Bank of Scotland plc

Results Announcement

For the year to 31 December 2009

Member of the Lloyds Banking Group

FORWARD LOOKING STATEMENTS

This announcement contains forward looking statements with respect to the business, strategy and plans of Bank of Scotland plc, its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about the Group's or the Group's management's belief and expectations, are forward looking statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. The actual future results of Bank of Scotland plc may differ materially from the results expressed or implied in these forward looking statements as a result of a variety of factors, including, without limitations, UK domestic and global economic and business conditions, the ability to derive cost savings and other benefits as well as to mitigate exposures from the integration with the Lloyds Banking Group, risks concerning borrower credit quality, market related trends and developments, changing demographic trends, changes in customer preferences, changes to regulation, the policies and actions of Governmental and regulatory authorities in the UK or jurisdictions outside the UK, including other European countries and the US, exposure to regulatory scrutiny, legal proceedings or complaints, competition and other factors. Please refer to the rights issue prospectus issued by Lloyds Banking Group plc on 3 November 2009 for a discussion of such factors together with examples of forward looking statements. The forward looking statements contained in this announcement are made as at the date of this announcement, and Bank of Scotland plc undertakes no obligation to update any of its forward looking statements.

CONTENTS

FINANCIAL REVIEW

Results

The consolidated income statement is on page 6 and shows that the loss before tax for the year ended 31 December 2009 is £15,284 million and the loss attributable to equity shareholders is £12,240 million.

Principal activities

Bank of Scotland plc (the 'Bank') together with its subsidiaries (the 'Group') provide a range of banking and financial services through branches and offices in the UK and overseas.

The Group's revenue is earned through interest and fees on a broad range of financial services products including current and savings accounts, personal loans, credit cards and mortgages within the retail market; loans and capital market products to commercial, corporate and asset finance customers; and private banking.

Acquisition of the Group by Lloyds Banking Group plc

On 16 January 2009, Lloyds Banking Group plc acquired 100 per cent of the ordinary share capital of HBOS plc, the Group's parent company.

Business review

The loss before tax increased by £4,649 million or 44 per cent to £15,284 million. The trading surplus increased by 75 per cent or £2,386 million to £5,584 million but is more than offset by the increase in the impairment charge, which reflects the weak credit environment and current economic conditions.

Net interest income decreased by £2,345 million or 27 per cent to £6,195 million as both interest income and interest expense fell in response to the historically low interest rate environment that has prevailed throughout the current year. Other income increased by £4,338 million from £632 million to £4,970 million. During the year, the Bank received a payment of £3,000 million from its fellow banking subsidiary, Lloyds TSB Bank plc, to support the financial and reputational position of the Group and to facilitate the ongoing integration of the Group's banking operations. Net trading income improved by £2,382 million from a loss of £2,938 million to a loss of £556 million, reflecting the inclusion of substantial write-downs associated with the dislocation in financial markets in 2008. The Group's insurance activities have ceased following the sale of St. Andrew's in the last quarter of 2008. Net fee and commission income decreased £483 million or 31 per cent to £1,096 million reflecting lower volumes of new business.

Operating expenses decreased 6 per cent or £356 million to £5,581 million, principally as a result of lower depreciation. This was offset by increased goodwill impairment which increased by £243 million to £385 million. The 2009 charge was principally in respect of Lex Vehicle Leasing Services.

Impairment losses increased by £8,005 million or 66 per cent. This largely represents falls in the values of commercial real estate and the impact of the economic deterioration during the year, including the effects of rising unemployment and reduced corporate cash flows. Significant provisions were required against the Group's Irish and Australian commercial real estate portfolios.

The Group suffered an additional loss of £100 million in 2009 in respect of the disposal of the Australian businesses, BankWest and St. Andrews, in addition to the £845 million loss recorded in 2008.

Loans and advances to customers fell by £48,675 million, or 10 per cent, to £439,538 million reflecting activity undertaken in accordance with the strategy to reduce assets associated with non-relationship lending. Customer accounts decreased by £11,428 million, or 4 per cent, to £265,971 million resulting in a decrease in the customer loans to deposits ratio from 176 per cent at 31 December 2008 to 165 per cent at 31 December 2009.

Loans and advances to banks increased from £12,445 million to £91,259 million and deposits from banks increased from £97,066 million to £174,338 million reflecting transactions with other parts of the Lloyds Banking Group following the acquisition of HBOS plc by Lloyds Banking Group plc in January 2009.

Debt securities in issue decreased by £69,291 million or 37 per cent as some of the maturing debt securities were replaced by deposits by banks as the Group repositioned its funding through transactions with other Lloyds Banking Group subsidiaries.

Shareholders' equity has increased by £10,486 million to £22,147 million as capital injections and gains on available-for-sale assets during the year were significantly greater than the Group's loss for the year.

PRINCIPAL RISKS AND UNCERTAINTIES

At present the most significant risks faced by the Bank are:

Legal and regulatory
Definition: The risk of regulatory action leading to fine and/or public censure and/or successful legal action being taken against the Bank as a result of failure to meet one or more legal and/or regulatory requirements either in the UK or overseas.

Features: The industry is currently subject to a wide range of international and UK consultations on proposals to change the regulatory requirements. For example the Basel Committee on Banking Supervision has issued proposals with respect to capital and liquidity requirements for banks ('Strengthening the resilience of the banking sector' and 'International framework for liquidity risk measurement, standards and monitoring') and proposals have also been issued for new capital requirements for insurance ('Solvency II'). In the UK proposals have been issued for governance, along with discussion papers on recovery and resolution ('Living Wills') arrangements and also potentially conduct of business requirements, all of which could have significant implications for past business as well as future product offerings for customers. There is a high level of uncertainty both as to the financial outcome in terms of specific requirements and the speed of implementation in the UK and internationally.

The Group is currently assessing the impacts of these regulatory proposals. The Group currently meets and exceeds its regulatory capital requirements and expects to continue to do so. However, the FSA could impose more stringent capital and liquidity requirements, and/or introduce new ratios and/or change the manner in which it applies existing requirements to recapitalised banks, including those within the Group. Any one or combination of these events could result in the Group being forced to raise further capital or to divest assets.

The Group has made good preparations for the FSA's new liquidity regime (ILAS) and is ready to meet the reporting implications later in the year.

The Bank's policy is to maintain high levels of compliance with regulatory requirements and it will organise its business to maintain this level of compliance as the requirements become clearer, being mindful of maintaining an appropriate balance between risk and reward.

Credit
Definition: The risk of reductions in earnings and/or value, through financial loss, as a result of the failure of the party with whom the Bank has contracted to meet its obligations (both on and off balance sheet).

Features: Arising from the Bank's lending activities in its Retail, Wholesale and Wealth and International business units. Over the last two years the deteriorating economic outlook, both in the UK and overseas, brought about by the banking crisis has impacted the financial services industry resulting in further high profile losses and write downs. The Bank is impacted by the economic downturn and a further worsening of the business environment could adversely impact earnings.

This poses a major risk to the Bank and its lending to:

Retail customers: where reducing affordability and/or asset values arising from a combination of house price falls; continuing high, or increasing level of unemployment; consumer over indebtedness; and rising interest rates impacts both secured and unsecured retail exposures.

Wholesale customers: where companies are facing increasingly difficult business conditions, resulting in corporate default levels rising and leading to increases in corporate impairment. The Group has exposures in both the UK and internationally, including Ireland, the US, Australia and Spain. There are particular concentrations to financial institutions and in commercial real estate and joint ventures, with high leverage and exposure throughout the capital structure.

The Bank follows a through the economic cycle, relationship based, business model with robust risk management processes, appropriate appetites and experienced staff in place.

Liquidity and funding

Definition: Liquidity risk is defined as the risk that the Bank has insufficient financial resources to meet its commitments as they fall due, or can only secure them at excessive cost. Funding risk is defined as the risk that the Bank does not have sufficiently stable and diverse sources of funding or the funding structure is inefficient.

Features: Arising in the banking business and reflecting the risk that the Bank is unable to attract and retain either retail, wholesale or corporate deposits or issue debt securities. Like all major banks, the Bank is dependent on confidence in the short and longer term wholesale funding markets; should the Bank, due to exceptional circumstances, be unable to continue to source sustainable funding and provide liquidity when necessary, it could impact its ability to fund its financial obligations.

Liquidity risk is managed within a Board approved framework using a range of metrics to monitor the Bank's profile against its stated appetite and potential market conditions.

The key dependencies for successfully funding the Bank's balance sheet include the continued functioning of the money and capital markets at their current levels; successful right sizing of the Group's balance sheet; the continuation of HM Treasury facilities in accordance with the terms agreed, limited further deterioration in the UK's and the Group's credit rating and no significant or sudden withdrawal of deposits resulting in increased reliance on money markets or UK Government support schemes. A return to the extreme market conditions of 2008 would place a strain on the Bank's ability to meet its financial commitments.

Customer treatment

Definition: The risk of regulatory censure and/or a reduction in earnings/value, through financial or reputational loss, from inappropriate or poor customer treatment.

Features: Customer treatment and how the Bank manages its customer relationships affects all aspects of the Bank's operations and is closely aligned with achievement of Lloyds Banking Group's strategic aim – to create deep long lasting relationships with its customers. There is currently a high level of scrutiny regarding the treatment of customers by financial institutions from the press, politicians and regulatory bodies (including the OFT and FSA).

The OFT has said that it still has significant concerns about the operation of the current account market and that it believes changes are required for the market to work in the best interest of consumers. Whilst acknowledging recent and planned improvements by the banks, the OFT expressed its continued concern that unarranged overdraft charges are difficult to understand, not transparent and not subject to effective consumer controls. The OFT is discussing these issues with the banks, consumer groups and other organisations, with the aim of reporting on progress by the end of March 2010.

Treating Customers Fairly remains the key principle underpinning the FSA's consumer protection objective. An additional challenge for the Bank is ensuring the fair treatment of customers during integration of the two heritage businesses. As a result the customer relationship management risks posed by integration are carefully considered through the integration governance process in place. If the Bank is unable to demonstrate the fair treatment of its customers there is the risk of increased complaints from customers, the potential for regulatory action (which could include reviews of past business and/or the payment of fines and compensation) and adverse media coverage (leading to reputational damage in the marketplace).

The Bank has policies, procedures and governance arrangements in place to facilitate the fair treatment of customers.

People

Definition: The risk of reduction in earnings and/or value, through financial or reputational loss, from failure to retain, train, reward, recruit and incentivise appropriately skilled staff, inappropriate staff behaviour or industrial action.

Features: The delivery of the Bank's objectives is underpinned by the ability to attract, retain and develop the best talent in the industry. The challenges to the people agenda have never been greater with increased regulatory and public interest in remuneration practices, the effects of the Government shareholding and the impacts of integration. The Bank welcomes the regulation of remuneration provided there is an international consensus and we will comply with the FSA code. We have successfully managed the initial stages of integration, working at pace to establish control by defining and implementing the new organisational structures and we continue to proactively manage the relationship with our colleagues and unions during this period of change. The Bank has policies, procedures and governance arrangements in place to ensure the effective management of people risk as we integrate and grow our business. The Lloyds Banking Group has published proposals to harmonise employee terms and conditions including action to restrict the benefit to long-term employees of the legacy defined benefit schemes. The Bank actively manages its relationships with unions, but is aware of the danger of industrial action, business disruption and reputational impact arising from union behaviour and communications. People risk is closely monitored as a key risk indicator, as well as being subject to oversight by the Board.

Integration

Definition: The risk that the Bank fails to realise the business growth opportunities, revenue benefits, cost synergies, operational efficiencies and other benefits anticipated from, or incurs unanticipated costs and losses associated with integration with Lloyds Banking Group plc.

Features: The integration of the Bank with Lloyds Banking Group plc presents one of the largest integration challenges that has been seen in the UK financial services industry. There is a risk that the Bank may fail to realise the business growth opportunities, revenue benefits, cost synergies, operational efficiencies and other benefits anticipated from the acquisition of HBOS plc by Lloyds Banking Group plc, or may incur unanticipated costs and losses associated as a result. As a consequence, the Bank results may suffer as a result of operational, financial management and other integration risks.

The risk of failure to deliver synergy benefits or publicly stated targets could potentially result in a loss of shareholder or market confidence with negative perceptions of the Lloyds Banking Group's integration strategy. As we go through the integration process there is a danger of losing key staff potentially impacting on integration.

Lloyds Banking Group has created an integration executive board, chaired by the Group operations director, to oversee the integration process. The interests of the Bank are considered at this forum. We are now one year into the integration programme and have a fully developed and functioning governance framework to manage these risks, with clear understanding of the dependencies and phased deliverables through to 2012.

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2009

	Note	**2009** **£ million**	2008 (restated)[1] £ million
Interest and similar income		**19,060**	36,093
Interest and similar expense		**(12,865)**	(27,553)
Net interest income		**6,195**	8,540
Fee and commission income		**1,304**	1,961
Fee and commission expense		**(208)**	(382)
Net fee and commission income		**1,096**	1,579
Net trading income		**(556)**	(2,938)
Insurance premium income		**–**	215
Subvention income		**3,000**	–
Other operating income		**1,430**	1,776
Other income	4	**4,970**	632
Total income		**11,165**	9,172
Insurance claims		**–**	(37)
Total income, net of insurance claims		**11,165**	9,135
Operating expenses	5	**(5,581)**	(5,937)
Trading surplus		**5,584**	3,198
Impairment	6	**(20,055)**	(12,050)
Share of results of joint ventures and associates		**(713)**	(938)
Loss on sale of businesses	7	**(100)**	(845)
Loss before tax		**(15,284)**	(10,635)
Taxation	8	**3,057**	2,448
Loss for the year		**(12,227)**	(8,187)

Profit attributable to minority interests		**13**	51
Loss attributable to equity shareholders		**(12,240)**	(8,238)
Loss for the year		**(12,227)**	(8,187)

[1] See note 22.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2009

	2009 £ million	2008 (restated)[1] £ million
Loss for the year	**(12,227)**	(8,187)
Other comprehensive income:		
Movements in revaluation reserve in respect of available-for-sale financial assets, net of tax:		
Change in fair value	**1,877**	(5,897)
Transferred to income statement in respect of disposals	**2**	(17)
Transferred to income statement in respect of impairment	**446**	915
	2,325	(4,999)
Movement in cash flow hedging reserve, net of tax:		
Effective portion of changes in fair value taken to other comprehensive income	**(442)**	(2,801)
Net gains transferred to the income statement	**645**	1,844
	203	(957)
Currency translation differences, net of tax	**9**	95
Other comprehensive income for the year, net of tax	**2,537**	(5,861)
Total comprehensive income for the year	**(9,690)**	(14,048)
Total comprehensive income attributable to minority interests	**13**	51
Total comprehensive income attributable to equity shareholders	**(9,703)**	(14,099)
Total comprehensive income for the year	**(9,690)**	(14,048)

(1) See note 22.

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2009

	Note	**31 December 2009**	31 December 2008 (restated)[1]	1 January 2008 (restated)[1]
		£ million	£ million	£ million
Assets				
Cash and balances at central banks		**2,905**	2,502	2,944
Items in course of collection from banks		**534**	445	945
Trading and other financial assets at fair value through profit or loss	9	**27,867**	23,430	55,789
Derivative financial instruments		**30,222**	50,517	13,794
Loans and receivables:				
Loans and advances to banks		**91,259**	12,445	4,095
Loans and advances to customers	10	**439,538**	488,213	485,201
Debt securities		**31,211**	38,878	527
		562,008	539,536	489,823
Available-for-sale financial assets		**21,565**	28,035	49,980
Investment properties		**30**	43	34
Investments in joint ventures and associates		**423**	1,193	1,739
Goodwill		**376**	667	1,041
Other intangible assets		**91**	108	110
Tangible fixed assets		**4,903**	5,527	6,300
Current tax recoverable		**745**	865	–
Deferred tax assets		**5,153**	3,182	–
Other assets		**4,522**	3,126	6,067
Total assets		**661,344**	659,176	628,566

[1] See note 22.

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2009

	Note	**31 December 2009 £ million**	31 December 2008 (restated)[1] £ million	1 January 2008 (restated)[1] £ million
Equity and liabilities				
Liabilities				
Deposits from banks		**174,338**	97,066	41,513
Customer accounts		**265,971**	277,399	297,621
Items in course of transmission to banks		**495**	521	542
Trading and other financial liabilities at fair value through profit or loss		**27,372**	18,851	22,552
Derivative financial instruments		**27,452**	40,827	12,160
Notes in circulation		**981**	957	1,034
Debt securities in issue	13	**119,157**	188,448	206,520
Liabilities arising from insurance contracts and participating investment contracts		**–**	–	24
Liabilities arising from non-participating investment contracts		**–**	–	98
Other liabilities		**6,291**	4,235	4,912
Current tax liabilities		**3**	23	728
Deferred tax liabilities		**–**	–	965
Other provisions		**247**	145	172
Subordinated liabilities	14	**16,684**	18,779	17,881
Total liabilities		**638,991**	647,251	606,722
Equity				
Share capital	15	**5,847**	1,324	499
Share premium account	15	**26,684**	11,018	6,343
Other reserves	16	**(2,094)**	(4,694)	1,167
Retained profits		**(8,290)**	4,013	13,479
Shareholders' equity		**22,147**	11,661	21,488
Minority interests		**206**	264	356
Total equity		**22,353**	11,925	21,844
Total equity and liabilities		**661,344**	659,176	628,566

(1) See note 22.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2009

	Attributable to equity shareholders					
	Share capital and premium £ million	Other reserves £ million	Retained profits £ million	Total £ million	Minority interests £ million	Total £ million
Balance as at 1 January 2008	6,842	1,167	13,479	21,488	356	21,844
Total comprehensive income	–	(5,861)	(8,238)	(14,099)	51	(14,048)
Dividends	–	–	(1,228)	(1,228)	(43)	(1,271)
Issue of ordinary and preference shares	5,500	–	–	5,500	–	5,500
Repayment of capital to minority shareholders	–	–	–	–	(100)	(100)
Balance as at 31 December 2008	**12,342**	**(4,694)**	**4,013**	**11,661**	**264**	**11,925**
Total comprehensive income	**–**	**2,537**	**(12,240)**	**(9,703)**	**13**	**(9,690)**
Dividends	**–**	**–**	**–**	**–**	**(12)**	**(12)**
Issue of ordinary and preference shares	**20,189**	**–**	**–**	**20,189**	**–**	**20,189**
Capital redemption reserve	**–**	**63**	**(63)**	**–**	**–**	**–**
Extinguishment of minority interest	**–**	**–**	**–**	**–**	**(59)**	**(59)**
Balance as at 31 December 2009	**32,531**	**(2,094)**	**(8,290)**	**22,147**	**206**	**22,353**

CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2009

	2009	2008 (restated)[1]
	£ million	£ million
Loss before tax	**(15,284)**	(10,635)
Adjustments for:		
Change in operating assets	**45,204**	(73,045)
Change in operating liabilities	**911**	33,318
Non-cash and other items	**24,760**	16,143
Tax received (paid)	**374**	(1,061)
Net cash provided by (used in) operating activities	**55,965**	(35,280)
Cash flows from investing activities		
Purchase of available-for-sale financial assets	**10,935**	55,637
Proceeds from sale and maturity of available-for-sale financial assets	**(15,760)**	(18,238)
Purchase of fixed assets	**(188)**	(565)
Proceeds from sale of fixed assets	**54**	587
Acquisition of businesses, net of cash acquired	**(279)**	(454)
Disposal of businesses, net of cash disposed	**137**	1,224
Net cash provided by (used in) investing activities	**(5,101)**	38,191
Cash flows from financing activities		
Dividends paid to equity shareholders	**–**	(1,228)
Dividends paid to minority interests	**(12)**	(43)
Interest paid on subordinated liabilities	**(816)**	(1,323)
Proceeds from issue of subordinated liabilities	**–**	3,000
Proceeds from issue of ordinary shares	**20,189**	5,500
Repayment of subordinated liabilities	**(1,781)**	(3,405)
Minority interest acquired	**–**	242
Repayment of capital to minority shareholders	**(59)**	(353)
Net cash provided by financing activities	**17,521**	2,390
Effects of exchange rate changes on cash and cash equivalents	**39**	(245)
Change in cash and cash equivalents[2]	**68,424**	5,056
Cash and cash equivalents at beginning of year	**7,967**	2,911
Cash and cash equivalents at end of year	**76,391**	7,967

Cash and cash equivalents comprise cash and balances at central banks (excluding mandatory deposits) and amounts due from banks with a maturity of less than three months.

(1) Following the reclassification of the Group balance sheet to align the presentation with the presentation practices adopted by Lloyds Banking Group plc (as detailed in note 22) the cash flow statement has been represented on a basis consistent with the reclassified balance sheet.

(2) Mandatory reserve deposits of £373 million at 1 January 2008 have been reclassified from loans and advances to banks to cash and balances at central banks. In addition, total cash and cash equivalents at 1 January 2008 have been restated to include certain cash deposits held with the Central Bank of Ireland of £853 million and cash held at the central bank as collateral against notes in circulation of £881 million which are available to finance the Group's day to day operations. The cash flow statement has been adjusted accordingly.

NOTES

1. Basis of preparation

The global upheaval in the financial markets that occurred during 2008 has abated during the latter part of 2009. The steps taken in 2008 by HM Treasury through the introduction of the Government Guarantee Scheme for senior funding and the Bank of England through various facilities have together continued to provide assurance of liquidity support to the banking markets. Notwithstanding the improvement in market liquidity during 2009, Lloyds Banking Group continues to be reliant upon these facilities in order to maintain its wholesale funding position. The Bank is dependent upon its ultimate parent, Lloyds Banking Group plc and its fellow subsidiary undertaking, Lloyds TSB Bank plc to provide capital and funding.

During the year, Lloyds Banking Group has taken steps to strengthen the Bank's capital position in order to provide a buffer against further shocks arising from the economic environment.

Based upon projections prepared by management, which take into account the funding needs of the Lloyds Banking Group as a whole and which assume that the Government sponsored facilities will continue to be available, the directors are satisfied that the Bank has adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements of the Group have been prepared on a going-concern basis.

2. Accounting policies and presentation

These financial statements as at and for the year to 31 December 2009 have been prepared in accordance with the Listing Rules of the Financial Services Authority relating to Preliminary Results. They do not include all of the information that will be included in the full annual financial statements. The Group's consolidated financial statements as at and for the year ended 31 December 2009 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. Copies of the 2009 annual report and accounts will be published on the Lloyds Banking Group's website, www.lloydsbankinggroup.com, or are available upon request from the Group Secretariat, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN.

Accounting policies

There have been no significant changes to the accounting policies applied to these consolidated financial statements compared to those applied by the Group in its 2008 annual report and accounts.

The following new IFRS pronouncements relevant to the Group have been adopted in these consolidated financial statements:

(i) *IAS 1 (revised), 'Presentation of Financial Statements'.* The revised standard prohibits the presentation of items of income and expense (that is 'non-owner changes in equity') in the statement of changes in equity, requiring 'non-owner changes in equity' to be presented separately from owner changes in equity. All non-owner changes in equity are required to be shown in a performance statement. Entities can choose whether to present one performance statement (the statement of comprehensive income) or two statements (the income statement and statement of comprehensive income). The Group has elected to present two statements: an income statement and a statement of comprehensive income. The financial statements have been prepared under the revised disclosure requirements; the application of this revised standard which affects presentation only, has not had any impact on amounts recognised in these financial statements.

2. Accounting policies and presentation (continued)

(ii) *Amendments to IFRS 7 'Financial Instruments: Disclosures – Improving Disclosures about Financial Instruments'.* The amendment requires enhanced disclosures about fair value measurement and liquidity risk in the financial statements. In particular, the amendment requires disclosure of fair value measurements by level of a fair value measurement hierarchy. As the amendments only result in additional disclosures, the amendments have not had any impact for amounts recognised in these financial statements.

(iii) *IFRS 8 'Operating Segments'.* This new standard replaces IAS 14 'Segment Reporting' and requires that the financial statements include financial and descriptive information about operating segments which are based on how financial information is reported and evaluated internally. The chief operating decision maker for the Group has been identified as the Group Executive Committee (GEC). The Group is managed on the entity basis and not by segment, and consequently the GEC does not assess performance or allocate resources on a segmental basis; accordingly no segmental information is provided. A brief overview of the Group's sources of income is provided in the Financial Review.

The ultimate parent undertaking, Lloyds Banking Group plc, produces consolidated accounts which set out the basis of the segments through which it manages performance and allocates resources across the consolidated Lloyds Banking Group.

Presentation

The presentation of the Group's income statement and balance sheet have been conformed to the presentation adopted by Lloyds Banking Group. Comparatives have been reclassified to conform to the revised presentation (note 22).

3. Critical accounting estimates and judgements

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions in applying the accounting policies that affect the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, actual results reported in future periods may be based upon amounts which differ from those estimates. Estimates, judgements and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

With the exception of the matter described below, the nature of the significant judgements made by management in applying the accounting policies, and the key sources of estimation uncertainty applied by the Group in these financial statements are the same as those applied by the Group in its 2008 annual report and accounts.

The Group accounts for its revenue on loans and receivables on an effective interest rate basis. This approach takes into account interest received or paid and fees and commission paid or received that are integral to the yield as well as incremental transaction costs and all other premiums and discounts. Following the acquisition of HBOS plc, of which Bank of Scotland plc is its principal banking subsidiary, by Lloyds Banking Group plc on 16 January 2009, the Group reviewed the effective interest rate methodology applied to the Group's mortgage portfolio. As a result of this methodology review, the Group has revised the period over which the fees, commissions and costs are spread into the yield. This change in accounting estimate has resulted in an additional charge to the income statement of £945 million in the year to 31 December 2009.

4. Other income

	2009 £m	2008 £m
Fee and commission income:		
Current account fees	**329**	361
Insurance broking	**239**	254
Card and debit card fees	**212**	253
Other fees and commissions	**524**	1,093
	1,304	1,961
Fees and commission expense	**(208)**	(382)
Net fee and commission income	**1,096**	1,579
Net trading income	**(556)**	(2,938)
Insurance premium income	**–**	215
Subvention income	**3,000**	–
Other operating income	**1,430**	1,776
Total other income	**4,970**	632

During the year the Bank received a payment of £3,000 million from its fellow banking subsidiary, Lloyds TSB Bank plc, to support its financial and reputational position and to facilitate the ongoing integration of the Group’s banking operations.

5. Operating expenses

	2009 £m	2008 £m
Administrative expenses:		
Staff	**2,647**	2,710
Premises and equipment	**412**	478
Other expenses	**1,044**	1,065
	4,103	4,253
Depreciation and amortisation:		
Tangible assets	**1,068**	1,508
Intangible assets	**25**	34
	1,093	1,542
Goodwill impairment	**385**	142
Total operating expenses	**5,581**	5,937

The goodwill impairment charge of £385 million includes the write-down, triggered primarily by deteriorating economic conditions, of the goodwill arising on the acquisition of Lex Vehicle Leasing Services (£265 million).

6. Impairment

	2009 £m	2008 £m
Impairment losses on loans and receivables:		
Loans and advances to customers	**18,231**	9,857
Debt securities and classified loans and receivables	**1,199**	923
	19,430	10,780
Impairment of available-for-sale financial assets	**620**	1,270
Other credit risk provisions	**5**	–
Total impairment charged to the income statement	**20,055**	12,050

7. Loss on sale of businesses

	2009 £m	2008 £m
Loss on the sale of Bank of Western Australia Limited and St. Andrews Australia Pty Limited	**(100)**	(845)

On 8 October 2008 the Group agreed the sale of part of its Australian operations, principally Bank of Western Australia Limited and St Andrews Australia Pty Limited, to Commonwealth Bank of Australia Limited. The sale completed on 19 December 2008 and resulted in an estimated pre-tax loss on disposal of £845 million (including goodwill written-off of £240 million). The agreement provided for adjustments to the consideration received in certain circumstances and as a result a further loss of £100 million has been recognised in the current year.

8. Taxation

A reconciliation of the credit that would result from applying the standard UK corporation tax rate to the loss before tax to the tax credit is given below:

	2009 £m	2008 £m
Loss before tax	**(15,284)**	(10,635)
Tax credit thereon at UK corporation tax rate of 28.0% (2008: 28.5%)	**4,279**	3,031
Factors affecting credit:		
Goodwill impairment	**(110)**	(26)
Disallowed and non-taxable items	**(41)**	(64)
Overseas tax rate differences	**(428)**	(83)
Gains exempted or covered by capital losses	**(16)**	102
Adjustments in respect of previous periods	**45**	166
Impairment of financial instruments	**43**	(52)
Reduction in deferred tax from changes in tax rates	**–**	(10)
Effect of profit or loss in joint ventures and associates	**(196)**	(268)
Tax losses where no deferred tax provided	**(484)**	(310)
Other items	**(35)**	(38)
Tax credit	**3,057**	2,448

9. Trading and other financial assets at fair value through profit or loss

	2009 £m	2008 £m
Trading assets	**27,611**	22,571
Other financial assets at fair value through profit or loss:		
Debt securities	**4**	563
Equity shares	**252**	296
	256	859
	27,867	23,430

10. Loans and advances to customers

	2009 £m	2008[1] (restated) £m
Agriculture, forestry and fishing	**772**	854
Energy and water supply	**1,129**	890
Manufacturing	**6,836**	7,436
Construction	**11,169**	11,456
Transport, distribution and hotels	**21,496**	22,664
Postal and telecommunications	**1,449**	958
Property companies	**65,144**	63,807
Financial, business and other services	**72,076**	92,988
Personal:		
Mortgages	**252,745**	263,644
Other	**19,518**	23,854
Lease financing	**4,990**	5,655
Hire purchase	**3,486**	4,700
	460,810	498,906
Allowance for impairment losses on loans and advances (note 11)	**(21,272)**	(10,693)
Total loans and advances to customers	**439,538**	488,213

[1] Following the acquisition of the Group by Lloyds Banking Group, the industry classification of loans and advances has been aligned to a basis consistent with the presentation practices adopted by Lloyds Banking Group, and comparatives have been restated accordingly.

Loans and advances to customers include advances securitised under the Group's securitisation and covered bonds programmes. Further details are given in note 12.

11. Allowance for impairment losses on loans and receivables

	2009 £m	2008 £m
Balance at 1 January	**11,616**	3,373
Exchange and other adjustments	**(10)**	135
Advances written off	**(7,494)**	(2,515)
Recoveries of advances written off in previous years	**36**	107
Unwinding of discount	**(391)**	(149)
Charge to the income statement in the year (note 6)	**19,430**	10,780
Disposal of subsidiary undertakings	**–**	(115)
Balance at 31 December	**23,187**	11,616
Loans and advances to customers	**21,272**	10,693
Debt securities classified as loans and receivables	**1,915**	923
Balance at 31 December	**23,187**	11,616

12. Securitisation and covered bonds

The Group's principal securitisation and covered bonds programmes, together with the balances of the advances subject to notes in issue at 31 December, are listed below.

		As at 31 December 2009		As at 31 December 2008[1]	
		Gross assets securitised £m	**Notes in issue £m**	Gross assets securitised £m	Notes in issue £m
Securitisation	*Type of asset*				
Permanent	UK residential mortgages	**38,915**	**31,878**	38,602	38,490
Balliol	UK residential mortgages	**12,771**	**12,819**	12,701	12,549
Pendeford	UK residential mortgages	**12,240**	**9,174**	12,894	9,870
Trinity	UK residential mortgages	**11,033**	**11,466**	12,975	12,638
Mound	UK residential mortgages	**8,779**	**7,153**	10,147	8,238
Picard	US residential mortgage backed securities	**7,897**	**7,897**	–	–
Brae	UK residential mortgages	**7,838**	**9,588**	9,213	9,955
Deva	UK residential mortgages	**6,691**	**6,906**	6,747	6,703
Wolfhound	Irish residential mortgages	**6,522**	**6,585**	4,083	4,107
Penarth	Credit card receivables	**5,155**	**2,699**	4,189	2,633
Candide	Dutch residential mortgages	**4,812**	**4,834**	5,569	5,704
Dakota	UK residential mortgages	**3,832**	**3,826**	3,988	3,885
Handbridge	Personal loans	**3,730**	**2,613**	–	–
Tioba	UK residential mortgages	**2,094**	**2,249**	2,647	2,568
Prominent	Commercial loans	**928**	**976**	1,053	1,149
Bella	Motor vehicle loans	**443**	**470**	–	–
Other	UK residential mortgages	**64**	**169**	68	179
		133,744	**121,302**	124,876	118,668
Less held by the Group			**(87,359)**		(75,960)
Total securitisations			**33,943**		42,708
Covered bonds					
Residential mortgage-backed covered bonds		**61,537**	**49,644**	51,756	49,408
Social housing loan-backed covered bonds		**3,407**	**2,976**	3,475	2,919
		64,944	**52,620**	55,231	52,327
Less held by the Group			**(23,060)**		(18,305)
Total covered bonds			**29,560**		34,022
Total securitisations and covered bonds			**63,503**		76,730

[1] Following the acquisition of the Group by Lloyds Banking Group, the presentation of gross securitised assets and notes in issue has been aligned to a basis consistent with the presentation practices adopted by Lloyds Banking Group and comparatives have been represented accordingly.

12. Securitisation and covered bonds (continued)

Securitisation

Loans and advances to customers and debt securities classified as loans and receivables include advances securitised under the Group's securitisation programmes, the majority of which have been sold by subsidiary companies to bankruptcy remote special purpose entities (SPEs). As the SPEs are funded by the issue of debt on terms whereby some of the risks and rewards of the portfolio are retained by the subsidiary, the SPEs are consolidated fully and all of these advances are retained on the Group's balance sheet, with the related notes in issue included within debt securities in issue. In addition to the SPEs detailed above the Group sponsors two conduit programmes, Grampian and Landale.

Covered bonds

Certain loans and advances to customers have been assigned to bankruptcy remote limited liability partnerships to provide security to issues of covered bonds by the Group. The Group retains all of the risks and rewards associated with these loans and the partnerships are consolidated fully and the loans retained on the Group's balance sheet, and the related covered bonds in issue included within debt securities in issue.

Cash deposits of £24,271 million (31 December 2008: £12,423 million) held by the Group are restricted in use to repayment of the debt securities issued by the SPEs, covered bonds issued by Bank of Scotland plc and other legal obligations.

In total the Group has securitised £124,088 million (31 December 2008: £97,363 million) of mortgage assets under certain securitisation and covered bond programmes and purchased all of the loan notes in issue relating to those issuances for £110,419 million (31 December 2008: £94,265 million). These transactions do not lead to any derecognition of the assets as the Group has retained all of the risks and rewards associated with the loan notes.

13. Debt securities in issue

	2009 **£m**	2008 £m
Medium term notes	**36,455**	48,630
Covered bonds (note 12)	**29,560**	34,022
Certificates of deposits	**6,413**	50,956
Securitisation notes (note 12)	**33,943**	42,708
Commercial paper	**12,786**	12,132
	119,157	188,448

All debt securities in issue are held at amortised cost.

Included within commercial paper above is £9,330 million (2008: £2,979 million) issued by the Grampian conduit and £138 million (2008: £nil million) issued by the Landale conduit.

14. Subordinated liabilities

	2009 £m	2008 £m
Preference shares	**800**	1,227
Preferred securities	**403**	403
Undated subordinated liabilities	**5,565**	5,948
Dated subordinated liabilities	**9,916**	11,201
	16,684	18,779

During the year, the Group was involved in a number of transactions which were designed to improve the overall capital structure of the Lloyds Banking Group. The Group redeemed undated subordinated notes in return for the issue of unsecured notes and also redeemed undated subordinated notes in return for the issue of innovative tier 1 securities. These exchanges resulted in a gain of £63 million.

The Group also redeemed two issues of preference shares in exchange for the issue of ordinary shares to its immediate parent, HBOS plc. This transaction gave rise to the transfer of £63 million from the Bank's distributable reserves to the capital redemption reserve (see note 16).

15. Share capital and premium

	Share capital £m	**Share premium £m**
At 1 January 2009	1,324	11,018
Ordinary shares issued in year	**4,523**	**15,666**
At 31 December 2009	**5,847**	**26,684**

16. Other reserves

	Merger and other reserves £m	Capital redemption reserve £m	Foreign currency translation reserve £m	Cashflow hedging reserve £m	Available for sale reserve £m	Total other reserves £m
At 1 January 2009	1,600	–	83	(1,042)	(5,335)	(4,694)
Redemption of preference shares		**63**	**–**	**–**	**–**	**63**
Change in fair value of hedging derivatives	**–**	**–**	**–**	**(613)**	**–**	**(613)**
Income statement transfer	**–**	**–**	**–**	**895**	**–**	**895**
Deferred tax thereon	**–**	**–**	**–**	**(79)**	**–**	**(79)**
Change in fair value of available-for-sale financial assets	**–**	**–**	**–**	**–**	**2,550**	**2,550**
Disposals	**–**	**–**	**–**	**–**	**3**	**3**
Impairment	**–**	**–**	**–**	**–**	**620**	**620**
Deferred tax thereon	**–**	**–**	**–**	**–**	**(848)**	**(848)**
Exchange and other adjustments	**–**	**–**	**(29)**	**–**	**38**	**9**
Total comprehensive income	**–**	**–**	**(29)**	**203**	**2,363**	**2,537**
At 31 December 2009	**1,600**	**63**	**54**	**(839)**	**(2,972)**	**(2,094)**

17. Contingent liabilities and commitments

	2009 £m	2008 restated[1] £m
Contingent liabilities		
Acceptances and endorsements	**5**	–
Other:		
Other items serving as direct substitutes	**99**	73
Performance bonds and other transaction-related contingencies	**1,251**	1,279
	1,350	1,352
Total contingent liabilities	**1,355**	1,352
Commitments		
Documentary credits and other short-term trade related transactions	**69**	137
Undrawn formal standby facilities, credit lines and other commitments to lend:		
Mortgage offers	**6,188**	11,847
Other commitments	**30,130**	38,364
	36,318	50,211
1 year or over original maturity	**17,665**	26,341
Total commitments	**54,052**	76,689

[1] Following the acquisition of the Group by Lloyds Banking Group, the presentation of financial guarantees has been aligned to our basis consistent with the presentation practices adopted by Lloyds Banking Group, and comparatives have been reclassified accordingly.

18. Reclassification of financial assets

In January 2009, the Group reclassified £1,825 million of debt securities classified as held for trading to debt securities classified as loans and receivables on the basis that there was no longer an active market for those assets, which are therefore more appropriately managed as loans. During the year impairment losses of £110 million have been charged to the income statement. If these assets had not been reclassified during the period an additional loss before tax of £13 million would have been recognised in the income statement.

In January 2009, the Group reclassified £649 million of securities classified as available-for-sale to debt securities classified as loans and receivables on the basis that there was no longer an active market for those assets, which are therefore more appropriately managed as loans. If these assets had not been reclassified during the period an additional negative adjustment of £70 million would have been recognised in the available-for-sale reserve.

19. Legal and regulatory matters

Payment Protection Insurance

In January 2009, the UK Competition Commission (the ‘Competition Commission’) completed its formal investigation into the supply of Payment Protection Insurance (PPI) services (except store card PPI) to non-business customers in the UK and published its final report on setting out its remedies. The Competition Commission decided to adopt various remedies including a prohibition on the active sale of PPI by a distributor to a customer within 7 days of the distributor’s sale of credit to that customer.

On 30 March 2009, Barclays Bank plc lodged an appeal in the UK Competition Appeal Tribunal (the ‘Competition Appeal Tribunal’) against the Competition Commission’s findings. Lloyds Banking Group, the ultimate parent undertaking of the Bank, was granted permission by the Competition Appeal Tribunal to intervene in the appeal. The Competition Appeal Tribunal handed down its judgment on 16 October 2009 finding in favour of Barclays in respect of its challenge to the Competition Commission’s prohibition of distributors selling PPI at the credit point of sale but it did not uphold Barclays’ challenge to the Competition Commission’s findings on market definition. The matter has now been referred back to the Competition Commission. This may or may not result in the Competition Commission ultimately reaching a different conclusion.

On 1 July 2008 the Financial Ombudsman Service referred concerns regarding the handling of PPI complaints to the FSA as an issue of wider implication. The Lloyds Banking Group has been working with other industry members and trade associations in preparing an industry response to address regulatory concerns regarding the handling of PPI complaints. On 29 September 2009, the FSA issued a consultation paper on PPI complaints handling. The FSA has escalated its regulatory activity in relation to past PPI sales generally and has proposed new guidance on the fair assessment of a complaint and the calculation of redress and a new rule requiring firms to reassess historically rejected complaints.

The statement on 29 September 2009 also announced that several firms had agreed to carry out reviews of past sales of single premium loan protection insurance. The Lloyds Banking Group has subsequently agreed in principle that it will undertake a review in relation to sales of single premium loan protection insurance made through its branch network since 1 July 2007. The precise details of the review are still being discussed with the FSA. The ultimate impact on the Group of any review and/or reassessment can only be known at the conclusion of these discussions and on publication of the FSA’s final rules.

Interchange fees

The European Commission has adopted a formal decision finding that an infringement of European Commission competition laws has arisen from arrangements whereby MasterCard issuers charged a uniform fallback interchange fee in respect of cross-border transactions in relation to the use of a MasterCard or Maestro branded payment card. The European Commission has required that the fee be reduced to zero for relevant cross-border transactions within the European Economic Area. This decision has been appealed to the General Court of the European Union (the ‘General Court’). Bank of Scotland plc and Lloyds TSB Bank plc (along with certain other MasterCard issuers) have successfully applied to intervene in the appeal in support of MasterCard’s position that the arrangements for the charging of a uniform fallback interchange fee are compatible with European Commission competition laws. Meanwhile, the European Commission and the UK’s OFT are pursuing investigations with a view to deciding whether arrangements adopted by other payment card schemes for the levying of uniform fallback interchange fees in respect of domestic and/or cross-border payment transactions also infringe European Commission and/or UK competition laws.

19. Legal and regulatory matters (continued)

As part of this initiative the OFT will also intervene in the General Court appeal supporting the European Commission's position. The ultimate impact of the investigations on the Group can only be known at the conclusion of these investigations and any relevant appeal proceedings.

Unarranged overdraft charges

The Supreme Court published its judgment in respect of the fairness of unarranged overdraft charges on personal current accounts on 25 November 2009, finding in favour of the litigant banks. On 22 December 2009, the OFT announced that it will not continue its investigation into the fairness of these charges. The Group is working with the regulators to ensure that outstanding customer complaints are concluded as quickly as possible and anticipate that most cases in the county courts will be discontinued. The Group expects that some customers will argue that despite the test case ruling they are entitled to a refund of unarranged overdraft charges on the basis of other legal arguments or challenges. The Group would robustly defend any such complaints or claims and does not expect any such complaints or claims to have a material effect on the Group.

Other legal proceedings

In addition, during the ordinary course of business the Group is subject to threatened or actual legal proceedings both in the UK and overseas. All such material cases are periodically reassessed, with the assistance of external professional advisers where appropriate, to determine the likelihood of the Group incurring a liability. In those instances where it is concluded that it is more likely than not that a payment will be made, a provision is established to management's best estimate of the amount required to settle the obligation at the relevant balance sheet date. In some cases it will not be possible to form a view, either because the facts are unclear or because further time is needed to properly assess the merits of the case and no provisions are held against such cases. However the Group does not currently expect the final outcome of any such case to have a material adverse effect on its financial position.

20. Related parties

On 16 January 2009 Lloyds Banking Group plc acquired HBOS plc and its subsidiaries, including Bank of Scotland plc and as a result Lloyds Banking Group and its subsidiaries became related parties.

The Group transacts with other Lloyds Banking Group companies during the ordinary course of business. Details of transactions and outstanding balances as at and for the year ended 31 December 2009 are set out below:

	2009 £m
Transactions	
Interest income	**277**
Interest expense	**(823)**
Other income	**2,530**

	As at 31 Dec 2009 £m
Balances	
Loans and advances to banks	**85,456**
Loans and advances to customers	**261**
Debt securities classified as loans and receivables	**554**
Trading and other financial assets designated at fair value through profit or loss	**876**
Derivative assets	**664**
Available-for-sale financial assets	**132**
Other assets	**197**
Deposits from banks	**(144,876)**
Trading liabilities	**(5,463)**
Debt securities in issue	**(1,578)**
Derivative liabilities	**(853)**
Subordinated liabilities	**(14)**

HM Treasury

On 15 January 2009, HM Treasury subscribed for £8.5 billion of new ordinary shares and £3.0 billion of new preference shares in HBOS plc which, at that time was the Bank’s ultimate parent company. Consequently, from 15 January 2009, HM Treasury became a related party of the Bank. On 16 January 2009, HBOS plc was acquired by Lloyds Banking Group plc, which became the Bank's ultimate parent company. As at 16 January 2009, HM Treasury had a 43.4 per cent interest in Lloyds Banking Group, and therefore HM Treasury remained a related party of the Bank.

There were no material transactions between the Group and HM Treasury during the period between 15 January 2009 and 31 December 2009 that were not made in the ordinary course of business or that are unusual in their nature or conditions.

21. Capital ratios

	As at 31 Dec 2009 £m	As at 31 Dec 2008 £m
Capital resources		
Core tier 1		
Ordinary share capital and reserves	**22,147**	11,661
Available-for-sale revaluation reserve	**2,972**	5,335
Cashflow hedging reserve	**839**	1,041
Other items	**150**	(376)
	26,108	17,661
Deductions from core tier 1		
Goodwill and other intangible assets	**(565)**	(1,211)
Excess expected loss	**(920)**	(536)
Other deductions	**(556)**	(484)
	(2,041)	(2,231)
Core tier 1 capital	**24,067**	15,430
Preference share capital	**800**	1,200
Innovative tier 1 capital	**698**	698
Total tier 1 capital	**25,565**	17,328
Tier 2		
Available-for-sale revaluation reserve in respect of equities	**22**	–
Undated subordinated debt	**5,206**	5,551
Eligible provisions	**1,669**	1,454
Dated subordinated debt	**8,691**	9,094
Deductions from tier 2		
Excess expected loss	**(920)**	(536)
Other deductions	**(556)**	(325)
Total tier 2 capital	**14,112**	15,238
	39,677	32,566
Supervisory deductions		
Unconsolidated investments	**(1,062)**	(919)
Total capital resources	**38,615**	31,647
Risk weighted assets	**322,866**	326,703
Core tier 1 ratio	**7.5%**	4.7%
Tier 1 capital ratio	**7.9%**	5.3%
Total capital ratio	**12.0%**	9.7%

22. Prior year reclassifications

The following table sets out the balance sheets as at 1 January 2008 and 31 December 2008 and the income statement for the year ended 31 December 2008 as presented in the 2008 financial statements of the Group with reclassifications made to present these statements on a basis consistent with the presentation practices adopted by Lloyds Banking Group plc:

Consolidated balance sheet as at 31 December 2008

		As previously presented £m	Balance sheet reclassifi-cations £m	As restated £m
Assets				
Cash and balances at central banks		2,502	–	2,502
Items in the course of collection from banks		445	–	445
Trading and other financial assets designated at fair value through profit or loss	(i)	22,571	859	23,430
Derivative financial instruments		50,517	–	50,517
Loans and receivables:				
Loans and advances to customers	(v)	473,015	15,198	488,213
Loans and advances to banks		12,445	–	12,445
Debt securities	(i)	–	38,878	38,878
		485,460	54,076	539,536
Investment securities	(i)	67,772	(67,772)	–
Available-for-sale financial assets	(i)	–	28,035	28,035
Investment property		43	–	43
Interests in joint ventures and associates		1,193	–	1,193
Goodwill and other intangible assets	(iv)	1,148	(1,148)	–
Goodwill	(iv)	–	667	667
Other intangible assets	(iv)	–	108	108
Property and equipment/tangible fixed assets	(ii), (iv)	1,187	4,340	5,527
Operating lease assets	(ii)	3,967	(3,967)	–
Deferred costs	(iii)	2	(2)	–
Current tax recoverable		865	–	865
Deferred tax assets		3,182	–	3,182
Other assets	(iii)	2,430	696	3,126
Prepayments and accrued income	(iii)	694	(694)	–
Total assets		643,978	15,198	659,176

22. Prior year reclassifications (continued)

Consolidated balance sheet as at 31 December 2008

		As previously presented £m	Balance sheet reclassifi-cations £m	As restated £m
Liabilities				
Deposits from banks		97,066	–	97,066
Customer accounts	(v)	262,201	15,198	277,399
Items in course of transmission to banks	(vi)	–	521	521
Trading and other financial liabilities at fair value through profit or loss		18,851	–	18,851
Derivative financial instruments		40,827	–	40,827
Notes in circulation		957	–	957
Debt securities in issue		188,448	–	188,448
Other liabilities	(vi)	2,250	1,985	4,235
Current tax liabilities		23	–	23
Accruals and deferred income	(vi)	2,306	(2,306)	–
Other provisions	(vi)	345	(200)	145
Subordinated liabilities/other borrowed funds		18,779	–	18,779
Total liabilities		632,053	15,198	647,251
Net assets		11,925	–	11,925

The significant balance sheet reclassifications (none of which require the remeasurement of an asset or liability) are in relation to:

(i) the reclassification of investment securities (£67,772 million) to trading and other financial assets at fair value through the profit and loss (£859 million); available-for-sale financial assets (£28,035 million) and debt securities classified as loans and receivables (£38,878 million);

(ii) the reclassification of operating lease assets (£3,967 million) to tangible fixed assets;

(iii) the reclassification of deferred costs (£2 million) and prepayments and accrued income (£694 million) to other assets;

(iv) the reclassification of goodwill and intangible assets into their separate components, goodwill (£667 million) and other intangibles (£108 million) and the reclassification of software items deemed integral to the equipment balance from within intangibles to tangible fixed assets (£373 million);

(v) the representation of certain customer deposit amounts (£15,198 million) available for offset onto a gross basis; and

(iv) the reclassification of accruals and deferred income (£2,306 million) to other liabilities, the reclassification of other liabilities (£521 million) to items in the course of transmission to banks. The reclassification of other provisions (£200 million) to other liabilities.

22. **Prior year reclassifications** (continued)

Consolidated balance sheet as at 1 January 2008

		As previously presented £m	Balance sheet reclassifi-cations £m	As restated £m
Assets				
Cash and balances at central banks		2,944	–	2,944
Items in course of collection from banks		945	–	945
Trading and other financial assets at fair value through profit or loss	(i)	54,681	1,108	55,789
Derivative financial instruments		13,794	–	13,794
Loans and receivables:				
Loans and advances to customers	(v)	460,267	24,934	485,201
Loans and advances to banks		4,095	–	4,095
Debt securities	(i)	–	527	527
		464,362	25,461	489,823
Investment securities	(i)	51,615	(51,615)	–
Available-for-sale financial assets	(i)	–	49,980	49,980
Investment property		34	–	34
Interests in joint ventures and associates		1,739	–	1,739
Goodwill and other intangible assets	(iv)	1,517	(1,517)	–
Goodwill	(iv)	–	1,041	1,041
Other intangible assets	(iv)	–	110	110
Property and equipment/tangible fixed assets	(ii) (iv)	1,291	5,009	6,300
Operating lease assets	(ii)	4,643	(4,643)	–
Other assets	(iii)	4,637	1,430	6,067
Prepayments and accrued income	(iii)	1,430	(1,430)	–
Total assets		603,632	24,934	628,566

22. Prior year reclassifications (continued)

Consolidated balance sheet as at 1 January 2008

		As previously presented £m	Balance sheet reclassifi-cations £m	As restated £m
Liabilities				
Deposits from banks		41,513	–	41,513
Customer accounts	(v)	272,687	24,934	297,621
Items in course of transmission to banks	(vi)	–	542	542
Trading portfolio and other financial liabilities at fair value through profit or loss		22,705	(153)	22,552
Derivative financial instruments		12,160	–	12,160
Notes in circulation		881	153	1,034
Debt securities in issue		206,520	–	206,520
Insurance contract liabilities		24	(24)	–
Investment contract liabilities		98	(98)	–
Liabilities arising from insurance contracts and participating investment contracts		–	24	24
Liabilities arising from non-participating investment contracts		–	98	98
Other liabilities	(vi)	2,560	2,352	4,912
Current tax liabilities		728	–	728
Deferred tax liabilities		965	–	965
Accruals and deferred income	(vi)	2,894	(2,894)	–
Other provisions		172	–	172
Subordinated liabilities/other borrowed funds		17,881	–	17,881
Total liabilities		581,788	24,934	606,722
Net assets		21,844	–	21,844

The significant balance sheet reclassifications (none of which require the remeasurement of an asset or liability) are in relation to:

(i) the reclassification of investment securities (£51,615 million) to trading and other financial assets at fair value through the profit or loss (£1,108 million); available-for-sale financial assets (£49,980 million), and debt securities classified as loans and receivables (£527 million);

(ii) the reclassification of operating lease assets (£4,643 million) to tangible fixed assets;

(iii) the reclassification prepayments and accrued income (£1,430 million) to other assets;

(iv) the reclassification of goodwill and intangible assets into their separate components of goodwill (£1,041 million) and other intangibles (£110 million) and the reclassification of software items deemed integral to the equipment balance within intangibles to tangible fixed assets (£366 million);

(v) the representation of certain customer deposit amounts (£24,934 million) available for offset onto a gross basis; and

(vi) the reclassification of accruals and deferred income (£2,894 million) to other liabilities, the reclassification of other liabilities (£542 million) to items in the course of transmission to banks.

22. **Prior year reclassifications** (continued)

Consolidated income statement for the year to 31 December 2008

		As previously presented £m	Alignment of income statement captions and presentation £m	As restated £m
Interest and similar income	(i)	39,332	(3,239)	36,093
Interest and similar expense	(i)	(31,039)	3,486	(27,553)
Fees and commission income	(i)	2,208	(247)	1,961
Fees and commission expense		(382)	–	(382)
Net earned premiums on insurance contracts/insurance premium income		215	(215)	–
Net trading income		(2,963)	25	(2,938)
Insurance premium income		–	215	215
Net investment income related to insurance and investment business		34	(34)	–
Other operating income		1,665	111	1,776
Change in investment contract liabilities		17	(17)	–
Net claims incurred on insurance contracts		(76)	76	–
Net change in insurance contract liabilities		22	(22)	–
Insurance claims		–	(37)	(37)
Operating expenses	(ii)	–	(5,937)	(5,937)
Administrative expenses	(ii)	(4,253)	4,253	–
Depreciation and amortisation:				
Intangible assets other than goodwill	(ii)	(153)	153	–
Property and equipment	(ii)	(211)	211	–
Operating lease assets	(ii)	(1,178)	1,178	–
		(1,542)	1,542	–
Goodwill impairment	(ii)	(142)	142	–
Impairment losses on loans and advances	(iii)	(9,857)	9,857	–
Impairment on investment securities	(iii)	(2,193)	2,193	–
Impairment	(iii)	–	(12,050)	(12,050)
Share of profits of jointly controlled entities	(iv)	(651)	651	–
Share of losses of associated undertakings	(iv)	(287)	287	–
Share of results of joint ventures and associates	(iv)	–	(938)	(938)
Non-operating income/loss on sale of businesses		(743)	(102)	(845)
Loss before tax		(10,635)	–	(10,635)
Taxation		2,448	–	2,448
Loss for the year		(8,187)	–	(8,187)

22. Prior year reclassifications (continued)

Certain income statement captions and presentations have been aligned to a basis consistent with the practices adopted by the Lloyds Banking Group for consistency purposes. The significant income statement reclassifications are in relation to:

(i) the representation of certain derivative income amounts (£3,486 million) that are available for offset onto a net basis from within interest and similar income to interest and similar expense and the reclassification of certain loan fees from fee and commission income to interest and similar income (£247 million) as they form part of the effective yield;
(ii) the reclassification of administrative expenses (£4,253 million), depreciation and amortisation (£1,542 million) and goodwill impairment (£142 million) to operating expenses;
(iii) the reclassification of impairment losses on loans and advances (£9,857 million) and investment securities (£2,193 million) to impairment losses; and
(iv) the reclassification of share of losses of jointly controlled entities (£651 million) and share of losses of associated undertakings (£287 million) to share of results of joint ventures and associates.

23. Post balance sheet events

On 23 December 2009 Lloyds Banking Group plc announced its intention to adjust the Group's corporate structure and transfer its current holding in HBOS plc, the immediate parent of the Bank. Lloyds Banking Group will continue to own the Group indirectly.

This transfer follows a review by management of the structure of Lloyds Banking Group and a programme to develop and implement a legal entity structure that is efficient from a financial, regulatory and capital perspective. This transfer has been approved by the Financial Services Authority, and became effective on 1 January 2010.

24. Ultimate parent undertaking

Bank of Scotland plc's ultimate parent undertaking and controlling party is Lloyds Banking Group plc (formerly Lloyds TSB Group plc) which is incorporated in Scotland. Lloyds Banking Group plc will produce consolidated accounts for the year ended 31 December 2009. Copies of the annual report and accounts of Lloyds Banking Group plc and Bank of Scotland plc for the year ended 31 December 2008 may be obtained from the Group Secretariat, Lloyds Banking Group, 25 Gresham Street, London EC2V 7HN or downloaded via www.lloydsbankinggroup.com

25. Other information

The financial information included in this news release does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006. Statutory accounts for the year ended 31 December 2009 were approved by the directors on 25 February 2010 and will be delivered to the Registrar of Companies following publication. The auditors' report on these accounts was unqualified and did not include a statement under sections 237(2) (accounting records or returns inadequate or accounts not agreeing with records and returns) or 237(3) (failure to obtain necessary information and explanations) of the Companies Act 2006.

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