proud to be different

We're different because we're a building society, run for the benefit of our members, unlike banks who put their shareholders first. Our principles of fairness, honesty and openness enable us to offer better rates and an excellent level of service. In fact, we have returned an estimated £4.3 billion to our members since 1996 through better deals on the products and services we offer.

- Underlying profit before tax of **£539.4 million**.
- Costs as a percentage of mean total assets reduced for **17th successive year**.
- Pricing benefits up **7%** to an estimated **£690 million**.
- Gross residential lending **£21.1 billion**.
- Unsecured gross personal lending up **16%** to **£1.3 billion**.
- Retail savings deposit growth of **£8.3 billion**.
- Current account sales up **9%**.
- Credit card sales up **16%**.

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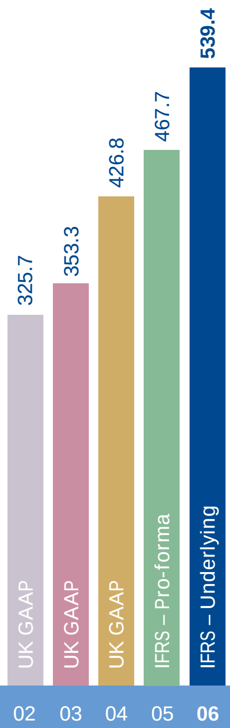


Profit before tax (£million)

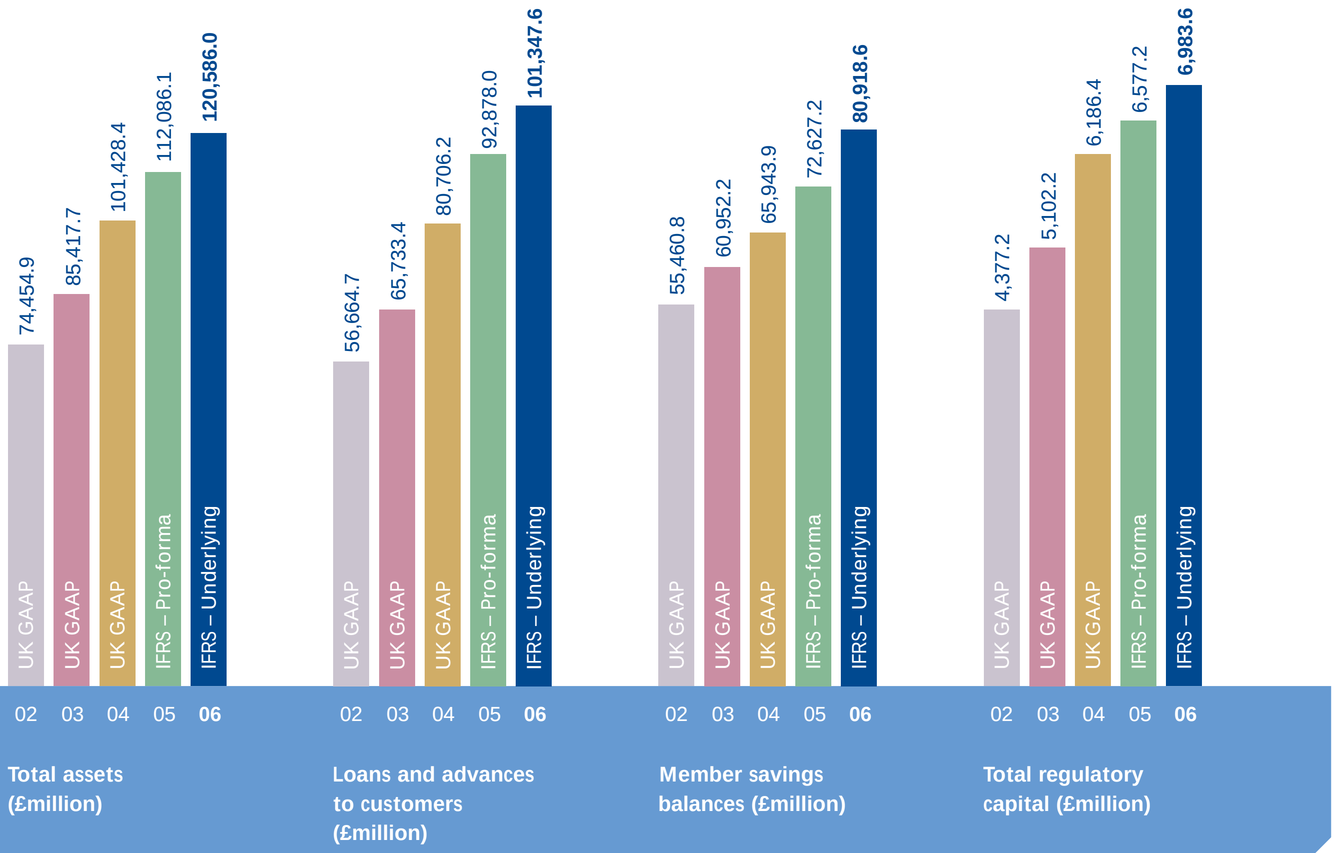
Total income net of claims on insurance contracts (£million)

Cost income ratio (%)

Financial Highlights

		2002 UK GAAP	2003 UK GAAP	2004 UK GAAP	2005 IFRS Pro-forma	**2006 IFRS Underlying**
Profit before tax	£m	325.7	353.3	426.8	467.7	**539.4**
Total income net of claims on insurance contracts	£m	1,173.9	1,259.0	1,349.7	1,518.4	**1,635.7**
Cost income ratio	%	64.7	64.1	64.1	61.9	**60.6**
Total assets	£m	74,454.9	85,417.7	101,428.4	112,086.1	**120,586.0**
Loans and advances to customers	£m	56,664.7	65,733.4	80,706.2	92,878.0	**101,347.6**
Member savings balances	£m	55,460.8	60,952.2	65,943.9	72,627.2	**80,918.6**
Total regulatory capital	£m	4,377.2	5,102.2	6,186.4	6,577.2	**6,983.6**

- Underlying profit before tax up **15.3%** to **£539.4 million.**
- Total income net of claims on insurance contracts up **7.7%** from £1,518.4 million to **£1,635.7 million**.
- Cost income ratio down from 61.9% to **60.6%**.
- Total assets up **7.6%** from £112.1 billion to **£120.6 billion**.
- Loans and advances to customers up **9.1%** from £92.9 billion to **£101.3 billion**.
- Member savings balances up **11.4%** from £72.6 billion to **£80.9 billion**.
- Total regulatory capital rose to **£7.0 billion** from £6.6 billion.



Chairman's Statement

Financial results

Nationwide has had another successful year. Our underlying pre-tax profit increased by 15.3% to £539.4 million and we have again improved our efficiency; our ratio of cost to income has been further reduced to 60.6%. Our total assets exceed £120 billion and our solvency ratio remains strong at 11%. Our asset quality is high; arrears on financial mortgages are around a third of the industry average. Further details of our financial performance can be found in the Business Review, which begins on page 6.

We estimate that last year we delivered a record £1,087 million of value to our members, comprising an estimated £690 million pricing benefits and £397 million retained profit. Since 1996 pricing benefits have amounted to £4.3 billion, which demonstrates the value which we as a building society can give to our members, since we do not need to pay dividends to shareholders.

Member involvement

One way in which members can express their opinion is by voting in the election of directors and on resolutions proposed at the Annual General Meeting. This differentiates us from our public company competitors whose customers do not have votes unless they are also shareholders. In recent years the number of members who have cast their vote has fallen. We are keen to reverse this and this year we are providing members who vote with the opportunity to raise £100,000 for charity, to help athletes with disabilities.

We are also making it easier for our members to vote by introducing a "Quick Vote" feature in the voting form and by proposing a resolution which, if passed, will make it possible for members to vote online in 2007.

In his review, Philip Williamson describes some of the ways in which we seek members' views on our products and services and act upon what we learn.

Community and environmental issues

We continue to carry out our broader responsibilities, from the way in which we engage our members and employees to helping protect the environment. For example, in October we entered into a one year contract to buy electricity from renewable energy sources. A summary of our community and environmental performance can be found on page 22 and we will publish full details in our *Better Society* report later this year.

We continue to support many charitable causes including Macmillan Cancer Support, which our employees voted in August should remain our flagship charity; Y Care International's appeal to help those whose lives were devastated by the Tsunami and Asian earthquakes; and the Nationwide Foundation, about which details can be found on page 26. In November we announced that we would become the main sponsor of Disability Sport Events in a deal worth £1 million over the next seven years.

Board and Employees

We were pleased to welcome as a non-executive director Suzanna Taverne who brings broad experience of strategy and finance of both private and public sector organisations. John Engestrom and Brian Walsh will be retiring from the Board at this year's Annual General Meeting. Brian Walsh has been deputy-chairman and chairman of the Audit Committee and John Engestrom has been chairman of the Remuneration Committee as well as a non-executive director of Nationwide Life. They have both made valuable contributions to the Board over many years for which we thank them.

I should also pay tribute to the enthusiasm, dedication and professionalism of our employees. The achievements of Nationwide are attributable to their efforts to put the interests of members first. On behalf of our members, the Board thanks our employees wholeheartedly.

Jonathan Agnew
Chairman

17 May 2006

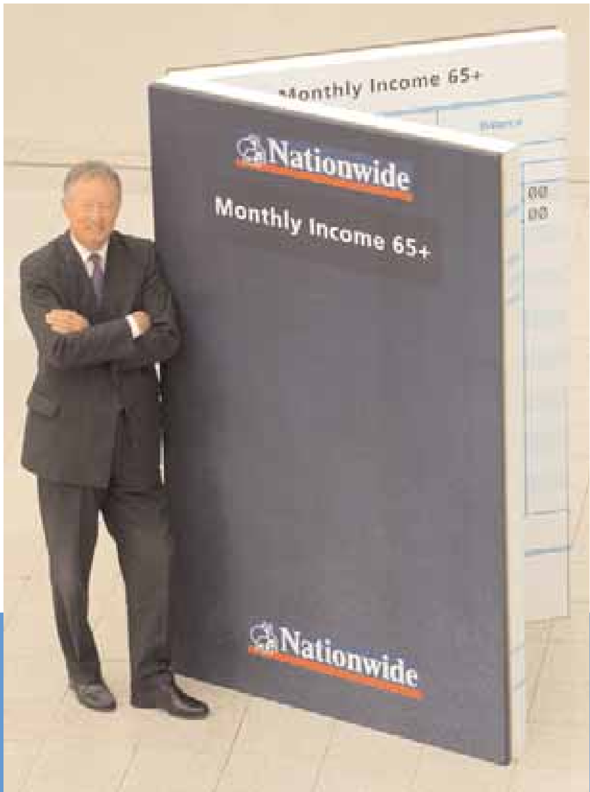
We estimate that last year we delivered a record £1,087m of value to our members

Chief Executive's Review

Proud to be different

I am delighted to be able to tell you that we have delivered another strong performance as a modern mutual building society. We have continued to put our members' interests first by ensuring they receive consistently good value products and services. Because we give better value than the banks, around 3,000 new members are joining us every single day.

We have performed exceptionally well in the retail savings market, achieving a market share of 12.8%. Most notably we have captured a significant proportion of the Child Trust Fund market. We have expanded our range of competitively priced products, and introduced new features to existing products, often in response to feedback from our members. One example is our Monthly Income 65+ account, which we launched at our Annual General Meeting last summer. The account offers a highly competitive rate, monthly interest and the convenience of a passbook – all features that our three million older members told us they wanted. Our Members' Summer and



Maturity Bonds offered market-leading rates and over 90,000 of them were opened by loyal members who have been with us for three years or more.

We were able to deliver more good news for older members when we re-introduced a travel product specifically for the over 65s. Many members in that age group were finding it increasingly difficult to find affordable travel insurance and we were delighted to be able to meet their needs. Similarly, we launched a whole of life plan for the over 55s, which guarantees acceptance between the ages of 55 and 75 without the need for a medical or statement of health.

In a highly competitive mortgage market, we've maintained our focus on making prime quality residential loans, achieving net advances of £6.3 billion. The quality of our residential mortgage book remains very high and no significant credit deterioration was identified in the year. In fact, for the second year running, we've had minimal bad debts write off for residential mortgages. We have continued to offer excellent value as a lender, and we have made several improvements to our mortgage range. In January we launched a lifetime tracker product that tracks the Bank of England Base Rate for up to 40 years. We also introduced a 'switch and fix' facility that gives borrowers confidence when taking out a tracker mortgage that they can switch to one of our fixed rate products at any time without paying early redemption charges.

We have maintained our fair and transparent approach by ensuring that our personal loan customers get our published rates. This is in contrast to many of the banks that advertise one rate but charge a different, usually

Around 3,000 new members are joining us every single day

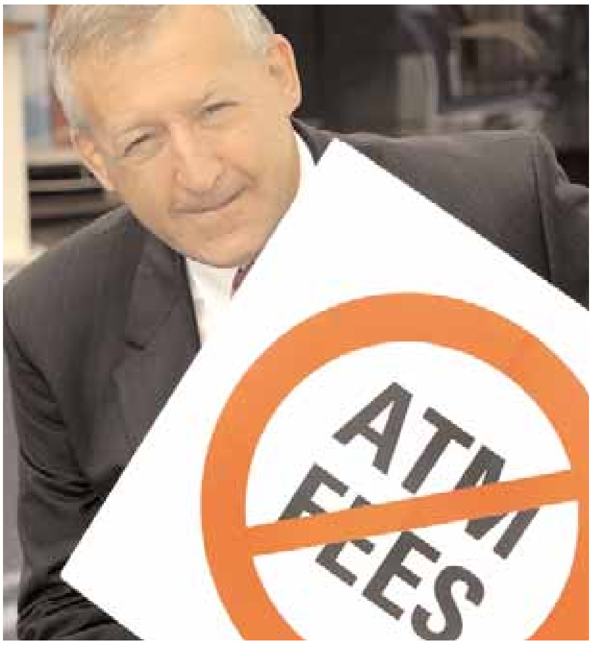
Chief Executive's Review

CONTINUED

>>> higher, rate depending on the customer's credit rating. We changed the pricing structure for our personal loans in January, introducing our lowest ever rate for customers borrowing over £7,500.

Nationwide Investment Group celebrated its 10th anniversary this year. Since its inception, it has grown to manage around £5 billion and has in excess of 800,000 customer relationships. Its products reflect the value people expect from the Nationwide brand – for example, its Target Return Fund has achieved impressive growth and exceeded its target in its first year. In the wholesale market, we became the first UK building society to issue a Covered Bond. The €2 billion 10-year transaction gives us access to new global capital market investors, strengthening our position as the world's largest building society.

Evidence of the long-term good value our products offer could be found in *The Sunday Times*, where our e-Savings, Cash ISA and TESSA-only ISA accounts were named regularly among those offering the most consistent return over the last three years. We also appeared 1,854 times in 'best buy' tables published by the national press and picked up several prestigious awards from major industry magazines, including 'Best Building Society', 'Best Remortgage Lender' and 'Best First Time Buyer Lender' from *Your Mortgage*. Further acclaim came from PressWatch, the independent press monitoring agency, who named us the financial services provider with the most positive press coverage for the sixth consecutive year.



Member involvement

Listening to our members remains high on our agenda, and we have continued to develop a range of mechanisms through which our members can voice their opinion. Our directors, including myself, met members at TalkBack events around the country to discuss the issues that affect the running of their Society. Our online debates have also been popular, attracting a record number of participants who prefer to do business with us over the internet.

Our Customer Experience Tracker – involving an external accredited research company telephoning around 2,000 members on our behalf every month – has helped us pinpoint where we're doing well, not so well and what's important to our members. In addition, our employees have recorded over 120,000 pieces of feedback – from casual remarks to formal complaints – at the point of engagement. This information, together with what we learn from other sources of feedback, has helped us understand members' expectations and allowed us to deliver a range of improvements to our products and services. For example, in some of our busiest branches we have installed extra counters and cash machines, and we have made several of our forms clearer and processes simpler. These adjustments, no matter how small, add up to improve our members' experience overall, so that they'll want to keep doing business with us and will recommend us to their friends and family.

Consumer champion

We have continued to campaign hard on behalf of consumers, not least on the matter of people's access to their own money from free cash machines. We forecast that in 2006, UK consumers will pay a record £250 million to withdraw money from charging cash machines. By way of an example to the rest of the industry, in November we introduced even clearer signage on all of our cash machines so consumers could see at a glance that they would not be charged. We would like to see all providers of cash machines introduce equivalent signage to make it easier for consumers to differentiate between those machines that charge and those that don't.

Our policy of not charging a foreign currency loading fee for customers who use our cards abroad has continued to receive recognition from the media and appreciation from UK holidaymakers. In February we highlighted another issue by launching a guide card to raise awareness among members of the pitfalls of Dynamic Currency Conversion (DCC). The guide card recommends that in many of the most popular holiday destinations it is advantageous to opt to pay for purchases in the local currency when using a

We appeared **1,854 times** in 'best buy' tables

Chief Executive's Review

CONTINUED

credit or debit card. We estimate that in July 2005 alone UK holidaymakers were charged almost £5 million by retailers using DCC overseas.

Easier to do business with

We are now two years into our £300 million six-year investment programme to improve access to our services for members – whether that's by phone, post, online or throughout our network of branches and agencies. So far, over 160 branches have benefited from this investment, including the opening of a new branch in Washington, Tyne & Wear. In February we opened a new call centre in Wakefield, providing employment for up to 300 people. It's our third new call centre in four years, reflecting our commitment to keeping call centres in the UK and supporting the communities from which we have grown.

In August we launched a Telephone Self Service banking facility, giving our current account customers a fully automated facility to carry out transactions. The service uses the latest speech recognition technology supported by traditional 'touch tone' functions to allow customers to access their account anytime, anywhere. So far, over 50,000 members have registered for the service.

Our greatest asset

I believe strongly that it's our people who give us the competitive edge. To maintain that edge, we are investing £100 million over the next five years in our front-line employees. As well as recruiting an extra 350 people into our branch network and call centres, and creating over 1,000 opportunities for promotion, we are strengthening our management structure and providing sales coaching and compliance management. We expect this investment to bear fruit over the next few years in the form of better service and stronger sales.

Once again this year, we achieved a high position in *The Sunday Times* Best Big Companies to Work For annual survey of UK employers, which is judged primarily on employees' feedback. While third place was not quite the top spot we had achieved the year before, it was still a hugely satisfying result given the greater number of organisations who had competed for places.

We have continued to lead the way with our employment policies. In June we extended our terms and conditions to allow employees to work until the age of 75 if they wish to do so. While giving greater choice to our people, we recognise there is a business benefit too – older employees help increase levels of satisfaction among our customers.

Involving employees in the shaping of our employment policies has helped us achieve a high level of employee commitment. To ensure our people's interests continue to be at the heart of our plans, we have established an Employee Involvement Committee, involving representatives from our Staff Union. The Committee will ensure employees are informed and consulted on specific issues and promote a strong local dialogue between managers and employees.

Finally, I would like to add my thanks to those expressed by the Chairman and the Board to all our employees. I never cease to be inspired by their commitment and professionalism. I'm very proud to lead such a great team.

Philip Williamson
Chief Executive

17 May 2006

We are investing £100m over the next five years in our front-line employees

Business Review

Overview

We operate as a retailer of a broad range of personal financial services products to provide maximum value to our membership through better pricing and an excellent service delivered using an efficient distribution and support infrastructure.

The success of this strategy is evidenced by our delivering a broad range of financial services products to our members whilst increasing our underlying profit before tax to £539.4 million, an increase of 15.3% compared with 2005 pro-forma results of £467.7 million. This resulted in £397.2 million profit (2005 – £367.0 million) being retained in the business for future growth and investment. At the same time we also generated a record estimated £690 million (2005 – £644 million) in the form of pricing benefit to our members by offering better rates and by charging lower fees and charges than our competitors.

Our funding is primarily from retail members and this year we were particularly successful in the UK retail savings market where we achieved a market share of 12.8% - substantially greater than our par share of 9.2%. In the wholesale funding market, we became the first UK building society to issue a Covered Bond. The €2 billion 10 year transaction gives us access to new global capital market investors.

In a highly competitive mortgage market, we have maintained our focus on prime quality residential loans, achieving net advances of £6.3 billion. The quality of our residential mortgage book remains very high and the incidence of arrears is less than one third of the industry average.

We continued to increase our share of the current account, credit card and personal loan markets. Non-mortgage and savings sales volumes increased by 20%, reflecting our continued focus on expanding the franchise. Overall, total retail sales increased by 12%, evidence of success of our investment programme to improve access to our services for members. We are now two years into the £300 million six-year programme to improve access by phone, post, on-line or through our network of branches and agencies. So far, over 160 branches and over 60 agencies have been refurbished. In February, a new call centre in Wakefield was opened. In addition to this investment in infrastructure, we are investing £100 million over the next five years in our front line employees including recruiting an extra 350 people into our branch network and call centres.

International Financial Reporting Standards

The 2006 results have been prepared using International Financial Reporting Standards (IFRS) for the first time. IFRS differs from UK GAAP which was used in the preparation of the 2005 financial statements. The impact of IFRS on the 2005 financial results was published in a restatement on 22 September 2005 and is available at www.nationwide.co.uk/about_nationwide/results_accounts/.

In the UK retail savings market we achieved a market share of 12.8%

Business Review

CONTINUED

2006 underlying results

As a consequence of the introduction of IFRS, the 2006 balance sheet and income statement are subject to a certain amount of volatility arising from the requirement to fair value derivatives and hedge accounting and the consolidation on a line by line basis of our life insurance business. Where appropriate, certain aspects of the results for 2006 are presented to reflect management's view of the underlying results, to provide a clearer representation of the underlying performance of the Group.

As a result of the IFRS requirement to consolidate the Group's life business on a line by line basis, the income statement includes amounts attributable to policyholders which affect profit before tax, the most significant of which is policyholder tax. Under IFRS, tax on policyholder investment returns is included in the Group's tax charge rather than being offset against the related income. In order to provide a clearer representation of the performance of the Group, these items have been offset in the underlying results.

2005 pro-forma results

Comparative analysis of the results is also complicated as a result of certain IFRS only having been applied from 5 April 2005. This means that the revised IFRS 2005 results only include the impact of certain of the IFRS used in the preparation of the 2006 results. To facilitate comparison and understanding of the 2006 results, 2005 pro-forma comparatives have been prepared. These show how the 2005 results would have looked, where it is possible to determine what the impact would have been, if all the standards had been effective in 2005. However, they do not show the full impact of all the IAS 39 accounting rules as hedges and financial assets to be fair valued were only designated and documented from 5 April 2005.

Management's view is that a comparison of like-for-like 2006 underlying and 2005 pro-forma results provides the best measure of performance. The primary focus of the business review commentary is therefore against these measures.

Profit before tax shown on a reported basis and underlying basis for 2006 and on a reported and pro-forma basis for 2005 are set out as follows:

2006	**As reported £m**	**Adjustments £m**	**Underlying £m**
Net interest income	1,234.3	-	1,234.3
Other income net of claims on insurance contracts	410.3	(8.9)	401.4
Gains from derivatives and hedge accounting	10.9	(10.9)	-
Total income net of claims on insurance contracts	1,655.5	(19.8)	1,635.7
Administrative expenses	873.7	-	873.7
Depreciation and amortisation	117.5	-	117.5
Impairment losses on loans and advances to customers	76.6	-	76.6
Provisions for liabilities and charges	32.1	-	32.1
Impairment gains on investment securities	(3.6)	-	(3.6)
Profit before tax	559.2	(19.8)	539.4

Comparison of like-for-like 2006 underlying and 2005 pro-forma results provides the best measure of performance

Business Review

CONTINUED

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2005	As reported £m	Adjustments £m	Pro-forma £m
Net interest income	1,191.6	(24.2)	1,167.4
Other income net of claims on insurance contracts	357.9	(6.9)	351.0
Total income net of claims on insurance contracts	1,549.5	(31.1)	1,518.4
Administrative expenses	833.2	-	833.2
Depreciation and amortisation	107.1	-	107.1
Impairment losses on loans and advances to customers	46.6	10.0	56.6
Provisions for liabilities and charges	46.7	-	46.7
Impairment losses on investment securities	2.0	5.1	7.1
Profit before tax	513.9	(46.2)	467.7

The adjustments can be analysed as follows:	**2006 £m**	2005 £m
Implementation of IAS 39 and IFRS 4:		
• Effective interest basis		(35.3)
• Impairment losses on investment securities		(5.1)
• Insurance		0.1
• Impairment losses on loans and advances to customers		(10.0)
	-	(50.3)
Gains from derivatives and hedge accounting	**(10.9)**	-
Policyholder tax	**(8.9)**	4.1
	(19.8)	(46.2)

Performance by Business Stream

Nationwide operates three main business streams as follows:

- Personal Financial Services – Mortgages, savings, banking, consumer lending, general insurance, life insurance and investment business.
- Commercial – Commercial lending and Treasury income generation activities together with at.home nationwide limited, the Society's residential letting subsidiary.
- Group – Treasury group operations, capital and items classified as being non-attributable to our core business areas.

The contribution to underlying profit before tax against pro-forma comparatives by each of these business streams is set out in the table below.

	Contribution before tax		
	2006 Underlying £m	2005 Pro-forma £m	Growth %
Personal Financial Services	**270.9**	231.9	16.8
Commercial	**194.2**	160.3	21.1
Group	**74.3**	75.5	(1.6)
	539.4	467.7	15.3

Personal Financial Services (PFS) Business Stream	**2006 Underlying £m**	2005 Pro-forma £m	Growth %
Net interest income	**921.3**	861.3	7.0
Other income	**351.8**	318.7	10.4
Total income	**1,273.1**	1,180.0	7.9
Expenses	**896.2**	844.6	6.1
Impairment and other provisions	**106.0**	103.5	2.4
Contribution from PFS	**270.9**	231.9	16.8

Underlying profit before tax increased by 15.3% to £539.4m
(2005 – pro-forma £467.7m)

Business Review

CONTINUED

The underlying contribution from the PFS business stream increased by 16.8% to £270.9 million which represents just over half of the Group's total contribution. All of the pricing benefit given to our members is delivered through this business stream which reduces its relative contribution. The total number of PFS sales has grown by 12% compared with 2005. Within this we have achieved 20% growth in non-mortgage and savings sales, reflecting our focus on expanding our franchise.

Expenses increased by 6.1% reflecting growth in volumes, particularly in high transaction products such as our current account and credit card. Unsecured loan impairment charges increased to £73.7 million (2005 – pro-forma £53.1 million). Whilst much of the additional charge has arisen from increased volumes in lending, approximately £8 million has arisen from a worsening in rates of delinquency. Secured loan impairment charges are minimal for the current and previous year. Arrears across all products remain significantly better than industry averages. A further provision of £28.5 million for the cost of customer redress relating to all current and estimated future endowment review claims has been raised (2005 – £44.6 million).

Lending

Loans and advances to customers total £101.4 billion of which £86.9 billion (86%) relates to retail lending activity.

The composition of our PFS lending continues to be low risk. At 4 April 2006, 95% of our PFS lending was residential mortgages, 2% was buy to let mortgages, 2% was unsecured personal loans with the balance of 1% lending on overdrafts and credit cards. This mix is not expected to change significantly going forward.

UK residential mortgage market

2005/06 was a year of some recovery in the housing market. Activity levels recovered as borrowers' pessimism about a house price crash evaporated. This latent demand was boosted further by the cut in base rate in August and fed into a modest acceleration in house prices from the autumn. The value of house purchase approvals increased by an estimated 22% compared with last year and reached levels similar to the boom of spring 2004.

Higher house prices helped to swell gross mortgage lending for house purchases, while highly competitive mortgage rates and the maturing of fixed rate products in the autumn helped to support remortgaging, which accounted for an estimated 40% (2005 – 43%) of all mortgage lending. While the value of total market gross advances increased by 9% over the year, strong competition also led to higher redemptions. This dampened net lending, which grew by only around 2.5% over the same period and put increased emphasis on retention strategies.

UK residential mortgages – Nationwide performance

Total gross lending was £21.1 billion (2005 – £23.2 billion), a market share of 7.0% (2005 – 8.4%). Net lending was £6.3 billion (2005 – £10.9 billion). We continued to be highly successful in retaining borrowers and this has made a significant contribution to net lending this year. Our 7.2% market share of principal repaid in the Group was below our mortgage par share of 9.0%. This strong performance was partly driven by our policy of charging between 0.5% to 1% less interest on our standard variable rate mortgage compared with our major competitors as well as having competitively priced fixed and tracker products available to existing borrowers on the same terms as new borrowers. In addition, good service and an active policy of customer contact enabled us to retain borrowers with maturing fixed rate and tracker rate mortgage products.

During the year we have extended the range of options available to our borrowers by including the facility to add reservation fees to the loan balance or to forego the fee completely and pay a slightly higher interest rate. In January, we launched a lifetime tracker product that tracks the Bank of England base rate for up to 40 years. We also introduced a 'switch and fix' facility that gives borrowers confidence when taking out a tracker mortgage that they can switch to one of our fixed rate products at any time without paying early redemption charges.

The profile of our new lending has remained low risk. Based on value, the proportion of lending to first-time buyers has increased to 15% (2005 – 12%). 82% (2005 – 86%) of new lending was in respect of next time buyers, remortgages and on further advances with the borrowers having a proven payment track record. Only 3% (2005 – 2%) was in respect of buy to let.

Loans and advances to customers total **£101.4bn**
of which £86.9bn (86%) relates to retail lending activity

Business Review

CONTINUED

Our prudent lending to creditworthy customers is demonstrated by continuing high asset quality. The average loan to value (LTV) of the residential book has remained broadly constant at 39% and new lending has averaged 55%. The number of Group mortgages 3 or more months in arrears reduced by 10% over the year compared with an increase in the market of 11% (Council of Mortgage Lenders' (CML) figures March 2005 to March 2006). The overall proportion of mortgages 3 or more months in arrears as a proportion of the book is 0.28% (2005 – 0.31%) compared to the March 2006 CML average of 0.97% (March 2005 – 0.87%).

Personal loans

Personal loans are offered through the Society's personal loans subsidiary, Nationwide Trust Limited. Gross unsecured personal loan lending increased by 15.5% to £1.3 billion (2005 – £1.1 billion). Loans are sold through our retail network, over the telephone and via the internet. Nationwide Trust has in excess of 310,000 unsecured personal loan customers, a 14% increase on last year.

The growth has not been at the expense of quality of lending. We continue to maintain prudent lending criteria employing the use of credit scoring, affordability and indebtedness rules as part of our assessment of whether to lend or not. This process results in approximately one in every two unsecured loan applications received being rejected. Most of our borrowers are 'known to Nationwide' with over 75% already being members or customers of the Group.

In line with industry wide credit experience, we have seen increases in the impairment charge on our personal loan book. However, continuing high levels of asset quality are demonstrated by the ratio of the value of loans 30 days or more in arrears as a percentage of the total book being 4.6% (2005 – 4.1%), around 40% lower than the average for members of the Finance and Leasing Association.

Savings and investments

UK savings and investments market

The market for UK retail funds has intensified in the year with lenders looking to fund more of their lending from retail savers. There has also been stronger competition from savings only competitors and increased fundraising by National Savings to support Government spending.

UK savings and investments market – Nationwide performance

Despite this continued competition, we achieved a 12.8% (2005 – 11.1%) share of the overall increase in UK retail savings, representing £8.3 billion (2005 – £6.7 billion). This compared favourably with a par share of 9.2%. Total retail member deposits as at 4 April 2006 amounted to £80.9 billion (2005 – £72.6 billion) and represent our primary source of funding. We have consolidated our position as the second largest savings provider in the UK with Nationwide's savings accounts, on average, 0.4% better priced than those of our competitors.

Strong savings flows were primarily driven by our e-Savings and Individual Savings Accounts (ISAs) products which in aggregate generated £5.4 billion (2005 - £5.0 billion) of net receipts. The Society again launched a number of highly competitive bonds throughout the year. A major product innovation was the Monthly Income 65+ launched in July, an account designed specifically for the over 65s. Since its launch in July 2005, around 80,000 accounts have been opened with over £1.7 billion attracted.

The Society, through its wholly owned subsidiary Nationwide Unit Trust Managers Limited (NUTM), writes a range of investment contracts including unit trusts and ISAs. At 4 April 2006 our range of unit trust investment products held by our customers had a market value of over £2.5 billion (2005 – £2.0 billion). Following last year's re-launch of its range of investments, abolishing initial charges and introducing a £20 minimum monthly investment, NUTM has recorded 94,000 sales (excluding Child Trust Funds) (2005 – 61,000). Nationwide continues to be one of only a handful of national high street providers to offer the choice of an equity or cash based Child Trust Fund with over 103,000 equity applications received since launch.

Banking

Current accounts

The Society's current account, the 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 a market leading rate of up to 4.25% credit interest and no charge for overseas transactions. More than 48% of FlexAccount customers now regularly use our internet banking service, (2005 – 25%) and over 2.4 million members are registered to use Nationwide's online banking service.

In August we launched a Telephone Self Service banking facility, giving our current account customers a fully automated facility to carry out transactions. The service uses the latest speech recognition technology supported by traditional 'touch tone' functions to allow customers to access their account anytime, anywhere. So far, over 50,000 members have registered for the service.

The FlexAccount is a highly competitive account with a range of good value features

Business Review

CONTINUED

The total number of Nationwide current accounts is now in excess of 3.6 million. Our market share of new accounts is estimated at nearly 11% (based on CACI's Current Account and Savings Market Database).

Credit cards

The Society continues to differentiate its credit card from others on offer in the UK by not charging for international use and by allocating payments to clear the most expensive debt first. Growth in the credit card market has been largely unchanged year on year with market gross lending in 2006 only 1% lower than in 2005. The market has been moving away from large bonus cash reward and free balance transfers as these products have become unprofitable for suppliers. In response, Nationwide repositioned the portfolio by launching new introductory terms for the classic card and closing the cash reward card to new business.

Despite this slowing market in the year we issued 252,000 new credit card accounts (2005 – 217,000) taking total accounts up to 974,000 (2005 – 796,000) and total cards in issue to 1,222,000 (2005 – 1,054,000). Balances outstanding on credit cards at the year end amounted to £670 million (2005 – £567 million).

As with personal loans, there has been an increase in the impairment charge in line with industry wide credit experience. However, asset quality compared with the industry remains very favourable with the value of 30 days or more in arrears as a percentage of the book being 6.9% (2005 – 6.4%). We are around 30% lower than the average for APACS (Association for Payment Clearing Services) members.

General insurance

During the year, over 322,000 (2005 – 431,000) general insurance covers were sold and the book stood at over 1.5 million (2005 – 1.6 million) covers at the year end. The primary general insurance products we sell are buildings and contents insurance, payment protection policies, motor insurance, travel insurance and personal accident insurance. Sales of general insurance products are often linked to mortgage sales. The reduction in the number of general insurance covers sold in the year reflects the lower volume of mortgage sales experienced this year.

We have continued to use leading insurers as third-party underwriters and the commission and profit share we receive is an important source of non-interest income. Despite the reduction in covers sold we still earned a consistent £119 million (2005 – £119 million) from commission and profit share during the year.

On 1 December 2005, Nationwide launched annual travel insurance for the over 65 market. The policy covers Europe and where other high street banks are able to offer this product it is priced competitively in comparison. Having re-entered the market, take-up has been positive and feedback from members has been complimentary. We will continue to look for product gaps and ways of making our existing products more attractive.

Life assurance

The Society, through its wholly owned subsidiary, Nationwide Life Limited (NL), writes a range of investment and protection products. These include two types of insurance product: term life assurance and critical illness cover. 65,000 life policies were sold during the year (2005 – 74,000 policies). As with general insurance covers, this lower volume of life policies stems from the lower volume of mortgages issued this year. NL also provides pension contracts and Guaranteed Equity Bonds. Nationwide's guaranteed equity bond was improved and re-launched in September 2005; the new offer has improved sales by around 36%.

Pricing benefit

The estimated pricing benefit is calculated by comparing the price of each of our products (including interest rates, fees and charges) with the equivalent products of our main competitors. During the year we generated an estimated £690 million (2005 – £644 million) in the form of pricing benefit to our members by offering better rates and by charging lower fees and charges than our competitors. Benefit generated over the year for mortgage borrowers has now come into line with that generated for savers. This reflects the increasing proportion of competitively priced fixed rate and tracker rate mortgages. Pricing benefit is distributed to members as follows:

On 1 December 2005, Nationwide launched annual travel insurance for the over 65 market

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> > > Pricing benefit distributed to members

	2006		2005	
	£m	**%**	£m	%
Benefit to mortgage borrowers	**252**	**37**	216	34
Benefit to savers	**251**	**36**	259	40
Benefit to members with other products	**187**	**27**	169	26
	690	**100**	644	100

Distribution channels

We are continuing the £300 million, six year investment programme announced in 2004 to develop a modern business and to ensure that our branch, telephones and other access channels are maintained at the modern standards expected by our members. This programme is going very well with over 160 branches refurbished or re-sited since its inception, investment in our agency network is well underway and a number of technology investments have already been successfully deployed. To allow our customers to do business, when and how they wish, we have continued our investment in UK call centres with a new facility in Wakefield which opened in February 2006. All of our call centres remain in the UK. In addition to the investment in physical infrastructure we will also be investing £100 million over the next 5 years in our front line employees. As well as recruiting an extra 350 people into our branch network and call centres and creating over 1,000 opportunities for promotion, we are strengthening our management structure and providing additional sales coaching and compliance management.

Commercial Business Stream

	2006 Underlying £m	2005 Pro-forma £m	Growth %
Net interest income	**199.6**	186.7	6.9
Other income	**37.3**	22.9	63.0
Total income	**236.9**	209.6	13.0
Expenses	**43.6**	42.4	2.8
Impairment and other provisions	**(0.9)**	6.9	(113.0)
Contribution from Commercial	**194.2**	160.3	21.1

The underlying contribution from the Commercial business stream increased by 21.1% to a record £194.2 million. This represents around 35% of the Group's total contribution in both years, an impressive performance given that assets account for only 15% of the Group's total. The book continues to be high quality, with record levels of gross lending achieved in the year. This was achieved against a background of further competition which continues to increase pressure on margins. Underlying contribution from investment assets held by Treasury was £29.8 million (2005 – £9.0 million) an increase of 230%. This increase arises from additional investment return in the current year and an impairment gain as compared with a charge last year. The contribution from at.home nationwide was £13.1 million (2005 – pro-forma £4.6 million), an increase of 185% on the previous year. This increase primarily arises from revaluation gains in the current year as compared with losses last year.

Commercial lending

Commercial lending is a significant part of our business and of our total loans and advances to customers of £101.4 billion, £14.5 billion (14%) is in respect of commercial lending.

The composition of our commercial portfolio at 4 April 2006 was 33% to UK Registered Social Landlords, 6% to

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support Private Finance Initiatives and the balance of 61% secured on other commercial property. Loans to Registered Social Landlords are secured on residential property. Loans advanced under Private Finance Initiatives are secured on cash flows from Government backed contracts. Commercial property loans are fully secured against properties supported by strong cash flows and tenant covenants. In addition, loans are well diversified by industry type and geographic location. There is no speculative lending and no development finance. In terms of counterparty concentration, the largest single borrower represents only 2.0% of the total commercial book.

We remain the lender with the largest volume of funding commitments to Registered Social Landlords. Whilst there have been fewer transfers of municipal housing stock from local authorities this year, there have been several refinancings and increases in borrowing as Registered Social Landlords merge in response to government initiatives to increase efficiency.

Gross commercial lending in the year totalled £5.5 billion (2005 – £4.3 billion) representing an increase of 27.8% with balances outstanding of £14.5 billion (2005 – £12.7 billion). Redemptions have been contained at the level seen last year. Net lending of £1.8 billion constitutes a record performance.

Asset quality remains strong. Commercial lending arrears levels of 3 months or more have improved year on year from 79 to 69 cases.

at.home nationwide

at.home is the Society's residential letting subsidiary. The subsidiary represents a non-core, non strategic activity and it has been decided to dispose of the business. The Society has been in exclusive negotiation for the sale of the at.home property portfolio and contracts were exchanged for sale on 15 May 2006. The disposal will not have a material impact on the income statement or balance sheet of the Group.

Group Business Stream

	2006 Underlying £m	2005 Pro-forma £m	Growth %
Net interest income	**113.4**	119.4	(5.0)
Other income	**12.3**	9.4	30.9
Total income	**125.7**	128.8	(2.4)
Expenses	**51.4**	53.3	(3.6)
Contribution from Group	**74.3**	75.5	(1.6)

Contribution from the Group business stream was £74.3 million (2005 – £75.5 million) a decrease of 1.6%. The contribution from this business stream includes the contribution derived from capital held for regulatory purposes in excess of that allocated to other business streams, on the basis of an economic capital assessment, together with other elements of contribution that cannot be allocated directly to business streams. It also includes contribution from the Group's Treasury operations, excluding the contribution from assets held solely for investment purposes which is included in the contribution from the Commercial business stream.

Liquidity

Liquidity balances totalled £14.7 billion at 4 April 2006 (2005 – £15.3 billion) representing a prudential liquidity ratio of 10.0% (2005 –11.5%). Prudential liquidity has been managed down in the year to improve the efficiency of the balance sheet. We continue to have no exposure to emerging markets. 96% of our Treasury investment portfolio comprised assets which are rated single A or better.

Wholesale funding

Total wholesale funding decreased by £0.7 billion. At 4 April 2006, wholesale balances stood at £29.2 billion (2005 – £29.9 billion) representing a funding ratio of 26.6% (2005 – 28.6%). This is one of the lowest levels of wholesale funding of organisations of comparable size and provides significant headroom for additional funding in the future in addition to our retail deposit taking activities.

During the year, we successfully executed our inaugural covered bond to further broaden our global investor base.

We continue to have no exposure to emerging markets. 96% of our Treasury investment portfolio comprised assets which are rated single A or better

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>>> The €2 billion issue was the first by a UK building society. We were pleased that Nationwide was recognised for the success of this transaction by being awarded 'Best Covered Bond Deal of the Year' by *Euroweek* magazine. The Society has continued to enjoy a strong appetite from wholesale funding investors and has operated successful Medium Term Note (MTN) programmes in the Dollar, Euro and Sterling markets. During the year, we transacted a £500 million 5 year Sterling issue on the EMTN programme with strong demand from our UK investor base. The funding programmes have been updated, so that the EMTN and US MTN programmes are fully compliant with the new EU Prospective Directive.

Our short and medium term credit ratings from the major rating agencies have remained stable during the year. They are as follows:

	Short term	Long term
Fitch IBCA	F1+	AA-
Moody's	P-1	Aa3
S&P	A-1	A+

Performance by Income Statement Category

Profit

A summary income statement on an underlying and pro-forma basis is as follows:

	2006 Underlying £m	2005 Pro-forma £m	Growth %
Net interest income	**1,234.3**	1,167.4	5.7
Other income	**401.4**	351.0	14.4
Total income	**1,635.7**	1,518.4	7.7
Expenses	**991.2**	940.3	5.4
Impairment and other provisions	**105.1**	110.4	(4.8)
Profit before tax	**539.4**	467.7	15.3

The Group has seen a strong growth in underlying profit before tax of 15.3% to £539.4 million compared with 2005 pro-forma results. The increase in profit was consistent with our strategy of retaining sufficient profit to allow continued investment in the business and to support its future growth.

On a reported basis, profit before tax has increased 8.8% to £559.2 million from £513.9 million. However, the reported 2006 profit includes fair value gains from derivatives and hedge accounting (£10.9 million) and policyholder tax (£8.9 million) and the reported 2005 comparative does not include the impact of some of the IFRS standards (IAS 32, IAS 39 and IFRS 4) that are only applied from 5 April 2005. Management's view is that a comparison of like-for-like 2006 underlying and 2005 pro-forma results provide the best measure of performance. A reconciliation from reported to underlying and pro-forma pre-tax profit is included on pages 7 and 8.

Net interest income

Net interest income is earned on a combination of our PFS and Commercial products together with interest income from activity within Treasury.

Net interest income increased by 5.7% to £1,234.3 million in the year compared with 2005 pro-forma results. Effective margin management throughout the year has maintained the net interest margin at 1.06%, a reduction of only 3 basis points from last year.

Throughout the current year we have had a LIBOR denominated net asset exposure of approximately £20 billion which benefited from LIBOR being an average of 9 basis points higher than base rate. This differential was 15 basis points lower than last year and its impact represented 2 of the 3 basis points reduction in the net interest margin.

Other income

Other income primarily comprises income earned from the sale and manufacture of insurance products together with administration fees not included within interest margin. During the year underlying other income increased by 14.4% to £401.4 million compared with 2005 pro-forma results reflecting our strong general insurance book and continued focus on banking products and personal loans.

The €2bn covered bond issue was the first by a UK building society

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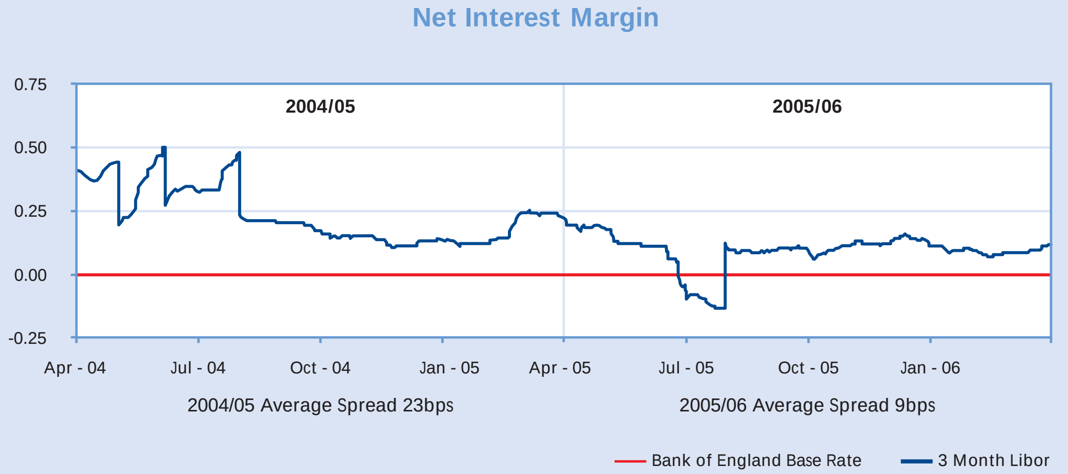

Expenses	2006 £m	2005 £m
Employee costs:		
• Wages and salaries	**348.7**	341.9
• Social security costs	**29.6**	29.6
• Pension costs – defined benefit plans	**81.1**	76.2
	459.4	447.7
Other administrative expenses	**414.3**	385.5
Depreciation and amortisation	**117.5**	107.1
	991.2	940.3

Total expenses amounted to £991.2 million representing an increase of 5.4% over 2005. This increase compares with an increase in assets of around 8% over the year and a rise in underlying total income of 7.7%. As a result our cost to mean total asset ratio improved for the 17th successive year to 0.85% (2005 – pro-forma 0.88%) and the underlying cost to income ratio, one of our principal measures of efficiency, improved to 60.6% (2005 – pro-forma 61.9%).

Total expenses include increased costs arising from the continued investment in our customer service improvement programme. During the year we opened our fifth UK regional call centre in Wakefield and have continued with our extensive branch refurbishment programme. We have also announced a £100 million investment in our people ensuring that an additional 350 employees will be available to serve our customers in our branches and call centres. Whilst increasing costs in the current year, these initiatives will continue to improve our retailing capacity and ensure continued future income growth.

Impairment losses on loans and advances	2006 £m	2005 Pro-forma £m	Growth %
Secured lending	**2.9**	3.5	(17.1)
Unsecured lending	**73.7**	53.1	38.8
Customer redress	**32.1**	46.7	(31.3)
Treasury investments	**(3.6)**	7.1	(150.7)
	105.1	110.4	(4.8)

Underlying cost to income ratio improved to 60.6% (2005 - pro-forma 61.9%)

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>>> Our high quality lending policy has again resulted in a minimal impairment charge arising from secured lending.

In line with other lenders we have experienced an increase in the impairment charge for unsecured lending products. Whilst much of the additional charge has arisen from increased volumes in lending, approximately £8 million has arisen from a worsening in rates of delinquency. However, our levels of arrears remain significantly lower than industry averages for all unsecured products.

The charge from customer redress primarily relates to the estimated cost of all current and estimated future endowment review claims.

Following an improvement in the credit quality of a particular treasury investment security, an impairment gain has been recognised resulting in a £3.6 million credit from treasury investments.

Taxation

The effective rate of tax was 29.0% (2005 – 28.6%) compared with the standard rate of corporation tax of 30%. Under IFRS, the tax charge in respect of the life assurance subsidiary is included on an actual basis rather than using the 30% ‘gross up’ permitted under UK GAAP. Stripping out the life assurance subsidiary, the effective rate of tax was 27.9% (2005 – 29.2%).

Gains from derivatives and hedge accounting

Following the introduction of IFRS all derivatives entered into by Nationwide, which under UK GAAP were held off balance sheet, are now recorded on the balance sheet at fair value with any fair value movements being taken to the income statement. Derivatives are only used to limit the extent to which the Group will be affected by changes in interest rates, exchange rates or other factors specified in building society legislation. Derivatives are therefore used exclusively to hedge risk exposures and are not used for speculative purposes.

Where effective hedge accounting relationships can be established, the movement in the fair value of the derivative instrument is offset in full or in part by opposite movements in fair value of the underlying asset or liability being hedged. Any ineffectiveness arising from different movements in fair value will trend to zero over time so any recorded ineffectiveness is excluded from underlying results in that accounting period.

In addition, we enter into certain derivative contracts which, although efficient economically, cannot be included in effective hedge accounting relationships. Consequently, although the implicit interest cost of the underlying instrument and associated derivatives are included in ‘Net interest income’ in the income statement, fair value movements on such derivatives are included in ‘Gains from derivatives and hedge accounting’. These fair value movements are therefore also excluded from underlying results as they will not be realised in cash terms.

Accordingly £10.9 million gains from derivatives and hedge accounting has been deducted to arrive at underlying profit. In future periods if net losses are recorded these will similarly be added in calculating underlying profit.

Our levels of arrears remain significantly lower than industry averages for all unsecured products

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Capital Structure

Regulatory capital stood at £7.0 billion (2005 – £6.6 billion) with the Group's total solvency ratio remaining strong at 11.0% (5 April 2005 – 11.1%). The Tier 1 solvency ratio stood at 8.8% (5 April 2005 – 8.8%). Both ratios remain well in excess of the minimum established by the Society's regulator.

	2006 **£m**	2005 (note i) £m
Tier 1		
General reserve	**4,825.6**	4,432.7
Permanent interest bearing shares (note ii)	**700.0**	700.0
Pension fund deficit add back (note iii)	**126.0**	113.0
Intangible assets	**(80.5)**	(44.2)
	5,571.1	5,201.5
Tier 2		
Revaluation reserve	**117.0**	103.0
Subordinated debt (note ii)	**1,484.0**	1,446.9
Collective impairment allowance	**145.2**	134.9
	1,746.2	1,684.8
Deductions	**333.7**	309.1
Total capital	**6,983.6**	6,577.2
Risk weighted assets (£bn)	**63.6**	59.1
Tier 1 ratio (%)	**8.8**	8.8
Total capital (%)	**11.0**	11.1
Tier 2 to Tier 1 ratio (%)	**31.3**	32.4

Notes

(i) The comparative information is at 5 April 2005 to incorporate the impact of IAS 32, IAS 39 and IFRS 4.

(ii) Permanent interest bearing shares and subordinated debt exclude any fair value adjustments arising from micro hedging that are included in the consolidated balance sheet.

(iii) The regulatory capital rules allow the pension fund deficit to be added back to regulatory capital and a deduction taken instead for an estimate of the additional contributions to be made in the next 5 years, less associated deferred tax.

Regulatory capital stood at £7.0 bn (2005 – £6.6bn) with the Group's total solvency ratio remaining strong at 11.0% (5 April 2005 – 11.1%)

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>>> Nationwide continued to make progress on its preparations for Basel II. A notable achievement last year was the submission of the waiver application to the FSA in December 2005 within the first wave of applicants. The waiver seeks permission to use the Internal Ratings Based approach to credit risk on all our major portfolios. Given the quality and composition of our business, the Internal Ratings Based approach offers us a potential reduction in our regulatory capital requirement. Basel II is scheduled to commence with effect from 1 January 2007.

Pension Fund (Retirement Benefit Obligations)

The majority of Group employees are members of the Nationwide Pension Fund ('the Fund'). The Group operates both Final Salary and Career Average Revalued Earnings (CARE) defined benefit arrangements.

The valuation of the Fund at 31 March 2006 resulted in a deficit of £283.6 million (2005 – £342.6 million) using the methodology set out in IAS 19. Our total retirement benefit liability under IAS 19, including other schemes, is £294.2 million (2005 – £351.6 million). On an actuarial basis the Fund deficit is estimated at around £100 million (2005 – £230 million). We have been actively managing this deficit and have taken a number of steps to contain and reduce the deficit over time:

- Final Salary arrangements closed to new members since December 2001
- Employee contributions (final salary arrangements) increased from 5% to 6½% (7% from 1 July 2006)

- A series of three special contributions of £50 million to be paid in the period 2005/06 – 2006/07
- The Fund's Trustees have worked closely with their advisors to optimise the investment strategy for the Fund's assets.

We will continue to review our options to manage the Fund in a timely and responsible way such that the deficit is reduced to a neutral position over the next ten years.

Outlook

The economy throughout 2005/06 was relatively benign, with a slight rise in unemployment and weak consumer spending. As a result, interest rates remained low and relatively stable throughout the year. We expect conditions to improve during 2006, although threats to consumer spending such as oil prices and utility bills are expected to result in interest rates continuing to remain relatively low.

We expect UK gross residential lending in 2006/07 to be slightly higher than 2005/06 at around £306 billion. This will be driven mainly by a more buoyant housing purchase market, with remortgage activity largely unchanged.

Throughout the year we have continued to comment on the state of the UK housing market by monthly publication of our House Price Index. Prices in 2005 increased by 3%, and we expect a similar rise in 2006. We expect the strong start to the housing market for 2006/07 to moderate somewhat as high prices and stretched affordability of first-time buyers reduces demand towards historic trends.

Our monthly Consumer Confidence Index was formally launched in August 2005, measuring consumer views on their current and expected future situations. Expectations form an important element in decision making and the results indicate some pessimism about future prospects for consumer spending. This is likely to constrain the growth in both personal loan and credit card markets, where we expect net lending to be slightly lower than 2005/06 at around £9 billion and £4 billion respectively.

Our core markets have seen fierce competition throughout 2005/06. We expect this to continue in 2006/07 as lenders seek to protect their market shares, with a continued squeeze on retail margins. With a strong opening pipeline of business and an excellent track record on retention, we expect to deliver mortgage asset growth in line with our par share of 9%, funded with a cost effective mix of retail and wholesale funds.

Our asset growth will be dominated by good quality prime residential mortgages. Although the extremely benign credit conditions of the last few years are unlikely to continue, we do not expect them to deteriorate significantly.

Our asset growth will be dominated by good quality prime residential mortgages

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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. In particular we are reviewing a number of initiatives to improve our capacity and capability to reduce overall cost and improve income. This should lead to the delivery of increased profits while maintaining the distribution of substantial pricing benefits to our members.

Risk Management and Control

Overview

Nationwide seeks to manage appropriately all the risks that arise from its activities. The principal risks inherent within our business are credit risk, market risk, liquidity risk and operational risk. In addition, insurance risk arises within our life insurance subsidiary.

We have a formal structure for managing these risks within the Group. This structure consists of three key elements:

Firstly, we have documented our approach to the management of risk in our risk appetite statement and in our detailed risk policy statements. These statements cover all of the risks mentioned above and they are reviewed annually by the management committees mentioned below and, in the case of the risk appetite statement, by the Board. Risk appetite is implemented through risk limits and the allocation of economic capital.

Secondly, we have well established risk functions within the Group. These functions sit within our Risk Management Division. The role of these functions is to set limits which are consistent with our risk appetite, to monitor and report on compliance with those limits and generally to provide an oversight role in relation to the management of risk. However, prime responsibility for managing risk, and for ensuring controls are put in place in respect of risk, lies with the business units within the Group. This division of responsibility is in accordance with best practice recognised within the industry and by our regulator, the FSA.

Finally, we have a committee structure which supports the management of risk within the Group. There are four key management committees with risk responsibilities:

- Credit Committee (Retail) and Credit Committee (Treasury and Commercial), which have responsibility for credit risk
- Assets and Liabilities Committee (ALCO), which has responsibility for market and liquidity risk
- Chief Executive's Committee, which has responsibility for operational risk.

Insurance risk is managed by the board of our life insurance subsidiary. All of the management committees

mentioned above, and the board of our life company, includes appropriate representation from amongst our executive and divisional directors, as well as from our risk functions. In addition to these committees, oversight of the risk management framework and control systems is provided by the Audit Committee on behalf of the Board.

Credit Risk

Credit risk is the risk that a customer or counterparty will fail to meet their obligations to us as they become due. Credit risk arises primarily from loans and other credit based products (such as current account facilities and credit cards) available to our retail customers, loans to our commercial customers and from the liquid and investment assets held by our Treasury Division.

Retail credit risk is managed centrally from within the Retail Credit Risk function in Risk Management Division. We have sought to distance the credit decision from our sales force and to make these decisions within the central team. We have accomplished this by developing and maintaining automated decision systems that differentiate credit risks for residential mortgage loans and other consumer products and services. A specialist retail underwriting unit considers those loan applications which require individual underwriting, but this unit sits within Risk Management Division, not within the sales force. The policy in respect of retail credit risk is maintained by the Retail Credit Risk function and is set by the Credit Committee (Retail). This committee receives regular reports from Retail Credit Risk on the performance of all retail credit portfolios.

We have sought to distance the credit decision from our sales force and to make these decisions within the central team

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Commercial credit risk is managed by our Commercial Division, which is responsible for all commercial lending activities, and the Commercial Credit Risk function within Risk Management Division. The Commercial Credit Risk team underwrite all new loans and monitor existing loans. Loans above certain levels also require approval from the Credit Committee (Commercial and Treasury) or from our Large Exposures Approval Committee, which is a committee of the Board. The Commercial Credit Risk team also maintain the policy and limits in respect of commercial credit risk and monitor compliance with the limits, providing reports to the Credit Committee (Commercial and Treasury) on performance of the commercial portfolios.

Credit risk within our Treasury Division arises from the investments held by Treasury in order to meet our liquidity requirements and for general business purposes. This aspect of credit risk is managed by Treasury Division and the Treasury Credit Risk function within Risk Management Division. The Treasury Credit Risk team underwrite all new facilities and monitor existing facilities. They also set and monitor compliance with policy and limits, reporting to the Credit Committee (Commercial and Treasury) in the same way as the Commercial Credit Risk function does in relation to commercial credit risk.

Market Risk

Market risk is the risk that the value of, or income arising from, the Group's assets and liabilities changes as a result of changes in interest rates or exchange rates. Market risk incorporates a range of risks, but the principal elements are interest rate risk and foreign currency risk.

Interest rate risk arises from the mortgage, savings and other financial services products that we offer. The varying interest rate features and maturities on these products, and the use of wholesale funds to support these products, create interest rate risk exposures due to the imperfect matching of interest rates between different financial instruments and the timing differences on the re-pricing of assets and liabilities. This risk is managed through the use of appropriate financial instruments, including derivatives.

Foreign currency risk arises as a result of activity undertaken by the Group when raising and investing funds in currencies other than Sterling, which is done in order to manage wholesale funding costs and the returns on liquid assets and to provide diversity in funding and investment markets. Currency risk is managed primarily through the use of currency swaps and forward foreign exchange contracts. The risk is also managed, where appropriate, by

Interest rate risk is managed through the use of appropriate financial instruments, including derivatives

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foreign exchange currency liabilities being matched with assets denominated in the same foreign currency.

Treasury Division is responsible for managing our exposure to all aspects of market risk within the operational limits set out in the Group's market risk policies. Oversight is provided by the Market Risk team within the Risk Management Division and by the ALCO, which includes representation from the Treasury Division and the Risk Management Division. ALCO approves the market risk policy and receives regular reports on all aspects of market risk, including interest rate risk and foreign currency risk.

Our Treasury Division uses derivative instruments in managing various aspects of market risk. However, in doing so it complies with the Building Societies Act 1986 which limits our use of derivatives to the management of changes in interest rates, exchange rates or other factors defined by the Act.

Liquidity Risk

Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due, or can do so only at excessive cost. The objective of our liquidity policy is therefore to enable us to maintain sufficient liquid assets to cover cash flow imbalances and fluctuations in funding, to maintain full public confidence in our business and to enable us to meet all our financial obligations.

The day-to-day management of liquidity is the responsibility of the Treasury Division, which manages our portfolio of liquid assets and our contingency funding plans. Our liquidity risk policy is monitored by ALCO, which receives regular reports on our liquidity position, and the Market Risk team within the Risk Management Division. We also comply with regulatory guidelines which govern the scope and nature of the Group's holdings of liquid assets.

Operational Risk

Operational risk is the risk of a loss arising from inadequate or failed internal processes or systems, human error or external events. For the purposes of managing operational risk, we divide it into a number of discrete areas of risk which include, for example, process management, systems failure and fraud risk.

We manage operational risk through the Group's business units, with senior management having responsibility for understanding how operational risk impacts on their business unit and for putting in place the appropriate controls or other mitigation actions, for example, insurance. The business units are supported by a central Operational Risk and Controls team within the Risk Management Division, which co-ordinates activity across a network of operational risk officers who work within the business units.

Our Chief Executive's Committee, which is our principal management committee, has responsibility for operational risk and receives a monthly report on the Group's operational risk profile.

Graham Beale
Group Finance Director
17 May 2006

The day-to-day management of liquidity is the responsibility of the Treasury Division, which manages our portfolio of liquid assets and our contingency funding plans

Community and Environmental Affairs

Introduction

The Community and Environmental Affairs team at Nationwide works to support the communities in which we operate and to manage our approach to sustainability. For us, this entails operating and growing the business in such a way as to meet the needs of the present whilst conserving resources for future generations. It is based on our core values of fairness, honesty, integrity and transparency.

Sustainability is widely considered to have three elements: economic (or financial), social and environmental. For Nationwide, economic considerations are important in order to ensure that we have a sustainable business for our members and employees. As an integral part of our stance on mutuality, we play a strong and active role in supporting communities across the UK. Nationwide is not a major polluter and strong financial performance enables us to play an important role in protecting the environment.

It also allows us to make appropriate fiscal contributions and during the year we paid taxes in excess of £750m on behalf of the Nationwide Group, employees and members.

Further details of our economic policies, objectives and performance can be found elsewhere in this Annual Report and Accounts.

Governance and accountability

Our Sustainability Committee, chaired by Deputy Chief Executive Bernard Simpson, meets quarterly to review strategy and activities. The Committee is made up of senior managers from across the business.

Co-ordination of management activities is the responsibility of the Head of our Community and Environmental Affairs department. The Community and Environmental Affairs team strives to ensure that Nationwide makes an active contribution and positive impact upon the communities and environments in which it operates. Our employees are also encouraged to take personal responsibility to create a more sustainable Society.

A Sustainability Improvement Group ensures that the most significant social and environmental issues are managed across the business. The Group focuses on our three most significant sustainability impacts: energy, transport and waste.

Sustainability strategy

In September 2005, our Board approved a strategy which acknowledged that generally we perform well in social areas but need to make further progress in terms of the environment, especially given the increasing risks in connection with climate change. We will be doing more work to enable us to quantify the impact of sustainability on our business activities. Key initiatives that have been agreed are to:

- develop and publicise numerical performance targets;
- build sustainability more fully into the corporate purchasing process;
- examine the case for launching an ethical investment product;
- review Treasury investment criteria in terms of social and environmental responsibility.

BITC Corporate Responsibility Index 2005

In our second submission to the Business in the Community Corporate Responsibility Index in 2005 we improved our ranking from 74th to 68th in the Top 100 Companies that Count. This confirmed that in some areas, such as employee policies and practices, we are performing

As an integral part of our stance on mutuality, we pay a strong and active role in supporting communities across the UK

Community and Environmental Affairs

CONTINUED

strongly but in others we had room for improvement. For instance, we need to publicly report on performance against targets. We will ensure that we continue to improve our audit and assurance processes and engage more comprehensively with all stakeholders.

Reporting

Our *Better Society* report sets out our approach to our members, employees, communities, the environment and our partners. It also details our performance in these areas, shows our targets for improvements and identifies the challenges that we face. Further information can be found on our Better Society website, at www.nationwide.co.uk/bettersociety.

Diversity

We are committed to promoting a supportive and inclusive culture for all our employees, members and business partners. We seek to harness the strengths and talents of each of our employees to create a productive workforce that puts members first and which generates ever greater value for them. Diversity is important to business plans throughout Nationwide, and increased awareness of it helps maximise productivity and value.

We strive for equal opportunities at all levels of our business and we encourage employee diversity in order to eliminate discrimination and to reflect and understand the communities in which we operate. This is supported by our Diversity and Equality of Opportunity Committee (DEOC) chaired by our Deputy Chief Executive and comprised of senior managers from across the business and the General Secretary of the Nationwide Group Staff Union. The DEOC is responsible for developing actions relating to diversity and taking them forward as part of their business plans.

These include:

- identifying ways of overcoming barriers to better diversity, as well as setting clear and measurable goals for doing so;
- evaluating the workforce with external benchmarking data and recommending changes as necessary;
- maintaining action plans, best practice bulletins and case studies on the diversity intranet site according to an agreed communications strategy;
- sponsoring the Disability Action Group which leads our discussions on disability issues for members and employees.

We work closely with Business in the Community's Race for Opportunity programme, which works to reap the business benefits of an effective diversity action plan in the fields of employment, marketing to ethnic minorities, ethnic minority small businesses, and community involvement programmes. In 2005 we achieved Gold status in their national benchmarking survey and were included in the 'Most Improved' category.

We are also a member of the Employers' Forum on Disability, which focuses on disability in the workplace. It is funded and managed by employers and has over 375 members. The Forum is recognised as the authoritative voice on disability and works closely with Government and other stakeholders, sharing best practice to make it easier to employ disabled people and to serve disabled customers.

Employee commitment

We also look carefully at how we engage with our employees and whether their commitment impacts positively upon our members. Over the last three years we have established, through our Viewpoint employee survey, that satisfaction with leadership, reward and recognition, training and development and resourcing all play a key part in driving-up employee engagement, as does alignment with our corporate values, PRIDE.

The relationship between employee commitment, customer advocacy and business performance has been quantified in our "service profit chain" research which we call Project Genome.

In addition to conducting our own research in this area, we also collaborate with the University of Bath, which has established that our employees' opinions on sustainability and fairness (both internal and external) have a major positive impact on their commitment. Research will continue over the course of the coming year to enable us to have a better understanding of this relationship.

We are committed to promoting a supportive and inclusive culture for all our employees, members and business partners

Community and Environmental Affairs

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Community

We have over 150 years' experience of working in positive partnership with the community. Our commitment today remains as strong as ever. With over 11 million members and over 16,000 employees, we have a physical presence in almost 1,000 locations across the UK. To reinforce our commitment to this local presence, we go to great lengths to ensure that our community activities reach every corner of the UK, are relevant to our members, to our employees and to the communities in which they take place.

We focus very clearly on projects which are of lasting benefit, which involve the broadest possible cross-section of the community and which help the most marginalised communities in the UK.

Highlights in 2005/06 include:

- a £1 million partnership deal with Disability Sport Events (DSE) building on a successful five year relationship, which will help with talent identification and team selection in the run-up to the 2008 and 2012 Paralympics in Beijing and London. As part of our aim of achieving one million votes at this year's Annual General Meeting, the Society will donate 10p to DSE for every vote cast, up to a total of £100,000;
- our annual World's Biggest Coffee Morning fundraising event in support of Macmillan Cancer Support raised over £16,000 in 2005. Macmillan has been our flagship charity for over 12 years and we have raised over £4 million for people living with cancer;
- through our Cats' Eyes for Kids campaign, we have contributed to a 43% reduction in UK child pedestrian casualties by donating over 10 million branded reflectors to primary school pupils and providing supporting information to 25,000 UK schools. By wearing a reflector, a child pedestrian can be visible at 150 metres with low beam headlights compared to only 30 metres without one;
- recognising around 12,000 individuals and groups engaged in community volunteering via our Nationwide Awards for Voluntary Endeavour.

Our employees are generous with their time and respond magnificently to appeals of all kinds. Nationwide employees donated almost £15,000 to the Tsunami appeal through payroll giving – adding to the extraordinary £2.4 million donated by members and the public through our branches.

Employees can recognise their colleagues' contributions by nominating them for our Community and Environment Awards, held twice a year.

Environment

Everything we do leads to environmental impacts – from our internal operations to our products and services. We have been working to improve our understanding and measurement of these impacts and how we consider them in decision-making. Wherever possible we are working to reduce the negative impacts whilst delivering our business objectives.

To help us to do this, we have developed an Environmental Management System (EMS) that covers our core business operations. Using the EMS, we have identified our three most significant environmental impacts and their causes:

- climate change due to emissions from energy and transport use;
- resource use from consumption of paper and other consumables, such as building materials;
- generation of waste from office activities and catering.

We also consider the impact of our water use and our impact on biodiversity from our use of land, although these are less significant issues.

Renewable energy

In October 2005 we entered into a one year contract to buy electricity from renewable energy sources, such as wind, new hydroelectric and biomass. As a result, when the electricity Nationwide uses in its branch network and other buildings is generated, it will not add to greenhouse gas emissions.

We focus very clearly on projects which are of lasting benefit, which involve the broadest possible cross-section of the community and which help the most marginalised communities in the UK

Community and Environmental Affairs

CONTINUED

Paper

Due to the nature of our business we use a lot of paper. To reduce the negative impacts of this we:

- encourage our employees to think before they print;
- continue to improve our technology systems so that employees and members can access relevant information, products and services online without printing;
- have increased the use of paper that has some recycled content, which reduces the need for virgin wood pulp, decreases the amount of waste which goes to landfill and reduces the amount of energy and water needed in its production;
- reduce the amount of plastics used in our marketing material. Apart from a very few exceptions where there is a particular requirement, our binders and folders are made from paper over board as opposed to PVC or polypropylene. Where practicable, no laminates or PVC are used.

Waste and recycling

We have developed a waste management plan for our major buildings using Government guidelines. We have introduced the following initiatives:

- waste paper recycling at our major administration buildings;
- confidential waste paper shredding and recycling from the branch network;
- waste recycling facilities are available at our major administration buildings for bottles, spectacles, clothes, stamps and toner cartridges;
- Save-a-Cup plastic cup recycling scheme in our major administration buildings. The cups are recycled into pencils, rulers and other items.

Partners

We appreciate that our sustainability performance is best improved by working closely with partners including suppliers.

Sustainable timber

We buy a significant amount of timber and furniture for our property refurbishments and are working with our suppliers to implement a system which, in time, will ensure that all of the timber we buy is certified under the Forest Stewardship Council or similar schemes. This approach enables us to trace the original source of our timber so that we can be sure that it is coming from well managed forests. Our major shopfitters are already certified under one or more of these schemes.

Fairtrade coffee

Nationwide is pleased to work with Percol to offer Fairtrade coffee to employees through its vending machines at our main administration centres. This unique partnership is now entering its third year and was the first of its kind in the UK. It helps to raise awareness amongst our employees, partners and visitors.

Corporate clothing

For the past six years, we have sought to make a stand when it comes to sourcing materials for our corporate clothing. We apply both ethical and environmental criteria so that there is a traceable chain from the source to the end product.

The standards of labour, social and environmental conditions agreed with our suppliers are independently verified every six months. We also have a recycling procedure in place to ensure all our obsolete garments are recycled.

Nationwide
Disability Sport Events
Creating Champions Together

We have developed a waste management plan for our major buildings using Government guidelines

Nationwide Foundation

The Nationwide Foundation

Supporting communities nationwide

Since it was set up in 1997, the Nationwide Foundation has received over £24 million from Nationwide Building Society which has been distributed to more than 2,000 charities across the United Kingdom. The Nationwide Foundation is a registered charity (no 1065552) and company limited by guarantee which makes donations to registered charities, and is funded principally from contributions from Nationwide Building Society. It is a separate legal entity from the Society and is run by its own Board of Trustees.

The Foundation's membership consists of those who became Society members on or after 2 November 1997. These members agreed to assign to the Foundation any potential windfall benefit to which they might be entitled in the event of the Society undergoing conversion or takeover. Some longer standing Society members have chosen to make this assignment as well. There are now over five million members of the Foundation.

In the financial year ended 31 March 2005, the Foundation made donations to 311 organisations across the United Kingdom, totalling £2.3 million, under its previous criteria of Volunteering and Rural Communities. During 2005, the Trustees carried out an in-depth strategic review, and in Autumn 2005, the Foundation launched its new funding criteria. The chosen theme for the funding programme was Supporting Families, which was influenced by the Foundation's previous work in this field, in particular its aims of tackling social exclusion.

The Foundation now runs two grants programmes with the theme of Supporting Families. These are the Small Grants Programme (SGP) and the Investor Programme. The SGP offers one-off grants of up to £5,000 to registered charities with an income of under £500,000, for work which supports people affected by domestic violence. During the financial year ended 31 March 2006, the SGP awarded 35 grants amounting to over £50,000.

The Investor Programme encompasses three key aims which were identified to help fulfil the vision of the Supporting Families programme. These are to:

- promote the well-being of young men, women and children whose lives have been affected by domestic violence and to reduce the prevalence of domestic violence through increased service provision, education and awareness raising;
- improve the quality of life of families with a member or members in prison, through the provision of services responsive to their needs;
- provide young people who are or have been involved with the criminal justice system with a rehabilitation programme designed to obtain the skills, confidence and personal support networks to enable them to lead fulfilled and successful lives.

In 2005 – 2006, the focus was on the first of these aims which was concerned with the support of those affected by, and the prevention of, domestic violence. The Investor Programme has a budget of £1.25 million for each aim and will fund six charities through each of the aims over a three year period. Of the £1.25 million, 20% (£250,000) will be set aside for partnership working activities. The six charities chosen to take part in the first aim are: Broken Rainbow, 18 and Under, Refuge, Respect, Leeway Norwich Women's Aid

The Foundation has received over £24m from Nationwide Building Society which has been distributed to more than 2,000 charities

Nationwide Foundation

CONTINUED

Photography courtesy of Home-Start, which was supported by the Foundation through the New Generation Initiative.

and Kurdistan Refugee Women's Organisation. Grants of around £900,000 were agreed in support of these charities in the financial year ended 31 March 2006.

The new grants programmes were influenced by the New Generation Initiative (NGI), the Foundation's major grant-making initiative which was launched in April 2000. It enabled charities working with parents to expand their activities significantly, by providing £2.2 million of core funding for three to five years. The five partner charities chosen to take part in this initiative were: Parentline Plus, Straight Talking, Home-Start, M6 Theatre Company and Action for Prisoners' Families. The NGI is now in its fifth year and has benefited thousands of parents, grandparents, children and families each day in the UK through the support of parent telephone help-lines, the provision of direct day-to-day support through local schemes offering befriending opportunities, information packs and parenting education programmes.

The NGI's unique form of funding in the voluntary sector has provided many valuable lessons for charities and funding organisations. These include the additional benefits of providing funding which is long term, flexible and towards core work. It also encouraged collaborative working amongst the charities funded. Shared Intelligence, an independent consultancy, was appointed to monitor and evaluate the NGI. The results of Shared Intelligence's findings have been innovatively presented in the form of a Virtual Town. This demonstrates how the lives of parents, children and families would have benefited if it had been possible for the NGI work to have taken place in one particular town. The results of the evaluation can be viewed on the Foundation's website, in written format and as a Flash movie. The Foundation celebrated the success of the NGI at an event at the House of Commons in December 2005, which was attended by representatives of the charities and the charitable sector, MPs and peers.

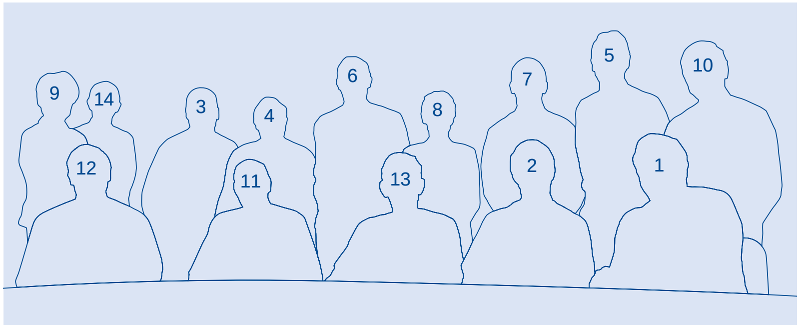
More information about the Foundation is available from:

The Nationwide Foundation
Nationwide House, Pipers Way
Swindon SN38 2SN

Telephone: 01793 655113; Fax: 01793 652409
Email: enquiries@nationwidefoundation.org.uk
Website: www.nationwidefoundation.org.uk

The Foundation enabled charities working with parents to expand their activities significantly by providing £2.2m of core funding

Board of Directors
As at 4 April 2006



[1]
Jonathan Agnew (64)
Chairman
Jonathan Agnew was appointed to the Board in 1997 and became Chairman in 2002. His experience has been in financial services businesses. 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 and is currently Chairman of Beazley Group and The Cayenne Trust and a Director of Rightmove.

[2]
Philip Williamson (58)
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 and Commercial Director. Before joining Nationwide he held senior appointments within the banking and property industries. He is currently President of the European Mortgage Federation and has recently stepped down as Chairman of the Building Societies Association. He will become Chairman of Investors In People (UK) on 1 June 2006.

[3]
Brian Walsh (61)
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 career has spanned over 30 years in industry and finance and he has particular strengths in the financial management of major companies. Previous positions include Finance Director, GKN plc and executive Director, Credit Suisse First Boston.

[4]
Bernard Simpson (58)
Deputy Chief Executive and 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 current responsibilities include marketing, the branch network, internet banking and telephone operations. He is Chairman of The Nationwide Foundation and a Director of various subsidiaries.

Board of Directors

CONTINUED

[5]
Graham Beale (47)
Group Finance Director
Graham Beale joined the Society in 1985 and has worked extensively in the finance function and in other parts of the Group. He was appointed to the Board on 5 April 2003 and his current executive responsibilities are finance and planning, risk management, legal compliance, internal audit and treasury. He is a Director of NBS Fleet Services Limited and various other subsidiaries.

[6]
Stuart Bernau (54)
Commercial & Communications Director
Stuart Bernau joined the Society in 1990 and was appointed a Director in 1996. His current responsibilities include commercial lending, communications, Nationwide Investment Group, general insurance and UCB Home Loans Corporation Ltd. He was appointed Chairman of the Financial Services Skills Council on 23 February 2006.

[7]
Jim Willens (49)
Group Services Director
Jim Willens joined the Society in 1978 and became Retail Director on 1 January 2002. He currently has executive responsibility for banking, savings and mortgages, technology, member account administration and group services. He has served as a Director of the Society's life insurance and unit trust subsidiaries and its specialist lending business, UCB Home Loans Corporation Ltd. Before joining Nationwide, he worked for two major banks.

[8]
Stella David (43)
Non-executive Director
Stella David joined the Board on 16 April 2003, bringing considerable expertise in general management as well as branding, marketing and the management of consumer goods. In November 2005 she became Senior Vice President and Chief Marketing Officer for the international drinks group Bacardi Ltd and prior to this she was Vice President of their Global Operations.

[9]
Suzanna Taverne (46)
Non-executive Director
Suzanna Taverne joined the Board on 16 November 2005. Her experience is in management, strategy and finance. Prior to her appointment she held various positions in the public sector and industry and was formerly a Director of Imperial College London, Managing Director of the British Museum, Director of Strategy at Pearson plc, a Consultant at Saatchi & Saatchi plc, Finance Director of The Independent and a Senior Manager at S.G. Warburg & Co Ltd. She is currently Chair of the National Council for One Parent Families.

[10]
John Engestrom (64)
Non-executive Director
John Engestrom was appointed a Director in 1997. He is a Director of the Society's life insurance and unit trust subsidiaries and brings expertise in the insurance sector to the Board. He is Chairman of the Society's Remuneration Committee. His extensive experience included 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.

[11]
Robert Walther (62)
Non-executive Director
Robert Walther joined the Board on 1 July 2002. He is also a Director of the Society's life insurance and unit trust subsidiaries. His background in investment and insurance was mainly built within a mutual organisation. He was Chief Executive of Clerical Medical from 1995 to 2001, which he joined in 1965. He is currently Chairman of Fidelity European Values plc, and a non-executive Director of BUPA.

[12]
Geoffrey Howe (56)
Non-executive Director
Geoffrey Howe joined the Board on 1 January 2005. He brings considerable legal, regulatory and management experience to the Board. He is currently Chairman of Jardine Lloyd Thompson Group plc and a Director of Investec plc and the JP Morgan Fleming Overseas Investment Trust plc. He was formerly Chairman of Railtrack Group plc, a Director and Group General Counsel of Robert Fleming Holdings Ltd and managing partner of Clifford Chance.

[13]
Richard Handover (59)
Non-executive Director
Richard Handover joined the Board on 1 May 2000 and has extensive knowledge of and experience in the management of businesses within the retail sector. He is Chairman of the Adult Learning Inspectorate and a non-executive Director of Royal Mail and was Vice-Chairman of Business in the Community. He is Chairman of the Strategy Board for the Office for Standards in Education (OFSTED).

[14]
Derek Ross (55)
Non-executive Director
Derek Ross joined the Board on 1 December 2004. He has extensive experience in audit and financial advisory services particularly in areas of treasury and risk management. Prior to his appointment he was a senior partner of Deloitte & Touche LLP for 18 years and previously for 7 years a corporate treasurer and tax manager with Black & Decker.

Directors' Report
For the year ended 4 April 2006

The Directors have pleasure in presenting their Annual Report and Accounts for the year ended 4 April 2006.

As set out more fully in the Statement of Accounting Policies, this Annual Report and Accounts has been prepared in accordance with International Financial Reporting Standards (IFRS) for the first time. Accordingly the comparative information is different from that previously reported. Additionally, (as permitted by IFRS 1) the 2005 results exclude the impact of IAS 32, IAS 39 and IFRS 4 and therefore are not directly comparable with those for 2006. All financial information given in this directors' report is taken solely from the statutory results prepared on the above basis. Unaudited, like-for-like results which allow comparison between 2005 and 2006 are given in the Business Review on pages 6 to 21.

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 in the Business Review on pages 6 to 21.

Profits and capital

Profit before tax was £559.2 million (2005 – £513.9 million). The profit after tax transferred to the general reserve was £397.2 million (2005 – £367.0 million).

Total Group reserves at 4 April 2006 were £5,031.4 million (2005 – £4,563.6 million) after taking into account the revaluation reserve of £117.0 million (2005 – £103.0 million) and the available for sale reserve of £88.8 million (2005 – £nil).

Gross capital at 4 April 2006 was £7,218.9 million (2005 – £6,695.6 million) including £1,446.3 million (2005 – £1,439.8 million) of subordinated debt and £741.2 million (2005 – £692.2 million) of subscribed capital. The ratio of gross capital as a percentage of shares and borrowings at 4 April 2006 was 6.6% (2005 – 6.5%) and the free capital ratio was 6.0% (2005 – 5.8%). (See the annual business statement on page 100 for an explanation of these ratios.)

Mortgage arrears

The Group mortgage portfolios at 4 April 2006 included 466 mortgage accounts (2005 – 570), including those in possession, where payments were more than 12 months in arrears. The total amount of principal loans outstanding in these cases was £41.2 million (2005 – £37.7 million). The total amount of arrears in these cases was £5.4 million (2005 – £5.6 million) or 0.01% (2005 – 0.01%) of total mortgage balances.

Charitable and political donations

During the year the Group made charitable donations of £2,324,287 (2005 – £1,343,009) including £2,000,000 (2005 – £1,000,000) to The Nationwide Foundation, a report on which is given on pages 26 to 27. 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 36 days at 4 April 2006 (2005 – 27 days).

Risk management

The financial management objectives and policies of the Group are shown in the Business Review on page 19 and in note 47 on pages 79 to 88.

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' Report

CONTINUED

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

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

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, CCMI (Deputy Chairman)

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

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

G J Beale BSc, ACA (Group Finance Director)

S D M Bernau BSc (Econ), FCIB, MCT (Commercial & Communications Director)

J H Willens MBA, DMS, ACIB (Group Services Director)

Mrs S J David MA (Cantab)

J Engestrom MBA

R G Handover

G M T Howe MA (Cantab)

D A Ross BSc, LLB, FCA, ACMA, CTA (Fellow), FCT

Ms S Taverne

R P Walther MA, FIA

Ms S Taverne was appointed as a non-executive Director on 16 November 2005.

J G W Agnew, B A Walsh, P F Williamson, S D M Bernau, J Engestrom and R P Walther will retire at the Annual General Meeting on 20 July 2006. All except B A Walsh and J Engestrom will stand for re-election. Ms S Taverne will also 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 re-appoint PricewaterhouseCoopers LLP as auditors will be proposed at the Annual General Meeting.

J G W Agnew
Chairman

17 May 2006

Report of the Directors on Corporate Governance
For the year ended 4 April 2006

The Board of Directors (the 'Board') is committed to best practice in corporate governance. This Report on Corporate Governance explains how the Society applies the principles in the Combined Code on Corporate Governance (the 'Code') issued by the Financial Reporting Council as well as meeting guidance for building societies issued by the Financial Services Authority (the 'FSA'). The Board considers that the Society 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. Each committee comprises only non-executive Directors and each committee has a different Chairman. A non-executive Director also attends the Assets and Liabilities Committee. The terms of reference of each committee are published on the Society's website. The composition of the committees is shown on page 35. 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 ten formal Board meetings each year. In addition the non-executive Directors meet without executive Directors present, at least once a year. Other non-executive Directors meet without the Chairman once a year. The attendance record during the year of members at formal meetings of the Board and its committees is shown on page 35.

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 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 currently comprises five executives and nine 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: The Nomination Committee 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-executive Directors 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 an induction on joining the Board and should regularly update and refresh their skills and knowledge.

Report of the Directors on Corporate Governance

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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 Director's 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: The Board has adopted a methodology to evaluate the performance and effectiveness of individual Directors and of the Board as a whole and its committees. Each Director has a Performance Agreement and (as needed) a 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 makes recommendations to the Board about appointments to the Board and its Committees in accordance with the Board Composition and Succession Plan a copy of which Plan is published on the Society's website. 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 will retire at the AGM on 20 July 2006. 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.

Remuneration

The Report of the Directors on Remuneration (on pages 36 to 38) 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 30 to 31).

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 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 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 the Audit Committee regularly reviews the operational risk profile in the context of the Group's risk appetite. The operational 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.

Report of the Directors on Corporate Governance

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>>> The principal categories of financial risk inherent in the Group's business are described in greater detail in the Business Review under the heading Risk Management and Control (on page 19) 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 operational 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 maintenance of sound systems of risk management and internal control, and following review by the Audit Committee it is satisfied that the Society's systems are appropriate 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 five 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 Audit 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 re-appointment 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 services includes a requirement that the engagement of the auditors for non-audit services requires prior approval of the Committee where the proposed fee for non-audit work exceeds a certain amount or 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 discretionary services where the aggregate fees for all non-audit services would exceed a limit set from time to time 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 has met eight times over the course of this year. The Committee usually excludes all executives from part of its meetings and the Committee annually meets with only the external auditors. By invitation of the Committee, executives and others regularly attending part of its meetings include the Divisional Director Audit, the Deputy Chief Executive and Chief Operating Officer, the Group Finance Director, the Divisional Director Risk Management, the Divisional Director Legal Compliance 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 meeting of the Board following a meeting of the Committee.

The Audit Committee has adopted a 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. The evaluation process includes the completion of a standard review proforma by members of the Committee and by the Divisional Director 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 view 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 conversation, in

Report of the Directors on Corporate Governance

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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. At the AGM the Chief Executive gives a presentation on the main developments in the business and members present have the opportunity to raise questions and put forward their views. 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.

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 as a member 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	Nomination Committee	Remuneration Committee
J G W Agnew, Chairman of Board and the Nomination Committee	10(10)	-	6(6)	-
G J Beale	10(10)	-	-	-
S D M Bernau	9(10)	-	-	-
Mrs S J David	10(10)	-	6(6)	5(5)
J Engestrom, Chairman of the Remuneration Committee	10(10)	8(8)	6(6)	5(5)
R G Handover	10(10)	5(8)	1(1)	5(5)
G M T Howe	9(10)	-	1(1)	4(5)
D A Ross	10(10)	7(8)	-	-
B K Simpson	10(10)	-	-	-
Ms S Taverne	4(4)	-	-	-
B A Walsh, Deputy Chairman, Chairman of the Audit Committee and Senior Independent Director	10(10)	8(8)	6(6)	5(5)
R P Walther	9(10)	7(8)	1(1)	1(1)
J H Willens	10(10)	-	-	-
P F Williamson	10(10)	-	-	-

J G W Agnew
Chairman

17 May 2006

Report of the Directors on Remuneration
For the year ended 4 April 2006

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 (the 'Code') 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 on pages 37 and 38.
- 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 bonus scheme to reward success at the end of the financial year and a medium-term incentive plan 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 plan 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 of specific financial and operational targets, which are the same as those adopted for the employee bonus scheme.

  The scheme is designed to deliver a basic bonus award of 20% of basic salary for executive Directors (24% in the case of the Chief Executive) for on-target performance, with a possible maximum of 40% for above-target performance (48% 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 is designed so that, with effect from 2003/04 onwards, 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 change with effect from 2004/05 onwards) 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 of 50% for above-target performance (60% in the case of the Chief Executive). The target bonus for subsequent three-year periods has been increased to 35% of basic salary (40% in the case of the Chief Executive) with a maximum for above-target performance of 60% (70% in the case of the Chief Executive).
- Executive Directors are members of the Nationwide Pension Fund, details of which are set out in the Notes to the 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 on page 38 shows the value of executive Directors' pension benefits including those arising from unapproved schemes. Directors' pension arrangements have been reviewed in the light of legislative changes for the simplification of tax treatment of pensions with effect from April 2006. This will be reported in the Report of the Directors on Remuneration for the year ended 4 April 2007.
- 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 on pages 37 and 38.

Report of the Directors on Remuneration

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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 a range of data including 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. The non-executive Directors' emoluments are reviewed every two years, the last review having resulted in an increase with effect from 1 April 2005. Details of non-executive Directors' emoluments are set out in Table 1 on pages 37 and 38.
- There are no bonus schemes for the Chairman and other non-executive Directors and non-executive Directors do not qualify for pension entitlement or for other benefits.

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 has established a Remuneration Committee (the 'RemCo'), currently comprising Mr Engestrom (Chairman), Mrs David, Mr Handover, Mr Howe, Mr Walsh and Mr Walther. The terms of reference of the RemCo are available on request from the Secretary and are published on the Society's website.

The RemCo is responsible 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 RemCo'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 meetings 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). Reviews with Hay Group Ltd take place annually to compare the salaries of similarly sized jobs in a selected group of 21 financial services companies, with those being paid to the Society's directors. Any increases in basic salary approved by the RemCo are based on this analysis.

The RemCo is not responsible for the remuneration of non-executive Directors (other than the Chairman). A panel comprising the executive Directors and the Chairman 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. A review of the non-executive Directors' remuneration takes place every two years.

Table 1 Directors' emoluments

	2006			2005		
	Society Fees	**Subsidiary Fees**	**Total**	Society Fees	Subsidiary Fees	Total
Non-executive Directors	**£000**	**£000**	**£000**	£000	£000	£000
J G W Agnew (Chairman)	**200**	**-**	**200**	160	-	160
Mrs S J David	**45**	**-**	**45**	36	-	36
J Engestrom	**61**	**16**	**77**	45	14	59
Ms R E Evans (Retired 31 March 2005)	**-**	**-**	**-**	35	-	35
R G Handover	**49**	**-**	**49**	40	-	40
G M T Howe (Appointed 1 Jan 2005)	**43**	**-**	**43**	9	-	9
D A Ross (Appointed 1 Dec 2004)	**51**	**-**	**51**	15	-	15
Ms S Taverne (Appointed 16 Nov 2005)	**15**	**-**	**15**	-	-	-
B A Walsh (Deputy Chairman)	**90**	**-**	**90**	70	-	70
R P Walther	**49**	**16**	**65**	42	14	56
Total	**603**	**32**	**635**	452	28	480
Pension payments to past Directors in respect of services as Directors			**463**			476

Subsidiary fees relate to fees payable as a Director of Nationwide Life Ltd and Nationwide Unit Trust Managers Ltd.

Report of the Directors on Remuneration

CONTINUED

>>> Table 1 Directors' emoluments (continued)

Executive Directors	Salary £000	Annual bonus £000	Benefits £000	3-year medium term bonus £000	Sub-total £000	Increase in accrued pension £000	Total £000
2006							
P F Williamson (Chief Executive)	**575**	**338**	**37**	**345**	**1,295**	**34**	**1,329**
B K Simpson	**432**	**210**	**25**	**216**	**883**	**27**	**910**
G J Beale	**340**	**168**	**25**	**170**	**703**	**29**	**732**
S D M Bernau	**357**	**173**	**28**	**179**	**737**	**23**	**760**
J H Willens	**300**	**144**	**25**	**150**	**619**	**20**	**639**
	2,004	**1,033**	**140**	**1,060**	**4,237**	**133**	**4,370**
2005							
P F Williamson (Chief Executive)	540	353	33	243	1,169	45	1,214
B K Simpson	410	223	26	184	843	28	871
G J Beale	300	162	26	135	623	33	656
S D M Bernau	338	183	25	152	698	22	720
J H Willens	280	153	24	126	583	28	611
	1,868	1,074	134	840	3,916	156	4,072

Directors' emoluments are audited information.

Table 2 Directors' pension benefits

Executive Directors	**Accrued pension at 4.4.06 £000 (a)**	Accrued pension at 4.4.05 £000 (b)	**Transfer value at 4.4.06 £000 (c)**	Transfer value at 4.4.05 £000 (d)	**Change in transfer value £000 (c)-(d)**	**Additional pensions earned in a year £000 (e)**	**Transfer value of the increase £000 (f)**	**Directors' contributions in a year £000 (g)**
P F Williamson (Chief Executive)	**273**	239	**5,197**	3,805	**1,392**	**28**	**536**	**16**
B K Simpson	**266**	239	**5,031**	3,788	**1,243**	**21**	**391**	**16**
G J Beale	**162**	133	**1,866**	1,320	**546**	**25**	**293**	**22**
S D M Bernau	**212**	189	**3,410**	2,602	**808**	**17**	**280**	**16**
J H Willens	**164**	144	**2,134**	1,613	**521**	**17**	**216**	**19**

Notes:

(a) and (b) show deferred pension entitlements at 4 April 2006 and 2005 respectively.

(c) is the transfer value of the deferred pension in (a) calculated at 4 April 2006.

(d) is the equivalent transfer value at 4 April 2005 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).

(g) contributions are inclusive of salary sacrifice contributions.

J Engestrom
Chairman of the Remuneration Committee

17 May 2006

Independent Auditors' Report
To the members of Nationwide Building Society

We have audited the Group and Society Annual Accounts of Nationwide Building Society for the year ended 4 April 2006 which comprise the Group and Society Income Statements, the Group and Society Balance Sheets, the Group and Society Statements of Recognised Income and Expense, the Group and Society Cash Flow Statements and the related notes. These Annual Accounts have been prepared under the accounting policies set out therein. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

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, including the Annual Accounts, the Directors' Remuneration Report, the Annual Business Statement and the Directors' Report in accordance with applicable law and International Financial Reporting Standards (IFRS), as adopted by the European Union, are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the Annual Accounts and the part of the Directors' Remuneration Report to be audited in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). 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 into 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 and whether the Annual Accounts and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Building Societies Act 1986, regulations made under it and Article 4 of the IAS Regulation. We also report to you our opinion as to whether certain information included within the Annual Business Statement gives a true representation of the matters in respect of which it is given, whether the information given in the Directors' Report is consistent with the accounting records and the Annual Accounts, and whether the Annual Business Statement and the Directors' Report have been prepared in accordance with the applicable requirements of the Building Societies Act 1986 and regulations made under it.

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

We read other information contained in the Annual Report and consider whether it is consistent with the audited Annual Accounts. This other information comprises only the Financial Highlights, the Chairman's Statement, the Chief Executive's Review, the Business Review, the remainder of the Report of the Directors on Remuneration and the Report of the Directors on Corporate Governance. We 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. Our responsibilities do not extend to any other information.

Basis of Audit Opinion

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Annual Accounts and the part of the Directors' Remuneration Report to be audited 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 and the part of the Directors' Remuneration Report to be audited.

Opinion

In our opinion:

- the Annual Accounts give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's and the Society's affairs at 4 April 2006 and of the Group's and the Society's income and expenditure and cash flows 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 part of the Directors' Remuneration Report to be audited, the Annual Business Statement and the Directors' Report have each been prepared in accordance with the applicable requirements of the Building Societies Act 1986 and regulations made under it and, as regards the Annual Accounts, Article 4 of the IAS Regulation.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London
17 May 2006

Income Statements
For the year ended 4 April 2006

	Notes	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Interest receivable and similar income	3	**5,799.9**	5,211.2	**5,551.3**	4,977.6
Interest expense and similar charges	4	**4,565.6**	4,019.6	**4,525.8**	3,979.9
Net interest income		**1,234.3**	1,191.6	**1,025.5**	997.7
Fee and commission income	5	**309.3**	384.0	**281.0**	348.8
Fee and commission expense	6	**(2.9)**	(102.8)	**(2.8)**	(92.9)
Premiums on insurance contracts and fair value gains on insurance assets	7	**278.9**	197.1	**-**	-
Income from investments	8	**7.9**	0.3	**59.3**	33.6
Other operating income	9	**25.5**	31.7	**8.1**	5.4
Gains from derivatives and hedge accounting	10	**10.9**	-	**9.7**	-
Total income		**1,863.9**	1,701.9	**1,380.8**	1,292.6
Insurance claims and change in liabilities	7	**208.4**	152.4	**-**	-
Total income net of claims on insurance contracts		**1,655.5**	1,549.5	**1,380.8**	1,292.6
Administrative expenses	11	**873.7**	833.2	**820.2**	788.5
Depreciation and amortisation		**117.5**	107.1	**115.0**	104.3
Impairment losses on loans and advances to customers	13	**76.6**	46.6	**48.9**	32.1
Provisions for liabilities and charges	37	**32.1**	46.7	**28.5**	44.6
Impairment (gains)/losses on investment securities	17	**(3.6)**	2.0	**(3.6)**	2.0
Profit before tax		**559.2**	513.9	**371.8**	321.1
Taxation	14	**162.0**	146.9	**109.7**	102.5
Profit after tax		**397.2**	367.0	**262.1**	218.6

The accounting policies and notes on pages 44 to 98 form part of these Accounts.

The results have been prepared under IFRS. In accordance with the transitional rules on first-time adoption of IFRS, the 2005 comparatives do not follow IAS 32 'Financial Instruments: Presentation' ('IAS 32'), IAS 39 'Financial Instruments: Recognition and Measurement' ('IAS 39'), and IFRS 4 'Insurance Contracts' ('IFRS 4') but instead follow applicable UK GAAP requirements.

The main impacts on the comparative income statement, had these standards been applied, would have been:

- Fee and commission income and expense would have been lower and interest receivable would have increased due to the recognition of certain fees on an effective interest basis spread over the expected life of the asset;
- Impairment losses on loans and advances to customers would have reflected impairment only where objective evidence of impairment existed; and
- The movement in the fair value of derivatives and hedged risk would have been included within gains/(losses) from derivatives and hedge accounting.

Balance Sheets
At 4 April 2006

	Notes	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Assets					
Cash and balances with the Bank of England		**368.6**	362.5	**367.8**	362.1
Loans and advances to banks	16	**1,364.0**	751.6	**1,017.4**	481.3
Investment securities – available for sale	17	**13,007.7**	14,145.0	**11,421.0**	12,859.8
Derivative financial instruments	18	**541.1**	-	**511.3**	-
Insurance and other financial assets at fair value	7	**1,918.2**	1,825.2	**21.3**	-
Fair value adjustment for portfolio hedged risk	19	**(52.2)**	-	**(52.2)**	-
Loans and advances to customers	20	**101,347.6**	92,721.9	**92,597.9**	84,646.8
Investments in equity shares	21	**22.0**	14.9	**2.2**	1.9
Investments in group undertakings	22	**-**	-	**10,846.3**	8,374.8
Value of in force life insurance contract business	23	**125.4**	127.6	**-**	-
Intangible fixed assets	24	**80.5**	44.2	**80.5**	44.2
Property, plant and equipment	25	**648.0**	620.0	**629.5**	602.3
Investment properties	26	**279.1**	242.6	**10.2**	9.3
Accrued income and expenses prepaid	27	**416.8**	366.7	**560.6**	463.2
Deferred tax assets	28	**110.0**	81.9	**149.5**	127.1
Other assets	29	**409.2**	292.7	**65.0**	72.7
Total assets		**120,586.0**	111,596.8	**118,228.3**	108,045.5
Liabilities					
Shares	30	**80,918.6**	72,594.1	**80,918.6**	72,594.1
Deposits from banks	31	**2,697.4**	2,453.3	**1,805.2**	1,647.3
Other deposits	32	**3,161.4**	2,802.4	**7,225.1**	4,590.1
Due to customers	33	**2,608.3**	2,257.0	**941.1**	935.7
Debt securities in issue	34	**20,767.6**	22,377.6	**19,571.7**	21,422.8
Fair value adjustment for portfolio hedged risk	19	**53.9**	-	**53.9**	-
Derivative financial instruments	18	**631.3**	-	**563.0**	-
Insurance contract liabilities	35	**1,190.5**	1,132.1	**-**	-
Other liabilities	36	**515.8**	404.9	**350.1**	309.0
Provisions for liabilities and charges	37	**40.3**	49.0	**29.0**	41.1
Accruals and deferred income	38	**313.5**	373.4	**270.9**	355.0
Subordinated liabilities	39	**1,446.3**	1,439.8	**1,446.3**	1,439.8
Subscribed capital	40	**741.2**	692.2	**741.2**	692.2
Current tax liabilities		**174.3**	105.8	**141.0**	85.4
Retirement benefit obligations	41	**294.2**	351.6	**293.6**	351.0
Total liabilities		**115,554.6**	107,033.2	**114,350.7**	104,463.5
General reserve	42	**4,825.6**	4,460.6	**3,714.5**	3,479.1
Revaluation reserve	43	**117.0**	103.0	**116.8**	102.9
Available for sale reserve	44	**88.8**	-	**46.3**	-
Total reserves & liabilities		**120,586.0**	111,596.8	**118,228.3**	108,045.5

The accounting policies and notes on pages 44 to 98 form part of these Accounts.

In accordance with the transitional rules on first-time adoption of IFRS, the 2005 comparatives do not follow IAS 32, IAS 39, and IFRS 4 but instead follow applicable UK GAAP requirements.

Approved by the Board of Directors on 17 May 2006.

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

Statements of Recognised Income and Expense
For the year ended 4 April 2006

		Group		Society	
	Notes	**2006 £m**	2005 £m	**2006 £m**	2005 £m
Available for sale investments - net fair value gain	44	**55.3**	-	**48.9**	-
Property revaluation	43	**24.1**	24.9	**24.0**	24.9
Actuarial (loss)/gain on retirement benefit obligations	41	**(6.1)**	104.9	**(6.1)**	104.8
Taxation on items through equity		**(23.4)**	(38.2)	**(19.8)**	(38.3)
Net income recognised directly in reserves		**49.9**	91.6	**47.0**	91.4
Net profit for the year		**397.2**	367.0	**262.1**	218.6
Total recognised income and expense for the year		**447.1**	458.6	**309.1**	310.0

Impacts arising from changes in accounting policies

Adoption of IFRS 4 and IAS 39	**33.3**	-	**0.9**	-
Tax on adoption of IFRS 4 and IAS 39	**(12.6)**	-	**(14.4)**	-
Adoption of IFRS 4 and IAS 39	**20.7**	-	**(13.5)**	-

The accounting policies and notes on pages 44 to 98 form part of these Accounts.

The results for 2006 have been prepared under IFRS. In accordance with the transitional rules on first-time adoption of IFRS, the 2005 comparatives do not follow IAS 32, IAS 39 and IFRS 4 but instead follow applicable UK GAAP requirements.

Cash Flow Statements
For the year ended 4 April 2006

	Notes	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Cash flows from operating activities					
Profit before tax		**559.2**	513.9	**371.8**	321.1
Adjustments for:					
• Non-cash items included in profit before tax	49	**133.1**	211.0	**123.4**	202.4
• Changes in operating assets	49	**(10,110.1)**	(12,566.2)	**(11,199.5)**	(12,321.8)
• Changes in operating liabilities	49	**8,519.8**	9,111.3	**9,869.5**	8,524.9
• Interest paid on subordinated liabilities		**(54.8)**	(46.7)	**(54.8)**	(46.7)
• Interest paid on subscribed capital		**(46.8)**	(46.9)	**(46.8)**	(46.9)
• Taxation		**(149.5)**	(103.8)	**(99.1)**	(64.5)
Net cash flows from operating activities		**(1,149.1)**	(2,927.4)	**(1,035.5)**	(3,431.5)
Cash flows from investing activities					
Purchase of investment securities		**(9,989.9)**	(12,122.9)	**(9,327.7)**	(11,178.7)
Sale and maturity of investment securities		**10,286.5**	15,623.2	**9,823.5**	15,251.5
Purchase of property, plant and equipment		**(76.9)**	(109.4)	**(75.2)**	(107.5)
Sale of property, plant and equipment		**1.9**	2.7	**1.9**	3.0
Purchase of investment properties		**(23.1)**	(8.9)	**-**	(0.2)
Sale of investment properties		**5.0**	9.3	**-**	-
Purchase of intangible fixed assets		**(77.6)**	(17.0)	**(77.6)**	(17.0)
Net cash flows from investing activities		**125.9**	3,377.0	**344.9**	3,951.1
Cash flows from financing activities					
Issue of subordinated liabilities		**-**	513.9	**-**	513.9
Net cash flows from financing activities		**-**	513.9	**-**	513.9
Net (decrease)/increase in cash		**(1,023.2)**	963.5	**(690.6)**	1,033.5
Cash and cash equivalents at start of year		**4,985.3**	4,013.6	**4,070.5**	3,028.9
Cash and cash equivalents at end of year	49	**3,962.1**	4,977.1	**3,379.9**	4,062.4

An explanation of the significant changes between the cash flow statement prepared under UK GAAP and IFRS is included in note 49.

Notes to the Accounts

1 Statement of Accounting Policies

Changes in Accounting Policies

At the start of the year the Group adopted International Financial Reporting Standards (IFRS) for the first time. The impact of the adoption of IFRS on the Group's results for 2004/05 was published on 22 September 2005 in the 'Restatement of 2004/05 Financial Results to International Financial Reporting Standards' document. Copies of this are available at www.nationwide.co.uk/about_nationwide/results_accounts/. The impact of the adoption of IFRS has also been summarised in notes 51 and 52 on pages 91 to 95 of these accounts.

Comparative information for 2004/05 has been restated to take into account the requirements of all of the standards except for IAS 32, IAS 39 and IFRS 4. In accordance with the transitional rules of IFRS, these standards have been implemented with effect from 5 April 2005 and the balance sheet at this date has been adjusted accordingly. Where comparative figures have been prepared under UK GAAP the accounting policies have been disclosed on pages 52 and 53.

Basis of preparation

These financial statements have been prepared in accordance with IFRS as adopted by the European Union; interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC); and with those parts of the Building Societies (Accounts and Related Provisions) Regulations 1998 applicable to organisations reporting under IFRS. The financial statements have been prepared under the historical cost convention as modified by the revaluation of land and buildings, available for sale investments, derivatives and other financial assets at fair value through the income statement. A summary of the Group's accounting policies is set out below.

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Further details on critical accounting estimates are given in note 2.

The Group has applied early IFRS 7 'Financial Instruments: Disclosures' prospectively from 5 April 2005 and the amendments to IAS 19 'Employee Benefits' issued by the International Accounting Standards Board in August 2005 and December 2004 respectively.

The Group has not applied early the following amendments:

- the amendment to IAS 1 'Presentation of Financial Statements: Capital Disclosures'. This amendment requires disclosure on the level of the Group capital and how this is managed.
- amendments to IAS 39 and IFRS 4 'Financial Guarantee Contracts'. These amendments require financial guarantee contracts to be accounted for as financial instruments rather than insurance contracts.
- amendment to IAS 39 'The Fair Value Option'. This amendment allows financial liabilities to be measured at fair value through the income statement only if certain conditions are met.

In addition to the exemption from the requirement to restate comparatives under IAS 32, IAS 39 and IFRS 4, IFRS 1 grants certain optional exemptions from the full requirements of IFRS when adopting IFRS for the first time. The Group has elected to use the following exemptions in arriving at the 5 April 2004 IFRS opening balances for the purposes of these financial statements:

- Business combinations

The Group has opted to apply IFRS 3 'Business Combinations' prospectively. Consequently, goodwill previously amortised has not been restated in the opening IFRS balance sheet at 5 April 2004.

- Employee benefits

The Group has elected to apply IAS 19 'Employee Benefits' prospectively. As at 5 April 2004, all cumulative actuarial gains and losses on the Group's retirement benefit schemes have been recognised.

Basis of consolidation

The Group accounts consolidate the assets, liabilities and results of the Society and all its subsidiaries.

Subsidiaries are all entities, including special purpose entities, over which the Society has the power to govern the financial and operating policies generally. Subsidiaries are fully consolidated from the date on which control is transferred to the

Notes to the Accounts

CONTINUED

1 Statement of Accounting Policies (continued)

Group and are de-consolidated from the date that control ceases. Upon consolidation, inter-company transactions, balances and unrealised gains on transactions are eliminated.

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 individually significant transactions arising between 31 March and the Society's year end. Certain special purpose entities 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 is 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.

Interest receivable and interest expense

For instruments measured at amortised cost the effective interest method is used to measure the carrying value of a financial asset or a liability and to allocate associated interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

In calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, early redemption penalty charges) but does not consider future credit losses. The calculation includes all fees received and paid and costs borne that are an integral part of the effective interest rate and all other premiums or discounts above or below market rates.

Interest income on available for sale investments, derivatives and other financial assets at fair value through the income statement is included in interest receivable and similar income.

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

Fees and commissions

Direct fees and costs incremental to generating a financial instrument are deferred and spread as interest receivable or expense on an effective interest basis.

Other fees and commissions are recognised on the accruals basis as services are provided, or on the performance of a significant act.

Segmental Reporting

A business segment is defined as a group of assets and operations providing products and services that are subject to different risks and returns from those of other business segments. The Group considers that business segments are its primary reporting format for segment analysis. Business segments are based on the Group's management and internal reporting structures.

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.

Intangibles

IAS 38 'Intangible Assets' requires the capitalisation of certain expenditure relating to software development costs. Software development costs are capitalised if it is probable that the asset created will generate future economic benefits. Costs incurred to establish technological feasibility or to maintain existing levels of performance are recognised as an expense.

Web costs are capitalised where the expenditure is incurred on developing an income generating website.

Where software costs are capitalised, they are amortised using the straight line method over their estimated useful lives (3 to 5 years). The amortisation periods used are reviewed annually.

Notes to the Accounts

CONTINUED

1 Statement of Accounting Policies (continued)

Computer application software licences are recognised as intangible fixed assets and amortised using the straight line method over their useful lives.

Leases

Leases entered into by the Group are primarily operating leases.

(a) As lessee

Operating leases are leases that do not transfer substantially all the risks and rewards incidental to ownership to the lessee. The Group has entered into operating leases for land and buildings. Operating lease payments are charged to the income statement on a straight line basis over the life of the lease.

(b) As lessor

Lease income receivable under operating leases is credited to the income statement on a straight line basis over the life of the lease.

Taxation including deferred tax

Corporation tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which profits arise. The tax effects of tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and laws that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

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

Deferred tax related to fair value re-measurement of available for sale investments, which are charged or credited directly to the available for sale reserve, is also credited or charged directly to the available for sale reserve and is subsequently recognised in the income statement together with the deferred gain or loss.

Property, plant and equipment

Freehold and long leasehold properties comprise mainly branches and office buildings.

Branches and non specialised buildings are stated at revalued amounts, being the fair value, determined by market based evidence, at the date of the valuation less any subsequent accumulated depreciation and subsequent impairment. Valuations are completed annually by independent surveyors.

Increases in the valuations of branches and non specialised buildings are credited to the revaluation reserve except where they reverse decreases for the same asset previously recognised in the income statement, in which case the increase in the valuation is recognised in the income statement. Decreases in valuations are recognised in the income statement except where they reverse amounts previously credited to the revaluation reserve for the same asset, in which case the decrease in valuation is recognised in the revaluation reserve.

Other property, plant and equipment, including specialised administration buildings and short leasehold buildings, are included at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items, major alterations and refurbishments. Where applicable, directly attributable borrowing costs incurred in the construction of qualifying assets are capitalised.

Land is not depreciated. Depreciation on other assets commences when the assets are ready for their intended use and is calculated using the straight line method to allocate their cost or valuation over the following estimated useful lives:

Branches and non specialised buildings	60 years
Specialised administration buildings	25 to 43 years
Short leasehold buildings	over the period of the lease
Other equipment	3 to 10 years

Notes to the Accounts

CONTINUED

1 Statement of Accounting Policies (continued)

Estimated useful lives are reviewed annually, and adjusted if appropriate, in the light of technological developments, usage and other relevant factors.

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the net disposal proceeds with the carrying amount of the asset and are included in the income statement.

Investment properties

Investment properties, which comprise of properties held for rental, are stated at fair value. The properties are revalued annually by independent surveyors supported by market evidence. Changes in fair value are included in the income statement.

Depreciation is not charged on investment properties.

Financial liabilities

Borrowings, including shares, deposits, debt securities in issue and subordinated liabilities are recognised initially at fair value, being the issue proceeds net of premiums, discounts and transaction costs incurred.

Borrowings are subsequently measured at amortised cost using the effective interest method. Amortised cost is adjusted for the amortisation of any transaction costs and premiums and discounts. The amortisation is recognised in interest expense and similar charges using the effective interest method.

Permanent Interest Bearing Shares (subscribed capital), which are redeemable at specific dates at the option of the Society, are classified as financial liabilities.

Financial liabilities are derecognised when the obligation is discharged, cancelled or has expired.

Borrowings that are designated as hedged items are subject to measurement under the hedge accounting requirements described in the derivatives and hedge accounting policy note.

Financial assets

The Group classifies its financial assets at inception into the following three categories:

(a) Financial assets at fair value through the income statement

This category consists of derivative financial assets and those assets designated as financial assets at fair value through the income statement at inception. Certain of the Group's investment securities, held to meet insurance liabilities, are included in this category, as well as mortgage commitments entered into where a loan has not yet been made. The Group does not hold any financial assets classified as held for trading.

Financial assets at fair value through the income statement are carried at fair value. The fair values are quoted market prices (where there is an active market), or are based on valuation techniques (where there is no active market or the securities are unlisted). Valuation techniques include the use of recent arm's length transactions, discounted cash flow analysis and other commonly used valuation techniques.

Gains and losses arising from the changes in the fair values are recognised in the income statement.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Group's residential and commercial mortgage loans, unsecured lending and loans to banks are classified as loans and receivables.

Loans are recognised when the funds are advanced to customers. Loans and receivables are carried at amortised cost using the effective interest method.

(c) Available for sale (AFS)

AFS assets are non-derivative financial assets that are not classified into either of the two categories above.

Notes to the Accounts

CONTINUED

1 Statement of Accounting Policies (continued)

AFS assets are initially measured at fair value. Subsequently, AFS assets are carried at fair value. The fair values are quoted market prices (where there is an active market), or based on valuation techniques (where there is no active market or the securities are unlisted).

Unrealised gains and losses arising from changes in the fair values are recognised directly in the available for sale reserve, except for impairment losses, and foreign exchange gains and losses, which are recognised in the income statement. Gains and losses arising on the sale of AFS assets, including any cumulative gains or losses previously recognised in the available for sale reserve, are recognised in the income statement.

The Group has not classified any financial assets into the held to maturity category.

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

Financial assets are derecognised when the rights to receive cash flows have expired or where substantially all of the risks and rewards of ownership have been transferred.

The impact of hedging on the measurement of financial assets is detailed in the derivatives and hedge accounting policy note.

Impairment of financial assets

(a) Assets carried at amortised cost

The Group assesses at each balance sheet date whether, as a result of one or more events that occurred after initial recognition, there is objective evidence that a financial asset or group of financial assets are impaired. Evidence of impairment may include indications that the borrower or group of borrowers are experiencing significant financial difficulty, default or delinquency in interest or principal payments or the debt being restructured to reduce the burden on the borrower.

The Group first assesses whether objective evidence of impairment exists either individually for assets that are separately significant or individually or collectively for assets that are not separately significant. If there is no objective evidence of impairment for an individually assessed asset it is included in a group of assets with similar credit risk characteristics and collectively assessed for impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The resultant provisions have been deducted from the appropriate asset values in the balance sheets.

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

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised the provision is adjusted and the amount of the reversal is recognised in the income statement.

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

Loans subject to collective impairment assessment and whose terms have been renegotiated are no longer considered to be past due or impaired but are treated as new loans after the minimum required number of payments under the new arrangements have been received. Loans subject to individual impairment assessment, whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired or are considered to be past due.

Notes to the Accounts

CONTINUED

1 Statement of Accounting Policies (continued)

(b) Available for sale assets

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets are impaired. In the case of investment securities classified as available for sale, a significant or prolonged decline in the fair value of the asset below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available for sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised – is recognised in the income statement.

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

Derivatives and hedge accounting

Derivatives are entered into to reduce exposures to fluctuations in interest rates, exchange rates, market indices and credit risk.

(a) Derivative financial instruments

Derivatives are initially measured at fair value and are subsequently remeasured to fair value at each reporting date with movements recorded in the income statement. Fair values are obtained from quoted prices prevailing in active markets and valuation techniques, including discounted cash flow models, as appropriate. All derivatives are classified as assets where their fair value is positive and liabilities where their fair value is negative. Where there is the legal ability and intention to settle net, then the derivative is classified as a net asset or liability, as appropriate.

(b) Embedded derivatives

A number of complex contracts contain both a derivative and a non-derivative component, in which case the derivative is termed an embedded derivative. If the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract, and the overall contract itself is not carried at fair value, the embedded derivative is accounted for separately and reported at fair value with gains and losses being recognised in the income statement.

(c) Hedge accounting

When transactions meet the criteria specified in IAS 39, the Group applies fair value hedge accounting so that changes in the fair value of the underlying asset or liability that are attributable to the hedged risk are recorded in the income statement to offset the fair value movement of the related derivative.

To qualify for hedge accounting at inception the hedge relationship must be clearly documented. At inception the derivative must be expected to be highly effective in offsetting the hedged risk, and effectiveness must be tested throughout the life of the hedge relationship.

The Group discontinues hedge accounting when:

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

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

If the derivative no longer meets the criteria for hedge accounting, the cumulative fair value hedging adjustment is amortised over the period to maturity of the previously designated hedge relationship. If the underlying item is sold or repaid, the unamortised fair value adjustment is immediately reflected in the income statement.

In a micro hedge, the carrying value of the hedged item is adjusted for the change in value of the hedged risk. In the case of a portfolio hedge, the adjustment is included in fair value adjustments for hedged risk.

Notes to the Accounts

CONTINUED

1 Statement of Accounting Policies (continued)

Employee benefits

(a) Pensions

The Group operates a number of pension arrangements. The majority of the Group's employees are members of the Nationwide Pension Fund ('the Fund'). The Group also operates other arrangements for certain current and former Directors and Officers and for one subsidiary undertaking.

All of the pension arrangements are defined benefit plans. A defined benefit plan is one that defines the benefit an employee will receive on retirement, depending on such factors as age, length of service and salary.

The liability recognised in the balance sheet in respect of the defined benefit pension plans is the present value of the defined benefit obligation at the balance sheet date less the fair value of plan assets. The defined benefit obligation is calculated by the independent actuary using the projected unit credit method and assumptions agreed with the Group. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of high-quality corporate bonds that have terms to maturity approximating to the terms of the related pension liability.

Actuarial gains and losses arise from experience adjustments (the effects of differences between previous actuarial assumptions and what has actually occurred) and changes in actuarial assumptions. Actuarial gains and losses are recognised in full, in the year they occur, in the statement of recognised income and expense.

Past service costs are recognised immediately in the income statement, unless the changes to the benefits are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past service costs are amortised on a straight line basis over the vesting period.

(b) Other post retirement obligations

The Group provides post retirement healthcare to a small number of former employees. The Group recognises this obligation and the actuarial gains and losses in a similar manner to the defined benefit pension plans.

(c) Other long term employee benefits

The cost of bonuses payable twelve months or more after the end of the year in which they are earned are recognised immediately in the year in which the employees render the related service.

(d) Short term employee benefits

The cost of short term employee benefits, including wages and salaries, social security costs and healthcare for current employees is recognised in the year of service.

Long term life insurance

(a) Classification of contracts

The Group issues linked contracts that transfer both insurance risk and financial risk, and term and annuity contracts that transfer insurance risk. Contracts that contain significant insurance risk for the Group are accounted for as insurance liabilities. Such contracts may also contain financial risk. Contracts that do not contain significant insurance risk are classified as investment contracts and are accounted for as financial liabilities. Premiums are recognised as revenue when they become payable by the contract holder. Claims and surrenders are recognised when notified and maturities are recognised on the policy maturity date.

(b) Recognition and measurement of insurance liabilities

Premiums on term insurance contracts are recognised as revenue when they become due for payment. Single premiums on linked contracts are recognised as revenue when the policy comes into force. A liability for contractual benefits that are expected to be incurred in the future is recognised when the premiums are recognised. Benefits are accounted for on maturity or when the insured event occurs. The increase or decrease in the liability for contractual benefits and benefits paid is included in claims on insurance contracts in the income statement.

The liability for contractual benefits under term insurance contracts is the discounted value of future benefit payments, allowing for assumptions as to mortality, persistency, future premiums, maintenance expenses and investment income. The liability for linked contracts is adjusted for the changes in the fair value of the underlying assets.

The Group enters into reinsurance contracts in relation to some long term insurance contracts. Insurance liabilities that are reinsured are included gross with corresponding reinsurance assets included in other assets.

Notes to the Accounts

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1 Statement of Accounting Policies (continued)

A liability adequacy test is performed using current best estimates of future contractual cash flows, claims handling and administrative expenses and investment income from assets backing the liabilities. Any deficiency is immediately charged to the income statement by establishing a provision for losses arising from the liability adequacy test.

(c) Embedded value

The embedded value method of accounting is used to measure the Group's interest in the long term life insurance contract business. This represents the present value of in force insurance contract business together with the net assets.

The value of in force life insurance contract business is determined using assumed economic parameters (future investment returns and risk discount rate) and mortality, persistency, expense assumptions and future expense inflation. The present value of the in force business is determined on a pre tax basis with changes in the valuation included in other operating income.

(d) Consolidation

Other assets and liabilities relating to the life insurance business are included in the appropriate categories in the Group balance sheet.

Foreign currency translation

The consolidated financial statements are presented in Sterling, which is the functional currency of the parent undertaking. Items included in the financial statements of each of the Group's entities are measured using their functional currency. Foreign currency transactions are translated into Sterling using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are retranslated at the rate prevailing at the year end.

Foreign exchange gains and losses resulting from the retranslation and settlement of these items are recognised in the income statement.

Non-monetary assets that are measured at fair value are translated using the exchange rate at the date that the fair value was determined. Exchange differences on equities and similar non-monetary items held at fair value through the income statement, are reported as part of the fair value gain or loss.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet if, and only if, there is a currently enforceable legal right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise an asset and settle the liability simultaneously.

Sale and repurchase agreements (including stock borrowing and lending)

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

Similarly, where the Group borrows or purchases securities subject to a commitment to resell them (a 'reverse repo') but does not acquire the risks and rewards of ownership, the transactions are treated as collateralised loans, and the securities are not included in the balance sheet.

The difference between sale and repurchase price is accrued over the life of the agreements using the effective interest method.

Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and non-restricted balances with central banks, treasury bills and other eligible bills, loans and advances to banks, other amounts due from banks and short term government securities.

Provisions and contingent liabilities

A provision is recognised when there is a present obligation as a result of a past event, it is probable that the obligation will be settled and it can be reliably estimated.

Contingent liabilities have not been recognised.

Notes to the Accounts

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1 Statement of Accounting Policies (continued)

UK GAAP Accounting Policies

In accordance with the transitional rules on first-time adoption of IFRS, the 2005 statutory comparatives do not follow IAS 32, IAS 39 and IFRS 4 but instead follow applicable UK GAAP requirements. We have reproduced below those UK GAAP accounting policies that apply to the 2005 comparatives.

Income recognition

Interest is recognised in the income statement 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.

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, which are amortised from purchase to maturity less provision for any impairment in value.

Derivatives

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 expense 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 accrued income and expenses prepaid.

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 statement.

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.

Notes to the Accounts

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1 Statement of Accounting Policies (continued)

Specific and general provisions are deducted from loans and advances. The charge to the income statement 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 receivable and similar 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.

2 Judgements in applying accounting policies and critical accounting estimates

The Group has to make judgements in applying its accounting policies which affect the amounts recognised in the accounts. In addition, estimates and assumptions are made that could affect the reported amounts of assets and liabilities within the following financial year. The most significant areas where judgements and estimates are made are as follows:

Impairment provisions on loans and advances

In accordance with the accounting policy on the impairment of financial assets carried at amortised cost where objective evidence exists that a loss has been incurred, the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

Key assumptions included in the measurement of the incurred loss include data regarding the probability of any account going into default, the probability of defaulted accounts progressing to possession and the eventual loss incurred in the event of forced sale or write off. These assumptions are based on observed historical data and updated as management considers appropriate to reflect current and future conditions. The accuracy of the impairment provision would therefore be affected by unexpected changes in the above assumptions.

To the extent that actual losses incurred differ from that estimated by 10%, the impairment provisions on loans and advances would change by an estimated £15.0 million.

Impairment of available for sale assets

The Group determines that available for sale investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates, among other factors, the normal volatility in valuation, evidence of a deterioration in the financial health of the investee, industry and sector performance and operational and financing cash flows.

Fair value of derivatives and available for sale assets

The fair values of derivative financial instruments and available for sale assets are calculated using valuation techniques, including discounted cash flow models, where market values are not available. Changes in assumptions used in the models could affect the reported fair value of financial instruments.

Retirement benefit obligations

The Group has to make assumptions on the expected return on pension plan assets, mortality, inflation and future salary rises when valuing its pension liability and the cost of benefits provided. Changes in assumptions could affect the reported liability, service cost and expected return on pension plan assets.

The impact of a 0.1% increase in the inflation assumption would be to increase the carrying value of the pension obligations by approximately £40 million and vice versa. The impact of a 0.1% increase in the discount rate would be to reduce the value of the pension obligations by approximately £40 million and vice versa.

Provisions for liabilities and charges

The Group establishes provisions for the estimated cost of making redress payments to customers in respect of past product sales, in those cases where the original sales processes are found to have been deficient. The ultimate cost is inherently uncertain and in determining the level of provisions required it is necessary for management to exercise significant judgement. The principal assumptions underlying the provisions relate to the number of cases requiring redress

Notes to the Accounts

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2 Judgements in applying accounting policies and critical accounting estimates (continued)

and the estimated average cost of redress per case; these will be affected by external factors beyond the control of management, such as regulatory actions and the performance of the financial markets. Therefore over time it is possible that adjustments will be necessary to the level of provisions held.

Effective interest rates (EIR)

To calculate the appropriate EIR the Group makes assumptions of the expected lives of financial instruments and the anticipated level of early redemption penalty charges. The most critical assumption is the anticipated level of early redemption penalty charges.

The impact of a 10% increase in the anticipated level of early redemption penalty charges would result in an increase of the value of the loans on the balance sheet of £2.2 million and vice versa.

Taxation

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

3 Interest receivable and similar income

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
On loans fully secured on residential property	**4,481.8**	3,988.5	**4,104.7**	3,640.4
On other loans:				
• Connected undertakings	**-**	-	**402.4**	356.5
• Other	**743.6**	672.9	**612.9**	548.2
On investment securities	**548.4**	574.5	**456.8**	500.9
On other liquid assets	**64.8**	92.7	**14.2**	48.9
Other interest receivable	**1.1**	7.0	**0.1**	5.9
Net expense on financial instruments hedging assets	**(127.8)**	(196.5)	**(127.8)**	(195.2)
Expected return on pension assets (note 41)	**88.0**	72.1	**88.0**	72.0
	5,799.9	5,211.2	**5,551.3**	4,977.6

Included within interest receivable and similar income is interest accrued on impaired financial assets: Group £11.7 million, Society £7.9 million and the unwind of the discount on the impairment provisions: Group £4.1 million, Society £4.1 million (note 13).

4 Interest expense and similar charges

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
On shares held by individuals	**3,125.7**	2,769.0	**3,125.7**	2,769.0
On other shares	**0.3**	0.7	**0.3**	0.7
On subscribed capital	**47.1**	47.3	**47.1**	47.3
On deposits and other borrowings:				
• Subordinated liabilities	**64.8**	48.9	**64.8**	48.9
• Connected undertakings	**-**	-	**129.9**	68.2
• Other	**379.8**	337.9	**258.1**	242.1
Debt securities in issue	**830.0**	707.0	**788.9**	695.0
Foreign exchange differences	**2.3**	1.3	**2.4**	1.3
Net expense on financial instruments hedging liabilities	**35.6**	29.4	**28.6**	29.4
Pension interest cost (note 41)	**80.0**	78.1	**80.0**	78.0
	4,565.6	4,019.6	**4,525.8**	3,979.9

Notes to the Accounts

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5 Fee and commission income

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Mortgage related fees	**20.3**	128.0	**17.1**	113.0
Banking and savings fees	**144.8**	114.3	**144.6**	114.1
General insurance fees	**116.3**	117.1	**94.7**	97.8
Other fees and commissions	**27.9**	24.6	**24.6**	23.9
	309.3	384.0	**281.0**	348.8

From 2006, the vast majority of mortgage related fees are included in interest receivable and similar income. Under the IFRS transitional rules, in 2005 these fees were all included in fee and commission income.

6 Fee and commission expense

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Mortgage related fees	**1.8**	43.7	**1.8**	41.1
Mortgage related commission	**-**	57.8	**-**	50.5
Other fees and commissions	**1.1**	1.3	**1.0**	1.3
	2.9	102.8	**2.8**	92.9

From 2006, the vast majority of mortgage related fees and mortgage related commissions are included in interest receivable and similar income. Under the IFRS transitional rules, in 2005 these fees and commissions were all included in fee and commission expense.

7 Insurance premiums and insurance claims and change in liabilities

	Group 2006 £m	Group 2005 £m
Insurance premiums receivable:		
• Gross	**170.9**	159.1
• Reinsurers' share	**(24.0)**	(17.6)
Fair value gains on insurance assets	**132.0**	55.6
Premiums on insurance contracts and fair value gains on insurance assets	**278.9**	197.1

The Group, as a proxy for policyholders, is required to record taxes on investment income and gains each year. Fair value gains on insurance assets therefore include £8.9 million of gains (2005 – loss of £4.1 million) on policyholder assets which are offset in the taxation charge.

£1,896.9 million (2005 – £1,825.2 million) of insurance and other financial assets at fair value relates to assets of the life insurance business.

	Group 2006 £m	Group 2005 £m
Insurance claims paid:		
• Gross	**193.6**	148.9
• Reinsurers' share	**(10.2)**	(6.9)
Change in provisions for insurance liabilities:		
• Gross	**94.2**	29.6
• Reinsurers' share	**(69.2)**	(19.2)
Insurance claims and change in liabilities	**208.4**	152.4

8 Income from investments

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Income from equity shares	**7.9**	0.3	**0.4**	0.3
Income from shares in subsidiary undertakings	**-**	-	**58.9**	33.3
	7.9	0.3	**59.3**	33.6

Notes to the Accounts

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9 Other operating income

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Other operating income includes:				
• Change in value of in force life insurance contract business	**1.5**	14.1	**-**	-
• Rental income from investment property	**16.2**	16.0	**0.4**	0.6
• Profit on sale of investment properties	**1.0**	1.0	**-**	-
• Profit/(loss) on revaluation of investment properties	**5.9**	(2.8)	**0.9**	0.9

10 Gains from derivatives and hedge accounting

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Gains less losses on derivatives:				
• Derivatives designated as fair value hedges	**(83.3)**	-	**(29.1)**	-
• Other derivatives	**38.6**	-	**38.6**	-
Adjustment for hedge accounting	**54.5**	-	**(0.9)**	-
Other	**1.1**	-	**1.1**	-
	10.9	-	**9.7**	-

11 Administrative expenses

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Employee costs:				
• Wages and salaries	**348.7**	341.9	**324.0**	317.0
• Social security costs	**29.6**	29.6	**27.4**	27.4
• Pension costs – defined benefit plans (note 41)	**81.1**	76.2	**75.2**	72.1
	459.4	447.7	**426.6**	416.5
Other administrative expenses	**414.3**	385.5	**393.6**	372.0
	873.7	833.2	**820.2**	788.5

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Other administrative expenses include:				
• Property operating lease rental	**28.9**	27.2	**27.7**	26.6
• Direct operating expenses on investment properties	**4.5**	4.6	**-**	-
• Other property costs	**37.1**	35.9	**35.8**	35.4
• Postage and communications	**56.6**	55.1	**53.7**	52.0
• Computer costs	**44.5**	43.1	**39.2**	38.6
• Marketing and advertising	**23.7**	21.6	**21.6**	19.2
• Money transmission and other bank costs	**37.8**	37.2	**30.2**	29.6
• Legal and professional	**20.1**	13.1	**13.8**	8.5
• Training, education and other staff costs	**42.4**	39.5	**42.7**	40.7
• Other	**118.7**	108.2	**128.9**	121.4
	414.3	385.5	**393.6**	372.0

The remuneration of the auditors, PricewaterhouseCoopers LLP, is set out below:

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Auditors' remuneration and expenses:				
• Statutory audit fees	**1.1**	0.8	**0.8**	0.6
• Audit related and regulatory fees	**0.5**	0.1	**0.4**	-
	1.6	0.9	**1.2**	0.6
• Further assurance fees	**0.3**	0.3	**0.3**	0.3
• Tax advisory	**0.1**	-	**0.1**	-
• Other	**0.1**	0.1	**0.1**	0.1
	2.1	1.3	**1.7**	1.0

Notes to the Accounts

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11 Administrative expenses (continued)

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 services they are precluded from performing which includes all management consultancy services. All non-audit services, where the fee is expected to exceed a de minimis limit, are subject to pre-approval by the Audit Committee. The increase in the statutory audit fee and the audit related and regulatory fees is due to extra work required in preparation for and following the introduction of IFRS.

12 Employees

	Group		Society	
	2006	2005	**2006**	2005
The average number of persons employed during the year was:				
• Full-time	**11,030**	10,693	**10,182**	9,844
• Part-time	**5,187**	5,066	**4,982**	4,875
	16,217	15,759	**15,164**	14,719
Society				
• Central administration	**7,123**	6,757	**7,123**	6,757
• Branches	**8,041**	7,962	**8,041**	7,962
Subsidiaries	**1,053**	1,040	**-**	-
	16,217	15,759	**15,164**	14,719

Central administration employee numbers include employees engaged in direct customer-facing operations in administrative centres.

13 Impairment provisions on loans and advances to customers

Group	Loans fully secured on residential property Individual £m	Loans fully secured on residential property Collective £m	Loans fully secured on land Individual £m	Loans fully secured on land Collective £m	Other loans Individual £m	Other loans Collective £m	Total Individual £m	Total Collective £m
At 5 April 2005	0.4	30.7	9.7	21.4	-	82.8	10.1	134.9
Charge/(credit) for the year	**1.2**	**(0.3)**	**0.2**	**1.8**	**-**	**73.7**	**1.4**	**75.2**
Amounts written off during the year	**(0.9)**	**(0.3)**	**(0.5)**	**-**	**-**	**(67.6)**	**(1.4)**	**(67.9)**
Amounts recovered during the year	**1.1**	**-**	**0.8**	**-**	**-**	**6.5**	**1.9**	**6.5**
Unwind of discount of provision	**-**	**-**	**(0.6)**	**-**	**-**	**(3.5)**	**(0.6)**	**(3.5)**
At 4 April 2006	**1.8**	**30.1**	**9.6**	**23.2**	**-**	**91.9**	**11.4**	**145.2**

Society	Loans fully secured on residential property Individual £m	Loans fully secured on residential property Collective £m	Loans fully secured on land Individual £m	Loans fully secured on land Collective £m	Other loans Individual £m	Other loans Collective £m	Total Individual £m	Total Collective £m
At 5 April 2005	0.3	22.9	9.7	21.4	-	54.5	10.0	98.8
Charge/(credit) for the year	**0.7**	**(1.3)**	**0.2**	**1.8**	**-**	**47.5**	**0.9**	**48.0**
Amounts written off during the year	**(0.5)**	**(0.2)**	**(0.5)**	**-**	**-**	**(45.7)**	**(1.0)**	**(45.9)**
Amounts recovered during the year	**0.8**	**-**	**0.8**	**-**	**-**	**2.3**	**1.6**	**2.3**
Unwind of discount of provision	**-**	**-**	**(0.6)**	**-**	**-**	**(3.5)**	**(0.6)**	**(3.5)**
At 4 April 2006	**1.3**	**21.4**	**9.6**	**23.2**	**-**	**55.1**	**10.9**	**99.7**

Following the adoption of IAS 39 at 5 April 2005 the existing general and specific provisions under UK GAAP were released to the general reserve. At the same time the collective and individual provisions were set up in accordance with IAS 39, with an adjustment made to the general reserve. The closing balances under UK GAAP at 4 April 2005 were as follows:

Notes to the Accounts

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13 Impairment provisions on loans and advances to customers (continued)

2005	UK GAAP Group £m	UK GAAP Society £m
Loans fully secured on residential property		
• General	99.9	93.0
• Specific	5.9	4.9
Loans fully secured on land		
• General	60.0	59.9
• Specific	7.1	7.1
Other loans		
• General	4.4	1.9
• Specific	50.0	30.5
Total		
• General	164.3	154.8
• Specific	63.0	42.5
	227.3	197.3

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

14 Taxation

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Current Tax:				
• UK corporation tax at 30% (2005 – 30%)	**183.7**	144.4	**124.9**	100.9
• Corporation tax – adjustment in respect of prior years	**4.1**	(0.6)	**3.9**	2.2
	187.8	143.8	**128.8**	103.1
Isle of Man income tax	**0.7**	0.3	**-**	-
Total current tax	**188.5**	144.1	**128.8**	103.1
Deferred tax (note 28):				
• Current year	**(26.5)**	1.1	**(19.2)**	-
• Adjustment in respect of prior periods	**-**	1.7	**0.1**	(0.6)
Total deferred taxation	**(26.5)**	2.8	**(19.1)**	(0.6)
Taxation	**162.0**	146.9	**109.7**	102.5

The Society's tax charge includes payments for the surrender of tax losses to subsidiary undertakings totalling £0.2 million (2005 – receipts in consideration for the surrender of tax losses by subsidiary undertakings totalling £0.4 million).

The Group, as a proxy for policyholders, is required to record taxes on investment income and gains each year. Accordingly, the tax attributable to life insurance policyholder earnings is included in taxation. The tax attributable to policyholder earnings was a charge for the Group of £8.9 million (2005 – income of £4.1 million).

Further information about deferred tax is presented in note 28.

The actual tax charge differs from the theoretical amount that would arise using the standard rate of corporation tax in the UK as follows:

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Profit before tax	**559.2**	513.9	**371.8**	321.1
Tax calculated at a tax rate of 30% (2005 - 30%)	**167.8**	154.2	**111.5**	96.3
Effect of different tax rates in other countries	**(1.7)**	(3.3)	**-**	-
Effect of life subsidiary	**6.3**	(3.4)	**-**	-
(Income)/expenses not taxable/deductible for tax purposes:				
• Building depreciation	**2.5**	1.6	**2.3**	1.6
• Other	**(4.1)**	(2.5)	**4.8**	3.8
Prior year adjustments	**4.1**	1.1	**4.0**	1.6
Utilisation of previously unrecognised tax losses	**(12.9)**	(0.8)	**(12.9)**	(0.8)
Taxation	**162.0**	146.9	**109.7**	102.5

Notes to the Accounts

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15 Segmental reporting

The Group operates entirely in the UK and the Isle of Man and accordingly no geographical analysis has been presented.

The Group reports through the following three business segments:

- Personal Financial Services includes the provision of mortgages (including UCB our specialist lending subsidiary), banking and savings, credit card, unsecured personal lending (through our subsidiary Nationwide Trust), general insurance products, life insurance and unit trust investments.
- Commercial includes all 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. Treasury income generation activities and at.home, Nationwide's subsidiary residential letting agency are also included within this segment.
- Group includes the costs and income associated with managing the Group's capital position and the wholesale funding and liquid asset management of the Group. It also includes rental income and associated property costs on properties surplus to the Society's retail needs and costs which cannot be meaningfully allocated to a business segment.

Income has been attributed to the business segments in which it is generated. Funding costs have been calculated using a funds transfer pricing methodology which reflects the nature of the interest received or paid. The transfer pricing flows are shown as revenues from other segments.

Administrative expenses and depreciation have been allocated to segments based on the resources consumed, except where they cannot be meaningfully allocated in which case they have been included in the Group business segment.

Capital is allocated to each business segment for investment purposes and is based on economic capital principles. No charge has been made for capital.

2006	Personal Financial Services £m	Commercial £m	Group £m	Consolidation adjustments £m	Total £m
Net interest income	**1,116.0**	**898.3**	**(780.0)**	**-**	**1,234.3**
Other income net of claims on insurance contracts	360.7	37.3	12.3	-	410.3
External revenues	1,476.7	935.6	(767.7)	-	1,644.6
Revenue from other segments	(194.7)	(698.7)	893.4	-	-
Total revenue	**1,282.0**	**236.9**	**125.7**	**-**	**1,644.6**
Administrative expenses	783.9	39.8	50.0	-	873.7
Depreciation and amortisation	112.3	3.8	1.4	-	117.5
Impairment losses on loans and advances to customers	73.9	2.7	-	-	76.6
Provisions for liabilities and charges	32.1	-	-	-	32.1
Impairment gains on investment securities	-	(3.6)	-	-	(3.6)
Segment results*	**279.8**	**194.2**	**74.3**	**-**	**548.3**
Gains from derivatives and hedge accounting					10.9
Profit before tax					**559.2**
Taxation					162.0
Profit after tax					**397.2**
Segment assets	171,332.4	17,679.2	17,337.7	(85,971.1)	120,378.2
Unallocated assets					207.8
Total assets					**120,586.0**
Segment liabilities	173,716.9	14,795.7	28,348.0	(102,001.7)	114,858.9
Unallocated liabilities					695.7
Total liabilities					**115,554.6**
Capital expenditure	148.8	26.4	4.4	-	**179.6**

*The Personal Financial Services segment result of £279.8 million differs from the corresponding Underlying result in the Business Review of £270.9 million (see page 8) as the latter excludes the tax attributable to policyholder earnings (note 14).

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15 Segmental reporting (continued)

2005	Personal Financial Services £m	Commercial £m	Group £m	Consolidation adjustments £m	Total £m
Net interest income	977.2	859.1	(644.7)	-	1,191.6
Other income net of claims on insurance contracts	308.5	40.0	9.4	-	357.9
External revenues	1,285.7	899.1	(635.3)	-	1,549.5
Revenue from other segments	(78.0)	(686.1)	764.1	-	-
Total revenue	1,207.7	213.0	128.8	-	1,549.5
Administrative expenses	744.1	38.6	50.5	-	833.2
Depreciation and amortisation	100.5	3.8	2.8	-	107.1
Impairment losses on loans and advances to customers	48.0	(1.4)	-	-	46.6
Provisions for liabilities and charges	46.7	-	-	-	46.7
Impairment losses on investment securities	-	2.0	-	-	2.0
Segment results	268.4	170.0	75.5	-	513.9
Profit before tax					513.9
Taxation					146.9
Profit after tax					367.0
Segment assets	157,698.4	15,602.0	12,951.1	(74,823.2)	111,428.3
Unallocated assets					168.5
Total assets					111,596.8
Segment liabilities	159,321.3	13,027.1	26,701.2	(92,718.9)	106,330.7
Unallocated liabilities					702.5
Total liabilities					107,033.2
Capital expenditure	118.9	12.7	3.1	-	134.7

In accordance with the transition rules on first time adoption of IFRS, the 2005 comparatives do not follow IAS 32, IAS 39 and IFRS 4 but instead follow applicable UK GAAP requirements. Note the corresponding results in the Business Review have been prepared on a pro-forma basis which include the full application of IAS 32, IFRS 4 and the application of IAS 39 excluding gains from derivatives and hedge accounting.

16 Loans and advances to banks

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Placements with banks with a maturity on acquisition of:				
• Less than 3 months	**1,111.5**	520.6	**878.6**	355.4
• More than one year but less than five years	**113.7**	105.1	**-**	-
	1,225.2	625.7	**878.6**	355.4
Mandatory reserve deposits with the Bank of England	**138.8**	125.9	**138.8**	125.9
	1,364.0	751.6	**1,017.4**	481.3

Placements with banks with a maturity on acquisition of less than 3 months are included in the total cash and cash equivalents figure in note 49.

Mandatory reserve deposits with the Bank of England are not available for use in the Group's day to day operations.

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17 Investment securities – available for sale

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Government investment securities	**842.1**	769.0	**691.9**	605.7
Other public sector investment securities	**43.2**	3.7	**-**	-
Private sector investment securities:				
• Listed	**9,395.2**	8,749.3	**8,001.7**	7,631.1
• Unlisted	**2,727.2**	4,623.0	**2,727.4**	4,623.0
	13,007.7	14,145.0	**11,421.0**	12,859.8
Investment securities have remaining maturities as follows:				
• Accrued interest	**75.5**	73.1	**68.1**	67.7
• In not more than one year	**4,617.5**	5,963.1	**4,567.5**	5,918.0
• In more than one year	**8,314.7**	8,108.8	**6,785.4**	6,874.1
	13,007.7	14,145.0	**11,421.0**	12,859.8

On the adoption of IAS 39, financial assets with a fair value of: Group £14,272.1 million, Society £12,948.5 million (carrying value under UK GAAP: Group £14,145.0 million, Society £12,859.8 million) were redesignated from debt securities held at amortised cost to investment securities – available for sale.

Following the adoption of IAS 39 at 5 April 2005, the existing general impairment provision of Group and Society £15.7 million and specific impairment provision of Group and Society £14.1 million under UK GAAP were released to the general reserve. At the same time an impairment loss of Group and Society £14.1 million was recognised in the general reserve. During the year an impairment gain of Group and Society £3.6 million (2005 – Group and Society loss £2.0 million) has been recognised in the income statement as a result of an improvement in the credit quality of a particular treasury investment security. As a consequence a cumulative impairment loss at 4 April 2006 of Group and Society £10.5 million (2005 – Group and Society £29.8 million) has been charged to the general reserve.

£84.6 million (2005 – £101.9 million) of investment securities are pledged as collateral under sale and repurchase agreements.

Investment securities include asset backed securities of £1,169.2 million (2005 – £876.6 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.

The investment securities portfolio contains some highly liquid instruments which have a life of 3 months or less, these securities are classified as cash equivalents in accordance with IAS 7 'Cash Flow Statements'. In the Group accounts £2,133.5 million (2005 – £3,375.0 million) and in the Society accounts £2,133.5 million (2005 – £3,344.9 million) of investment securities are included in the total cash equivalents figure in note 49.

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18 Derivative financial instruments

All derivative financial instruments are held for economic hedging purposes although not all derivatives are designated as hedging instruments under the terms of IAS 39. The table below analyses derivatives between those designated as hedging instruments and those which, whilst in economic hedging relationships, are not designated as hedging instruments:

2006	Contract/notional amount £m	Fair value Assets £m	Fair value Liabilities £m
Derivatives held for hedging			
a) Society			
Derivatives designated as fair value hedges			
• Interest rate swaps	64,204.1	283.7	463.4
Other derivatives			
• Cross currency interest rate swaps	4,213.2	198.7	56.4
• Caps, collars and floors	388.9	0.1	0.1
• Forward foreign exchange	2,550.9	2.5	33.8
• Forward rate agreements	10,550.0	0.4	0.1
• Interest rate futures	6,469.0	0.1	-
• Interest rate swaps	15,313.5	25.8	3.4
• Credit default swaps	1,442.6	-	5.8
	105,132.2	511.3	563.0
b) Subsidiary			
Derivatives designated as fair value hedges			
• Interest rate swaps	1,397.0	-	68.3
Other derivatives			
• Interest rate swaps	1,369.2	29.8	-
Group	107,898.4	541.1	631.3

Group

2006	Contract/notional amount £m	Fair value Assets £m	Fair value Liabilities £m
Derivatives have remaining maturities as follows:			
• In not more than one year	44,448.7	33.9	96.0
• In more than one year	63,449.7	507.2	535.3
	107,898.4	541.1	631.3

Society

2006	Contract/notional amount £m	Fair value Assets £m	Fair value Liabilities £m
Derivatives have remaining maturities as follows:			
• In not more than one year	44,448.7	33.9	96.0
• In more than one year	60,683.5	477.4	467.0
	105,132.2	511.3	563.0

The fair values noted above are stated excluding accrued interest. Accrued income of Group £308.7 million (2005 – £221.8 million) and Society £292.7 million (2005 – £221.8 million) has been included in Accrued income and expenses prepaid (note 27) and accruals of Group £83.4 million (2005 – £159.1 million) and Society £78.3 million (2005 – £159.1 million) have been included in Accruals and deferred income (note 38).

Contract/notional amount indicates the amount outstanding at the balance sheet date and does not represent amounts at risk. The Group did not adopt IAS 32 and IAS 39 until 5 April 2005. The derivative disclosures relating to 4 April 2005 are those required under FRS 13 (the relevant UK GAAP standard at that date) and are included in note 53.

Notes to the Accounts

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19 Fair value adjustment for portfolio hedged risk

In a micro hedge, the carrying value of the hedged item is adjusted for the change in the fair value of the hedged risk. In the case of a portfolio hedge, the adjustment is included in this heading.

20 Loans and advances to customers

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Loans fully secured on residential property	**89,587.4**	82,303.2	**82,821.4**	76,172.3
Loans fully secured on land	**8,050.2**	7,300.5	**7,771.7**	6,819.7
Other loans	**3,592.3**	3,118.2	**1,887.1**	1,654.8
	101,229.9	92,721.9	**92,480.2**	84,646.8
Fair value adjustment for micro hedged risk	**117.7**	-	**117.7**	-
	101,347.6	92,721.9	**92,597.9**	84,646.8

Under the Building Societies Act 1997, 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 loans fully secured on land include Group £578.7 million (2005 – £719.4 million) of loans which are fully secured on residential property, and Society £300.3 million (2005 – £238.9 million) of loans which are fully secured on residential property.

Maturity analysis

Loans and advances to customers have remaining maturities as follows:

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Repayable on demand	**967.6**	723.7	**833.3**	757.9
Other loans and advances by residual maturity repayable:				
• In not more than three months	**794.4**	554.0	**793.2**	552.5
• In more than three months but not more than one year	**2,545.9**	2,331.0	**2,058.4**	1,911.4
• In more than one year but not more than five years	**13,892.0**	11,804.1	**12,631.0**	10,724.4
• In more than five years	**83,186.6**	77,549.3	**76,274.9**	70,910.8
	101,386.5	92,962.1	**92,590.8**	84,857.0
Impairment provision on loans and advances (note 13)	**(156.6)**	(227.3)	**(110.6)**	(197.3)
Deferred mortgage guarantee income	**-**	(12.9)	**-**	(12.9)
Fair value adjustment for micro hedged risk	**117.7**	-	**117.7**	-
	101,347.6	92,721.9	**92,597.9**	84,646.8

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 Group or Society.

Covered bonds

Loans and advances to customers include £1,742.1 million (2005 – nil) for both the Group and Society which have been transferred from the Society to Nationwide Covered Bonds LLP, a bankruptcy remote special purpose vehicle which is consolidated by the Group. The loans secure £1,401.9 million (2005 – nil) of covered bonds issued by the Society. The covered bonds are included in debt securities in issue (note 34). The loans are retained on the Society's balance sheet as the Society substantially retains the risks and rewards relating to the loans.

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21 Investments in equity shares

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
At 5 April 2005	14.9	9.0	1.9	1.7
Movements	**7.1**	5.9	**0.3**	0.2
At 4 April 2006	**22.0**	14.9	**2.2**	1.9

22 Investments in group undertakings

	Shares £m	Loans £m	Total £m
At 5 April 2005	693.7	7,681.1	8,374.8
Additions	**427.2**	**2,201.2**	**2,628.4**
Redemptions/repayments	**-**	**(156.9)**	**(156.9)**
At 4 April 2006	**1,120.9**	**9,725.4**	**10,846.3**

The interests of the Society in its principal subsidiary undertakings, all of which are consolidated, as at 4 April 2006 are set out below:

100% held subsidiary undertakings	Nature of business
First Nationwide	Investment company
Monument (Sutton) Limited	Property rental
Nationwide International Limited*	Offshore deposit taker
Nationwide Investments (No.1) Limited	Investment company
Nationwide Life Limited*	Life insurance
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

*Regulated entities which are subject to regulations which require them to maintain capital at agreed levels and so governs the availability of funds for distribution as dividends.

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

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

The Group has interests in a number of entities which give rise to the risks and rewards that are in substance no different than if they were 100% held subsidiary undertakings. As a consequence, these entities are consolidated in the Group accounts.

Other subsidiary undertakings	Nature of business	Country of registration	Country of operation
Great Eastern Investment Partnership	Investment company	England and Wales	UK
Nationwide Covered Bonds LLP	Mortgage acquisition and guarantor of covered bonds	England and Wales	UK
Moulton Trust S.a.r.l.	Investment company	Luxembourg	Luxembourg
Cobbler Funding Limited	Investment company and issuer of commercial paper	Jersey	Jersey
Cobbler Funding No.1 Limited	Investment company	Jersey	Jersey
Cobbler Funding No.2 Limited	Investment company	Jersey	Jersey
Cobbler Funding No.3 Limited	Investment company	Jersey	Jersey
Cobbler Funding No.4 Limited	Investment company	Jersey	Jersey
Cobbler Funding LLC	Issuer of commercial paper	Delaware, USA	USA

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23 Value of in force life insurance contract business

The value of in force life insurance business has been derived by using the following key assumptions:

- Expected future profits after tax from business currently in force have been discounted at a rate of 7.5% (2005 – 8.0%) per annum, reduced in line with the fall in interest rates during the year.
- Future investment returns of 4.25% (2005 – 4.75%) gross per annum for fixed interest investments and 6.25% (2005 – 6.75%) for equity investments, again reduced in line with the fall in interest rates during the year. The investment return for guaranteed return products is linked to the matching assets.
- Expense inflation rate of 3.5% (2005 – 3.5%) gross is unchanged in line with industry expectations of salary and price inflation.
- Mortality and morbidity for the future based on the Group's and general industry experience and expectation of future trends of the type of business concerned.
- Expenses and withdrawals for the future based on own recent experience of the type of business concerned.

24 Intangible fixed assets

2006	**Computer software**		**Total**
	Externally acquired	**Internally developed**	
Group and Society	**£m**	**£m**	**£m**
Cost			
At 5 April 2005	112.3	20.7	133.0
Additions	**69.2**	**9.5**	**78.7**
Disposals	**(39.2)**	**-**	**(39.2)**
At 4 April 2006	**142.3**	**30.2**	**172.5**
Amortisation			
At 5 April 2005	80.2	8.6	88.8
Charge for the year	**36.1**	**6.3**	**42.4**
Disposals	**(39.2)**	**-**	**(39.2)**
At 4 April 2006	**77.1**	**14.9**	**92.0**
Net book value			
At 4 April 2006	**65.2**	**15.3**	**80.5**

2005	Computer software		Total
	Externally acquired	Internally developed	
Group and Society	£m	£m	£m
Cost			
At 5 April 2004	104.3	11.7	116.0
Additions	8.0	9.0	17.0
At 4 April 2005	112.3	20.7	133.0
Amortisation			
At 5 April 2004	56.4	3.2	59.6
Charge for the year	23.8	5.4	29.2
At 4 April 2005	80.2	8.6	88.8
Net book value			
At 4 April 2005	32.1	12.1	44.2

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>>> 25 Property, plant and equipment

Group	Branches and non specialised buildings £m	Specialised administration buildings £m	Short leasehold buildings £m	Total land and buildings £m	Plant and machinery £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation							
At 5 April 2005	282.5	103.0	37.5	423.0	103.9	769.6	1,296.5
Additions	**5.7**	**0.5**	**1.2**	**7.4**	**15.9**	**54.5**	**77.8**
Revaluation	**25.1**	**-**	**-**	**25.1**	**-**	**-**	**25.1**
Disposals	**-**	**-**	**(13.6)**	**(13.6)**	**-**	**(4.4)**	**(18.0)**
At 4 April 2006	**313.3**	**103.5**	**25.1**	**441.9**	**119.8**	**819.7**	**1,381.4**
Depreciation							
At 5 April 2005	-	41.4	29.1	70.5	78.4	527.6	676.5
Charge for the year	**2.4**	**3.6**	**1.2**	**7.2**	**10.6**	**57.3**	**75.1**
Revaluation	**(2.4)**	**-**	**-**	**(2.4)**	**-**	**-**	**(2.4)**
Disposals	**-**	**-**	**(13.6)**	**(13.6)**	**-**	**(2.2)**	**(15.8)**
At 4 April 2006	**-**	**45.0**	**16.7**	**61.7**	**89.0**	**582.7**	**733.4**
Net book value							
At 4 April 2006	**313.3**	**58.5**	**8.4**	**380.2**	**30.8**	**237.0**	**648.0**

Group	Branches and non specialised buildings £m	Specialised administration buildings £m	Short leasehold buildings £m	Total land and buildings £m	Plant and machinery £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation							
At 5 April 2004	252.0	102.9	36.0	390.9	95.2	681.4	1,167.5
Additions	8.5	0.1	1.8	10.4	9.2	89.2	108.8
Revaluation	23.4	-	-	23.4	-	-	23.4
Disposals	(1.4)	-	(0.3)	(1.7)	(0.5)	(1.0)	(3.2)
At 4 April 2005	282.5	103.0	37.5	423.0	103.9	769.6	1,296.5
Depreciation							
At 5 April 2004	-	37.9	27.8	65.7	71.7	464.8	602.2
Charge for the year	2.0	3.5	1.6	7.1	7.2	63.6	77.9
Revaluation	(2.0)	-	-	(2.0)	-	-	(2.0)
Disposals	-	-	(0.3)	(0.3)	(0.5)	(0.8)	(1.6)
At 4 April 2005	-	41.4	29.1	70.5	78.4	527.6	676.5
Net book value							
At 4 April 2005	282.5	61.6	8.4	352.5	25.5	242.0	620.0

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25 Property, plant and equipment (continued)

Society	Branches and non specialised buildings £m	Specialised administration buildings £m	Short leasehold buildings £m	Total land and buildings £m	Plant and machinery £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation							
At 5 April 2005	271.2	103.0	37.0	411.2	102.4	739.5	1,253.1
Additions	**5.7**	**0.5**	**1.2**	**7.4**	**15.6**	**53.1**	**76.1**
Revaluation	**23.8**	**-**	**-**	**23.8**	**-**	**-**	**23.8**
Disposals	**-**	**-**	**(13.6)**	**(13.6)**	**-**	**(4.2)**	**(17.8)**
At 4 April 2006	**300.7**	**103.5**	**24.6**	**428.8**	**118.0**	**788.4**	**1,335.2**
Depreciation							
At 5 April 2005	-	41.4	28.7	70.1	77.4	503.3	650.8
Charge for the year	**2.1**	**3.6**	**1.2**	**6.9**	**10.4**	**55.3**	**72.6**
Revaluation	**(2.1)**	**-**	**-**	**(2.1)**	**-**	**-**	**(2.1)**
Disposals	**-**	**-**	**(13.6)**	**(13.6)**	**-**	**(2.0)**	**(15.6)**
At 4 April 2006	**-**	**45.0**	**16.3**	**61.3**	**87.8**	**556.6**	**705.7**
Net book value							
At 4 April 2006	**300.7**	**58.5**	**8.3**	**367.5**	**30.2**	**231.8**	**629.5**

Society	Branches and non specialised buildings £m	Specialised administration buildings £m	Short leasehold buildings £m	Total land and buildings £m	Plant and machinery £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation							
At 5 April 2004	240.5	102.9	35.4	378.8	93.5	652.4	1,124.7
Additions	8.4	0.1	1.9	10.4	9.0	87.3	106.7
Revaluation	23.8	-	-	23.8	-	-	23.8
Disposals	(1.5)	-	(0.3)	(1.8)	(0.1)	(0.2)	(2.1)
At 4 April 2005	271.2	103.0	37.0	411.2	102.4	739.5	1,253.1
Depreciation							
At 5 April 2004	-	37.9	27.4	65.3	70.4	442.0	577.7
Charge for the year	1.7	3.5	1.6	6.8	7.0	61.3	75.1
Revaluation	(1.7)	-	-	(1.7)	-	-	(1.7)
Disposals	-	-	(0.3)	(0.3)	-	-	(0.3)
At 4 April 2005	-	41.4	28.7	70.1	77.4	503.3	650.8
Net book value							
At 4 April 2005	271.2	61.6	8.3	341.1	25.0	236.2	602.3

Branches and non specialised buildings are included at fair value. Valuations, performed by independent surveyors, consist of a mixture of full and interim valuations and were undertaken as at 4 April 2006 in accordance with the Appraisal and Valuation manual published by the Royal Institution of Chartered Surveyors. Valuations are based on active market prices.

Specialised administration buildings and short leasehold buildings are included at cost less accumulated depreciation.

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26 Investment properties

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
At 5 April 2005	242.6	244.8	9.3	8.2
Additions from acquisitions	**18.8**	7.7	**-**	-
Additions from subsequent expenditure	**4.3**	1.2	**-**	0.2
Revaluation	**17.7**	(2.8)	**0.9**	0.9
Disposals	**(4.3)**	(8.3)	**-**	-
At 4 April 2006	**279.1**	242.6	**10.2**	9.3

Investment properties are carried at fair value. The valuations are undertaken by independent valuers in accordance with the Appraisal and Valuation manual published by the Royal Institution of Chartered Surveyors. Valuations are based on active market prices.

27 Accrued income and expenses prepaid

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Accruals relating to derivative financial instruments	**308.7**	221.8	**292.7**	221.8
Amounts owed by subsidiary undertakings	**-**	-	**201.7**	140.4
Other	**108.1**	144.9	**66.2**	101.0
	416.8	366.7	**560.6**	463.2

28 Deferred tax assets

Deferred tax is provided in full on temporary differences under the liability method at the standard UK corporation tax rate of 30% (2005 – 30%).

The movements on the deferred tax account are as follows:

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
At 4 April 2005	81.9		127.1	
Adoption of IFRS 4 and IAS 39	**(1.3)**		**(3.2)**	
Brought forward at 5 April 2005	**80.6**	122.9	**123.9**	164.8
Income statement income/(charge)	**26.5**	(2.8)	**19.1**	0.6
Future consortium relief	**11.6**	-	**11.6**	-
Available for sale investments – net fair value gain	**(0.4)**	-	**3.2**	-
Property revaluation	**(10.1)**	(6.8)	**(10.1)**	(6.8)
Retirement benefit obligations	**1.8**	(31.4)	**1.8**	(31.5)
Taxation on items through equity	**(8.7)**	(38.2)	**(5.1)**	(38.3)
At 4 April 2006	**110.0**	81.9	**149.5**	127.1

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28 Deferred tax assets (continued)

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

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Retirement benefit obligations	**108.2**	118.7	**108.2**	118.6
Provisions for loan impairment	**35.4**	58.3	**20.1**	47.5
Life insurance business	**(32.4)**	(32.3)	**-**	-
Other provisions	**61.0**	(0.5)	**65.7**	(0.8)
Accelerated tax depreciation	**8.7**	(1.3)	**8.8**	(0.6)
Available for sale investments	**(22.7)**	-	**(17.0)**	-
Property revaluation	**(60.5)**	(61.0)	**(48.6)**	(37.6)
Tax losses carried forward	**12.3**	-	**12.3**	-
	110.0	81.9	**149.5**	127.1

Deferred tax assets are all anticipated to be recoverable after 1 year.

The deferred tax charge/(credit) in the income statement comprises the following temporary differences (note 14):

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Accelerated tax depreciation	**(10.0)**	(1.8)	**(9.4)**	(1.9)
Retirement benefit obligations	**12.4**	4.4	**12.3**	4.4
Provisions for loan impairment	**(3.0)**	1.4	**(0.3)**	0.4
Other	**(13.6)**	(1.3)	**(9.4)**	(1.3)
Tax losses carried forward	**(12.3)**	-	**(12.3)**	-
Other temporary differences	**-**	0.1	**-**	(2.2)
	(26.5)	2.8	**(19.1)**	(0.6)

29 Other assets

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Reinsurance assets (note 35)	**245.0**	175.8	**-**	-
Other	**164.2**	116.9	**65.0**	72.7
	409.2	292.7	**65.0**	72.7

30 Shares

	Group & Society	
	2006 £m	2005 £m
Held by individuals	**80,910.2**	72,575.5
Other shares	**8.4**	18.6
	80,918.6	72,594.1
Shares are repayable from the balance sheet date in the ordinary course of business as follows:		
Accrued interest	**549.4**	574.8
Repayable on demand	**76,008.7**	69,315.3
Other shares by residual maturity repayable:		
• In not more than three months	**934.6**	392.3
• In more than three months but not more than one year	**2,125.8**	1,908.3
• In more than one year but not more than five years	**1,300.1**	403.4
	80,918.6	72,594.1

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31 Deposits from banks

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Deposits from banks are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**13.5**	18.4	**13.5**	18.4
Repayable on demand	**470.2**	292.0	**468.4**	292.0
Other amounts owed to banks with residual maturity repayable:				
• In not more than three months	**953.3**	969.7	**882.5**	948.7
• In more than three months but not more than one year	**427.8**	485.7	**306.0**	344.1
• In more than one year but not more than five years	**732.6**	650.8	**34.8**	34.1
• In more than five years	**100.0**	36.7	**100.0**	10.0
	2,697.4	2,453.3	**1,805.2**	1,647.3

Deposits from banks include £84.6 million (2005 – £101.9 million) in respect of sale and repurchase agreements.

32 Other deposits

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Amounts owed to subsidiary undertakings	**-**	-	**4,063.7**	1,788.0
Other	**3,161.4**	2,802.4	**3,161.4**	2,802.1
	3,161.4	2,802.4	**7,225.1**	4,590.1
Other deposits are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**26.3**	33.3	**31.3**	37.5
Repayable on demand	**0.8**	3.7	**3,880.9**	1,608.8
Other amounts owed to depositors with residual maturity repayable:				
• In not more than three months	**1,907.4**	1,746.3	**1,929.4**	1,780.0
• In more than three months but not more than one year	**1,180.2**	939.4	**1,236.4**	1,015.9
• In more than one year but not more than five years	**46.7**	79.7	**147.1**	147.9
	3,161.4	2,802.4	**7,225.1**	4,590.1

33 Due to customers

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Amounts due to customers are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**11.5**	7.7	**4.4**	4.9
Repayable on demand	**2,069.6**	1,711.0	**936.7**	930.8
Other amounts owed to customers with residual maturity repayable:				
• In not more than three months	**354.3**	384.0	**-**	-
• In more than three months but not more than one year	**122.6**	85.5	**-**	-
• In more than one year but not more than five years	**50.3**	68.8	**-**	-
	2,608.3	2,257.0	**941.1**	935.7

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34 Debt securities in issue

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Certificates of deposit	**6,780.9**	7,802.4	**5,528.6**	7,725.6
Fixed and floating rate notes	**13,937.4**	13,479.1	**13,937.4**	13,479.1
Other debt securities	**223.6**	1,096.1	**223.6**	218.1
	20,941.9	22,377.6	**19,689.6**	21,422.8
Fair value adjustment for micro hedged risk	**(174.3)**	-	**(117.9)**	-
	20,767.6	22,377.6	**19,571.7**	21,422.8
Debt securities in issue are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**154.6**	177.5	**154.6**	177.5
Other debt securities in issue with residual maturity repayable:				
• In not more than one year	**11,063.9**	10,277.9	**9,897.1**	9,400.0
• In more than one year	**9,723.4**	11,922.2	**9,637.9**	11,845.3
	20,941.9	22,377.6	**19,689.6**	21,422.8
Fair value adjustment for micro hedged risk	**(174.3)**	-	**(117.9)**	-
	20,767.6	22,377.6	**19,571.7**	21,422.8

Debt securities in issue include Group and Society £1,401.9 million (2005 – nil) of covered bonds secured on certain loans and advances to customers (note 20).

35 Insurance contract liabilities

	Group 2006 £m	Group 2005 £m
Insurance contract liabilities:		
• Gross	**1,190.5**	1,132.1
• Reinsurers' share (note 29)	**(245.0)**	(175.8)
Net insurance contract liabilities	**945.5**	956.3

The Group offers various insurance products including critical illness and term assurance. Certain liabilities are reinsured.

Under the terms of a Memorandum of Understanding entered into between leading members of the life insurance and bancassurance sectors, the Association of British Insurers and the UK Accounting Standards Board, insurers are encouraged to provide certain disclosures that would have been required by UK GAAP in their financial statements. The Group is providing these additional disclosures.

Regulatory capital requirements of insurance contract business

The Society's life insurance subsidiary, Nationwide Life, is regulated by the Financial Services Authority (FSA) and as a condition of being able to transact business as a life insurer, is required to hold a minimum level of capital which is calculated with respect to the mix of business written. In calculating these capital requirements, the FSA requires certain adjustments to be made in the valuation of assets and liabilities in comparison to those used in the financial statements.

Nationwide Life also regularly prepares an Individual Capital Assessment (ICA) which is an assessment of the amount of capital required to ensure that it can cover its liabilities to policyholders to a given level of confidence. Resources are maintained to cover the higher of the ICA and FSA requirements.

Notes to the Accounts

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35 Insurance contract liabilities (continued)

Details of the life insurance subsidiary's regulatory capital are as follows:

	2006 £m	2005 £m
Shareholder's funds	**304.7**	282.5
Adjustments to assets	**(94.5)**	(96.0)
Available capital to meet regulatory requirements	**210.2**	186.5

The numbers quoted in the above table for the current year are based on management's current expectations in advance of completion of the annual financial return to the FSA. The 2005 numbers have been restated to reflect the final position as reported in the prior year annual financial return to the FSA.

The relevant capital requirement is the minimum solvency requirement determined in accordance with FSA regulations. The available capital has been calculated after deducting liabilities that include additional prudential margins. At 31 March 2006, the available capital of £210.2 million (2005 – £186.5 million) was 285% (2005 – 273%) of the capital requirement of £73.8 million (2005 – £68.4 million) in comparison to management's target minimum of 200%. The level of available capital is sensitive to certain key assumptions used in the calculation of life insurance contract liabilities, the most significant of which are mortality risk (in respect of term assurances) and morbidity risk (in respect of critical illness policies or term assurances with critical illness acceleration).

Options and guarantees

The Group's life insurance products contain certain options and guarantees.

A significant proportion of insurance contract business is represented by guaranteed equity bonds. These bonds, which are normally offered for a fixed period of five or six years, offer the policyholder the opportunity to invest in equity markets with the added benefit of a guarantee that, on maturity of the bond, it will return at least the minimum of the premium invested plus a pre-defined portion of the growth in the relevant equity index. On death of the policyholder, the contract guarantees to return the higher of the premium received or the premium plus relevant equity growth, plus a death benefit of 1%. The exposure to the market risk is matched by an asset designed specifically for the guaranteed equity bond. As a result there is little sensitivity to market movements.

In order to minimise exposure to the underlying investment or liquidity risk, the life insurance subsidiary purchases bespoke structured products which are designed to deliver, at maturity, a return which exactly matches the benefits payable to the policyholder. It further reduces its exposure to credit risk (i.e. the failure of the counterparty to deliver the appropriate funds) by use of a collateral arrangement.

The life insurance subsidiary measures its liabilities under these contracts based on the fair value of the underlying investments together with a provision in respect of margins for mortality, expenses, tax and counterparty risk.

36 Other liabilities

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
Third party income tax withheld	**204.6**	179.3	**204.5**	179.3
Consortium relief	**11.6**	-	**11.6**	-
Other liabilities	**299.6**	225.6	**134.0**	129.7
	515.8	404.9	**350.1**	309.0

37 Provisions for liabilities and charges

	Group 2006 £m	Society 2006 £m
At 5 April 2005	49.0	41.1
Provisions utilised	**(40.8)**	**(40.6)**
Charge for the year	**32.1**	**28.5**
At 4 April 2006	**40.3**	**29.0**

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37 Provisions for liabilities and charges (continued)

Provisions have been made in respect of various customer claims including potential claims on endowment policies as described below.

The Group sold a substantial number of endowment policies to the Group'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 provision includes the estimate of the Group's liability for such claims.

38 Accruals and deferred income

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Accruals relating to derivative financial instruments	**83.4**	159.1	**78.3**	159.1
Deferred income recognition on unit trust products	**3.9**	10.3	**-**	-
Interest accrued on subordinated liabilities	**18.4**	9.0	**18.4**	9.0
Interest accrued on subscribed capital	**5.2**	5.2	**5.2**	5.2
Accruals relating to investment properties	**11.4**	-	**-**	-
Other	**191.2**	189.8	**169.0**	181.7
	313.5	373.4	**270.9**	355.0

39 Subordinated liabilities

	Group & Society	
	2006 £m	2005 £m
Subordinated Floating Rate Notes due 2013(€400m)	**279.4**	274.1
5 1/4% Subordinated Notes due 2014 ($225m)	**128.0**	120.2
3 3/8% Subordinated Notes due 2015 (€750m)	**523.9**	513.9
5% Subordinated Notes due 2015 ($400m)	**227.7**	213.7
5 1/4% Subordinated Notes due 2018 (£)	**200.0**	200.0
8 5/8% Subordinated Notes due 2018 (£)	**125.0**	125.0
	1,484.0	1,446.9
Fair value adjustment for micro hedged risk	**(30.7)**	-
Unamortised premiums and issue costs	**(7.0)**	(7.1)
	1,446.3	1,439.8

All of the Society's subordinated liabilities are unsecured. The Society may, with the prior consent of the FSA, redeem some of the subordinated notes early as follows:

- All (but not some only) of the Floating Rate Notes due 2013 at par (100%) on 11 April 2008, by 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 the 11 April 2008 the initial interest margin of 0.6% over Euribor will increase by a further 0.5%.
- All (but not some only) of the 3 3/8% Notes due 2015 at par (100%) on 17 August 2010 (or each subsequent interest payment date), by giving not less than 15 nor more than 30 days notice to the holders. In the event the Society does not redeem the notes early the interest rate will convert to a floating rate equal to the aggregate of 3 month Euribor and 0.76%.
- All (but not some only) of the 5 1/4% Notes due 2018 at par (100%) on 12 February 2013, by 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.
- All or some of the 8 5/8% Notes at the higher of par (100%) or the benchmark 8 3/4% 2017 Gilt, by 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 Permanent Interest Bearing 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.

Notes to the Accounts

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40 Subscribed capital

	Group & Society 2006 £m	2005 £m
7.791% 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**	400.0
	700.0	700.0
Fair value adjustment for micro hedged risk	**49.4**	-
Unamortised premiums and issue costs	**(8.2)**	(7.8)
	741.2	692.2

All Permanent Interest Bearing Shares (PIBS) are unsecured and denominated in Sterling. The first two tranches were issued on 13 March 2000. Total net proceeds of the issue were £295.7 million. The third issue of £400.0 million was issued on 6 February 2004. The net proceeds of the issue were £395.0 million.

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 FSA. 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 5 year benchmark Gilt rate.

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.

41 Retirement benefit obligations

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Present value of funded obligations	**1,826.4**	1,473.8	**1,824.0**	1,472.0
Fair value of plan assets	**1,542.8**	1,131.2	**1,541.0**	1,130.0
	283.6	342.6	**283.0**	342.0
Present value of unfunded obligations	**7.0**	4.6	**7.0**	4.6
Total pension liabilities	**290.6**	347.2	**290.0**	346.6
Post retirement healthcare	**3.6**	4.4	**3.6**	4.4
	294.2	351.6	**293.6**	351.0

The Group operates several defined benefit pension arrangements. The majority of the Group's employees are members of the Nationwide Pension Fund. The Group also operates other pension arrangements for certain current and former Directors and Officers, as well as for one subsidiary company.

The amounts recognised in the income statement are as follows:

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Current service cost	**83.3**	75.7	**77.4**	71.6
Past service cost	**-**	2.0	**-**	2.0
	83.3	77.7	**77.4**	73.6
Capitalised as intangible fixed assets	**(2.2)**	(1.5)	**(2.2)**	(1.5)
Included in employee costs (note 11)	**81.1**	76.2	**75.2**	72.1
Pension interest cost (note 4)	**80.0**	78.1	**80.0**	78.0
Expected return on assets (note 3)	**(88.0)**	(72.1)	**(88.0)**	(72.0)
	73.1	82.2	**67.2**	78.1

Notes to the Accounts

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41 Retirement benefit obligations (continued)

Changes in the present value of defined benefit pension obligations are as follows:

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
At 5 April 2005	1,478.4	1,413.5	1,476.6	1,411.9
Current service cost	**83.3**	75.7	**77.4**	71.6
Past service cost	**-**	2.0	**-**	2.0
Pension interest cost	**80.0**	78.1	**80.0**	78.0
Employee contributions	**2.0**	9.0	**2.0**	9.0
Subsidiary undertakings contributions	**-**	-	**5.8**	4.0
Actuarial losses/(gains)	**212.3**	(75.9)	**211.8**	(75.9)
Benefits paid	**(22.6)**	(24.0)	**(22.6)**	(24.0)
At 4 April 2006	**1,833.4**	1,478.4	**1,831.0**	1,476.6

The Group does not charge the net defined benefit cost to subsidiary companies that participate in the Nationwide Pension Fund. Consequently, the cost to the subsidiary companies equals the contributions payable to the Fund.

Changes in the fair value of plan assets are as follows:

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
At 5 April 2005	1,131.2	972.4	1,130.0	971.5
Expected return on assets	**88.0**	72.1	**88.0**	72.0
Actuarial gains	**205.4**	28.5	**204.9**	28.4
Contributions by employer	**138.8**	73.2	**132.9**	69.1
Employee contributions	**2.0**	9.0	**2.0**	9.0
Subsidiary undertakings contributions	**-**	-	**5.8**	4.0
Benefits paid	**(22.6)**	(24.0)	**(22.6)**	(24.0)
At 4 April 2006	**1,542.8**	1,131.2	**1,541.0**	1,130.0

The major categories of plan assets for the pension funds are as follows:

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
UK equities	**571.6**	425.7	**570.1**	425.1
Non-UK equities	**592.1**	422.2	**592.1**	421.8
Bonds	**312.8**	272.3	**312.7**	272.2
Property and cash	**66.3**	11.0	**66.1**	10.9
	1,542.8	1,131.2	**1,541.0**	1,130.0

None of the Funds' assets are invested in the Nationwide Group (4 April 2005 – nil).

The amounts recognised in respect of pension obligations in the statement of recognised income and expense are as follows:

	Group		Society	
	2006 £m	2005 £m	2006 £m	2005 £m
Cumulative actuarial gains at 5 April 2005	104.4	-	104.3	-
Actuarial (loss)/gains in the year*	**(6.9)**	104.4	**(6.9)**	104.3
Cumulative actuarial gains at 4 April 2006	**97.5**	104.4	**97.4**	104.3

*In addition an actuarial gain of Group and Society £0.8 million (2005 – £0.5 million) was recognised in respect of post retirement healthcare.

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>>> 41 Retirement benefit obligations (continued)

Amounts for the current and the previous year are as follows:

	Group		Society	
	2006 £m	2005 £m	**2006 £m**	2005 £m
Experience gains on plan liabilities	**8.0**	23.0	**8.0**	23.0
Changes in actuarial assumptions	**(220.3)**	52.9	**(219.8)**	52.9
Actuarial (losses)/gains on plan liabilities	**(212.3)**	75.9	**(211.8)**	75.9
Experience gains on plan assets	**205.4**	28.5	**204.9**	28.4

The principal actuarial assumptions used were as follows:

	Group & Society	
	2006 %	2005 %
Discount rate	**5.0**	5.5
Expected return on plan assets	**7.0**	7.4
Future salary increases*	**4.6**	4.7
Future pension increases	**2.7**	2.6
Inflation	**2.8**	2.7

*Plus additional 1.2% per annum until 4 April 2007.

The assumptions on mortality are determined by the actuarial tables known as PA92C2006 Short Cohort for current pensioners and PA92C2016 Short Cohort for future pensioners. The assumptions are illustrated by the following years of life expectancy at age 60:

	2006	2005
Retired members		
• Males	**24.6**	24.4
• Females	**27.5**	27.3
Non-retired members		
• Males	**25.6**	25.5
• Females	**28.4**	28.3

The expected rate of return on plan assets is determined for each asset class by reference to the Gilt (government bond) rate at 4 April 2006.

The Group estimates that its contributions to the pension funds during the year ended 4 April 2007, including special contributions of £100 million, will be £200 million.

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42 General reserve

Movements in general reserves were as follows:

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
At 4 April 2005	4,460.6		3,479.1	
Effective interest basis	**(8.7)**		**(5.3)**	
Available for sale assets	**16.0**		**12.4**	
Derivatives and hedging	**(94.4)**		**(94.4)**	
Derecognition of financial liabilities	**(33.1)**		**(33.1)**	
Insurance	**(3.3)**		**-**	
Loan impairment and suspended interest	**86.0**		**92.2**	
Tax	**9.6**		**5.8**	
Brought forward at 5 April 2005	**4,432.7**	4,019.1	**3,456.7**	3,186.2
Profit for the year	**397.2**	367.0	**262.1**	218.6
Actuarial (loss)/gain on retirement benefit obligations	**(6.1)**	104.9	**(6.1)**	104.8
Tax on actuarial (loss)/gain on retirement benefit obligations	**1.8**	(31.4)	**1.8**	(31.5)
Transfer from revaluation reserve	**-**	1.0	**-**	1.0
At 4 April 2006	**4,825.6**	4,460.6	**3,714.5**	3,479.1

The above adjustments between 4 April 2005 and 5 April 2005 have been made in accordance with the transitional rules of IFRS, whereby adjustments necessary to comply with IAS 32, IAS 39 and IFRS 4 were made as at 5 April 2005 rather than in the comparative year. Further details about the adjustments can be found in note 52 and at www.nationwide.co.uk/about_nationwide/results_accounts/.

43 Revaluation reserve

Movements in revaluation reserves were as follows:

	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Brought forward at 5 April 2005	103.0	85.9	102.9	85.8
Revaluation increase on land and buildings	**24.1**	24.9	**24.0**	24.9
(Increase) in deferred tax liability on the revaluation of land and buildings	**(10.1)**	(6.8)	**(10.1)**	(6.8)
Transfer (to) general reserve	**-**	(1.0)	**-**	(1.0)
At 4 April 2006	**117.0**	103.0	**116.8**	102.9

44 Available for sale reserve

Movements in available for sale reserves were as follows:

	Group 2006 £m	Society 2006 £m
At 4 April 2005	-	-
Available for sale assets on adoption of IAS 39	**70.8**	**29.1**
Tax on adoption of IAS 39	**(22.2)**	**(20.2)**
Brought forward at 5 April 2005	**48.6**	**8.9**
Net gains from changes in fair value	**59.8**	**53.3**
Amounts transferred to income statement on disposal and impairment	**(4.5)**	**(4.4)**
(Increase) in tax liability	**(15.1)**	**(11.5)**
At 4 April 2006	**88.8**	**46.3**

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45 Memorandum items - Commitments

2006	Group Contract amount £m	Group Credit risk weighted amount £m	Society Contract amount £m	Society Credit risk weighted amount £m
Irrevocable undrawn loan facilities	**3,279.4**	**775.2**	**3,085.2**	**720.8**
Unpaid share capital of subsidiary company	**-**	**-**	**28.3**	**28.3**
Undrawn formal standby facilities, credit lines and other commitments to lend	**25.0**	**2.5**	**25.0**	**2.5**
	3,304.4	**777.7**	**3,138.5**	**751.6**

2005	Group Contract amount £m	Group Credit risk weighted amount £m	Society Contract amount £m	Society Credit risk weighted amount £m
Irrevocable undrawn loan facilities	2,762.3	750.5	2,321.5	640.3
Unpaid share capital of subsidiary company	-	-	28.3	28.3
Undrawn formal standby facilities, credit lines and other commitments to lend	49.0	4.9	49.0	4.9
	2,811.3	755.4	2,398.8	673.5

46 Financial commitments

Capital commitments	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Capital expenditure contracted for but not provided for in the Accounts	**25.2**	24.8	**21.7**	15.9

Leasing commitments	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
At the balance sheet date, commitments under operating leases relating to land and buildings were as follows:				
Amounts falling due:				
• Within one year	**22.7**	22.3	**22.3**	21.7
• Between one and five years	**61.9**	64.1	**60.9**	62.1
• After five years	**95.2**	94.0	**92.0**	90.6
	179.8	180.4	**175.2**	174.4
At the balance sheet date, subleasing payments receivable under non-cancellable subleases	**8.0**	8.0	**8.0**	7.7
At the balance sheet date, future minimum lease payments receivable under non-cancellable operating leases were as follows:				
Amounts falling due:				
• Within one year	**4.6**	5.7	**4.6**	5.6
• Between one and five years	**13.2**	12.3	**13.1**	12.1
• After five years	**16.0**	14.9	**15.8**	14.9
	33.8	32.9	**33.5**	32.6

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47 Financial instruments

Strategy in using financial instruments

Financial instruments incorporate the vast majority of the Group and Society's assets and liabilities. Given the dominant position of the Society within the Group structure, the term 'Group' is used in the remainder of this note to cover the activities of both Group and Society. Furthermore since the risks of the organisation are managed on a Group basis, the risk disclosures have been presented below only on a consolidated basis.

The Group accepts deposits from customers at both fixed and floating interest rates for various periods and seeks to earn an interest margin by investing these funds in high quality assets – predominantly mortgages. The Group seeks to increase those margins by consolidating short term funds and lending for longer periods at higher rates whilst maintaining sufficient liquidity to meet all claims which might fall due. The Group does not trade in financial instruments.

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.

The principal derivatives used in balance sheet risk management are interest rate swaps, forward rate agreements, interest rate options, cross-currency interest rate swaps, rate futures, foreign exchange contracts and credit derivatives. Derivatives are used to hedge 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. In most cases derivatives are transacted by the Society on behalf of the rest of the Group. Group risk exposures are recorded on the Society's information systems and monitored accordingly.

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 an integrated approach to risk management.

Activity	Risk	Type of derivative instrument used
Fixed rate savings products and funding activities in Sterling 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 swaps

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 Nationwide Investment 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.

The accounting policy for derivatives and hedge accounting is described in the Statement of Accounting Policies. Where possible fair value hedge accounting is employed but no use is made of cash flow hedge accounting.

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47 Financial instruments (continued)

Control of derivatives

The Assets and Liabilities Committee (ALCO) is responsible for setting limits over the use of derivative products for managing exposure to interest rates, foreign exchange rates and equity indices. The Credit Committee sets Group credit policy and regularly monitors and reviews credit exposures arising in all aspects of Group 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. Credit exposures arising on derivative contracts with certain counterparties are collaterised with cash deposits, to mitigate credit exposures. All Group derivatives activity is contracted with OECD financial institutions.

The principal financial risks to which the Group is exposed are interest rate, credit, foreign exchange, liquidity and insurance risk. Each of these is considered below. Additional information on risk management and control is included in the Business Review.

Interest rate 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 derivative instruments and cash instruments such as loans, deposits and bonds.

The Group does not run a trading book and therefore does not have the type of higher risk exposure run by many banking institutions. Given our policy of hedging fixed rate assets and liabilities back to floating rate, outright interest rate risk arises mainly from the Board's decision to invest the Group's reserves according to a specified fixed rate maturity profile. The level of risk can deviate from this – subject to limits – in particular as a result of decisions made by the Group's Treasury department to temporarily deviate from the benchmark profile in the light of market conditions.

The Group uses three metrics to monitor interest rate risk and details of these are set out below. The limits around these three metrics have been set by ALCO and reflect the Group's low risk appetite.

Value at Risk (VaR). This is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. In its day to day monitoring Nationwide uses a 10 day horizon and a 99% confidence level.

The VaR model used by Nationwide incorporates underlying risk factors based on interest rate volatilities and correlations. Potential movements in market prices are calculated by reference to market data from the last two years equally weighted. Exposures against limits are reviewed daily by management. Actual outcomes are monitored from time to time to test the validity of the assumptions and parameters/factors used in the VaR calculation.

Although a valuable guide to risk, VaR needs to be viewed in the context of the following limitations:

- historic data is not necessarily a good guide to future events;
- the use of a 99% confidence level, by definition, does not take account of changes in value that might occur beyond this level of confidence. The VaR numbers may not encompass all potential events, particularly those that are extreme in nature;
- VaR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

Sensitivity analysis (PV01 sensitivity). This is used to assess the change in value of the Group's current net worth against a one basis point (0.01%) parallel rise in interest rates. As is the case with VaR, this analysis is done on a daily basis separately for each currency (but with the main risk arising from Sterling exposures) and in aggregate.

Stress testing (PV200 sensitivity). This is calculated in a similar manner to PV01 but against a much more severe 200 basis point (2.0%) parallel rise in interest rates. Both PV01 and PV200 numbers are generated daily.

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47 Financial instruments (continued)

The current limits and average exposures for Sterling through the reporting period are as follows:

	Limit	**Average exposure**	Limit	Average exposure
	2006	**2006**	2005	2005
	£m	**£m**	£m	£m
VaR	**25.0**	**13.3**	25.0	16.6
Sensitivity analysis (PV01)	**0.7 to 1.1**	**0.8**	0.9	0.8
Stress testing (PV200)	**142.7 to 268.0**	**167.3**	260.0	195.0

All exposures include investment of the Group's reserves.

The stress test results for the last four quarters were £181.2 million, £152.4 million, £166.5 million and £169.2 million (2005 – £190 million, £191 million, £196 million and £203 million).

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

Credit risk

The Group takes on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment provisions are provided for losses that have been incurred at the balance sheet date (see note 13). Significant changes in the economy, or a sector that represents a concentration in the Group's portfolio, could result in losses that are different from those provided for at the balance sheet date. Management therefore carefully manages its exposure to credit risk.

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.

Prior to advancing funds, an assessment is made of the credit quality of borrowers and other counterparties, including retail customers. Multiple rating methodologies may be used to inform the rating decision on individual large credits. For smaller credits, a single source may suffice such as an automated credit scoring system result. It is the Group's policy to lend responsibly, and establish that loans are within the customer's capacity to repay, rather than to rely exclusively on security. Actual exposures against limits are monitored daily.

Maximum credit risk exposure at 4 April 2006 approximates to the carrying value for all assets apart from loans and advances to customers where the carrying value includes an uplift of £117.7 million in respect of hedged interest rate risk.

The classes of financial instruments to which the Group are most exposed are loans and advances to customers (note 20), loans and advances to banks, investment securities – available for sale (note 17), other financial assets at fair value and derivative financial instruments (note 18).

Credit risk - Loans and advances to customers

Of the £101.4 billion within this class, £89.6 billion (88.4%) is fully secured on residential property with a further £8.1 billion (8.0%) fully secured on land. Only £3.7 billion (3.6%) is therefore unsecured and this is primarily made up of other commercial loans, personal loans, credits cards and overdrafts.

Loans and advances to customers can be analysed between retail (£86.9 billion) and commercial (£14.5 billion) books.

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47 Financial instruments (continued)

a) Retail

The retail portfolio is predominantly made up of loans fully secured on residential property (£84.3 billion) with some unsecured consumer lending (£2.6 billion). By their nature, our retail lending books are comprised of a large number of smaller loans, have low volatility of credit risk outcomes and are intrinsically highly diversified.

In respect of its retail book, the Group operates across the whole of the UK but lending is biased towards the south east of England reflecting the concentration of branches in that region and asset growth trends. As at 4 April 2006 around 46% of the residential mortgage book was in respect of the south east.

In its specialist mortgage lender, UCB, the Group sells loans in the markets of self-certification and buy to let distributed through intermediaries. UCB balances outstanding at the year end were £6.0 billion of which £1.7 billion were in respect of buy to let.

The average loan to value (LTV) ratio of the Group's retail loan portfolio is estimated at 39% (2005 – 38%) whilst the average LTV of new residential mortgage lending was 55% (2005 – 53%). Further LTV information on the Group's retail loan portfolio is set out as follows:

	2006 %	2005 %
Loan to value analysis:		
Total book		
< 70%	**88**	90
70% - 80%	**6**	6
80% - 90%	**5**	3
>90%	**1**	1
Average loan to value of stock (indexed)	**39**	38
Average loan to value of new business	**55**	53
New business profile:		
First-time buyers	**15**	12
Home movers	**25**	26
Remortgagers	**57**	60
Buy to let	**3**	2

Nationwide Group asset quality continues to significantly outperform both the secured and unsecured lending markets. The proportion of residential lending cases currently more than 3 months in arrears being 0.28% (2005 – 0.31%) against an industry average of 0.97% (CML figure as at March 2006). For consumer lending, the value of personal loans over 30 days in arrears as a percentage of total loans is 4.6% (2005 – 4.1%) and remains around 40% lower than the average of the members of the Finance and Leasing Association (December 2005). For credit card accounts, the value of loans over 30 days in arrears as a percentage of total card accounts is 6.9% (2005 – 6.4%) and, on a comparable basis, around 30% lower than the average of the members of APACS (December 2005).

The table below provides further information on retail loans and advances by payment due status as at 4 April 2006:

	£bn	%
Not impaired:		
Neither past due nor impaired	**85.2**	**98**
Past due up to 3 months but not impaired	**1.4**	**2**
Impaired:		
Past due 3 to 6 months	**0.2**	**-**
Past due 6 to 12 months	**0.1**	**-**
Past due over 12 months (£26.2 million)	**-**	**-**
Possessions* (£11.8 million)	**-**	**-**
	86.9	**100**

*Against possession cases, £20.6 million of collateral is held.

£44.4 million of loans that would be past due or impaired have had their terms renegotiated.

Notes to the Accounts

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47 Financial instruments (continued)

b) Commercial

The make up of the commercial book at 4 April 2006 is as follows:

	£bn	%
Loans secured on commercial property	8.9	61
Loans to Registered Social Landlords	4.7	33
Loans advanced under the Private Finance Initiative	0.9	6
	14.5	100

In terms of counterparty concentration, the largest single borrower, including undrawn commitments, represents only 2.0% of the total commercial book.

Loans secured on commercial property as at 4 April 2006 are well diversified by industry type and an analysis is provided below:

	£bn	%
Residential	2.4	27
Retail	2.1	24
Office	2.0	22
Industrial and warehouse	1.1	12
Leisure and hotel	0.7	8
Owner occupied	0.5	5
Other	0.1	2
	8.9	100

Loans to Registered Social Landlords are secured on residential property. Loans advanced under the Private Finance Initiative are secured on cash flows from Government backed contracts.

Asset quality remains strong with only 69 commercial cases three months or more in arrears (2005 – 79 cases). Arrears balances were £3.3 million (2005 – £2.6 million). The table below provides further information on commercial loans and advances by payment due status as at 4 April 2006:

	£bn	%
Not impaired:		
Neither past due nor impaired	14.1	97
Past due up to 3 months but not impaired	0.4	3
Impaired:		
Past due 3 to 6 months (£4.3 million)	-	-
Past due 6 to 12 months (£1.7 million)	-	-
Past due over 12 months (£13.8 million)	-	-
Possessions* (£0.1 million)	-	-
	14.5	100

*Against possession cases, £0.1 million of collateral is held.

£2.1 million of loans that would be past due or impaired have had their terms renegotiated.

Notes to the Accounts

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>>> 47 Financial instruments (continued)

Credit risk – Loans and advances to banks, investment securities – available for sale, other financial asset at fair value and derivative financial instruments

Credit risk within our Treasury Division arises from the investments held by Treasury in order to meet the liquidity requirements and for general business purposes. This aspect of credit risk is managed by Treasury Division and the Commercial and Treasury Risk function within Risk Management Division. The Commercial and Treasury Risk team underwrites all new facilities and monitors existing facilities. They also set and monitor compliance with policy and limits, reporting to the Credit Committee (Commercial and Treasury).

For credit purposes, the Treasury portfolio at 4 April 2006 comprises the following three sub-portfolios:

	£bn	%
Financial institutions & sovereigns	**11.8**	**70**
Asset backed securities	**4.2**	**25**
Corporates	**0.8**	**5**
	16.8	**100**

As at 4 April 2006 99.9% of the Treasury portfolio exposure was neither past due nor impaired. There are no assets that would otherwise be past due or impaired whose terms have been renegotiated. As at 4 April 2006 96% of our Treasury investment portfolio comprised assets which are rated single A or better. We continue to have no exposure to emerging markets or non investment grade debt.

The Group determines that Treasury assets are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, the Group evaluates among other factors, the normal volatility in valuation, evidence of deterioration in the financial health of the investee, industry and sector performance and operational and financing cash flows. £23.9 million (0.1%) of the Treasury portfolio is classed as impaired in accordance with this definition. A cumulative impairment loss of £10.5 million has been recognised in the general reserve in respect of these assets.

The Treasury Risk function monitors exposure concentrations against a variety of criteria including industry sector/asset class and country of risk. The Treasury portfolio exposure is well spread across both industry sectors and jurisdictions. Geographical exposure is principally within Europe at £7.5 billion (45%), UK £5.0 billion (30%) and North America £2.7 billion (16%). Industry sector/asset class exposure is principally to overseas banks at £7.9 billion (47%), UK financial institutions at £2.4 billion (14%) and residential mortgage backed securities £1.7 billion (10%) and other financial institutions at £0.8 billion (5%).

Collateral held as security for Treasury assets is determined by the nature of the instrument. Loans, debt securities, treasury and other eligible bills are generally unsecured with the exception of asset backed securities and similar instruments, which are secured by pools of financial assets. The ISDA Master Agreement is Nationwide's preferred agreement for documenting derivative activity. It is common for a Credit Support Annex (CSA) to be executed in conjunction with the ISDA Master Agreement. Under a CSA, collateral is passed between parties to mitigate the market contingent counterparty risk inherent in the outstanding positions. The posting of collateral is also used to reduce the credit exposure arising on sale and repurchase transactions and guaranteed equity bonds.

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

Treasury portfolio credit mitigation

The Group has the following credit derivatives in place hedging assets in the available for sale portfolio:

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47 Financial instruments (continued)

(a) The credit risk on £597.6 million (2005 – £604.4 million) of assets has been hedged by the Group entering into a credit derivative. Under the terms of this overall risk mitigating transaction the Group 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 £31.0 million (2005 – £28.0 million).

(b) An additional £8.6 million credit derivative was taken out during the year for protection on an individual asset, not previously covered.

(c) A forward starting credit derivative has been entered into during the year to cover the credit risk on £239.0 million of assets within the available for sale portfolio when the existing structure, noted in (a) above, is subject to call in August 2007.

All of the above credit derivatives have been undertaken with A+ or above rated US and European banking institutions.

Foreign exchange risk

Foreign exchange risk is the risk that the Sterling value of, or net income from, assets/liabilities that are denominated in foreign currency changes as a consequence of changes to foreign exchange rates.

The UK is the only significant geographical area of operation for the Group. However, some funding and investment activity is undertaken in foreign currencies so some exposure to foreign exchange risk exists. This exposure is hedged on balance sheet or by using derivatives to eliminate material currency exposures.

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. The ALCO sets limits on the level of exposure by currency and in total, which are monitored daily. The limits in place will permit only those exposures that are necessary to avoid the frequent and inefficient use of FX markets in connection with the maintenance of the Group's currency portfolios.

VaR is also used to monitor the risk arising from open foreign currency positions. For VaR calculation purposes the exposure for each currency is based on a projection of cash flows for all instruments (or parts of two sided instruments such as currency swaps) denominated in that currency. Under this methodology the exposure calculation measures future income. For daily currency VaR reports the same parameters are used as for interest rate VaR i.e. a 10 day holding period, a 99% confidence level and with volatilities and correlations based on 2 years of historic data equally weighted. The currency VaR is subject to the same methods of preparation, objectives and limitations as the interest rate VaR discussed above.

	2006			2005		
	Average	**High**	**Low**	Average	High	Low
VaR	**£1.1m**	**£1.4m**	**£0.8m**	£1.0m	£1.3m	£0.8m

Liquidity risk

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

The Group 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 it to meet all financial obligations. This is achieved through maintaining a prudent level of liquid assets, through management control of the growth of business and through wholesale funding facilities.

For each material class of financial liability a maturity analysis is provided in notes 30 to 34. In practice, customer demand deposits will be repaid later than on the earliest date on which repayment can be required.

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47 Financial instruments (continued)

As additional support the Group maintains committed standby facilities. As at 4 April 2006, the Group and Society maintained £1.5 billion of committed standby facilities (2005 – £1.8 billion), of which £0.7 billion (2005 – £0.9 billion) are due to mature within one year.

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date.

At 4 April 2006 – Residual maturity	**Repayable on demand £m**	**Up to 3 months £m**	**3 - 12 months £m**	**1 - 5 years £m**	**More than 5 years £m**	**Total £m**
Assets						
Liquid assets	**368.6**	**4,266.0**	**1,538.5**	**5,496.5**	**3,070.7**	**14,740.3**
Loans and advances to customers	**811.0**	**794.5**	**2,546.5**	**13,899.1**	**83,296.5**	**101,347.6**
Other assets	**738.9**	**413.2**	**265.8**	**1,620.5**	**1,459.7**	**4,498.1**
Total assets	**1,918.5**	**5,473.7**	**4,350.8**	**21,016.1**	**87,826.9**	**120,586.0**
Liabilities						
Shares	**76,495.1**	**954.2**	**2,152.7**	**1,316.6**	**-**	**80,918.6**
Amounts owed to banks, customers and debt securities in issue	**2,540.6**	**9,528.3**	**6,683.2**	**9,943.5**	**539.1**	**29,234.7**
Other liabilities	**698.7**	**292.7**	**418.1**	**1,057.1**	**747.2**	**3,213.8**
Subordinated liabilities	**-**	**-**	**-**	**-**	**1,446.3**	**1,446.3**
Subscribed capital	**-**	**-**	**-**	**-**	**741.2**	**741.2**
Total liabilities	**79,734.4**	**10,775.2**	**9,254.0**	**12,317.2**	**3,473.8**	**115,554.6**
Net liquidity gap	**(77,815.9)**	**(5,301.5)**	**(4,903.2)**	**8,698.9**	**84,353.1**	**5,031.4**

At 4 April 2005 – Residual maturity	Repayable on demand £m	Up to 3 months £m	3 - 12 months £m	1 - 5 years £m	More than 5 years £m	Total £m
Assets						
Liquid assets	362.5	5,384.4	1,172.4	5,853.5	2,486.3	15,259.1
Loans and advances to customers	483.5	554.0	2,331.0	11,804.1	77,549.3	92,721.9
Other assets	1,047.9	254.6	187.3	976.1	1,149.9	3,615.8
Total assets	1,893.9	6,193.0	3,690.7	18,633.7	81,185.5	111,596.8
Liabilities						
Shares	69,852.1	396.0	1,937.2	408.8	-	72,594.1
Amounts owed to banks, customers and debt securities in issue	2,014.4	9,155.0	6,039.6	11,827.0	854.3	29,890.3
Other liabilities	591.9	292.5	260.3	823.6	448.5	2,416.8
Subordinated liabilities	-	-	-	-	1,439.8	1,439.8
Subscribed capital	-	-	-	-	692.2	692.2
Total liabilities	72,458.4	9,843.5	8,237.1	13,059.4	3,434.8	107,033.2
Net liquidity gap	(70,564.5)	(3,650.5)	(4,546.4)	5,574.3	77,750.7	4,563.6

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47 Financial instruments (continued)

Liquid assets include cash in hand and balances with the Bank of England, loans and advances to banks and investment securities – available for sale.

Other assets include derivative financial instruments, fair value adjustment for portfolio hedged risk, other financial instruments at fair value, investments in equity shares, other assets, deferred tax assets and accrued income and expenses prepaid.

Other liabilities include derivative financial instruments, fair value adjustment for portfolio hedged risk, insurance contract liabilities, other liabilities, provisions for liabilities and charges, accruals and deferred income, current tax liabilities and retirement benefit obligations.

The Board is responsible for setting limits over the level and composition of liquidity balances. The ALCO is responsible for setting limits over the level and maturity profile of wholesale funding and for monitoring the composition of the Group balance sheet. A liquidity stress test is performed each month to confirm that the limits set by the Board remain appropriate.

The following is an analysis of gross contractual cash flows payable under financial liabilities as at 4 April 2006:

Gross contractual cash flows	Repayable on demand £m	Up to 3 months £m	3 - 12 months £m	1 - 5 years £m	More than 5 years £m	Total £m
Shares	76,495.1	994.4	2,225.8	1,423.8	-	81,139.1
Amounts owed to banks, customers and debt securities in issue	2,540.6	9,761.3	7,123.9	10,880.4	596.4	30,902.6
Other liabilities	698.7	317.9	482.3	1,274.0	826.6	3,599.5
Subordinated liabilities	-	-	37.4	185.9	1,539.9	1,763.2
Subscribed capital	-	-	41.7	187.6	1,301.4	1,530.7
Total liabilities	79,734.4	11,073.6	9,911.1	13,951.7	4,264.3	118,935.1

For information on the contractual maturity of gross loan commitments see note 45.

Insurance risk

Insurance risk is the risk that arises from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities. The following risks exist:

- the occurrence of any events specifically insured against;
- for long term insurance business, adverse mortality, morbidity and persistency experience; and
- expense overruns relative to pricing or provisioning assumptions.

The Group manages its exposure to insurance risk by restricting its exposure to market risk through economic hedging and operating as a unit linked office, prudent product design, applying strict underwriting criteria, transferring risk to reinsurers, managing claims, establishing prudent reserves and matching assets to liabilities.

The Group's insurance contract liabilities can be analysed as follows:

Product	Gross £m	Reinsurers' share £m	Net liability £m
Guaranteed equity bonds (GEB)	889.7	-	889.7
Term assurance	273.5	245.0	28.5
Total excluding unit linked products	1,163.2	245.0	918.2
Unit linked	27.3	-	27.3
Total (note 35)	1,190.5	245.0	945.5

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>>> 47 Financial instruments (continued)

In order to minimise exposure to the underlying investment or liquidity risk on GEB, the Group purchases bespoke structured products which are designed to deliver, at maturity, a return which matches the benefits payable to the policyholder and the tax liability that has been incurred on behalf of policyholders. The Group further reduces its exposure to credit risk (i.e. the failure of the counterparty to deliver the appropriate funds) by use of a collateral arrangement.

Our term assurance business is reinsured with 3 reinsurers whose credit ratings are A- or higher.

The Group has no with profit liabilities.

Fair values of financial assets and liabilities

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the Group balance sheets at fair value.

	Group		Society	
2006	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m
Financial assets				
Loans and advances to banks	1,364.0	1,364.0	1,017.4	1,017.4
Loans and advances to customers	101,347.6	101,319.1	92,597.9	92,570.7
Financial liabilities				
Shares	80,918.6	80,916.2	80,918.6	80,916.2
Deposits from banks	2,697.4	2,682.3	1,805.2	1,790.1
Other deposits	3,161.4	3,160.5	7,225.1	7,224.2
Due to customers	2,608.3	2,609.1	941.1	941.1
Debt securities in issue	20,767.6	20,688.3	19,571.7	19,492.4
Subordinated liabilities	1,446.3	1,506.8	1,446.3	1,506.8
Subscribed capital	741.2	747.3	741.2	747.3

a) Loans and advances to customers

Loans and advances are net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

b) Deposits and borrowings

The estimated fair value of deposits with no stated maturity, which includes non-interest-bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits and other borrowings without quoted market price is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

c) Debt securities in issue

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

48 Related party transactions

Subsidiary, parent and ultimate controlling party

The Group is controlled by the Nationwide Building Society registered in England and Wales which is also considered to be the ultimate parent. Details of subsidiary undertakings can be found in note 22 to these accounts.

Notes to the Accounts

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48 Related party transactions (continued)

Key management compensation

Total compensation for key management personnel for the year by category of benefit was as follows:

	2006 £'000	2005 £'000
Short term employee benefits	**3,812**	3,556
Post employment benefits	**133**	156
Other long term benefits	**1,060**	840
Total key management personnel compensation for year	**5,005**	4,552

Transactions with related parties

A number of transactions are entered into with related parties in the normal course of business. These include loans, deposits and the payment and recharge of administrative expenses. The volumes of related party transactions, outstanding balances at the year end, and relating expense and income for the year are as follows:

	Society Subsidiaries		Group and Society Key management personnel	
	2006 £m	2005 £m	2006 £m	2005 £m
Loans payable to the Society				
Loans outstanding at 5 April 2005	7,681.1	7,190.7	1.7	1.9
Loans issued during the year	**2,201.2**	746.6	**0.6**	-
Loan repayments during the year	**(156.9)**	(256.2)	**(0.9)**	(0.2)
Loans outstanding at 4 April 2006	**9,725.4**	7,681.1	**1.4**	1.7
Deposits payable by the Society				
Deposits outstanding at 5 April 2005	1,788.0	1,213.4	3.0	2.1
Deposits issued during the year	**2,279.9**	833.5	**0.6**	1.4
Deposit repayments during the year	**(4.2)**	(258.9)	**(1.7)**	(0.5)
Deposits outstanding at 4 April 2006	**4,063.7**	1,788.0	**1.9**	3.0
Net interest income				
Interest receivable	**402.4**	356.5	**0.1**	0.1
Interest expense payable	**129.9**	68.2	**0.1**	0.1
Other income and expenses				
Fees and expenses paid to the Society	**0.6**	0.9	**-**	-
Fees and expenses paid by the Society	**21.4**	23.5	**-**	-

Transactions with key management personnel

Transactions with key management personnel are on the same terms and conditions applicable to other employees within the Group.

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 20 July 2006 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.

Transactions with Group companies

Transactions with Group companies arise in the normal course of business. Interest on outstanding loans and deposits accrues at a transfer price rate agreed between the Society and its subsidiaries.

Notes to the Accounts

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49 Notes to the cash flow statements

Non-cash items included in profit before tax	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Net (decrease)/increase in impairment provisions	**(70.8)**	5.4	**(86.6)**	2.5
Impairment (gains)/losses on investment securities	**(3.6)**	2.0	**(3.6)**	2.0
Depreciation and amortisation	**117.5**	107.1	**115.0**	104.3
Loss/(profit) on sale of property, plant and equipment	**(1.6)**	(2.1)	**(0.7)**	(1.2)
Interest on subordinated liabilities	**64.8**	48.9	**64.8**	48.9
Interest on subscribed capital	**47.1**	47.3	**47.1**	47.3
(Gain) on the revaluation of land and buildings	**(3.5)**	(0.4)	**(2.0)**	(0.5)
(Gain)/loss on revaluation of investment properties	**(5.9)**	2.8	**(0.9)**	(0.9)
(Gains) from derivatives and hedge accounting	**(10.9)**	-	**(9.7)**	-
	133.1	211.0	**123.4**	202.4

Changes in operating assets	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Loans and advances to banks	**(21.5)**	(16.2)	**(12.9)**	(20.1)
Investment securities	**(409.0)**	(177.2)	**(276.5)**	(160.4)
Derivative financial instruments and fair value adjustment for portfolio hedged risk	**(595.7)**	-	**(567.1)**	-
Other financial instruments at fair value	**(463.5)**	(116.0)	**(21.3)**	-
Loans and advances to customers	**(8,437.2)**	(12,021.2)	**(7,746.8)**	(11,483.2)
Other operating assets	**(183.2)**	(235.6)	**(2,574.9)**	(658.1)
	(10,110.1)	(12,566.2)	**(11,199.5)**	(12,321.8)

Changes in operating liabilities	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Shares	**8,324.5**	6,650.2	**8,324.5**	6,650.1
Deposits from banks, customers and other	**954.4**	(343.5)	**2,798.3**	(279.5)
Derivative financial instruments and fair value adjustment for portfolio hedged risk	**685.2**	-	**616.9**	-
Debt securities in issue	**(1,610.0)**	2,671.1	**(1,851.1)**	2,023.0
Insurance contract liabilities	**58.4**	25.2	**-**	-
Retirement benefit obligations	**(57.4)**	10.4	**(57.4)**	10.5
Other operating liabilities	**164.7**	97.9	**38.3**	120.8
	8,519.8	9,111.3	**9,869.5**	8,524.9

Cash and cash equivalents	Group 2006 £m	Group 2005 £m	Society 2006 £m	Society 2005 £m
Cash and balances with the Bank of England	**368.6**	362.5	**367.8**	362.1
Loans and advances to other banks repayable in 3 months or less*	**1,460.0**	1,239.6	**878.6**	355.4
Investment securities with a maturity period of 3 months or less	**2,133.5**	3,375.0	**2,133.5**	3,344.9
	3,962.1	4,977.1	**3,379.9**	4,062.4

On the adoption of IAS 39 certain components of the cash equivalents were re-stated from cost to fair value. This resulted in a net increase of cash and cash equivalents at 5 April 2005 by £8.2 million from £4,977.1 million to £4,985.3 million for the Group and an increase of £8.1 million from £4,062.4 million to £4,070.5 million for the Society.

The Group is required to maintain balances with the Bank of England which, at 4 April 2006, amounted to for the Group and Society £138.8 million (2005 – £125.9 million). These balances are included within loans and advances to banks on the balance sheet and are not included in the cash and cash equivalents in the cash flow statement as they are not liquid in nature.

*The loans and advances to banks cash equivalents include amounts classified as 'Other financial assets at fair value' on the balance sheet.

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49 Notes to the cash flow statements (continued)

Explanation of the significant adjustments to the cash flow statements prepared under IFRS

Under IFRS the cash flow statement is prepared in order to reconcile the movement in cash and cash equivalents, under UK GAAP only the movement in cash was reconciled. Cash, under IFRS and UK GAAP, comprises cash in hand and demand deposits. In addition cash equivalents comprise balances of highly liquid investments with maturity of three months or less from the date of acquisition. A number of debt securities included as liquid resources under UK GAAP and some loans and advances to banks are included as cash equivalents since they have a maturity period of three months or less from the date of acquisition or issue.

50 Post balance sheet events

In May 2006 contracts were exchanged with a third party for the sale of investment properties with a carrying value of £268.9 million owned by at.home nationwide limited, a wholly owned undertaking. The sale will not have a material impact on the income statement or balance sheet of the Group.

51 Reconciliation of net assets and profit under UK GAAP to IFRS

The Group reported under UK GAAP in its previously published financial statements for the year ended 4 April 2005. The analysis below shows reconciliations of net assets and profit as reported under UK GAAP to the revised net assets and profit under IFRS. Note 52 shows a more detailed restatement of the 2004/05 comparative financial results to IFRS for the Group.

Reconciliation of net profit for the year ending 4 April 2005

	Notes	Group 2005 £m	Society 2005 £m
Profit before taxation reported under UK GAAP		517.1	315.3
Retirement benefits	52b	2.3	2.4
Fixed assets and intangibles	52c, 52d	2.1	2.5
Investment properties	52e	(2.8)	0.9
Insurance	52a	(6.8)	-
Other	52f	2.0	-
Profit before taxation reported under IFRS		513.9	321.1
Taxation charge under UK GAAP		151.8	100.4
IFRS adjustment	52g	(4.9)	2.1
Taxation charge under IFRS		146.9	102.5
Net profit for the year under IFRS		367.0	218.6

Reconciliation of reserves at 4 April 2005

		Group			Society		
	Notes	General reserve £m	Revaluation reserve £m	Total £m	General reserve £m	Revaluation reserve £m	Total £m
Balance under UK GAAP		4,710.9	228.0	4,938.9	3,786.9	134.4	3,921.3
Retirement benefits	52b	(444.3)	-	(444.3)	(443.5)	-	(443.5)
Fixed assets and intangibles	52c, 52d	(0.9)	13.5	12.6	3.0	9.6	12.6
Investment properties	52e	102.2	(102.2)	-	5.0	(5.0)	-
Insurance	52a	2.2	-	2.2	-	-	-
Other	52f	(20.3)	-	(20.3)	-	-	-
Tax	52g	110.8	(36.3)	74.5	127.7	(36.1)	91.6
Balance under IFRS		4,460.6	103.0	4,563.6	3,479.1	102.9	3,582.0

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>>> 51 Reconciliation of net assets and profit under UK GAAP to IFRS (continued)

Reconciliation of reserves at 5 April 2004

	Group			Society		
	General reserve £m	Revaluation reserve £m	Total £m	General reserve £m	Revaluation reserve £m	Total £m
Balance under UK GAAP	4,341.1	211.9	4,553.0	3,571.0	110.7	3,681.7
Retirement benefits	(551.4)	-	(551.4)	(550.6)	-	(550.6)
Fixed assets and intangibles	(3.0)	12.0	9.0	0.5	8.4	8.9
Investment properties	108.5	(108.5)	-	4.0	(4.0)	-
Insurance	3.5	-	3.5	-	-	-
Other	(22.5)	-	(22.5)	-	-	-
Tax	142.9	(29.5)	113.4	161.3	(29.3)	132.0
Balance under IFRS	4,019.1	85.9	4,105.0	3,186.2	85.8	3,272.0

52 Restatement of 2004/05 Financial Results to IFRS for the Group

Restated Financial Information – Excludes the effects of IAS 32, IAS 39 and IFRS 4
Income Statement for the year ended 4 April 2005

	Notes	UK GAAP 2005 £m	Insurance (note 52a) £m	Other effects of transition to IFRS £m	IFRS 2005 £m
Interest receivable and similar income	52b	5,094.8	44.3	72.1	5,211.2
Interest expense and similar charges	52b	3,905.6	35.9	78.1	4,019.6
Net interest income		1,189.2	8.4	(6.0)	1,191.6
Fee and commission income	52f	377.4	4.8	1.8	384.0
Fee and commission expense		(109.1)	6.3	-	(102.8)
Premiums on insurance contracts and fair value gains on insurance assets		-	197.1	-	197.1
Income from investments		0.3	-	-	0.3
Other operating income	52d, 52e	69.9	(35.8)	(2.4)	31.7
Total income		1,527.7	180.8	(6.6)	1,701.9
Insurance claims and change in liabilities		-	152.4	-	152.4
Total income net of claims on insurance contracts		1,527.7	28.4	(6.6)	1,549.5
Administrative expenses	52b, 52c	815.8	35.2	(17.8)	833.2
Depreciation and amortisation	52c	99.5	-	7.6	107.1
Impairment losses on loans and advances to customers		46.6	-	-	46.6
Provisions for liabilities and charges		46.7	-	-	46.7
Impairment losses on investment securities		2.0	-	-	2.0
Profit before tax		517.1	(6.8)	3.6	513.9
Taxation	52g	151.8	(5.4)	0.5	146.9
Profit after tax		365.3	(1.4)	3.1	367.0

Notes to the Accounts

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52 Restatement of 2004/05 Financial Results to IFRS for the Group (continued)

Restated Financial Information – Excludes the effects of IAS 32, IAS 39 and IFRS 4
Balance Sheet at 4 April 2005

	Notes	UK GAAP 2005 £m	Insurance (note 52a) £m	Other effects of transition to IFRS £m	IFRS 2005 £m
Assets					
Cash and balances with the Bank of England		362.5	-	-	362.5
Loans and advances to banks		635.6	116.0	-	751.6
Investment securities – available for sale		14,145.0	-	-	14,145.0
Insurance and other financial assets at fair value		-	1,825.2	-	1,825.2
Loans and advances to customers		92,721.9	-	-	92,721.9
Investments in equity shares		14.9	-	-	14.9
Value of in force life insurance contract business		-	127.6	-	127.6
Intangible fixed assets	52c	-	-	44.2	44.2
Property, plant and equipment	52c	660.9	-	(40.9)	620.0
Investment properties		233.3	-	9.3	242.6
Accrued income and expenses prepaid	52b	463.6	9.1	(106.0)	366.7
Deferred tax assets	52g	39.9	(32.5)	74.5	81.9
Other assets		396.7	(104.0)	-	292.7
Long term life assurance business assets		1,917.3	(1,917.3)	-	-
Total assets		111,591.6	24.1	(18.9)	111,596.8
Liabilities					
Shares		72,594.1	-	-	72,594.1
Deposits from banks		1,650.6	802.7	-	2,453.3
Other deposits		2,819.5	(17.1)	-	2,802.4
Due to customers		2,257.0	-	-	2,257.0
Debt securities in issue		22,377.6	-	-	22,377.6
Insurance contract liabilities		-	1,132.1	-	1,132.1
Other liabilities		390.1	14.8	-	404.9
Provisions for liabilities and charges	52b	60.7	-	(11.7)	49.0
Accruals and deferred income		353.5	1.2	18.7	373.4
Subordinated liabilities		1,439.8	-	-	1,439.8
Subscribed capital		692.2	-	-	692.2
Current tax liabilities		100.3	5.5	-	105.8
Retirement benefit obligations	52b	-	-	351.6	351.6
Long term life assurance business liabilities		1,917.3	(1,917.3)	-	-
Total liabilities		106,652.7	21.9	358.6	107,033.2
General reserve	51	4,710.9	2.2	(252.5)	4,460.6
Revaluation reserve	51	228.0	-	(125.0)	103.0
Total reserves & liabilities		111,591.6	24.1	(18.9)	111,596.8

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>>> 52 Restatement of 2004/05 Financial Results to IFRS for the Group (continued)

Restated Financial Information – Includes the effects of IAS 32, IAS 39 and IFRS 4
Group Balance Sheet at 4 April and 5 April 2005

	Notes	IFRS 4 April 2005 £m	Derivatives and hedge accounting (note 52h) £m	Other effects of IAS 32, IAS 39 & IFRS 4 £m	IFRS 5 April 2005 £m
Assets					
Cash and balances with the Bank of England		362.5	-	-	362.5
Loans and advances to banks		751.6	-	-	751.6
Investment securities – available for sale	52k	14,145.0	47.2	79.9	14,272.1
Derivative financial instruments		-	262.0	-	262.0
Fair value adjustment for portfolio hedged risk		-	(15.2)	-	(15.2)
Insurance and other financial assets at fair value		1,825.2	-	-	1,825.2
Loans and advances to customers	52i, 52j	92,721.9	78.8	77.3	92,878.0
Investments in equity shares	52k	14.9	-	6.9	21.8
Value of in force life insurance contract business	52l	127.6	-	(3.5)	124.1
Intangible fixed assets		44.2	-	-	44.2
Property, plant and equipment		620.0	-	-	620.0
Investment properties		242.6	-	-	242.6
Accrued income and expenses prepaid		366.7	(42.8)	-	323.9
Deferred tax assets	52g	81.9	-	(1.3)	80.6
Other assets		292.7	-	-	292.7
Total assets		111,596.8	330.0	159.3	112,086.1
Liabilities					
Shares		72,594.1	-	33.1	72,627.2
Deposits from banks		2,453.3	-	-	2,453.3
Other deposits		2,802.4	-	-	2,802.4
Due to customers		2,257.0	-	-	2,257.0
Debt securities in issue	52i	22,377.6	(27.6)	0.8	22,350.8
Derivative financial instruments		-	452.5	-	452.5
Fair value adjustment for portfolio hedged risk		-	3.4	-	3.4
Insurance contract liabilities	52l	1,132.1	-	(35.8)	1,096.3
Other liabilities	52l	404.9	-	35.6	440.5
Provisions for liabilities and charges		49.0	-	-	49.0
Accruals and deferred income		373.4	(58.0)	-	315.4
Subordinated liabilities	52i	1,439.8	33.2	(0.1)	1,472.9
Subscribed capital	52i	692.2	20.9	(0.7)	712.4
Current tax liabilities	52g	105.8	-	11.3	117.1
Retirement benefit obligations		351.6	-	-	351.6
Total liabilities		107,033.2	424.4	44.2	107,501.8
General reserve		4,460.6	(94.4)	66.5	4,432.7
Revaluation reserve		103.0	-	-	103.0
Available for sale reserve		-	-	48.6	48.6
Total reserves & liabilities		111,596.8	330.0	159.3	112,086.1

Notes to the Accounts

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52 Restatement of 2004/05 Financial Results to IFRS for the Group (continued)

Explanation of the effect of the transition to IFRS

52a IFRS requires a line by line consolidation of all income statement and balance sheet items. Therefore, all life insurance items are included in the appropriate lines in the IFRS Group Accounts.

52b IFRS requires that the net deficit in respect of the defined benefit plans is recognised on the balance sheet. The expected return on pension assets and on the unwind of the discount of pension liabilities are now included in the income statement.

52c IAS 38 'Intangible Assets' requires software development costs to be capitalised where they meet certain criteria. Previously, all in-house development costs were expensed. In addition, software costs are now included in intangible fixed assets rather than in property, plant & equipment.

The impact on the income statement is a reduction of £3.7 million in administrative expenses. The impact on the balance sheet at 4 April 2005 is a reclassification of software costs of £31.6 million and a further increase of £12.6 million in intangible fixed assets representing the capitalisation of software development costs previously written off.

Under IFRS depreciation is charged on branches and non specialised buildings. The impact is an additional depreciation charge of £2.0 million.

52d Under IFRS, losses incurred on revalued property are reported in the income statement. This has resulted in an increase in the revaluation reserve of £13.5 million with a corresponding reduction in the general reserve and the reversal of previous years' losses has resulted in an increase in other income of £0.4 million.

52e Under IFRS, gains and losses arising on the revaluation of investment properties are included in the income statement. This has resulted in a net valuation loss of £2.8 million in other operating income.

The net surplus of the fair values over historic costs resulted in a reclassification of £102.2 million from the revaluation reserve to the general reserve.

52f Upfront unit trust fees previously recognised on receipt are now deferred and recognised over the life of the contract.

52g Under IFRS, additional deferred tax liabilities in respect of the revaluation of properties are recognised. The impact on the general reserve at 4 April 2005 was a decrease of £24.6 million and the impact on the revaluation reserve was a decrease of £36.3 million.

All other adjustments made under IFRS have been tax effected where appropriate.

52h To manage the accounting volatility that would otherwise arise, the Group uses fair value hedge accounting, which matches changes in the fair value of the hedged risk with changes in the fair value of related derivatives within the income statement.

An adjustment has been made at 5 April 2005 to measure all derivatives at fair value and to reflect the establishment as at that date of IAS 39 compliant hedge relationships. The overall effect has been to reduce general reserves by £94.4 million.

52i Interest income and expense together with fees and costs paid/received throughout the expected life of a loan, that are considered direct and incremental to a loan relationship are recognised on an effective interest basis.

The opening IFRS adjustment at 5 April 2005 is made up of the total amount of fees, costs and early redemption penalty interest that would have been deferred had the Group always recognised relevant income and costs on an effective interest basis. The impact on the general reserve at 5 April 2005 is a reduction of £8.7 million.

52j The net impact of more stringent evidence testing required by IFRS has resulted in a decrease in the carrying value of loan provisions of £86.0 million.

52k Under IFRS, investment securities are classified as available for sale and are therefore included at their fair values. The impact is an increase in investment securities and investments in equity shares of £86.8 million.

52l Under IFRS 4, certain contracts previously accounted for as insurance contracts have been reclassified as financial liabilities.

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53 Financial Instruments 2005 UK GAAP disclosures

As previously stated, in accordance with the transitional rules on the first time adoption of IFRS, the 2005 comparatives do not follow IAS 32, IAS 39 and IFRS 4 but instead follow the applicable UK GAAP requirements. Consequently, the comparative numbers do not reflect the fair values of financial instruments including derivatives.

We therefore show below information relating to financial instruments at 4 April 2005 disclosed in our 2005 accounts prepared in accordance with UK GAAP Financial Reporting Standard 13 'Derivatives and other financial instrument disclosures'.

Derivatives

The tables below analyse derivatives by type of contract and maturity and show the contract or underlying principal amounts, and positive and negative fair values of contracts. Contract amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. 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.

Group	Contract amount 2005 £m	Positive fair value 2005 £m	Negative fair value 2005 £m
Exchange rate contracts:			
• Cross-currency interest rate swaps	4,197.3	28.3	(117.4)
• Forward foreign exchange	3,889.4	46.5	(11.9)
	8,086.7	74.8	(129.3)
Interest rate contracts:			
• Interest rate swaps	58,725.2	347.5	(384.5)
• Swaptions	102.3	2.8	-
• Forward rate agreements	19,372.4	1.0	(0.4)
• Caps, collars and floors	2,157.0	0.5	-
	80,356.9	351.8	(384.9)
Credit contracts	839.5	-	(8.5)

Analysis of derivatives by remaining maturity

	Contract amount 2005 £m	Replacement cost 2005 £m
Exchange rate contracts:		
• Under one year	3,901.7	47.2
• Between one and five years	3,660.8	24.5
• Over five years	524.2	3.1
	8,086.7	74.8
Interest rate contracts:		
• Under one year	38,046.5	153.0
• Between one and five years	35,948.7	111.3
• Over five years	6,361.7	87.5
	80,356.9	351.8
Credit contracts:		
• Under one year	-	-
• Between one and five years	839.5	-
• Over five years	-	-
	839.5	-

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

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53 Financial Instruments 2005 UK GAAP disclosures (continued)

Interest rate sensitivity

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 2005 – Repricing date	Not more than three months £m	More than three months but not more than six months £m	More than six months but not more than one year £m	More than one year but not more than five years £m	More than five years £m	Non-interest bearing £m	Total £m
Assets							
Liquid assets	12,120.2	210.0	128.0	1,950.0	202.0	532.9	15,143.1
Loans and advances to customers	51,282.1	4,535.0	3,943.0	28,647.0	4,555.0	(240.2)	92,721.9
Fixed assets	-	-	-	-	-	894.2	894.2
Other assets	-	-	-	-	-	2,832.4	2,832.4
Total assets	63,402.3	4,745.0	4,071.0	30,597.0	4,757.0	4,019.3	111,591.6
Liabilities							
Shares	66,289.1	1,542.0	1,746.0	2,983.0	34.0	-	72,594.1
Amounts owed to credit institutions, other customers and debt securities in issue	21,804.8	1,719.0	2,087.0	2,818.0	439.0	236.9	29,104.7
Other liabilities	-	-	-	-	-	2,821.9	2,821.9
Subordinated liabilities	273.0	-	-	-	1,166.8	-	1,439.8
Subscribed capital	-	-	-	-	692.2	-	692.2
Reserves	-	-	-	-	-	4,938.9	4,938.9
Total liabilities	88,366.9	3,261.0	3,833.0	5,801.0	2,332.0	7,997.7	111,591.6
Off balance sheet items	26,437.0	(4,304.0)	3,261.0	(22,508.0)	(2,886.0)	-	-
Interest rate sensitivity gap	1,472.4	(2,820.0)	3,499.0	2,288.0	(461.0)	(3,978.4)	-
Cumulative interest rate sensitivity gap	1,472.4	(1,347.6)	2,151.4	4,439.4	3,978.4	-	

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 £m	Losses £m	Net losses £m
Amounts deferred in the balance sheet as at 4 April 2004	6.8	(15.2)	(8.4)
Amounts recognised in the year to 4 April 2005	(3.8)	1.4	(2.4)
Amounts not recognised during the year and deferred in the balance sheet as at 4 April 2005	3.0	(13.8)	(10.8)
Expected to be recognised in the year to 4 April 2006	1.5	(1.0)	0.5
Expected to be recognised thereafter	1.5	(12.8)	(11.3)

Notes to the Accounts

CONTINUED

> > > 53 Financial Instruments 2005 UK GAAP disclosures (continued)

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.

	Gains £m	Losses £m	Net gains / (losses) £m
Unrecognised gains and losses on hedges as at 4 April 2004	304.4	(476.3)	(171.9)
Of which recognised in the year to 4 April 2005	(56.7)	(16.4)	(73.1)
Gains and losses arising not recognised in the year to 4 April 2005	247.7	(492.7)	(245.0)
Gains and losses arising in the year to 4 April 2005 that were not recognised in that year	(54.0)	78.1	24.1
Unrecognised gains and losses on hedges as at 4 April 2005	193.7	(414.6)	(220.9)
Of which expected to be recognised in the year to 4 April 2006	16.7	(3.9)	12.8
Expected to be recognised thereafter	177.0	(410.7)	(233.7)

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 2005. 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 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 for options 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.

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 book value for subordinated liabilities includes £2.5 million included within prepayments and accrued income and accruals and deferred income.

The book value for subscribed capital includes £5.2 million included within accruals and deferred income.

	2005	
Assets/(Liabilities)	Book value £m	Fair value £m
On balance sheet:		
• Liquid assets	14,654.7	14,665.4
• Wholesale liabilities	(26,830.3)	(26,777.9)
• Subordinated liabilities	(1,442.3)	(1,497.5)
• Subscribed capital	(697.4)	(727.3)
Off balance sheet	124.8	(96.1)

Annual Business Statement
For the year ended 4 April 2006

1 Statutory percentages

	2006 %	Statutory limit %
Lending limit	**14.9**	25.0
Funding limit	**26.6**	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 impairment provisions on loans and advances to customers less liquid assets, property, plant and equipment, intangible fixed assets, investment properties and insurance 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

2 Other percentages

	2006 %	2005 %
As a percentage of shares and borrowings:		
• Gross capital	**6.6**	6.5
• Free capital	**6.0**	5.8
• Liquid assets	**13.4**	14.9
Profit for the financial year as a percentage of mean total assets	**0.34**	0.34
Management expenses as a percentage of mean total assets	**0.85**	0.88

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

- 'Shares and borrowings' represent the total of shares, deposits from banks, other deposits, amounts due to customers and debt securities in issue.
- 'Gross capital' represents the aggregate of general reserve, revaluation reserve, available for sale reserve, subscribed capital and subordinated liabilities.
- 'Free capital' represents the aggregate of gross capital and provisions for collective impairment losses on loans and advances to customers less property, plant and equipment and intangible fixed assets.
- 'Liquid assets' represent the total of cash in hand and balances with the Bank of England, loans and advances to banks and investment 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

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3 Information relating to directors and other officers

At 4 April 2006

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, Chairman Beazley Furlonge Ltd, Chairman Rightmove plc The Cayenne Trust plc, Chairman Thos Agnew & Sons Ltd
B A Walsh MSc (Econ), FCMA, CCMI Deputy Chairman 27 May 1944	Building Society Director	2 August 1999	
P F Williamson BA (Econ), FCIB, FRSA 11 December 1947	Chief Executive	5 April 1996	Corporate Forum for International Service, Chairman European Mortgage Federation, President Royal Society of Arts, Fellow Swindon Initiative, Chairman
B K Simpson MIMIS, FRSA 29 January 1948	Deputy Chief Executive and Chief Operating Officer	2 May 1994	Monument (Sutton) Ltd The Nationwide Foundation, Chairman Nationwide Anglia Property Services Ltd NBS Fleet Services Ltd
G J Beale BSc, ACA 19 October 1958	Group Finance Director	5 April 2003	First Nationwide Nationwide Anglia Property Services Ltd Nationwide Investments (No.1) Ltd NBS Fleet Services Ltd
S D M Bernau BSc (Econ), FCIB, MCT 15 August 1951	Commercial & Communications Director	1 November 1996	at.home nationwide ltd, Chairman Council of Mortgage Lenders Executive Committee, Member Ethos Independent Financial Services Ltd, Chairman Financial Services Skills Council, Chairman Nationwide BES Fund Managers Ltd, Chairman Nationwide Home Loans Ltd Nationwide Housing Trust Ltd, Chairman Nationwide Lease Finance Ltd Nationwide Life Ltd Nationwide Mortgage Corporation Ltd, Chairman Nationwide Syndications Ltd, Chairman Nationwide Unit Trust Managers Ltd The Minchinhampton Golf Club Ltd UCB Home Loans Corporation Ltd, Chairman

Annual Business Statement

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3 Information relating to directors and other officers (continued)

At 4 April 2006

J H Willens MBA, DMS, ACIB 7 June 1956	Group Services Director	1 January 2002	NBS Fleet Services Ltd
Mrs S J David MA (Cantab) 20 November 1962	Company Director	16 April 2003	Bacardi-Martini (Monaco) S.A.M., Monaco Bacardi & Company Ltd, Liechtenstein Bacardi Global Brands Incorporated, United States Bacardi Global Brands Ltd
J Engestrom MBA 7 February 1942	Company Director	1 March 1997	EJS Partners Ltd Nationwide Life Ltd Nationwide Unit Trust Managers Ltd Wellington Underwriting Agencies Ltd Wellington Underwriting plc
R G Handover 13 April 1946	Company Director	1 May 2000	Adult Learning Inspectorate, Chairman Dauntsey's School, Chairman Royal Mail Holdings plc The Community Foundation for Wiltshire and Swindon, Chairman Office for Standards in Education (OFSTED), Chairman of Strategy Board
G M T Howe MA (Cantab) 3 September 1949	Company Director	1 January 2005	Gateway Electronics Components Ltd Investec Ltd, South Africa Investec plc Jardine Lloyd Thompson Group plc, Chairman JP Morgan Fleming Overseas Investment Trust plc
D A Ross BSc, LLB, FCA, ACMA, CTA (Fellow), FCT 1 August 1950	Building Society Director	1 December 2004	
Ms S Taverne 3 February 1960	Company Director	16 November 2005	National Council for One Parent Families, Chair Vlessing & Taverne Ltd
R P Walther MA, FIA 31 July 1943	Company Director	1 July 2002	British United Provident Association Ltd BUPA Health Assurance Ltd BUPA Insurance Ltd Fidelity European Values plc, Chairman Nationwide Life Ltd Nationwide Unit Trust Managers Ltd

Annual Business Statement

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3 Information relating to directors and other officers (continued)

At 4 April 2006

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.

Officers

Name	Occupation	Directorships
A J Alexander ACA	Divisional Director (Finance)	
R T Bailey DMS	Divisional Director (Insurance)	Foundation Insurance Ltd, Isle of Man Nationwide Life Ltd Nationwide Unit Trust Managers Ltd
S C Clode BSc (Econ), MA, PhD	Divisional Director (Marketing)	Lingmoor View Management Ltd Nationwide Life Ltd Nationwide Trust Ltd, Chairman Nationwide Unit Trust Managers Ltd
L J Coleman BA (Hons), MBA	Divisional Director (Treasury)	First Nationwide Nationwide Lease Finance Ltd
M W Humphreys BSc, PhD	Divisional Director (Information Technology)	Nationwide Home Loans Ltd UCB Home Loans Corporation 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
R Johnston LLB, F Col, ACII	Divisional Director (Legal Compliance)	
P Leydon ACIB	Divisional Director (Audit)	
Mrs M R Mason	Divisional Director (Member Account Administration)	
S G Nowell	Divisional Director (Risk Management)	
C P Reed	Divisional Director (Customer Service & Communications)	Institute of Customer Service
D J Rigney ACMA, MBA	Divisional Director (Personnel & Development)	HM Land Registry
J A Sutherland MA, MBA, FCIB, Dip FS	Divisional Director (Branch Network)	Nationwide Life Ltd Nationwide Unit Trust Managers Ltd
J R Wood	Divisional Director (Banking, Savings & Mortgages)	Aldbury Housing Association Northamptonshire Grammar School Charitable Trust, Member The Nationwide Foundation Nationwide International Ltd, Isle of Man

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