ANNUAL REPORT & ACCOUNTS

2011

the COVENTRY
TLC not PLC

Chairman
David Harding

Deputy Chairman and Senior Independent Director
Bridget Blow

Chief Executive
David Stewart

Executive directors
Colin Franklin, Sales and Marketing Director
John Lowe, Finance Director

Non-executive directors
Roger Burnell
Ian Geden
Ian Pickering
Fiona Smith
Glyn Smith

Secretary and General Counsel
Gill Davidson

Senior Management
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Peter Elcock
Rachel Haworth
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PERFORMANCE HIGHLIGHTS 2011

Strongly profitable

£84.6m

Profit before FSCS levy and merger related items increased by 12% over 2010.

(Operating profit after impairments and before exceptional items)

Net interest margin

0.72%

Just 0.72%, reflecting the benefit to members of sector leading cost-efficiency.

(Net interest income/Average total assets)

The most cost-efficient society

0.37%

Spending just 37p for every £100 of assets, Coventry is the most cost-efficient building society reported in the UK.

(Administrative expenses, depreciation and amortisation/Average total assets)

Very low impairments

0.05%

Amongst the lowest level reported by any major bank or building society.

(Impairment losses on loans and advances to customers/Average loans and advances to customers)

Increased lending

£4.0bn

Gross mortgage lending equivalent to 17% of all mortgage advances by building societies and mutual lenders.

Supporting homeowners

£1.7bn

Net mortgage lending equivalent to 18% of total growth in mortgage balances in the UK.

Record mortgage market share

£19.2bn

Coventry's share of total UK mortgage stock has increased by two thirds since 2006.

Growth in member savings

£1.4bn

Growth in 2011 represents double the Society's natural market share.

Record savings market share

£19.0bn

Record share of total UK savings, increasing balances by over 130% since 2006.

Fully funded loans

104%

All loans funded by savings and reserves.

Capital resources

£974m

Member reserves and other capital resources increased by £58m, providing security to members.

(Equity, subordinated liabilities and subscribed capital)

The highest capital ratio

22.8%

The highest core tier 1 ratio reported by any major high street bank or building society.

CHAIRMAN'S STATEMENT

Last year I reflected that 2010 might be seen as a period of relative calm before the developing sovereign debt crisis heightened economic uncertainties, bringing about the possibility of a second credit crunch and a return to recession across Europe.

Unfortunately this concern was well-founded. As we enter 2012, Government plans to reduce the UK budget deficit are being threatened by weaker economic growth, with reductions in revenue exacerbated by increased welfare expenditure as unemployment rises.

This difficult domestic environment is compounded by the ongoing crisis in the eurozone. At the end of 2011 the risk of sovereign debt default was already restricting the functioning of wholesale markets leading to concerns of a further credit squeeze.

As the economic crisis moves to its next phase, likely to be characterised by a sustained period of low growth, low interest rates and higher levels of unemployment, it is appropriate to review the performance of Coventry Building Society, not only in 2011 but for the five years since the first onset of the financial crisis in 2007.

The important point is that in 2011, as in the whole of this period, the Society delivered extremely strong results. This was achieved at a time of significant organisational change as the merger and integration of Stroud & Swindon Building Society was completed on time and within budget. This project has greatly enhanced the service offering to members. To achieve this whilst maintaining our normal mortgage and savings activity reflects great credit on those involved.

The Chief Executive's Review explains the 2011 performance in detail. I will focus on the longer term performance which I believe underlines the role that building societies, with sufficient clarity of strategy and excellence in execution, are capable of playing in the savings and mortgage market.

Over the five years of the credit crisis[1], during which time the new mortgage lending market contracted from £345 billion per annum to £141 billion per annum, the Society has lent £17.5 billion, maintaining a positive net lending position in every single year. Coventry is the only top ten building society to have increased its asset size in each one of the last five years.

Our share of net advances increased during this period from 0.8% to over 18% simply because we have been able to continue lending at a time when many of our peers or larger competitors have been unable to do so. As a result, our share of total mortgage stock has increased by two thirds.

The fact that this has been achieved without any diminution in the quality of lending is shown by the low level of arrears and defaults on the mortgage book, with 3 month arrears significantly less than half the industry average[2] and impairment charges that remain amongst the lowest reported by large mortgage lenders.

In addition, the Society has maintained strong credit ratings as recognised by major rating agencies, Fitch Ratings (A) and Moody's (A3). At the end of the period, the Society's core tier 1 ratio was 22.8%, the highest reported of any major building society, or indeed large mortgage lender.

The total organic growth in savings balances in the five years from the start of 2007 has been £8.6 billion (excluding £2.2 billion of balances acquired through the merger with Stroud & Swindon Building Society).

This performance represents the highest reported rate of organic growth in market share of any top ten building society. It is also worth highlighting that the Society's funding position has been further strengthened throughout the period by repeated success in accessing wholesale markets, raising in excess of £2 billion over the last five years, including inaugural covered bond issuances in 2011.

The Society has continued to invest in its systems, its branches and offices and in its people. In 2006 I reported that the Society's cost to mean asset ratio was the lowest in the building society sector at 0.53%. It is highly significant that Coventry has continued to be the best-performing society in this regard in every subsequent year, with the cost to mean asset ratio now lowered to just 0.37%. This is a considerable achievement given the substantial investment we have made to keep up with the changing requirements of the financial regulators.

I am particularly pleased that the Society's remarkable performance since 2006 has also been marked by an increase in the support to local communities and national charities alike. The Society has undertaken successful partnerships with RNIB, Macmillan Cancer Support, Age UK and The Royal British Legion, supported national fundraising events including Children in Need and Comic Relief and, possibly most importantly, provided volunteers and financial help to numerous local community groups.

The Society continues to be active in promoting greater understanding of personal finance amongst local schoolchildren and has extended this support to adults via partnerships with local advice centres.

The passion and commitment shown by members of staff in supporting these initiatives shows very well the type of organisation we aim to be.

In my opinion, the Society's performance throughout this period has been outstanding. The core values in which Coventry has always believed as a member focused traditional building society, providing a safe home for savings and maintaining a cautious approach to lending, are now recognised widely as a sound basis for a robust business model. It will come as no surprise, therefore, that I, and the rest of the Board, remain unanimous in believing that Coventry should stay an independent mutual building society.

This outstanding performance over the last five years is also a tribute to the executive management. Since 2006 half of the 20 largest building societies in the UK have lost their independence and some of the largest banks in the country have failed. As I consider the cost of these failures in terms of declining competition and choice, in terms of individual uncertainty or the loss of livelihoods, I am struck by the often understated contribution that Coventry's success represents.

As the UK economy faces further years of low growth and austerity measures – the "lost decade" we see increasingly discussed by analysts and media alike – the need for a robust and secure financial organisation, providing a safe haven for savings and mortgages for people to buy and move home, has never been greater. In this uncertain economic environment, I take confidence from the Society's outstanding record and believe that it remains well placed to serve both its borrowing and savings members.

I should like to thank the executive team and every member of staff for the commitment and skill they have shown in ensuring the continued success of Coventry Building Society.

David Harding
Chairman

[1] From 31 December 2006 to 31 December 2011.
[2] Council of Mortgage Lenders (CML).

FIVE YEAR HIGHLIGHTS

1 January 2007 to 31 December 2011

Strongly profitable

£309.7m

Profitability remained strong throughout the period, adding significantly to the capital and reserves of the Society.

(Profit before tax for the years ended 2007 to 2011)

Increased mortgage lending

£17.5bn

Continued lending as competitors cut back, increasing the Society's share of the new mortgage lending market from 0.85% to 2.81%. This resulted in the Society becoming a top ten lender for the first time in 2008, a position it has retained in each subsequent year.

Growth in mortgage balances

£9.2bn

The Society's share of UK net lending increased from 0.8% in 2006 to over 18% in both 2010 and 2011. This resulted in the largest reported organic increase in market share of a top ten building society.

Growth in member savings

£10.8bn

Coventry grew organically its share of the total savings market at a faster rate than any other large building society, with savings balances rising to a record £19.0 billion.

Growth in assets

£12.2bn

Coventry is the only top ten building society to grow its assets and report a profit in each of the last five years.

Very low impairments

0.08%

These continue to be amongst the lowest level reported by any major bank or building society.

(Five year average of impairment losses on loans and advances to customers/Five year average loans and advances to customers)

The most cost-efficient society

0.53% to 0.37%

Coventry was the most cost-efficient major building society in each of the last five years, lowering the cost to mean asset ratio from 0.53% to 0.37%. This means we spend 37p for every £100 of assets - the best ever performance reported by any UK building society.

(Administrative expenses, depreciation and amortisation/Average total assets)

Strengthened capital

£974m

The Society added £240m to its capital reserves during the period. At 22.8%, Coventry has the highest reported core tier 1 ratio of any major high street bank or building society highlighting financial strength and high quality assets.

(Equity, subordinated liabilities and subscribed capital)

Highly rated

'A' rated

Coventry Building Society is 'A' rated by Moody's (A3) and Fitch (A) and has remained so throughout the period. Its underlying Bank Financial Strength Rating is second only to one high street UK bank and no UK building society is higher rated using this measure.

Committed to communities

£6.5m plus

Over £6.5m has been donated to community and charitable activities, including £5.6m to The Royal British Legion's Poppy Appeal.

Investing in people

Gold

The Society has been assessed by Investors in People at Gold status. Coventry is one of the first retail financial services organisations to have received this recognition.

FOS complaints table

0

Coventry has not appeared in any of the tables of complaints published to date by the Financial Ombudsman Service (FOS), because too few complaints have been referred. It is the largest UK mortgage lender never to have appeared.

CHIEF EXECUTIVE'S REVIEW

I am pleased to report that Coventry Building Society once again recorded an outstanding annual performance, sustaining a track record of success that has set it apart from its peers since the financial crisis began in 2007.

In 2011, the Society continued to operate at levels well above its natural market share, recording further substantial growth in mortgages. A similar increase in the Society's share of the savings market was achieved, demonstrating our strength in growing retail deposits significantly in a very competitive environment.

Underlying profitability[1] also increased, reflecting continued control of costs and low levels of provisions.

When I reflect on the reports I have written since becoming Chief Executive I am reminded of the consistency of their content, during periods that extend from favourable conditions to the very difficult times we have experienced more recently.

This consistency is not to be underestimated. It is a sad fact that in the five years since the credit crisis began half of the top 20 building societies have lost their independence.

The outstanding ability of the Society to perform so strongly in this environment is underpinned by its simple business model and an unequivocal responsibility for serving the interests of its members. I believe that the Society's mutual status, and our resolve to manage the business accordingly, has been a key factor in this success.

The aim to retain balance between saving and borrowing members, without the demands of external shareholders to maximise profit, enables a consistent long-term view and, most importantly, moderates the requirement for risk-taking.

It promotes fairness, security and value as its key attributes. A focus on cost-efficiency whilst meeting the service expectations of members supports these goals.

However, it is the successful execution of this business model over many years that underpins Coventry's strength and in particular our ability to maintain control of risk, margin and cost that is the root of our consistent success.

This consistency can be seen clearly in our mortgage performance. Although our share of the mortgage market has increased significantly in the last five years to record levels, this is largely the result of maintaining lending volumes in a contracting market.

In 2011, the Society advanced £4.0 billion (2010: £3.5 billion). This equates to around 17% of all building society and mutual advances, whilst in net lending terms, the Society achieved over 18% of the total UK market, broadly maintaining the share we reported last year (2010: 20%).

For the fourth consecutive year, we expect to be one of the top ten mortgage lenders in the UK, a performance which was achieved for the first time in 2008. This position, for a business that in 2007 had a nominal market share of just under 1%, demonstrates very clearly not only the reduction of lending capacity over the last few years, but our success in maintaining lending volumes at pre-credit crisis levels.

In these conditions it is critical that we continue to focus on high quality business. In this, the constraints experienced by a number of our competitors have been to our advantage and I am pleased to confirm that Coventry's lending in 2011 was once again concentrated in low risk sectors.

[1] Underlying profitability refers to 'Operating profit after impairments and before exceptional items'.

It is important that our lending remains sustainable and prudent. We have avoided those high risk sectors that have resulted in significant losses elsewhere. Coventry has not undertaken commercial or second charge lending, and our exposure to unsecured lending is insignificant.

This prudent and responsible approach is in the interest of individual borrowers and the Society as a whole. The results are shown by an arrears performance which remains significantly better than for the industry and has improved in the last 12 months. As at 31 December 2011, only 0.79% of mortgage balances were 2.5% or more in arrears, below the equivalent figure for the combined Coventry and Stroud & Swindon societies in 2010, and below the Coventry figure of 2009.

The corresponding figure for the performance of the enlarged Society judged against the FSA's latest published view of the industry remains 44% of industry average (30 September 2011).

It is a similar position when considering numbers of accounts rather than balances. Just 0.56% of Coventry mortgages were more than six months in arrears, once again very substantially less than the industry average as reported by the Council of Mortgage Lenders (1.12%).

There were just 94 properties in possession at the end of 2011 (2010: 107), from a total population of around 185,000 accounts.

The Society's buy-to-let lending also significantly outperforms the industry average and consistently performs as well as owner occupied mortgages of the same loan to value (LTV). As LTVs for buy-to-let loans are restricted below those we would provide for owner-occupiers, this means that arrears on our buy-to-let lending are lower than for any other class of business.

The quality of the mortgage lending, which is both a measure of the strength of the Society and a demonstration of the values on which it is based, is highlighted by the low level of impairments that are amongst the lowest reported by any of the larger UK mortgage lenders. I expect this to continue with an average LTV advanced in 2011 of just 55.6%. The average LTV, as adjusted for changes in house prices, of the overall mortgage book is just 50%.

The capability to maintain the Society's lending performance relies upon attracting and retaining funds. Coventry has an unrivalled record amongst its peer group of building societies in achieving significant organic savings growth throughout the economic downturn.

In the four years, 2007 to 2010, the Society grew retail savings balances organically by £7.2 billion, and added a further £2.2 billion through the merger with Stroud & Swindon Building Society. In 2011, we again performed extremely strongly and grew savings deposits by a further £1.4 billion.

Another strength of the Society has been our continued access to wholesale funding. We are one of only two building societies that have successfully accessed the senior public unsecured markets during the credit crisis. In 2011 we built on the success of unsecured bond issuances in 2009 and 2010 by launching our first sterling covered bond in April. This long-term bond raised £750 million and was followed in October by our first euro-denominated covered bond for which we issued €650 million.

The pricing on both deals was not only advantageous in comparison with the acquisition of retail funds, but competitive when compared with similar transactions completed by much larger institutions. The high level of demand and the price achieved shows the confidence that investors have in the Society and in particular the strength of our financial position.

Coventry's extremely strong funding position, which is based on the successful acquisition of retail deposits supported by continued access to wholesale investors, brings long-term competitive advantage supporting both future growth and ongoing benefit to members in the form of well-priced savings and mortgages.

A further source of strength stems from our rigorous focus on cost-efficiency. Undoubtedly our continued growth supports this and I am pleased to report that in 2011 we expect to retain our position as the most cost-efficient society in the UK.

In 2011 we completed the full integration of Stroud & Swindon Building Society. It is my belief that completing the integration more quickly than seems usual in this type of merger was the right thing for our members. The integration has brought practical benefits and minimised disruption to services, and also allowed us to return our focus to our core activities. It has been very successful, demonstrating the Society's capability to manage large projects whilst still meeting ambitious growth objectives and reflects great credit on all the staff involved. Improved income and low costs combined to produce an increase in operating profit before impairments and exceptional items to £94.5 million.

The outcome of this year's excellent performance is a further substantial growth in profitability. Discounting the provision we have made for the Financial Services Compensation Scheme to compensate for the mistakes of others, the charitable donation to the Poppy Appeal and the exceptional items recorded in 2010 and 2011 as a result of the merger with Stroud & Swindon, the profits of the Society rose from £75.3 million to £84.6 million, increasing by over 12%.

This is the highest recorded by the Society, exceeding previous records in 2009 and 2010. The benefits are clear as, following provisions for tax, we were able to transfer £46.6 million to the Society's reserves, further increasing our long-term capital strength.

At a time when the capital requirements of financial organisations remain a subject of some debate, it is worthy of note that Coventry also retains the highest reported core tier 1 ratio of any major high street bank or building society at 22.8%.

We must never forget that the foremost responsibility of a building society is to protect the interests of members and, particularly during times of economic turmoil, this means providing financial security.

The strong capital position of the Society, reinforced by our ongoing profitability, is central to this. It underscores the prudence of our lending and our approach to new opportunities. Our responsibility to the membership will always be paramount in investigating, and then pursuing or withdrawing from, potential opportunities, whether it is Stroud & Swindon or Northern Rock.

If our member focused approach drives decision-making across all the activities of the Society, the judgement on these decisions is shown by the ratings afforded by the two credit agencies that review the building society sector closely.

It has been a significant year in this regard. The economic turmoil continued to focus the attention of Fitch Ratings and Moody's Investor Services on the inherent strength of organisations and during 2011 a large number of banks and building societies have been downgraded.

I am pleased to say that Coventry is not one of them. The Society has maintained its 'A' class rating from both agencies ('A' and 'A3'). Indeed, in 2011 we were one of just three major UK banks and building societies not to have a negative action taken by one or both of these agencies, and we are the only building society that can make this claim. This is a significant endorsement of the financial strength of the Society based on our excellent asset quality, our ability to fund mortgage growth and our cost-efficiency. We are now seeing the benefit of a consistent, stable and positive rating which differentiates us from our competitors and may well influence individual savers as well as organisational investors.

Particularly telling was the review conducted by Moody's in 2011, which in October led to the reduction of uplift to institutions' ratings as a result of assumed systemic significance and hence central bank support. This action led to 12 UK banks and building societies being downgraded, with the Society unaffected. If the benefit of potential central bank support is removed from ratings, and the underlying Bank Financial Strength Rating (BFSR) compared, only one UK high street bank has a higher BFSR than Coventry. No building society is higher rated using this measure.

I have talked at length about the strength of the Society's financial performance in 2011, based on the consistent application of a member-focused strategy. This focus drives all aspects of our activities and during 2011 we have continued to invest in developing the service we offer our members.

An important part of this is listening to what members tell us and acting on what they say. In 2011 we completed a rotation of our Members' Council, the voluntary committee of members that meets quarterly to discuss the performance of the Society and gives valuable input to our ongoing developments.

In the three years the Council has been operating, we have had many useful conversations with the 12 inaugural members, who have given their views, good and bad, on all aspects of the Society from our product portfolio to the development of our online and telephone services.

Whilst it is sensible to recruit new members to the Council to broaden the perspective and promote continual challenge, I would like to thank all those who have taken part to date. They have proved the value of this forum and have served the Society and their fellow members extremely well. I look forward to working with the new Council in the coming months.

In addition to maintaining our programme of roadshows, which provide an opportunity for members to meet staff from the counter to the Board, we have expanded our customer research to encompass surveys of branch, telephone, online and intermediary customers.

The results have been invaluable, particularly as we look to enhance the efficiency of the way we serve members whilst meeting their expectations in the service they receive. This has been particularly relevant in the development of our telephone system which was receiving mixed feedback a year ago. As a result we changed our approach to ensure quick and simple access to an advisor, and this has proved a very welcome step forward.

I believe this example demonstrates clearly the ethos of the Society. If we don't get something right first time, our aim is to resolve it quickly, to our members' satisfaction.

The proof of this approach lies in our record on complaints. The number of complaints per customer reported by the Society is amongst the lowest of any large bank or building society.

For those complaints that cannot be resolved to the customer's satisfaction, the Financial Ombudsman Service (FOS), is the final arbiter of disputes and it publishes tables of complaints referred to it. Our aim to treat customers fairly is borne out by the FOS statistics which report the number of complaints referred to it in a six month period. Since FOS first published, in 2009, six monthly tables of total complaints received, Coventry has yet to appear. This is because we simply do not have enough referred complaints to register and we are comfortably the largest high street bank or building society to be able to say this.

Naturally the combination of significant business growth and an approach which puts members' interest at the centre of our decision-making is also recognised in the independent awards the Society won in 2011.

The ones that stand out are those that are based on the experience of customers. I was particularly pleased that the Society was named the 'Best Regional Branch Network' by Your Money, nominated by its readers and judged by an extensive mystery shopping exercise. Our branch network is more than a service channel. It is part of the fabric of our local communities and fulfils an essential role in the lives of thousands of our members every week.

Equally it was very good to be recognised for our mortgage performance by people who know better than most how difficult the market has been. Your Mortgage awarded Coventry its 'Best Building Society' award based on the views of intermediaries and their clients. The Society appreciates very well the role intermediaries play in helping their customers through the complexities of buying and moving home, and we will continue to support them by offering competitive products and service based on fairness and expertise.

Recognising the impact of today's uncertain economic environment on the Society, it is sobering to reflect on the impact on individuals and communities.

We must do all we can to support the work of community groups and charities who make such a difference to people's lives.

In 2011, the Society supported through its maturing programme of community activity, around 260 charities and community groups. Members of staff gave their time, expertise and enthusiasm in raising funds and directly volunteering for a wide variety of organisations ranging from local charities to raising over £40,000 for Children in Need.

We can also use our expertise to support charities directly through the provision of affinity products. I have talked about the success of our partnership with The Royal British Legion before, but with the total funds donated to the Poppy Appeal since 2008 now in excess of £5.6 million, it is clear how important this initiative has become to supporting its vital work.

The need to promote greater understanding of personal finance has never been more relevant. The work we do to encourage greater financial literacy amongst schoolchildren continues to be a priority and the results are proving to be extremely positive.

Helping the next generation to understand and prepare for the difficulties of the current environment provides an interesting challenge as I look forward to the years ahead.

As the UK and international economies adjust to a new reality reflecting a reduction in the availability of affordable credit, organisations and individuals must do the same. The age of austerity may well be a long-lasting phenomenon.

In such an environment, traditional values count. I have said, many times now, that the Society has the right business model to succeed with its emphasis on prudence, responsibility and fairness.

The performance of the Society over the last five years has shown this to be the case and I remain confident that it will be able to maintain this outstanding record in 2012 and beyond.

David Stewart
Chief Executive

THE DIRECTORS AND SECRETARY

BRIDGET BLOW, DEPUTY CHAIRMAN AND SENIOR INDEPENDENT DIRECTOR (62)

Bridget Blow has been a non-executive director since 2007. As an experienced company director, Bridget has a strong information technology background, having been Chief Executive of ITNET plc. She is a past president of the Birmingham Chamber of Commerce and Industry and a non-executive director of Birmingham Hippodrome.

Bridget was a non-executive director of the Bank of England between 2000 and 2005.

She is Chairman of Trustmarque Group and Harvard International plc.

Bridget became the Society's Deputy Chairman in 2009. She is also Senior Independent Director, Chairman of the Society's Remuneration Committee, a member of the Board Audit Committee and the Nominations and Governance Committee.

ROGER BURNELL (61)

Roger Burnell joined the Board as a non-executive director in 2008 and is a Chartered Accountant with over 25 years' senior executive experience. He worked as Finance Director and Managing Director of several businesses within the Thomson Travel Group before becoming Group Chief Operating Officer in 1998.

Since retiring from his executive roles Roger has continued to work at Board level through a number of non-executive directorships, including previously as Chairman of International Life Leisure Group, Chairman of The First Resort and Chairman of HomeForm Group.

Roger is currently Senior Independent Director of Thomas Cook Group plc and a member of the Society's Board Risk Committee and the Remuneration Committee.

GILL DAVIDSON, SECRETARY AND GENERAL COUNSEL (46)

Gill Davidson is a qualified solicitor and joined the Society in 2011 following over 10 years working in financial services. She started her career at Pinsent & Co. in Birmingham in 1987 and has subsequently undertaken a number of different roles, including Secretary to another building society, before joining the Society.

Gill is the principal legal advisor to the Board and is also responsible for compliance oversight of regulatory conduct risk and governance. In addition to her role as a member of the senior executive team she serves as Secretary to the Board and all its Committees and is also Secretary to the Trustees of the Society's pension scheme.

COLIN FRANKLIN (56)

Colin Franklin joined the Society over 30 years ago and has held line management responsibility for a number of areas including the branch network, operations and sales.

Joining the Society's executive team in 2005, Colin was appointed to the Board as Director of Sales and Marketing in 2009, with responsibility for sales operations, distribution, product development and marketing. He is also Managing Director of Godiva Mortgages Limited, the Society's intermediary lending subsidiary.

IAN GEDEN (58)

Ian Geden has been a non-executive director since 2008. He is a member of the Board Audit Committee and the Remuneration Committee.

Most of his 30 years' financial services experience has been in the mutual sector, including NFU Mutual where he was Chief Executive before retiring at the end of 2008. Ian was also Vice Chairman of the Association of British Insurers (ABI) and was Chairman of the Association of Mutual Insurers. Ian is a non-executive director of The Police Mutual.

DAVID HARDING, CHAIRMAN (64)

David Harding joined the Board as a non-executive director in 1996, becoming Deputy Chairman in 1999 and Chairman in 2005. He is also Chairman of the Nominations & Governance Committee and a member of the Remuneration Committee.

Holding an Economics degree from the University of Nottingham and a Masters degree from Nottingham Business School, David is a Fellow of the Chartered Institute of Management Accountants and has experienced a wide career in finance. His career included board positions with several major listed companies including Railtrack plc, Rugby Group Plc and T&N plc. He was Chairman of PD Ports Plc until 2006.

David is Senior Independent Director of Enterprise Inns plc and a non-executive director of the Royal Mint. He is a local magistrate and Deputy Chairman of the Bench.

JOHN LOWE (39)

John Lowe joined Coventry in 2007, initially to manage the Corporate Planning and Product Development functions, before assuming the role of Deputy Finance Director in 2009. He has been a member of the Society's Board since 2010 when he was appointed to the role of Finance Director.

A graduate of Oxford University and a Chartered Accountant, having qualified with Deloitte, John has over 15 years' experience of financial services gained across a broad range of businesses. He is a member of the Board Risk Committee.

IAN PICKERING (56)

Ian Pickering joined the Society's Board as a non-executive director in 2005. He is a qualified Chartered Accountant.

Ian has worked in senior positions in the engineering industry for much of the last 25 years and was formerly a Chief Executive of Manganese Bronze Holdings plc. Prior to this he was a director of the Dennis Group plc.

Ian is a non-executive director of Latchways plc and Bedford Hospital NHS Trust, whose Audit Committee he chairs, and is a member of the Council of Cranfield University. He is a member of the Auditing Practices Board of the Financial Reporting Council.

Ian is Chairman of the Society's Board Risk Committee and Chairman of the Models & Ratings Committee. He is also a member of the Board Audit Committee.

FIONA SMITH (53)

Fiona Smith joined the Board as a non-executive director in 2002. Fiona is a Solicitor and was General Counsel and Company Secretary of Severn Trent plc from 2006 until 2011. Prior to this she was General Counsel and Company Secretary at National Grid plc, where she worked for 15 years, and then at Transport for London.

Fiona is a member of the Board Risk Committee and the Remuneration Committee.

GLYN SMITH (59)

Glyn Smith joined the Board in 2010, following the merger with Stroud & Swindon Building Society, where he was also a non-executive director. He has over 30 years' experience in the financial services sector, most notably as a senior executive at Barclays Bank PLC and as Finance Director of Portman Building Society.

Glyn is a graduate of the University of Cambridge, a Chartered Accountant and member of the examinations team for the Institute of Chartered Accountants in England and Wales.

Since 2003 he has worked at board level through a number of non-executive directorships, including Domestic & General Group PLC, Covent Garden Market Authority and two Primary Care Trusts.

Glyn is Chairman of the Board Audit Committee and a member of the Board Risk Committee.

DAVID STEWART, CHIEF EXECUTIVE (46)

David Stewart is a graduate of Warwick University and qualified as a Chartered Accountant with KPMG. In 2002 he joined the Board as Finance Director, before assuming Board responsibility for the Sales and Marketing functions in 2004. He was appointed Chief Executive in 2006.

Prior to joining the Society, David gained financial services experience at DBS Management plc where he was Group Finance Director and then Group Chief Executive.

David is Deputy Chairman of the Building Societies Association and is a member of both the Chairman's and Executive Committees of the Council of Mortgage Lenders.

He is a member of the Board Risk Committee and the Nominations and Governance Committee.

DIRECTORS' REPORT

BUSINESS OBJECTIVES AND ACTIVITIES

The Society's principal objective is the provision of a range of personal financial services including mortgage finance for house purchase and improvements, savings, investment products and insurance.

The directors consider that all activities carried out during the year were within the powers set out in the Memorandum of the Society.

BUSINESS REVIEW

The Society recorded an excellent performance in 2011, maintaining a record of achievement over a period of sustained economic challenge.

The Society's ability to enhance its strong funding position, to lend responsibly, to retain its sector-leading cost-efficiency and to remain strongly profitable in each of the five preceding years of credit crisis, recession and uncertainty constitutes one of the strongest performances reported by a UK bank or building society. The Society is the only top ten UK building society to record organic mortgage and savings growth each year.

Coventry Building Society has provided a safe and secure home for its growing membership. The confidence that individual savers and borrowers have in the Society is reflected by credit rating agencies and the support of institutional investors. The Society has been 'A' rated throughout the economic downturn (Fitch 'A', Moody's 'A3'), and Moody's 2011 review rated its Bank Financial Strength Rating second only to one UK high street bank with no other building society being more highly rated.

The Society's business performance is reviewed by the Chairman (pages 2 and 3) and the Chief Executive (pages 5 to 9).

External environment

The brief period of economic recovery witnessed during 2010 was reversed in 2011 by the developing sovereign debt crisis in western economies.

In the eurozone, a number of interventions were made during 2011, intended to stabilise the economies of Portugal, Greece, Italy and Spain.

By the end of 2011 these interventions had failed to restore market confidence. Concerns about the prospect of defaults and the impact on the stability of the financial system continued to restrict activity in the wholesale markets, whilst the outlook for economic growth domestically and in Europe worsened during the year. As a result the UK Government has been required to extend the timescale to balance the national budget whilst further quantitative easing has been initiated by the Monetary Policy Committee. UK unemployment rose during 2011 and is forecast to do so in 2012 and, not unexpectedly, public confidence declined through the year.

The Bank of England Base Rate, which had widely been forecast to rise during 2011, was maintained at 0.50%, and expectations are now for this to continue throughout 2012 and into 2013.

The housing market remained subdued. Activity was half that witnessed prior to the onset of the initial credit crisis in 2007. Property valuations have been protected by an ongoing shortfall of supply as the UK population continues to grow and demographic changes lead to more single person households. The low base rate has also helped to support mortgage affordability. Although more mortgages were offered in the market at higher loan to values during 2011, lending remains restricted, particularly to first-time buyers.

Overall, economic prospects for 2012 remain uncertain.

Impact on Coventry Building Society

Whilst economic conditions weakened significantly during 2011, the Society once again recorded an extremely strong performance, showing the benefits of both a straightforward and consistent business strategy and the excellence in execution which has set it apart in recent years.

The traditional business model of a mutual building society requires it to attract and retain savings balances to fund responsible lending, adding to capital reserves in the form of sustainable levels of profitability.

The Society has once again achieved each of these objectives. The core strength which underpins these achievements is the capability to maintain a balance of savings and lending without recourse to higher levels of risk, in turn supported by sector leading cost-efficiency.

The Society's continued success in an increasingly competitive retail savings market requires financial strength and operational expertise. Security of funding has been enhanced by continued access to wholesale investors and has ensured that the Society has been able to maintain profitable and prudent lending.

The benefits of this responsible approach are evidenced in the form of low levels of arrears and impairments which have protected profitability and the transfer of retained profit to regulatory capital reserves.

As well as financial security and the provision of fair long-term value in savings and mortgages, we also have an overriding duty to our members to provide products that meet their needs.

During the first half of 2011, the court case concerning the sale of Payment Protection Insurance was completed, and as a result, a number of lenders have identified millions, in some cases, billions of pounds in additional provisions to cover the mis-selling of these products. Coventry was not required to make any provision as a result of this ruling. The Board believes this example demonstrates how decisions have been taken in the interests of individual members, in the form of product design and sales processes, that are in the interests of the Society as a whole.

The current economic climate presents challenges for all members and the Society aims to provide long-term value across our portfolio for the benefit of savers and borrowers alike. Around 95% of the variable rate savings products that were in existence at the time the Bank of England Base Rate began its fall from 5.00% in October 2008 to 0.50% in March 2009, have seen interest rates improve relative to the Bank Base Rate, and the rate paid on 94% of saving balances is in excess of Base Rate. This has helped to protect hundreds of thousands of Coventry savers from the full impact of the unprecedented low interest rates. For example, the average interest rate paid on cash ISAs, is over 2%, compared to a market average of 0.61%.

We have done this whilst maintaining the lowest standard variable rate of any of our peer group[1] of larger building societies. The Society's ability to report strong profits and compete for new business whilst providing long-term value for existing members underlines the strength of our business model and our commitment to operate in line with our values.

This member-focused approach is also reflected by a responsible investment strategy. The eurozone crisis has highlighted the degree of connectivity and hence risk of contagion within the financial services sector. Coventry Building Society has just £3.4 million invested in Irish banks as at 29 February 2012, and no exposure to the following eurozone countries: Portugal, Italy, Greece and Spain.

The Society retained 'A' ratings from both Moody's (A3) and Fitch (A) credit rating agencies, and notably was not included in the Moody's statement in the second half of 2011 which resulted in the downgrading of 12 UK banks and building societies.

This performance was achieved during a year of considerable internal change. Although the merger with Stroud & Swindon Building Society was legally completed on 1 September 2010, much of the benefit to the wider membership has been achieved through the integration of the two societies following this date. This work was completed at the end of September 2011 to a timescale and level of integration that was more challenging than in most similar mergers in the building society sector.

It is worth repeating that the Society has prospered during a period of extreme economic uncertainty and challenge. With these conditions set to continue for the foreseeable future, the Board believes it retains the right business model, strategy and expertise to remain financially strong and protect the interests of current and future members.

In addition to the economic uncertainties, 2011 was also marked by developments in the regulatory environment. The Society believes that regulation should reflect the circumstances of individuals and organisations alike, and a 'one size fits all' approach may weaken a faltering housing market. It is encouraging that the FSA is conducting significant consultation into the impact of proposed changes, particularly in regard to the mortgage market and, most importantly, has demonstrated a willingness to listen and develop plans accordingly.

FUTURE DEVELOPMENTS

Looking ahead to 2012 it is clear that the economic environment will remain uncertain and fast-moving. Whatever the developments, in the UK or internationally, it can be expected that the challenges of low economic growth and low interest rates will dictate what happens in the housing market for the immediate future.

The key for all mortgage lenders will be security of funding and the cost of this funding, which will be determined by restricted credit markets and a crowded retail savings market, will continue to present challenges.

Coventry Building Society remains well placed to succeed. The ability to compete effectively in retail markets has been proven from the earliest point in the credit crisis, and has been a consistent source of the Society's strength in the ensuing five years of economic turmoil. In addition, the Society's past performance and strong ratings position gives confidence that it will continue to attract institutional investors, securing additional funding strength.

The Society's control of costs and margin has ensured a sustainable level of profitability, which continues to enhance exceptionally strong capital ratios (22.8%), that is supported by the excellent asset quality of its mortgage book and low levels of impairments.

Coventry Building Society has core strength in the fundamentals of operating a successful savings and mortgage model. More importantly it has a track record of decision-making that puts member's interests first. This combination of strong foundations and a prudent member-focused strategy has been shown to be extremely successful. The Board continues to believe that the Society is well positioned to report further progress in 2012 and beyond.

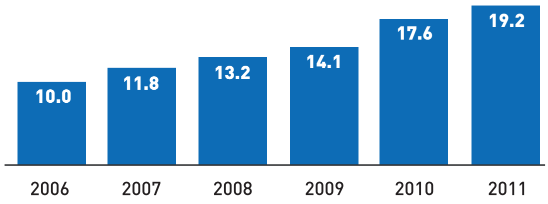
[1] Peer group of larger building societies defined as building societies with reported assets of between £5 billion and £50 billion.

DIRECTORS' REPORT
(continued)

KEY PERFORMANCE INDICATORS

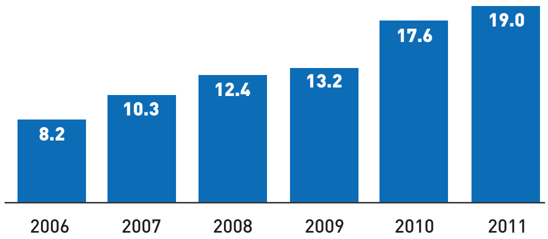
TOTAL LOANS (£bn)

- Mortgage market share has increased by two thirds over the last five years.
- This represents the largest reported organic growth in market share of any top ten building society.
- Mortgage assets continue to be of very high quality with an average indexed loan to value ratio of the overall mortgage book of just 50%.



TOTAL RETAIL SAVINGS (£bn)

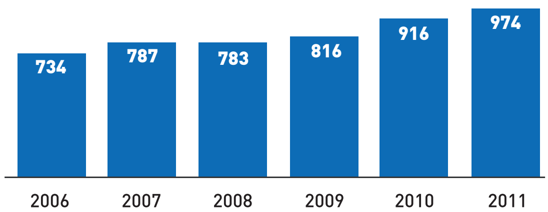
- Savings balances have grown by £10.8 billion.
- This represents the largest reported organic growth in market share of any top ten building society.



TOTAL CAPITAL (£m)*

- Consistent financial performance has resulted in an increase in capital resources of £240 million between 1 January 2007 and 31 December 2011.
- Coventry has the highest reported core tier 1 ratio of any UK building society or top ten mortgage lender (22.8%).

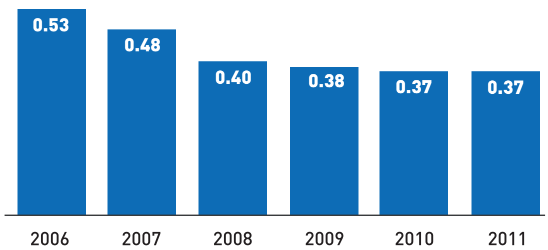
* Total capital is comprised of equity, subscribed capital and subordinated liabilities.



COST TO MEAN ASSET RATIO (%)*

- Cost to mean asset ratio is just 0.37%, maintaining the Society's class leading efficiency.
- 0.37% represents the lowest ratio ever reported by a UK building society.

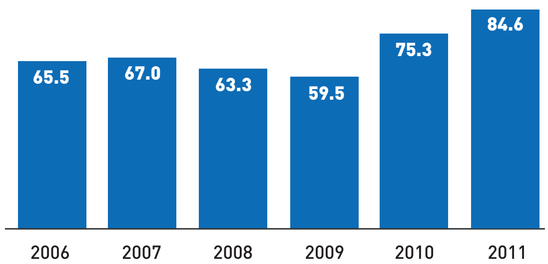
* Administrative expenses, depreciation and amortisation/Average total assets.



OPERATING PROFIT BEFORE EXCEPTIONAL ITEMS (£m)

- Underlying profits* of the Society have increased to a record £84.6 million.
- Coventry is the only top ten building society to report growth in assets and a profit in each of the last five years.

* Operating profit after impairments and before exceptional items.



GROUP ACCOUNTS

The Accounts show the consolidated Group results of the Society and its subsidiaries, and the Society as a single entity.

PROFIT AND CAPITAL

Discounting the exceptional items recorded in 2010 and 2011 as a result of the merger with Stroud & Swindon, the contribution made to the Financial Services Compensation Scheme to meet the costs of the mistakes of others, and the charitable donation to the Poppy Appeal, the underlying profits of the Society rose from £75.3 million to £84.6 million. As a result, the Group's profit after tax amounted to £46.6 million (2010: £84.9 million), which was added to reserves.

The Group holds capital to protect its depositors, to cover inherent risks, to support the development of the business and to provide a cushion for unexpected losses. In assessing the adequacy of its capital, the Group considers its risk appetite and the material risks to which it is exposed. Capital adequacy and capital resources are monitored on the basis of the framework developed by the Basel Committee on Banking Supervision and subsequently implemented in the UK by the UK regulator, the Financial Services Authority (FSA).

Prior to 1 January 2008, the Group followed the requirements of the Capital Accord (Basel I). Since 1 January 2008 the Group has complied with the EU Capital Requirements Directive (Basel II). From this date the FSA granted the Group permission to use the Basel II Internal Ratings Based (IRB) approach to retail credit risk and capital management. This allows the Group to set capital levels using internally developed models that reflect the credit quality of the Group's mortgage book rather than through standardised percentages set by the FSA. This permission reflects the Group's detailed understanding of its customer base and control of its credit risk profile. In 2010, Coventry Building Society merged with the Stroud & Swindon Building Society, which used the standardised approach to retail credit risk management. The Group intends to adopt the IRB approach for these mortgages in due course.

The table overleaf summarises the composition of regulatory capital for the Group as at 31 December 2011 and 31 December 2010. At 31 December 2011, and throughout the year, the Group complied in full with the capital requirements that were in force. Further information on how the Group manages capital can be found on page 25. The Group calculates its capital requirement under Basel II using the IRB approach for prime residential and buy-to-let mortgage exposures (excluding those transferred from the Stroud & Swindon merger), and the standardised approach in calculating the capital requirements for other risk areas.

DIRECTORS' REPORT
(continued)

Capital structure

	Notes	2011 £m	2010 £m
Tier 1			
General reserve		**747.9**	704.5
Pension fund surplus adjustment	1	**(3.9)**	(7.2)
Intangible assets	2	**(9.5)**	(12.2)
Deductions from tier 1 capital	3	**(9.2)**	(15.3)
Core tier 1 capital		**725.3**	669.8
Permanent interest bearing shares	4	**160.0**	160.0
Total tier 1 capital		**885.3**	829.8
Tier 2			
Collective provisions for impairment	5	**0.4**	0.8
Subordinated debt	6	**67.0**	67.0
Deductions from tier 2 capital	3	**(9.2)**	(15.3)
Total tier 2 capital		**58.2**	52.5
Total capital		**943.5**	882.3
IRB approach			
Credit risk – Retail exposures		**1,920.7**	1,522.6
Standardised approach			
Credit risk – Retail exposures		**776.7**	896.3
Credit risk – Liquidity book		**199.0**	340.0
Credit risk – Other		**83.9**	50.0
Operational risk		**202.4**	235.0
Risk-weighted assets		**3,182.7**	3,043.9
Core tier 1 ratio (%)		**22.8**	22.0

1. Pension fund surplus - note 12 (page 57)
2. Intangible assets - note 23 (page 66)
3. Under Basel II a deduction is made for the excess of expected losses on loans and advances to customers, calculated on an IRB basis, over accounting provisions, and are allocated 50% to Tier 1 and 50% to Tier 2 capital.
4. Permanent interest bearing shares - principal amount outstanding only, note 37 (page 75)
5. Under Basel II collective provisions for impairment relating to loans and advances to customers, calculated on a standardised basis, are included as Tier 2 capital.
6. Subordinated debt - principal amount outstanding only, note 36 (page 75).

Core tier 1 ratio

The Society retains a strong capital position with a core tier 1 ratio of 22.8% (2010: 22.0%).

Impact of Basel III

The European Commission published its proposal for implementing the provisions of Basel III in July 2011. This proposal (in the form of a draft regulation and directive) is currently under negotiation within the EU. Basel III introduces stricter definitions of what constitutes capital. Current instruments which do not meet the stricter definitions, principally the Society's Permanent Interest Bearing Shares, will be gradually derecognised for capital purposes over a ten year period starting in 2013.

Basel III had no effect in 2011, and the Society has considered the impact of the introduction of these rules on future levels of capitalisation, including under stress testing. The directors consider that the Society will continue to remain well capitalised and there is no foreseeable requirement to issue additional capital instruments. Nevertheless, the Society is monitoring market developments and may consider issuing Basel III compliant capital instruments should the market present favourable opportunities to do so.

ASSETS

Advances during the year amounted to £4.0 billion, contributing to total loan balances of £19.2 billion.

The assets of the Group increased by £2.2 billion to £24.5 billion at 31 December 2011, representing growth of 9.8%. Changes in intangible assets and property, plant and equipment are detailed in notes 23 and 24 to the Accounts.

At 31 December 2011, there were 268 mortgage accounts 12 months or more in arrears (2010: 336). The balances on these accounts totalled £31.0 million (2010: £38.7 million) and the value of these arrears was £5.0 million (2010: £8.3 million).

CREDITOR PAYMENT POLICY

The Society's policy is to agree the terms of payment at the start of trading with the supplier and to pay in accordance with its contractual and other legal obligations.

CHARITABLE AND POLITICAL DONATIONS

The Society provided for donations of £1.1 million (2010: £1.8 million) to charitable organisations during the year. This included a provision for £1.0 million (2010: £1.7 million) to The Royal British Legion's Poppy Appeal and £50,000 (2010: £50,000) to the Coventry Building Society Charitable Foundation.

The amount donated to The Royal British Legion illustrates the strength of the ongoing relationship with the Legion for which the Society has developed a portfolio of products. By 31 December 2011, the total support given to the Poppy Appeal since the launch of the first Poppy Bond in October 2008 had reached £5.6 million. The number of members holding accounts which support the Legion now totals close to 130,000.

No contributions were made for political purposes. However, as a result of the Political Parties, Elections and Referendums Act 2000, time allowed for employees to carry out civic duties and political activity can amount to a donation. The Society supports a very small number of employees in this way.

CORPORATE RESPONSIBILITY, ENVIRONMENTAL AND EMPLOYEE FACTORS

Staff

The directors welcome the opportunity to recognise the commitment and professionalism of all staff in enabling the Society to record another outstanding performance in 2011.

As the economic challenges develop from year to year, it is understandable that the focus should be on the overall financial and business performance of the Society in very difficult circumstances.

However, at such times the reputation of an organisation is paramount, and it is the day-to-day ability of the Society to maintain the confidence of its members whilst competing in restricted markets that stands behind the financial performance.

The ability of the Society to succeed in an increasingly competitive savings market has already been noted, as has the importance of security of funding. This requires flexibility and speed of action to be built into the everyday operation of customer-facing and processing operations and places significant demands on the members of staff that work in these areas.

Their experience and skill is vital in managing a flow of work that can change considerably as the Society identifies and pursues market opportunities, whilst maintaining the quality of service that our members value and expect.

It is also the case that the financial services industry has changed rapidly and will continue to do so through regulatory developments, the application of new technologies and ongoing innovation. The Society's ability to protect the interests of members whilst continuing to grow, requires the development and application of new skills whilst retaining the values that have held it in such good stead over the years.

This responsibility is shared by everyone at the Society. The importance attached to 'Putting Members First', the Society's guiding principle, is manifest in all aspects of the organisation from the recruitment of new members of staff and their initial induction, to training and development and the day-to-day management of activities.

In early 2012, the Society was awarded Gold status by Investors in People in its triennial review. This respected independent award places the Society in the top 3.0% of accredited organisations in the UK. This follows a specific review undertaken in 2011 in which Investors in People assessed the Society's merger with Stroud & Swindon Building Society and reported that it was a "model of its kind".

It is clearly understood that the Society's success, which requires a shared understanding of the values of the organisation, requires the commitment of every member of staff. The directors are confident that the performance of the Society over many years demonstrates this in action and would like to take this opportunity to thank all staff for their contribution in 2011.

The Society will continue to invest to provide the right environment and opportunities for members of staff to achieve their potential and meet the expectations of the Society's membership.

DIRECTORS' REPORT
(continued)

Community
The difficult economic conditions have created additional hardship for many individuals and communities. It is likely that this will be exacerbated as public spending and private investment continues to be withdrawn.

The Society has, over a number of years, developed an established programme of support that reflects the core competences of the organisation and the needs of local communities.

Of particular note has been the ongoing work to enhance financial literacy, which now spans a range of initiatives from supporting numeracy and literacy in primary schools, to working with specialist finance academies and tackling personal debt issues amongst adults through partnerships with Citizens Advice Bureaus in Coventry and Stroud. These initiatives are well regarded by the organisations involved, in particular the consistency of the Society's support over a sustained period.

The directors believe that the Society's links between its core business activities and supporting vulnerable people demonstrates the best of corporate responsibility in action. An example during 2011 was a pilot undertaken with Coventry Citizens Advice Bureau and Coventry Law Centre which extended the Society's experience in supporting individuals in arrears to a broader audience.

The Society is nearing the end of its three year programme of support for Age UK. During this time almost £150,000 has been raised, but of equal importance has been the opportunity to increase awareness amongst staff and members of the work undertaken by Age UK, and the issues faced by the UK's elderly. It is unfortunately the case that vulnerable people are disproportionately affected at times of economic hardship, including being targeted by criminal activity. There have been a number of examples where members of staff have identified and protected elderly members from abuse, an understanding that has been reinforced by the partnership with Age UK.

From this point, the Society will build on the established relationship with The Royal British Legion, supporting it not only through the established portfolio of Poppy products which by the end of 2011 had resulted in over £5.6 million being donated to the Poppy Appeal, but also as our corporate charity. The directors understand the value and relevance of the work undertaken by The Royal British Legion and also appreciate the many expressions of support received from members since this relationship began in 2008.

The final element of the Society's programme is devoted to supporting local communities, often through the personal commitment of members of staff, but also through the activities of the Coventry Building Society Charitable Foundation, now in its 13th year of operation. It is noticeable that the number of requests for help have risen in recent years, with nearly 50 small local organisations receiving grants from the Foundation in 2011. These now include organisations in the geographic area previously served by Stroud & Swindon Building Society, and the grant available to the Foundation will be increased in 2012 to accommodate the greater area of operation and the rise in demand for help.

The enthusiasm and commitment of members of staff to the community programme continues to be the critical element in determining success. Whether helping achieve a record-breaking fundraising contribution to Children in Need, committing to long-term reading support for a schoolchild, or volunteering to help run a local community group, as in previous years, many staff have chosen to become involved at some point during 2011.

Supporting the communities we serve is one of the values of the Society and it will continue to be an intrinsic part of the service provided.

Environment
The Society remains committed to reducing the environmental impact of its activities, in particular seeking to limit the amount of paper used and to ensure recycling opportunities are maximised, whilst also aiming to source energy responsibly and to reduce usage where possible.

The directors understand the close link between these aims and the objective of the business to maintain an efficient and cost-effective organisation.

During 2011 the Society's continued growth required opening an additional office building in Coventry. The opportunity was taken to refurbish the building and update key heating, air-conditioning, insulation and lighting systems and controls in accordance with environmental best practice with the aim of minimising ongoing energy consumption. The energy performance of the building has been significantly improved with lighting being 36% more efficient, whilst the heating (215%) and cooling (40%) systems are exceptionally energy efficient.

The improvements offered by all of these systems results in substantially reduced annual carbon dioxide emissions, providing sustainable environmental improvements whilst allowing greater flexibility and control in managing internal working conditions.

The Society has completed its programme to install smart meters in branches, complementing similar systems in place in all head office buildings, and is starting to realise the benefits of this proactive energy management. In addition the Society maintains a proactive approach to energy procurement which has enabled renewable energy to be sourced cost-effectively for use at head office sites.

Although it has been identified in previous reports, it is worth confirming that all paper used within Coventry Building Society is recycled via a secure facility, which results in both an environmental and a security benefit. In addition, over 95% of all literature produced by the Society uses recycled paper.

Awards

The directors are pleased to report that the Society's outstanding performance in 2011 was once again reinforced by a number of independently assessed awards.

The financial services industry has witnessed a proliferation of awards intended to enhance consumer knowledge and decision-making. The Society wins many such awards and it is worth highlighting those that are based on genuine customer perspectives.

One that is particularly pleasing, because it also measures the Society's success in managing the integration of Stroud & Swindon Building Society, is the award by Your Money of 'Best Regional Branch Network'. Coventry Building Society recognises that the role of branches often extends beyond a simple transactional sales and service relationship and, as a result, has invested significantly in developing the capability of branch staff and the environment in which they serve members. The award of 'Best Regional Branch Network' reflects this investment and is particularly noteworthy because nominations resulted from the experience of customers, and assessment included independent mystery shopping.

'Your Mortgage' magazine awarded Coventry Building Society the title of 'Best Building Society' for 2011. The award was made on the basis of information provided by mortgage intermediaries and their clients with the citation acknowledging the "long term, good value of its mortgages and savings... coupled with its superlative service".

Similar recognition was provided by MoneyNet who judged the Society as the 'Overall Best Savings Provider' in 2011, a position that has already been retained for 2012 along with an additional award for 'Best Overall Current Account'.

Although not technically an award, the themes of trust and service are also reflected in the ongoing performance of the Society in its handling of member issues. As was mentioned last year, in 2009 the Financial Ombudsman Service (FOS) began publishing details of the complaints that had been referred to it, having failed to be resolved by the organisation concerned. Having had significantly fewer than the minimum 30 complaints required for inclusion in the FOS tables in each of the reporting periods, the Society is comfortably the largest high street bank or building society not to have appeared in this publication.

GOING CONCERN

In preparing the financial statements the directors must satisfy themselves that it is reasonable for them to conclude it is appropriate to adopt the going concern basis.

The Society meets its day-to-day liquidity requirements, through managing both its retail and wholesale funding sources and is required to maintain sufficient liquid assets to comply with regulatory requirements, in order to continue to be authorised to carry on its business.

The Society's business activities, together with the factors likely to affect its future development, performance, position, liquidity and capital structure are set out in the Chairman's Statement, Chief Executive's Review and this Directors' Report. In addition, the Risk Management Report and note 40 to the Accounts includes further information on the Society's objectives, policies and processes for managing its exposure to liquidity, credit, market, operational and business risk, along with details of its financial instruments and hedging activities.

The directors believe that the Society is well placed to manage its business risks, despite the current uncertain economic outlook. After considering factors including default rates on loans, house price movements and the Society's capital and liquidity position including the use of stress testing, the directors are confident that the Society has adequate resources for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report & Accounts.

PRINCIPAL RISKS AND UNCERTANTIES

The principal risks and uncertainties faced by the Society are set out in the Risk Management Report on pages 20 to 25.

CORPORATE GOVERNANCE

The Directors' Report on Corporate Governance can be found on pages 26 to 31.

DIRECTORS' STATEMENT PURSUANT TO THE DISCLOSURE AND TRANSPARENCY RULES

The directors confirm that, to the best of each person's knowledge and belief:

- The financial statements, prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group and Society; and
- The management report contained in this Directors' Report and the Risk Management Report includes a fair review of the development and performance of the business and the position of the Group and Society, together with a description of the principal risks and uncertainties that they face.

AUDITORS

Following a review by the Board Audit Committee, the Board has agreed that a resolution proposing the re-appointment of Ernst & Young LLP as auditors of the Society will be submitted at the Society's 2012 AGM.

On behalf of the Board

David Harding
Chairman
29 February 2012

RISK MANAGEMENT REPORT

OVERVIEW

The Society is a mutual organisation run for the long-term benefit of its members. This objective is known throughout the Society as 'Members First'. In keeping with this mutual status, the Board adopts a prudent approach to managing risk geared towards long-term value creation for the benefit of members. This low risk appetite is monitored and enforced through the Society's risk management structure described below.

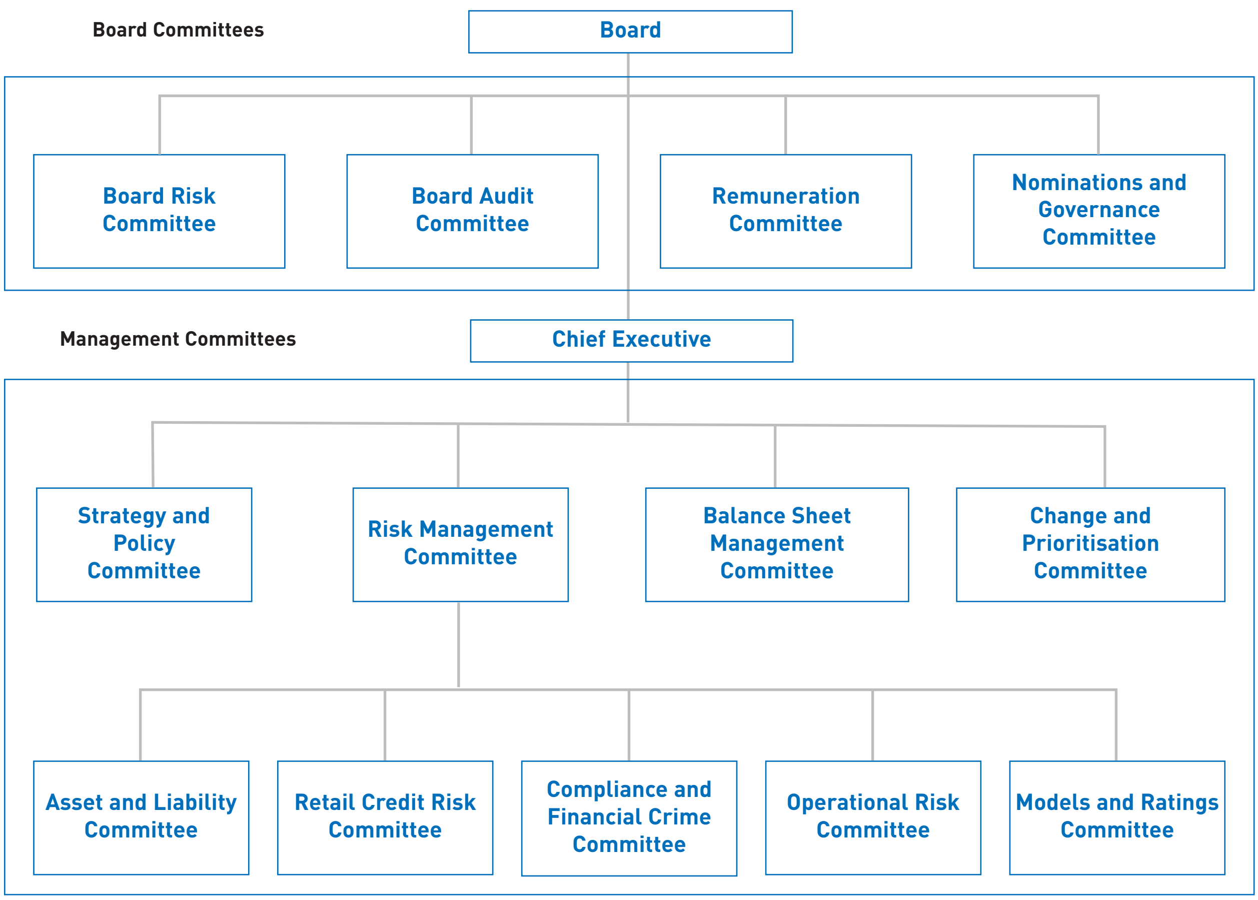
Risk management structure

The Society's risk management structure is based on a three lines of defence model:

- First line of defence – risk management is primarily the responsibility of all managers and staff of the Society. Management have a responsibility to understand how risk impacts their area of the business and for putting in place controls or mitigating activities.
- Second line of defence – policies and oversight are required to challenge managers and staff effectively in their performance of risk management activities and to provide risk management expertise. This is provided through risk support functions and risk committees. The Chief Risk Officer reports to the Chief Executive and has an independent reporting line directly to the Chairman of the Board Risk Committee.
- Third line of defence – the Society's internal audit function is responsible for independently reviewing the effectiveness of the Society's risk management structure and adherence to processes. The Head of Internal Audit reports to the Chief Executive and has an independent reporting line directly to the Chairman of the Board Audit Committee. The Board Audit Committee approves the work programme of internal audit and receives reports of the results on the work performed.

During 2011 changes were introduced to the Society's management committees to enhance oversight of the Society's performance and risk management.

The structure and responsibility of management and Board Committees are set out below:



GOVERNANCE AND OVERSIGHT

BOARD COMMITTEES

Details of the Board Committees can be found in the Directors' Report on Corporate Governance on pages 26 to 31.

SENIOR MANAGEMENT COMMITTEES

Strategy and Policy Committee

Chaired by the Chief Executive and comprised of the executive directors and senior management. This is the senior executive decision making body representing the key business areas within the Society and oversees the strategic development, operational and business performance of the Society.

Risk Management Committee (RMC)

Chaired by the Chief Risk Officer and comprised of the executive directors and senior management. This Committee ensures that risk is being identified and managed efficiently across the Society and that the Society's Risk Management Framework remains effective. It keeps under review the Board's risk appetite statement, Internal Capital and Liquidity Adequacy Assessments, and recommends changes to the Board, through the Board Risk Committee. The minutes of the Committee are presented to the Board Risk Committee.

The Society also has a number of sub-committees that report to the RMC. The details of these Committees are as follows:

- **Asset and Liability Committee (ALCO)**
  Chaired by the Finance Director and comprised of the executive directors and senior management. The Committee oversees the asset and liability risks faced by the Society, specifically market risk, wholesale credit risk and liquidity risk. Further it recommends to the Board, through RMC and the Board Risk Committee, key treasury policy changes and risk frameworks for approval. The minutes of the Committee are presented to the Board Risk Committee.

- **Retail Credit Risk Committee**
  Chaired by the Chief Risk Officer and comprised of the executive directors and senior management. This Committee monitors the management of retail credit risk across the Society and its subsidiaries and the performance of the mortgage books to ensure compliance with limits approved by the Board. Further it recommends to the Board, through RMC and the Board Risk Committee, key lending policy changes and frameworks such as the retail credit risk appetite statement.

- **Compliance and Financial Crime Committee**
  Chaired by the Chief Risk Officer and comprised of senior management. This Committee oversees regulatory conduct risk, compliance and financial crime policy and risk.

- **Operational Risk Committee**
  Chaired by the Head of Marketing and comprised of senior management. This Committee monitors operational risk, business continuity, safety and security in the Society. Further it recommends to the Board, through RMC and the Board Risk Committee, the operational risk appetite statement.

- **Models and Ratings Committee**
  Chaired by a non-executive director (Ian Pickering) and comprised of executive directors and senior management. This Committee monitors the performance of the Society's Basel II credit risk rating system.

Balance Sheet Management Committee

Chaired by the Finance Director and comprised of the executive directors and senior management. This Committee oversees the balance sheet strategy of the Society, including product management, pricing and margin management of the retail savings and lending portfolios.

Change and Prioritisation Committee

Chaired by the Chief Executive and comprised of the executive directors and senior management. This Committee is responsible for prioritisation and approval of all projects, including project expenditure, in line with the Society's corporate plan.

PRINCIPAL RISKS AND UNCERTAINTIES

The Society seeks to understand and manage the various risks that arise from its operations and classifies the principal risks it faces according to five broad categories. These are credit risk, market risk, liquidity risk, operational risk (including compliance and financial crime) and business risk. The procedures put in place to manage these risks are described below:

Credit risk

Credit risk is the risk that customers or counterparties will not meet their financial obligations to the Society as they fall due.

Retail credit risk

For a building society, this risk is most likely to present itself in the potential inability of borrowers to repay their mortgage. The Society's exposure to this risk is managed by a specialist department that reports to the Chief Risk Officer, and in turn to the Retail Credit Risk Committee.

Retail credit risk is managed through a combination of an automated decision system and statistical modelling (including the use of credit scoring) that seeks to identify those customers who pose a greater risk of not repaying their mortgage, and the Society's underwriting process which seeks to ensure that customers only assume a debt that they can afford to repay, thereby safeguarding both themselves and the Society. Retail credit risk is further mitigated by the application of loan to value (LTV) policy rules which form a key element of mortgage product design. This ensures the Society has a prudent margin to repay any given mortgage, even in the event of a fall in property values.

Lending policy is monitored by the Retail Credit Risk Committee, which meets monthly. The Committee is a sub-committee of the RMC and is tasked with ensuring that the quality of new business and overall exposures are within the prudent limits set by the Board, and that the performance of the book is being monitored and trends identified. In this respect, regular stress testing is undertaken that seeks to establish the extent to which losses may emerge in a variety of scenarios, including severe stresses. Should a borrower find themselves in financial difficulty, the Society has established procedures to ensure that it responds fairly, appropriately and sympathetically. Typically, this involves working with the borrower to clear arrears or making other arrangements commensurate with the borrower's circumstances. This can include overpayments to clear arrears or providing a temporary concessionary arrangement to that borrower (defined as 'forbearance'). Each case is reviewed on its own merits by a specialist department, and we always attempt to work with the borrower in difficulty to resolve matters to our mutual satisfaction taking into account an individual borrower's financial situation (see note 40 to the Accounts).

The Retail Credit Risk Committee closely monitors the use of forbearance measures and strict policies exist for circumstances in which the Society will, for example, capitalise arrears. Other measures such as temporary transfers to interest only payments are regularly reviewed and the Society has seen a reduction in this particular measure over the last 12 months.

Should the borrower's situation deteriorate significantly, the Society may take possession of the underlying property. Regular reviews of the Society's arrears management function is undertaken to ensure that borrowers are being treated fairly and in line with established policies and procedures.

The Society has recently developed a quantitative and qualitative retail credit risk appetite statement and has also enhanced its stress testing framework. Regular stress testing is undertaken to ensure the Society continues to remain within its retail credit risk appetite.

Wholesale credit risk

Credit risk within the treasury function (wholesale credit risk) arises from the portfolio of liquid assets held, and represents the risk that counterparties will fail to repay amounts when due. The Society has a low appetite for this form of risk. As such, exposures are restricted to good quality counterparties with a low risk of failure, and limits and exposures are set accordingly. Treasury exposures and limits are focused in the main on UK institutions, with additional limits extended to a small number of highly rated banks in Europe and other developed economies. Limits are set in line with a Board approved wholesale credit policy, which sets maximum limits taking into account internal analysis, external credit ratings, country of domicile and any other relevant factors. All credit limits require Board approval, and are subject to an initial assessment of the creditworthiness of the counterparty, with the approved limit then subject to at least an annual review. Exposure is reviewed on a daily basis to ensure that it remains within the approved limits. Ongoing developments for Treasury counterparties are closely monitored by a specialist credit team, and are reported to, and reviewed by, a dedicated Treasury Credit Committee. This Committee meets weekly and is chaired by the Chief Risk Officer. The Committee is empowered to take immediate action to reduce limits where this is warranted by developments. The Committee reports through ALCO to the RMC and Board Risk Committee.

Details of the Society's exposure to credit risk are contained in note 40 to the Accounts.

Market risk

Market risk is the risk that the value of income derived from the Society's assets and liabilities may change adversely as a result of changes in interest rates, foreign exchange rates or house prices. The Society's policy is to manage these risks prudently, which is ensured through the setting of limits by the Board. The Society ensures compliance with these limits through a combination of matching assets and liabilities with off-setting interest rate or currency characteristics, and by the use of derivative financial instruments such as interest rate swaps and caps, foreign exchange swaps and foreign exchange forward purchase contracts. Control of market risk exposure is overseen by

ALCO, which makes reports to the RMC and the Board Risk Committee. The most significant elements of market risk for the Society are interest rate risk, foreign currency risk and house price risk, each of which are described below.

The Society is further strengthening its second line of defence for oversight and independent assessment of the various market risks by the establishment of a Balance Sheet Risk Management team reporting to the Chief Risk Officer.

Interest rate risk

Interest rate risk arises from the different interest rate characteristics of the Society's mortgages and savings products and from other financial instruments. In particular, the issue of fixed and capped rate mortgages and fixed rate savings products exposes an organisation that principally operates within a variable rate environment (such as the Society) to the risk that interest rate fluctuations could cause either a reduction in interest income or an increase in interest expense relative to other interest flows.

Where the Society has issued fixed rate mortgages, the risk is that a general increase in interest rates would leave the Society facing higher interest expense, but without a compensating increase in interest income. In these circumstances, the Society would typically take out an interest rate swap with a counterparty bank under which the Society's fixed rate income is exchanged for one based on a variable rate which would be expected to follow the general pattern of interest rate movements and thereby reduce the Society's exposure. Similarly, in cases of issuing fixed rate savings products, the Society would typically take out an interest rate swap under which the Society receives a fixed rate of interest and pays a variable rate. With capped rate mortgages, the risk is that if the rates increase above a pre-determined level, the Society will be unable to increase its mortgage rate on these products to compensate. In these circumstances, the Society would typically purchase a rate cap that will pay a variable rate if an agreed index rate (for example, LIBOR) exceeds a certain level. In addition, the Society regularly forecasts the impact of movements in the Bank of England Base Rate on the Society's balance sheet to ensure any potential adverse impact can be anticipated. This information is reported to ALCO.

The Society does not trade or take speculative positions on derivatives.

Foreign currency risk

Foreign currency risk arises as a result of the Society's activities in raising funds and making investments in foreign currencies. This is undertaken to ensure wholesale funds are obtained cost-effectively across a wide pool of potential providers, but exposes the Society to the risk of an appreciation in the value of foreign currency denominated liabilities or a deterioration in the value of the foreign currency denominated assets if exchange rates change. The risk is managed through the use of currency swaps and foreign currency forward contracts and also, where appropriate, by the matching of foreign currency liabilities with assets denominated in the same currency.

Details of the Society's exposure to interest rate and foreign currency risk are contained in note 40 to the Accounts.

House price risk

House price risk is present in two forms. Most significantly this risk arises from the value of the property forming the security for a mortgage being insufficient to repay the loan in the event of default and subsequent repossession. The Society manages this risk through a combination of prudent loan to value limits at inception and ongoing monitoring to ensure that bad debt provisions are sufficient to cover the potential losses that may arise in repossession situations.

With respect to lifetime mortgages, house price risk also arises from the 'no negative equity' guarantee, whereby the borrower is guaranteed that the amount recoverable by the Society at the end of the mortgage will not exceed the value of the property.

Under these loans, the borrower receives an advance but makes no payments of interest or principal until the loan is redeemed. The interest is added to the loan and recovered by the Society when the loan is redeemed. The 'no negative equity' guarantee therefore exposes the Society to the risk that the value of the property at the time of redemption is lower than the loan plus accumulated interest. The Society manages this risk by granting loans only at relatively low loan to value ratios, subject to the age of the borrower, and through the use of statistical modelling to stress potential exposures within acceptable prudent limits. Only 2% of the Society's outstanding mortgage balances have been advanced on this type of product. The Society does not currently offer these products to new applicants.

The risks presented by house price movements are evaluated through stress testing and monitored by the Retail Credit Risk Committee and ALCO and, through these Committees, by the RMC and the Board Risk Committee.

RISK MANAGEMENT REPORT
(continued)

Liquidity risk

Liquidity risk is the risk that the Society will be unable to meet its financial obligations as they fall due or can do so only at excessive cost. The risk is managed principally by holding funds in cash accounts and other easily realisable liquid assets. The amount and composition of liquid assets held is subject to guidance from the FSA and to the Society's regular stress testing programme that ensures it remains adequate. The stress testing programme, and other policies addressing liquidity risk, are set out in the Society's annual Individual Liquidity Adequacy Assessment (ILAA). The ILAA considers a range of time horizons from one day to several years and is compliant with the BIPRU 12 regime that was introduced by the FSA in 2010. This has resulted in a greater proportion of the liquidity book being represented by UK Government securities or invested with the Bank of England via a current account. Whilst these assets realise a relatively low yield, this reflects the very low credit risk represented by a AAA rated sovereign entity, such as the UK Government, and ensures the assets can readily be converted into cash to meet liabilities, as they fall due. Day-to-day management of the Society's liquidity position is the responsibility of the Liquidity Planning team working closely with the Treasury and Balance Sheet Management functions and is monitored by ALCO and, through this Committee, by the RMC and the Board Risk Committee.

Liquidity risk is also managed through sale and repurchase arrangements (repos). Treasury assets are encumbered through repo and stock lending programmes, which ensure that these assets remain liquid and readily realisable.

Operational risk

Operational risk is the risk of loss arising from inadequate internal processes, people and systems or from external events. These risks are managed as an integral part of the operation of each of the Society's business units. Management has a responsibility to understand how operational risk impacts the area of the business for which they are responsible, and for putting in place controls or mitigating activities, overseen and challenged by the Operational Risk team which acts as the second line of defence. This team also ensures co-ordination of the Society's operational risk assessment, risk event management process, operational risk stress testing, controls design and other associated activities and is overseen by the Operational Risk Committee, RMC and the Board Risk Committee.

Key operational risks are considered more broadly in the context of potential linkages to reputational risk, regulatory and compliance risk, change risk, legal risks, information technology and systems risk and business risk. The Society regularly stress tests such risks better to understand and manage the impacts of their occurrence and quantification to support regulatory capital allocation. This educates the Society's broader stress testing framework, including reverse stress testing.

Regulatory and compliance risk

The Society is committed to meeting its legal and regulatory responsibilities and has a team dedicated to developing business standards and policy, overseeing regulatory change and monitoring compliance. In particular the Society is focused on delivering positive customer outcomes in the development and distribution of its products and services. These activities are overseen by the Compliance and Financial Crime Committee.

Financial crime

Financial crime is managed by the Society's Financial Crime team which is part of the risk management function, reporting directly to the Chief Risk Officer and overseen by the Society's Compliance and Financial Crime Committee.

This reflects the Society's desire to recognise and structure Financial Crime as a separate discipline with dedicated expertise to respond professionally to the evolving and substantial threat to the security and the safe operation of all financial institutions. Given the rapidly growing developments in technology, cyber-crime and communication and social media, the Society pays close attention to the source, likelihood and impact of financial crime generally and the various ways in which this could manifest itself. As such, the Society continues to increase investment in resourcing its Financial Crime team and monitoring and control systems to prevent increasingly sophisticated criminal attacks.

Security and safety

The Society has a duty of care to its staff, members and visitors whilst present on Society premises. The Society has in place comprehensive health and safety polices and a compliance regime which includes internal and external inspection, the maintenance and testing of equipment as well as appropriate training programmes which are all reviewed regularly. This work is overseen by the Security and Safety Committee which reports to the Operational Risk Committee, RMC and Board each month.

Business continuity

In addition the Society has developed Business Continuity Plans to manage situations in which buildings, systems or significant staff are unavailable, for example, in the event of a flu pandemic or the loss of utilities. The Society's Business Continuity Plan is overseen by the Business Continuity Committee which reports into the Operational Risk Committee and is overseen by RMC and the Board Risk Committee.

Business risk

Business risk encompasses those aspects of the external environment that have the potential to affect the Society's business model. This is particularly relevant in the context of the multiple major regulatory initiatives currently being proposed or implemented, including ones which cover liquidity, capital, governance, the special resolution regime, reform of the Financial Services Compensation Scheme and conduct of business, including a review of the mortgage market and retail distribution. The regulatory agenda is considered to be of strategic importance and as such it is actively considered by all directors and senior management with the support of the compliance function.

Further details of risk exposures are available in our Pillar 3 Disclosures on the Society's website: thecoventry.co.uk/pillar3

CAPITAL

The Board determines the level of capital required to support the Society's business objectives through its Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP evaluates the Group's risk management framework, together with financial projections contained in the corporate plan, in order to assess the significant risks to which it is exposed and the capital resources it needs to support its risk exposure over a five year horizon.

The ICAAP incorporates expected future capital requirements from changes in business volumes, mix of assets and activities within the context of current and anticipated future risks, and market stress scenarios. The ICAAP is used by the FSA in its Supervisory Review and Evaluation Process (SREP) through which it sets the Group's capital requirements as Individual Capital Guidance (ICG). The amount, composition and adequacy of the Group's capital requirement is determined by assessing the Basel II minimum capital requirement, the impact of stress and scenario tests and the Group's ICG.

The ICAAP is reviewed by the Board Risk Committee before submission to the Board for formal approval as part of the corporate planning process. The Society's internal audit function reviews the accuracy and consistency of the financial information included within the ICAAP document.

Capital levels for the Group are reported to and monitored by the Board on a monthly basis. The Group continues to be strongly capitalised and manages its capital substantially above the ICG and Basel II transitional floors at all times. The Group's core tier 1 capital ratio is the highest reported by any building society.

Further details of the Group's capital can be found on pages 15 and 16.

DIRECTORS' REPORT ON CORPORATE GOVERNANCE

The Board is accountable to the Society's members for the operation of the Society and places the highest priority on good corporate governance.

This report explains how the Board applies the principles of the UK Corporate Governance Code, 'the Code' (formerly the Combined Code which was updated in 2010) issued by the Financial Reporting Council and the BSA Guidance for Building Societies on the Code. The Board has considered the requirements of the revised Code and will continue to comply in a manner which is proportionate to the Society's size and scale. Where the provisions of the Code and any revisions to it, have not been adopted an explanation is provided below.

THE BOARD OF DIRECTORS

The Society's Rules detail the appointment process for directors and require that the Board comprises not less than six, nor more than 12 directors. The Board has determined that its current composition is appropriate. The Board currently comprises a Chairman, six independent non-executive directors and three executive directors.

The following persons served as directors of the Society during the year: Bridget Blow, Roger Burnell, Colin Franklin, Ian Geden, David Harding, John Lowe, Ian Pickering, Fiona Smith, Glyn Smith, David Stewart and Phil Vaughan (resigned 28 April 2011).

No director has any interest in the shares or debentures of any associated body of the Society.

The Board has a formal schedule of matters that are reserved to it, and it has also delegated authority in other matters to a number of Board Committees, as described below. The Board has set clear terms of reference for these committees and has clearly documented delegated authority to the executive directors and senior management together with reporting systems for financial results, risk exposure and control assessment.

The Board applies principles of good governance by adopting the following procedures:

- the Board's role is to set the Society's risk appetite, strategy, review performance, risk management and ensure that the necessary resources are in place for it to meet its objectives. The Board also has a general duty to ensure that the Society operates within its Rules, relevant laws, rules and guidance issued by relevant regulatory authorities and that proper accounting records and effective systems of internal control are established, maintained, documented and audited. In particular the Board's role is to provide overall direction to the Society and to safeguard the interests of its members. Other powers are devolved to the executive directors and senior management;

- the Board meets monthly (except August), and also holds an annual strategy review meeting. The non-executive directors also meet, without executive directors present, at least once a year;

- the size and composition of the Board and the senior management team is kept under review to ensure that there is adequate succession planning for executive and non-executive directors and that the Board has the appropriate skills and experience for the direction of the Society's activities;

- directors receive accurate, timely and clear information and it is the responsibility of the Chairman to ensure that this information is considered by the Board;

- the Chairman also ensures that, on appointment, non-executive directors receive a comprehensive tailored induction programme that covers the Society's business and regulatory environment. Non-executive directors update their skills, knowledge and familiarity with the Society through presentations by senior managers and by attending relevant bespoke internal and external courses; and

- all directors have access to the advice and services of the Secretary and General Counsel, whose appointment is a matter for the Board. The Secretary and General Counsel is responsible for ensuring compliance with Board procedures and advising the Board, through the Chairman, on governance related matters.

The Society maintains liability insurance cover for directors and officers as permitted by the Building Societies Act 1986.

Set out in the table below are details of the directors during 2011 and their attendance record at Board meetings and relevant Board committee meetings during the year.

BOARD COMMITTEES AND MEETINGS 2011

Name	Title	Number of Board Meetings – 14	Number of Board Audit Committee Meetings – 6	Number of Board Risk Committee Meetings – 9	Number of Nominations and Governance Committee Meetings – 1	Number of Remuneration Committee Meetings – 4
David Harding	Chairman	14		9	1	4
Bridget Blow	Deputy Chairman	14	5[1]	3[3]	1	4
Roger Burnell	Non-executive director	14	2[2]	9		4
Colin Franklin	Sales and Marketing Director	14		4[3]		
Ian Geden	Non-executive director	13	5	4[3]		3
John Lowe	Finance Director	14		9		
Ian Pickering	Non-executive director	14	6	9		3
Fiona Smith	Non-executive director	13		4[3]		4
Glyn Smith	Non-executive director	13	6	9		4
David Stewart	Chief Executive	14		9	1	
Phil Vaughan	Chief Operating Officer (resigned 28 April 2011)	3[4]		3[4]		

[1] Re-appointed to the Board Audit Committee on 22 June 2011 – maximum number of Board Audit meetings is 5 as previously a member up to May 2011.
[2] Retired as a member of the Board Audit Committee on 22 June 2011 – maximum number of Board Audit meetings is 2.
[3] Retired as a member of the Board Risk Committee on 22 June 2011 – maximum number of Board Risk meetings is 4.
[4] Resigned on 28 April 2011 – maximum number of Board and Board Risk meetings is 4.

NON-EXECUTIVE DIRECTORS

In the opinion of the Board, Bridget Blow, Roger Burnell, Ian Geden, Ian Pickering, Fiona Smith and Glyn Smith are independent in character and judgement. In accordance with the Code the Board acknowledges that the test of independence is not appropriate in relation to the Chairman, David Harding.

Bridget Blow undertakes the duties of Senior Independent Director insofar as they are relevant to a mutual organisation.

CHAIRMAN AND CHIEF EXECUTIVE

The roles of the Chairman and Chief Executive are held by different people and are distinct in their purpose.

The Chairman is responsible for leading the Board and ensuring that it acts effectively. The Chief Executive has overall responsibility for managing the Society and for implementing the strategies and policies agreed by the Board.

David Harding and Bridget Blow were re-elected Chairman and Deputy Chairman respectively on 25 May 2011.

PERFORMANCE EVALUATION

The performance of the non-executive directors and each of the Board Committees is appraised by the Nominations and Governance Committee, and the Chairman's performance is reviewed by the rest of the Board, in the absence of the Chairman.

DIRECTORS' REPORT ON CORPORATE GOVERNANCE
(continued)

The Board also periodically reviews its own performance, and in 2011 the Chairman commissioned Praesta Partners LLP to undertake an externally facilitated Board Effectiveness Review to look at the way the Board was working, particularly given the FSA's increasing requirements of building society directors. The Review confirmed that the Board operated effectively and made certain recommendations as to how the Board Committee structure might be improved which have been adopted.

In addition, all directors have open and direct access to the Chairman and to the Senior Independent Director in order to raise any issues of concern.

APPOINTMENTS TO THE BOARD

The appointment of new directors is considered by the Nominations and Governance Committee which makes recommendations to the Board. In accordance with Rule 25 of the Society's Rules, all directors are subject to election by members at the AGM following their appointment or, where applicable, at the next following AGM. In addition, all directors must receive approval from the FSA as an approved person in order to fulfil their controlled function as a director.

In considering appointments to the Board the directors recognise and value the contribution that may be made from individuals with a broad range of skills and professional and business experience.

Under Rule 26, directors have to submit themselves for re-election at least once every three years.

The directors retiring by rotation are Roger Burnell, Ian Geden and David Stewart.

David Harding joined the Board in 1996, becoming Chairman in 2005. Fiona Smith joined the Board in 2002. The Code has recommended that non-executive directors should only serve a term of more than nine years in exceptional circumstances, although comments in the Walker Review of Governance in Banks and Other Financial Institutions have recognised the importance of retaining experience in the sector.

In February 2012, the Board, excluding, for this purpose, the Chairman, conducted a review to assess David Harding's performance as Chairman. They confirmed that he has led the Board effectively through a period of transition and difficult market conditions during which time the Society has performed extremely well.

In accordance with the Code, the Chairman, on behalf of the Board conducted a review of Fiona Smith concluding that she remained independent and provided effective challenge. In February 2012, excluding for this purpose Fiona Smith, the Chairman reported his conclusions to the Board and the Board supported Fiona Smith's re-election for a further period of 12 months.

The Board has decided unanimously to recommend for re-election by the members at this year's AGM the following directors:

Roger Burnell
Ian Geden
David Harding
Fiona Smith
David Stewart

As noted above, although it is not obliged to do so, the Society complies with and has regard to the revisions to the Code in 2010 insofar as it is appropriate. In this connection the Board has considered the provisions of the revised Code and does not feel that it would be appropriate, at present, to submit the entire Board for annual re-election by the members. The Board will continue to keep under review the appropriateness of the revised Code's provisions on the annual election of directors.

In addition to attendance at Board and committee meetings, as detailed below, and meetings with senior management and branch visits, non-executive directors are required to complete a detailed induction programme (on appointment) and to participate in a structured programme of director training in order to keep abreast with new regulatory requirements and some of the more technical aspects of the role. Non-executive directors are also encouraged to engage with the Society's members through the AGM process, the Society's Members Council Meetings and the Society's programme of member roadshows.

BOARD COMMITTEES

The Board has established a number of committees that have their own terms of reference. Details of the principal Board Committees, including their membership, are set out below.

BOARD RISK COMMITTEE

The Board Risk Committee assists the Board in fulfilling its oversight responsibilities for risk management across the Society. In particular the Committee undertakes the following:

- oversees and advises the Board in relation to current and potential future risk exposures to the Society, including determination of risk appetite, risk limits and tolerances across the full range of risks to which the Society may be exposed;

- satisfies itself on the design and completeness of the Society's internal control and assurance framework relative to the risks that it faces including culture, policy, processes, structure and systems;
- reviews major initiatives, such as acquisitions or change projects, and seeks assurance that appropriate due diligence has been carried out and that any associated movement in risks to which the Society may be exposed remains within risk appetite.

The Committee meets monthly and the members of the Committee are:

Ian Pickering (Committee Chairman, appointed 1 December 2011, and non-executive director)
Roger Burnell (non-executive director)
Peter Elcock (Chief Risk Officer)
John Lowe (Finance Director)
Glyn Smith (non-executive director)
Fiona Smith (non-executive director, reappointed as a member of the Committee on 22 February 2012, following retirement on 22 June 2011)
David Stewart (Chief Executive)

David Harding (Board Chairman) served as Committee chairman up to 1 December 2011 and retired as a member of the Committee in January 2012. The Society's Secretary and General Counsel attends Board Risk Committee meetings.

BOARD AUDIT COMMITTEE

The responsibilities of the Committee are in line with the provisions of the Financial Reporting Council Guidance on Audit Committees. The main function of the Committee is to assist the Board in fulfilling its oversight responsibilities with specific regard to:

- monitoring the integrity of the half-year and annual financial statements and any formal announcements relating to financial performance, focusing particularly on significant financial reporting judgements contained in them;
- reviewing the adequacy of systems of internal control and risk management processes;
- approving the annual internal audit plan;
- monitoring the effectiveness of the external audit process and making recommendations to the Board on the appointment, re-appointment and remuneration of the external auditors;
- ensuring that an appropriate relationship between the Society and the external auditors is maintained, including reviewing non-audit services which can be provided and fees; and
- reviewing the effectiveness of the internal audit function. The Committee is responsible for approving the appointment and removal of the Head of Internal Audit.

In 2011, the Committee met six times in the execution of its responsibilities and, in particular, considered reports on the following matters:

- the Society's risk management framework and systems of internal control;
- the integrity of financial statements;
- the activities of internal and external auditors, including the effectiveness of the internal audit function and the performance of the external auditor;
- the appointment of the external audit firm to undertake non-audit services;
- the effectiveness of the Committee; and
- the Society's whistle-blowing arrangements.

Reports were provided by the finance, internal audit, operational risk and compliance functions and the external auditors.

The Committee also held private discussions with the external auditors, the Chief Risk Officer and the Head of Internal Audit. The minutes of the Board Audit Committee are distributed to the Board and the Committee Chairman reports verbally to the Board meeting immediately following Committee meetings.

The Committee regularly reviews and monitors the Society's relationship with the external auditors to ensure that auditor independence and objectivity is maintained at all times, taking into consideration relevant UK professional and regulatory requirements. The Committee has developed a policy and framework which defines unacceptable non-audit assignments, pre-approval of acceptable non-audit assignments and procedures for approval of other non-audit assignments. This framework ensures that at no time will the external auditors audit their own work, make management decisions for the Society, create a conflict of interest or find themselves in the role of advocate for the Society. Further, the Society's policy and framework requires that the external auditors should not be appointed if the threat is other than clearly insignificant, unless appropriate safeguards can be applied to eliminate or reduce the threat of objectivity to an acceptable level.

During 2011 the Society engaged the external audit firm to provide significant non-audit services. These engagements included services connected with the merger with Stroud & Swindon Building Society and other regulatory, accounting and taxation advice. Prior to the engagement the Committee undertook a review, within the terms of the Society's policy and framework, to satisfy itself on the following:

(i) the skills and experience of the audit firm,
(ii) the safeguards in place to eliminate or reduce any threat to objectivity and independence,

(iii) the nature of the non-audit services,
(iv) the fees to be incurred for non-audit services, and
(v) the criteria which govern the compensation of the individuals performing the audit.

During 2011 the Committee received advice on its role and responsibilities to review and monitor the external auditor's independence and objectivity and the audit partner, Mr Wallace, provided assurance to the Committee that he was satisfied that appropriate safeguards were put in place within the audit firm to satisfy the requirements of the Auditing Practices Board Ethical Standard 5. Mr Wallace confirmed to the Committee that the objectivity of his opinion on the Society's financial statements would not be impaired. The Committee concluded, prior to each engagement for the provision of non-audit services, that it would be in the best interests of the Society to proceed with the appointment of the audit firm to undertake such services. The Committee keeps non-audit engagements under review and receives regular reports from the audit partner confirming that adequate safeguards remain in place. The Society also assigned services to a number of major accountancy firms during the year.

Details of the fees paid to the external auditors for audit and non-audit services are set out in note 9 in the Accounts.

The outcome of the Committee's monitoring informs the Committee's recommendation to the Board on the re-appointment of the external auditors. The final decision on the recommendation to the members is reserved for the Board.

The Committee ran a tender in relation to the Society's external audit work in 2007 and plans to run a similar exercise by 2014.

The Committee consists of the following non-executive directors only:

Glyn Smith (Committee Chairman since 1 December 2011)
Ian Pickering (Committee Chairman up to 1 December 2011)
Bridget Blow (Reappointed as a member of the Committee on 22 June 2011, following retirement in May 2011)
Roger Burnell (Retired from the Committee on 22 June 2011)
Ian Geden

The Society's external auditors, the Chief Executive, Finance Director, Chief Risk Officer, Secretary and General Counsel, Head of Internal Audit and other senior managers attend meetings as required by the Committee. In addition, the external auditors meet members of the Committee in a private session at least annually.

The Chairman of the Committee, Glyn Smith, has recent and relevant financial experience and is a Chartered Accountant.

The Committee also completed a self appraisal exercise in 2011 and considers that it has met its responsibilities and performed its duties with appropriate levels of care and expertise.

NOMINATIONS AND GOVERNANCE COMMITTEE

The Committee consists of:

David Harding, Chairman of the Society and Committee Chairman
Bridget Blow, Deputy Chairman
David Stewart, Chief Executive

The Committee is responsible for making recommendations to the Board on matters relating to the composition of the Board (including Board succession planning, the appointment of new directors, the re-appointment of retiring directors, the appointment of non-executive and executive directors to Committees of the Board and senior management appointments).

In 2011 the Committee met and considered, amongst other things, its terms of reference, Board Committee membership and the appointment of a new Secretary and General Counsel and Chief Risk Officer.

Through the AGM process the Society issues a standing invitation to members to apply for the position of non-executive director. Through this process a number of candidates were interviewed by members of the Committee in 2011 and previous appointments to the Board through this process include the appointments in 2008 of two new non-executive directors. External consultants and recruitment specialists are also employed by the Society in considering director and senior management succession planning.

REMUNERATION COMMITTEE

Since January 2012 the Committee consists of:

Bridget Blow, Deputy Chairman and Senior Independent Director (Committee Chairman)
Roger Burnell
Ian Geden
David Harding
Fiona Smith

Throughout 2011 all the non-executive directors were members of the Remuneration Committee. Ian Pickering and Glyn Smith retired from the Committee in January 2012.

The Committee is responsible for considering and approving the remuneration of executive directors and senior management and also sets targets for the Society's performance related bonus scheme in which all staff members participate. During 2011 the Committee has reviewed the implications of the FSA's Remuneration Code and approved the Society's Remuneration Policy Statement on behalf of the Board. In 2011 the Committee met four times. Further details of the Committee, the remuneration policy and directors' service contracts can be found in the Directors' Remuneration Report on pages 32 to 36.

The Code states that the Remuneration Committee should set the remuneration of the Chairman. However, the Board believes that it is more appropriate for the remuneration of the Chairman to be set and reviewed in the same manner as that used to determine the remuneration for the other non-executive directors. It is therefore dealt with by the Board, acting upon a recommendation from the executive directors and excluding, for this purpose, the Chairman. No director takes part in the discussion of his/her own remuneration.

The terms of reference of the Board Risk Committee, Board Audit Committee, the Nominations and Governance Committee and the Remuneration Committee, and the letters of appointment for non-executive directors, are available on request from the Secretary and General Counsel.

INTERNAL CONTROLS

Responsibility for implementing sound and effective systems of internal control has been delegated by the Board to senior management. The internal audit function provides independent assurance to the Board on the effectiveness of the systems of internal control through the Board Audit Committee.

The information received and considered by the Board Audit Committee provided assurance that, during 2011, there were no material breaches of control or regulatory requirements and that, overall, the Society maintained adequate systems of internal control.

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

- regular reports to the Board, through the Board Audit Committee, from the internal audit function in respect of their independent audits of risk management processes and the effectiveness of internal controls across the Society. The Head of Internal Audit has direct access to the Chairman of the Board Audit Committee;

- regular reports to the Board, through the Board Risk Committee, from the Risk function on the principal operational, credit, business and regulatory risks facing the Society and the strength of the controls in place to mitigate such risks. The Chief Risk Officer has direct access to the Chairman of the Board Risk Committee;

- regular reports and presentations to the Board by the Chairmen of the various Board Committees – see above; and

- reports presented by the Chief Risk Officer at each Board meeting.

The Society is committed to internal control and risk management in the operation of the Society and to deal with areas for improvement, which come to the attention of executive management and the Board promptly. The Society has a comprehensive system for reporting business, operational and financial performance to the Board.

The Society has a number of functions including Finance, Risk and Compliance, that establish and monitor the implementation of policies and processes across the Society. Each of these functions is subject to review by the internal audit function.

The internal audit function is responsible for independently reviewing and reporting on the adequacy and effectiveness of internal controls operated by management across the Society, thereby helping to evaluate and improve the effectiveness of risk management, regulatory compliance, control and governance processes. Through its programme of work, agreed by the Board Audit Committee, the internal audit function is able to provide assurance on control effectiveness.

The Board is satisfied that during 2011 the Society maintained an adequate system of internal control that met the requirements of the Code.

RELATIONS WITH MEMBERS

The Society's members comprise its shareholding investors and borrowers. The majority of its customers are therefore members and the Society encourages feedback from them on all aspects of the Society's activities.

All members who are eligible are also encouraged to exercise their vote at the AGM either by attending in person or by voting by proxy, for which purpose they are sent a proxy voting form and reply-paid envelope, or they can vote in any branch or online. All proxy votes are counted. All resolutions are taken on a poll and the Chairman indicates the level of proxies lodged on each resolution by announcing the numbers for and against the resolution and the number withheld. A separate resolution is proposed on each item including a resolution on the Annual Report & Accounts. The Society employs Electoral Reform Services Limited to act as independent scrutineers and ensure the votes are properly received and recorded.

DIRECTORS' REMUNERATION REPORT

INTRODUCTION

This report informs members of the policy for the remuneration of both executive and non-executive directors who are equally responsible in law for directing the Society's affairs.

In order to comply with the disclosure requirements of the Capital Requirements Directive (CRD 3), in respect of 'Code Staff', this report also outlines the responsibilities and decision-making process for determining remuneration policy, the link between pay and performance and the design and structure of remuneration, including the performance pay plans.

REMUNERATION DISCLOSURE REQUIREMENTS

The Society is compliant with the FSA's Remuneration Code, and meets the additional requirements of the FSA's rules regarding remuneration disclosure, in compliance with the CRD 3.

These additional disclosures focus on the remuneration policies and practices for staff who have a material impact on the Society's risk profile ('Code Staff'). Code staff consist of executive directors, non-executive directors and certain senior managers in control functions (e.g. human resources, audit, risk and compliance).

Responsibility for the approval and periodic review of the Society's remuneration policy, while having due regard to the FSA's Remuneration Code, rests with the Board Remuneration Committee. This includes ensuring that the Society complies with the FSA remuneration disclosure requirements.

SOCIETY REMUNERATION POLICY - PRINCIPLES

The Society's remuneration policy is based on the following key principles:

- the remuneration of directors and other Code Staff, including staff in control functions, is in line with the FSA's Remuneration Code;
- total rewards, subject to satisfactory performance, should be competitive and positioned around the market median for the comparator group;
- incentive plans, performance measures and targets are stretching and aligned with members' interests;
- policy is designed to recruit and retain quality staff at all levels and to ensure that remuneration packages reflect their responsibilities, performance and experience;
- remuneration promotes sound and effective risk management and does not encourage excessive risk taking;
- remuneration strategy is in line with the business strategy, objectives, values and long-term interests of the Society;
- remuneration strategy does not result in conflicts of interests;
- remuneration is consistent with the overall financial stability of the Society and does not present material risk to this stability;
- bonus payments will be limited or withdrawn where individual or business performance does not merit payment of a bonus;
- where staff do not perform to the required standard, under performance will not be rewarded;
- remuneration of staff in control functions does not affect their independence in any way;
- the performance of all staff is reviewed each year against agreed individual and business objectives. The outcome of this review is taken into account when considering pay decisions; and
- no executive director, senior manager or member of staff is involved in the setting of his or her own remuneration.

REMUNERATION COMMITTEE

The Board has overall responsibility for the Society's remuneration, which is delegated to the Remuneration Committee. The Committee consists exclusively of non-executive directors and is chaired by Bridget Blow, Deputy Chairman and Senior Independent Director.

The Remuneration Committee is responsible for setting and reviewing the elements that comprise the remuneration package for executive directors and senior management. These currently comprise a base salary, performance related bonuses, pension arrangements and other benefits. The Committee sets the targets of the Long Term Incentive Plan (LTIP) for executive directors and senior management and for the Society's annual performance related bonus scheme in which all staff members participate on the same basis.

In fulfilling this responsibility, the Remuneration Committee has taken full account of industry best practice as advised by the FSA and reviewed the remuneration policies of the Society's peer group and other businesses of a similar size and complexity.

Independent consultants have been commissioned to review the Society's remuneration for senior managers, and for executive and non-executive directors, including the Chairman; Towers Watson provides general salary benchmarking data to the Society, and KPMG LLP has provided advice on matters relating to the remuneration of executive directors and other senior management. In 2011 the Remuneration Committee met four times.

POLICY FOR EXECUTIVE DIRECTORS

Executive directors are employed by the Society and are required to devote substantially the whole of their time to its affairs. The policy of the Board is to recruit and retain high calibre executive directors and to ensure that their remuneration reflects their responsibilities, experience and performance.

As would be expected, the Remuneration Committee has taken full account of best practice in executive reward and in corporate governance. The UK Corporate Governance Code states that "a significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance". It continues that performance related elements should be "stretching and designed to promote the long-term success of the company". In doing so, it provides that some bonus arrangements are necessary if the Society is to meet the requirements of the Code.

The Remuneration Committee accepts best practice recommendations and believes that carefully controlled performance related bonuses, which enable a flexible approach to remuneration, are in the best interests of the Society and its members. It enables payments to be aligned accurately to results and ensures that the Society's costs are reduced if for any reason financial performance deteriorates.

The Committee believe that a combination of short and long-term plans support this objective. However it is essential that these payments are not excessive, and added together they are currently limited to a maximum of 60% of fixed pay. In addition, as described further below, all payments are signed off by the Remuneration Committee which takes account of a number of factors to ensure that remuneration is consistent with and promotes effective risk management and fair treatment of members.

Whilst the Remuneration Committee accepts that best practice requires that a significant proportion of remuneration should be paid by way of variable, performance related pay, it is alert to the risk of excessive bonus payments and therefore it continues to set the potential for bonuses at levels below those typically available at similar institutions.

The results of the Society's annual benchmarking exercise, together with the Society's remuneration policy, were reviewed by KPMG LLP who confirmed that the potential for variable pay for the executive directors (comprising the annual performance related bonus and the LTIP) is below market median, as is the level of total remuneration.

The FSA's Remuneration Code indicates that at least 50% of any variable remuneration component is to be made in shares, share linked instruments or other equivalent non-cash instruments, subject to an undefined retention period and the de minimis rules. As a membership owned, mutual institution no such instruments currently exist. This sector wide issue is recognised by the FSA and ways to address this anomaly are under discussion, with resolution required by 1 July 2012. The structure of the Society's Long Term Incentive Plan meets the FSA's requirements for part of the variable element of remuneration to be deferred for certain staff.

The principal elements of the Society's remuneration packages are described in the following sections:

a) Base salary

For all employed staff, including executive directors, the Society aims to pay fair and competitive salaries, linked to individual performance. To ensure this, salaries are compared to market rates with the aim of paying market median rates for experienced staff who have minimal training needs and who are performing to a good standard or above.

For each role there is a salary range, which allows for salaries to increase as individuals become more experienced in their role. Some areas of the business have accreditation or salary progression schemes which apply a minimum salary level when certain performance criteria have been demonstrated consistently.

b) Annual performance related bonus

All eligible staff participate in a discretionary annual performance related bonus scheme. Eligibility is dependent upon satisfactory individual performance. It applies to all staff on the same terms, including executive directors and senior management, Code Staff and staff in control functions. It does not apply to non-executive directors.

The scheme is reviewed each year in the light of business plans. The target requires that a certain level of profit before tax and certain exceptional items is achieved, with the Board retaining the discretion to change the threshold target in the light of unforeseen events and the determination of exceptional items. The Remuneration Committee also takes into account the Society's non-financial performance including customer satisfaction before an annual performance related bonus is calculated.

The annual performance related bonus is calculated as a percentage of base annual salary as at 31 December each year, the last day of the scheme year. There is no guarantee that a payment will result.

In line with the FSA's Remuneration Code, the Remuneration Committee will adjust the annual performance related bonus in respect of Code Staff if it deems this to be appropriate, taking into account a range of factors including satisfactory individual performance, risk management and customer service.

c) Long Term Incentive Plan

The Remuneration Committee established the Long Term Incentive Plan (LTIP) to ensure a strong link between the remuneration package of executive directors and senior managers and the interests of members through an assessment of the long-term performance of the Society.

The subsequent provision of the FSA's Remuneration Code confirmed the requirement for part of the variable remuneration to be deferred for certain staff. The Long Term Incentive Plan fulfils this requirement.

The primary objective of this plan is to align remuneration with the longer term goals of the Society. The LTIP also helps the Society to recruit and retain high calibre individuals and to ensure that their remuneration packages reflect their responsibilities, performance and experience.

In 2011, an LTIP grant was made, whereby participants are eligible to receive a performance related payment based on the financial performance of the Society over a rolling three year period from 2011-2013. These are accrued in the accounts over the vesting period.

The plan is designed to make payments in the year following the end of the three year period provided that consistent and strong performance is achieved against the three year plan. An on-target performance would provide a 10% of salary payment for executive directors and a 5% of salary payment for other senior management, with a current maximum of 40% (executive directors) or 20% (senior management) for substantial over-performance over the period. This is below the 50% of salary maximum currently permitted under the Society's Rules. There are currently three executive directors and four senior managers that have been awarded grants under one or more of the Society's LTIP schemes.

The Scheme requires that a certain level of profitability is achieved whilst maintaining the competitiveness of the Society's savings and mortgage products as measured by the interest rates offered. The Remuneration Committee reviews all payments and can award a lower amount if appropriate. To protect the interests of members, the Committee may amend any payment if it considers it appropriate in light of either the Society's overall performance or economic conditions. In making its assessment the Remuneration Committee may take into account any one or more of the following factors:

- market share;
- customer and member satisfaction;
- health and safety record;
- risk management factors;
- overall financial performance of the Society relative to the performance of other building societies and in light of the market conditions prevailing during the performance period;
- individual performance; and
- any other factors the Remuneration Committee feels are relevant.

All payments under the LTIP are subject to approval by the Remuneration Committee and are not pensionable.

d) Pension arrangements

Coventry Building Society closed its final salary pension scheme to all new entrants, including senior managers, in December 2001, replacing it with a defined contribution pension scheme.

No special arrangements have been put in place for the executive directors or senior management since this change was implemented and consequently the Finance Director, who joined subsequent to 2002, is an active member of the Society's funded defined contribution pension scheme.

David Stewart left the final salary scheme immediately before being appointed Chief Executive in July 2006, and joined the defined contribution scheme.

The Sales and Marketing Director, whose long service at the Society pre-dates 2002 by a number of years, continues to be a member of the Society's contributory final salary pension scheme.

Full details of executive directors' pension benefits can be found in note 11 on pages 55 and 56 to the Accounts.

e) Other benefits

Each executive director is provided with a fully expensed car or a cash alternative, and personal membership of a private medical insurance scheme.

NON-EXECUTIVE DIRECTORS

Non-executive directors are independent of the Society's management and are not required to devote the whole of their time to its affairs.

A Committee consisting of the Chairman, Chief Executive, Finance Director and Head of Human Resources has been established in 2012, to set and review the elements that comprise the remuneration of non-executive directors. No director takes part in the discussion of his or her own remuneration and recommendations for the remuneration of the Chairman are made by executive management.

Fees of non-executive directors, are reviewed annually in light of their responsibilities and comparative information from other building societies, and financial institutions. Consistent with the Society's approach to the remuneration of executive directors, the Society has reviewed fees paid by similar institutions and found that those paid at Coventry are typically below those made elsewhere.

Non-executive directors do not participate in any performance related pay or bonus scheme, pension arrangements or other benefits.

Directors emoluments are disclosed in Note 11 to the Accounts, on pages 55 and 56.

DIRECTORS' SERVICE CONTRACTS

In 2006 the Society entered into a service contract with David Stewart (Chief Executive), and is terminable by David Stewart on six months' notice and by the Society on one year's notice.

In 2009 the Society appointed Colin Franklin (Sales and Marketing Director) to the Board. A service contract was entered into which is terminable by Colin Franklin on six months' notice and by the Society on one year's notice.

In 2010 the Society appointed John Lowe (Finance Director) to the Board. A service contract was entered into, which is terminable by John Lowe on six months' notice and by the Society on one year's notice.

Phil Vaughan (Chief Operating Officer) resigned from the Board on 28 April 2011.

AGGREGATE REMUNERATION DATA

The Prudential Sourcebook for Banks, Building Societies and Investment Firms (BIPRU) requires the Society to disclose aggregate remuneration data for all staff and separately for all Board directors, senior management and members of staff whose actions have a material impact on the risk profile of the firm (Code Staff). Total fixed pay paid to all employees in 2011 was £46.4 million and variable pay was £4.6 million. Details of remuneration to Code Staff are detailed on page 36.

2011 ANNUAL PERFORMANCE BONUS – SUMMARY OF PERFORMANCE

The Society has performed strongly in 2011, exceeding each of its key performance targets. Details of this performance are set out in the Chairman's Statement (pages 2 and 3), Chief Executive's Review (pages 5 to 9), Directors' Report (pages 12 to 19), with highlights also included on page 1.

This outstanding performance gave rise to a calculated bonus for all 1,749 eligible members of staff equivalent to 13% of base salary. The bonus percentage payable to each of the executive directors is the same as all other eligible staff.

2009-2011 LONG TERM INCENTIVE PLAN – SUMMARY OF PERFORMANCE

The Society has achieved outstanding results throughout the period of assessment, underpinning Coventry's pre-eminent position in the UK building society sector. The Society exceeded substantially each of the targets set in its plans for the period.

Further information in respect of this performance is provided in the Chairman's Statement (pages 2 and 3), Chief Executive's Review (pages 5 to 9) and Directors' Report (pages 12 to 19). Highlights are also included on page 4.

The Remuneration Committee considers that Coventry's performance, during a period of continued economic uncertainty which has resulted in significant challenges for all financial institutions, compares favourably with that of all major banks and building societies.

Taking into account both overall performance and that against the specific 2009 LTIP targets, the Remuneration Committee approved a payment for each participant equivalent to 15% of base salary at 1 January 2009.

DIRECTORS' REMUNERATION REPORT
(continued)

The remuneration relevant to Code Staff, comprising senior management and other material risk takers was as follows for 2011 and 2010:

Aggregate remuneration data for Jan-Dec 2011

	Number of staff	**Fixed pay[3] £m**	**Variable pay[4] £m**
Senior managers[1]	**23**	**2.9**	**0.5**
Other material risk takers[2]	**14**	**0.9**	**0.1**
Total	**37**	**3.8**	**0.6**

1. Non-executive directors, executive directors and senior managers including Stroud & Swindon executives for period January to May 2011. Non-executive directors' fees are included under fixed pay; no variable pay is awarded to non-executive directors.
2. Other Code Staff to cover those whose actions have a material impact on the risk profile of the Society, including Stroud & Swindon Code Staff.
3. Fixed pay includes basic pay, allowances and employer pension contributions.
4. Variable pay includes the annual performance related bonus (£0.3m) for 2011 (paid March 2012) and the LTIP 2011-2013 payment granted (not paid) in 2011 (£0.3m). The LTIP payment included above is the maximum possible under the scheme (40% executive directors and 20% senior managers of salary as at the Grant Date); the actual payment will be subject to the performance criteria outlined on page 34.

Aggregate remuneration data for Jan-Dec 2010

	Number of staff	Fixed pay[3] £m	Variable pay[4] £m
Senior managers[1]	20	2.3	0.5
Other material risk takers[2]	13	0.7	0.1
Total	33	3.0	0.6

1. Non-executive directors, executive directors and senior managers including Stroud & Swindon executives for period September to December 2010. Non-executive directors' fees are included under fixed pay; no variable pay is awarded to non-executive directors.
2. Other Code Staff to cover those whose actions have a material impact on the risk profile of the Society, including Stroud & Swindon Code Staff for period September to December 2010.
3. Fixed pay includes basic pay, allowances and employer pension contributions.
4. Variable pay includes the annual performance related bonus (£0.3m) for 2010 (paid March 2011) and the LTIP 2010-2012 payment granted (not paid) in 2010 (£0.3m). The LTIP payment included above is the maximum possible under the scheme (40% of salary as at the Grant Date); the actual payment will be subject to the performance criteria outlined on page 34.

On behalf of the Board

Bridget Blow
Chairman of the Remuneration Committee

29 February 2012

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The following statement, which should be read in conjunction with the statement of the auditors' responsibilities on page 38, is made by the directors to explain their responsibilities in relation to the preparation of the Annual Accounts, Annual Business Statement and Directors' Report.

The directors are responsible for preparing the Annual Report, Annual Business Statement, Directors' Report and the Annual Accounts in accordance with applicable law and regulations.

The Building Societies Act 1986 (the Act) requires the directors to prepare Group and Society Annual Accounts for each financial year. Under that law they are required to prepare the Group Annual Accounts in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and applicable law and have elected to prepare the Society Accounts on the same basis.

The Group and Society Annual Accounts are required by law and IFRS as adopted by the EU to present fairly the financial position and the performance of the Group and the Society; the Building Societies Act 1986 provides in relation to such Annual Accounts that references in the relevant part of that Act to Annual Accounts giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and Society Annual Accounts, the directors are required to:

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the Annual Accounts on the going concern basis, unless it is inappropriate to presume that the Group and Society will continue in business.

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

The directors are responsible for ensuring that the Group:

- keeps proper accounting records that disclose with reasonable accuracy at any time the financial position of the Group and Society, in accordance with the Act; and
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business (in accordance with the rules made by the FSA under the Financial Services and Markets Act 2000).

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

The directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future. For this reason, the Annual Accounts continue to be prepared on the going concern basis.

INDEPENDENT AUDITORS' REPORT

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF COVENTRY BUILDING SOCIETY

We have audited the Group and Society financial statements of Coventry Building Society for the year ended 31 December 2011 which comprise the Group and Society Income Statements, Group and Society Statements of Comprehensive Income, Group and Society Statements of Financial Position, the Group and Society Statements of Changes in Members' Interests, the Group and Society Statements of Cash Flows and the related notes 1 to 42. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Society's members, as a body, in accordance with Section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITOR

As explained more fully in the Directors' Responsibilities Statement set out on page 37, the directors are responsible for the preparation of the financial statements which give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and Society's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

OPINION ON FINANCIAL STATEMENTS

In our opinion the financial statements:

- give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's and the Society's affairs as at 31 December 2011 and of the Group's and the Society's income and expenditure for the year then ended; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

OPINION ON OTHER MATTERS PRESCRIBED BY THE BUILDING SOCIETIES ACT 1986

In our opinion:

- the Annual Business Statement and the Directors' Report have been prepared in accordance with the requirements of the Building Societies Act 1986;
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the accounting records and the financial statements; and
- the information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given.

MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

We have nothing to report in respect of the following matters where the Building Societies Act 1986 requires us to report to you if, in our opinion:

- proper accounting records have not been kept by the Society; or
- the Society financial statements are not in agreement with the accounting records; or
- we have not received all the information and explanations and access to documents we require for our audit.

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

29 February 2012

INCOME STATEMENTS

for the year ended 31 December 2011

	Notes	Group 2011 £m	Society 2011 £m	Group 2010 £m	Society 2010 £m
Interest receivable and similar income	3	**730.0**	**808.1**	599.5	678.0
Interest payable and similar charges	4	**(562.5)**	**(676.8)**	(453.5)	(557.3)
Net interest income		**167.5**	**131.3**	146.0	120.7
Fees and commissions receivable	5	**15.0**	**14.0**	15.9	15.1
Fees and commissions payable	6	**(1.9)**	**(1.8)**	(1.5)	(1.4)
Other operating income	7	**0.9**	**0.7**	0.6	0.5
Net gains/(losses) from derivative financial instruments	8	**0.5**	**0.5**	(0.7)	(0.7)
Total income		**182.0**	**144.7**	160.3	134.2
Administrative expenses	9	**(78.9)**	**(76.0)**	(68.0)	(65.6)
Amortisation of intangible assets	23	**(3.5)**	**(3.5)**	(3.0)	(3.0)
Depreciation of tangible fixed assets	24,25	**(5.1)**	**(5.0)**	(4.3)	(4.3)
Operating profit before impairments and exceptional items		**94.5**	**60.2**	85.0	61.3
Impairment losses on loans and advances to customers	13	**(9.9)**	**(6.3)**	(11.8)	(8.9)
Release of provision for impairment of debt securities	14	**-**	**-**	2.1	2.1
Operating profit after impairments and before exceptional items		**84.6**	**53.9**	75.3	54.5
Provision for FSCS levies	15,35	**(13.4)**	**(13.4)**	(5.6)	(5.6)
Integration and merger related costs		**(10.7)**	**(10.7)**	(11.2)	(11.2)
Operating profit after impairments and exceptional items		**60.5**	**29.8**	58.5	37.7
Gain on business combination		**-**	**-**	43.8	70.7
Charitable donation to Poppy Appeal	16	**(1.0)**	**(1.0)**	(1.7)	(1.7)
Profit before tax		**59.5**	**28.8**	100.6	106.7
Taxation	17	**(12.9)**	**(5.0)**	(15.7)	(10.0)
Profit for the financial year		**46.6**	**23.8**	84.9	96.7

Profit for the financial year arises from continuing operations and is attributable to the members of the Society.

STATEMENTS OF COMPREHENSIVE INCOME

for the year ended 31 December 2011

	Notes	Group 2011 £m	Society 2011 £m	Group 2010 £m	Society 2010 £m
Profit for the financial year		**46.6**	**23.8**	84.9	96.7
Other comprehensive income					
Actuarial (loss)/gain on retirement benefit obligation:					
Actuarial (loss)/gain on defined benefit pension plan	12	**(4.3)**	**(4.3)**	5.0	5.0
Tax credit/(charge) on actuarial loss/gain on defined benefit pension plan	12,17	**1.1**	**1.1**	(1.4)	(1.4)
Available-for-sale investments:					
Fair value movements on Available-for-sale assets taken to reserves		**177.0**	**177.0**	52.1	52.1
Amount transferred to income statement[1]		**(157.4)**	**(157.4)**	(33.1)	(33.1)
Tax charge on fair value movements	17	**(5.2)**	**(5.2)**	(5.3)	(5.3)
Other comprehensive income for the year, net of tax		**11.2**	**11.2**	17.3	17.3
Total comprehensive income for the year, net of tax		**57.8**	**35.0**	102.2	114.0

The accounting policies and notes on pages 44 to 89 form part of these Accounts.

[1] Where a hedging relationship exists, this amount is transferred to 'Net gains/(losses) from derivative financial instruments', with other amounts being recognised within 'Interest receivable and similar income'.

STATEMENTS OF FINANCIAL POSITION

as at 31 December 2011

	Notes	Group 2011	Society 2011	Group 2010	Society 2010
		£m	£m	£m	£m
Assets					
Cash in hand and balances with the Bank of England	18	1,607.0	1,600.1	1,444.2	1,443.8
Loans and advances to credit institutions	19	388.3	319.3	193.4	193.4
Debt securities	20	2,846.3	2,846.3	2,864.0	2,864.0
Other liquid assets		0.5	0.5	30.3	30.3
		4,842.1	4,766.2	4,531.9	4,531.5
Non-current assets held for sale	26	2.5	2.5	3.9	3.9
Loans and advances to customers	21	19,240.0	14,023.0	17,573.7	13,523.7
Hedge accounting adjustment		68.7	68.7	40.6	40.6
Derivative financial instruments	33	259.7	169.4	73.4	73.4
Investments in subsidiary undertakings	22	-	9,758.0	-	7,217.3
Intangible assets	23	9.5	9.5	12.2	12.2
Property, plant and equipment	24	32.8	32.8	28.1	28.1
Investment properties	25	5.7	0.6	5.8	0.6
Pension benefit surplus	12	3.9	3.9	7.2	7.2
Deferred tax assets	27	14.5	6.7	19.4	8.2
Prepayments and accrued income		7.2	6.8	6.1	5.7
Total assets		24,486.6	28,848.1	22,302.3	25,452.4
Liabilities					
Shares	28	18,964.1	18,964.1	17,634.3	17,634.3
Deposits from banks	29	510.9	510.9	1,315.4	1,315.4
Other deposits	30	23.0	23.0	34.1	34.1
Amounts owed to other customers	31	549.3	549.3	645.2	645.2
Debt securities in issue	32	2,863.8	2,863.8	1,533.3	1,533.3
Hedge accounting adjustment		201.5	148.4	21.3	21.3
Derivative financial instruments	33	336.0	299.8	139.4	139.4
Current tax liabilities		5.1	1.6	10.1	6.4
Deferred tax liabilities	27	3.0	3.0	5.6	5.6
Accruals and deferred income		16.1	13.2	12.1	9.7
Other liabilities	34	19.8	4,494.5	16.6	3,167.5
Provisions for liabilities and charges	35	20.3	20.3	15.9	15.9
Pension benefit obligations	12	-	-	3.1	3.1
Subordinated liabilities	36	68.2	68.2	68.2	68.2
Subscribed capital	37	161.3	161.3	161.3	161.3
Total liabilities		23,742.4	28,121.4	21,615.9	24,760.7
Equity					
General reserve		747.9	730.4	704.5	709.8
Available-for-sale reserve		(3.7)	(3.7)	(18.1)	(18.1)
Total liabilities and equity		24,486.6	28,848.1	22,302.3	25,452.4
Memorandum item					
Financial commitments	38	125.9	93.4	152.4	108.0

The accounting policies and notes on pages 44 to 89 form part of these Accounts.

Approved by the Board of directors on 29 February 2012.

David Harding
Chairman

David Stewart
Chief Executive

John Lowe
Finance Director

STATEMENTS OF CHANGES IN MEMBERS' INTERESTS

for the year ended 31 December 2011

Group	Notes	General reserve £m	Available-for-sale reserve £m	Total £m
As at 1 January 2011		**704.5**	**(18.1)**	**686.4**
Profit for the financial year		**46.6**	**-**	**46.6**
Actuarial loss on defined benefit pension plan (net of tax)	12,17	**(3.2)**	**-**	**(3.2)**
Net movement in Available-for-sale reserve (net of tax)		**-**	**14.4**	**14.4**
As at 31 December 2011		**747.9**	**(3.7)**	**744.2**
As at 1 January 2010		616.0	(31.8)	584.2
Profit for the financial year		84.9	-	84.9
Actuarial gain on defined benefit pension plans (net of tax)	12,17	3.6	-	3.6
Net movement in Available-for-sale reserve (net of tax)		-	13.7	13.7
As at 31 December 2010		704.5	(18.1)	686.4

Society	Notes	General reserve £m	Available-for-sale reserve £m	Total £m
As at 1 January 2011		**709.8**	**(18.1)**	**691.7**
Profit for the financial year		**23.8**	**-**	**23.8**
Actuarial loss on defined benefit pension plan (net of tax)	12,17	**(3.2)**	**-**	**(3.2)**
Net movement in Available-for-sale reserve (net of tax)		**-**	**14.4**	**14.4**
As at 31 December 2011		**730.4**	**(3.7)**	**726.7**
As at 1 January 2010		609.5	(31.8)	577.7
Profit for the financial year		96.7	-	96.7
Actuarial gain on defined benefit pension plans (net of tax)	12,17	3.6	-	3.6
Net movement in Available-for-sale reserve (net of tax)		-	13.7	13.7
As at 31 December 2010		709.8	(18.1)	691.7

The accounting policies and notes on pages 44 to 89 form part of these Accounts.

STATEMENTS OF CASH FLOWS

for the year ended 31 December 2011

	Notes	Group 2011 £m	Society 2011 £m	Group 2010 £m	Society 2010 £m
Cash flows from operating activities					
Profit before tax		**59.5**	**28.8**	100.6	106.7
Adjustments for:					
Non-cash items included in profit before tax	42	**59.8**	**57.1**	(5.0)	(29.8)
Changes in operating assets	42	**(1,565.8)**	**(395.2)**	(1,235.6)	(407.9)
Changes in operating liabilities	42	**472.2**	**476.4**	1,545.7	1,546.6
Interest paid on subordinated liabilities		**(5.1)**	**(5.1)**	(3.9)	(3.9)
Interest paid on subscribed capital		**(12.2)**	**(12.2)**	(12.3)	(12.3)
Taxation		**(19.7)**	**(19.7)**	(7.1)	(7.1)
Net cash flows from operating activities		**(1,011.3)**	**130.1**	382.4	1,192.3
Cash flows from investing activities					
Purchase of investment securities		**(7,276.7)**	**(7,276.7)**	(5,687.0)	(5,687.0)
Sale and maturity of investment securities		**7,468.8**	**7,468.8**	6,796.2	6,796.2
Purchase of property, plant and equipment		**(8.8)**	**(8.8)**	(5.6)	(5.6)
Purchase of intangible assets		**(3.1)**	**(3.1)**	(3.1)	(3.1)
Cash and cash equivalents acquired on transfer of engagements		**-**	**-**	10.8	9.7
Net cash flows from investing activities		**180.2**	**180.2**	1,111.3	1,110.2
Cash flows from financing activities					
Loans from connected undertakings		**-**	**1,323.8**	-	508.6
Loans to connected undertakings		**-**	**(2,540.7)**	-	(1,315.6)
Repurchase of subordinated liabilities		**-**	**-**	(55.0)	(55.0)
Repurchase of debt securities		**(45.0)**	**(45.0)**	(629.0)	(629.0)
Issue of debt securities		**1,316.5**	**1,316.5**	400.0	400.0
Net cash flows from financing activities		**1,271.5**	**54.6**	(284.0)	(1,091.0)
Net increase in cash		**440.4**	**364.9**	1,209.7	1,211.5
Cash and cash equivalents at start of year		**1,537.8**	**1,537.4**	328.1	325.9
Cash and cash equivalents at end of year	42	**1,978.2**	**1,902.3**	1,537.8	1,537.4

The accounting policies and notes on pages 44 to 89 form part of these Accounts.

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES

The following accounting policies have been applied consistently in dealing with items that were considered material in relation to the Accounts.

BASIS OF PREPARATION

These Accounts have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU; interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC); and with those parts of the Building Societies (Accounts and Related Provisions) Regulations 1998 applicable to organisations reporting under IFRS.

The Accounts have been prepared on an historical cost basis, as modified by the revaluation of Available-for-sale debt securities and certain financial instruments which are measured at fair value. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges and are otherwise carried at cost are adjusted to record changes in the fair values attributable to the risks that are being hedged. These hedge accounting adjustments are recorded in the statement of financial position.

BUSINESS COMBINATIONS

The Society merged with Stroud & Swindon Building Society on 1 September 2010. This business combination has been accounted for using the acquisition method, following the requirements of IFRS 3 (Revised) 'Business Combinations' which was endorsed by the EU in June 2009. Results relating to the merger with Stroud & Swindon Building Society are included within the Society's results effective from the date of completion of the merger, 1 September 2010.

CHANGES IN ACCOUNTING POLICY

The following standards and interpretations, relevant to the Group have been adopted during the year:

IFRS 7 *Financial Instruments: Disclosures (Amendment)*

The amendments to IFRS 7 is effective for annual periods beginning on or after 1 January 2011. These amendments require additional disclosure in relation to concentrations of risk and on the effect of collateral held as security on the maximum credit risk exposure (see note 40).

IAS 24 *Related Party Disclosures (Amendment)*

The amended standard became effective for annual periods beginning on or after 1 January 2011. It clarifies the definition of a related party to simplify the identification of such relationships and to eliminate inconsistencies in its application. The revised standard introduced a partial exemption of disclosure requirements for government-related entities. The amendment does not have a significant impact on the financial statements of the Group.

IFRIC 14 *Prepayments of a minimum funding requirement (Amendment)*

The amendment to IFRIC 14 is effective for annual periods beginning on or after 1 January 2011 with retrospective application. The amendment provides guidance on assessing the recoverable amount of a net pension asset. The amendment permits an entity to treat the prepayment of a minimum funding requirement as an asset. The amendment does not have a significant impact on the financial statements of the Group.

Improvements to IFRSs

Improvements to IFRSs was issued in May 2010, containing several small amendments to its existing standards. The Group has considered the impact of these improvements and has made adjustments to the disclosure in the financial statements.

FUTURE ACCOUNTING DEVELOPMENTS

The following standards and interpretations, relevant to the Group, were not effective at 31 December 2011 and have not been applied in preparing these financial statements. The anticipated impact of these standards and interpretations are listed below:

IFRS 7 *Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities (Amendment)*

The amendments to IFRS 7 shall be effective for annual periods beginning on or after 1 January 2013. The amendment requires new disclosures for all recognised financial instruments that are set-off in the statement of financial position. Financial instruments on the Group's statement of financial position are shown as gross amounts before set-off. The Group does not expect any significant impact on the financial position or performance.

IFRS 9 *Financial Instruments: Classification and Measurement*

IFRS 9 as issued, reflects the first phase of the International Accounting Standards Board's (IASB) work on the replacement of IAS 39 *Financial Instruments: Recognition and measurement* and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard is effective for annual periods beginning on or after 1 January 2015.

In subsequent phases, the Board will address hedge accounting and impairment. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets and financial liabilities. However, the Group has determined that the effect will be quantified in conjunction with the other phases when issued, to present a comprehensive picture.

IFRS 10 *Consolidated Financial Statements*

IFRS 10 reflects the requirements for determining when a reporting entity controls another entity, and the principles applied when preparing consolidated financial statements replacing IAS 27 *Consolidated and Separate Financial Statements* and SIC 12 *Consolidation – Special Purpose Entities*. The standard is effective for annual periods on or after 1 January 2013. Due to the simple structure of the Group and its subsidiaries, the Group does not expect the adoption of IFRS 10 to have a significant effect on the entities that are consolidated within the Group.

IFRS 11 *Joint Arrangements*

IFRS 11 defines the joint arrangements with joint control, and reflects the principles applied when preparing consolidated financial statements replacing IAS 31 *Interest in Joint Ventures* and SIC 13 *Jointly-controlled Entities – Non-monetary Contributions by Venturers*. The standard is effective for annual periods on or after 1 January 2013. The adoption of IFRS 11 is not expected to have an effect on the profit and reserves of the Group as it does not have a joint control arrangement.

IFRS 12 *Disclosure of Interests in Other Entities*

IFRS 12 includes all the disclosure requirements for subsidiaries, joint arrangements, associates and structured entities. The standard is effective for annual periods on or after 1 January 2013. IFRS 12 is a disclosures-only standard and therefore will have no effect on profit or loss, or the reserves of the Group.

IFRS 13 *Fair Value Measurement*

IFRS 13 provides guidance on how to measure the fair value of financial and non-financial assets and liabilities when required or permitted by IFRS. The standard is effective for annual periods on or after 1 January 2013. The adoption of IFRS 13 is not expected to significantly affect the fair value of certain assets and liabilities held by the Group, as the valuation methods adopted by the Group are in line with the principles identified in this new standard.

IAS 1 *Presentation of Financial Statements (Amendment)*

The amendments to IAS 1 require changes to the presentation of the statement of comprehensive income. Items that could be reclassified to profit or loss at a future point in time would be presented separately from items that will never be reclassified. The effective date of the standard is 1 January 2013. The adoption of these amendments will only affect the presentation of the statement of comprehensive income.

IAS 12 *Income Taxes (Amendments)*

The effective date of the amendments is for years beginning 1 January 2012. The amendments to IAS 12 require an entity to measure deferred tax relating to an asset depending on whether the entity expects to recover the carrying amount of the asset through use or sale. Where assets are measured at fair value, the amendment provides a practical solution to the problem by introducing a presumption that recovery of the carrying amount will, normally, be through sale. The Group's assets include intangible fixed assets and property, plant and equipment and are held with the intention of recovering profits through use, rather than the sale of the asset. As the Group adopts the amortised cost model, the Group does not expect the adoption of these amendments would affect its profit and reserves.

IAS 19 *Employee Benefits (Amendments)*

The amendments to IAS 19 remove the option to defer the recognition of actuarial gains and losses; the corridor approach. All changes in the value of defined benefit plans will be recognised in profit or loss and other comprehensive income. The effective date of the standard is 1 January 2013. As the Group recognises all actuarial gains and losses immediately, the removal of the corridor approach will have no impact on the results of the Group.

IAS 27 *Separate Financial Statement*

The IASB issued a revised standard to complement IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, and IFRS 12 *Disclosure of Interests in Other Entities*. The standard outlines the accounting and disclosure requirements for investments in subsidiaries, joint ventures, and associates when an entity prepares separate financial statements. The standard requires an entity preparing separate financial statements to account for those investments at cost or in accordance with IFRS 9 *Financial Instruments*. The standard is effective for annual periods beginning on or after 1 January 2013.

1. ACCOUNTING POLICIES (continued)

IAS 28 *Investments in Associates and Joint Ventures*
This standard prescribes the accounting for investments and associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. The standard is effective for annual periods beginning on or after 1 January 2013. The Group does not have associates or joint venture investments and therefore, no impact is anticipated from the adoption of this standard.

BASIS OF CONSOLIDATION
The Group Accounts consolidate the assets, liabilities and results of the Society and all its subsidiary companies.

The financial statements are presented in sterling millions (£m), and are rounded to the nearest hundred thousand except where otherwise indicated.

Subsidiaries are all entities, including special purpose entities, controlled by the Society. Control exists when the Society has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The Society's investment in its subsidiaries is recognised in the statement of financial position at cost. Intragroup transactions, balances and unrealised gains on transactions between Group companies are eliminated in the consolidated accounts.

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

In calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes the spread of various incentives, fees and charges, both paid and received by the Group, across the expected life of the loan account. Items spread in this way include:

- initial interest rate discounts;
- cash backs and other customer incentives; and
- certain fees and charges paid and received by the Group.

The purpose of using the effective interest rate method is to recognise interest income at a more level yield across the expected life of the product than would be obtained by recognising income as it is received.

Discounts received on loans and advances to customers which were acquired as a result of the merger, are recognised over the life of the asset, in line with the effective interest rate method and are recognised within interest receivable and similar income.

Interest income on Available-for-sale debt securities is included in interest receivable and similar income.

FEES AND COMMISSIONS
Fees and commissions receivable and payable that are not spread across expected asset lives under the effective interest rate method are taken to income on an accruals basis as services are provided, or on the completion of an act to which the fee relates.

SEGMENTAL REPORTING
The Group operates solely within the retail financial services sector and within the United Kingdom. As such, no detailed segmental analysis is required.

INTANGIBLE ASSETS
Intangible assets consist of software development costs and other intangible assets. Software development costs and purchased software that is not an integral part of a related hardware purchase are recognised as an intangible asset. Amortisation of such assets is charged to the income statement on a straight line basis over the useful life of the asset. The useful life of computer software is between three and eight years.

Other intangible assets arise from retail deposits acquired by the Group. These are amortised using the straight line method over the estimated useful life of 16 months. The amortisation period is reviewed annually. Other intangible assets were fully amortised as at 31 December 2011.

LEASES AND CONTRACT PURCHASE AGREEMENTS

The determination of whether an arrangement is, or contains, a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Where the Group enters into a lease that entails taking substantially all the risks and rewards of ownership of an asset, the agreement is treated as a finance lease. The asset is recorded in the balance sheet within property, plant and equipment and is depreciated over its estimated useful life. If there is no reasonable certainty that the Group will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the lease term and its useful life. Future instalments under such leases, net of finance charges, are included within creditors. Rentals payable are apportioned between the finance element, which is charged to the income statement at a constant annual rate, and the capital element which reduces the outstanding obligation for future instalments.

All other leases are accounted for as operating leases and payments are charged to administrative expenses on a straight line basis over the period of the lease. Rents receivable are credited to other operating income on a straight line basis over the period of the lease.

TAXATION INCLUDING DEFERRED TAX

Income tax on the profits for the year comprises current and deferred taxation.

Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates and laws that are enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements, with the exception that deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carried forward tax credits or tax losses can be utilised.

Deferred tax assets and liabilities are measured on a non-discounted basis at the tax rates that are expected to apply when the related asset is realised or liability settled, based on tax rates and laws enacted or substantively enacted by the balance sheet date.

Income tax is charged or credited directly to equity if it relates to items that are credited or charged to equity. Otherwise income tax is recognised in the income statement.

INVESTMENT PROPERTIES, PROPERTY, PLANT AND EQUIPMENT

Investment property is property held to earn rentals or for capital appreciation or for both, rather than for sale or use in the business. The Group recognises investment properties at cost less accumulated depreciation and any accumulated impairment. The carrying values of investment properties are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment. As permitted by IFRS 1 *First-time adoption of International Financial Reporting Standards,* the Group treated previous valuations of certain properties as the deemed cost of those properties on transition to IFRS. The carrying values of property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

An asset's carrying value is written down immediately to its recoverable amount if the asset's carrying value is greater than its estimated recoverable amount.

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

Depreciation is provided on a straight line basis over the anticipated useful life of the asset as follows:

• Freehold buildings (including investment properties)	Over a period of 50 years
• Leasehold buildings	Shorter of remaining term of the lease and useful life
• Equipment, fixtures, fittings and vehicles	Three to eight years

1. ACCOUNTING POLICIES (continued)

NON-CURRENT ASSETS HELD FOR SALE

A non-current asset is classified as held for sale if the Group will recover the carrying amount principally through a sale transaction rather than through continuing use. A non-current asset classified as held for sale is measured at the lower of the carrying amount and fair value less costs to sell. If the asset is acquired as part of a business combination it is initially measured at fair value less costs to sell. Assets classified as held for sale are shown separately on the face of the statement of financial position.

FINANCIAL ASSETS

All financial assets are measured initially at their fair value plus transaction costs, except in the case of financial assets recorded at fair value through profit or loss. The Group classifies its financial assets at inception into the following categories:

- **Financial assets at fair value through profit or loss**

This category consists of derivative financial assets. Derivative financial assets are carried at fair value. The fair values are quoted market prices where there is an active market, or are based on valuation techniques where there is not.

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

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

- **Loans and receivables**

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

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

- **Available-for-sale**

Available-for-sale assets are non-derivative financial assets that are designated as such or not classified into either of the two categories above. Available-for-sale assets are initially measured at fair value. Subsequently, Available-for-sale assets are carried at fair value. The fair values, in the majority of cases, are based on quoted market prices or prices obtained from counterparties. In cases where quoted market prices are not available, discounted cash flow valuations are used.

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

Derecognition

Financial assets are derecognised when the rights to receive cash flows have expired or where substantially all of the risks and rewards of ownership have been transferred. In respect of the Group's secured funding structure, the Group sells to another entity, Coventry Building Society Covered Bonds LLP, the right to receive the cash flows arising on the loans which have been transferred. However, other than in a default or insolvency scenario, the Society receives substantially all of the profit of that entity, and hence retains substantially all of the risks and rewards of the transferred loans. Therefore the transferred loans are retained on the Society's balance sheet.

Hedging

The impact of hedging on the measurement of financial assets is detailed in the derivatives (page 49) and hedge accounting (page 49) policy note.

FINANCIAL LIABILITIES

Financial liabilities incorporates shares, bank and other deposits, amounts owed to other customers, debt securities in issue, derivative financial liabilities, subordinated liabilities and subscribed capital. Financial liabilities are initially measured at fair value plus transaction costs directly attributable to the acquisition or issue.

Financial liabilities (other than derivatives) are subsequently measured at amortised cost, adjusted for the amortisation of any transaction costs, premiums and discounts. The amortisation is recognised in interest payable and similar charges using the effective interest rate method. Derivatives are measured at fair value through profit or loss.

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

Financial liabilities are derecognised when the obligation is discharged, cancelled or has expired. Financial liabilities that are designated as hedged items are subject to measurement under the hedge accounting requirements. The impact of hedging on the measurement of financial liabilities is detailed in the derivatives (see below) and hedge accounting (see below) policy note.

IMPAIRMENT OF LOANS AND ADVANCES TO CUSTOMERS

The Group assesses its loans and advances to customers for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event (or events) that has occurred after initial recognition and before the balance sheet date and has a reliably measurable impact on the estimated future cash flows of the loan amount.

Impairment is categorised as either individual impairment (where individual assets have been assessed for loss) or collective impairment (where losses are assessed as being present in a portfolio of loans, but they cannot be attributed to individual accounts). As well as loans that are individually or collectively identified as being impaired, recognition is also made of accounts where forbearance has been exercised and agreement has been reached with customers in financial difficulty to temporarily forego some element of the payment due.

If there is objective evidence that an impairment loss on loans and advances to customers has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred). The carrying amount of the asset is reduced through the use of an impairment provision and the amount of the loss is recognised in the income statement.

When a loan is not collectable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recorded in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the customer's credit rating), the previously recognised impairment loss is reversed by adjusting the impairment provision. The amount of the reversal is recognised in the income statement.

SALE AND REPURCHASE AGREEMENTS

Securities lent or sold subject to a commitment to repurchase them (a 'repo') are retained on the balance sheet when substantially all the risks and rewards of ownership remain within the Group. The counterparty liability is included separately in the balance sheet, as appropriate. The difference between the sale and repurchase price is accrued over the life of the agreements using the effective interest rate method.

DERIVATIVE FINANCIAL INSTRUMENTS

The Group holds derivative financial instruments for the purposes of managing the risks associated with its various fixed and capped rate assets, its fixed rate liabilities and its foreign currency transactions. In accordance with legislation and its treasury policy, the Group holds derivative financial instruments only for risk management and not for speculative or trading purposes.

All derivative financial instruments are stated in the Accounts at fair value, with movements in fair value taken through the income statement under 'net (losses)/gains from derivative financial instruments' in the period in which the movement occurred. Fair values are calculated by discounted cash flow models using yield curves that are based on observable market data or are based on valuations from counterparties.

HEDGE ACCOUNTING

All derivatives entered into by the Group are for the purpose of providing an economic hedge. Full details of hedging activities are contained in note 33. Hedge accounting is an optional treatment, subject to the satisfaction of specific rules and conditions set out in IAS 39. The Group periodically tests hedge effectiveness and applies fair value hedge accounting, so that changes in the fair value of the underlying asset or liability that are attributable to the hedged risk are recorded in the income statement to offset the fair value movement of the related derivative.

NOTES TO THE ACCOUNTS
(continued)

1. ACCOUNTING POLICIES (continued)

The Group uses derivative financial instruments to mitigate the interest rate risk and foreign currency risk that arises from the Group's lending and funding activities. The Group elects to treat all such derivatives, as fair value hedges and adopting the fair value hedge accounting provisions of IAS 39. This treatment is consistent with the economic purpose of using the derivative instruments, which is to provide a hedge against the movement in the fair value of fixed rate and foreign currency assets and liabilities. The Group recognises movements on the balance sheet in respect of the hedged portion of the fair values of the underlying assets and liabilities that should materially offset the volatility that may arise from recognising the fair value movements of the derivatives themselves.

PENSION COSTS

The Group operates a defined benefit pension scheme and a defined contribution scheme for members of staff.

Contributions to the defined contribution pension schemes are recognised as an expense in the income statement as incurred, on an accruals basis.

The Group's net obligation under the defined benefit pension scheme is assessed annually by an independent qualified actuary. The net obligation is calculated as the difference between the fair value of the scheme's assets and the amount of future entitlements earned by scheme members from service in the current and prior periods, discounted back to present values using a rate based on an index of long-dated AA rated corporate bonds. This calculation allows the net obligations of the scheme to be expressed as either a surplus or deficit, which is recognised as respectively either an asset or liability in the Group's Accounts at the balance sheet date.

Pension costs for service in the period are assessed in accordance with advice from a qualified actuary and are recognised in the income statement. Pension fund actuarial gains or losses are recognised in full in the year they occur in the statement of comprehensive income.

FOREIGN CURRENCY TRANSLATION

The consolidated financial statements are presented in sterling, which is the functional currency of the Group.

Foreign currency transactions are translated into sterling using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are retranslated at the rate prevailing at the year end. Foreign exchange gains and losses resulting from the retranslation and settlement of these items are recognised in the income statement.

LIQUID ASSETS

Liquid assets consist of cash in hand and balances with the Bank of England, loans and advances to credit institutions, debt securities and other liquid assets. Other liquid assets consists of amounts advanced to other non-credit institutions.

The Group uses various debt securities (certificates of deposit, gilts, etc) to maintain its liquidity position. These debt securities are classified as Available-for-sale under the terms of IAS 39 and, as such, are recorded in the Accounts at fair value, with changes in fair value taken to the Available-for-sale reserve within equity reserves.

If debt securities are sold, the gain or loss on sale is measured as the difference between sale proceeds and original cost (net of any discount or premium on acquisition). Any fair value adjustments already recognised are released from reserves at the time of the sale and offset against the gain or loss.

When a decline in the fair value of an Available-for-sale financial asset has been recognised directly in equity reserves and there is objective evidence that the asset is impaired, the cumulative loss recognised in equity reserves is removed and recognised in the income statement.

CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash and non-restricted balances with central banks and loans and advances to credit institutions.

PROVISIONS AND CONTINGENT LIABILITIES

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

Contingent liabilities are potential obligations from past events which shall be confirmed by future events. Contingent liabilities are not recognised within the balance sheet.

EXCEPTIONAL ITEMS

Exceptional items are items of income and expenditure that are disclosed separately on the basis that they are material, either by their nature or their size, to the understanding of the Group's financial performance, and they significantly distort the comparability of financial performance between periods. This primarily consists of costs incurred during 2010 and 2011, relating directly to the merger with Stroud & Swindon Building Society, which comprise of deal costs, integration costs, and overhead costs which do not form part of the long-term ongoing business.

'Gain on business combination' has been recognised below 'Operating profit after impairments and exceptional items', as the gain does not form part of operating activities.

2. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

JUDGEMENTS

In the process of applying the Group's accounting policies, the directors have made the following judgements and estimates that have the most significant effect on the amounts recognised in the financial statements.

Debt securities

The Group maintains a portfolio of liquid assets to ensure it has sufficient funds available to meet its financial commitments as they fall due. A large part of this portfolio is made up of debt securities, for which there are various accounting treatments permitted under IAS 39. The Group has adopted the 'Available-for-sale' treatment as this most closely matches the way debt securities are used within the business, with a portfolio of assets maintained for continuing use, and individual assets available to be sold depending on particular requirements for funding or the maintenance of interest yields. This treatment requires that debt securities are recognised at fair value with movements in fair value taken to equity reserves.

The determination of whether Available-for-sale instruments are impaired is assessed based on similar criteria to financial assets carried at amortised cost.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using interest rate yield curves and other relevant market data. These are judged to be the most appropriate valuation inputs. The valuation of financial instruments, and the associated inputs are disclosed in more detail in note 40.

Deferred tax

The Group recognises deferred tax on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available to utilise the asset. The Group considers that sufficient future taxable profit will, in fact, be available to utilise all the Group's deferred tax assets and the Group has therefore recognised deferred tax assets where they have arisen.

Pension schemes

The Group's defined contribution and defined benefit pension schemes are accounted for under the terms of IAS 19. The standard requires the calculation of the net assets or liabilities of the defined benefit scheme and their inclusion in the statement of financial position. The result is dependent in part on the interest rate used to discount scheme liabilities back to present value. IAS 19 requires that this should equate to a rate available on an AA rated corporate bond. In practice, the rates available on such bonds cover a wide range and there is therefore a range of possible outcomes that could be disclosed as the pension scheme's net position. In order to avoid this uncertainty, the directors have selected a rate from within a narrow range recommended by the Group's professional pension scheme advisors. This range has been based on an index of related corporate bond yields. The impact of a 0.1% decrease in the rate used to discount the future value of the benefit obligation would be to increase the present value of the liability by £3.2 million. The impact of increasing life expectancy by an additional year, increases the present value of the scheme liability by £3.1 million.

ESTIMATION UNCERTAINTY

The key assumptions regarding the future and other key sources of estimation uncertainty at the balance sheet date that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below.

2. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Loan impairment and other provisions

IAS 39 requires that loan losses are only recognised where there is objective evidence of impairment. The Group has applied this requirement in determining the level of losses present in its loans and advances to customers, but has been required to apply management judgement in determining the financial impact of this impairment. IAS 39 makes a distinction between individual and collective impairment. Individual impairment relates to situations where individual assets are assessed for loss. The Group has used this approach on loans in possession and those in arrears. Estimates that have been applied include, assessing the likelihood of the loan going into possession for those cases currently in arrears, the length of time expected to be required to complete the sale of properties in possession, and the expected costs of realisation. Collective impairment relates to cases where losses are assessed as being present in a loan portfolio, but they cannot be identified to individual accounts. This approach has been used to calculate a value of incurred but not reported losses, where statistical analysis has been used to determine a value for losses where a loss event has already impacted an account, but has not yet manifested itself in arrears data. A portfolio approach is also used on sections of the loan book where there are known problems but individual accounts are again as yet not identifiable. This method has been applied to loans advanced on city centre buy-to-let flats where a problem of oversupply is having a negative effect on prices and ease of sale, with the result that the Group has made an impairment provision against these assets. If future house price movements differ from expectations by 5% (of the expected movement), the impact on the impairment provision would be £0.1 million.

Estimated asset lives

The Group recognises interest on loans and advances to customers on the basis of their effective interest rate. This is a constant rate that averages out the effect of incentives and fees across the expected life of the loan account. A critical assumption in the calculation is the expected life, as this determines the assumed period over which customers may be paying various differentiated interest rates. The calculation of the effective interest rate uses assumptions on expected life that are based on the historic experience of similar products. These assumptions are monitored to ensure their ongoing appropriateness. Changes in the amortised cost balance arising from actual product life experience differing from the assumed life, are periodically calculated and an adjustment made to the loan balance, with a corresponding adjustment to interest income. An increase in the assumption of expected life of 1% would result in an increase to loans and advances to customers of £2.3 million. Also within the calculations, provision has been made for the uncertainty of the estimates in order to reduce the risk of overstatement of interest income.

Valuation of derivatives and Available-for-sale assets

The fair values of derivative financial instruments, Available-for-sale assets, and hedge items for hedge accounting purposes are based on open market prices, where available. If open market prices are not available, the Group uses valuation techniques which comprise discounted cash flow valuation models. The valuation of caps and floors also take account of the optionality within these instruments. The assumptions in these models are periodically reviewed to ensure that they remain relevant.

FSCS levy provision

The Society is committed to paying levy charges of the UK Financial Services Compensation Scheme (FSCS) (see note 15).

All deposit-taking institutions who are members of the FSCS are required to contribute to the administrative and capital costs of the FSCS in safeguarding the deposits of savers in failed financial institutions. The Society is, and continues to be, a member of the FSCS.

Contributions to the FSCS are calculated according to a prescribed formula using the retail savings balances of all deposit-taking institutions that are members of the FSCS. The provision for these costs in this year's Accounts relates to payments to be made in future periods. The actual payments to be made are subject to change because they are based on estimations of the repayments by failed institutions and future interest rates. The impact of a 50bp increase in the interest rate assumption would result in increasing the carrying value of the FSCS provision by approximately £2.2 million.

3. INTEREST RECEIVABLE AND SIMILAR INCOME

	Group 2011	**Society 2011**	Group 2010	Society 2010
	£m	**£m**	£m	£m
On loans fully secured on residential property	**730.5**	**501.7**	635.6	483.8
On other loans				
Connected undertakings	**-**	**230.9**	-	154.1
Other	**3.9**	**2.8**	5.2	3.8
	734.4	**735.4**	640.8	641.7
Interest and other income on debt securities	**77.7**	**77.7**	59.4	59.4
Interest and other income on other liquid assets	**5.8**	**5.5**	4.4	4.4
Net expense on hedging instruments	**(87.9)**	**(10.5)**	(105.1)	(27.5)
Total	**730.0**	**808.1**	599.5	678.0

Included within 'Interest receivable and similar income' is interest accrued of £8.3 million (2010: £8.7 million) for the Group and £5.8 million (2010: £6.3 million) for the Society on impaired financial assets.

The Group believes that interest receivable and similar income comprises revenue for the purposes of IAS 1.

4. INTEREST PAYABLE AND SIMILAR CHARGES

Bank and customer				
Subordinated liabilities	**5.1**	**5.1**	3.9	3.9
Other	**11.6**	**11.6**	21.4	21.4
Debt securities in issue	**95.5**	**74.1**	43.8	43.8
Other borrowed funds				
On shares held by individuals	**511.5**	**511.5**	423.1	423.1
On other shares	**0.1**	**0.1**	0.1	0.1
On subscribed capital	**12.2**	**12.2**	12.3	12.3
On loans from connected undertakings	**-**	**46.3**	-	26.2
Net (income)/expense from hedging instruments	**(73.5)**	**15.9**	(51.1)	26.5
Total	**562.5**	**676.8**	453.5	557.3

5. FEES AND COMMISSIONS RECEIVABLE

Mortgage related fees	**3.6**	**2.6**	3.3	2.5
General insurance fees	**6.0**	**6.0**	5.8	5.8
Other fees and commissions	**5.4**	**5.4**	6.8	6.8
Total	**15.0**	**14.0**	15.9	15.1

6. FEES AND COMMISSIONS PAYABLE

Funding related fees	**0.2**	**0.2**	0.6	0.6
Other fees and commissions	**1.7**	**1.6**	0.9	0.8
Total	**1.9**	**1.8**	1.5	1.4

7. OTHER OPERATING INCOME

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	**£m**	£m	£m
Rents receivable	**0.7**	**0.4**	0.4	0.3
Other	**0.2**	**0.3**	0.2	0.2
Total	**0.9**	**0.7**	0.6	0.5

8. NET GAINS/(LOSSES) FROM DERIVATIVE FINANCIAL INSTRUMENTS

	Group 2011	Society 2011	Group 2010	Society 2010
Gains less losses on derivatives:				
Derivatives designated as fair value hedges	**12.3**	**(40.9)**	27.8	27.8
Movement in fair value of hedged items attributable to hedged risk	**(11.6)**	**41.6**	(29.2)	(29.2)
	0.7	**0.7**	(1.4)	(1.4)
Other derivatives	**(0.2)**	**(0.2)**	0.7	0.7
Total	**0.5**	**0.5**	(0.7)	(0.7)

9. ADMINISTRATIVE EXPENSES

	Group 2011	Society 2011	Group 2010	Society 2010
Employee costs				
Wages and salaries	**42.4**	**42.4**	34.7	34.7
Social security costs	**4.2**	**4.2**	3.4	3.4
Pension costs				
Defined benefit plan (note 12)	**(0.3)**	**(0.3)**	1.2	1.2
Defined contribution plan	**0.8**	**0.8**	0.7	0.7
	47.1	**47.1**	40.0	40.0
Other expenses	**31.8**	**28.9**	28.0	25.6
Total	**78.9**	**76.0**	68.0	65.6

The remuneration of the auditors, Ernst & Young LLP, is set out below.

	Group 2011	Society 2011	Group 2010	Society 2010
Audit fees for the statutory audit	**0.2**	**0.2**	0.3	0.3
Fees payable for other services:				
Other services in relation to taxation	**0.3**	**0.3**	0.3	0.3
All other services	**0.2**	**0.2**	0.3	0.3
Total	**0.7**	**0.7**	0.9	0.9

The Group's policy in relation to the use of its auditors on non-audit engagements sets out the nature of services they are generally precluded from performing. Further details on the Society's policy is included within the Corporate Governance Report on pages 29 to 30. All non-audit engagements provided by the Group's auditors, are subject to pre-approval by either the Audit Committee or the Finance Director, depending upon the nature of the non-audit engagement.

10. STAFF NUMBERS

	2011	2011	2010	2010
Group and Society	**Full-time**	**Part-time**	Full-time	Part-time
The average number of persons employed during the year (including executive directors) was:				
Head office and administrative centres	**889**	**306**	741	262
Branches	**416**	**236**	341	219
Total	**1,305**	**542**	1,082	481

11. DIRECTORS' EMOLUMENTS

The emoluments of the Group's directors are listed below:

	Salary	Annual[1] bonus	Long Term[2] Incentive Plan	Pension[4] contributions	Increase in accrued pension	Taxable benefits	Total
Executive directors	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**	**£000**
2011							
David Stewart	**335**	**44**[3]	**44**[3]	**58**	**2**	**42**	**525**
John Lowe	**215**	**29**	**-**	**19**	**-**	**11**	**274**
Colin Franklin	**140**	**18**	**20**	**33**	**3**	**14**	**228**
Phil Vaughan (resigned 28.04.2011)	**93**	**-**	**-**	**8**	**-**	**7**	**108**
Total	**783**	**91**	**64**	**118**	**5**	**74**	**1,135**
2010							
David Stewart	314	35	44	78	1	15	487
John Lowe (appointed 14.10.2010)	39	20	-	2	-	3	64
Colin Franklin	136	15	18	31	12	16	228
Rob Green (resigned 14.10.2010)	204	-	-	19	-	19	242
Phil Vaughan	193	21	28	19	-	14	275
Total	886	91	90	149	13	67	1,296

1. The performance of the Society during 2011 gave rise to a payment for all 1,749 eligible members of Coventry staff (2010: 1,501), including executive directors, equivalent to 13% (2010: 11%) of basic salary.
2. Payments made under the Long Term Incentive Plan are in relation to the performance of the three financial years 2009, 2010 and 2011. The Remuneration Committee approved a payment of 15% (2010: 15%) of base salary at 1 January 2009 (2010: 1 January 2008) to participants in the scheme at that date, reflecting the Group's performance over this period.
3. David Stewart, elected to waive £38,000 of his payments in order to help support students from disadvantaged backgrounds to study at Warwick University. Total remuneration accepted was £487,000, unchanged from 2010.
4. David Stewart and John Lowe are active members of the Group's funded defined contribution pension scheme.

NOTES TO THE ACCOUNTS
(continued)

11. DIRECTORS' EMOLUMENTS (continued)

DEFINED BENEFIT SCHEME

Pension benefits earned by directors

	Director's contribution	Accrued pension per annum at 31.12.2011	Transfer value of accrued benefits 31.12.2010	Transfer value of accrued benefits 31.12.2011	Difference in transfer value less contributions
	£000	**£000**	**£000**	**£000**	**£000**
David Stewart[1]	**-**	**41**	**600**	**828**	**228**
Colin Franklin	**11**	**55**	**1,114**	**1,442**	**317**

1. David Stewart is also a deferred member of the Group's contributory final salary pension scheme, having left the final salary pension scheme immediately before being appointed Chief Executive in July 2006.

Details of the executive directors' service contracts are contained in section 3 of the Annual Business Statement.

	2011	2010
Non-executive directors	**£000**	£000
David Harding (Chairman)	**78**	77
Bridget Blow (Deputy Chairman, Senior Independent Director and Chair of the Remuneration Committee)	**50**	50
Roger Burnell	**40**	39
Ian Geden	**40**	39
Ian Pickering (Chair of the Board Risk Committee)	**50**	50
Fiona Smith	**40**	39
Glyn Smith (appointed 22.09.2010) (Chair of the Audit Committee appointed 01.12.2011)	**41**	11
Total	**339**	305

No pension contributions were made for non-executive directors.

12. PENSION SCHEME

The Group operates a funded defined benefit scheme and a funded defined contribution pension scheme for employees and executive directors. The Coventry defined benefit scheme has been closed to new members since December 2001. The defined benefit scheme provide benefits based on final pensionable salary with assets held in separate trustee-administered funds.

On 31 December 2011, the Coventry Building Society Superannuation Fund merged with Stroud & Swindon Building Society Retirement Benefit Plan. As at the 31 December 2010, the two defined benefit schemes were shown separately on the balance sheet. The Coventry Building Society Superannuation Fund was presented as a defined benefit surplus totalling £7.2 million as at 31 December 2010, and the Stroud & Swindon Building Society Retirement Benefit Plan was presented as a defined benefit obligation of £3.1 million.

12. PENSION SCHEME (continued)

The cost of a defined benefit scheme is assessed in accordance with the advice of a qualified actuary on the basis of valuations using the projected unit method. The main assumptions used in the valuations were:

i) an investment return pre-retirement of 0.8% (2010: 1.2%) per annum in excess of projected salary increases;

ii) for the Coventry Building Society Superannuation Fund an investment return post-retirement of 1.8% (2010: 2.1%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued prior to 6 April 2006 and 2.6% (2010: 3.1%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued after 6 April 2006; and

iii) for the Stroud & Swindon Building Society Retirement Benefit Plan, an investment return post-retirement of 1.8% (2010: 2.5%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued prior to 6 April 1997, 1.3% (2010: 1.8%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued from 6 April 1997 to 31 July 2002, 1.8% (2010: 2.1%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued from 1 August 2002 to 5 April 2006 and 2.6% (2010: 3.1%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued after 6 April 2006.

The Group contributed 24.5% (2010: 24.5%) of members' pensionable salaries over the year to 31 December 2011 into the Coventry Building Society Staff Superannuation Fund. The Group also contributed 28.9% (2010: 28.9%) of members' pensionable salaries until July 2011, and then contributed 25.3% for the remainder of the year to 31 December 2011 into the Stroud & Swindon Building Society Retirement Benefit Plan. During 2011, contributions into the merged Coventry Building Society Staff Superannuation Fund totalled £3.8 million. The Group estimates its contribution into the merged fund for the following 12 months to be £3.6 million.

	2011	2010
Group and Society	**£m**	£m
Present value of funded obligations	**(142.9)**	(133.8)
Fair value of plan assets	**146.8**	137.9
Funded status/Pension benefit surplus	**3.9**	4.1
The amounts recognised in the income statement		
Current service cost	**2.1**	1.8
Interest cost on benefit obligations	**7.0**	5.9
Expected return on plan assets	**(8.2)**	(6.5)
Gains on curtailment	**(1.2)**	-
Total (credit)/charge within administrative expenses	**(0.3)**	1.2
Actual return on plan assets	**7.8**	11.4
Changes in the present value of the defined benefit obligations		
Defined benefit obligation at 1 January	**133.8**	89.0
Acquired on transfer of engagements	**-**	38.9
Gains on curtailment	**(1.2)**	-
Current service cost	**2.1**	1.8
Interest cost	**7.0**	5.9
Employee contributions	**0.7**	0.7
Actuarial losses/(gains)	**3.9**	(0.2)
Benefits paid	**(3.4)**	(2.3)
Defined benefit obligation at 31 December	**142.9**	133.8

12. PENSION SCHEME (continued)

	2011	2010
Group and Society	**£m**	£m
Changes in the fair value of plan assets		
Fair value of plan assets at 1 January	**137.9**	95.9
Acquired on transfer of engagements	**-**	30.1
Expected return on plan assets	**8.2**	6.5
Actuarial (losses)/gains	**(0.4)**	4.8
Contributions by employer	**3.8**	2.2
Employee contributions	**0.7**	0.7
Benefits paid	**(3.4)**	(2.3)
Fair value of plan assets at 31 December	**146.8**	137.9
The amount recognised in the statements of other comprehensive income		
Actuarial (loss)/gain	**(4.3)**	5.0
Tax credit/(charge) on actuarial loss/gain at 25% (2010: 27%)	**1.1**	(1.4)
Actuarial (loss)/gain net of tax	**(3.2)**	3.6

As a result of the merger with Stroud & Swindon Building Society, a curtailment gain of £1.2 million was recognised during the year.

The major categories of plan assets as a percentage of the fair value of total plan assets, and their expected rates of return are:

	Expected return at balance sheet date	Plan assets at 31.12.2011	Expected return at balance sheet date	Plan assets at 31.12.2010
	%	**%**	%	%
Equities	**7.2**	**19**	8.2	25
Corporate bonds	**4.8**	**20**	5.5	20
Government bonds	**3.2**	**33**	4.2	21
Alternatives	**4.9**	**28**	5.7	34
		100		100

At 31 December 2011, the Coventry Building Society Superannuation Fund held assets totalling £0.5 million which were invested in Coventry Building Society Permanent Interest Bearing Shares (PIBS) (2010: £0.5 million).

To develop the expected long-term rate of return on assets assumption, the Group considered the current level of expected returns on risk free investments (primarily Government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each asset class. The expected return for each asset class, as shown above, was then weighted based on the asset allocation to develop the expected long-term rate of return on assets assumption for the portfolio and then a deduction of 0.02% (2010: 0.14%) made for expenses. This resulted in the selection of 4.8% (2010: 5.8%).

12. PENSION SCHEME (continued)

The principal actuarial assumptions used are as follows:

Weighted average assumptions used to determine benefit obligations at	**31.12.2011**	31.12.2010
	%	%
Discount rate	**4.8**	5.5
Rate of pensionable salary increase	**4.0**	4.3
Weighted average assumptions used to determine net pension cost for the year ended		
Discount rate	**5.5**	5.5
Expected long-term return on fund assets	**5.8**	6.2
Rate of pensionable salary increase	**4.3**	4.6
Rates of inflation (Retail Price Index)	**3.5**	3.2

Weighted average life expectancy for mortality tables used to determine benefit obligations at

	31.12.2011		31.12.2010	
	Male	**Female**	Male	Female
Member age 60 (current life expectancy)	**26.2**	**28.9**	26.1	28.8
Member age 45 (life expectancy at age 60)	**28.3**	**30.9**	28.2	30.8

The assumptions on mortality are determined by the actuarial tables known as S1PXA (YOB) medium cohort 1% underpin for current and future pensioners (2010: S1PXA (YOB) medium cohort for current and future pensioners).

		Financial year ending			
Fund history	**2011**	2010	2009	2008	2007
Fair value of fund assets at end of year (£m)	**146.8**	137.9	95.9	80.4	94.1
Benefit obligation at end of year (£m)	**142.9**	133.8	89.0	71.5	82.5
Surplus (£m)	**3.9**	4.1	6.9	8.9	11.6
Difference between expected and actual return on fund assets					
Amount (£m)	**(0.4)**	4.9	9.5	(20.8)	(1.2)
Percentage of fund assets (%)	**(0.3)**	3.6	9.9	(25.9)	(1.3)
Actuarial losses/(gains) on fund liabilities					
Amount (£m)	**3.9**	(0.2)	12.8	(16.4)	(11.1)
Percentage of fund liabilities (%)	**2.7**	(0.1)	14.4	(22.9)	(13.5)

NOTES TO THE ACCOUNTS
(continued)

13. IMPAIRMENT PROVISIONS ON LOANS AND ADVANCES TO CUSTOMERS

	Loans fully secured on residential property	Other loans	Total
Group	**£m**	**£m**	**£m**
At 1 January 2011			
Individual impairment	14.3	0.6	14.9
Collective impairment	5.4	0.8	6.2
	19.7	1.4	21.1
Charge for the year			
Individual impairment	7.8	1.8	9.6
Collective impairment	0.7	(0.4)	0.3
	8.5	1.4	9.9
Amounts written off individual impairment	(8.3)	(1.6)	(9.9)
At 31 December 2011			
Individual impairment	13.8	0.8	14.6
Collective impairment	6.1	0.4	6.5
Total	19.9	1.2	21.1

	Loans fully secured on residential property	Other loans	Total
Society			
At 1 January 2011			
Individual impairment	10.5	0.5	11.0
Collective impairment	3.9	0.6	4.5
	14.4	1.1	15.5
Charge for the year			
Individual impairment	5.8	1.3	7.1
Collective impairment	(0.4)	(0.4)	(0.8)
	5.4	0.9	6.3
Amounts written off individual impairment	(6.5)	(1.1)	(7.6)
At 31 December 2011			
Individual impairment	9.8	0.7	10.5
Collective impairment	3.5	0.2	3.7
Total	13.3	0.9	14.2

When arriving at the impairment provision, the Group has considered accounts with forbearance indicators. The Group notes that accounts with forbearance indicators were immaterial in number and value. See page 80, Credit risk – forbearance for further details.

13. IMPAIRMENT PROVISIONS ON LOANS AND ADVANCES TO CUSTOMERS (continued)

	Loans fully secured on residential property	Other loans	Total
Group	£m	£m	£m
At 1 January 2010			
Individual impairment	15.3	2.5	17.8
Collective impairment	5.3	0.3	5.6
	20.6	2.8	23.4
Charge for the year			
Individual impairment	7.7	3.5	11.2
Collective impairment	0.1	0.5	0.6
	7.8	4.0	11.8
Amounts written off individual impairment	(8.7)	(5.4)	(14.1)
At 31 December 2010			
Individual impairment	14.3	0.6	14.9
Collective impairment	5.4	0.8	6.2
Total	19.7	1.4	21.1

Society			
At 1 January 2010			
Individual impairment	11.7	2.2	13.9
Collective impairment	3.6	0.3	3.9
	15.3	2.5	17.8
Charge for the year			
Individual impairment	5.5	2.8	8.3
Collective impairment	0.3	0.3	0.6
	5.8	3.1	8.9
Amounts written off individual impairment	(6.7)	(4.5)	(11.2)
At 31 December 2010			
Individual impairment	10.5	0.5	11.0
Collective impairment	3.9	0.6	4.5
Total	14.4	1.1	15.5

The provisions above have been deducted from the appropriate asset values in the statement of financial position.

NOTES TO THE ACCOUNTS
(continued)

14. PROVISION FOR IMPAIRMENT OF DEBT SECURITIES

The Group made a final recovery of £2.1 million from the administrators of Kaupthing, Singer & Friedlander in 2010.

15. PROVISION FOR FSCS LEVIES

All deposit-taking institutions that are members of the UK Financial Services Compensation Scheme (FSCS) are required to contribute to the costs of the FSCS in safeguarding the deposits of savers in failed financial institutions. The Society is, and continues to be, a member of the FSCS.

Contributions to the FSCS are calculated according to a prescribed formula using the retail savings balances of all deposit-taking institutions who are members of the FSCS.

The Group has provided £13.4 million in its 2011 Accounts with respect to the estimated levies for the period 2012/13 and revisions for the levy estimate for the period 2011/12 previously provided in its 2010 Accounts (2010: £5.6 million for the period 2011/12 and revisions for the period 2010/11).

These costs are 'exceptional' because they are outside of the Group's control and are dependent upon the extent of failures of other deposit-taking institutions who are members of the FSCS.

16. CHARITABLE DONATION TO POPPY APPEAL

During 2011 the Society again partnered with The Royal British Legion to raise funds for the annual Poppy Appeal. The Society has provided for a donation of £1.0 million (2010: £1.7 million) to the Poppy Appeal.

17. TAXATION

	Group 2011	**Society 2011**	Group 2010	Society 2010
	£m	**£m**	£m	£m
Current tax				
UK corporation tax at 26.5% (2010: 28.0%)	**11.9**	**6.8**	15.6	10.4
UK corporation tax - adjustment in respect of prior years	**(2.4)**	**(1.8)**	(0.6)	(0.6)
Total current tax	**9.5**	**5.0**	15.0	9.8
Deferred tax				
Current year	**4.9**	**1.6**	0.3	(0.2)
Adjustment in respect of prior years	**(1.5)**	**(1.6)**	0.4	0.4
Total deferred tax	**3.4**	**-**	0.7	0.2
Total	**12.9**	**5.0**	15.7	10.0

The effective tax rate for the year is 21.7% for the Group and 17.4% for the Society (2010: 15.6% for the Group and 9.4% for the Society). Further information relating to deferred tax is presented in note 27.

17. TAXATION (continued)

The tax on items reported through other comprehensive income is as follows:

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Statement of comprehensive income				
Tax (credit)/charge on actuarial loss/gain on defined benefit pension plan	**(1.1)**	**(1.1)**	1.4	1.4
Tax charge on fair value movements	**5.2**	**5.2**	5.3	5.3
Total	**4.1**	**4.1**	6.7	6.7

The actual tax charge for the period differs from the UK standard corporation tax rate of 26.5% (2010: 28.0%). The differences are explained below.

	Group 2011	Society 2011	Group 2010	Society 2010
Profit before tax	**59.5**	**28.8**	100.6	106.7
Tax at UK standard rate of corporation tax on Profit before tax of 26.5% (2010: 28.0%)	**15.8**	**7.6**	28.2	29.9
Adjustments in respect of prior years	**(3.9)**	**(3.4)**	(0.2)	(0.2)
Gain on business combination	**-**	**-**	(12.3)	(19.8)
Effect of rate change	**1.0**	**0.3**	(0.1)	(0.1)
Expenses not deductible for tax purposes	**-**	**0.5**	0.1	0.2
Total	**12.9**	**5.0**	15.7	10.0

On 23 March 2011, the Chancellor announced a further reduction in the standard rate of corporation tax to 25% from the already announced 27% to 26% from 1 April 2011. The 25% rate was substantively enacted in July 2011. The Group considers that the temporary differences included in the deferred tax calculation will, for the most part, reverse after 1 April 2012 and therefore the deferred tax assets and liabilities have been calculated using the 25% rate.

The UK Government also confirmed its intention to reduce the rate further by 1% per annum falling to 23% with effect from 1 April 2014. If the 23% tax rate had already been substantively enacted this would have reduced the net deferred tax as at 31 December 2011 by £0.4 million. We do not expect the proposed reductions in the statutory rate to 23%, once substantively enacted, to have a material effect on the Group's current or deferred tax charge.

18. CASH IN HAND AND BALANCES WITH THE BANK OF ENGLAND

	Group 2011	Society 2011	Group 2010	Society 2010
Cash in hand and balances with the Bank of England other than mandatory reserve deposits	**1,591.1**	**1,584.2**	1,427.9	1,427.5
Mandatory reserve with the Bank of England	**15.9**	**15.9**	16.3	16.3
Total	**1,607.0**	**1,600.1**	1,444.2	1,443.8

The mandatory reserve deposits with the Bank of England of £15.9 million (2010: £16.3 million) are not available for use in the Group's day-to-day operations. All other balances with the Bank of England are not mandatory and are readily accessible.

NOTES TO THE ACCOUNTS
(continued)

19. LOANS AND ADVANCES TO CREDIT INSTITUTIONS

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Loans and advances to credit institutions have remaining maturities as follows:				
Accrued interest	0.1	0.1	1.0	1.0
Repayable on demand	143.6	143.6	70.6	70.6
Other loans and advances by residual maturity repayable				
In not more than three months	243.6	174.6	106.0	106.0
In more than three months but not more than one year	1.0	1.0	15.8	15.8
Total	388.3	319.3	193.4	193.4

20. DEBT SECURITIES

	Group 2011	Society 2011	Group 2010	Society 2010
Available-for-sale:				
UK Government investment securities	1,781.4	1,781.4	1,019.4	1,019.4
Analysis of transferable debt securities				
Listed	786.5	786.5	1,165.2	1,165.2
Unlisted	278.4	278.4	679.4	679.4
Total	2,846.3	2,846.3	2,864.0	2,864.0
Debt securities have remaining maturities as follows:				
In not more than one year	560.5	560.5	905.3	905.3
In more than one year	2,285.8	2,285.8	1,958.7	1,958.7
Total	2,846.3	2,846.3	2,864.0	2,864.0
Movements during the year of transferable securities are analysed below:				
At 1 January	2,864.0	2,864.0	3,538.0	3,538.0
Acquired on transfer of engagements	-	-	398.9	398.9
Additions	7,276.7	7,276.7	5,687.0	5,687.0
Maturities and disposals	(7,468.8)	(7,468.8)	(6,796.2)	(6,796.2)
Gains from changes in fair value	174.4	174.4	36.3	36.3
At 31 December	2,846.3	2,846.3	2,864.0	2,864.0

21. LOANS AND ADVANCES TO CUSTOMERS

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Loans fully secured on residential property	19,163.4	13,977.1	17,485.7	13,470.2
Other loans				
Loans fully secured on land	11.4	1.1	14.5	2.0
Other loans	65.2	44.8	73.5	51.5
	76.6	45.9	88.0	53.5
Total	**19,240.0**	**14,023.0**	17,573.7	13,523.7

Other loans incorporate £0.9 million (2010: £1.0 million) of loans that are fully secured on residential property and that were made to corporate bodies such as Housing Associations prior to 1 July 1998, the date upon which the Society became subject to the powers of the Building Societies Act 1997. Although the classification of these assets is not consistent with similar loans made after 1 July 1998 that are included in 'loans fully secured on residential property', this treatment has been adopted in order to comply with the requirements of the Building Societies Act 1997. Other loans also include unsecured personal loans.

Maturity analysis

The remaining maturity of loans and advances to customers at the balance sheet date is as follows:

	Group 2011	Society 2011	Group 2010	Society 2010
In not more than one year	104.8	91.7	111.9	91.5
In more than one year	19,156.3	13,945.5	17,482.9	13,447.7
	19,261.1	14,037.2	17,594.8	13,539.2
Impairment provision (note 13)	(21.1)	(14.2)	(21.1)	(15.5)
Total	**19,240.0**	**14,023.0**	17,573.7	13,523.7

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

Covered bonds

The Society established Coventry Building Society Covered Bonds LLP (LLP) in July 2008, in order to provide security for issues of covered bonds made by the Society to external counterparties. The LLP is consolidated by the Group.

During the year, Coventry Building Society issued two public covered bonds. In April 2011, the Society issued a £750 million seven year deal and a further €650 million three year deal in October 2011.

Loans and advances to customers include £4,474.7 million (2010: £3,051.7 million) for both the Group and Society for which the beneficial interest has been transferred from the Society to the LLP. The loans secure the £2,200.0 million and €650.0 million (2010: £2,000.0 million) of covered bonds issued by the Society. The loans are retained on the Society's balance sheet as the Society retains substantially all the risks and rewards relating to the loans.

22. INVESTMENTS IN SUBSIDIARY UNDERTAKINGS

	Shares	Loans	Total 2011
Society	£m	£m	£m
Cost and net book value			
At 1 January	13.2	7,204.1	7,217.3
Additions	-	2,540.7	2,540.7
At 31 December	**13.2**	**9,744.8**	**9,758.0**

NOTES TO THE ACCOUNTS
(continued)

22. INVESTMENTS IN SUBSIDIARY UNDERTAKINGS

The Society has the following subsidiary undertakings all of which are consolidated:

Subsidiary undertakings	Principal activity
Godiva Mortgages Limited	Mortgage lending
ITL Mortgages Limited	Mortgage lending and mortgage acquisition vehicle
Stroud & Swindon Funding Company	Funding company for mortgage acquisitions
Stroud & Swindon Funding Company (No.2) Limited	Funding company for mortgage acquisitions
Five Valleys Property Company Limited	Investment properties holding company
Coventry Financial Services Limited	Non-trading
Coventry Property Services Limited	Non-trading
Godiva Financial Services Limited	Non-trading
Godiva Housing Developments Limited	Non-trading
Godiva Savings Limited	Non-trading
Godiva Securities and Investments Limited	Non-trading
Coventry Building Society Covered Bonds LLP	Intra-group mortgage acquisition and guarantor of covered bonds

All of the above subsidiaries are 100% directly or indirectly owned by Coventry Building Society. The subsidiaries are wholly owned subsidiaries incorporated in England and Wales and operate in the UK. All of the subsidiaries have an accounting reference date of 31 December and are included in the Group's consolidated Financial Statements.

23. INTANGIBLE ASSETS

	Software expenditure 2011	**Other intangible assets 2011**	**Total 2011**	Software expenditure 2010	Other intangible assets 2010	Total 2010
Group	**£m**	**£m**	**£m**	£m	£m	£m
Cost						
At 1 January	**13.4**	**3.0**	**16.4**	11.4	-	11.4
Additions	**3.1**	**-**	**3.1**	3.1	-	3.1
Acquired on transfer of engagement	**-**	**-**	**-**	-	3.0	3.0
Retirements	**(3.8)**	**-**	**(3.8)**	(1.1)	-	(1.1)
At 31 December	**12.7**	**3.0**	**15.7**	13.4	3.0	16.4
Amortisation						
At 1 January	**3.5**	**0.7**	**4.2**	1.5	-	1.5
Charge for the year[1]	**3.5**	**2.3**	**5.8**	3.0	0.7	3.7
Amortisation on retirements	**(3.8)**	**-**	**(3.8)**	(1.0)	-	(1.0)
At 31 December	**3.2**	**3.0**	**6.2**	3.5	0.7	4.2
Net book value at 31 December	**9.5**	**-**	**9.5**	9.9	2.3	12.2

[1] The amortisation charge of other intangible assets has been included within 'Integration and merger related costs' within the income statement.

23. INTANGIBLE ASSETS (continued)

Society	Software expenditure 2011 £m	Other intangible assets 2011 £m	Total 2011 £m	Software expenditure 2010 £m	Other intangible assets 2010 £m	Total 2010 £m
Cost						
At 1 January	12.9	3.0	15.9	10.9	-	10.9
Additions	3.1	-	3.1	3.1	-	3.1
Acquired on transfer of engagement	-	-	-	-	3.0	3.0
Retirements	(3.8)	-	(3.8)	(1.1)	-	(1.1)
At 31 December	12.2	3.0	15.2	12.9	3.0	15.9
Amortisation						
At 1 January	3.0	0.7	3.7	1.0	-	1.0
Charge for the year[1]	3.5	2.3	5.8	3.0	0.7	3.7
Amortisation on retirements	(3.8)	-	(3.8)	(1.0)	-	(1.0)
At 31 December	2.7	3.0	5.7	3.0	0.7	3.7
Net book value at 31 December	9.5	-	9.5	9.9	2.3	12.2

[1] The amortisation charge of other intangible assets has been included within 'Integration and merger related costs' within the income statement.

Other intangible assets are in respect of retail deposits and customer relationships arising on the merger with Stroud & Swindon Building Society.

24. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings			Equipment, fixtures, fittings and vehicles	Total
	Freehold	Long leasehold	Short leasehold		
Group and Society	£m	£m	£m	£m	£m
Cost					
At 1 January 2011	7.9	3.9	3.2	43.0	58.0
Additions	-	-	0.2	8.6	8.8
Transferred from non-current assets held for sale	1.4	-	-	-	1.4
Disposals	-	-	-	(2.9)	(2.9)
At 31 December 2011	9.3	3.9	3.4	48.7	65.3
Depreciation					
At 1 January 2011	1.1	0.4	2.1	26.3	29.9
Charge for the year	0.2	0.2	0.1	4.5	5.0
Depreciation on disposals	-	-	-	(2.4)	(2.4)
At 31 December 2011	1.3	0.6	2.2	28.4	32.5
Net book value at 31 December 2011	8.0	3.3	1.2	20.3	32.8

Disposals relate to assets that were retired during the year.

24. PROPERTY, PLANT AND EQUIPMENT (continued)

	Land and buildings			Equipment, fixtures, fittings and vehicles	Total
	Freehold	Long leasehold	Short leasehold		
Group and Society	£m	£m	£m	£m	£m
Cost					
At 1 January 2010[1]	6.4	3.5	3.2	40.1	53.2
Acquired on transfer of engagements	1.5	0.4	-	-	1.9
Additions	-	-	-	5.6	5.6
Disposals	-	-	-	(2.7)	(2.7)
At 31 December 2010	7.9	3.9	3.2	43.0	58.0
Depreciation					
At 1 January 2010[1]	1.0	0.3	2.0	25.0	28.3
Charge for the year	0.1	0.1	0.1	4.0	4.3
Depreciation on disposals	-	-	-	(2.7)	(2.7)
At 31 December 2010	1.1	0.4	2.1	26.3	29.9
Net book value at 31 December 2010	6.8	3.5	1.1	16.7	28.1

[1] Freehold property as at 1 January 2010 was restated and excludes freehold property held for investment purposes. See note 25 for details on the freehold properties held for investment purposes.

Equipment, fixtures, fittings and vehicles includes assets held under finance leases as follows:

	2011	2010
Group and Society	**£m**	£m
Net book value	**0.9**	1.1
Accumulated depreciation	**0.6**	0.7

The net book value of land and buildings occupied by the Group for its own activities is as follows:

Group and Society		
At 31 December	**11.6**	10.5

25. INVESTMENT PROPERTIES

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Cost				
At 1 January	5.9	0.7	0.7	0.7
Acquired on transfer of engagements	-	-	5.2	-
At 31 December	5.9	0.7	5.9	0.7
Amortisation				
At 1 January	0.1	0.1	0.1	0.1
Charge for the year	0.1	-	-	-
At 31 December	0.2	0.1	0.1	0.1
Net book value at 31 December	5.7	0.6	5.8	0.6
Fair value at 31 December	6.9	1.3	6.5	1.3

Investment properties generally include residential properties and offices ancillary to branch premises which are not occupied by the Group.

Depreciation is provided by the Group to write off the cost less the estimated residual value of investment properties (excluding land) by equal instalments over their useful economic life of 50 years. Land is not depreciated. Any impairment in the value of properties is dealt with through the income statement as it arises.

The investment properties were valued by a qualified chartered surveyor, who is a member of the Royal Institute of Chartered Surveyors (RICS). The properties were valued on the basis of market value, and the valuation was carried out in accordance with the RICS Appraisal and Valuation Standards. As the investment properties are held at depreciated historical cost, this valuation has not been reflected in the carrying value of the assets. No impairment of the investment properties was made during the year.

26. NON-CURRENT ASSETS HELD FOR SALE

As at 31 December 2011, non-current assets held for sale comprises one freehold property which was acquired as a result of the merger with Stroud & Swindon Building Society. The property is expected to be sold in the financial year beginning 1 January 2012.

During the year, a freehold property was transferred from non-current assets held for sale to property, plant and equipment and was occupied by the Group.

27. DEFERRED TAX

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

	Group 2011	Society 2011	Group 2010	Society 2010
Deferred tax assets				
Provisions	0.5	0.5	0.3	0.3
Pension scheme benefit from special contribution	-	-	0.1	0.1
IFRS transitional fair value adjustments	0.9	0.9	1.3	1.3
Excess of depreciation over capital allowances	0.3	0.3	0.1	0.1
Defined benefit pension plan deficit	-	-	0.8	0.8
Transfer of engagements - fair value adjustments	12.8	5.0	16.8	5.6
Total	14.5	6.7	19.4	8.2

NOTES TO THE ACCOUNTS
(continued)

27. DEFERRED TAX (continued)

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Deferred tax liabilities				
Excess of capital allowances over depreciation	-	-	1.0	1.0
IFRS transitional fair value adjustments	1.5	1.5	2.0	2.0
Defined benefit pension plan surplus	1.0	1.0	2.0	2.0
Transfer of engagements - fair value adjustments	0.5	0.5	0.6	0.6
Total	3.0	3.0	5.6	5.6
Statement of other comprehensive income				
Tax (credit)/charge on actuarial loss/gain on defined benefit pension plan	(1.1)	(1.1)	1.4	1.4

28. SHARES

	Group 2011	Society 2011	Group 2010	Society 2010
Held by individuals	18,956.0	18,956.0	17,626.5	17,626.5
Other shares	8.1	8.1	7.8	7.8
Total	18,964.1	18,964.1	17,634.3	17,634.3

	Group 2011	Society 2011	Group 2010	Society 2010
Shares are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	165.9	165.9	167.6	167.6
Repayable on demand	14,297.0	14,297.0	13,840.0	13,840.0
Shares with residual maturity repayable:				
In more than three months but not more than one year	3,596.0	3,596.0	865.0	865.0
In more than one year but not more than five years	905.2	905.2	2,761.7	2,761.7
Total	18,964.1	18,964.1	17,634.3	17,634.3

29. DEPOSITS FROM BANKS

	Group 2011	Society 2011	Group 2010	Society 2010
Deposits from banks are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	0.8	0.8	0.7	0.7
Repayable on demand	3.1	3.1	8.6	8.6
Other amounts owed to banks with residual maturity repayable:				
In not more than three months	507.0	507.0	1,306.1	1,306.1
Total	510.9	510.9	1,315.4	1,315.4

Deposits from banks include £501 million (2010: £1,294 million) in respect of sale and repurchase agreements.

30. OTHER DEPOSITS

	Group 2011	Society 2011	Group 2010	Society 2010
Other deposits are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	-	-	0.1	0.1
Amounts owed to depositors with residual maturity repayable:				
In not more than three months	23.0	23.0	25.0	25.0
In more than three months but not more than one year	-	-	9.0	9.0
Total	23.0	23.0	34.1	34.1

31. AMOUNTS OWED TO OTHER CUSTOMERS

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	**£m**	£m	£m
Amounts owed to other customers are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	**1.9**	**1.9**	2.8	2.8
Repayable on demand	**25.2**	**25.2**	40.8	40.8
Other amounts due to customers with residual maturity repayable:				
In not more than three months	**451.8**	**451.8**	428.2	428.2
In more than three months but not more than one year	**61.3**	**61.3**	159.1	159.1
In more than one year but not more than five years	**9.1**	**9.1**	14.3	14.3
Total	**549.3**	**549.3**	645.2	645.2

32. DEBT SECURITIES IN ISSUE

	Group 2011	Society 2011	Group 2010	Society 2010
Certificates of deposit	**192.4**	**192.4**	134.2	134.2
Fixed rate notes	**2,581.7**	**2,581.7**	1,262.1	1,262.1
Floating rate notes	**89.7**	**89.7**	137.0	137.0
Total	**2,863.8**	**2,863.8**	1,533.3	1,533.3

Debt securities in issue are repayable from the balance sheet date in the ordinary course of business as follows:

	Group 2011	Society 2011	Group 2010	Society 2010
Accrued interest	**46.0**	**46.0**	12.4	12.4
Other debt securities in issue with residual maturity repayable:				
In not more than one year	**701.6**	**701.6**	178.9	178.9
In more than one year	**2,116.2**	**2,116.2**	1,342.0	1,342.0
Total	**2,863.8**	**2,863.8**	1,533.3	1,533.3

33. DERIVATIVE FINANCIAL INSTRUMENTS

	2011			2010		
	Contract/ notional amount	**Fair value assets**	**Fair value liabilities**	Contract/ notional amount	Fair value assets	Fair value liabilities
Group	**£m**	**£m**	**£m**	£m	£m	£m
Derivatives designated as fair value hedges						
Interest rate swaps	**11,854.0**	**258.6**	**299.8**	9,857.9	71.2	138.3
Interest rate caps	**748.0**	**0.3**	**-**	343.0	0.1	-
Cross currency swaps	**570.1**	**-**	**36.2**	-	-	-
Other derivatives						
Interest rate floors	**40.0**	**0.8**	**-**	40.0	1.1	-
Currency swaps	**-**	**-**	**-**	164.2	1.0	1.1
Total derivatives	**13,212.1**	**259.7**	**336.0**	10,405.1	73.4	139.4

Contract/notional amount indicates the amount outstanding at the balance sheet date and does not represent amounts at risk.

NOTES TO THE ACCOUNTS
(continued)

33. DERIVATIVE FINANCIAL INSTRUMENTS (continued)

	2011 Contract/ notional amount	2011 Fair value assets	2011 Fair value liabilities	2010 Contract/ notional amount	2010 Fair value assets	2010 Fair value liabilities
Group	**£m**	**£m**	**£m**	£m	£m	£m
Derivatives have remaining maturities as follows:						
In not more than one year	**5,006.2**	**13.9**	**14.8**	3,717.9	13.9	20.3
In more than one year	**8,205.9**	**245.8**	**321.2**	6,687.2	59.5	119.1
Total derivatives	**13,212.1**	**259.7**	**336.0**	10,405.1	73.4	139.4

	2011 Contract/ notional amount	2011 Fair value assets	2011 Fair value liabilities	2010 Contract/ notional amount	2010 Fair value assets	2010 Fair value liabilities
Society						
Derivatives designated as fair value hedges						
Interest rate swaps	**11,104.1**	**168.3**	**299.8**	9,857.9	71.2	138.3
Interest rate caps	**748.0**	**0.3**	**-**	343.0	0.1	-
Other derivatives						
Interest rate floors	**40.0**	**0.8**	**-**	40.0	1.1	-
Currency swaps	**-**	**-**	**-**	164.2	1.0	1.1
Total derivatives	**11,892.1**	**169.4**	**299.8**	10,405.1	73.4	139.4

Contract/notional amount indicates the amount outstanding at the balance sheet date and does not represent amounts at risk.

	2011 Contract/ notional amount	2011 Fair value assets	2011 Fair value liabilities	2010 Contract/ notional amount	2010 Fair value assets	2010 Fair value liabilities
Society						
Derivatives have remaining maturities as follows:						
In not more than one year	**5,006.2**	**13.9**	**14.8**	3,717.9	13.9	20.3
In more than one year	**6,885.9**	**155.5**	**285.0**	6,687.2	59.5	119.1
Total derivatives	**11,892.1**	**169.4**	**299.8**	10,405.1	73.4	139.4

HEDGING ACTIVITIES

Fair value hedges
At 31 December 2011 the Group held the following interest rate derivative contracts which qualify for hedge accounting:

- Interest rate swap agreements under which the Group pays a fixed rate of interest and receives interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate mortgage assets as a result of changes in market interest rates. These swaps have a nominal principal amount of £3,792.7 million (2010: £3,531.9 million) and a net negative fair value of £98.2 million (2010: net negative £80.1 million).

- Interest rate swap agreements under which the Group receives a fixed rate of interest and pays interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate share liabilities as a result of changes in market interest rates. These swaps have a nominal principal amount of £4,465.0 million (2010: £4,180.0 million) and a net positive fair value of £37.0 million (2010: net positive £12.0 million).

- Interest rate swap agreements under which the Group pays a fixed rate of interest and receives interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate gilts, Government guaranteed bonds, bonds issued by supranational organisation or covered bonds, purchased in the wholesale market as a result of changes in market interest rates. These swaps have a nominal principal amount of £1,448.0 million (2010: £737.0 million) and a net negative fair value of £196.9 million (2010: net negative £30.0 million).

33. DERIVATIVE FINANCIAL INSTRUMENTS (continued)

Fair value hedges (continued)

- Interest rate swap agreements under which the Group receives a fixed rate of interest and pays interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate bonds or liabilities issued in the wholesale market as a result of changes in market interest rates. These swaps have a nominal principal amount of £2,148.3 million (2010: £1,409.0 million) and a net positive fair value of £216.9 million (2010: net positive £31.0 million).

- Interest rate cap agreements under which the Group pays an initial premium and is subsequently compensated to the extent that LIBOR exceeds the cap strike rate. These caps are used to hedge changes in the fair value of exposure to the risk that market rates exceed the cap on capped rate mortgage assets. These caps have a nominal principal amount of £748.0 million (2010: £343.0 million) and a net positive fair value of £0.3 million (2010: net positive £0.1 million).

- Cross currency swaps under which the Group receives interest at a fixed rate of euros and pays interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of euro denominated bonds issued in the wholesale market as a result of changes in market interest rates and exchange rates. These cross currency swaps have a nominal principal amount of £570.1 million (2010: £nil) and a net negative fair value of £36.2 million (2010: £nil).

- The derivative gains and losses for the year in respect of fair value hedges comprise gains on derivatives of £12.3 million (2010: £27.8 million) and associated losses on hedged items of £11.6 million (2010: £29.2 million).

Hedges not qualifying for hedge accounting

Interest rate floor agreements under which the Group pays an initial premium and is subsequently compensated to the extent that LIBOR falls below the floor strike rate. These floors are used to hedge the risk of long-term low rates of interest. These floors have a nominal principal amount of £40.0 million (2010: £40.0 million) and a net positive fair value of £0.8 million (2010: £1.1 million).

During the year, there was a maturity of the cross currency swap under which the Group received interest at EURIBOR and paid interest based on LIBOR. This swap was used to hedge exposure to changes in the fair value of euro denominated bonds issued in the wholesale market as a result of changes in market interest rates and exchange rates. At 31 December 2011, there were no cross currency swaps not qualifying for hedge accounting (2010: nominal principal of £82.0 million and net positive fair value of £1.0 million).

During the year, there was also a maturity of the foreign exchange swap under which the Society had sold euros for pounds sterling at the exchange rate current to the deal and agreed that at a future date it would sell at an agreed exchange rate pounds sterling for the same value of euros that was originally exchanged. This swap was used to hedge exposure to changes in the value of future cash flows on euro denominated bonds issued in the wholesale market as a result of changes in exchange rates. At 31 December 2011, there were no foreign exchange swaps not qualifying for hedge accounting (2010: nominal principal of £82.2 million net negative fair value of £1.1 million).

The derivative gains and losses for the year in respect of hedges that do not qualify for hedge accounting comprise losses on derivatives of £0.2 million (2010: gains of £0.7 million).

34. OTHER LIABILITIES

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Other liabilities falling due within one year are as follows:				
Amounts due to connected undertakings	-	4,474.7	-	3,150.9
Tax deducted at source from interest paid	14.3	14.3	11.2	11.2
Other taxation and social security	2.2	2.2	1.8	1.8
Finance leases	0.4	0.4	0.6	0.6
Other creditors	2.4	2.4	2.5	2.5
	19.3	4,494.0	16.1	3,167.0
Other liabilities falling due after more than one year but in less than five years:				
Finance leases	0.5	0.5	0.5	0.5
Total	19.8	4,494.5	16.6	3,167.5

35. PROVISIONS FOR LIABILITIES AND CHARGES

	FSCS 2011	Other provisions 2011	Total 2011	FSCS 2010	Other provisions 2010	Total 2010
Group and Society	£m	£m	£m	£m	£m	£m
At 1 January	10.5	5.4	15.9	8.8	1.3	10.1
Acquired on transfer of engagement	-	-	-	0.8	-	0.8
Charge for the year	13.4	0.2	13.6	5.6	4.2	9.8
Provisions utilised	(5.4)	(3.8)	(9.2)	(4.7)	(0.1)	(4.8)
At 31 December	18.5	1.8	20.3	10.5	5.4	15.9

The FSCS provision is expected to be utilised in two payments of £7.2 million and £11.3 million in September 2012 and September 2013 respectively, to cover the FSCS levy periods 2011/12 and 2012/13. Further details relating to the FSCS charge are detailed in note 15.

Other provisions have also been recognised in respect of circumstances that may give rise to various customer claims. It is expected that the liability will mainly crystallise over the next five years.

The Group has no further contingent liabilities to report.

36. SUBORDINATED LIABILITIES

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Subordinated liabilities owed to note holders are as follows:				
Fixed rate subordinated notes 2016 - 12.25%	7.0	7.0	7.0	7.0
Fixed rate subordinated notes 2017 - 8.37%	10.0	10.0	10.0	10.0
Fixed rate subordinated notes 2021 - 6.12%	10.1	10.1	10.1	10.1
Fixed rate subordinated notes 2022 - 6.469%	15.5	15.5	15.5	15.5
Fixed rate subordinated notes 2026 - 6.33%	10.2	10.2	10.2	10.2
Fixed rate subordinated notes 2032 - 7.54%	15.4	15.4	15.4	15.4
Total	68.2	68.2	68.2	68.2

All the subordinated liabilities are denominated in sterling. The notes are repayable in the years stated, or earlier in accordance with their terms at the option of the Society, with the prior consent of the FSA.

The rights of repayment of the holders of the notes are subordinated to the claims of all depositors, creditors and shareholders in the Society, as regards the principal of the notes and accrued interest.

37. SUBSCRIBED CAPITAL

	Group 2011	Society 2011	Group 2010	Society 2010
Subscribed capital owed to permanent interest holding members is as follows:				
Permanent interest bearing shares	161.3	161.3	161.3	161.3

Interest is paid in arrears on £40 million permanent interest bearing shares at the rate of 12 1/8% per annum in half-yearly instalments, and on £120 million permanent interest bearing shares at the rate of 6.092% per annum in half-yearly instalments. The shares are repayable only in the event of a winding up of the Society or otherwise with the prior consent of the FSA. In a winding up or dissolution of the Society the claims of the holders of permanent interest bearing shares would rank behind all other creditors of the Society and the claims of members holding shares as to principal and interest. The holders of permanent interest bearing shares are not entitled to any share in any final surplus upon a winding up or final dissolution of the Society.

38. FINANCIAL COMMITMENTS

	Group 2011	Society 2011	Group 2010	Society 2010
Undrawn mortgage loan facilities	125.9	93.4	152.4	108.0

Subject to the satisfaction of previously agreed loan to value ratios, the Group is committed to £125.9 million (2010: £152.4 million) of undrawn mortgage loan facilities (Society £93.4 million, 2010: £108.0 million) relating to its lifetime and flexible mortgage products.

39. CAPITAL AND LEASING COMMITMENTS

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	£m	£m	£m
Capital commitments				
Capital expenditure contracted for but not provided for in the Accounts	**0.2**	**0.2**	1.6	1.6

Leasing commitments

Future minimum lease payments under non-cancellable operating leases relating to land and buildings were as follows:

	Group 2011	Society 2011	Group 2010	Society 2010
Amounts falling due:				
Within one year	**3.2**	**3.2**	3.1	3.1
Between one and five years	**9.6**	**9.6**	10.3	10.3
After five years	**8.7**	**8.7**	9.8	9.8
Total	**21.5**	**21.5**	23.2	23.2
Lease payments recognised as an expense in the period	**3.7**	**3.7**	3.1	3.1

Leasing payments due as lessor

	Group 2011	Society 2011	Group 2010	Society 2010
At the balance sheet date, future minimum sub-leasing payments receivable under non-cancellable subleases	**0.7**	**0.7**	1.0	1.0
At the balance sheet date, future minimum lease payments receivable under non-cancellable leases were as follows:				
Within one year	**0.2**	**0.2**	0.2	0.2
Between one and five years	**0.4**	**0.4**	0.3	0.3
After five years	**0.2**	**0.2**	0.2	0.2
Total	**0.8**	**0.8**	0.7	0.7

40. FINANCIAL INSTRUMENTS

Use of financial instruments

The risks of the organisation are managed on a Group basis and therefore all risk disclosures in this note have been presented on a consolidated basis. The term 'Group' is used in the remainder of this note to cover the activities of both the Group and the Society.

Deposits are accepted from customers at both fixed and variable interest rates for various periods. The Group earns interest margin on these deposits by investing in mortgages.

The Group holds derivative financial instruments for the purposes of managing the risks associated with its various fixed and capped rate assets and liabilities and its foreign currency transactions. In accordance with its treasury policy, and the Building Societies Act 1986, the Group holds derivative financial instruments only for risk management and not for speculative or trading purposes.

The Group's policy is to manage its exposure to these risks within prudent limits. It does this through a combination of matching assets and liabilities with offsetting interest rate or exchange rate characteristics and by the use of derivative financial instruments such as interest rate swaps, forward rate agreements, interest rate options, cross currency interest rate swaps and foreign exchange contracts.

The accounting policy for derivatives and hedge accounting is described in the Accounting Policies in note 1.

Control and monitoring procedures

The Asset and Liability Committee (ALCO) sets limits over the use of derivative products for managing exposure to interest rates and foreign exchange rates, sets Group wholesale credit policy and regularly monitors and reviews exposures. ALCO reports through the Risk Management Committee to the Board Risk Committee.

The Retail Credit Risk and Lending Committee sets Group retail credit policy and regularly monitors and reviews exposures in this area. The Credit Risk and Lending Committee reports through the Risk Management Committee to the Board Risk Committee.

The principal risks the Group faces are interest rate, credit, foreign currency and liquidity risk. Each risk, and the control procedures surrounding its management, are described in detail in the Risk Management Report (see pages 20 to 25).

Interest rate risk

The Group evaluates the impact on margin of various interest rate scenarios to monitor interest rate risk. The Group uses basis point sensitivity analysis to assess the change in the value of the Group's balance sheet net worth against a 100 basis point (1.0%) parallel shock to interest rates.

Details of this sensitivity analysis are set out overleaf. The limits around these scenarios are proposed by ALCO and approved by the Board. The Group's approach surrounding the management of interest rate risk are detailed within the Risk Management Report (see page 23).

All exposures include investment of the Group's reserves.

NOTES TO THE ACCOUNTS
(continued)

40. FINANCIAL INSTRUMENTS (continued)

Interest rate risk (continued)

The following table shows the impact on net worth through the reporting period:

	+100bps 2011	-100bps 2011	+100bps 2010	-100bps 2010
	£m	£m	£m	£m
Impact on equity reserves	(13.7)	14.0	(18.7)	18.8
Impact on profit and loss	11.1	(6.4)	11.8	(8.3)

The impact on equity reserves considers movements in the underlying value of assets and liabilities carried at fair value, based on the shift in market interest rates, whereas the impact on profit or loss considers the impact on the Group results in respect of shift in the return on the Group's assets and liabilities.

The following table sets out the carrying amount of the Group's financial instruments that are exposed to interest rate risk and the expected interest reset date of those instruments.

	Three months or less	More than three months less than six months	More than six months less than one year	More than one year less than five years	More than five years	Non-interest bearing	Total
At 31 December 2011	£m	£m	£m	£m	£m	£m	£m
Assets							
Liquid assets	2,951	-	-	355	1,278	258	4,842
Loans and advances to customers	12,652	931	1,051	3,939	621	46	19,240
Fixed assets	-	-	-	-	-	48	48
Other assets and adjustments	-	-	-	-	-	357	357
Total assets	15,603	931	1,051	4,294	1,899	709	24,487
Liabilities and equity							
Shares	(9,816)	(1,028)	(4,780)	(2,997)	(24)	(319)	(18,964)
Deposits, amounts owed to customers and debt securities	(1,188)	(566)	(73)	(554)	(1,500)	(66)	(3,947)
Other liabilities and adjustments	-	-	-	-	-	(603)	(603)
Subordinated liabilities	-	-	-	-	(68)	-	(68)
Subscribed capital	-	-	-	-	(161)	-	(161)
Reserves	-	-	-	-	-	(744)	(744)
Total liabilities and equity	(11,004)	(1,594)	(4,853)	(3,551)	(1,753)	(1,732)	(24,487)
Derivative financial instruments	(2,658)	524	2,904	(761)	142	(151)	-
Interest rate sensitivity gap	1,941	(139)	(898)	(18)	288	(1,174)	-

The table above is based on the contractual interest rate reset date, which may differ from the contractual maturity date.

40. FINANCIAL INSTRUMENTS (continued)

Interest rate risk (continued)

At 31 December 2010	Three months or less £m	More than three months less than six months £m	More than six months less than one year £m	More than one year less than five years £m	More than five years £m	Non-interest bearing £m	Total £m
Assets							
Liquid assets	3,244	78	17	515	605	73	4,532
Loans and advances to customers	10,781	925	847	4,342	647	32	17,574
Fixed assets	-	-	-	-	-	46	46
Other assets and adjustments	-	-	-	-	-	150	150
Total assets	14,025	1,003	864	4,857	1,252	301	22,302
Liabilities and equity							
Shares	(9,466)	(1,442)	(1,944)	(4,532)	(96)	(154)	(17,634)
Deposits, amounts owed to customers and debt securities	(2,090)	(72)	(47)	(512)	(750)	(57)	(3,528)
Other liabilities and adjustments	-	-	-	-	-	(225)	(225)
Subordinated liabilities	-	-	-	-	(68)	-	(68)
Subscribed capital	-	-	-	-	(161)	-	(161)
Reserves	-	-	-	-	-	(686)	(686)
Total liabilities and equity	(11,556)	(1,514)	(1,991)	(5,044)	(1,075)	(1,122)	(22,302)
Derivative financial instruments	(709)	277	555	(314)	340	(149)	-
Interest rate sensitivity gap	1,760	(234)	(572)	(501)	517	(970)	-

Credit risk

Credit risk is the risk that customers or counterparties will be unable to meet their financial obligations to the Group as they fall due. Impairment provisions are provided for losses that have been incurred at the balance sheet date (see note 13). The Group's policies in respect of managing credit risk are detailed in the Risk Management Report (see pages 21 and 22).

Maximum credit risk exposure at 31 December 2011 approximates to the carrying value for all assets and loan commitments.

Of the £19,240.0 million 'loans and advances to customers', £19,174.8 million (99.7%) (2010: 99.6%) is fully secured on residential property and land and £65.2 million (0.3%) (2010: 0.4%) relates to unsecured personal loans.

The average indexed current loan to value ratio of the Group's loans and advances to customers is 50% (2010: 50%).

The Group's number of customers in arrears as a percentage of loans and advances to customers compared to the Council of Mortgage Lenders' (CML) data is shown overleaf:

40. FINANCIAL INSTRUMENTS (continued)

Credit risk (continued)

	Group 2011	CML[1] 2011	Group 2010	CML 2010
	%	%	%	%
Greater than three months	1.16	1.98	1.17	2.11
Greater than six months	0.56	1.12	0.59	1.23
Greater than one year	0.14	0.48	0.18	0.55
In possession	0.05	0.12	0.06	0.11

[1] Council of Mortgage Lenders' data (as at 31 December 2011).

Advances to customers are supported by collateral in the form of residential properties. Below is an analysis of the collateral against these advances.

Loan to value analysis on advances to customers:

	New lending 2011	Mortgage balances 2011	New lending 2010	Mortgage balances 2010
Indexed loan to value:	%	%	%	%
< 50%	32.48	47.04	35.32	48.82
50% to 65%	37.58	20.79	31.45	18.86
65% to 75%	17.56	12.99	22.65	11.22
75% to 85%	11.07	9.74	9.69	9.39
85% to 95%	1.31	5.44	0.89	6.32
> 95%	-	4.00	-	5.39
Total	100.00	100.00	100.00	100.00

The table below provides further information by payment due status:

	2011	2011	2010	2010
	£m	%	£m	%
Not impaired				
Not past due	18,337.2	95.31	16,588.5	94.40
Past due up to three months	643.3	3.34	736.7	4.19
Impaired				
Past due over three to six months	129.5	0.67	120.2	0.68
Past due over six months or in litigation	119.4	0.62	117.2	0.67
In possession	10.6	0.06	11.1	0.06
Total	19,240.0	100.00	17,573.7	100.00

The Group held properties valued at £11.6 million (2010: £13.3 million) pending their sale as collateral against loan repossession cases of £10.6 million (2010: £11.1 million) which are classified in 'loans and advances to customers' in the statement of financial position.

- **Credit risk - forbearance**

Customers subject to forbearance measures actioned by the collections department as at 31 December 2011 represented 0.34% of the total book by outstanding balance, and 0.30% of the total book by number of cases.

40. FINANCIAL INSTRUMENTS (continued)

- **Credit risk – treasury liquidity book**

	Exposure value by Moody's rating Aaa-Aa3	A1-A3	Baa1-Baa3	Other	Unrated	Total
2011	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Central banks and sovereigns	**3,623.9**	**-**	**-**	**-**	**-**	**3,623.9**
Multilateral development banks (supranational bonds)	**188.7**	**-**	**-**	**-**	**-**	**188.7**
Financial institutions	**366.6**	**348.2**	**35.0**	**17.7**	**27.8**	**795.3**
Mortgage-backed securities	**228.7**	**5.0**	**-**	**-**	**-**	**233.7**
Local authorities	**-**	**-**	**-**	**-**	**0.5**	**0.5**
Total	**4,407.9**	**353.2**	**35.0**	**17.7**	**28.3**	**4,842.1**

Exposures rated as 'Other', comprise of Irish financial institutions (see below) and other UK building societies. 'Unrated' institutions relate to smaller building societies and local authorities.

	Exposure value by Moody's rating Aaa-Aa3	A1-A3	Baa1-Baa3	Other	Unrated	Total
2010	£m	£m	£m	£m	£m	£m
Central banks and sovereigns	2,817.6	-	-	-	-	2,817.6
Multilateral development banks (supranational bonds)	108.4	-	-	-	-	108.4
Financial institutions	1,014.8	91.2	28.7	-	79.9	1,214.6
Mortgage-backed securities	361.0	-	-	-	-	361.0
Local authorities	-	-	-	-	30.3	30.3
Total	4,301.8	91.2	28.7	-	110.2	4,531.9

As at the year end, the Group had financial assets invested in financial institutions in Ireland, with a fair value of £7.7 million (amortised cost: £8.4 million). The Group has no exposures to financial institutions, central banks or sovereigns based in Portugal, Italy, Greece or Spain. The table below shows the maturity profile of the financial assets in Irish financial institutions. On 20 February 2012, £5.0 million due within three months of 31 December 2011 had been repaid in full by the deposit counterparty.

	Up to three months	More than three months less than six months	More than six months less than one year	More than one year	Total
	£m	**£m**	**£m**	**£m**	**£m**
Ireland (fair value)	**4.8**	**2.9**	**-**	**-**	**7.7**
Ireland (amortised cost)	**5.0**	**3.4**	**-**	**-**	**8.4**

Foreign currency risk

Foreign currency risk arises as a result of the Group's activities in raising funds and making investments in foreign currencies. This is undertaken to ensure wholesale funds are obtained cost-effectively across a wide pool of potential providers, but exposes the Group to the risk of an appreciation in the value of foreign currency denominated liabilities or a deterioration in the value of the foreign currency denominated assets.

The risk is managed through the use of currency swaps and foreign currency forward contracts and also, where appropriate, by the matching of foreign currency liabilities with assets denominated in the same currency.

40. FINANCIAL INSTRUMENTS (continued)

Foreign currency risk (continued)
After taking into account the effects of cross currency swaps, the Group has no material net exposure to foreign exchange risk fluctuations or changes in foreign currency interest rates. ALCO sets limits on the level of exposure by currency which are monitored daily.

House price risk
House price risk arises from the value of the property forming the security for the mortgage being insufficient to repay the loan in the event of default and subsequent repossession. The Group manages this risk through a combination of prudent loan to value limits at inception and constant monitoring to ensure that bad debt provisions are sufficient to cover the potential losses that may arise in repossession situations. Further details of the Group's policies for managing house price risk are set out within the Risk Management Report (see page 23).

Liquidity risk
Liquidity risk is the risk that the Group has insufficient funds to meet its financial obligations as they fall due. This could manifest itself in extreme scenarios such as an inability to raise new wholesale funding to replace existing funding as it matures, or a run on retail funds. Details of the Group's approach for managing liquidity risk are detailed in the Risk Management Report (see page 24).

	2011	2010
	%	%
Liquidity ratio	**21.1**	21.4

Liquidity risk – maturity analysis
For each material class of financial liability the contractual maturity analysis is provided in notes 28 to 33. In practice, customer deposits will be repaid later than on the contractual date on which the repayment can be required.

The following is an analysis of gross contractual cash flows payable under financial liabilities:

	Repayable on demand	Up to three months	More than three months less than six months	More than six months less than one year	More than one year less than five years	More than five years	Total
At 31 December 2011	£m	£m	£m	£m	£m	£m	£m
Liabilities							
Shares	14,423	7	539	3,212	950	-	19,131
Deposits, amounts owed to customers and debt securities	25	1,099	588	94	671	1,500	3,977
Other liabilities and adjustments	-	102	57	45	240	163	607
Subordinated liabilities	-	1	11	2	34	57	105
Subscribed capital	-	2	4	6	165	42	219
Total liabilities	14,448	1,211	1,199	3,359	2,060	1,762	24,039
Undrawn loan facilities	126	-	-	-	-	-	126
Leasing commitments	-	1	1	2	10	8	22

40. FINANCIAL INSTRUMENTS (continued)

Liquidity risk – maturity analysis (continued)

	Repayable on demand	Up to three months	More than three months less than six months	More than six months less than one year	More than one year less than five years	More than five years	Total
At 31 December 2010	£m	£m	£m	£m	£m	£m	£m
Liabilities							
Shares	13,641	102	129	1,086	2,879	-	17,837
Deposits, amounts owed to customers and debt securities	50	1,903	109	105	555	845	3,567
Other liabilities and adjustments	-	34	27	51	87	11	210
Cross currency swaps	-	-	-	-	6	1	7
Subordinated liabilities	-	-	-	5	28	83	116
Subscribed capital	-	2	4	6	49	162	223
Total liabilities	13,691	2,041	269	1,253	3,604	1,102	21,960
Undrawn loan facilities	152	-	-	-	-	-	152
Leasing commitments	-	1	1	2	10	10	24

Repayments of shares which are subject to notice are treated as if the notice were to be given immediately. In practice, deposits in the form of fixed bonds, notice accounts, regular savings accounts and some other transactional accounts are held by customers over the longer term and for this reason the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

The tables above exclude cash flows beyond five years (other than the repayment of principal) that relate to subscribed capital.

Capital management

The Group's approach to capital management is detailed in the Directors' Report on pages 15 and 16.

40. FINANCIAL INSTRUMENTS (continued)

Fair values
Set out below is a comparison by category of the carrying amounts and the fair values of all the Group's, and shown separately, the Society's, non-derivative financial instruments.

	Carrying amount 2011	**Fair value 2011**	Carrying amount 2010	Fair value 2010
Group	**£m**	**£m**	£m	£m
Financial assets				
Cash	**1,607.0**	**1,607.0**	1,444.2	1,444.2
Debt securities - Available-for-sale:				
UK Government investment securities	**1,781.4**	**1,781.4**	1,019.4	1,019.4
Analysis of transferable debt securities				
Listed	**786.5**	**786.5**	1,165.2	1,165.2
Unlisted	**278.4**	**278.4**	679.4	679.4
Total	**2,846.3**	**2,846.3**	2,864.0	2,864.0
Loans and advances at amortised cost				
Loans and advances to credit institutions	**388.3**	**388.2**	193.4	193.5
Loans and advances to customers	**19,240.0**	**19,836.5**	17,573.7	18,470.9
Other deposits	**0.5**	**0.5**	30.3	30.3
Total	**19,628.8**	**20,225.2**	17,797.4	18,694.7
Financial liabilities at amortised cost				
Shares	**18,964.1**	**18,782.0**	17,634.3	17,781.5
Deposits, amounts owed to customers and debt securities	**3,947.0**	**4,301.3**	3,528.0	3,588.2
Subordinated liabilities	**68.2**	**92.2**	68.2	91.7
Permanent interest bearing shares	**161.3**	**238.3**	161.3	214.9
Total	**23,140.6**	**23,413.8**	21,391.8	21,676.3

Loans and advances to customers - fair values
The fair value of loans to customers is assessed as the present value of the expected cash flows. Future cash flows are projected using contractual interest payments, contractual repayments and the expected prepayment behaviour of borrowers. Prepayment behaviour includes adjustments that are dependent on the expected future interest rate environment and projected market factors. These cash flows are then discounted using expected future interest rates adjusted with a risk premium to reflect the risk factors inherent in these cash flows.

40. FINANCIAL INSTRUMENTS (continued)

Fair values (continued)

	Carrying amount 2011	**Fair value 2011**	Carrying amount 2010	Fair value 2010
Society	**£m**	**£m**	£m	£m
Financial assets				
Cash	**1,600.1**	**1,600.1**	1,443.8	1,443.8
Debt securities - Available-for-sale:				
UK Government investment securities	**1,781.4**	**1,781.4**	1,019.4	1,019.4
Analysis of transferable debt securities				
Listed	**786.5**	**786.5**	1,165.2	1,165.2
Unlisted	**278.4**	**278.4**	679.4	679.4
Total	**2,846.3**	**2,846.3**	2,864.0	2,864.0
Loans and advances at amortised cost				
Loans and advances to credit institutions	**319.3**	**319.2**	193.4	193.5
Loans and advances to customers	**14,023.0**	**14,287.3**	13,523.7	14,444.8
Other deposits	**0.5**	**0.5**	30.3	30.3
Total	**14,342.8**	**14,607.0**	13,747.4	14,668.6
Financial liabilities at amortised cost				
Shares	**18,964.1**	**18,782.0**	17,634.3	17,781.5
Deposits, amounts owed to customers and debt securities	**3,947.0**	**4,301.3**	3,528.0	3,588.2
Subordinated liabilities	**68.2**	**92.2**	68.2	91.7
Permanent interest bearing shares	**161.3**	**238.3**	161.3	214.9
Total	**23,140.6**	**23,413.8**	21,391.8	21,676.3

Loans and advances to customers - fair values

The fair value of loans to customers is assessed as the present value of the expected cash flows. Future cash flows are projected using contractual interest payments, contractual repayments and the expected prepayment behaviour of borrowers. Prepayment behaviour includes adjustments that are dependent on the expected future interest rate environment and projected market factors. These cash flows are then discounted using expected future interest rates adjusted with a risk premium to reflect the risk factors inherent in these cash flows.

Fair value hierarchy

The Group uses the following hierarchy for determining and disclosing financial instruments which are carried at fair value:

- Level 1: quoted prices in active markets for the same instrument;
- Level 2: quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data; and
- Level 3: valuation techniques for which any significant input is not based on observable market data.

NOTES TO THE ACCOUNTS
(continued)

40. FINANCIAL INSTRUMENTS (continued)

Fair values (continued)

31 December 2011	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m
Financial assets				
Derivative financial instruments				
Interest rate swaps	**-**	**258.6**	**-**	**258.6**
Interest rate caps	**-**	**0.3**	**-**	**0.3**
Interest rate floors	**-**	**0.8**	**-**	**0.8**
Total	**-**	**259.7**	**-**	**259.7**
Debt securities - Available-for-sale:				
UK Government investment securities	**1,781.4**	**-**	**-**	**1,781.4**
Analysis of transferable debt securities				
Listed	**786.5**	**-**	**-**	**786.5**
Unlisted	**-**	**278.4**	**-**	**278.4**
Total	**2,567.9**	**278.4**	**-**	**2,846.3**
Financial liabilities				
Derivative financial instruments				
Interest rate swaps	**-**	**299.8**	**-**	**299.8**
Currency swaps	**-**	**36.2**	**-**	**36.2**
Total	**-**	**336.0**	**-**	**336.0**

31 December 2010				
Financial assets				
Derivative financial instruments				
Interest rate swaps	-	71.2	-	71.2
Interest rate caps	-	0.1	-	0.1
Interest rate floors	-	1.1	-	1.1
Cross currency interest rate swaps	-	1.0	-	1.0
Total	-	73.4	-	73.4
Debt securities - Available-for-sale:				
UK Government investment securities	1,019.4	-	-	1,019.4
Analysis of transferable debt securities				
Listed	1,165.2	-	-	1,165.2
Unlisted	-	679.4	-	679.4
Total	2,184.6	679.4	-	2,864.0
Financial liabilities				
Derivative financial instruments				
Interest rate swaps	-	138.3	-	138.3
Currency swaps	-	1.1	-	1.1
Total	-	139.4	-	139.4

40. FINANCIAL INSTRUMENTS (continued)

Fair values (continued)

Financial instruments recorded at fair value

The following is a description of the determination of fair value for financial instruments which are recorded at fair value using valuation techniques. These incorporate the Group's estimate of assumptions that a market participant would make when valuing the instruments.

- **Level 1 - Financial investments - Available-for-sale**

Market and counterparty prices have been used to determine the fair value of listed debt securities. The fair values of all other instruments have been calculated using valuation models which use discounted cash flow analysis which incorporates observable market data including the use of prevailing interest rates and credit valuation adjustments to discount expected future cash flows.

- **Level 2 - Derivatives**

Derivative products valued using a valuation technique with observable market inputs are interest rate swaps and currency swaps. The valuation techniques applied are swap models using present value calculations. The models incorporate various assumptions including interest rate curves, foreign exchange spot and forward rates, and the credit quality of counterparties.

41. RELATED PARTY TRANSACTIONS

ULTIMATE CONTROLLING PARTY

The Group is controlled by Coventry Building Society registered in England and Wales, which is also considered to be the ultimate parent.

TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL

Transactions with key management personnel are on the same terms and conditions applicable to members and other employees within the Group. The directors are considered to be the only 'key management' for the purposes of the related party transactions disclosures under IAS 24. Key management personnel also incorporates non-executive directors.

In accordance with Section 68 of the Act, the Society maintains a register of loans falling within Section 65 made to directors and connected persons. A statement containing requisite particulars of such transactions may be inspected by members at the Society's AGM or at the Registered Office of the Society during the period 15 days prior to the AGM.

NOTES TO THE ACCOUNTS
(continued)

41. RELATED PARTY TRANSACTIONS (continued)

TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL (continued)

	2011	2010
Aggregate loans and deposits of directors	**£000**	£000
Loans payable by directors to the Society		
Loans outstanding at 1 January	**1,409.8**	1,205.1
Loans issued during the year (including existing loans on appointment as director)	**-**	335.4
Loan repayments during the year (net of interest)	**(174.1)**	(130.7)
Loans outstanding at 31 December	**1,235.7**	1,409.8
Deposits payable by the Society		
Deposits outstanding at 1 January	**2,758.9**	2,290.2
Deposits issued during the year	**1,248.5**	1,424.1
Deposit repayments during the year (net of interest)	**(1,089.4)**	(955.4)
Deposits outstanding at 31 December	**2,918.0**	2,758.9
Net interest income/(expense)		
Interest receivable	**18.3**	28.7
Interest payable	**(47.0)**	(43.4)
Total	**(28.7)**	(14.7)

TRANSACTIONS WITH GROUP COMPANIES

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

	£m	£m
Loans payable to the Society		
Loans outstanding as at 1 January	**7,204.1**	5,313.5
Acquired on transfer of engagements	**-**	575.0
Loans issued during the year	**2,540.7**	1,315.6
Loans outstanding as at 31 December	**9,744.8**	7,204.1
Net interest receivable	**329.9**	231.7
Fees and expenses paid to the Society	**2.7**	1.8

Interest on outstanding loans and deposits accrues at a transfer price rate agreed between the Society and its subsidiaries.

42. NOTES TO THE STATEMENTS OF CASH FLOWS

	Group 2011	Society 2011	Group 2010	Society 2010
	£m	**£m**	£m	£m
Non-cash items included in profit before tax				
Net increase in impairment provisions	**9.9**	**6.3**	11.8	8.9
Depreciation and amortisation	**10.9**	**10.8**	7.3	7.3
Interest on subordinated liabilities	**5.1**	**5.1**	3.9	3.9
Interest on subscribed capital	**12.2**	**12.2**	12.3	12.3
Increase in fair value adjustment of hedged risk	**5.0**	**6.0**	9.0	9.0
Other non-cash movements	**16.7**	**16.7**	(5.5)	(0.5)
Gain on business combinations	**-**	**-**	(43.8)	(70.7)
	59.8	**57.1**	(5.0)	(29.8)
Changes in operating assets				
Decrease in loans to credit institutions and other liquid assets	**111.6**	**111.6**	378.8	378.8
Increase in loans and advances to customers	**(1,676.2)**	**(505.6)**	(1,621.5)	(793.7)
(Increase)/decrease in prepayments and accrued income	**(0.2)**	**(0.2)**	1.5	1.5
(Increase)/decrease in other assets	**(1.0)**	**(1.0)**	5.6	5.5
	(1,565.8)	**(395.2)**	(1,235.6)	(407.9)
Changes in operating liabilities				
Increase in shares	**1,331.5**	**1,331.5**	2,113.2	2,113.2
Decrease in deposits and other borrowings	**(910.6)**	**(910.6)**	(396.7)	(395.9)
Increase/(decrease) in debt securities in issue	**25.4**	**25.4**	(212.9)	(212.9)
Increase in accruals and deferred income	**35.0**	**34.5**	63.9	62.3
Decrease in other liabilities	**(9.1)**	**(4.4)**	(21.8)	(20.1)
	472.2	**476.4**	1,545.7	1,546.6
Cash and cash equivalents				
Cash and balances with the Bank of England (note 18)	**1,591.1**	**1,584.2**	1,427.9	1,427.5
Due from other banks	**387.1**	**318.1**	109.9	109.9
	1,978.2	**1,902.3**	1,537.8	1,537.4

Cash and cash equivalents excludes the balance which the Group is required to maintain with the Bank of England which, at 31 December 2011, amounted to £15.9 million (2010: £16.3 million).

ANNUAL BUSINESS STATEMENT

for the year ended 31 December 2011

1. STATUTORY PERCENTAGES

	2011 %	Statutory limits %
Lending limit	**2.5**	25.0
Funding limit	**17.3**	50.0

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

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

X = business assets, being the total assets of the Group plus loan impairment less liquid assets, intangible assets and property, plant and equipment. The value of X used is the value at 31 December 2011.

Y = the principal value of, and interest accrued on, loans owed to the Group which are fully secured on residential property. The value of Y used is the value at 31 December 2011.

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

X = shares and borrowings, being the aggregate of:

i) the principal value of, and interest accrued on, shares in the Society;

ii) the principal value of, and interest accrued on, the amounts deposited with the Society by banks, credit institutions and other customers; and

iii) the principal value of, and interest accrued on, the amounts of debt securities of the Society.

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

2. OTHER PERCENTAGES

	2011	2010
	%	%
As a percentage of shares and borrowings:		
Gross capital	**4.25**	4.32
Free capital	**4.06**	4.12
Liquid assets	**21.1**	21.4
As a percentage of mean total assets:		
Profit for the financial year	**0.20**	0.42
Management expenses	**0.37**	0.37

The above percentages have been calculated from the Group Accounts.

'Shares and borrowings' represents the total of shares, deposits from banks, other deposits, amounts owed to other customers and debt securities in issue.

'Gross capital' represents the aggregate of reserves, subordinated liabilities and subscribed capital.

'Free capital' represents the aggregate of gross capital and collective impairment less intangible assets and property, plant and equipment.

'Liquid assets' represent the total of cash in hand and balances with the Bank of England, loans and advances to credit institutions, debt securities and other liquid assets.

'Mean total assets' represent the average of the 2011 and 2010 total assets.

'Management expenses' represent the aggregate of administrative expenses, amortisation of intangible assets and depreciation of property, plant and equipment.

3. INFORMATION RELATING TO DIRECTORS AND OTHER OFFICERS

Part 1 - Directors

Name (Date of birth)	Occupation	Other directorships	Date of appointment as a director of the Society
David A Harding, JP, BA, MPhil, FCMA (Chairman) (29.07.1947)	Company Director	Enterprise Inns plc The Royal Mint Limited	01.10.1996
Bridget P Blow (Deputy Chairman) (02.06.1949)	Company Director	Birmingham Hippodrome Limited Birmingham Hippodrome Theatre Trust Limited Bridget Blow Consulting Limited Harvard International plc Kensington Green (Management) Limited Trustmarque Acquisitions Limited Trustmarque Group Limited Trustmarque Intermediary Limited Trustmarque Solutions Limited	01.02.2007
Roger D Burnell, BSc, FCA (08.04.1950)	Company Director	Thomas Cook Group plc Clarence Mansions Management Company Limited	01.09.2008
Colin T Franklin, FCIB (15.06.1955)	Building Society Sales & Marketing Director	Godiva Mortgages Limited Five Valleys Property Company Limited ITL Mortgages Limited	07.07.2009
Ian S Geden, FCII (08.07.1953)	Company Director	The Police Mutual	01.09.2008
John Lowe, BA (Oxon), ACA (26.10.1972)	Building Society Finance Director	Godiva Mortgages Limited Coventry Financial Services Limited Coventry Property Services Limited Godiva Financial Services Limited Godiva Housing Developments Limited Godiva Savings Limited Godiva Securities and Investments Limited Berry Birch & Noble Management Limited (in liquidation) Stroud and Swindon Funding Company Stroud and Swindon Funding Company (No. 2) Limited Coventry Building Society Covered Bonds LLP	14.10.2010
Ian Pickering, MA (Cantab), FCA (16.10.1955)	Company Director	Electrocab Limited Bedford Hospital NHS Trust Member of the Council of Cranfield University Member of the Auditing Practices Board of the Financial Reporting Council Latchways PLC	01.09.2005
Fiona B Smith, LLB (03.01.1959)	Solicitor		01.12.2002
Glyn Smith, MA, (Cantab), FCA (15.09.1952)	Company Director	Covent Garden Market Authority Bournemouth & Poole Teaching PCT Dorset PCT Examiner – ICAEW ITL Mortgages Limited	22.09.2010

3. INFORMATION RELATING TO DIRECTORS AND OTHER OFFICERS (continued)

Part 1 - Directors (continued)

Name (Date of birth)	Occupation	Other directorships	Date of appointment as a director of the Society
David Stewart, BA, ACA (18.08.1965)	Building Society Chief Executive	Godiva Mortgages Limited Coventry Financial Services Limited Coventry Property Services Limited Godiva Financial Services Limited Godiva Housing Developments Limited Godiva Savings Limited Godiva Securities and Investments Limited Stroud and Swindon Funding Company Stroud and Swindon Funding Company (No. 2) Limited Coventry Building Society Covered Bonds LLP Deputy Chair of the Building Societies Association Member of the Council of Mortgage Lenders Chairman's Committee Member of the Council of Mortgage Lenders Executive Committee	11.02.2002

Documents may be served on the above named directors at:
C/O Secretary and General Counsel, Oak Tree Court, Binley Business Park, Harry Weston Road, Coventry CV3 2UN.

In 2006 the Group entered into a service contract with David Stewart (Chief Executive) and is terminable by David Stewart on six months' notice and by the Group on one year's notice.

In 2009 the Group appointed Colin Franklin (Sales and Marketing Director) to the Board. A service contract was entered into which is terminable by Colin Franklin on six months' notice and by the Group on one year's notice.

In 2010 the Group appointed John Lowe (Finance Director) to the Board. A service contract was entered into which is terminable by John Lowe on six months' notice and by the Group on one year's notice.

Part 2 – The Secretary

Name	Occupation	Directorships
Gill Davidson, LLB	Secretary and General Counsel	Wrendale Consulting Limited Coventry Building Society Covered Bonds LLP

Part 3 – Senior management team

Name	Occupation	Directorships
Julian M J Atkins, BSc, MBA, FCIPD, FCIB	Head of Human Resources	
Peter Elcock, ACIB, DipFS, MBA	Chief Risk Officer	Cornhill Consulting Limited
Rachel C Haworth, BA, MCIM	Head of Marketing & Communications	Lyng Hall Trust
Darin J Landon	Head of Sales	
Sally A Wrigglesworth, MBA, ACIB	Head of Customer Service	Arab Horse Society

ANNUAL BUSINESS STATEMENT
(continued)

4. SUBSIDIARIES CARRYING ON BUSINESS

At 31 December 2011 the Society held (directly or indirectly) a 100% beneficial ownership in the following subsidiary companies, incorporated in England and Wales:

	Share capital authorised £	Share capital issued £
Godiva Mortgages Limited	1,000	20
Stroud and Swindon Funding Company	11,745,000	11,741,343
Stroud and Swindon Funding Company (No. 2) Limited	200,000,000	133,641,371
ITL Mortgages Limited	104,000,000	1,473,802
Five Valleys Property Company Limited	99,000,000	1

The Society also has an interest in Coventry Building Society Covered Bonds LLP which gives rise to risks and rewards that are in substance no different than if it was a subsidiary undertaking and therefore is fully consolidated into the Group Accounts. Coventry Building Society Covered Bonds LLP is registered in England and Wales.

5. SUBSIDIARIES NOT CARRYING ON BUSINESS

At 31 December 2011 the Society held shares in the following directly wholly owned subsidiary companies, all of which are incorporated in England and Wales:

	Percentage owned directly by Society %	Share capital issued £
Coventry Financial Services Limited	100	20
Coventry Property Services Limited	100	20
Godiva Financial Services Limited	100	20
Godiva Housing Developments Limited	100	20
Godiva Savings Limited	100	2
Godiva Securities and Investments Limited	100	20

At the same date, the authorised share capital of Godiva Savings Limited was £1,000. The authorised share capital of each of the other subsidiary companies was £100.

6. PRINCIPAL OFFICE

Coventry Building Society is a building society, incorporated and domiciled in the United Kingdom. The address of the registered office is: Economic House, PO Box 9, High Street, Coventry, CV1 5QN.

GLOSSARY

The following glossary defines terminology within the Annual Report & Accounts to assist the reader and to facilitate comparison with publications by other institutions:

Arrears
The financial value of unpaid obligations, which arises when contractual payments are not paid when they fall due.

Available-for-sale reserve
The Available-for-sale reserve contains unrealised gains and losses arising from changes in the fair values of non-derivative financial assets that are categorised as Available-for-sale.

Basel II
The recommendations on banking regulation made by the Basel Committee on Banking Supervision, and implemented in the EU via the Capital Requirements Directive, which came into force on 1 January 2007. The Basel II framework introduced the concept of three 'pillars' for regulation. Pillar 1 sets out the minimum capital requirements for firms, and under Pillar 2 firms will take a view of whether additional capital is required for risks not covered in Pillar 1. Pillar 3 improves market information by requiring firms to publish details of risks and capital management.

Basel III
The Basel Committee on Banking Supervision issued strengthened proposals in response to the recent financial crisis, which are referred to as Basel III. These proposals are a long-term package of changes that are due to commence on 1 January 2013 with an expected transition period running until 2021.

BIPRU
The Prudential sourcebook for Banks, Building Societies and Investment Firms, which sets out the FSA's rules regarding risk, capital and liquidity in particular.

BSA
Building Societies Association (BSA) represents mutual lenders and deposit takers across the UK.

BFSR
Bank Financial Strength Ratings (BFSR) are applied by Moody's Investors Service and reflect their opinion of a financial institution's intrinsic, stand-alone, financial strength relative to all other financial institutions rated by the agency.

Business risk
The risk that the external environment has the potential to affect the Society's business model.

Buy-to-let (BTL) mortgage
A mortgage secured on a residential property that is rented out to tenants.

Charitable donation to Poppy Appeal
Represents the value of the donation made by the Society to The Royal British Legion's Poppy Appeal.

Code Staff
A group of employees to which the FSA's Remuneration Code applies. Code staff consist of executive directors, non-executive directors and certain senior managers in control functions (e.g. human resources, audit, risk and compliance) who could have a material impact on the firm's risk profile.

Council of Mortgage Lenders (CML)
A trade association for the residential mortgage lending industry.

Contractual maturity
The date in the terms of a financial instrument on which the last payment or receipt under the contract is due for settlement.

Core tier 1 capital
Core tier 1 capital comprising general reserves, less intangible assets, pension surplus and other regulatory deductions.

Core tier 1 ratio
Core tier 1 capital as a percentage of risk-weighted assets.

GLOSSARY
(continued)

Covered bonds
Debt securities backed by a portfolio of mortgages that are segregated from the issuer's other assets solely for the benefit of the holders of the covered bonds. The Society issues covered bonds as part of its funding activities.

Credit risk
The risk that the customer or wholesale counterparty is unable to honour their obligations as they fall due.

Currency swap
An arrangement in which two parties exchange specific principal amounts of different currencies at inception and subsequently exchange interest payments on the principal amounts. Often, one party will pay a fixed interest rate, while the other will pay a floating exchange rate (though there are also fixed-fixed and floating-floating arrangements). At the maturity of the swap, the principal amounts are usually re-exchanged.

Debt securities
Transferable instruments creating or acknowledging indebtedness. They include bonds, certificates of deposit and loan notes. The holder of a debt security is typically entitled to the payment of principal and interest, together with other contractual rights under the terms of the issue. Debt securities are generally issued for a fixed term and redeemable by the issuer at the end of that term. Debt securities can be secured on other assets or unsecured.

Deferred tax asset/(liability)
Income taxes recoverable (or payable) in future periods resulting from temporary or timing differences, between the accounting value of assets and liabilities and the tax base of those assets and liabilities.

Defined benefit obligation
The present value of expected future payments required to settle the obligations of a defined benefit plan resulting from past employee service.

Defined benefit plan
Pension or other post-retirement benefit plan offering guaranteed benefits usually as a fraction of the final salary.

Defined contribution plan
Pension or other post-retirement benefit plan where the employer's obligation is limited to its contributions to the fund.

Deposits from banks
Money deposited with the Group by banks and recorded as liabilities. They include money-market deposits, and other short-term deposits.

Derivative financial instrument
A contract or agreement, the value of which reflects changes in an underlying index such as an interest rate, foreign exchange rate or market index. The contract requires either no initial investment, or an initial investment that is smaller than would be required for other types of contracts with a similar response to market factors. The most common types of derivatives are interest rate swaps.

Effective interest rate method (EIR)
The method used to measure the carrying value of a financial asset or a liability. EIR allocates associated interest income or expense to produce a level yield, either to maturity or to the next re-pricing date.

Eurozone
An economic and monetary union (EMU) of 17 EU member states that have adopted the euro (€) as their common currency and sole legal tender.

Exposure
The maximum loss that a financial institution might suffer if a borrower or wholesale counterparty fails to meet their obligations.

Fair value
The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial Services Compensation Scheme (FSCS)
The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the FSA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.

Fitch Ratings
Fitch Ratings is a credit rating agency which provides credit ratings and research covering debt instruments and securities for financial institutions and governments.

Forbearance
Measures to assist customers in financial difficulty. Typically, this involves working with the customer to make arrangements where some element of contractually due amounts are temporarily forgone by the lender. An example would include temporary transfers to interest only.

Foreign currency risk
The risk of loss arising as a result of adverse movements in exchange rates on investments in foreign currencies.

Free capital
The aggregate of gross capital and provisions for collective impairment losses on loans and advances to customers, less; property, plant and equipment, investment properties, non-current assets held for sale and intangible assets.

Financial Services Authority (FSA)
Financial Services Authority (UK) is an independent non-governmental body, given statutory powers by the Financial Services and Markets Act 2000.

Financial Ombudsman Service (FOS)
Financial Ombudsman Service provides an independent and impartial service to resolve individual complaints that consumers and financial institutions have been unable to settle themselves.

General reserve
The general reserve is the accumulation of historic and current year profits and includes actuarial gains and losses on the defined benefit pension plan (net of tax).

Gross capital
The aggregate of equity, subscribed capital and subordinated liabilities.

Gross mortgage lending
New mortgage lending advanced during the year.

IAS
International Accounting Standards. A set of standards stating how particular types of transactions and other events should be reflected in financial statements.

IFRIC
International Financial Reporting Interpretations Committee. IFRIC interpret the application of IASs and IFRSs and provide timely guidance on financial reporting issues not specifically addressed in IASs and IFRSs, in the context of the International Accounting Standards Board framework.

IFRS
International Financial Reporting Standards. A set of international accounting standards stating how particular types of transactions and other events should be reported in financial statements.

Individual Liquidity Adequacy Assessment (ILAA)
The Society's own assessment of the liquidity resources it requires in order to remain within the risk tolerances it has set. This will include an evaluation of potential stresses based on regulatory benchmarks and on Society specific tests.

GLOSSARY
(continued)

Impaired loans
A loan is impaired if there is objective evidence that an impairment event has occurred, and that the event has an impact on the estimated future cash flows of the loan which can be reliably estimated. Impairment may be caused by a single event, or a combination of events.

Impairment provision
Provisions held against impaired assets on the balance sheet. The provisions represent management's best estimate of losses incurred in the loan portfolio at the balance sheet date.

Impairment ratio
Impairment losses on loans and advances to customers as a percentage of average loans and advances to customers.

Individual/collectively assessed loan impairment provisions
Impairment is measured individually for assets that are individually identified as at the balance sheet date as being impaired, and collectively for homogenous asset classes where there is evidence of impairment event(s) but these have not yet manifested themselves as individually identified impaired accounts.

Individual Capital Guidance (ICG)
Guidance from the FSA on the levels of capital to be held by the Society to meet its minimum regulatory capital requirements.

Interest rate risk
The risk that income received or paid is adversely affected by interest rate fluctuations on the Society's mortgage and savings products.

Interest rate swap
A contract under which two counterparties agree to exchange periodic interest payments based on a predetermined notional principal amount.

Internal Capital Adequacy Assessment Process (ICAAP)
The Society's own assessment of the amount of capital that it needs to hold in respect of its regulatory requirements (for credit, market and operational risks) and for other risks. This assessment includes determination of a capital buffer to be held in case of potential economic stress.

Internal ratings-based approach (IRB)
An advanced approach to measuring capital requirements in respect of credit risk under Pillar 1 of Basel II. The IRB approach may only be used with permission from the FSA.

International Accounting Standards Board (IASB)
An independent standard-setting body of the International Accounting Standards Committee Foundation. The members of the IASB are responsible for the development and publication of International Financial Reporting Standards (IFRS) and for approving interpretations of IFRS as developed by the International Financial Reporting Interpretations Committee (IFRIC).

Level 1 fair values
Fair value derived from unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 fair values
Fair value derived from inputs other than quoted prices that are observable for the asset or liability, either directly (i.e. a price) or indirectly (i.e. derived from prices).

Level 3 fair values
Fair value derived from inputs for the asset or liability that are not based on observable market data.

LIBOR
London Inter-Bank Offer Rate. The interest rate at which banks can borrow funds from other banks. The LIBOR is derived from a filtered average of the interbank deposit rates for large loans with maturities between overnight and one full year.

Liquid assets
Assets held in order to be able to generate funds at short notice. This will comprise cash in hand, balances with the Bank of England, debt securities (including gilts), and loans to credit institutions.

Liquidity risk
The risk that the Society cannot meet its financial obligations as they fall due or can secure them only at excessive cost.

Loan to value (LTV)
LTV is the amount of mortgage loan as a percentage of the value of the property.

Management expenses
The aggregate of administrative expenses, depreciation and amortisation.

Market risk
The potential losses or decrease in value of the Group balance sheet as a result of adverse market movements. Specific types of market risk include interest rate risk, foreign exchange risk and house price risk.

Member
A person who has a share investment or a mortgage loan with the Society.

Merger and integration related costs
Primarily consists of costs incurred during 2010 and 2011, relating directly to the merger with Stroud & Swindon Building Society.

Moody's Investor Services
Moody's Investor Services is a credit rating agency which provides credit ratings and research covering debt instruments and securities for financial institutions and governments.

Net interest income
The difference between interest receivable on assets and similar income and interest paid on liabilities and similar charges.

Operational risk
The risk of loss arising from inadequate or failed internal processes, people and systems, or from external events.

Past due
A financial asset such as a loan is past due when the counterparty has failed to make a payment when contractually due.

Permanent interest bearing shares (PIBS)
Unsecured, perpetual deferred shares of the Society offering a fixed coupon. These are a form of Tier 1 capital. PIBS rank behind the claims of all subordinated debt holders, depositors, or creditors of the Society. PIBS are also known as subscribed capital.

Pension fund surplus
The assets in a pension fund that are in excess of its liabilities.

Repo
An agreement to sell a financial security together with a commitment by the seller to repurchase the asset at a specified price on a given date. In substance this forms a secured loan, with the difference between the purchase price and repurchase price being the interest rate.

Retail deposits
Deposits from individuals, not from corporations, other financial institutions or sovereign entities.

Risk appetite
The articulation of the level of risk that the Society is willing to take (or not take) in order to safeguard the interests of the Society's members, whilst also achieving business objectives.

Risk-weighted assets (RWA)
The value of assets, after adjustment to reflect the degree of risk they represent in accordance with the relevant Basel II rules.

GLOSSARY
(continued)

Senior unsecured market
The market for bonds, issued by corporate bodies and financial institutions, which are not secured by any collateral and are not subordinated to any other liabilities of the issuer.

Shares
Funds deposited by a person in a retail savings account with the Society. Such funds are recorded as liabilities of the Society.

Standardised approach
The basic method used to calculate capital requirements for credit risk under Basel II. In this approach the risk-weighting used in the capital calculation are determined by specified percentages.

Subordinated liabilities
Liabilities which, in the event of insolvency or liquidation of the issuer, are subordinated to the claims of depositors and other creditors of the issuer.

Subscribed capital
See permanent interest bearing shares (PIBS).

Tier 1 capital
A component of regulatory capital comprising core tier 1 capital and permanent interest bearing shares (PIBS).

Tier 2 capital
A component of regulatory capital comprising qualifying subordinated debt and eligible collective impairment allowances, less certain regulatory deductions.

Transfer of engagements
Assets and liabilities acquired as a result of the merger with Stroud & Swindon Building Society.

UK Corporate Governance Code (the Code)
Guidance issued by the Financial Reporting Council (formerly known as the Combined Code which was updated in 2010) on a number of key components of effective board practice such as: board leadership, remuneration, accountability and reporting transparency.

Underlying profit
Operating profit after impairments and before exceptional items.

Wholesale funding market
The market for lending and borrowing by large companies, financial institutions and sovereign entities.

the
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TLC not PLC

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