income from shares in subsidiary undertaking	**–**	–	**69.4**	43.8
	0.4	0.2	**69.8**	44.0

4 Other operating income

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
Other operating income includes:				
Movement in value of long term life assurance business	**44.8**	43.7	**–**	–

5 Administrative expenses

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	£m	£m
Employee costs				
• Wages and salaries	**312.4**	288.9	**294.4**	271.1
• Social security costs	**29.5**	23.5	**27.9**	21.7
• Other pension costs	**46.1**	47.0	**43.6**	44.1
	388.0	359.4	**365.9**	336.9
Other administrative expenses	**368.8**	356.2	**363.8**	358.0
	756.8	715.6	**729.7**	694.9
Other administrative expenses include:				
Property rentals under operating leases	**26.8**	26.7	**26.1**	26.0
Auditors' remuneration and expenses				
• Statutory audit fees	**0.9**	0.8	**0.6**	0.5
• Audit related and regulatory fees	**0.1**	0.1	**0.1**	0.1
	1.0	0.9	**0.7**	0.6
• Further assurance services	**0.3**	0.2	**0.3**	0.2
• Tax advisory	**0.1**	0.1	**0.1**	0.1
	1.4	1.2	**1.1**	0.9

The Group adopted its current policy in relation to the use of its auditors on non audit engagements during 2003. This policy sets out the types of service they are precluded from performing which includes all management consultancy services. Certain de minimis limits for non audit fees have also been established. All non audit fees where the fee is expected to exceed the relevant limit, are subject to pre-approval by the Audit Committee. In addition each Audit Committee meeting receives a report of amounts paid and payable to the auditors.

6 Employees

	Group 2004	Group 2003	Society 2004	Society 2003
The average number of persons employed during the year was:				
• Full-time	**10,676**	10,542	**9,809**	9,678
• Part-time	**4,885**	4,647	**4,712**	4,479
	15,561	15,189	**14,521**	14,157
Building society				
• Central administration	**6,268**	5,941	**6,268**	5,941
• Branches	**8,253**	8,216	**8,253**	8,216
Subsidiaries	**1,040**	1,032	**–**	–
	15,561	15,189	**14,521**	14,157

Employee numbers include 464 (2003 – 458) people relating to the Group's life assurance operation whose costs are included in other operating income (Note 4). Central administration employee numbers include employees engaged in direct customer-facing operations in administrative centres.

Notes to the Accounts (continued)

7 Directors' emoluments

Directors' emoluments are shown as part of the Report of the Directors on Remuneration in accordance with Schedule 5, paragraphs 4 and 5 to the Building Societies (Accounts and Related Provisions) Regulations 1998.

8 Pension arrangements

The majority of the Group's employees are members of the defined benefit scheme the Nationwide Pension Fund (the 'Fund').

The Group also participates in other pension arrangements for a number of employees of subsidiary companies and has two unapproved pension schemes, one unfunded scheme for certain Directors who were members of the Board prior to 10 January 1990 and a funded scheme for executive Directors and Officers whose benefits are unable to be provided in full using an approved pension arrangement.

The pension cost included in administrative expenses under SSAP 24 (Note 5) and the cash contributions paid to the Fund are based on the latest full actuarial valuation as at 31 March 2001. The valuation was performed using the projected unit method in respect of pension benefits and the current unit method in respect of lump sum death in service benefits.

The next full actuarial valuation will be as at 31 March 2004. The results will not be available until after the publication of these accounts.

The assumptions used in assessing the pension cost are a matter of judgement for the independent actuary in consultation with the Society. The assumptions used in determining the cash contribution are recommended by the independent actuary and are agreed with the Fund Trustees. The assumptions, which are based on the latest full actuarial valuation under SSAP 24 as at 31 March 2001, and the resulting pension charge are summarised below:

	Cash contribution and pension cost assumptions (Years ended 4 April 2004 and 4 April 2003)
Rate of return on investments	6.8% (before retirement) 5.8% (after retirement)
Rate of increase in salaries	4.3% – 5.3% per annum
Rate of increase in pensions	2.4% per annum
Market value of the Fund's assets, excluding money purchase additional voluntary contributions	£752.0 million
Market value as a percentage of the value of the benefits based on service to date, allowing for assumed future salary and pension increases	98%
Long term regular cost	17.3%
Employer's cash contribution rate	19.1%
Employees' contribution rate	5%

8 Pension arrangements (continued)

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Pension charge for the year (Note 5)	**46.1**	47.0	**43.6**	44.1
The pension charge is calculated after taking account of:				
• Amortisation of pension fund deficit	**1.0**	1.0	**1.0**	1.0
Cumulative excess of cash contributions paid to the Fund over the SSAP 24 pension charge included in:				
• Prepayments and accrued income (Note 19)	**(108.3)**	(5.3)	**(108.3)**	(5.3)
• Provisions for liabilities and charges including charge for contribution to unfunded Directors' pension obligations (Note 27)	**5.6**	5.4	**5.6**	5.3
Provision for part-time employee pension rights included in Provisions for liabilities and charges (Note 27)	**0.5**	0.6	**0.5**	0.6

Because of lower investment returns and declining stock markets, the Directors consider that the deficit in the Fund has increased significantly since the last full actuarial valuation at 31 March 2001. Consequently, in May 2003, an additional £100 million was paid into the Fund to reduce the deficit. The employees' contribution rate was increased from 5% to 6% on 1 July 2003 for members in the final salary section of the Fund.

The Group's pension arrangements for employees who joined the Fund after 31 December 2001 are based on a career average of revalued earnings ('CARE') rather than their final salary. The employer's cash contribution rate for these employees is 12.6%. The employees' contribution rate is 5%.

The Group provides concessionary rate mortgages and limited post-retirement healthcare benefits to certain of its former employees. The cost of providing these benefits is not significant and is recognised in the Income and Expenditure Account as it is incurred.

FRS 17 DISCLOSURES

The Group has continued to account for pensions under SSAP 24. Financial Reporting Standard 17, Retirement Benefits, will fundamentally change the calculation and reporting of the cost of retirement benefits. The transitional arrangements of FRS 17 requires additional disclosures as set out below. Only the Nationwide Pension Fund is of a material size for the purposes of this note. As explained above, a full actuarial valuation of the Fund was carried out at 31 March 2001 and has been updated to take account of the requirements of FRS 17, to 4 April 2004 by qualified independent actuaries.

MAIN FINANCIAL ASSUMPTIONS

The major assumptions used for the FRS 17 disclosures are:

	4 April 2004 (%pa)	4 April 2003 (%pa)	4 April 2002 (%pa)
Inflation	**3.0**	2.6	2.7
Rate of general long term increase in salaries	**5.0**	4.6*	4.7*
Rate of increase to pensions in payment	**2.8**	2.6	2.7
Discount rate for scheme liabilities	**5.5**	5.5	6.0

*plus an additional 1% p.a. until 4 April 2004

Notes to the Accounts (continued)

8 Pension arrangements (continued)

	Long term rate of return expected at 4 April 2004	**Value at 4 April 2004 £m**	Long term rate of return expected at 4 April 2003	Value at 4 April 2003 £m	Long term rate of return expected at 4 April 2002	Value at 4 April 2002 £m
SCHEME ASSETS AND LIABILITIES AND EXPECTED RETURN						
Equities	**7.9%**	**729**	7.7%	490	8.1%	578
Bonds (gilts)	**5.1%**	**224**	4.9%	146	5.5%	167
Other	**4.9%**	**10**	4.3%	28	4.1%	24
Total market value of assets	**7.2%**	**963**	6.9%	664	7.4%	769
Present value of scheme liabilities		**(1,394)**		(1,152)		(965)
Deficit in the scheme		**(431)**		(488)		(196)
Related deferred tax asset		**129**		146		59
Net pension liability		**(302)**		(342)		(137)

The assets of the scheme are mainly invested with Fidelity Pensions Management, Barclays Global Investors Limited and UBS Global Asset Management UK Ltd.

Money purchase pension assets and liabilities (AVCs) are excluded from the table above.

The decrease in the net pension liability arises from an increase in the market value of investments and includes the net effect of the special contribution of £100 million, as discussed above, and changes in actuarial assumptions mainly relating to mortality rates and the long-term outlook for inflation that have lead to an increase in scheme liabilities.

The position shown represents the funded status of the Fund based on the market conditions at 4 April 2004. Market related calculations are subject to daily variations. The net pension liability shown does not represent a debt of the Society. Contributions to the Fund will continue to be determined in accordance with the full triennial actuarial valuations.

8 Pension arrangements (continued)

If the requirements of FRS 17 were fully adopted in the Annual Accounts in the year to 4 April 2004 the impact would be:

	2004	2003
	£m	£m
Amount charged to operating profit:		
Current service cost	(55)	(47)
Past service cost	(2)	–
Total operating charge	(57)	(47)
Amount charged to other finance income:		
Expected return on pension scheme assets	47	58
Interest on pension scheme liabilities	(65)	(59)
Net amount charged to other finance income	(18)	(1)
Analysis of amount in the statement of total recognised gains and losses:		
Actual return less expected return on pension scheme assets	108	(197)
Experience gains and losses arising on scheme liabilities	(2)	(3)
Changes in assumptions underlying the present value of scheme liabilities	(120)	(86)
Actuarial loss recognised in the statement of total recognised gains and losses	(14)	(286)
Analysis of movement in deficit during the year:		
Deficit in scheme at beginning of the year	(488)	(196)
Current service cost	(55)	(47)
Other finance charge	(18)	(1)
Contributions	146	42
Past service charge	(2)	–
Actuarial loss	(14)	(286)
Deficit in scheme at the end of the year	(431)	(488)
Details of experience gains and losses for the year to 4 April 2004:		
Difference between expected and actual return on scheme assets:		
• Amount (£ million)	108	(197)
• Percentage of scheme assets	11.2%	29.7%
Experience (losses) on scheme liabilities:		
• Amount (£ million)	(2)	(3)
• Percentage of the present value of the scheme liabilities	0.1%	0.3%
Total amount recognised in the statement of total recognised gains and losses:		
• Amount (£ million)	(14)	(286)
• Percentage of the present value of the scheme liabilities	1.0%	24.8%

If the net pension liability had been recognised in the Annual Accounts, the Group's liabilities would increase by £302 million and the Group's general reserve at 4 April 2004 would be as follows:

	4 April 2004	4 April 2003
	£m	£m
General reserve excluding net pension liability	4,341.1	4,021.0
SSAP 24 prepayment (net of deferred tax)	(75.8)	(3.7)
Pension liability (net of deferred tax)	(302.0)	(342.0)
	3,963.3	3,675.3

Notes to the Accounts (continued)

9 Tax on profit on ordinary activities

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Current tax:				
UK corporation tax at 30% (2003 – 30%)	**113.6**	118.4	**104.9**	76.3
Corporation tax – adjustment in respect of prior periods	**1.5**	(33.9)	**1.2**	(32.1)
	115.1	84.5	**106.1**	44.2
Double taxation relief	**(7.6)**	–	**(7.6)**	–
	107.5	84.5	**98.5**	44.2
Isle of Man income tax	**0.2**	0.2	**–**	–
Taxation relating to change in value of long term life assurance business	**13.4**	13.1	**–**	–
Total current tax	**121.1**	97.8	**98.5**	44.2
Deferred tax (Note 18):				
Current year	**(6.2)**	(6.9)	**(7.5)**	2.8
Adjustment in respect of prior periods	**(6.0)**	(0.3)	**(7.2)**	(2.3)
	108.9	90.6	**83.8**	44.7

The Society's tax charge includes payments in consideration for the surrender of tax losses by subsidiary undertakings totalling £16.7 million (2003 – £1.4 million).

The actual current tax charge for the year differs from that calculated using the standard rate of corporation tax in the UK. The differences are explained below:

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Profit on ordinary activities before tax	**426.8**	353.3	**301.8**	168.8
Profit on ordinary activities before tax at the standard rate of UK corporation tax of 30% (2003 – 30%)	**128.0**	106.0	**90.5**	50.7
Effects of:				
Specifically allowable and non deductible items	**(14.0)**	10.3	**(1.2)**	10.9
Depreciation for the period in excess of capital allowances	**6.3**	2.7	**7.7**	2.7
Effect of change in non allowable bad debt provisions	**3.3**	5.8	**3.7**	4.6
Effect of changes in other provisions	**(3.4)**	8.2	**(2.8)**	8.7
Gains exempted or covered by capital losses	**(0.6)**	(1.3)	**(0.6)**	(1.3)
Adjustment to current tax charge in respect of previous periods	**1.5**	(33.9)	**1.2**	(32.1)
Current tax charge for the year	**121.1**	97.8	**98.5**	44.2

During 2003 a number of long standing tax issues were resolved permitting the release of prior year tax provisions.

10 Segmental reporting

	Group 2004 Profit/(Loss) before tax	Group 2004 Total assets	Group 2004 Net assets	Group 2003 Profit/(Loss) before tax	Group 2003 Total assets	Group 2003 Net assets
	£m	**£m**	**£m**	£m	£m	£m
Analysis of class of business:						
Retail	**299.0**	**71,039.4**	**3,148.2**	287.6	57,431.1	2,627.2
Commercial	**174.1**	**12,383.0**	**1,003.6**	165.6	10,762.6	889.6
Group	**(46.3)**	**18,006.0**	**401.2**	(99.9)	17,224.0	669.3
	426.8	**101,428.4**	**4,553.0**	353.3	85,417.7	4,186.1

Retail represents the provision of personal financial services including all the attributable income and expenditure relating to retail mortgages, unsecured and secured personal lending, credit card, insurance products and FlexAccount. Nationwide's strategy of better pricing means that retail profit contribution is intentionally reduced.

Commercial includes all of the costs and income associated with the Group's lending to Registered Social Landlords and other loans to support investment in commercial properties and residential housing.

Group includes the costs and income associated with managing the Group's capital position, fixed asset investment portfolio, wholesale funding and the liquid asset management of the Group.

Administrative expenses and depreciation have been allocated to segments based on resources consumed, except where they cannot be meaningfully allocated in which case they are included within Group items. Group items include rental income and associated property costs plus the core Group administrative expenses that have not been allocated to business segments.

Capital is allocated to each business segment for investment purposes and is based upon the regulatory capital framework. No charge has been made for capital.

11 Loans and advances to credit institutions

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Loans and advances to credit institutions have remaining maturities as follows:				
Accrued interest	**3.6**	0.3	**3.2**	0.3
Repayable on demand	**139.4**	109.5	**117.6**	86.8
Other loans and advances by residual maturity repayable:				
• In not more than three months	**1,212.2**	654.5	**1,212.1**	654.4
• In more than three months but not more than one year	**108.9**	211.5	**–**	–
	1,464.1	975.8	**1,332.9**	741.5

Notes to the Accounts (continued)

12 Debt securities

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	£m	£m
Government debt securities	**430.1**	482.6	**243.8**	284.1
Other public sector debt securities	**–**	8.8	**–**	8.3
Issued by public bodies	**430.1**	491.4	**243.8**	292.4
Private sector debt securities	**15,220.7**	15,169.6	**14,725.3**	14,822.7
	15,650.8	15,661.0	**14,969.1**	15,115.1

The amount of bank and building society certificates of deposits included in the above was £5,282.6 million (2003 – £5,183.2 million).

Debt securities have remaining maturities as follows:

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	£m	£m
• Accrued interest	**109.9**	111.0	**106.1**	106.2
• In not more than one year	**8,928.3**	8,053.3	**8,806.0**	8,004.6
• In more than one year	**6,612.6**	7,496.7	**6,057.0**	7,004.3
	15,650.8	15,661.0	**14,969.1**	15,115.1
Transferable debt securities comprise:				
• Listed	**9,115.5**	9,577.3	**8,433.8**	9,059.8
• Unlisted	**6,535.3**	6,083.7	**6,535.3**	6,055.3
	15,650.8	15,661.0	**14,969.1**	15,115.1
Market value of transferable debt securities:				
• Government debt securities	**446.8**	500.8	**257.2**	299.0
• Other public sector securities	**–**	8.9	**–**	8.4
• Private sector debt securities	**15,244.9**	15,422.3	**14,757.2**	15,017.8
	15,691.7	15,932.0	**15,014.4**	15,325.2

The market value of bank and building society certificates of deposit included in the above was £5,279.4 million (2003 – £5,187.1 million).

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	£m	£m
Market value of listed transferable debt securities	**9,223.7**	9,841.3	**8,546.4**	9,262.6
Included in debt securities are:				
• Unamortised premiums	**18.8**	38.5	**5.6**	9.3
• Unamortised discounts	**(130.6)**	(115.3)	**(130.6)**	(115.3)

The Directors consider that the primary purpose of holding securities is prudential. The securities are held as liquid assets with the intention of use on a continuing basis in the Group's activities and are therefore classified as financial fixed assets rather than current assets.

12 Debt securities (continued)

The carrying value of debt securities is net of a specific provision of £1.9 million (2003 – £21.5 million) and a general provision of £25.8 million (2003 – £35.7 million) recognising impairment within a portfolio of assets held for their long term investment potential (Note 13). The credit risk on £716.6 million (Sterling equivalent at 4 April 2004; 2003 – £838.8 million) of assets within this investment portfolio has been hedged by the Society entering into a credit derivative. Under the terms of this overall risk mitigating transaction the Society retains the risk of credit losses on the assets which are covered by the credit derivative and certain other reference assets, up to a maximum of £76.1 million (Sterling equivalent at 4 April 2004; 2003 – £78.5 million), which is divided into two distinct tranches. Under the first tranche, the Society bears the first tier of credit losses up to an amount of £27.9 million (2003 – £28.8 million), of which £8.7 million (2003 – £25.4 million) is already reflected in the provisions against debt securities. Beyond this level, the Society's second tranche of exposure to credit losses of £48.2 million (2003 – £49.7 million) is impacted once £23.5 million (2003 – £24.2 million) of loss protection has been utilised. All of the Society's credit loss protection under the transaction will be settled by the credit derivative counterpart, an A+ rated US Banking institution.

£177.9 million (2003 – £304.9 million) of debt securities are subject to sale and repurchase agreements.

Debt securities include asset backed securities of £273.5 million owned by a bankruptcy remote special purpose vehicle. The acquisitions of the asset backed securities have been funded primarily through the issue of commercial paper reported in Debt Securities in Issue (Note 24). The vehicle is owned by a charitable trust and therefore is not a legal subsidiary of the Nationwide Group. However it has been included in the accounts as a quasi-subsidiary (see Note 16) and the assets and liabilities have been fully consolidated because the vehicle gives rise to risks and rewards that are in substance no different than if it were a subsidiary.

Movements during the year of debt securities all of which are held as financial fixed assets are analysed as follows:

	Group	Society
	£m	£m
Adjusted cost and net book value (excluding accrued interest)		
At 5 April 2003	15,550.0	15,008.9
Additions	**27,249.5**	**26,323.2**
Disposals/maturities	**(26,943.9)**	**(26,223.6)**
Other movements	**(314.7)**	**(245.5)**
At 4 April 2004	**15,540.9**	**14,863.0**

13 Amounts released and provisions against fixed asset investments

	Specific	General	Total
	£m	£m	£m
Group and Society			
Provisions at 5 April 2003	21.5	35.7	57.2
(Release) for the year	**(16.3)**	**(9.9)**	**(26.2)**
Amounts written off	**(3.3)**	**–**	**(3.3)**
Provisions at 4 April 2004	**1.9**	**25.8**	**27.7**

Provisions for impairment have been deducted in arriving at the carrying value of debt securities (as shown in Note 12) in the balance sheet.

Notes to the Accounts (continued)

14 Loans and advances to customers

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Loans fully secured on residential property	**70,762.2**	57,212.4	**64,996.2**	51,994.3
Other loans:				
• Loans fully secured on land	**7,433.5**	6,561.3	**6,837.3**	5,976.9
• Other loans	**2,510.5**	1,959.7	**1,332.4**	969.6
	80,706.2	65,733.4	**73,165.9**	58,940.8

The Group formally adopted The Building Societies Act 1997 on 2 January 1998. Under the Act, loans to corporate bodies & registered social landlords already existing at the date of adoption may not be reported as loans fully secured on residential property. Accordingly, the reported other loans fully secured on land include Group £849.8 million (2003 – £932.6 million) and Society £260.0 million (2003 – £361.0 million) of loans which are fully secured on residential property.

MATURITY ANALYSIS

Loans and advances to customers have remaining maturities as follows:

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Repayable on demand	**604.0**	522.5	**597.1**	494.3
Other loans and advances by residual maturity repayable:				
• In not more than three months	**512.7**	527.8	**511.0**	374.7
• In more than three months but not more than one year	**1,855.6**	1,435.1	**1,503.4**	1,182.8
• In more than one year but not more than five years	**10,415.6**	8,003.7	**9,532.6**	7,255.0
• In more than five years	**67,566.4**	55,505.0	**61,243.0**	49,861.8
	80,954.3	65,994.1	**73,387.1**	59,168.6
Less				
• Provisions for bad and doubtful debts (Note 15)	**221.8**	214.7	**194.9**	183.2
• Deferred mortgage guarantee income	**26.3**	46.0	**26.3**	44.6
	80,706.2	65,733.4	**73,165.9**	58,940.8

The maturity analysis is produced on the basis that where a loan is repayable by instalments, each such instalment is treated as a separate repayment. Arrears are spread across the remaining term of the loan.

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

15 Provisions for bad and doubtful debts

	Loans fully secured on residential property		Other loans fully secured on land		Other loans		Total	
	Specific	General	Specific	General	Specific	General	Specific	General
	£m	£m	£m	£m	£m	£m	£m	£m
Group								
At 5 April 2003	8.7	91.8	12.7	54.6	38.2	8.7	59.6	155.1
Amounts written off	**(1.5)**	**–**	**(3.4)**	**–**	**(41.1)**	**–**	**(46.0)**	**–**
Recoveries of amounts previously written off	**3.6**	**–**	**0.1**	**–**	**5.8**	**–**	**9.5**	**–**
Charge/(credit) for the year	**(4.9)**	**8.1**	**0.5**	**5.4**	**39.0**	**(4.5)**	**34.6**	**9.0**
At 4 April 2004	**5.9**	**99.9**	**9.9**	**60.0**	**41.9**	**4.2**	**57.7**	**164.1**
Society								
At 5 April 2003	8.0	84.0	12.7	54.6	19.4	4.5	40.1	143.1
Amounts written off	**(2.4)**	**–**	**(3.4)**	**–**	**(23.8)**	**–**	**(29.6)**	**–**
Recoveries of amounts previously written off	**2.9**	**–**	**0.1**	**–**	**1.6**	**–**	**4.6**	**–**
Charge/(credit) for the year	**(3.2)**	**9.0**	**0.5**	**5.3**	**27.5**	**(2.4)**	**24.8**	**11.9**
At 4 April 2004	**5.3**	**93.0**	**9.9**	**59.9**	**24.7**	**2.1**	**39.9**	**155.0**

These provisions have been deducted from the appropriate asset values shown in the balance sheets.

The total of non performing loans, being those on which interest is no longer being credited to the Income and Expenditure Account is as follows:

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
Non performing loans before provisions	**65.9**	87.4	**38.3**	59.6
Non performing loans after provisions	**42.8**	61.3	**28.1**	50.0

Notes to the Accounts (continued)

16 Investments

Investments in equity shares and subsidiary undertakings are financial fixed assets.

	Group	Society
	£m	£m
Investments in equity shares		
Cost and net book value		
At 5 April 2003	6.6	1.6
Additions	**2.4**	**0.1**
Disposals	**–**	**–**
At 4 April 2004	**9.0**	**1.7**

Society

Investments in associated undertakings

The Society has a 25.5% interest in the ordinary share capital of Grove Village Holdings Limited. Grove Village Holdings is a limited liability company, registered in England and operating in the UK.

	Shares	Loans	Total
	£m	£m	£m
Investments in subsidiary undertakings			
At 5 April 2003	749.2	6,514.1	7,263.3
Additions	**7.0**	**795.7**	**802.7**
Redemptions/repayments	**(62.5)**	**(119.1)**	**(181.6)**
At 4 April 2004	**693.7**	**7,190.7**	**7,884.4**

The interests of the Society in its principal subsidiary undertakings, all of which are consolidated, as at 4 April 2004 are set out below:

Directly held subsidiary undertakings	Nature of business
First Nationwide	Investment company
Monument (Sutton) Limited	Property rental
Nationwide International Limited	Offshore investment
Nationwide Investments No 1 Limited	Investment company
Nationwide Life Limited	Life assurance
Nationwide Mortgage Corporation Limited	Mortgage book acquisition and management
Nationwide Syndications Limited	Syndicated lending
Nationwide Trust Limited	Consumer finance
Nationwide Unit Trust Managers Limited	Unit trust management
at.home nationwide limited	Property rental
Foundation Insurance Limited	Mortgage indemnity insurance
UCB Home Loans Corporation Limited	Centralised mortgage lender

All the above subsidiary undertakings are limited liability companies except First Nationwide which is an unlimited liability company with share capital.

16 Investments (continued)

The Society holds 100% of the issued ordinary share capital of all of its subsidiary undertakings.

All the above companies are registered in England and operate in the UK except for Nationwide International Limited and Foundation Insurance Limited which are registered and operate in the Isle of Man.

QUASI-SUBSIDIARIES

The Group has interests in a number of entities considered by the Directors to be quasi-subsidiaries because they do not meet the definition of a legal subsidiary but give rise to the risks and rewards that are in substance no different than if they were legal subsidiaries. As a consequence, these entities are consolidated in the same way as if they were subsidiaries.

The primary financial statements of these entities can be summarised as follows:

	Investment Companies 2004	Securitisation Companies 2004	Total 2004	Total 2003
	£m	£m	£m	£m
Profit & loss account				
• Interest receivable	35.9	3.4	39.3	14.1
• Interest payable	(35.7)	(3.4)	(39.1)	(14.1)
• Administrative expenses	(0.2)	–	(0.2)	–
Profit/(loss) for the period	–	–	–	–
Balance sheet				
Assets				
• Loans and advances to credit institutions	121.6	–	121.6	15.7
• Loans & advances to customers	–	78.4	78.4	71.5
• Debt securities	569.7	–	569.7	359.3
• Other assets	2.3	–	2.3	–
• Investments	7.4	–	7.4	5.0
Total assets	701.0	78.4	779.4	451.5
Liabilities				
• Amounts owed to credit institutions	68.5	78.4	146.9	92.2
• Debt securities in issue	383.2	–	383.2	111.6
• Other liabilities	249.3	–	249.3	247.7
Total liabilities	701.0	78.4	779.4	451.5
Cash flow statement				
• Net cash inflow from operating activities	325.2	–	325.2	362.1
• Capital expenditure and financial investment	(325.2)	–	(325.2)	(362.1)
Increase/(decrease) in cash	–	–	–	–

Notes to the Accounts (continued)

17 Tangible fixed assets

	Branches and non specialised buildings	Specialised administration buildings	Short leasehold buildings	Investment properties	Total land and buildings	Plant and machinery	Equipment fixtures, fittings and vehicles	Total
	£m	£m	£m	£m	£m	£m	£m	£m
Group								
Cost or valuation								
At 5 April 2003	221.5	102.6	35.2	207.9	567.2	92.4	699.3	1,358.9
Additions	**15.5**	**0.3**	**0.8**	**13.4**	**30.0**	**2.8**	**97.9**	**130.7**
Adjustment on revaluation	**24.9**	**–**	**–**	**24.1**	**49.0**	**–**	**–**	**49.0**
Disposals	**(1.7)**	**–**	**–**	**(8.8)**	**(10.5)**	**–**	**(12.0)**	**(22.5)**
At 4 April 2004	**260.2**	**102.9**	**36.0**	**236.6**	**635.7**	**95.2**	**785.2**	**1,516.1**
Depreciation								
At 5 April 2003	–	34.4	26.2	–	60.6	64.7	435.2	560.5
Charge for the year	**–**	**3.5**	**1.6**	**–**	**5.1**	**7.0**	**96.7**	**108.8**
Disposals	**–**	**–**	**–**	**–**	**–**	**–**	**(10.8)**	**(10.8)**
At 4 April 2004	**–**	**37.9**	**27.8**	**–**	**65.7**	**71.7**	**521.1**	**658.5**
Net book value								
At 4 April 2004	**260.2**	**65.0**	**8.2**	**236.6**	**570.0**	**23.5**	**264.1**	**857.6**
At 4 April 2003	221.5	68.2	9.0	207.9	506.6	27.7	264.1	798.4
Cost or valuation at 4 April 2004 is represented by:								
• Valuation	**260.1**	**–**	**–**	**236.6**	**496.7**	**–**	**–**	**496.7**
• Cost	**0.1**	**102.9**	**36.0**	**–**	**139.0**	**95.2**	**785.2**	**1,019.4**
	260.2	**102.9**	**36.0**	**236.6**	**635.7**	**95.2**	**785.2**	**1,516.1**

Cost or valuation of land and buildings includes £512.4 million (2003 – £444.9 million) in respect of freehold and long leasehold land and buildings which are not depreciated.

All freehold and long leasehold land and buildings except specialised administration buildings and investment properties were valued at 4 April 2004 on the basis of an open market valuation for existing use. A representative sample of around 25% of the branches and non specialised buildings has been valued by members of the Royal Institution of Chartered Surveyors who are either independent or employed by the Society and the remaining properties have been included at valuation based on the percentage movement in values shown by the sample. Investment properties are included at Directors' valuation.

17 Tangible fixed assets (continued)

	Branches and non specialised buildings	Specialised administration buildings	Short leasehold buildings	Total land and buildings	Plant and machinery	Equipment fixtures, fittings and vehicles	Total
	£m	£m	£m	£m	£m	£m	£m
Society							
Cost or valuation							
At 5 April 2003	210.4	102.6	34.7	347.7	90.8	672.2	1,110.7
Additions	**15.5**	**0.3**	**0.7**	**16.5**	**2.7**	**95.4**	**114.6**
Adjustment on revaluation	**24.4**	**–**	**–**	**24.4**	**–**	**–**	**24.4**
Disposals	**(1.6)**	**–**	**–**	**(1.6)**	**–**	**(11.5)**	**(13.1)**
At 4 April 2004	**248.7**	**102.9**	**35.4**	**387.0**	**93.5**	**756.1**	**1,236.6**
Depreciation							
At 5 April 2003	–	34.4	25.8	60.2	63.6	414.6	538.4
Charge for the year	**–**	**3.5**	**1.6**	**5.1**	**6.8**	**94.3**	**106.2**
Disposals	**–**	**–**	**–**	**–**	**–**	**(10.5)**	**(10.5)**
At 4 April 2004	**–**	**37.9**	**27.4**	**65.3**	**70.4**	**498.4**	**634.1**
Net book value							
At 4 April 2004	**248.7**	**65.0**	**8.0**	**321.7**	**23.1**	**257.7**	**602.5**
At 4 April 2003	210.4	68.2	8.9	287.5	27.2	257.6	572.3
Cost or valuation at 4 April 2004 is represented by:							
• Valuation	**248.7**	**–**	**–**	**248.7**	**–**	**–**	**248.7**
• Cost	**–**	**102.9**	**35.4**	**138.3**	**93.5**	**756.1**	**987.9**
	248.7	**102.9**	**35.4**	**387.0**	**93.5**	**756.1**	**1,236.6**

Cost or valuation of land and buildings includes £264.2 million (2003 – £225.9 million) in respect of freehold and long leasehold land and buildings which are not depreciated.

	Group		**Society**	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
Net book value of land and buildings is represented by:				
• Freehold	**507.9**	454.9	**295.4**	261.8
• Long leasehold	**53.9**	42.7	**18.2**	16.8
• Short leasehold	**8.2**	9.0	**8.1**	8.9
	570.0	506.6	**321.7**	287.5
Net book value of land and buildings occupied by the Group/Society for its own activities	**277.3**	265.5	**265.0**	224.3
Net book value of land and buildings based on historical cost is:				
• Cost	**448.7**	427.3	**285.3**	270.5
• Aggregate depreciation	**74.7**	69.7	**74.3**	69.3
Net book value	**374.0**	357.6	**211.0**	201.2

Notes to the Accounts (continued)

18 Other assets

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Value of long term life assurance business	**245.3**	213.9	**–**	–
Deferred taxation	**40.5**	28.3	**32.7**	18.0
Other	**124.1**	59.2	**77.8**	29.9
	409.9	301.4	**110.5**	47.9

The long term life assurance business has been valued using the following key assumptions:

- Expected future profits after tax from business currently in force have been discounted at a rate of 9.0% (2003 – 9.0%) per annum.
- Future investment returns of 5.0% (2003 – 4.5%) gross per annum for fixed interest investments and 7.0% (2003 – 6.5%) for equity investments. The investment return for guaranteed return products is linked to the matching assets.
- Expense inflation rate of 3.5% (2003 – 3.5%) gross.
- Mortality for the future based on general industry experience of the type of business concerned.
- Expenses and withdrawals for the future based on own recent experience of the type of business concerned.

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Deferred Taxation				
Brought forward at 5 April 2003	**28.3**	21.1	**18.0**	18.5
Deferred tax credit/(charge) in Income and Expenditure Account (Note 9)	**12.2**	7.2	**14.7**	(0.5)
Carried forward at 4 April 2004	**40.5**	28.3	**32.7**	18.0
The amounts provided for deferred taxation, which represent the full potential deferred assets/(liabilities), are set out below:				
Excess of capital allowances over depreciation	**(0.3)**	(5.3)	**0.2**	(6.0)
Interest adjustments	**(9.1)**	(9.1)	**(9.1)**	(9.1)
Other timing differences	**49.9**	42.7	**41.6**	33.1
	40.5	28.3	**32.7**	18.0

Provision is not made for any taxation liability which might arise on the disposal of premises at their balance sheet value as it is anticipated that either substantially all the properties will be retained by the Group or that any gains which arise on disposal will be eligible for roll-over relief or set off against available capital losses. The Directors are, therefore, of the opinion that the likelihood of any material liability arising in this respect is remote.

19 Prepayments and accrued income

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Accruals relating to off balance sheet instruments	**14.3**	35.8	**14.3**	35.8
Due from subsidiary undertakings	**–**	–	**151.3**	143.1
Prepayments related to pension fund (Note 8)	**108.3**	5.3	**108.3**	5.3
Other	**114.8**	79.9	**80.6**	69.0
	237.4	121.0	**354.5**	253.2

20 Assets and liabilities relating to long term life assurance business

	Group 2004 £m	Group 2003 £m
The assets and liabilities of the long term life assurance business of the Group are:		
Investments	**1,769.4**	1,453.4
Current assets	**13.5**	18.3
Long term life assurance business assets	**1,782.9**	1,471.7
Creditors	**774.6**	697.1
Long term life assurance fund	**1,008.3**	774.6
Long term life assurance business liabilities	**1,782.9**	1,471.7

The above investments are stated at market value.

21 Shares

	Group and Society 2004 £m	Group and Society 2003 £m
Held by individuals	**65,927.7**	60,938.9
Other shares	**16.2**	13.3
	65,943.9	60,952.2
Shares are repayable from the balance sheet date in the ordinary course of business as follows:		
Accrued interest	**470.6**	555.1
Repayable on demand	**62,412.7**	59,427.8
Other shares by residual maturity repayable:		
• In not more than three months	**435.1**	197.2
• In more than three months but not more than one year	**1,889.3**	453.4
• In more than one year but not more than five years	**736.2**	318.7
	65,943.9	60,952.2

Notes to the Accounts (continued)

22 Amounts owed to credit institutions

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	£m	£m
Amounts owed to credit institutions are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**13.0**	8.2	**13.0**	8.2
Repayable on demand	**337.8**	0.5	**337.8**	0.5
Other amounts owed to credit institutions by residual maturity repayable:				
• In not more than three months	**1,569.2**	1,433.5	**1,567.4**	1,432.9
• In more than three months but not more than one year	**193.4**	32.8	**147.5**	32.8
• In more than one year but not more than five years	**115.9**	119.4	**115.9**	119.4
• In more than five years	**–**	164.4	**–**	164.4
	2,229.3	1,758.8	**2,181.6**	1,758.2

Amounts owed to credit institutions include £177.9 million (2003 – £304.4 million) in respect of sale and repurchase agreements.

23 Amounts owed to other customers

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	£m	£m
Amounts owed to subsidiary undertakings	**–**	–	**1,213.4**	1,002.8
Other	**4,836.5**	4,539.5	**4,057.6**	3,827.8
	4,836.5	4,539.5	**5,271.0**	4,830.6
Amounts owed to other customers are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**21.6**	14.4	**21.1**	15.4
Repayable on demand	**1,253.6**	1,284.0	**2,120.9**	2,040.5
Other amounts owed to other customers with residual maturity repayable:				
• In not more than three months	**2,883.4**	2,666.6	**2,471.8**	2,422.4
• In more than three months but not more than one year	**515.5**	458.5	**512.6**	236.8
• In more than one year but not more than five years	**162.4**	86.8	**144.6**	86.3
• In more than five years	**–**	29.2	**–**	29.2
	4,836.5	4,539.5	**5,271.0**	4,830.6

24 Debt securities in issue

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Certificates of deposit	**10,844.5**	7,141.8	**10,537.8**	7,060.4
Fixed and floating rate notes	**8,647.7**	3,735.9	**8,647.7**	3,735.9
Other debt securities	**214.3**	210.4	**214.3**	210.4
	19,706.5	11,088.1	**19,399.8**	11,006.7
Debt securities in issue are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**75.1**	57.5	**75.1**	57.5
Other debt securities in issue with residual maturity repayable:				
• In not more than one year	**11,877.0**	7,708.2	**11,602.7**	7,708.2
• In more than one year	**7,754.4**	3,322.4	**7,722.0**	3,241.0
	19,706.5	11,088.1	**19,399.8**	11,006.7

25 Other liabilities

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Amounts falling due within one year:				
• Income tax	**160.5**	40.2	**160.4**	40.1
• Corporation tax	**57.5**	42.0	**46.7**	22.1
• Other creditors	**201.0**	167.8	**100.0**	70.9
	419.0	250.0	**307.1**	133.1
Other creditors include:				
Amounts due to subsidiary undertakings	**–**	–	**–**	1.4

26 Accruals and deferred income

	Group 2004	Group 2003	Society 2004	Society 2003
	£m	£m	**£m**	£m
Accruals relating to off balance sheet instruments	**145.0**	87.4	**145.0**	87.4
Interest accrued on subordinated liabilities	**7.4**	3.1	**7.4**	3.1
Interest accrued on subscribed capital	**5.2**	1.5	**5.2**	1.5
Other	**127.0**	167.0	**118.8**	160.2
	284.6	259.0	**276.4**	252.2

Notes to the Accounts (continued)

27 Provisions for liabilities and charges

	Pension obligations (Note 8)	Vacant premises and property rectification	Customer redress	Other provisions	Total
	£m	£m	£m	£m	£m
Group					
At 5 April 2003	6.0	3.6	10.3	2.0	21.9
Provisions utilised	(0.1)	(0.8)	(7.4)	–	(8.3)
Charge for the year	0.2	(0.1)	39.9	1.8	41.8
At 4 April 2004	**6.1**	**2.7**	**42.8**	**3.8**	**55.4**
Society					
At 5 April 2003	5.9	3.2	10.3	1.4	20.8
Provisions utilised	(0.1)	(0.6)	(7.4)	–	(8.1)
Charge for the year	0.3	–	(34.1)	2.4	36.8
At 4 April 2004	**6.1**	**2.6**	**37.0**	**3.8**	**49.5**

Pension obligations

This provision primarily represents Group and Society £5.6 million (2003 – £5.3 million) in respect of unfunded Directors' pension obligations with the remaining provision £0.5 million (2003 – £0.6 million), largely to provide certain pension rights to part-time employees.

Vacant premises and property rectification

This represents the estimated amounts in respect of the ongoing net costs of vacant premises and the Group's contractual liability to settle costs for the rectification work on one of the Society's specialised administration buildings and will be utilised over the period of the rectification work.

Customer redress

Provisions have been made in respect of various customer claims including potential claims on endowment policies as described in Note 32 and discussed in the Operating and Financial Review on page 14.

28 Subordinated liabilities

	Group and Society 2004	Group and Society 2003
	£m	£m
Subordinated Callable Floating Rate Notes 2013(€400m)	265.5	273.8
5 1/4% Subordinated Notes 2014 ($225m)	123.1	–
5% Subordinated Notes 2015 ($400m)	218.9	–
5 1/4% Subordinated Notes 2018 (£)	200.0	200.0
8 5/8% Subordinated Notes 2018 (£)	125.0	125.0
	932.5	598.8
Unamortised premiums and issue costs	(6.9)	(4.8)
	925.6	594.0

All of the Society's subordinated liabilities are unsecured. The Society may, with the prior consent of the Financial Services Authority redeem the notes under the following conditions:

- Redemption of all (but not some only) of the Callable Floating Rate Notes 2013 at par (100%) on 11 April 2008 after giving not less than 15 nor more than 30 days notice to the holders. In the event the Society does not redeem the Notes on 11 April 2008 the floating rate notes margin of 0.6% over euribor will increase by a further 0.5%.
- The 5 1/4% Notes 2014 issued in US$ in December 2003 cannot be redeemed prior to their stated maturity.
- The 5% Notes 2015 issued in US$ in July 2003 cannot be redeemed prior to their stated maturity.

28 Subordinated liabilities (continued)

- Redemption of all (but not some only) of the 5 1/4% Notes 2018 at par (100%) on 12 February 2013 after giving not less than 15 nor more than 30 days notice to the holders. In the event the Society does not redeem the Notes on 12 February 2013 the fixed rate of interest will become an aggregate of 1.98% and the then current 5 year benchmark Gilt rate.

- Redemption of all or some of the 8 5/8% Notes at the higher of par (100%) or the benchmark 8 3/4% 2017 Gilt, after giving not less than 30 nor more than 60 days notice to the holders.

The subordinated notes rank pari passu with each other and behind the claims against the Society of all depositors, creditors and investing members (other than holders of deferred shares) of the Society.

The interest rate risk arising from the issuance of fixed rate subordinated debt has been mitigated through the use of interest rate swaps.

29 Subscribed capital

	Group and Society 2004	Group and Society 2003
	£m	£m
7.971% Permanent Interest Bearing Shares	**200.0**	200.0
7.859% Permanent Interest Bearing Shares	**100.0**	100.0
5.769% Permanent Interest Bearing Shares	**400.0**	–
	700.0	300.0
Unamortised issue costs	**(8.3)**	(3.6)
	691.7	296.4

All Permanent Interest Bearing Shares ('PIBS') are unsecured and denominated in Sterling. The first two tranches above were issued on 13 March 2000. Total net proceeds of the issue were £295.7 million. The third issue of £400m was issued on 6 February 2004. The net proceeds of the issue were £395m.

The 7.971% PIBS are repayable, at the option of the Society, in whole in March 2015 or any fifth anniversary thereafter. The 7.859% PIBS are repayable, at the option of the Society, in whole in March 2030 or any fifth anniversary thereafter. The 5.769% PIBS are repayable at the option of the Society, in whole in February 2026 or any fifth anniversary thereafter. Repaying the PIBS requires the prior consent of the Financial Services Authority. If the PIBS are not repaid on a call date then the interest rate is reset at a margin to the yield on the then prevailing five-year benchmark Gilt.

PIBS rank pari passu with each other. They are deferred shares of the Society and rank behind the claims against the Society of all subordinated noteholders, depositors, creditors and investing members of the Society.

The interest rate risk arising from the issuance of fixed rate PIBS has been mitigated through the use of interest rate swaps.

30 Revaluation reserve

	Group fixed assets	Group investment properties	Group total	Society fixed assets
	£m	£m	£m	£m
At 5 April 2003	82.6	82.5	165.1	86.3
Surplus on revaluation	**24.9**	**24.1**	**49.0**	**24.4**
Transfer to general reserve	**(0.1)**	**(2.1)**	**(2.2)**	**–**
At 4 April 2004	**107.4**	**104.5**	**211.9**	**110.7**

Notes to the Accounts (continued)

31 General reserve

	Group	Society
	£m	£m
At 5 April 2003	4,021.0	3,353.0
Profit for the year	**317.9**	**218.0**
Transfer from revaluation reserve	**2.2**	**–**
At 4 April 2004	**4,341.1**	**3,571.0**

The transfer from revaluation reserve in the Group consists of the realisations of net property revaluation gains of previous years.

The general reserve includes £96.6 million (2003 – £72.3 million) of unrealised profit in respect of the increase in the value of the Group's long term life assurance business.

Translation gains arising from foreign currency borrowings, used to hedge investments in overseas subsidiary undertakings, of Group £11.3 million, Society £nil million, (2003 – Group translation losses of £3.8 million, Society £0.8 million), together with the related tax charge of Group £3.4 million, Society £nil million, (2003 – Group credit £1.1 million, Society £0.2 million), giving net gains of Group £7.9 million, Society £nil million, (2003 – Group net losses of £2.7 million, Society £0.6 million), have been taken to the reserves of the Group and Society respectively. These translation movements are matched by corresponding translation movements on the investments in the financial statements of the Society, and translation movements on the net assets of overseas subsidiary undertakings in the Group financial statements.

32 Memorandum items

	Group		Society	
	Contract amount	Credit risk weighted amount	Contract amount	Credit risk weighted amount
	£m	£m	£m	£m
a) Commitments				
2004				
Irrevocable undrawn loan facilities	**2,871.6**	**872.6**	**2,200.7**	**673.8**
Unpaid share capital of subsidiary company	**–**	**–**	**28.3**	**28.3**
Forward asset purchases and forward deposits placed	**–**	**–**	**–**	**–**
Undrawn formal standby facilities, credit lines and other commitments to lend greater than one year	**59.0**	**5.9**	**59.0**	**5.9**
	2,930.6	**878.5**	**2,288.0**	**708.0**
2003				
Irrevocable undrawn loan facilities	3,325.6	1,021.7	2,839.0	900.0
Unpaid share capital of subsidiary company	–	–	28.3	28.3
Forward asset purchases and forward deposits placed	156.9	46.3	156.9	46.3
Undrawn formal standby facilities, credit lines and other commitments to lend greater than one year	79.0	7.9	79.0	7.9
	3,561.5	1,075.9	3,103.2	982.5

32 Memorandum items (continued)

b) Contingent liabilities

The Society on its own account and, during the period from 1 January 1990 to 31 December 1995 as appointed representative of Guardian Assurance plc ('Guardian'), sold a substantial number of endowment policies to the Society's mortgage borrowers for the purpose of repaying their mortgage loans on maturity. The value of these policies is typically related to the performance of underlying investments in managed funds. As a result of the relatively poor performance of many of these funds and of the securities market generally over the past few years some policyholders have experienced, or expect to experience, a shortfall between the value of their policies and the value of their outstanding mortgage loans at maturity.

Some of these policyholders have brought claims alleging that they were unaware of the risk attached to this type of policy.

The Society is currently seeking to ascertain and will continue to evaluate the magnitude of any potential exposure in respect of endowment related claims. As far as policies sold by Guardian are concerned Guardian contends that it is entitled to be indemnified by the Society in respect of any liability on its part to compensate policyholders. On the basis of external legal advice the Society contends that it is not liable to indemnify Guardian.

The Society has decided to make a provision in relation to its estimate of liability for such claims or potential claims against policies sold on its own account as detailed in Note 27.

33 Financial commitments

	Group		Society	
	2004	2003	**2004**	2003
	£m	£m	**£m**	£m
Capital commitments				
Capital expenditure contracted for but not provided for in the Accounts	**11.4**	9.5	**10.9**	7.1

	Land and buildings	
	2004	2003
	£m	£m
Leasing commitments		
Group		
At the balance sheet date, annual commitments under operating leases relating to land, buildings and equipment were as follows:		
Leases which expire:		
• Within one year	**7.6**	5.4
• Between one and five years	**8.4**	10.2
• After five years	**10.8**	10.9
	26.8	26.5
Society		
At the balance sheet date, annual commitments under operating leases relating to land, buildings and equipment were as follows:		
Leases which expire:		
• Within one year	**7.6**	5.3
• Between one and five years	**8.1**	10.1
• After five years	**10.4**	10.5
	26.1	25.9

Notes to the Accounts (continued)

34 Consolidated cash flow statement

	2004 £m	2003 £m
Reconciliation of operating profit to net cash inflow from operating activities		
Operating profit	**426.8**	353.3
(Increase)/decrease in prepayments and accrued income	**(115.3)**	313.5
Increase in accruals and deferred income	**13.7**	61.6
Provisions for bad and doubtful debts	**43.6**	49.4
Loans and advances written off, net of recoveries	**(36.5)**	(41.4)
Amounts (released)/written off fixed asset investments	**(26.2)**	38.2
Depreciation and amortisation	**108.8**	91.5
Interest on subordinated liabilities	**40.0**	13.6
Interest on subscribed capital	**27.8**	24.0
Profit on sale of tangible fixed assets	**(2.1)**	(1.3)
Increase in provisions for liabilities and charges	**33.5**	17.3
(Increase) in value of long term life assurance business	**(44.8)**	(43.7)
Amortisation of debt securities	**344.2**	(163.4)
Other non-cash movements	**(19.1)**	(7.6)
Net cash inflow from trading activities	**794.4**	705.0
Net (increase) in loans and advances to customers	**(14,979.9)**	(9,076.7)
Net increase in shares	**4,991.7**	5,482.7
Net increase in amounts owed to credit institutions and other customers	**767.5**	501.6
Net increase in debt securities in issue	**8,618.4**	4,113.2
Net (increase) in equity securities	**(2.4)**	(3.0)
Net (increase)/decrease in loans and advances to credit institutions	**(458.4)**	14.1
Net (increase)/decrease in other assets	**(64.7)**	56.4
Net increase/(decrease) in other liabilities	**156.3**	(40.3)
Net cash (outflow)/inflow from operating activities	**(177.1)**	1,753.0

Analysis of changes in financing during the year

	Subscribed capital £m	Subordinated liabilities £m
At 5 April 2003	296.4	594.0
Cash inflow from financing	**400.0**	**341.9**
Amortisation of premiums and issue costs	**(4.7)**	**(10.3)**
At 4 April 2004	**691.7**	**925.6**

Analysis of the balances of cash as shown in the balance sheet

	2004 £m	Flows £m	2003 £m
Cash in hand and balances with the Bank of England	**310.5**	**(37.9)**	348.4
Loans and advances to credit institutions repayable on demand	**139.4**	**29.9**	109.5
	449.9	**(8.0)**	457.9

The Group is required to maintain balances with the Bank of England which, at 4 April 2004, amounted to £105.8 million (2003 – £93.6 million).

35 Financial instruments

A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability of another entity. The contract can be cash instruments such as bonds or derivative products. The Group is a retailer of financial instruments, mainly in the form of mortgages, savings and insurance products. The Group uses wholesale financial instruments to invest liquid asset balances and raise wholesale funding and to manage the risks arising from its operations.

The Group has a formal structure for managing risk. This structure includes risk limits, reporting lines, mandates and other control procedures, and is reviewed regularly by the Assets and Liabilities Committee ('ALCO'), which is charged with the responsibility for managing and controlling interest rate and currency exposures of the Group. The minutes of ALCO are presented to the Board.

Instruments used for risk management purposes include derivative financial instruments ('derivatives'), which are contracts or agreements whose value is derived from one or more underlying price, rate or index inherent in the contract or agreement, such as interest rates, exchange rates or stock market indices.

Derivatives are only used by the Group, in accordance with the Building Societies Act 1986, to limit the extent to which the Group will be affected by changes in interest rates, exchange rates or other factors specified in the legislation. Derivatives are used purely to hedge risk exposure and are not used for speculative purposes.

Types of derivatives

The principal derivatives used in balance sheet risk management are interest rate swaps, forward rate agreements, interest rate options, cross-currency interest rate swaps, foreign exchange contracts and credit derivatives. Derivatives are used to hedge Group balance sheet exposures arising from fixed and capped rate mortgage lending and fixed rate savings products, funding and investment activities in foreign currencies or involving fixed rate instruments or instruments with embedded options.

The following table describes the significant activities undertaken by the Group, the risks associated with such activities and the types of derivatives which are typically used in managing such risks. Such risks may alternatively be managed using on balance sheet instruments as part of the Group's integrated approach to risk management.

ACTIVITY	RISK	TYPE OF DERIVATIVE INSTRUMENT USED
Management of the investment of reserves and other net non-interest bearing liabilities	Sensitivity to changes in interest rates	Interest rate swaps and forward rate agreements
Fixed rate savings products and funding activities involving either fixed rate instruments or instruments with embedded options	Sensitivity to changes in interest rates	Interest rate swaps and options
Fixed and capped rate mortgage lending and investment activities involving either fixed rate instruments or instruments with embedded options	Sensitivity to changes in interest rates	Interest rate swaps and options
Investment and funding in foreign currencies	Sensitivity to changes in foreign exchange rates	Cross-currency interest rate swaps and foreign exchange contracts
Equity-linked investment products	Sensitivity to changes in equity indices	Equity-linked futures, options and interest rate swaps
Investment of liquid resources in debt securities	Sensitivity to changes in obligor credit risk leading to default	Credit default swap

Notes to the Accounts (continued)

35 Financial instruments (continued)

Derivative products which are combinations of more basic derivatives are used only in circumstances where the underlying position being hedged contains the same risk features. For example, guaranteed equity bonds issued by the Group may be hedged with a single contract incorporating both the interest rate and equity index risk incurred. In such cases the derivatives used will be designed to match exactly the risks of the underlying asset or liability. Exposure to market risk on such contracts is therefore fully hedged.

Control of derivatives

The Board has authorised the use of derivatives in accordance with the Building Societies Act 1986. Limits over the use of derivative products are the responsibility of ALCO with the exception of the Group Credit Committee which sets Group credit policy and regularly monitors and reviews credit exposures arising in all aspects of the Group's operations, including derivatives.

All exchange-traded instruments are subject to cash requirements under the standard margin arrangements applied by the individual exchanges. Such instruments are not subject to significant credit risk. Other derivative contracts are not subject to the cash requirements. The accounting policies for 'hedging instruments' are described in the Statement of Accounting Policies.

The table on the next page analyses derivatives by type of contract and maturity and shows the contract or underlying principal amounts, credit risk weighted amounts and replacement costs of contracts. Contract or underlying principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The credit risk weighted amount, which is calculated according to rules specified by the Financial Services Authority, is based on the replacement cost, but also takes into account measures of the extent of potential future exposure and the nature of the counterparty. The replacement cost represents the cost of replacing contracts with positive values, calculated at market rates current at the balance sheet date reflecting the Group's exposure should the counterparties default.

35 Financial instruments (continued)

	Contract or underlying principal amount 2004	Credit risk weighted amount 2004	Replacement cost 2004	Contract or underlying principal amount 2003	Credit risk weighted amount 2003	Replacement cost 2003
	£m	£m	£m	£m	£m	£m
Group						
Exchange rate contracts:						
• Cross-currency interest rate swaps	**579.6**	**22.3**	**3.1**	1,133.1	14.3	19.8
• Forward foreign exchange	**6,429.6**	**64.5**	**54.7**	3,289.0	8.6	9.1
	7,009.2	**86.8**	**57.8**	4,422.1	22.9	28.9
• Under one year	**6,647.8**	**66.5**	**55.4**	3,710.3	11.8	21.5
• Between one and five years	**256.1**	**12.4**	**2.4**	508.3	7.4	6.5
• Over five years	**105.3**	**7.9**	**–**	203.5	3.7	0.9
	7,009.2	**86.8**	**57.8**	4,422.1	22.9	28.9
Interest rate contracts:						
• Interest rate swaps	**43,372.8**	**210.6**	**364.8**	25,316.0	67.1	164.2
• Swaptions	**121.4**	**1.6**	**3.5**	68.9	2.6	12.2
• Forward rate agreements	**8,069.5**	**–**	**–**	1,544.9	–	0.1
• Caps, collars and floors	**7,819.3**	**9.3**	**0.9**	7,848.8	7.7	0.6
	59,383.0	**221.5**	**369.2**	34,778.6	77.4	177.1
• Under one year	**26,964.0**	**–**	**39.9**	8,775.7	6.3	31.3
• Between one and five years	**26,481.6**	**132.5**	**230.1**	22,121.9	32.2	50.7
• Over five years	**5,937.4**	**89.0**	**99.2**	3,881.0	38.9	95.1
	59,383.0	**221.5**	**369.2**	34,778.6	77.4	177.1
Equity and credit contracts:						
• Equity contracts	**1,396.7**	**112.6**	**893.2**	1,204.7	154.7	674.7
• Credit contracts	**829.5**	**–**	**–**	850.9	–	2.4
	2,226.2	**112.6**	**893.2**	2,055.6	154.7	677.1
• Under one year	**133.5**	**8.0**	**130.6**	17.5	3.6	16.9
• Between one and five years	**1,917.2**	**87.0**	**596.9**	1,904.6	123.6	535.9
• Over five years	**175.5**	**17.6**	**165.7**	133.5	27.5	124.3
	2,226.2	**112.6**	**893.2**	2,055.6	154.7	677.1

All of the Group's derivatives activity is contracted with OECD financial institutions.

The financial risks faced by the Group include liquidity risk, market risk and credit risk.

Liquidity risk

The Group's liquidity policy is to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding, to retain full public confidence in the solvency of the Group and to enable the Group to meet its financial obligations. This is achieved through maintaining a prudent level of liquid assets, through management control of the growth of the business and through wholesale funding facilities. As at 4 April 2004, the Group maintained £1.6 billion of committed standby facilities (2003 – £1.4 billion), of which £1.0 billion (2003 – £0.6 billion) are due to mature within one year.

Notes to the Accounts (continued)

35 Financial instruments (continued)

Market risk

The primary market risk faced by the Group is interest rate risk. The net interest income and market value of the Group is exposed to movements in interest rates. This exposure is managed on a continuous basis, within limits set by the Board, using a combination of on and off balance sheet instruments. In the table below items are allocated to time bands. After taking into account the various derivatives entered into by the Group, the interest rate sensitivity exposure of the Group by reference to the earlier of the next contractual interest rate repricing date and the maturity date was:

At 4 April 2004 – Repricing date

	Not more than 3 months	More than 3 months but not more than 6 months	More than 6 months but not more than 1 year	More than 1 year but not more than 5 years	More than 5 years	Non-interest bearing	Total
	£m	£m	£m	£m	£m	£m	£m
ASSETS							
Liquid assets	12,736.5	1,828.0	576.4	1,362.6	419.7	502.2	17,425.4
Loans and advances to customers	45,944.8	1,061.1	5,058.6	24,903.3	3,986.5	(248.1)	80,706.2
Fixed assets	–	–	–	–	–	857.6	857.6
Other assets	–	–	–	–	–	2,439.2	2,439.2
Total assets	58,681.3	2,889.1	5,635.0	26,265.9	4,406.2	3,550.9	101,428.4
LIABILITIES							
Shares	61,414.7	249.0	310.6	3,920.4	49.2	–	65,943.9
Amounts owed to credit institutions and other customers and debt securities in issue	21,887.2	2,929.7	562.5	1,072.5	210.7	109.7	26,772.3
Other liabilities	–	–	–	–	–	2,541.9	2,541.9
Subordinated liabilities	252.1	–	–	–	673.5	–	925.6
Subscribed capital	–	–	–	–	691.7	–	691.7
Reserves	–	–	–	–	–	4,553.0	4,553.0
Total liabilities	83,554.0	3,178.7	873.1	4,992.9	1,625.1	7,204.6	101,428.4
Off balance sheet items	24,528.5	1,368.1	(4,101.7)	(19,003.5)	(2,791.4)	–	–
Interest rate sensitivity gap	(344.2)	1,078.5	660.2	2,269.5	(10.3)	(3,653.7)	–
Cumulative interest rate sensitivity gap	(344.2)	734.3	1,394.5	3,664.0	3,653.7	–	

35 Financial instruments (continued)

At 4 April 2003 – Repricing date

	Not more than 3 months	More than 3 months but not more than 6 months	More than 6 months but not more than 1 year	More than 1 year but not more than 5 years	More than 5 years	Non-interest bearing	Total
	£m	£m	£m	£m	£m	£m	£m
ASSETS							
Liquid assets	12,909.6	1,050.0	607.9	1,074.6	829.1	514.0	16,985.2
Loans and advances to customers	39,893.2	1,384.5	2,802.5	18,046.3	3,819.2	(212.3)	65,733.4
Fixed assets	–	–	–	–	–	798.4	798.4
Other assets	–	–	–	–	–	1,900.7	1,900.7
Total assets	52,802.8	2,434.5	3,410.4	19,120.9	4,648.3	3,000.8	85,417.7
LIABILITIES							
Shares	58,379.4	114.2	385.5	1,992.4	72.0	–	60,943.5
Amounts owed to credit institutions and other customers and debt securities in issue	14,754.0	1,711.8	351.4	248.3	239.1	81.8	17,386.4
Other liabilities	–	–	–	–	–	2,011.3	2,011.3
Subordinated liabilities	272.4	–	–	–	321.6	–	594.0
Subscribed capital	–	–	–	–	296.4	–	296.4
Reserves	–	–	–	–	–	4,186.1	4,186.1
Total liabilities	73,405.8	1,826.0	736.9	2,240.7	929.1	6,279.2	85,417.7
Off balance sheet items	21,040.0	122.3	(2,137.2)	(15,250.6)	(3,774.5)	–	–
Interest rate sensitivity gap	437.0	730.8	536.3	1,629.6	(55.3)	(3,278.4)	–
Cumulative interest rate sensitivity gap	437.0	1,167.8	1,704.1	3,333.7	3,278.4	–	

These tables do not take into account the effect of interest rate options used by the Group. All options have been executed to hedge underlying risk positions and further information is given in the table on page 73.

Liquid assets include cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.

Other assets include equity shares, other assets, prepayments and accrued income and long term life assurance business assets.

Other liabilities include other liabilities, accruals and deferred income, provisions for liabilities and charges and long term life assurance business liabilities.

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.

The Group monitors market price risk daily by determining the effect on the Group's current net worth of a shift in interest rates broadly equivalent to 3% for short maturities tapering to 2% for maturities of 5 years or more. This is termed 'Immediate risk'.

The maximum limit for Immediate risk has been set by the Board at 8% of the Group's consolidated reserves at the beginning of each quarter in the Society's financial year.

Notes to the Accounts (continued)

35 Financial instruments (continued)

The size of Immediate risk at any time reflects the Group's degree of concurrence with the future levels of interest rates implied by current interest rate levels. During the year ended 4 April 2004, Immediate risk as a percentage of consolidated reserves at the beginning of each quarter was maintained in the range 4.9% to 5.6% (2003 – 4.3% to 5.4%), with an average of 5.2% (2003 – 4.7%). At 4 April 2004 its value was 4.9% (2003 – 5.1%).

The Group had a subsidiary whose functional currency was yen. The transaction underlying this investment ceased on 29 March 2004. Structural currency exposure related to this investment was fully hedged, consistent with the Group's policy on currency risk. Exchange movements on the translation of the investment and exchange movements net of taxation on the associated hedge transactions are recognised in the statement of total recognised gains and losses.

In line with the prudential guidance applying to all building societies and after taking account of foreign currency derivatives, the Group has no substantial net exposure to foreign exchange rate fluctuations or changes in foreign currency interest rates.

Credit risk

Credit risk is the risk that counterparties will not be able to meet their obligations as they fall due. The Credit Committee is responsible for approving and monitoring the Group's credit exposures which it does through reviewing and approving the Group's lending policy and credit scoring systems and through setting limits on credit exposures to individual counterparties and across countries and industrial sectors. The minutes of the Credit Committee are presented to the Board.

The Group has entered into a credit derivative in order to manage the credit risk of an investment portfolio. The credit derivative enables the Group to transfer a proportion of the credit risk relating to the relevant securities to a third party whilst retaining the underlying investment portfolio.

Recognised gains and losses on hedges

As explained in the Statement of Accounting Policies the Group uses hedge accounting to recognise gains and losses on instruments used for hedging specific financial instruments over the residual life of the underlying instruments. The table below shows the extent of hedge accounting within the Group:

	Gains	Losses	Net Gains/ (Losses)
	£m	£m	£m
Amounts deferred in the balance sheet as at 4 April 2003	14.1	(18.4)	(4.3)
Amounts recognised in the year to 4 April 2004	**(7.1)**	**2.6**	**(4.5)**
Amounts not recognised in the year to 4 April 2004	**7.0**	**(15.8)**	**(8.8)**
Amounts arising in the year to 4 April 2004 that were not recognised in that year	**(0.2)**	**0.6**	**0.4**
Amounts deferred in the balance sheet as at 4 April 2004	**6.8**	**(15.2)**	**(8.4)**
Expected to be recognised in the year to 4 April 2005	**(3.8)**	**1.4**	**(2.4)**
Expected to be recognised thereafter	**10.6**	**(16.6)**	**(6.0)**

Unrecognised gains and losses on hedges

Gains and losses on instruments used for hedging are not recognised, as these hedges are accounted for on an accruals basis in line with the underlying instruments being hedged. The following table shows gains and losses that would occur if these instruments were carried at market value.

35 Financial instruments (continued)

	Gains	Losses	Net Gains/ (Losses)
	£m	£m	£m
Unrecognised gains and losses on hedges as at 4 April 2003	142.1	(736.3)	(594.2)
Of which recognised in the year to 4 April 2004	**(20.5)**	**75.2**	**54.7**
Gains and losses arising not recognised in the year to 4 April 2004	**121.6**	**(661.1)**	**(539.5)**
Gains and losses arising in the year to 4 April 2004 that were not recognised in that year	**182.8**	**184.8**	**367.6**
Unrecognised gains and losses on hedges as at 4 April 2004	**304.4**	**(476.3)**	**(171.9)**
Of which expected to be recognised in the year to 4 April 2005	**9.3**	**(33.6)**	**(24.3)**
Expected to be recognised thereafter	**295.1**	**(442.7)**	**(147.6)**

The differences between book and fair value of off balance sheet instruments do not represent absolute gains or losses expected by the Group as they will be substantially offset by corresponding losses or gains arising from on balance sheet assets and liabilities.

FAIR VALUES OF FINANCIAL INSTRUMENTS

The table below compares the book and fair values of some of the Group's financial instruments by category as at 4 April 2004 and 4 April 2003. The fair value of a financial instrument represents the amount at which assets, liabilities and derivatives held could be sold between willing parties at the balance sheet date. Where available, market values have been used to determine fair values. Where market values are not available, fair values have been calculated. Option values have been calculated by using option-pricing models and other financial instruments values have been calculated by discounting cash flows at prevailing interest and exchange rates and credit spreads.

	2004				2003			
	Positive		**Negative**		Positive		Negative	
	Book value	**Fair value**	**Book value**	**Fair value**	Book value	Fair value	Book value	Fair value
	£m	£m	£m	£m	£m	£m	£m	£m
ASSETS/(LIABILITIES)								
On balance sheet instruments:								
Loans and advances to credit institutions	**1,358.3**	**1,362.0**	**–**	**–**	882.2	882.3	–	–
Debt securities	**15,650.8**	**15,695.9**	**–**	**–**	15,661.0	15,932.0	–	–
Other assets	**–**	**–**	**–**	**–**	–	–	–	–
Amounts owed to credit institutions	**–**	**–**	**(2,229.3)**	**(2,229.0)**	–	–	(1,834.8)	(1,835.1)
Amounts owed to other customers	**–**	**–**	**(3,064.2)**	**(3,065.8)**	–	–	(2,753.5)	(2,758.4)
Debt securities in issue	**–**	**–**	**(19,706.6)**	**(20,042.9)**	–	–	(11,006.7)	(11,054.7)
Subordinated liabilities	**–**	**–**	**(926.1)**	**(995.9)**	–	–	(588.0)	(703.7)
Subscribed capital	**–**	**–**	**(697.0)**	**(811.8)**	–	–	(297.9)	(364.5)
Off balance sheet instruments:								
Interest rate swaps	**64.2**	**364.8**	**(83.2)**	**(440.5)**	57.5	164.2	(64.2)	(750.3)
Forward rate agreements	**0.1**	**–**	**(0.1)**	**(0.9)**	(0.2)	0.1	–	–
Caps, collars and floors	**3.2**	**0.9**	**–**	**–**	7.1	0.6	–	(1.8)
Swaptions	**0.9**	**3.5**	**–**	**–**	(0.2)	12.2	–	–
Cross-currency interest rate swaps	**(0.5)**	**3.1**	**(9.9)**	**(101.1)**	(2.1)	19.8	(9.6)	(51.5)
Forward foreign exchange	**54.7**	**54.7**	**(85.9)**	**(85.9)**	9.1	9.1	(55.1)	(55.1)
Credit derivatives	**–**	**–**	**1.5**	**(25.5)**	1.6	2.4	–	–

Notes to the Accounts (continued)

35 Financial instruments (continued)

The book value of off balance sheet instruments represents the equivalent value at which such instruments would be carried in the balance sheet. This primarily consists of interest accruals and unaccreted forward points.

The table excludes certain financial assets and liabilities which are not listed or publicly traded, or for which a liquid and active market does not exist. It excludes mortgages, retail savings accounts and other balance sheet items whose book and fair values differ.

The book value for subordinated liabilities includes £1.8 million (2003 – £6.0 million) included within prepayments and accrued income and accruals and deferred income.

The book value for subscribed capital includes £5.2 million (2003 – £1.5 million) included within accruals and deferred income.

36 Non-Sterling assets and liabilities

	Group and Society	
	2004	2003
	£m	£m
The aggregate amount of assets and liabilities included in the balance sheet denominated in a currency other than Sterling was as follows:		
Assets	**8,347.8**	7,839.7
Liabilities	**12,519.2**	5,073.2

The Group’s non-Sterling assets and liabilities are hedged on balance sheet or by using derivatives to eliminate material currency exposures.

37 Directors' loans and related party transactions

The aggregate amount outstanding at the end of the financial year in respect of loans from the Society or a subsidiary company to Directors of the Society or persons connected with a Director of the Society was £1,859,573 (2003 – £1,196,285) representing loans to 9 persons (2003 – 10 persons).

A register is maintained by the Society containing details of loans, transactions and arrangements made between the Society or its subsidiary undertakings and Directors of the Society or persons connected with Directors of the Society. The register will be available for inspection by members at the Annual General Meeting on 22 July 2004 and during normal office hours at the Society's principal office (Nationwide House, Pipers Way, Swindon) during the period of 15 days prior to the meeting.

Included in fees and commissions receivable is an amount of £15.0 million (2003 – £11.4 million) receivable from the life assurance subsidiary in respect of life assurance products sold through the retail network, less associated sales force costs of £13.4 million (2003 – £11.4 million).

There are no other related party transactions which require disclosure under FRS 8 (Related Party Disclosures).

Annual Business Statement

For the year ended 4 April 2004

1 Statutory percentages

	2004 %	Statutory Limit %
Lending limit	**13.1**	25.0
Funding limit	**28.9**	50.0

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986 as amended by the Building Societies Act 1997.

The lending limit measures the proportion of business assets not in the form of loans fully secured on residential property and is calculated as (X–Y)/X where:

X = business assets, being the total assets of the Group plus provisions for bad and doubtful debts less liquid assets, fixed assets and long term life assurance business assets as shown in the Group Balance Sheet.

Y = the principal of, and interest accrued on, loans owed to the Group which are fully secured on residential property.

The funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals and is calculated as (X–Y)/X where:

X = shares and borrowings, being the aggregate of:

i) the principal value of, and interest accrued on, shares in the Society;
ii) the principal of, and interest accrued on, sums deposited with the Society or any subsidiary undertaking of the Society; and
iii) the principal value of, and interest accrued under, bills of exchange, instruments or agreements creating or acknowledging indebtedness and accepted, made, issued or entered into by the Society or any such undertaking, less any amounts qualifying as own funds.

Y = the principal value of, and interest accrued on, shares in the Society held by individuals otherwise than as bare trustees (or, in Scotland, simple trustees) for bodies corporate or for persons who include bodies corporate.

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

Annual Business Statement (continued)

For the year ended 4 April 2004

2 Other percentages

	2004	2003
	%	%
As a percentage of shares and borrowings:		
• Gross capital	**6.7**	6.5
• Free capital	**5.9**	5.7
• Liquid assets	**18.8**	21.7
Profit for the financial year as a percentage of mean total assets	**0.34**	0.33
Management expenses as a percentage of mean total assets	**0.93**	1.01

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

- 'Shares and borrowings' represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue.
- 'Gross capital' represents the aggregate of general reserve, revaluation reserve, subscribed capital and subordinated liabilities.
- 'Free capital' represents the aggregate of gross capital and general loss provisions for bad and doubtful debts less tangible and intangible fixed assets.
- 'Liquid assets' represent the total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.
- 'Mean total assets' represent the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.
- 'Management expenses' represent the aggregate of administrative expenses, depreciation and amortisation.

Annual Business Statement (continued)

For the year ended 4 April 2004

3 Information relating to Directors and other Officers

At 4 April 2004

Directors

Name and date of birth	Occupation	Date of appointment	Other directorships
J G W Agnew MA Chairman 30 July 1941	Banker	1 March 1997	Beazley Group plc Beazley Furlonge Ltd Jarvis plc Soditic Ltd Soditic SA Thos Agnew & Sons Ltd
B A Walsh MSc (Econ), FCMA, CIMgt Deputy Chairman 27 May 1944	Company Director	2 August 1999	
P F Williamson BA (Econ), FCIB 11 December 1947	Chief Executive	5 April 1996	Building Societies Association, Council Member
B K Simpson MIMIS, FRSA 29 January 1948	Deputy Chief Executive and Chief Operating Officer	4 May 1994	Nationwide Anglia Property Services Ltd Nationwide Trust Ltd NBS Fleet Services Ltd The Nationwide Foundation
G J Beale BSc, ACA 19 October 1958	Group Finance Director	5 April 2003	First Nationwide Investments Ltd First Nationwide Nationwide Anglia Property Services Ltd NBS Fleet Services Ltd
S D M Bernau BSc (Econ), FCIB, MCT 15 August 1951	Commercial and Treasury Director	1 November 1996	at.home nationwide ltd Council of Mortgage Lenders, Executive Committee Member Council of Mortgage Lenders, Chairman's Committee, Deputy Chairman Council of the Chartered Institute of Bankers, Member Ethos Independent Financial Services Ltd Financial Services National Training Organisation, Member First Nationwide First Nationwide Investments Ltd Nationwide BES Fund Managers Ltd Nationwide Housing Trust Ltd Nationwide Investments (No 1) Ltd Nationwide Lease Finance Ltd Nationwide Mortgage Corporation Ltd Nationwide Life Ltd Nationwide Syndications Ltd Nationwide Unit Trust Managers Ltd The Minchinhampton Golf Club Ltd

Annual Business Statement (continued)

For the year ended 4 April 2004

3 Information relating to Directors and other Officers (continued)

At 4 April 2004

Directors

Name and date of birth	Occupation	Date of appointment	Other directorships
J H Willens MBA, DMS, ACIB 7 June 1956	Retail Operations Director	1 January 2002	Institution of Financial Services Retail Faculty Board, Member Monument (Sutton) Ltd Nationwide Anglia Property Services Ltd Nationwide Home Loans Ltd Nationwide Life Ltd Nationwide Unit Trust Managers Ltd UCB Home Loans Corporation Ltd
Mrs S J David MA Cantab 20 November 1962	Company Director	16 April 2003	Bacardi UK Ltd Bacardi-Martini b.v. Bacardi-Martini Ltd First Drinks Brands Ltd Supervisory Board of Bacardi-Martini Netherlands NV The Pure Brewing Company Ltd Westbay Distributors Ltd
J Engestrom MBA 7 February 1942	Company Director	1 March 1997	Nationwide Life Ltd Nationwide Unit Trust Managers Ltd Wellington Underwriting Agencies Ltd Wellington Underwriting plc
Ms R E Evans MA 12 October 1957	Company Director	1 April 2002	General Medical Council, Lay Member and Chairman of Standards Committee Independent Inquiry into Drug Testing At Work, Chairman Law Society Governance Review Group, Member Ofcom Consumer Panel, Deputy Chair Panel of Independent Assessors, Office of the Commissioner for Public Appointments, Member Tribunals for Users Programme Interdepartmental Steering Group, non-executive Member
R G Handover 13 April 1946	Company Director	1 May 2000	Adult Learning Inspectorate, Chairman Business in the Community, Vice Chairman Royal Mail Holdings plc WHSmith plc, Chairman
R P Walther MA, FIA 31 July 1943	Company Director	1 July 2002	Fidelity European Values plc, Chairman JP Morgan Fleming Claverhouse Investment Trust plc, Chairman Nationwide Life Ltd Nationwide Unit Trust Managers Ltd

Documents may be served on any of the Directors at Burges Salmon LLP, Narrow Quay House, Narrow Quay, Bristol, BS1 4AH

Directors' Service Contracts

Details of the Directors' service contracts are shown in the Report of the Directors on Remuneration.

Directors' Share Options

No Director or other Officer, including connected persons, has any rights to subscribe for shares in, or debentures of, any connected undertaking of the Society.

Annual Business Statement (continued)

For the year ended 4 April 2004

3 Information relating to Directors and other Officers (continued)

At 4 April 2004

Officers

Name	Occupation	Directorships
R T Bailey DMS	Divisional Director (Branch Network)	
S C Clode BSc (Econ), MA, PhD	Divisional Director (Marketing)	Lingmoor View Management Ltd Nationwide Trust Ltd
A J del Strother BA, FCIB, FCIPD	Divisional Director (Personnel and Development)	The Nationwide Foundation
P Feldman BSc (Hons), PhD	Divisional Director (Banking and Savings)	BACS Ltd Cheque and Credit Clearing Company Ltd Council of Association of Payment and Clearing Services (APACS), Member LINK Interchange Network Ltd Nationwide International Ltd
M R Jenkins BA (Hons), FCA, DIPL	Divisional Director (Commercial)	at.home nationwide ltd Longwide Ltd Nationwide BES Fund Managers Ltd Nationwide Housing Trust Ltd Nationwide Lease Finance Ltd Nationwide Mortgage Corporation Ltd Nationwide Syndications Ltd
T L Morshead FCIM	Divisional Director (Mortgages and Insurance)	Ethos Independent Financial Services Ltd Foundation Insurance Ltd MBL Financial Services Ltd MBL Holdings Ltd Mortgage Brain Ltd Nationwide Life Ltd Nationwide Unit Trust Managers Ltd Premier Processing Services Ltd The Mortgage Trading Exchange Ltd
D G Parry ACIB, DMS	Divisional Director (Finance and Planning)	
D J Rigney ACMA, MBA	Divisional Director (Central Retail Operations)	
J A Sutherland MA, MBA, FCIB, Dip FS	Divisional Director (Member Account Administration)	Prospect Foundation Ltd
W P Tonks MA, CPFA	Divisional Director (Risk Management)	Council of Management of the Regulatory Policy Institute
F I Walsh BSc	Divisional Director (Technology)	Nationwide International Ltd
C R L Wilson	Divisional Director (Legal Compliance)	
J R Wood	Divisional Director (Treasury)	Aldbury Housing Association First Nationwide Nationwide Lease Finance Ltd

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