

**Company Number: SC 001111**

**CLYDESDALE BANK PLC**

**ANNUAL REPORT AND FINANCIAL STATEMENTS**

**30 SEPTEMBER 2004**

# CLYDESDALE BANK PLC

## ANNUAL REPORT AND FINANCIAL STATEMENTS

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**CLYDESDALE BANK PLC**  
**Officers and Professional Advisers**

<b>Directors</b>	<b>Executive:</b>	Ross Pinney Lynne Peacock David Thorburn
	<b>Non-executive:</b>	Karl Daniels * Sir David Fell * Richard Gregory OBE * Roy Nicolson Malcolm Williamson (Chairman)
		* Member of the European Board Audit Committee
<b>Secretary</b>		Myshele Shaw
<b>Registered Office</b>		30 St Vincent Place Glasgow G1 2HL
<b>Bankers</b>		National Australia Bank Limited
<b>Auditors</b>		KPMG Audit Plc Chartered Accountants Registered Auditor

# **CLYDESDALE BANK PLC**

## **Report of the Directors**

The Directors of Clydesdale Bank PLC (the "Bank") with its subsidiary undertakings (which together comprise the "Group") submit their report and consolidated Financial Statements for the year ended 30 September 2004.

### **Activities**

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

The Bank and its subsidiaries offer access to a comprehensive range of banking and other related financial services through 243 branches in Scotland, England and the Isle of Man. Developments in the Group's existing business and future prospects are discussed below.

### **Profits and appropriations**

The profit attributable to the shareholders for the year ended 30 September 2004 amounted to £60,129,000 (2003 £110,843,000).

Interim dividends totalling £45,000,000 (2003 £130,000,000) were paid during the year. The Directors do not recommend the payment of a final dividend in respect of this financial year (2003 £Nil).

### **Review of developments**

The Group has recorded a profit before tax on continuing operations of £90,010,000, a decrease of £71,416,000 on the same period last year. The result illustrates the challenging nature of the trading year, but in particular, our strong focus on providing more competitively priced products, which affected income; increased costs from investment in "growth" and "quality" programmes, higher pension charges, and several exceptional provision increases.

Clydesdale has also taken part of the shared charge for software asset write-downs within one of our sister group companies. Whilst this has affected the result, it has prepared us for the future as assets written down are being replaced by new technology.

The past financial year has seen the implementation of a broad range of initiatives that represent an investment in the growth, efficiency and quality of the Group.

Clydesdale has invested in building its brand, improving sales effectiveness and expanding the Bank's distribution footprint into the south of England, where at the end of September 2004, there were eight Clydesdale Bank Financial Solutions Centres and significant expansion plans in the next year. These centres offer integrated business and private banking services.

Customer retention and customer acquisition has improved materially and consistently in key targeted segments as a result of the above programme of investment.

In September, Clydesdale Bank signed an alliance with the Post Office to give customers access to transactional banking facilities at the 16,000 Post Offices across Scotland and rest of the UK. The same month we announced a £15 million investment to create a Flagship Financial Solutions Centre in Glasgow and refurbish our Head Office complex.

Clydesdale Bank introduced several competitive products including new current and savings accounts.

The establishment of a strategic relationship with Legal & General and AXA also enhanced the product offering to customers.

"Quality" programmes included the upgrading of our technology to enhance the mortgage process for customers and ensure we meet the new FSA mortgage and insurance regulations.

Clydesdale Bank's commitment to the communities in which we operate was recognised at the Scottish Sports Sponsorship Awards. Our partnership with BasketballScotland won the Best Sponsorship for Young People Award as well as the overall award of Scottish Sports Sponsorship of the Year. Our project "Art for All" won the Arts and Corporate Social Responsibility Award at the 2004 Arts & Business Scottish Award. Meanwhile, the Group's partnership with the charity National Children's Homes was extended to Clydesdale Bank in Spring 2004. Finally, a staff volunteering scheme was introduced during the year.

## **CLYDESDALE BANK PLC**

### **Report of the Directors (continued)**

#### **Directors and Directors' interests**

The current Directors are shown on page 2. Directors who are not full-time employees of the Company or a related body corporate are appointed in accordance with the Articles of Association and may be eligible for reappointment thereafter. The Director that was reappointed during the financial year was Richard Gregory OBE.

#### Appointments

Malcolm Williamson was appointed as a Non-executive Director and Chairman of the Bank on 8 June 2004.

Roy Nicolson was appointed as a Non-executive Director of the Bank on 9 July 2004.

Lynne Peacock was appointed as a Director of the Bank on 12 July 2004.

Karl Daniels was appointed Non-executive Director of the Bank on 22 July 2004.

Sir David Fell was appointed Non-executive Director of the Bank on 22 July 2004.

#### Resignations

Geoff Greer resigned as a Director of the Bank on 8 June 2004.

Sir Fraser Morrison CBE resigned as a Non-executive Director of the Bank on 8 June 2004.

The Lord Sanderson of Bowden DL resigned as a Non-executive Director and Chairman of the Bank on 8 June 2004.

John Stewart resigned as a Director of the Bank on 6 July 2004.

Sir Hugh Sykes DL resigned as a Non-executive Director of the Bank on 12 September 2004.

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

#### **Employee involvement**

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

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

Under the UK National Share Incentive Plan, the National EVA ® Share Offer gifted ordinary shares of A\$1,250 to eligible employees in January 2004, based on Group performance during 2002 - 2003. Participants are entitled to receive dividends and exercise voting rights whilst they are members of the plan.

#### **Employment of disabled persons**

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

#### **Charitable and political donations**

The total amount given for charitable purposes by the Group during the year ended 30 September 2004 was £84,000 (2003 £109,000). No political donations were made during the year (2003 £Nil).

## **CLYDESDALE BANK PLC**

### **Report of the Directors (continued)**

#### **Corporate governance**

It is the Bank's policy not to include all of the disclosures in respect of voluntary corporate governance Codes of Practice as it is a wholly owned subsidiary of NAB. The NAB Group's 2004 Annual Financial Statements detail the Corporate Governance framework applicable to the Bank and its subsidiaries. These disclosures are made after consideration of authoritative pronouncements on audit committees and associated disclosures in Australia, the USA, the United Kingdom and the Republic of Ireland.

#### **Accounting developments**

In July 2002, the Financial Reporting Council in Australia formally announced that Australian reporting entities would be required to comply with Australian accounting standards equivalent to International Financial Reporting Standards and other pronouncements set by the International Accounting Standards Board ("IASB") for financial years commencing on or after 1 January 2005.

Thus, the ultimate parent company NAB will be required to adopt these standards for the financial year commencing 1 October 2005 and the adoption of the standards will be first reflected in NAB Group's financial statements for the half-year ending 31 March 2006. In addition comparative financial information prepared in accordance with IFRS will be required for the year commencing 1 October 2004 for disclosure in the financial statements for the year to 30 September 2006.

As a result of this NAB Group requirement, the Group will be adopting IFRS in accordance with the timelines above. The adoption of these standards will have a material effect on the Group's reported financial performance and financial position and the Group continues to evaluate the areas impacted by adoption.

During the year, a dedicated IFRS project team operating under a range of separate workstreams focused on each difference in accounting that the team identified as requiring "significant effort" to implement. The approach adopted by the team was to document the differences between the Group's current accounting policies and IFRS. IFRS project management then set out detailed plans for the move to the new standards, including the business change and specification of Information Technology requirements. The scale of the impact on the Group's financial and operational Information Technology systems has been determined as significant.

IFRS frequently require application of fair value measurement techniques. This will potentially introduce greater volatility to the Group's financial performance. In particular, hedge accounting and loan loss provisioning will be major areas of activity affected by the proposed changes. It is not possible at this time to estimate reliably the quantitative impact of the changes upon the Group's financial performance and financial position or regulatory capital. There are also several other future changes that the Group will need to address including further amendments to IAS 39 "Financial Instruments: Recognition and Measurement". The Group continues to monitor these developments.

#### **Auditors**

In accordance with section 379 of the Companies Act 1985 KPMG Audit Plc will resign as auditors of the Group. A resolution to appoint Ernst & Young as auditors and empower the Directors to fix their remuneration will be proposed.

By order of the Board

Myshele Shaw  
Secretary  
8 November 2004

## **CLYDESDALE BANK PLC**

### **Statement of Directors' Responsibilities**

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

- select suitable accounting policies and then 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 Financial Statements; and
- prepare the Financial Statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Bank and Group and which enable them to ensure that the Financial Statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Bank and Group and to prevent and detect fraud and other irregularities.

## **CLYDESDALE BANK PLC**

### **Report of the Independent Auditors to the members of Clydesdale Bank PLC**

We have audited the Financial Statements on pages 8 to 47.

This report is made solely to the Bank's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members as a body, for our audit work, for this report, or for the opinions we have formed.

#### **Respective responsibilities of Directors and Auditors**

The Directors are responsible for preparing the Report of the Directors and, as described on page 6, the Financial Statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in United Kingdom by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the Financial Statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Report of the Directors is not consistent with the Financial Statements, if the Bank has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions with the Group is not disclosed.

#### **Basis of audit opinion**

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

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Financial Statements 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 Financial Statements.

#### **Opinion**

In our opinion, the Financial Statements give a true and fair view of the state of affairs of the Bank and Group as at 30 September 2004 and of the profit of the Group for the year then ended, and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc  
Chartered Accountants  
Registered Auditor  
Glasgow

23 November 2004

**CLYDESDALE BANK PLC**  
**Consolidated Profit and Loss Account**  
**for the year ended 30 September 2004**

	Note	2004 £'000	2003 £'000
Interest receivable and similar income		479,357	516,560
Interest payable		(184,730)	(192,407)
<b>Net interest income</b>		<b>294,627</b>	<b>324,153</b>
Fees and commissions receivable		125,177	131,822
Fees and commissions payable		(1,915)	(2,255)
Other operating income		27,302	28,761
<b>Non interest income</b>		<b>150,564</b>	<b>158,328</b>
<b>Operating income</b>		<b>445,191</b>	<b>482,481</b>
Administrative expenses	3	(274,329)	(246,746)
Depreciation	4	(24,648)	(14,132)
<b>Operating expenses</b>		<b>(298,977)</b>	<b>(260,878)</b>
<b>Group operating profit before provisions</b>		<b>146,214</b>	<b>221,603</b>
Provisions for bad and doubtful debts	13	(56,244)	(60,204)
<b>Group operating profit</b>		<b>89,970</b>	<b>161,399</b>
Share of operating profit in associated undertaking		40	27
<b>Profit on ordinary activities before tax</b>	4	<b>90,010</b>	<b>161,426</b>
Tax on profit on ordinary activities	7	(29,881)	(50,583)
<b>Profit for the financial year attributable to the shareholders</b>		<b>60,129</b>	<b>110,843</b>
Dividends	9	(45,000)	(130,000)
<b>Retained profit/(loss) for the financial year</b>	28	<b>15,129</b>	<b>(19,157)</b>

All material items dealt with in arriving at the profit on ordinary activities before tax for 2004 and 2003 relate to continuing activities.

**CLYDESDALE BANK PLC****Consolidated Statement of Total Recognised Gains and Losses  
for the year ended 30 September 2004**

	<b>2004</b> <b>£'000</b>	2003 £'000
Profit for the financial year attributable to the shareholders	<b>60,129</b>	110,843
Increase in revaluation reserve	<b>3,193</b>	1,693
<b>Total recognised gains and losses for the year</b>	<b><u>63,322</u></b>	<u>112,536</u>

The profit for the financial year attributable to the shareholders and total recognised gains and losses for the year includes £31,000 (2003 £24,000) in respect of the Group's share of the total recognised gains and losses of its associated undertaking.

**Consolidated Note of Historical Cost Profits and Losses  
for the year ended 30 September 2004**

	<b>2004</b> <b>£'000</b>	2003 £'000
Profit on ordinary activities before tax	<b>90,010</b>	161,426
Realisation of property revaluation gains of prior years	<b>215</b>	130
Difference between the historical cost depreciation charge and the actual depreciation charge for the year calculated on the revalued amount	<b>(699)</b>	(1,767)
<b>Historical cost profit before taxation</b>	<b><u>89,526</u></b>	<u>159,789</u>
<b>Historical cost retained profit/(loss) for the year</b>	<b><u>14,645</u></b>	<u>(20,824)</u>

**Reconciliation of Movements in Shareholders' Funds  
for the year ended 30 September 2004**

	<b>Group</b>		<b>Bank</b>	
	<b>2004</b> <b>£'000</b>	2003 £'000	<b>2004</b> <b>£'000</b>	2003 £'000
Profit for the financial year attributable to the shareholders	<b>60,129</b>	110,843	<b>56,167</b>	118,796
Dividends	<b>(45,000)</b>	(130,000)	<b>(45,000)</b>	(130,000)
Retained profit/(loss) for the year	<b>15,129</b>	(19,157)	<b>11,167</b>	(11,204)
Increase in revaluation reserve	<b>3,193</b>	1,693	<b>3,193</b>	1,693
Net increase/(decrease) in shareholders' funds	<b>18,322</b>	(17,464)	<b>14,360</b>	(9,511)
Opening shareholders' funds	<b>557,481</b>	574,945	<b>549,975</b>	559,486
<b>Closing shareholders' funds</b>	<b><u>575,803</u></b>	<u>557,481</u>	<b><u>564,335</u></b>	<u>549,975</u>

**CLYDESDALE BANK PLC**  
**Consolidated Balance Sheet at 30 September 2004**

	Note	2004 £'000	2003 £'000
<b>Assets</b>			
Cash and balances at central bank		60,151	65,672
Items in the course of collection from other banks		107,877	119,866
Loans and advances to banks	10	772,774	1,122,122
Loans and advances to customers	11	7,292,752	7,288,358
Debt securities	14	60,538	288
Equity shares	15	778	1,223
Interest in associated undertaking	16	2,049	2,018
Tangible fixed assets	18	267,986	133,135
Other assets	19	104,562	58,025
Deferred taxation	20	13,446	14,819
Prepayments and accrued income		78,098	78,726
<b>Total assets</b>	36	<b>8,761,011</b>	<b>8,884,252</b>
<b>Liabilities</b>			
Deposits by banks	21	802,893	1,181,963
Items in the course of transmission to other banks		20,661	20,268
Customer accounts	22	5,888,409	5,848,770
Debt securities in issue	23	3,000	3,000
Notes in circulation		823,890	681,751
Other liabilities	24	279,780	235,705
Accruals and deferred income		85,110	84,533
Provisions for liabilities and charges			
- other provisions for liabilities and charges	25	31,465	20,781
Subordinated liabilities			
- undated loan capital	26	250,000	250,000
		<b>8,185,208</b>	<b>8,326,771</b>
<b>Shareholders' funds</b>			
Called up share capital	27	204,785	204,785
Share premium account	28	45,215	45,215
Revaluation reserve	28	9,298	6,320
Profit and loss account	28	316,505	301,161
<b>Total shareholders' funds</b>		<b>575,803</b>	<b>557,481</b>
<b>Total liabilities and shareholders' funds</b>	36	<b>8,761,011</b>	<b>8,884,252</b>
<b>Memorandum items</b>			
Contingent liabilities			
- acceptances and endorsements		22,109	26,409
- guarantees and assets pledged as collateral security		151,895	179,086
- other contingent liabilities		309	-
	29	<b>174,313</b>	<b>205,495</b>
Commitments	29	<b>3,571,950</b>	<b>3,174,752</b>

These Financial Statements were approved by the Board of Directors on 8 November 2004 and were signed on its behalf by:

**Malcolm Williamson**  
Chairman

**Ross Pinney**  
Director

**CLYDESDALE BANK PLC****Balance Sheet of the Bank at 30 September 2004**

	Note	2004 £'000	2003 £'000
<b>Assets</b>			
Cash and balances at central bank		60,149	65,670
Items in the course of collection from other banks		107,877	119,866
Loans and advances to banks	10	772,774	1,122,122
Loans and advances to customers	11	7,440,277	7,308,331
Debt securities	14	60,538	288
Equity shares	15	778	1,223
Interest in associated undertaking	16	42	42
Investment in subsidiaries	17	179,499	179,499
Tangible fixed assets	18	87,106	85,481
Other assets	19	101,417	57,820
Deferred taxation	20	24,023	21,958
Prepayments and accrued income		82,143	82,407
<b>Total assets</b>	36	<b>8,916,623</b>	<b>9,044,707</b>
<b>Liabilities</b>			
Deposits by banks	21	802,893	1,181,963
Items in the course of transmission to other banks		20,661	20,268
Customer accounts	22	6,062,978	6,024,882
Debt securities in issue	23	3,000	3,000
Notes in circulation		823,889	681,751
Other liabilities	24	272,704	228,038
Accruals and deferred income		84,698	84,049
Provisions for liabilities and charges			
- other provisions for liabilities and charges	25	31,465	20,781
Subordinated liabilities			
- undated loan capital	26	250,000	250,000
		<b>8,352,288</b>	<b>8,494,732</b>
<b>Shareholders' funds</b>			
Called up share capital	27	204,785	204,785
Share premium account	28	45,215	45,215
Revaluation reserve	28	9,296	6,318
Profit and loss account	28	305,039	293,657
<b>Total shareholders' funds</b>		<b>564,335</b>	<b>549,975</b>
<b>Total liabilities and shareholders' funds</b>	36	<b>8,916,623</b>	<b>9,044,707</b>
<b>Memorandum items</b>			
Contingent liabilities			
- acceptances and endorsements		22,109	26,409
- guarantees and assets pledged as collateral security		151,895	179,086
- other contingent liabilities		309	-
	29	<b>174,313</b>	<b>205,495</b>
Commitments	29	<b>3,571,950</b>	<b>3,174,752</b>

These Financial Statements were approved by the Board of Directors on 8 November 2004 and were signed on its behalf by:

**Malcolm Williamson**  
Chairman

**Ross Pinney**  
Director

# **CLYDESDALE BANK PLC**

## **Notes to the Financial Statements**

### **1. Accounting policies**

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

The Financial Statements of the Group have been prepared under the historical cost convention in accordance with the special provisions of Part VII, Chapter II of the Companies Act 1985 (the "Act") relating to banking groups, modified by the revaluation of certain fixed assets. They have been prepared in accordance with applicable Accounting Standards, pronouncements of the Urgent Issues Task Force and applicable Statements of Recommended Accounting Practice, being those issued by the British Banker's Association and the Finance and Leasing Association. The format of the Consolidated Profit and Loss Account, Consolidated Balance Sheet, Balance Sheet and Notes to the Financial Statements is as prescribed by the amended Schedule 9 to the Act.

As permitted by section 230 of the Act, no profit and loss account is presented for the Bank.

In accordance with FRS 1 "Cash Flow Statements (Revised 1996)", no cash flow statement is presented as the Group is a wholly owned subsidiary of NAB which presents such a statement in its own published consolidated Financial Statements in which the Group's are consolidated.

### **Currency of presentation**

All amounts are expressed in pounds sterling and all references to £ are to pounds sterling unless otherwise stated.

### **Comparatives**

Certain comparatives have been reclassified to conform with changes in the current year's presentation.

### **Principles of consolidation**

All undertakings which are 'controlled' by the Bank are included in the consolidated Financial Statements. Control means the ability or power of the Bank to dominate decision making directly or indirectly in relation to the financial and operating policies of another undertaking, to enable that other undertaking to operate with it in pursuing its objectives.

All intercompany balances, transactions and profits are eliminated on consolidation. Subsidiary undertakings prepare financial statements for consolidation in conformity with the Bank's accounting policies.

Where subsidiary undertakings have been acquired or sold during the year, their operating results have been included from the date of acquisition or to the date of sale.

Associates are undertakings over which the Bank exerts significant influence but does not exercise control. Equity accounting for associates is adopted. The attributable share of profit and reserves of the associated undertaking is based on the management accounts as at 30 September 2004.

### **Foreign currency translation**

All foreign currency monetary assets and liabilities are translated at the rates of exchange ruling at the balance sheet date. Gains and losses arising from these retranslations are recognised immediately in the profit and loss account. All Group foreign currency income and expense amounts are translated at average rates of exchange for the year.

### **Loans and advances**

Loans and advances include overdrafts, credit card lending, market rate advances, bill financing, housing loans, lease finance and term lending. They are carried at recoverable amount represented by the gross value of the outstanding balances as adjusted for provisions for doubtful debts.

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 1. Accounting policies (continued)

#### Bad and doubtful debts

Provisions for doubtful debts provide for losses inherent in loans and advances.

The specific provision for doubtful debts is established to cover all identified doubtful debts and is recognised when there is reasonable doubt over the collectability of principal and interest in accordance with the loan agreement ("an impaired loan"). Amounts provided for are determined by specific identification or by management's determination of probable losses for individual loans that are considered impaired in relation to loan portfolios where specific identification is impracticable. For larger-balance loans that have been individually determined to be impaired, the level of specific provision required is based on an assessment of the recoverability of each loan. This takes into account available evidence on the collateral and other objective and subjective factors that may impact the collectability of the outstanding loan principal and interest. Management judgement is required in determining the valuation of the loan collateral. Independent valuations are frequently obtained by management to provide expert advice. Each portfolio of smaller-balance loans is collectively evaluated for impairment. Management considers overall portfolio indicators, including historical credit losses and delinquency rates, in determining the level of specific provision required for each portfolio. The historical experience of the Group has shown that management's judgement of the specific provisions required in the past has been reasonably accurate. The Group considers the assumptions used in the calculation of the specific provision to be reasonable and supportable in the existing economic environment. All bad debts are written off against the specific provision for doubtful debts in the reporting period in which they are classified as irrecoverable.

The Group has adopted a statistically-based provisioning methodology for its general provision for doubtful debts. Under this methodology, the Group estimates the level of losses inherent but not specifically identified in its existing credit portfolios at balance date. The statistical provisioning methodology is applied to existing credit portfolios, including loans and advances drawn down during the year.

For retail lending (smaller-balance homogeneous loans), the general provision is assessed at a portfolio level and is based on product loss rates, to make a provision for losses inherent in the portfolio but not yet identified at balance date. These rates are determined by reference to observed historical loss experience for the relevant product types.

In respect of non-retail lending, the amount of the general provision is determined by multiplying the customer's probability of default by the loss given default. The probability of default is determined by the Group's internal customer rating system. Internal ratings are assigned at the customer level. This system utilises objective, verifiable external data, such as external credit ratings, conducted by the Group's discrete specialist economics unit. The loss given default is the amount of an individual loan at risk having regard to the level of collateral held against that facility. The level of collateral held is determined on a loan-by-loan basis, based on the Group's assessment of the loan's security value at the time of loan application and any subsequent valuations.

A change in management's assessment of the predetermined parameters or outlook assumptions would be likely to result in a change to the Group's general provision for doubtful debts. To mitigate the risk of uncertainty and validate assumptions, the Group regularly reviews the parameters, key inputs and assumptions. In addition, the Group undertakes periodic sensitivity analysis to assess the impact of deterioration in credit risk on the credit portfolio. The Group considers the assumptions used in the calculation of the general provision for doubtful debts to be reasonable and supportable in the existing economic environment.

The operation of the statistically-based provisioning methodology is such that when individual loans are impaired, specific provisions will be raised partly by making a transfer from the general provision for doubtful debts. The general provision for doubtful debts is then re-established based on the remaining portfolios of credit exposures applying the above methodology.

#### Asset quality

A loan is considered to be impaired when, based on current information and events, the Group considers it is probable that it will be unable to collect all amounts due according to the contractual terms of the loan agreement.

The Group has disclosed certain components of its loan portfolios as impaired assets according to the classifications discussed below. Non-accrual loans consist of:

- non-retail loans which are contractually past due and there is sufficient doubt about the ultimate collectability of principal and interest to warrant the cessation of interest accruals; and
- impaired off-balance sheet credit exposures where current circumstances indicate that losses may be incurred.

# **CLYDESDALE BANK PLC**

## **Notes to the Financial Statements (continued)**

### **1. Accounting policies (continued)**

#### **Income recognition on non accrual loans**

When a loan is classified as non accrual, income ceases to be recognised in the profit and loss account on an accruals basis as reasonable doubt exists as to the collectability of interest and principal. Interest charged on non accrual loans in the current reporting period is reversed against income.

Cash receipts in relation to non accrual loans are recognised as interest income to the extent that the cash receipts represent unaccrued interest except where there is a contrary agreement with the borrower, or the receipts relate to proceeds from the sale of security, or are scheduled principal repayments.

#### **Leasing and hire purchase contracts**

Finance leases, in which the Group is the lessor, and hire purchase contracts are included in loans and advances to customers and are accounted for using the finance method, whereby income determined on an actuarial basis is taken to the profit and loss account over the term of the lease in proportion to the outstanding investment balance.

Lease rentals receivable and payable on operating leases are recognised in the profit and loss account in equal periodic amounts over the effective lease term.

#### **Debt securities**

Debt securities are public and other investment securities which are purchased with the positive intent and ability to hold until maturity. Such securities are recorded at original cost adjusted for the amortisation in equal annual instalments of premiums and discounts to maturity, and other than temporary diminutions in their value. Losses relating to other than temporary diminutions in the value of investment securities are recognised in the profit and loss account and the recorded values of those securities adjusted accordingly. The sale of an investment security would only be considered in those unusual and rare situations when significant unforeseeable changes in circumstance may have caused a change in intent without calling into question the Group's intent and ability to hold other investment securities to maturity in the future (for example, evidence of a significant deterioration in a security issuer's creditworthiness). In those unusual and rare instances where investment securities are sold prior to maturity, profits and losses on sale are taken to the profit and loss account when realised.

Investment securities are recorded on a trade date basis.

For the purpose of determining market value, listed investments are valued at bid prices and unlisted investments at Directors' valuation.

#### **Equity shares**

Equity shares consist of investments securities which are held for the long term and recorded at original cost less any provision for impairment in value.

For the purpose of determining market value, unlisted investments are valued at Directors' valuation.

# **CLYDESDALE BANK PLC**

## **Notes to the Financial Statements (continued)**

### **1. Accounting policies (continued)**

#### **Repurchase and reverse repurchase agreements**

Securities sold under agreements to repurchase are retained within the investment or other securities portfolios and accounted for accordingly. Liability accounts are used to record the obligation to repurchase. The difference between the sale and repurchase price represents interest expense and is recognised in the profit and loss account over the term of the repurchase agreement. The consideration paid for securities held under reverse repurchase agreements is recorded in receivables. The difference between the purchase and sale price represents interest income and is recognised in the profit and loss account over the term of the reverse repurchase agreement.

#### **Shares in subsidiary undertakings**

Shares in subsidiary undertakings are stated at original cost less any necessary provision for impairment. Losses relating to the impairment in the value of shares in subsidiary undertakings are recognised in the profit and loss account.

#### **Tangible fixed assets**

All land and buildings are revalued annually by Directors to reflect current market values. Directors' valuations are based on advice received from independent valuers on an existing use basis. Independent valuations are carried out regularly on an existing use basis, including directly attributable acquisition costs but without deducting expected selling costs. For properties that are vacant or let to third parties valuations are carried out on an open market basis. Revaluation increments are credited to the asset revaluation reserve, unless these reverse deficits on revaluation written off to the profit and loss account in prior years. To the extent that they reverse previous revaluation increments, revaluation decrements are charged against the asset revaluation reserve.

All other tangible fixed assets are carried at the lower of cost, less accumulated depreciation, and recoverable amount. If the carrying amount of a tangible fixed asset exceeds its recoverable amount, the asset is written down to the lower value.

With the exception of land, all tangible fixed assets are depreciated using the straight-line method, at rates appropriate to its estimated useful life to the Group, taking into account any residual value. Buildings and leasehold properties with more than 30 years unexpired, are depreciated over 30 years. Leasehold property with less than 30 years unexpired is depreciated over 10 years or the period of the lease, whichever is the shorter. Motor vehicles, fixtures and equipment are depreciated over their estimated useful lives, which range from 3 to 10 years. Residual values are determined on the dates of acquisition and revaluation of assets and are based on estimated realisable values, net of any realisation costs.

Profit or loss on the sale of tangible fixed assets, which is determined as the difference between the carrying amount of the tangible fixed assets at the time of disposal and the sale proceeds, is treated as operating income or expense.

#### **Provisions**

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

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

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 1. Accounting policies (continued)

#### Derivative financial instruments held or issued for purposes other than trading

The principal objective of using derivative financial instruments for purposes other than trading is to protect the level of net interest income, while maintaining acceptable levels of interest rate, credit and liquidity risk, and to facilitate the funding needs of the Group. To achieve this objective, a combination of derivative including swaps, futures, forwards, option and other contingent or exchange traded contracts in the interest rate and foreign exchange markets may be used.

Hedging derivatives must be effective at reducing the risk associated with the exposure being hedged and must be designated as a hedge at the inception of the contract. Accordingly, changes in the fair value of the hedging derivative must be closely correlated with changes in the fair value of the underlying exposure at inception of the hedge and over the term of the hedged exposure. The timing of the impact of hedging derivatives on the profit and loss account is consistent with the timing of the impact of the hedged items on the profit and loss account.

The net income or expense on derivatives used to manage interest rate exposures is recorded in net interest income on an accruals basis. If a derivative that is used to manage an interest rate exposure is terminated early, any resulting gain or loss is deferred within other assets or other liabilities and amortised to net interest income over the remaining period originally covered by the terminated contract. If the underlying interest rate exposure position ceases to exist, any deferred gain or loss is recognised immediately in other operating income.

Gains or losses on derivatives used to hedge exposures arising from anticipated future transactions, are deferred within other assets or other liabilities until such time as the accounting impact of the anticipated transaction is recognised in the Financial Statements. Such gains or losses only qualify for deferral where there is a high probability of the future transaction materialising. If it becomes apparent that the future transaction will not materialise, any deferred gain or loss is recognised immediately in other operating income.

Interest receivable and payable for interest rate swaps with the same counterparty are reported on a net basis as prepayments and accrued income or accruals and deferred income where a legal right of set-off exists.

#### Recognition of fee income including loan related fees and costs

Interest income is reflected in the profit and loss account when earned on an accruals basis. Dividend income is recorded in the profit and loss account on an accruals basis when the Group obtains control of the right to receive the dividend.

When fees and commissions relate to specific transactions or events, they are recognised as income in the period that the services are provided. When they are charged for services provided over a period, they are recognised as income on an accruals basis.

Loan origination fees, if material, are recognised in income over the life of the loan as an adjustment of yield. Direct loan origination costs, if material, are netted against the loan origination fees and the net amount recognised in income over the life of the loan as an adjustment of yield. All other loan related costs are expensed as incurred.

Application and activation lending fees received are recognised as income no later than when the loan is disbursed or the commitment to lend expires. Recurring management fees received are taken to the profit and loss account on an accruals basis. Credit card fees are taken to the profit and loss account when charged to the customer.

Incentives given in respect of mortgages and other loans, if material, are deferred and recognised over a period. The period used is the shorter of the term over which they can be recovered from the customer in the event of early termination or the period for which the incentive is given.

#### Pension and post retirement costs

Contributions to the Group's defined benefit pension scheme are charged to the profit and loss account so as to spread the expected cost of pensions, calculated in accordance with actuarial advice, on a systematic basis over employees' working lives. Pension arrangements cover a majority of employees and are operated through a defined benefit scheme funded by the Bank and its subsidiary undertakings. The pension cost relating to this scheme is assessed in accordance with advice of qualified actuaries, on the basis of triennial valuations, using the projected unit method. Variations from the regular cost are allocated on a straight line basis over the average remaining service lives of current employees. Where an excess of assets so allocated is greater than the regular cost of accruing benefits, the effect of the excess assets in the scheme is limited, on the grounds of prudence, to an amount equal to the regular cost.

## **CLYDESDALE BANK PLC**

### **Notes to the Financial Statements (continued)**

#### **1. Accounting policies (continued)**

##### **Pension and post retirement costs (continued)**

The Group recognises the cost of providing post retirement health care benefits in the profit and loss account, over the period of service during which employees become entitled to those benefits. Costs are estimated by projecting past claims experience, and are measured at present values by discounting future cash flows.

The expense recognised in the profit and loss account in relation to the defined contribution scheme represents the contributions payable to this scheme.

##### **Taxation**

The Group provides for taxation using tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred taxation is accounted for on an undiscounted basis at expected tax rates on all timing differences which occur where items are tax-effected in a period different from that in which they are recognised in the Financial Statements, except as otherwise required by FRS 19. Deferred tax assets are only recognised when it is more likely than not that the asset will be recoverable in the foreseeable future out of suitable taxable profits from which the timing differences and tax losses can be deducted.

Chargeable gains are provided for in determining the tax charge for the period if there is a binding agreement to dispose of an asset as at the balance sheet date.

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 2. Nature of business and segmental reporting

The assets, liabilities and results of the Bank and Group are derived from the business of banking and other related financial services in the United Kingdom.

### 3. Administrative expenses

	2004 £'000	2003 £'000
Staff costs		
- wages and salaries	61,751	58,628
- social security costs	4,840	4,606
- pension costs	18,158	12,104
	<u>84,749</u>	<u>75,338</u>
Administrative expenses		
-other	77,893	79,639
-recharges from parent and fellow subsidiary undertakings	105,388	91,769
-recharge of software impairment write-down from a fellow subsidiary undertaking	6,299	-
	<u>274,329</u>	<u>246,746</u>

### 4. Profit on ordinary activities before tax

	2004 £'000	2003 £'000
This is stated after:		

#### *Income*

Aggregate amounts receivable, including capital repayments, (net of depreciation of £315,984,000 (2003 £284,561,000))

under:

- finance leases and hire purchase contracts	30,829	38,155
- operating leases	6,147	2,371

#### *Charges*

Depreciation of tangible fixed assets (Note 18)	24,648	14,132
Charges incurred with respect to subordinated liabilities	12,931	10,785
Hire of computers and equipment	13	20
Rental of premises held under operating leases	13,287	11,944
Auditors' remuneration (including irrecoverable VAT)		

#### *Audit*

Audit services

- Bank	192	182
- Subsidiary undertakings	24	21
- Further assurance services	5	27

<u>221</u>	<u>230</u>
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On 14 July 2004, the Group announced its decision to wind down its National Custodian Services business, which was involved in the business of global custodians. The loss from this terminated activity in the year ended 30 September 2004 was £2,855,000 (2003 £1,813,000). Included in this figure are costs of £2,014,000 in relation to the impairment of assets and a provision of £6,317,000 in relation to the termination of the operation (Note 25).

## CLYDESDALE BANK PLC

### Notes to the Financial Statements (continued)

#### 4. Profit on ordinary activities before tax (continued)

The Bank is a wholly owned subsidiary of NAB Limited, which is required to comply with Australian Corporations Act 2001 and the Australian Securities and Investments Commission's Class Orders 98/2000 and 00/0319 pertaining to external audit indebtedness. The Bank complies with the requirements of Class Order 98/2000 and 00/0319 in that no member of KPMG Australia is indebted to the Bank unless such indebtedness is permitted under the terms of either of these class orders.

#### 5. Directors' emoluments

	2004 £'000	2003 £'000
Aggregate emoluments	652	520
Compensation for loss of office	-	244
	<u>652</u>	<u>764</u>

No Directors (2003 three) exercised share options in the year and three Directors (2003 four) became entitled to receive shares under long-term incentive schemes operated by the Bank's ultimate parent undertaking. No directors (2003 Nil) accrued retirement benefits under a money purchase pension scheme.

The aggregate emoluments of the highest paid Director in respect of those duties relevant to the Bank were £191,022 (2003 £121,326). The Bank pension contributions amounted to £Nil (2003 £Nil). The director exercised no share options in the year (2003 15,000) and was entitled to receive shares under the long term incentive scheme. The Bank pension contributions amounted to £Nil (2003 £Nil).

Three directors (2003 nil) who left office during the year were entitled, in terms of their contracts, to receive a payment in relation to their retirement. The payments totalled £316,704 (2003 £Nil).

#### 6. Pension scheme

The principal pension scheme of the Group is the Clydesdale Bank Pension Scheme, the assets of which are held in a separate trustee administered fund.

With effect from 1 January 2004 the Group participates in a defined contribution pension scheme for new staff and closed the original defined benefit scheme to new staff. This does not affect the pension arrangements of existing employees. In relation to this scheme the pension charge for the period for the Group and fellow subsidiary companies is disclosed in the Financial Statements of NAGE.

Actuarial valuations of the assets (using market values) and liabilities (using the projected unit method) of the scheme are carried out triennially, and updated annually, by qualified actuaries, to determine the financial position of the scheme to enable the group to establish the level of contributions to be made to the scheme. The latest formal actuarial valuation of the Clydesdale Bank Pension Scheme was carried out at 30 September 2001. In view of stock market volatility an interim actuarial review was undertaken to determine revised contribution rates and associated costs with an effect from 1 July 2003.

The principal actuarial assumptions adopted by the scheme following the interim review were:

	% p.a
Long term investment returns	
- new investments	6.75
- existing investments	6.25
Increase in pensionable remuneration	4.00
Post-retirement pension increases	2.50
Price inflation	2.50

The market value of the scheme's assets at the date of the formal valuation was £580,300,000. The actuarial value of the assets was sufficient to cover 99.4% of the benefits that had accrued to members, after allowing for expected future increases in earnings.

## CLYDESDALE BANK PLC

### Notes to the Financial Statements (continued)

#### 6. Pension scheme (continued)

The market value of the scheme's assets at the date of the interim review was £538,000,000. The actuarial value of the assets was sufficient to cover 80% of the benefits that had accrued to members, after allowing for expected future increases in earnings.

Of the total contributions made to the scheme of £25,929,000 (2003 £17,654,000), £8,838,000 (2003 £5,106,000) were made by fellow group undertakings in respect of employees originally employed by the Bank and entitled to continue as members of the scheme.

Contributions to the scheme are charged to the profit and loss account so as to spread the expected cost of pensions on a systematic basis over employees' working lives, currently estimated as being fourteen years. A long term investment rate on existing investments of 6.5% and an estimated retirement age of 60, together with the other actuarial assumptions detailed above are used by the Group to calculate the pension cost. As a result, contributions to the scheme were lower than the actuarial cost to the Bank and the existing prepayment has been reduced to £2,910,000 at 30 September 2004 (2003 £5,217,000).

The Bank also provides post-retirement health care under a defined benefit scheme for pensioners and their dependant relatives for which provision has been made.

With effect from 1 January 2004 the Group participates in a defined contribution pension scheme for new staff and closed the original defined benefit scheme to new staff. For the defined benefit schemes closed to new entrants, under the projected unit method the service cost as a percentage of pensionable payroll will increase as the members of the schemes approach retirement. This does not affect the pension arrangements of existing employees. In relation to this scheme the pension charge for the period for the Group and fellow subsidiary companies is disclosed in the Financial Statements of NAGE.

#### FRS 17 disclosure

Whilst the Group continues to account for pension costs in accordance with Statement of Standard Accounting Practice 24 "Accounting for Pension Costs", the following transitional disclosures are required under FRS 17 "Retirement Benefits", in relation to the defined benefit scheme.

The valuations were updated by the actuary on an FRS 17 basis as at 30 September 2002, 30 September 2003 and 30 September 2004 and the major assumptions used in these valuations were:

	<b>2004</b>	2003	2002
	<b>% p.a.</b>	% p.a.	% p.a.
Inflation	<b>2.80</b>	2.50	2.20
Rate of increase in salaries	<b>4.30</b>	4.00	3.70
Rate of increase for pensions in payment and deferred pensions	<b>2.80</b>	2.50	2.20
Discount rate	<b>5.67</b>	5.50	5.60

The assumptions used by the actuary are the best estimate chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice.

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**6. Pension scheme (continued)**

**FRS17 disclosure (continued)**

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

	<b>2004</b>	2003	2002
	<b>£'000</b>	£'000	£'000
<i>Assets in the scheme were as follows:</i>			
Equities	<b>505,000</b>	455,000	398,000
Government bonds	<b>76,000</b>	65,000	56,000
Cash	<b>7,000</b>	6,000	2,000
Corporate bonds	<b>39,000</b>	42,000	31,000
Total market value of scheme assets	<b>627,000</b>	568,000	487,000
Present value of scheme liabilities	<b>840,000</b>	780,000	686,000
Deficit in the scheme	<b>(213,000)</b>	(212,000)	(199,000)
Related deferred tax asset	<b>63,900</b>	63,600	59,700
Net pension liability	<b>(149,100)</b>	(148,400)	(139,300)
	<b>2004</b>	2003	2002
	<b>% p.a.</b>	% p.a.	% p.a.
<i>Expected rate of return on the above assets:</i>			
Equities	<b>8.70</b>	8.60	8.70
Government bonds	<b>4.90</b>	4.70	4.50
Cash	<b>4.75</b>	3.50	4.00
Corporate bonds	<b>5.50</b>	5.30	5.40

	<b>2004</b>	2003
	<b>£'000</b>	£'000
<b>Movement in deficit during the year</b>		
Deficit in the scheme at 1 October	<b>(212,000)</b>	(199,000)
Movement in year:		
Current service cost	<b>(21,400)</b>	(19,200)
Contributions	<b>27,100</b>	22,600
Past service cost	<b>(1,000)</b>	(4,900)
Other finance income	<b>2,500</b>	900
Actuarial loss	<b>(8,200)</b>	(12,400)
<b>Deficit in the scheme at 30 September</b>	<b>(213,000)</b>	(212,000)

The amount of this net pension liability would have a consequential effect on reserves if FRS 17 accounting was fully adopted.

	<b>2004</b>	2003
	<b>£'000</b>	£'000
<b>Analysis of the amount that would be charged to operating profit</b>		
Current service cost	<b>21,400</b>	19,200
Past service cost	<b>1,000</b>	4,900
<b>Total operating charge</b>	<b>22,400</b>	24,100

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**6. Pension scheme (continued)**

	<b>2004</b>	2003
	<b>£'000</b>	£'000
<b>Analysis of the amount that would be credited to other finance income</b>		
Expected return on pension scheme assets	<b>44,700</b>	38,800
Interest on pension scheme liabilities	<b>(42,200)</b>	(37,900)
<b>Net return</b>	<b>2,500</b>	900

	<b>2004</b>	2003
	<b>£'000</b>	£'000
<b>Analysis of amount that would be recognised in the statement of total recognised gains and losses</b>		
Actual return less expected return on pension scheme assets	<b>13,300</b>	44,800
Experience gains and losses arising on scheme liabilities	<b>1,500</b>	(4,200)
Changes in assumptions underlying the present value of the scheme liabilities	<b>(23,000)</b>	(53,000)
<b>Total amount that would be recognised in the statement of total recognised gains and losses</b>	<b>(8,200)</b>	(12,400)

*History of experience gains and losses*

	<b>2004</b>	2003	2002
<b>Difference between the expected and actual return on scheme assets</b>			
Amount (£'000)	<b>13,300</b>	44,800	(152,800)
Percentage of scheme assets	<b>2.1%</b>	7.9%	31.4%
<b>Experience gains and losses on scheme liabilities</b>			
Amount (£'000)	<b>1,500</b>	(4,200)	(10,200)
Percentage of the present value of the scheme liabilities	<b>0.2%</b>	0.5%	1.5%
<b>Total amount that would be recognised in statement of total recognised gains and losses</b>			
Amount (£'000)	<b>(8,200)</b>	(12,400)	(207,600)
Percentage of the present value of the scheme liabilities	<b>1.0%</b>	1.6%	30.3%

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**7. Tax on profit on ordinary activities**

**a) Analysis of charge in period**

	<b>2004</b>	2003
	<b>£'000</b>	£'000
The charge for taxation comprises:		
<i>Current tax</i>		
United Kingdom corporation tax at 30% (2003 30%)	<b>28,499</b>	45,725
Associated undertaking	<b>9</b>	3
Total current tax	<b><u>28,508</u></b>	<u>45,728</u>
<i>Deferred tax</i>		
Origination and reversal of timing differences		
- current year	<b>1,981</b>	5,110
- prior year	<b>(608)</b>	(255)
Total deferred tax	<b><u>1,373</u></b>	<u>4,855</u>
<i>Tax on profit on ordinary activities</i>	<b><u><u>29,881</u></u></b>	<u><u>50,583</u></u>

**b) Factors affecting tax charge for the period**

The tax assessed for the period differs from the standard rate of corporation tax in the UK (30%). The differences are explained below:

	<b>2004</b>	2003
	<b>£'000</b>	£'000
Profit on ordinary activities before tax	<b><u>90,010</u></b>	<u>161,426</u>
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK 30% (2003 30%)	<b><u>27,003</u></b>	<u>48,428</u>
Effects of:		
Expenses not deductible for tax purposes	<b>3,486</b>	2,410
Timing differences	<b>(1,981)</b>	(5,110)
Current tax charge for period	<b><u><u>28,508</u></u></b>	<u><u>45,728</u></u>

**c) Factors that may affect future tax charges**

There are no items which would materially affect the future tax charge. No provision is made for deferred tax on gains arising on the revaluation of fixed assets, as such gains would become taxable only if the asset were sold.

**8. Profit dealt with in the Financial Statements of the Bank**

The profit on ordinary activities after tax of the bank for the year is £56,167,000 (2003 £118,796,000).

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**9. Dividends**

	<b>2004</b>	2003
	<b>£'000</b>	£'000
Dividends paid		
1st interim - 22p per share (2003 34p per share)	<b>45,000</b>	70,000
2nd interim - Nilp per share (2003 29p per share)	<b>-</b>	60,000
	<b><u>45,000</u></b>	<u>130,000</u>

**10. Loans and advances to banks**

<b>Group and Bank</b>	<b>2004</b>	2003
	<b>£'000</b>	£'000
Remaining maturity:		
- on demand or at short notice	<b>274,722</b>	560,607
- 3 months or less	<b>466,716</b>	529,266
- 1 year or less but over 3 months	<b>-</b>	7,147
- 5 years or less but over 1 year	<b>6,513</b>	-
- over 5 years	<b>24,823</b>	25,102
	<b><u>772,774</u></b>	<u>1,122,122</u>
Amounts include:		
Due from parent and fellow subsidiary undertakings	<b><u>758,975</u></b>	<u>1,105,855</u>

**11. Loans and advances to customers**

	<b>Group</b>		<b>Bank</b>	
	<b>2004</b>	2003	<b>2004</b>	2003
	<b>£'000</b>	£'000	<b>£'000</b>	£'000
Remaining maturity:				
- on demand or at short notice	<b>2,212,344</b>	1,932,812	<b>2,459,540</b>	2,105,593
- 3 months or less	<b>773,987</b>	906,942	<b>783,987</b>	928,298
- 1 year or less but over 3 months	<b>617,524</b>	611,787	<b>499,672</b>	459,045
- 5 years or less but over 1 year	<b>1,578,822</b>	1,683,606	<b>1,491,487</b>	1,633,445
- over 5 years	<b>2,202,576</b>	2,234,683	<b>2,295,762</b>	2,260,991
	<b><u>7,385,253</u></b>	<u>7,369,830</u>	<b><u>7,530,448</u></b>	<u>7,387,372</u>
General and specific bad and doubtful debt provisions (Note 13)	<b><u>(92,501)</u></b>	<u>(81,472)</u>	<b><u>(90,171)</u></b>	<u>(79,041)</u>
	<b><u>7,292,752</u></b>	<u>7,288,358</u>	<b><u>7,440,277</u></b>	<u>7,308,331</u>
Amounts include:				
Due from subsidiary undertakings - unsubordinated			<b><u>686,242</u></b>	<u>618,033</u>

The costs of assets acquired by the Group during the year for the purpose of letting under finance leases and hire purchase contracts amounted to £12,491,468 (2003 £25,632,120) and £279,702,500 (2003 £281,258,053) respectively. The total closing balances of finance leases and hire purchase contracts were £110,200,000 (2003 £142,319,000) and £430,846,000 (2003 £458,171,000) respectively.

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**12. Concentration of exposure**

<b>Group</b>	<b>2004</b>	<b>2003</b>
<i>Loans and advances to customers</i>	<b>£'000</b>	£'000
Commercial and industrial	<b>1,662,466</b>	1,928,900
Agriculture, forestry, fishing and mining	<b>425,372</b>	416,995
Manufacturing	<b>133,144</b>	141,837
Construction	<b>120,472</b>	168,933
Financial, investment and insurance	<b>115,810</b>	111,033
Property	<b>588,406</b>	448,682
Other lease finance	<b>558,057</b>	600,491
Personal - mortgages	<b>2,486,310</b>	2,245,585
Personal - other	<b>1,276,108</b>	1,281,159
Other	<b>19,108</b>	26,215
	<b><u>7,385,253</u></b>	<u>7,369,830</u>

**13. Provisions for bad and doubtful debts**

	<b>Specific</b>	<b>General</b>	<b>Total</b>	<b>Specific</b>	<b>General</b>	<b>Total</b>
	<b>2004</b>	<b>2004</b>	<b>2004</b>	<b>2003</b>	<b>2003</b>	<b>2003</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Group</b>						
Opening balance	<b>22,875</b>	<b>58,597</b>	<b>81,472</b>	33,903	65,132	99,035
Charge/(credit) for the year	<b>50,196</b>	<b>6,048</b>	<b>56,244</b>	66,739	(6,535)	60,204
Amounts written off	<b>(61,811)</b>	-	<b>(61,811)</b>	(91,758)	-	(91,758)
Recoveries of amounts written off in previous years	<b>16,596</b>	-	<b>16,596</b>	13,991	-	13,991
<b>Closing balance</b>	<b><u>27,856</u></b>	<b><u>64,645</u></b>	<b><u>92,501</u></b>	<u>22,875</u>	<u>58,597</u>	<u>81,472</u>
<b>Bank</b>						
Opening balance	<b>21,767</b>	<b>57,274</b>	<b>79,041</b>	31,843	63,091	94,934
Charge/(credit) for the year	<b>49,298</b>	<b>6,012</b>	<b>55,310</b>	62,485	(5,817)	56,668
Amounts written off	<b>(60,776)</b>	-	<b>(60,776)</b>	(86,552)	-	(86,552)
Recoveries of amounts written off in previous years	<b>16,596</b>	-	<b>16,596</b>	13,991	-	13,991
<b>Closing balance</b>	<b><u>26,885</u></b>	<b><u>63,286</u></b>	<b><u>90,171</u></b>	<u>21,767</u>	<u>57,274</u>	<u>79,041</u>

£7,024,000 of the increase in the general provision charge in the year relates to changes in the assumptions underpinning the calculation.

	<b>Group</b>		<b>Bank</b>	
	<b>2004</b>	<b>2003</b>	<b>2004</b>	<b>2003</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
<b>Amounts included in</b>				
Loans and advances to customers (Note 11)	<b><u>92,501</u></b>	<u>81,472</u>	<b><u>90,171</u></b>	<u>79,041</u>
<b>Non accrual loans</b>				
Loans and advances to customers	<b>45,479</b>	43,507	<b>43,812</b>	40,374
Provisions	<b>(21,578)</b>	(16,892)	<b>(20,607)</b>	(15,784)
Total	<b><u>23,901</u></b>	<u>26,615</u>	<b><u>23,205</u></b>	<u>24,590</u>

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**14. Debt securities**

	<b>Book value 2004 £'000</b>	<b>Market value 2004 £'000</b>	<b>Book value 2003 £'000</b>	<b>Market value 2003 £'000</b>
<b>Group and Bank</b>				
<b>Issued by other issuers</b>				
<i>Investment securities</i>				
- other debt securities (unlisted)	<u><u>60,538</u></u>	<u><u>60,538</u></u>	<u><u>288</u></u>	<u><u>288</u></u>
<i>Amounts include</i>				
Due one year and over	<u><u>60,538</u></u>		<u><u>288</u></u>	

	<b>Cost £'000</b>	<b>Provisions £'000</b>	<b>Book value £'000</b>
<b>Investment securities</b>			
At 1 October 2003	988	(700)	288
Additions	60,250	-	60,250
Disposals	(700)	700	-
<b>At 30 September 2004</b>	<u><u>60,538</u></u>	<u><u>-</u></u>	<u><u>60,538</u></u>

**15. Equity shares**

	<b>Book value 2004 £'000</b>	<b>Market value 2004 £'000</b>	<b>Book value 2003 £'000</b>	<b>Market value 2003 £'000</b>
<b>Group and Bank</b>				
<b>Investment securities</b>				
- unlisted	<u><u>778</u></u>	<u><u>778</u></u>	<u><u>1,223</u></u>	<u><u>1,223</u></u>

	<b>Cost £'000</b>	<b>Provisions £'000</b>	<b>Book value £'000</b>
<b>Investment securities</b>			
At 1 October 2003	1,223	-	1,223
Charge for year	-	(209)	(209)
Disposals	(236)	-	(236)
<b>At 30 September 2004</b>	<u><u>987</u></u>	<u><u>(209)</u></u>	<u><u>778</u></u>

**16. Interest in associated undertaking**

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

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**17. Subsidiary undertakings**

<b>Bank</b>	<b>£'000</b>
<b>At 30 September 2004 and 2003</b>	<b><u>179,499</u></b>

**Principal subsidiary undertakings at 30 September 2004**

<b>Principal subsidiary undertakings</b>	<b>Nature of business</b>	<b>Country of incorporation and principal operations</b>
Clydesdale Europe Finance Limited	Structured finance	Jersey
Clydesdale Bank Asset Finance Limited	Leasing and hire purchase	Scotland

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

All of the above subsidiaries have 30 September year ends.

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**18. Tangible fixed assets**

*Movements on tangible fixed assets*

<b>Group</b>	<b>Freehold land and buildings £'000</b>	<b>Leases of 50 years and over unexpired £'000</b>	<b>Leases of under 50 years unexpired £'000</b>	<b>Motor vehicles, fixtures and equipment £'000</b>	<b>Total £'000</b>
<b>Cost or valuation</b>					
At 1 October 2003	44,643	3,158	22,675	204,712	275,188
Additions	1,790	446	6,049	150,732	159,017
Disposals	(1,498)	-	(402)	(4,814)	(6,714)
Surplus/(deficit) on revaluation	2,399	(2)	-	-	2,397
<b>At 30 September 2004</b>	<b>47,334</b>	<b>3,602</b>	<b>28,322</b>	<b>350,630</b>	<b>429,888</b>
<b>Accumulated depreciation</b>					
At 1 October 2003	144	17	13,012	128,880	142,053
Charge for the year	889	93	2,201	21,465	24,648
Disposals	(30)	(1)	(342)	(3,518)	(3,891)
Released on revaluation	(839)	(69)	-	-	(908)
<b>At 30 September 2004</b>	<b>164</b>	<b>40</b>	<b>14,871</b>	<b>146,827</b>	<b>161,902</b>
<b>Net book value</b>					
<b>At 30 September 2004</b>	<b>47,170</b>	<b>3,562</b>	<b>13,451</b>	<b>203,803</b>	<b>267,986</b>
At 30 September 2003	44,499	3,141	9,663	75,832	133,135
<b>Bank</b>					
<b>Cost or valuation</b>					
At 1 October 2003	44,643	3,158	22,675	153,140	223,616
Additions	1,790	446	6,049	4,653	12,938
Disposals	(1,498)	-	(402)	(4,814)	(6,714)
Surplus/(deficit) on revaluation	2,399	(2)	-	-	2,397
<b>At 30 September 2004</b>	<b>47,334</b>	<b>3,602</b>	<b>28,322</b>	<b>152,979</b>	<b>232,237</b>
<b>Accumulated depreciation</b>					
At 1 October 2003	144	17	13,012	124,962	138,135
Charge for the year	889	93	2,201	8,612	11,795
Disposals	(30)	(1)	(342)	(3,518)	(3,891)
Released on revaluation	(839)	(69)	-	-	(908)
<b>At 30 September 2004</b>	<b>164</b>	<b>40</b>	<b>14,871</b>	<b>130,056</b>	<b>145,131</b>
<b>Net book value</b>					
<b>At 30 September 2004</b>	<b>47,170</b>	<b>3,562</b>	<b>13,451</b>	<b>22,923</b>	<b>87,106</b>
At 30 September 2003	44,499	3,141	9,663	28,178	85,481

*Assets held under finance leases and hire purchase contracts*

The net book value of motor vehicles, fixtures and equipment includes assets held under finance leases and hire purchase contracts of £1,838,000 (2003 £1,971,000), net of accumulated depreciation of £5,049,000 (2003 £4,537,000).

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**18. Tangible fixed assets (continued)**

*Assets held under operating leases*

The net book value of motor vehicles, fixtures and equipment includes assets held under operating leases of £180,880,068 (2003 £47,649,000), net of accumulated depreciation of £16,762,763 (2003 £3,725,000).

*Residual values*

The following table sets out the maturity of the Group's un-guaranteed residual values of assets leased to customers:

<i>Recoverable</i>	<b>Operating Leases £'000</b>	<b>Finance Leases £'000</b>	<b>Total £'000</b>
1 year or less	655	-	655
2 years or less but greater than 1 year	2,131	-	2,131
5 years or less but greater than 2 years	45,175	449	45,624
Over 5 years	17,437	347	17,784
<b>Total</b>	<b>65,398</b>	<b>796</b>	<b>66,194</b>

Regular reviews are made of residual values in the light of available market data and impairments are made in respect of losses where ultimate recovery is in doubt.

*Valuations*

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

	<b>2004 £'000</b>	2003 £'000
At current year valuation	<b>46,831</b>	46,606
At cost	<b>32,427</b>	23,870
	<b>79,258</b>	70,476

Freehold, and leasehold properties where the original lease is more than thirty years, are revalued on a three year cycle. In addition all properties with a material carrying value are revalued annually to reflect their current market value existing use. These valuations are carried out by external qualified valuers (as defined in the RICS Appraisal and Valuation Manual), Donaldsons, Chartered Surveyors. The basis of valuation is existing use value and the professional valuations have been made in accordance with RICS Practice Statements and Guidance Notes.

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

	<b>2004 £'000</b>	2003 £'000
Cost	<b>89,457</b>	81,547
Accumulated depreciation	<b>(38,859)</b>	(37,178)
Net book value	<b>50,598</b>	44,369

*Land and buildings occupied for own activities*

	<b>Group and Bank</b>	
	<b>2004 £'000</b>	2003 £'000
Net book value	<b>56,419</b>	53,791

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**19. Other assets**

	<b>Group</b>		<b>Bank</b>	
	<b>2004</b>	2003	<b>2004</b>	2003
	<b>£'000</b>	£'000	<b>£'000</b>	£'000
Foreign exchange contracts	<b>13,904</b>	9,343	<b>13,904</b>	9,343
Sundry debtors	<b>5,269</b>	8,038	<b>5,269</b>	8,038
Other	<b>85,389</b>	40,644	<b>82,244</b>	40,439
	<b><u>104,562</u></b>	<u>58,025</u>	<b><u>101,417</u></b>	<u>57,820</u>
Amounts include:				
Due from parent and fellow subsidiary undertakings	<b><u>8,263</u></b>	<u>11,563</u>	<b><u>8,263</u></b>	<u>11,563</u>

**20. Deferred taxation**

<b>Group</b>	<b>2004</b>	2003
	<b>£'000</b>	£'000
Timing differences	<b>24,944</b>	24,112
Accelerated capital allowances	<b>(11,498)</b>	(9,293)
	<b><u>13,446</u></b>	<u>14,819</u>
<b>Bank</b>	<b>2004</b>	2003
	<b>£'000</b>	£'000
Timing differences	<b>24,205</b>	23,372
Accelerated capital allowances	<b>(182)</b>	(1,414)
	<b><u>24,023</u></b>	<u>21,958</u>
	<b>Group</b>	<b>Bank</b>
	<b>£'000</b>	<b>£'000</b>
At 1 October 2003	14,819	21,958
Charge to profit and loss account	(1,373)	2,065
<b>At 30 September 2004</b>	<b><u>13,446</u></b>	<b><u>24,023</u></b>

It is not considered necessary to provide for taxation on capital gains which might arise on the disposal of subsidiary undertakings at their balance sheet amounts, as it is anticipated that any liability will be either exempt or covered by other reliefs. Deferred taxation is not provided in respect of capital gains which might arise on the disposal of properties which are held for continuing use by the business. If there is a binding agreement to dispose of an asset then the liability to capital gains tax is included in the tax charge for the year.

There are no other material liabilities for deferred taxation not provided.

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**21. Deposits by banks**

<b>Group and Bank</b>	<b>2004</b> <b>£'000</b>	<b>2003</b> <b>£'000</b>
Repayable on demand	<b>84,655</b>	301,079
With agreed maturity dates or periods of notice by remaining maturity:		
- 3 months or less but not repayable on demand	<b>389,128</b>	626,220
- 1 year or less but over 3 months	<b>40,160</b>	2,637
- 5 years or less but over 1 year	<b>244,000</b>	200,000
- over 5 years	<b>44,950</b>	52,027
	<b><u>802,893</u></b>	<b><u>1,181,963</u></b>

Amounts include:

Due to parent and fellow subsidiary undertakings	<b><u>802,784</u></b>	<b><u>1,179,326</u></b>
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**22. Customer accounts**

	<b>Group</b>		<b>Bank</b>	
	<b>2004</b> <b>£'000</b>	<b>2003</b> <b>£'000</b>	<b>2004</b> <b>£'000</b>	<b>2003</b> <b>£'000</b>
Repayable on demand	<b>4,273,921</b>	4,200,274	<b>4,274,993</b>	4,202,887
With agreed maturity dates or periods of notice by remaining maturity:				
- 3 months or less but not repayable on demand	<b>1,113,076</b>	1,039,882	<b>1,113,076</b>	1,039,882
- 1 year or less but over 3 months	<b>417,855</b>	208,948	<b>591,354</b>	208,948
- 5 years or less but over 1 year	<b>66,097</b>	381,518	<b>66,095</b>	555,017
- over 5 years	<b>17,460</b>	18,148	<b>17,460</b>	18,148
	<b><u>5,888,409</u></b>	<b><u>5,848,770</u></b>	<b><u>6,062,978</u></b>	<b><u>6,024,882</u></b>

Amounts include :

Due to subsidiary undertakings			<b><u>176,086</u></b>	<b><u>176,112</u></b>
Due to parent and fellow subsidiary undertakings	<b><u>7,521</u></b>	<b><u>10,889</u></b>	<b><u>7,521</u></b>	<b><u>10,889</u></b>

**23. Debt securities in issue**

<b>Group and Bank</b>	<b>2004</b> <b>£'000</b>	<b>2003</b> <b>£'000</b>
Other debt securities in issue by remaining maturity:		
- 3 months or less	<b><u>3,000</u></b>	<b><u>3,000</u></b>

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 24. Other liabilities

	Group		Bank	
	2004 £'000	2003 £'000	2004 £'000	2003 £'000
Foreign exchange contracts	13,889	9,052	13,889	9,052
Taxation	5,861	6,921	2,417	3,375
Defeasance deposits	134,639	132,974	134,639	132,974
Other liabilities	125,391	86,758	121,759	82,637
	<u>279,780</u>	<u>235,705</u>	<u>272,704</u>	<u>228,038</u>
Amounts include:				
Due to parent and fellow subsidiary undertakings	<u>37,957</u>	<u>26,562</u>	<u>37,957</u>	<u>26,562</u>

### 25. Provisions for liabilities and charges

	Pensions and similar obligations £'000	Reorganisation £'000	Other £'000	Total £'000
<b>Group and Bank</b>				
At 1 October 2003	1,394	10,047	9,340	20,781
Charge to profit and loss account	3,525	-	15,602	19,127
Transfers	-	(504)	504	-
Provisions utilised	(317)	(5,934)	(2,192)	(8,443)
<b>At 30 September 2004</b>	<u>4,602</u>	<u>3,609</u>	<u>23,254</u>	<u>31,465</u>

#### Pensions and similar obligations

The Bank provided for post-retirement health care under a defined benefit scheme for pensioners and their dependent relatives for which a provision has been raised. This is a closed scheme and the provision will be utilised over the life of the remaining scheme members.

#### Reorganisation

A reorganisation provision was recognised during the year ended 30 September 2002 and related to a programme initiated by the ultimate parent company, NAB. This programme, which is based around a fundamental review of operations, is principally in relation to the streamlining of support and service functions. Implementation of the programme is underway and full utilisation of the provision is expected by March 2005.

#### Other

This category includes:

- provision for surplus leased space. The Group provides for committed rental expense on surplus lease space in line with the expected years' exposure on individual leases where the property is unoccupied. The provision will be utilised over the remaining life of the lease or until the lease is assigned. The provision is measured at present values by discounting anticipated future cash flows.
- provision for costs associated with claims for mis-sold endowment policies. If a customer believes that an endowment policy may have been mis-sold by the Bank, they are able to have the basis of the advice examined, subject to certain time limits. The provision recognised is the best estimate of future costs given current claims experience.
- provision for costs arising in respect of a number of legal actions and claims arising in the ordinary course of the Bank's business.
- a provision of £6,317,000 has been raised in the current financial year in respect of the closure of National Custodian Services, an operational unit within Clydesdale Bank PLC.

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 26. Subordinated liabilities

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

Details of subordinated liabilities in excess of 10% of the total balance are disclosed below.

	2004 £'000	2003 £'000
<b>Undated loan capital</b>		
5.53% Undated subordinated notes	65,000	85,000
5.185% Undated subordinated notes	30,000	30,000
	<u>95,000</u>	<u>115,000</u>
Other undated subordinated notes	155,000	135,000
	<u>250,000</u>	<u>250,000</u>

The rates of interest stated above apply as at 30 September 2004.

### 27. Called up share capital

	Number	£
<b>Authorised</b>		
Ordinary shares of £1 each - equity	<u>204,785,000</u>	<u>204,785,000</u>
<b>Allotted, called up and fully paid</b>		
Ordinary shares of £1 each - equity		
At 30 September 2004 and 2003		<u>204,785,000</u>

### 28. Reserves

	The Bank and subsidiary undertakings £'000	Associate £'000	Group £'000	Bank £'000
<b>Share premium account</b>				
At 30 September 2004 and 2003	<u>45,215</u>	<u>-</u>	<u>45,215</u>	<u>45,215</u>
<b>Revaluation reserve</b>				
At 1 October 2003	6,320	-	6,320	6,318
Revaluation of properties	3,193	-	3,193	3,193
Transfer to profit and loss account	(215)	-	(215)	(215)
At 30 September 2004	<u>9,298</u>	<u>-</u>	<u>9,298</u>	<u>9,296</u>

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

28. Reserves (continued)	The Bank and subsidiary undertakings	Associate	Group	Bank
Profit and loss account	£'000	£'000	£'000	£'000
At 1 October 2003	299,187	1,974	301,161	293,657
Retained profit for the financial year	15,098	31	15,129	11,167
Transfer from revaluation reserve	215	-	215	215
<b>At 30 September 2004</b>	<b>314,500</b>	<b>2,005</b>	<b>316,505</b>	<b>305,039</b>

## 29. Memorandum items

Group and Bank	Contract amount 2004 £'000	Risk weighted amount 2004 £'000	Contract amount 2003 £'000	Risk weighted amount 2003 £'000
<b>Contingent liabilities</b>				
Acceptance and endorsements	22,109	10,109	26,409	8,779
Guarantees and assets pledged as collateral security - guarantees and irrevocable letters of credit	151,895	91,638	179,086	113,019
Other contingent liabilities	309	309	-	-
	<b>174,313</b>	<b>102,056</b>	<b>205,495</b>	<b>121,798</b>
<b>Commitments</b>				
Other commitments				
- documentary credits and short term trade-related transactions	11,737	2,347	21,423	4,285
- undrawn formal standby facilities credit lines and other commitments to lend				
- 1 year or less	3,241,161	92,073	2,901,026	63,076
- over 1 year	319,052	-	252,303	-
	<b>3,571,950</b>	<b>94,420</b>	<b>3,174,752</b>	<b>67,361</b>

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

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

## 30. Capital commitments

The Group had future capital expenditure which had been contracted but not provided in the Financial Statements of £95,000 (2003 £Nil) at 30 September 2004.

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**31. Lease commitments**

<b>Group and Bank</b>	<b>Land and buildings</b>	Land and buildings
<b>Operating lease commitments</b>		
	<b>2004</b>	2003
	<b>£'000</b>	£'000
Payments committed to be made during the next year under non-cancellable operating leases which expire:		
- within 1 year	<b>171</b>	158
- between 1 and 5 years	<b>1,058</b>	2,416
- over 5 years	<b>11,551</b>	9,210
	<b>12,780</b>	11,784

**32. Other contingent liabilities**

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

**33. Derivatives and other financial instruments**

**a) Management of risk**

Management of risk is fundamental to the business of being a financial services provider and is an essential element of the Group's strategy. Financial services organisations face an array of risks.

An enterprise-wide risk management model structure implemented throughout the NAB Group comprises a common policy framework and a set of controls to achieve standardisation of risk/reward practices across the NAB Group. NAGE Group is responsible for the identification and quantification of the particular risks it is exposed to and for implementation of appropriate NAB Group policies, procedures and controls.

Overview and monitoring of this process throughout the NAB Group is undertaken by Risk Management. Risk Management comprises Credit Risk Management, Internal Audit, Operational Risk, Insurance, Regulatory Compliance, Market Risk and Legal. The Group is one of a number of United Kingdom and Republic of Ireland subsidiary companies of the NAB Group which has delegated oversight of risk management to NAGE. In managing risk, NAGE Risk Management operates within the common policy framework and follows the guidelines and procedures of the NAB Group.

NAGE Risk Management's role is to constantly monitor and systematically assess NAGE's risk profile in existing and proposed business operations, and to assist business units in the design and implementation of appropriate risk management policies and strategies. NAGE Risk Management also works with the businesses to promote awareness of the need to manage risk.

Developments continue to be made in the quantification of risks and the allocation of appropriate risk capital. Portfolio management methods are being adopted to manage the Group's risk profile. Modelling to forecast future risk management trends is being used increasingly to assist in decision making. This will continue to increase in importance as the NAB Group prepares to implement Basel II across the various risk streams.

Risk Management prepares and submits to the NAB Board of directors ("NAB Board"), the NAB Group risk profile. This document profiles the major recognised on-balance sheet and off-balance sheet strategy/performance and operational risks, together with procedures for their day-to-day management, control and responsibility.

The NAB Group Risk Committee reviews in greater detail the NAB Group's risk and return appetite and oversees the NAB Group's overall control framework. This Risk Committee has cross membership with the NAB Principal Board Audit Committee.

The NAB Group Risk Committee covers key elements of risk, including regulatory compliance, operational risk, market risk, internal audit, credit risk and balance sheet management. The framework is consistent with the proposed supervisory review process (Pillar 2) of Basel II.

## **CLYDESDALE BANK PLC**

### **Notes to the Financial Statements (continued)**

#### **33. Derivatives and other financial instruments (continued)**

##### **a) Management of risk (continued)**

The majority of risk policy decisions are made within each business unit.

A NAB Group Risk Forum comprising executive and senior management, is the principal risk policy decision making body within the NAB Group executive management. A Risk Management Committee also exists in NAGE.

This forum reviews and approves the more strategic risk assessments and is supported by the NAB Group Risk Management Committee, which has an operational focus, and Risk Management Committees in each region and/or line of business.

Major balance sheet risk areas and their management are outlined below but many other types of risk such as payment systems, computer systems fraud, legislative compliance, business continuity/disaster recovery and e-commerce, are routinely managed throughout NAGE.

The NAB Group has commenced a review of its Risk Management function both internally and through the engagement of external consultants in order to improve the Risk Management practices of the NAB Group by benchmarking them against best practice.

##### ***Operational Risk***

Operational risk is the risk of loss resulting from inadequate or failed processes, people or systems, or from external events.

The Operational Risk and Insurance function is responsible for:

- operational risk policy development;
- operational risk advice;
- business continuity planning advice;
- support in risk evaluation;
- operational risk reporting; and
- co-ordination of the risk assessment and approval process of new and re-engineered products and processes to ensure change initiatives are robustly assessed from a risk perspective.

Individual business units own and are responsible for the identification, assessment and mitigation of their risk profile. Various reports are produced at business unit's executive management, and Board level for their information and to assist in monitoring and where necessary determining appropriate actions.

To enhance the Group's ability to identify, measure and manage operational risk a framework and methodology has been developed and implemented. The methodology includes risk modelling and risk evaluation. Risk modelling is the statistical estimation of operational risk exposure based on internal and external historical loss experience and approved within NAGE Risk Policy validation processes. Risk evaluation involves the quality mapping and appraisal of the internal control environment based on end-to-end evaluation criteria.

##### ***Balance sheet risk***

The NAB Group Asset and Liability Management Committee ("NAB Group ALCO"), under delegated NAB Board authority, sets policies in relation to the management of structural balance sheet exposures. These exposures include structural interest rate risk, structural foreign exchange risk and liquidity risk. The NAB Group's global structural balance sheet risk is monitored against approved policies by NAB Group Balance Sheet Management and reported on a monthly basis to NAB Group ALCO. An Independent Risk Oversight function was created at the commencement of the year to oversee the balance sheet management process. The Independent Risk Oversight function is mandated to verify the quantum of balance sheet risk in addition to ensuring the robustness of the risk management process. It has dual but separate reporting lines to NAB Group ALCO and to the NAB Risk Committee via the Executive General Manager, Risk Management.

The NAGE Group has an Asset and Liability Management Committee ("NAGE Group ALCO") which has been delegated the responsibility for managing local structural balance sheet risks in accordance with NAB Group Balance Sheet Management policies. NAB Group ALCO supervises the management of these local structural risks and monitors activity for compliance with NAB Group policies.

## CLYDESDALE BANK PLC

### Notes to the Financial Statements (continued)

#### 33. Derivatives and other financial instruments (continued)

##### *Balance sheet risk (continued)*

Exposures are reported to NAGE ALCO on a monthly basis. NAGE has a Structural Earnings at Risk Limit to cover balance sheet interest rate exposure. This is allocated to business units by NAGE ALCO. Structural balance sheet risk is also reported regularly to NAB Group ALCO.

##### *Credit risk*

Credit risk is the potential that a bank borrower or a counterparty will fail to meet its obligations in accordance with agreed terms.

The NAB Group's credit risk management infrastructure is framed to provide principles and practices for the maintenance of appropriate asset quality across the NAB Group. These principles and practices are followed by the Group.

Credit Risk Management, a unit of Risk Management, is structured to develop and maintain credit policies and key credit risk systems, provide monitoring and reporting of asset quality, and undertake the independent oversight of credit portfolios across the Group.

The management of credit risk within the Group is achieved through both the traditional focuses on approval and monitoring of individual transactions together with analysis of the performance of the various credit risk portfolios. Portfolio monitoring covers such areas as industry or geographic concentrations and delinquency trends.

##### *Establishing an appropriate credit risk environment*

Significant credit risk strategies and policies are approved and reviewed annually by the NAB Board and the NAB Risk Committee which, through such policies as borrower (single large exposure) and industry concentration limits, also establishes the NAB Group's tolerance for risk. These policies are delegated to, and disseminated under the guidance and control of, executive management within each region.

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

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

##### *Credit granting process*

The Group has established processes for the granting of credit.

These include:

- establishment of overall credit limits at the level of individual borrowers and counterparties, and groups of connected counterparties for both on-balance sheet and off-balance sheet exposures;
- satisfaction with repayment capacity and integrity of the counterparty;
- use of financial covenants;
- use of collateral;
- consideration of economic and industry conditions; and
- an objective customer rating assessment system.

These are supported by documented policies and processes for the granting of credit within each region. The key elements of the process include:

- authorities for the approving of credit; and
- a system of overview of credit approvals by a higher level of authority to ensure adherence to policies and good credit practice.

The delegated authorities are aligned to the counterparty risk by the inclusion of customer ratings in the authority matrix.

The system, based on probability of default of a counterparty, has been implemented within the Group and provides meaningful differentiation of credit risk, enabling greater focus in pricing for risk.

## CLYDESDALE BANK PLC

### Notes to the Financial Statements (continued)

#### 33. Derivatives and other financial instruments (continued)

##### *Credit risk (continued)*

For consumer credit, scoring solutions are in place and are supported by the mandatory use of appropriate monitoring tools. These tools provide the essential continual review of data integrity, scorecard performance and decision strategies. Software to validate and verify input data is used globally to support data integrity and prevent fraudulent activity.

##### *Maintaining an appropriate credit administration, measurement and monitoring process*

Effective credit administration operations and adequate control over back office procedures such as monitoring documentation, contractual requirements, legal covenants and collateral are recognised as being vitally important aspects of the end-to-end credit process.

The NAB Group assigns these responsibilities to various business units within each region together with centralised structures supporting the branch network and business bankers.

Monitoring the condition of individual credits in the business units in the Financial Services businesses and Institutional Markets & Services principally rests with the customer-facing relationship managers, with overview by supervising authorities.

##### *Ensuring adequate controls over credit risk*

There is a formal process, undertaken by specialist units, of independent oversight of credit in each region across the NAB Group. Detailed quarterly reports are submitted to business unit executive management, EBAC and the risk committee. Additionally, credit processes and policy compliance are subject to internal audit and targeted credit reviews of specific business units or regions are undertaken as considered appropriate.

On a regular basis, credit facilities that are outside agreed arrangements are reported to the appropriate levels of authority for attention and monitoring of actions taken.

Credits showing adverse trends are passed to specialist units that undertake the collections and recovery processes. The NAB Group utilises skilled internal resources supported by external secondment.

Through the use of due diligence techniques, the NAB Group regularly targets areas of interest / concern within its credit portfolio to review and maintain the quality of the credit portfolio.

The Group has no significant concentration of exposures to any one counterparty other than to its ultimate parent NAB. The Group maintains overall credit risk limits on intercompany exposures to ensure exposure levels are acceptable in the event of default when settlement becomes due.

##### *Liquidity risk*

Liquidity risk is the risk that the Group is unable to service its cash flow obligations today or in the future. Liquidity within the Group is managed in accordance with the regulatory requirements of the UK Financial Services Regulatory Authority and with policies approved by the NAB Board with oversight from NAB ALCO and NAB ALCO.

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

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

A contingency plan has also been established for management of an escalated liquidity requirement where the Group experiences either restricted access to wholesale funding or a large increase in withdrawal of funds. The Group primarily sources an element of its liquidity requirements through transactions with the London Branch of NAB which has substantial access to the money markets.

## CLYDESDALE BANK PLC

### Notes to the Financial Statements (continued)

#### 33. Derivatives and other financial instruments (continued)

##### *Market risk*

Market risk is the risk that the value of financial instruments will be adversely affected by changes in the market value of the underlying instrument, reference rate or index.

Market risk is also relevant to the Group's activity in which it primarily acts as a counterparty to satisfy customers' needs through the provision of a full range of foreign exchange and interest rate related services including derivative financial instruments. In compliance with NAB Group policies, the Group enters into similar but opposite transactions with NAB to hedge their position and effectively eliminate any market risk.

##### *Financing and structural interest rate risk*

In carrying out its business activities, the Group strives to meet customer demand for products with various interest rate structures and maturities. Sensitivity to interest rate movements arises from mismatches in the repricing dates, cash flows and other characteristics of assets and liabilities. As interest rates and yield curves change over time, the size and nature of these mismatches may result in a loss or gain in earnings.

In managing structural interest rate risks, the primary objective is to limit the extent to which net interest income could be impacted by an adverse movement in interest rates. NAGE ALCO is responsible for managing the structural interest rate risk, in accordance with approved NAB Group policy.

Structural interest rate risk is calculated using balance sheet simulation processes that are undertaken across NAGE's banking operations. The result of balance sheet simulations, together with other balance sheet risk management information and strategies, are presented and reviewed by NAGE ALCO, NAB Group ALCO and at scheduled Board meetings.

The Group applies a wide range of interest rate scenarios in measuring structural interest rate risk. These interest rate scenarios are derived using estimates of volatility to generate a range of potential outcomes around the market implied yield curve. This provides the ability to derive a statistical distribution of potential movements in net interest income. To capture a wide range of potential outcomes, structural interest rate risk is measured to a 99% confidence interval.

#### **b) Use of derivatives**

The Group uses derivatives to hedge its own balance sheet position. The Group's principal objective in holding or issuing derivatives for purposes other than customer related transactions is asset and liability management. The operations of the Group are subject to the risk of interest rate fluctuations, to the extent that there is a difference between the amount of the interest-earning assets and interest-bearing liabilities that mature or reprice in specified periods. The principal objectives of asset and liability management are to protect levels of net interest income, while maintaining acceptable levels of interest rate and liquidity risk and to facilitate the funding needs of the Group. To achieve these objectives, the Group uses a combination of derivative financial instruments, including foreign exchange, futures, forward rate agreements, swaps, options, caps, floors, and other contingent or exchange traded contracts. These hedge transactions within the NAB Group's European subsidiaries are entered into with National Australia Bank Limited.

##### *Derivatives*

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

##### *Forward and futures contracts*

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

##### *Options*

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

## **CLYDESDALE BANK PLC**

### **Notes to the Financial Statements (continued)**

#### **33. Derivatives and other financial instruments (continued)**

##### *Swaps*

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

##### *Other financial instruments*

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

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 33. Derivatives and other financial instruments (continued)

#### Summary of outstanding derivative contracts

The following tables give the contract amount and fair values at balance sheet date of the Group's outstanding derivative contracts, distinguishing between foreign exchange rate and interest rate related contracts. The fair value is the amount at which instruments could be exchanged in an arm's length transaction. The notional contract amount does not represent the Group's real exposure to credit risk which is limited to the current cost of replacing contracts at current market rates should the counterparties default. No account is taken of master netting agreements which reduce the gross exposure. The fair value at a particular point in time gives no indication of whether future gains or losses will be incurred, or any indication of the size that those gains or losses are likely to be.

#### Group

	Contract amount		Fair value		Contract amount		Fair value	
	2004	2004	Positive	Negative	2003	2003	Positive	Negative
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
<b>Non trading derivatives</b>								
<i>Foreign exchange derivatives</i>								
Forward foreign exchange	1,194,064	12,751	12,736	1,151,720	7,718	7,455		
Other foreign exchange	142,398	1,153	1,153	168,960	1,484	1,483		
Total	<u>1,336,462</u>	<u>13,904</u>	<u>13,889</u>	<u>1,320,680</u>	<u>9,202</u>	<u>8,938</u>		
<i>Equity derivatives</i>								
Options	24,910	455	-	22,166	517	-		
<i>Commodity derivatives</i>								
Options	1,680	289	289	4,388	221	221		
<i>Interest rate derivatives</i>								
Swaps	5,395,763	27,676	66,593	5,665,537	59,467	97,640		
Forward rate agreements	930,000	-	461	-	-	-		
Options	989,994	7,487	11,661	976,410	7,586	15,912		
Total	<u>7,315,757</u>	<u>35,163</u>	<u>78,715</u>	<u>6,641,947</u>	<u>67,053</u>	<u>113,552</u>		
<b>Total non trading derivatives</b>	<b><u>8,678,809</u></b>	<b><u>49,811</u></b>	<b><u>92,893</u></b>	<b><u>7,989,181</u></b>	<b><u>76,993</u></b>	<b><u>122,711</u></b>		

An analysis of the contract amount and positive fair value of investments entered into with third parties by the counterparty type is set out below:

Counterparty	Contract amount		Fair value	
	2004	2004	2003	2003
	£'000	£'000	£'000	£'000
fellow subsidiary undertakings	7,295,138	27,552	6,484,344	41,109
Other OECD Banks	500	-	83,784	1,114
Other	1,383,171	22,259	1,421,053	34,770
Total	<u>8,678,809</u>	<u>49,811</u>	<u>7,989,181</u>	<u>76,993</u>
Remaining maturity:				
- within one year	4,448,006	23,641	2,705,832	26,896
- between one and five years	3,116,409	13,188	4,156,508	36,353
- over five years	1,114,394	12,982	1,126,841	13,744
Total	<u>8,678,809</u>	<u>49,811</u>	<u>7,989,181</u>	<u>76,993</u>

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 33. Derivatives and other financial instruments (continued)

#### Interest rate sensitivity gap analysis

Part of the Group's return on financial instruments is obtained from controlled mismatching of the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rates or, if earlier, the dates on which the instruments mature. The tables below summarise these repricing mismatches on the Group's non-trading book as at 30 September 2004 and 30 September 2003. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date.

#### Interest rate sensitivity gap

2004	Not more than three months	More than three months but not more than six months	More than six months but not more than one year	More than one year but not more than five years	More than five years	Non - interest bearing	Total
Group	£'000	£'000	£'000	£'000	£'000	£'000	£'000
<b>Assets:</b>							
Loans and advances to banks	752,844	159	172	10,836	505	8,258	772,774
Loans and advances to customers	5,412,389	232,263	378,657	903,345	432,935	(66,837)	7,292,752
Debt securities and equity shares	60,778	-	-	-	-	538	61,316
Other assets	-	-	-	-	-	634,169	634,169
<b>Total assets</b>	<b>6,226,011</b>	<b>232,422</b>	<b>378,829</b>	<b>914,181</b>	<b>433,440</b>	<b>576,128</b>	<b>8,761,011</b>
<b>Liabilities:</b>							
Deposits by banks	762,733	35,160	5,000	-	-	-	802,893
Customer accounts	4,958,464	151,108	118,087	56,877	888	602,985	5,888,409
Debt securities in issue	3,000	-	-	-	-	-	3,000
Other liabilities	134,639	-	-	-	-	1,106,267	1,240,906
Subordinated liabilities	250,000	-	-	-	-	-	250,000
Shareholders' funds	-	-	-	-	-	575,803	575,803
<b>Total liabilities and shareholders' funds</b>	<b>6,108,836</b>	<b>186,268</b>	<b>123,087</b>	<b>56,877</b>	<b>888</b>	<b>2,285,055</b>	<b>8,761,011</b>
Off balance sheet items	(624,835)	(94,547)	463,827	711,199	(455,644)	-	-
Interest rate sensitivity gap	(507,660)	(48,393)	719,569	1,568,503	(23,092)	(1,708,927)	-
<b>Cumulative gap</b>	<b>(507,660)</b>	<b>(556,053)</b>	<b>163,516</b>	<b>1,732,019</b>	<b>1,708,927</b>	<b>-</b>	<b>-</b>

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 33. Derivatives and other financial instruments (continued)

#### Interest rate sensitivity gap analysis (continued)

2003	Not more than three months	More than three months but not more than six months	More than six months but not one year	More than one year but not five years	More than five years	Non - interest bearing	Total
Group	£'000	£'000	£'000	£'000	£'000	£'000	£'000
<b>Assets:</b>							
Loans and advances to banks	1,089,744	-	-	7,147	16,958	8,273	1,122,122
Loans and advances to customers	5,663,567	197,447	240,290	869,187	317,867	-	7,288,358
Debt securities and equity shares	-	-	-	-	-	1,511	1,511
Other assets	-	-	-	-	-	472,261	472,261
<b>Total assets</b>	<b>6,753,311</b>	<b>197,447</b>	<b>240,290</b>	<b>876,334</b>	<b>334,825</b>	<b>482,045</b>	<b>8,884,252</b>
<b>Liabilities:</b>							
Deposits by banks	1,181,963	-	-	-	-	-	1,181,963
Customer accounts	4,765,809	124,553	105,346	205,132	1,192	646,738	5,848,770
Debt securities in issue	3,000	-	-	-	-	-	3,000
Other liabilities	132,974	-	-	-	-	910,064	1,043,038
Subordinated liabilities	250,000	-	-	-	-	-	250,000
Shareholders' funds	-	-	-	-	-	557,481	557,481
<b>Total liabilities and shareholders' funds</b>	<b>6,333,746</b>	<b>124,553</b>	<b>105,346</b>	<b>205,132</b>	<b>1,192</b>	<b>2,114,283</b>	<b>8,884,252</b>
Off balance sheet items	(1,861,989)	98,930	116,646	1,935,097	(288,684)	-	-
Interest rate sensitivity gap	(1,442,424)	171,824	251,590	2,606,299	44,975	(1,632,264)	-
<b>Cumulative gap</b>	<b>(1,442,424)</b>	<b>(1,270,600)</b>	<b>(1,019,010)</b>	<b>1,587,289</b>	<b>1,632,264</b>	<b>-</b>	<b>-</b>

These tables do not take into account the effect of the interest rate options used by the Group to hedge its own positions. Details of these options are shown above under the interest rate derivatives disclosures.

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

**CLYDESDALE BANK PLC**  
**Notes to the Financial Statements (continued)**

**33. Derivatives and other financial instruments (continued)**

**Unrecognised gains/(losses) on instruments used for hedging**

<b>2004</b>	<b>Gains £'000</b>	<b>Losses £'000</b>	<b>Total net gains/(losses) £'000</b>
At 1 October 2003	76,993	122,711	(45,718)
Gains and losses arising in previous years that were recognised in year ended 30 September 2003	48,986	61,688	(12,702)
Gains and losses arising before 1 October 2003 that were not recognised in year ended 30 September 2004	28,007	61,023	(33,016)
Gains and losses arising after 1 October 2003 that were not recognised in year ended 30 September 2004	21,804	31,870	(10,066)
<b>At 30 September 2004</b>	<b>49,811</b>	<b>92,893</b>	<b>(43,082)</b>
Of which gains and losses expected to be recognised in the year ended:			
30 September 2005	23,641	31,312	(7,671)
30 September 2006 or after	26,170	61,581	(35,411)
<b>2003</b>	<b>Gains £'000</b>	<b>Losses £'000</b>	<b>Total net gains/(losses) £'000</b>
At 1 October 2002	87,624	99,994	(12,370)
Gains and losses arising in previous years that were recognised in year ended 30 September 2003	18,544	17,816	728
Gains and losses arising before 1 October 2002 that were not recognised in year ended 30 September 2003	69,080	82,178	(13,098)
Gains and losses arising after 1 October 2002 that were not recognised in year ended 30 September 2003	7,913	40,533	(32,620)
<b>At 30 September 2003</b>	<b>76,993</b>	<b>122,711</b>	<b>(45,718)</b>
Of which gains and losses expected to be recognised in the year ended:			
30 September 2004	26,896	25,788	1,108
30 September 2005 or after	50,097	96,923	(46,826)

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 34. Fair values of financial instruments

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

The estimated fair values are based on relevant information available for the last two years at September 30. These estimates are subjective in nature and involve matters of judgement. Changes in assumptions could have a material impact on the amounts estimated. The methodologies and assumptions used in the net fair value estimates are described below. These are not considered critical accounting policies of the Group, as they do not impact the recognition and measurement of items in the financial statements.

There are various limitations inherent in this disclosure. Not all of the Group's financial instruments can be exchanged in an active trading market. In addition, it is the Group's intent to hold most of its financial instruments to maturity and therefore it is not probable that the fair values shown will be realised in a current transaction. The methods used to estimate fair value exclude a wide range of intangible, franchise and relationship benefits such as core deposits and credit card intangibles, which are integral to a complete assessment of the Group's financial position. As a consequence, the aggregate fair value does not represent the underlying value of the Group.

Group		Carrying Value 2004 £'000	Fair value 2004 £'000	Carrying Value 2003 £'000	Fair value 2003 £'000
	Footnote				
<b>Financial assets:</b>					
Cash and balances at central banks	(a)	60,151	60,151	65,672	65,672
Items in the course of collection from other banks	(a)	107,877	107,877	119,866	119,866
Loans and advances to banks	(b)	772,774	772,774	1,122,122	1,122,122
Loans and advances to customers	(b)	7,292,752	7,292,752	7,288,358	7,288,358
Debt securities	(c)	60,538	60,538	288	288
Equity shares	(c)	778	778	1,223	1,223
On balance sheet derivatives (see analysis in Note 33)	(d)	13,904	13,904	9,202	9,202
<b>Financial liabilities:</b>					
Deposits by banks	(e)	802,893	802,893	1,181,963	1,181,963
Items in the course of transmission to other banks	(a)	20,661	20,661	20,268	20,268
Customer accounts	(e)	5,888,409	5,888,409	5,848,770	5,848,770
Debt securities in issue	(f)	3,000	3,000	3,000	3,000
Notes in circulation	(a)	823,890	823,890	681,751	681,751
Subordinated liabilities	(f)	250,000	250,000	235,705	235,705
On balance sheet derivatives (see analysis in Note 33)	(d)	13,889	13,889	8,938	8,938

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

- the carrying amounts of these financial assets and financial liabilities approximate their fair value as they are short term in nature or are receivable or payable on demand;
- the carrying value of loans and advances is net of specific and general provisions for doubtful debts and unearned income. The fair values of loans and advances equate to the carrying value at 30 September.
- debt securities and equity shares consist of investment and other securities. The fair values of debt securities and equity shares are based on quoted closing market prices at September 30;
- the fair values of derivative financial instruments, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from quoted closing market prices at balance date, discounted cash flow models or option pricing models as appropriate;
- with respect to deposits by banks and customer accounts, the fair value equals the carrying value at 30 September; and

# CLYDESDALE BANK PLC

## Notes to the Financial Statements (continued)

### 34. Fair values of financial instruments (continued)

- (f) the fair value of debt securities in issue and subordinated liabilities are calculated based on quoted market prices. For those debt issues where quoted market prices are not available, the fair values equate to the carrying value at 30 September.

### 35. Related party transactions

#### *Transactions with directors, key management and their close family members*

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

	<b>Persons 2004 Number</b>	<b>Amount 2004 £'000</b>	Persons 2003 Number	Amount 2003 £'000
Loans - balance at 30 September	<u>8</u>	<u>2,152</u>	<u>6</u>	<u>1,195</u>

#### *Other related party transactions*

In the normal course of business the Group maintains accounts and conducts transactions with other members of the NAB Group. This business is conducted at prevailing market rates and terms and includes deposits taken and placed, interest rate and foreign exchange swaps and the provision of technology and other services. The Group has taken advantage of the exemption under FRS 8 "Related Party Transactions" not to disclose full details of these transactions as more than 90% of the voting rights of the Group are controlled by NAB Group and the consolidated Financial Statements of the NAB Group are publicly available.

The Group has transactions with the pension scheme detailed in note 6. The Group charges the pension scheme with the cost of administration which amounted to £90,218 in the year ended 30 September 2004 (2003 £65,974). The Group has deposits of £Nil (2003 £3,366,884) at the year end placed by the pension scheme at market rates.

### 36. Assets and liabilities denominated in foreign currency

	<b>Group</b>		<b>Bank</b>	
	<b>2004 £'000</b>	2003 £'000	<b>2004 £'000</b>	2003 £'000
Sterling	<b>8,394,831</b>	8,435,828	<b>8,550,443</b>	8,596,283
Currencies other than sterling	<b>366,180</b>	448,424	<b>366,180</b>	448,424
Total assets	<u><b>8,761,011</b></u>	<u>8,884,252</u>	<u><b>8,916,623</b></u>	<u>9,044,707</u>
Sterling	<b>8,394,831</b>	8,435,828	<b>8,550,443</b>	8,596,283
Currencies other than sterling	<b>366,180</b>	448,424	<b>366,180</b>	448,424
Total liabilities and shareholders' funds	<u><b>8,761,011</b></u>	<u>8,884,252</u>	<u><b>8,916,623</b></u>	<u>9,044,707</u>

The above table cannot be considered to reflect exposure to foreign exchange risk as it does not take into account off balance sheet items.

## CLYDESDALE BANK PLC

### Notes to the Financial Statements (continued)

#### 37. Employees

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

	<b>2004</b>	2003
	<b>Number</b>	Number
Managers	<b>580</b>	557
Clerical staff	<b>2,223</b>	2,324
	<b><u>2,803</u></b>	<u>2,881</u>

All staff are contracted employees of NAGE. The numbers above disclose the staff remunerated directly by the Group but exclude employees working within other NAGE subsidiaries who provide support services to the Group.

#### 38. Ultimate parent undertaking

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

Copies of Group Financial Statements prepared in respect of the Bank may be obtained from the Corporate Affairs Department, Clydesdale Bank PLC, 30 St. Vincent Place, Glasgow, G1 2HL.