Abbey National PLC

Transition to IFRS

Restatement of 2004 financial information from UK GAAP to IFRS

Contents

Forward looking statements

The information in this announcement does not comprise statutory accounts within the meaning of section 240 of the Companies Act 1985 (the "Act"). Statutory accounts for the year ended 31 December 2004 have been delivered to the Registrar of Companies in accordance with section 242 of the Act.

This announcement contains forward-looking statement, including such statements within the meaning of Section 27A of the US Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements concern or may affect future matters such as Abbey's future economic results, business plans and strategies and are based on current expectations of the directors. They are subject to a number of risks and uncertainties that might cause actual results and outcomes to differ materially from expectations outlined in these forward looking statements.

For more information on these risks and uncertainties, please refer to Abbey's Annual Report on Form 20-F filed with the US Securities and Exchange Commission.

Section 1

Introduction

Abbey in line with all listed entities in the European Union ("EU"), is required to adopt International Financial Reporting Standards ("IFRS") in preparing its consolidated financial statements for the year ending 31 December 2005

Up to 31 December 2004, the Abbey Group prepared its financial statements in accordance with UK Generally Accepted Accounting Principles ("UK GAAP"). This document sets out the impact of these changes upon the Group's financial position and reconciles the restated comparatives to previously published 2004 UK GAAP financial information.

Some of the standards, principally the treatment of pensions, financial instruments and life assurance accounting, represent a significant change from previous UK GAAP.

Key standards IAS 32 "Financial Instruments: Disclosure and Presentation", IAS 39 "Financial Instruments: Recognition and Measurement" and IFRS 4 "Insurance Contracts" have been applied prospectively from 1 January 2005 and no restatement of the profit and loss account or balance sheet will therefore be made for the impacts of these standards.

All other standards are to be applied retrospectively, therefore, the profit and loss account for the 6 months to 30 June 2004 and balance sheet as at 1 January 2004, 30 June 2004 and 31 December 2004 will be restated for the effect of these standards.

Guidance was given on the impacts of IFRS on Abbey both in the Abbey 2004 Preliminary Announcement and in the Abbey 2004 Annual Report and Accounts. Further guidance is given in the Abbey 2005 Interim announcement.

Overview

From 1 January 2005, the Group has been using IFRS as its primary financial reporting framework. Although the move to IFRS can significantly change the timing of earnings recognition in financial results and the level of reported earnings, it is important to note that there is no IFRS impact on business fundamentals and cash flows.

June 2004 Earnings Restatements

In accordance with the requirements of IFRS, revised results for the 6 months to 30 June 2004 include only those adjustments for standards implemented with effect from 1 January 2004. The impacts of adjustments for standards, which have been implemented with effect from 1 January 2005, have not been included.

The key changes to the profit and loss account to 30 June 2004 are:

- Profit before tax fell by £57 million from £350 million to £293 million.
- Profit attributable to equity shareholders fell by £8 million from £189 million to £181 million.

The changes reflect the accounting treatment of leasing, software capitalisation and the way in which the Group's life earnings are taxed

2004 Balance Sheet Restatements

The key changes relating to the Groups balance sheet are as at the following dates

1 January 2004

- Ordinary shareholders' equity reduced by £648 million to £4,052 million
- Total Assets increased by £15,113 million

30 June 2004

- Ordinary shareholders' equity reduced by £636 million to £4,199 million
- Total Assets increased by £17,535 million

31 December 2004

- Ordinary shareholders' equity reduced by £1,198 million to £3,094 million
- Total Assets increased by £15,360 million

The most significant item impacting on the Group's ordinary shareholders' equity is the recognition of the Group's net pensions deficit on balance sheet. Leasing and the write-off of certain intangible assets also have an impact.

The most significant item impacting the Group's total assets is the gross up of the Group's mortgage securitisation entities assets and liabilities, which were previously accounted for under UK GAAP using the linked presentation approach.

Section 2 of this document outlines the key differences between UK GAAP and IFRS that relate to standards that are applied retrospectively from 1 January 2004 onwards.

Section 3 describes the key differences between UK GAAP and IFRS that relate to standards that are applied prospectively from 1 January 2005 onwards.

Section 4 details the Group's provisional IFRS accounting policies expected to be applied from 1 January 2005.

The appendices show the following;

Appendix 1: Restated Consolidated Balance Sheet at 1 January 2004;
Appendix 2: Restated Consolidated Balance Sheet at 30 June 2004;
Appendix 3: Restated Consolidated Balance Sheet at 31 December 2004;
Appendix 4: Consolidated Profit and Loss Account for the period to 30 June 2004;
Appendix 5: Reconciliation of Ordinary Shareholders' Funds at 1 January 2004, 30 June 2004, 31 December 2004 and 1 January 2005.

It should be noted that all disclosures in this document are unaudited.

Abbey

Section 2

Differences between UK GAAP and IFRS - Retrospective

The significant differences between the Group's UK accounting policies and IFRS accounting policies are summarised below

UK GAAP	IFRS
(a) Goodwill	
Goodwill arising on acquisitions of subsidiaries and associate companies and joint ventures is capitalised and amortised through the profit and loss account on a straight line basis over its expected economic life. When there is an indication that goodwill has become impaired an impairment test is performed and if necessary goodwill is written off. Prior to 1998, goodwill arising on the acquisition of subsidiaries was eliminated directly against reserves.	Goodwill arising on acquisitions of subsidiaries and associates and joint ventures is capitalised and tested annually for impairment. Amounts recognised in the UK GAAP balance sheet at 1st January 2004 have been carried forward, after separating out intangible assets, into the balance sheet at deemed cost after being tested for impairment. Goodwill previously written off to reserves in accordance with UK GAAP has not been reinstated on the balance sheet. Goodwill amortised under UK GAAP in 2004 has been written back in the 2004 IFRS financial statements.
(b) Intangibles other than goodwill	
An intangible asset acquired in a business combination is capitalised separately from goodwill only if it can be disposed of separately from the business to which it contributes and its value can be measured reliably.	An intangible asset is recognised as an asset separately from goodwill if it is separable or it arises from contractual or other legal rights regardless of whether these rights are transferable or separable. Intangible assets are amortised through the income statement over the useful economic life of the asset. In addition, intangible assets are tested for impairment if there are circumstances that may indicate that the intangible asset is impaired. In 2004, impairment in the value of distribution channels was recognised due to the expectation of reduced profitability in a competitive UK protection market through the independent financial adviser channels in place at the date of Scottish Provident's acquisition. This impairment amounted to £135m.

Abbey

Differences between UK GAAP and IFRS - Retrospective (Continued)

UK GAAP	IFRS
(c) Software capitalisation	
Expenses on the purchase or development of computer software are charged to the income statement as incurred.	External and directly related internal costs of software are capitalised where the software will result in a directly measurable intangible asset. Amounts capitalised are amortised over their useful economic lives. In addition, capitalised software is tested for impairment if there are circumstances that may indicate that the intangible asset is impaired. In 2004, following the acquisition of Abbey by Grupo Santander Central Hispano and well-documented information technology improvements that are expected to follow the majority of capitalised software was amortised or impaired. This amortisation and impairment amounted to £109m.
(d) Consolidation	
The Group consolidates all entities controlled by it. Control is the ability to direct the financial and operating policies of the entity. In accordance with FRS 5, securitisation transactions, which qualify, are accounted for on the basis of linked presentation.	The Group consolidates all entities controlled by it using the acquisition method. A subsidiary is an entity, which the Group controls, including special purpose entities, which are in substance controlled by the Group. Linked presentation is not available under IFRS. Therefore, the gross assets and the related funding are presented separately. This has lead to a gross up of the balance sheet of £14.5 billion at 31 December 2004.
(e) Leasing	
Assets leased to customers under agreements, which transfer substantially all of the risks and rewards of ownership other than legal title are classified as finance leases. All other leases are classified as operating leases.	The rules governing the classification of leases as either finance leases or operating leases are similar to UK GAAP.

Differences between UK GAAP and IFRS - Retrospective (Continued)

UK GAAP	IFRS
(e) Leasing (continued)	
Income from finance leases is credited to the income statement using the actuarial after tax method to give a constant periodic rate of return on the net cash investment. For assets leased to customers under operating leases, income and depreciation are recognised in the profit and loss account using either the actuarial after tax method or the straight-line method, depending on the nature of the operating lease.	Finance lease income is recognised so as to give a constant rate of return on the net cash investment without taking account of tax payments and receipts ("actuarial before tax method") For operating leases, lease income and depreciation of operating lease assets is recognised on the straight-line basis.
(f) Pensions	
Where pensions are provided by means of a funded defined benefits scheme, annual contributions are based on actuarial advice. The expected cost of providing pensions is recognised on a systematic basis over the expected average remaining service lives of the members of the scheme of the scheme. Variations from regular cost are spread over the average remaining service lives of current employees.	For defined benefit schemes, an actuarial valuation of the scheme obligation and the fair value of the plan assets are made annually. The difference between the fair value of the plan assets and the present value of the defined benefit obligation at the balance sheet date. Cumulative actuarial gains and losses are taken directly to reserves. At 1 January 2004, pension assets and liabilities have been recognised in full. As at 31 December 2004 the pensions deficit gross of tax amounted to £1.2 billion.
(g) Dividends	
Dividends payable on ordinary shares are recorded in the period to which they relate.	Dividends are recorded in the period in which they are declared.
(h) Share based payments	
The cost of share-based instruments which are equity settled, are accounted for on a fair value basis, computed by reference to the grant date; such costs are expensed over the performance period to which the award relates. The amount charged to the income statement is credited to reserves.	Abbey became a subsidiary of Banco Santander Central Hispano, S.A, in 2004, and at that time, a number of options in the shares of Abbey were rolled over into Banco Santander Central Hispano, S.A shares. These share options along with all new grants of shares are satisfied by the purchase of shares in the open market.

Abbey

Differences between UK GAAP and IFRS - Retrospective (Continued)

UK GAAP	IFRS
(h) Share based payments (continued)	
	The treatment of share options granted to staff by subsidiaries in the shares of the parent is still being finalised by the International Financial Reporting interpretations Committee (IFRIC). The present guidance is that a subsidiary should treat such options as "cash settled" in the subsidiary accounts, whereas in the parent accounts such options should be treated as equity settled. This has resulted in an increase of £46m in share option expenses for 2004.
(i) Deferred tax	
Deferred tax is provided in full for all material timing differences that have not reversed at the balance sheet date. Provision is not made for specific items, which are not expected to result in taxable income in the future, namely gains on the revaluation of property and the unremitted earnings of subsidiary and associated companies.	Deferred tax is provided in full based on temporary differences, including items such as the revaluation of property and unremitted earnings of subsidiaries and associated companies where the Group is not able to control their distribution policies. The key impact being deferred tax provision on operating lease assets revalued at acquisition.
(j) Life assurance	
In order to reflect the different nature of the shareholders' and policyholders' interests in the long-term assurance business, the value of the long-term assurance business attributable to shareholders is included on the balance sheet and the assets and liabilities attributable to policyholders are classified under separate headings in the consolidated balance sheet. The value of shareholders interest in the long-term assurance business represents an estimate of the net present value of the profits inherent in the in-force policies, embedded value accounting. All life assurance products are accounted for in the same way; there is no distinction between investment products and insurance products	Assets, liabilities, income and expense of life assurance business are consolidated on a line-by-line basis. IFRS impacts on how insurance contracts are classified and subsequently accounted for. This is covered further in the section 3 of this document detailing the impacts of IFRS that are prospective in their application.

Abbey

Section 3

Differences between UK GAAP and IFRS - Prospective

Effects of the application of IAS 32, IAS 39 and IFRS 4

The significant differences between the Group's UK accounting policies and IFRS accounting policies applied to the treatment of financial instruments and insurance contracts, which have been incorporated into the opening balance sheet as at 1 January 2005, are as follows:

UK GAAP	IFRS
(a) Derivatives and hedge accounting	
Derivatives used for hedging purposes are measured on an accruals basis consistent with the assets, liabilities, positions or future cash flows being hedged. The gains and losses on these instruments (arising from changes in fair value) are not recognised in the income statement immediately as they arise. Such gains are either not recognised in the balance sheet or are recognised and carried forward. When the hedged transaction occurs, the gain or loss is recognised in the income statement at the same time as the hedged item. Derivatives that are not hedge accounted are recorded at fair value, with changes in fair value recorded in the profit and loss account. Products that contain certain embedded derivatives are valued with reference to the total product inclusive of the derivative element.	IAS 39 requires all derivatives to be recorded at fair value on the balance sheet. Provided all hedge accounting conditions are met and the hedging relationship is deemed to be effective, the derivative may be designated as a fair value hedge, cash flow hedge or hedge of a net investment in a foreign operation. The change in fair value of a fair value hedge is recorded in income along with the change in fair value, relating to the hedged risk, of the hedged asset or liability. The change in value of a cash flow hedge is recorded in equity to the extent it is effective and recycled to income as the hedged cash flows affect the income statement. The change in value of a net investment hedge is recorded in the translation reserve to the extent the hedge is effective and only released to the income statement when the underlying investment is sold. As at 1 January 2005, all hedging derivatives have been recognised at fair value and adjustments have been made to hedged items where fair value hedge accounting will be applied. Hedges have been designated and documented in compliance with IFRS. Where hedges were in place under UK GAAP that have not been designated as hedges under IFRS, the hedged item has been revalued to fair value and an adjustment made to opening equity. This revaluation will be amortised to the income statement on an ongoing basis in accordance with IFRS 1 "First-time Adoption of International Financial Reporting Standards"

Abbey

Differences between UK GAAP and IFRS - Prospective (continued)

UK GAAP	IFRS
(a) Derivatives and hedge accounting (continued)	
	Some hybrid contacts contain both a derivative and a non-derivative component. In such cases, the embedded component is termed an embedded derivative. Where the economic characteristics and risks of the embedded derivative are not closely related to those of the host contract, and the hybrid contract itself is not carried at fair value, the embedded derivative is bifurcated and reported at fair value with gains and losses being recognised in the income statement.
(b) Financial Instruments: financial assets	
Loans are measured at cost, less provisions for bad and doubtful debts. Debt securities and equity shares intended for use on a continuing basis in the Group's activities are classified as investment securities, and are stated at cost less provision for any permanent diminution in value. The cost of dated investment securities is adjusted for the amortisation of premiums and discounts. Other debt securities and equity shares that are held for trading purposes are carried at fair value.	Under IAS 39, financial assets are classified as held-to-maturity; available-for-sale; held for trading; designated as fair value through profit and loss; and loans and receivables. Financial assets classified as held-to-maturity or as loans and receivables are carried at amortised cost. Other financial assets are measured at fair value. Changes in the fair value of available-for-sale financial assets are reported in a separate component of shareholders equity. Changes in the fair value of financial assets held for trading or designated at fair value through the profit and loss are taken to the income statement. Financial assets can be classified as held-to-maturity only if they have a fixed maturity and the reporting entity has the ability and intent to hold to maturity. Trading financial assets are held for selling in the near term. IFRS allows any financial asset to be designated as fair value through profit and loss on initial recognition.

Abbey

Differences between UK GAAP and IFRS - Prospective (continued)

UK GAAP	IFRS
(c) Financial Instruments: financial liabilities	
Under UK GAAP, short positions in securities and trading derivatives are carried at fair value; all other financial liabilities are recorded at amortised cost.	IAS 39 requires all financial liabilities to be measured at amortised cost except those held for trading.
(d) Liabilities and equity	
Under UK GAAP, all shares were classified as shareholders' funds. An analysis of shareholders' funds between equity and non-equity interest is given.	There is no concept of non-equity shares under IFRS. Instruments are classified between equity and liabilities in accordance with the substance of the contractual arrangements. A non-derivative instrument is classified as equity if it does not include a contractual obligation either to deliver cash or to exchange financial instruments with another entity under potentially unfavourable conditions, and, if the instrument will or may be settled by the issue of equity, settlement does not involve the issue of a variable number of shares.
(e) Netting	
Under UK GAAP an intention to settle net is not a requirement for set off; the entity must have the ability to insist on net settlement and that ability is assured beyond doubt.	For a financial asset and financial liability to be offset, IFRS requires that an entity must intend to settle on a net basis or to realise the asset and settle the liability simultaneously.
(f) Loan Impairment	
Specific provisions are raised when the creditworthiness of a borrower has deteriorated such that the recovery of the whole or part of an outstanding advance is in serious doubt. Specific provisions are generally raised on an individual basis, although specific provisions may be raised on a portfolio basis for homogenous assets and where statistical techniques are appropriate. General provisions are raised to cover losses which are judged as present in loans and advances at the balance sheet date, but which have not been specifically identified as such. If collection of interest is doubtful, it is credited to a suspense account and excluded from the interest income in the income statement. The suspense account in the balance sheet is netted against the relevant loan.	Impairment losses are recognised where there is evidence of impairment, a result of one or more loss events that have occurred after initial recognition, and where these events have had an impact on the estimated cash flows of the financial asset or portfolio of financial assets. Impairments of loans and receivables are measured as the difference between the carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. Impairment is measured individually for assets that are individually significant and on a collective basis for portfolios with similar risk characteristics. Under IFRS, all impairment allowances are calculated in the same manner and there is no distinction between general and specific provisions.

Abbey

Differences between UK GAAP and IFRS - Prospective (continued)

UK GAAP	IFRS
(f) Loan Impairment (continued)	
	Interest on impaired loans is recognised using the original effective interest rate, being the rate used to discount the estimated future cash flows for calculating impairment.
(g) Effective interest rate and lending fees	
Under UK GAAP, loan origination fees are recognised when received unless they are charged in lieu of interest.	IAS 39 requires the amortised cost of a financial instrument to be calculated using the effective interest method. The effective interest method is the rate that discounts estimated future cash flows over an instrument's expected life to its net carrying value. It takes into account, all fees paid that are an integral part of the yield, transaction costs and all other premiums and discounts.
(h) Insurance contracts	
All contracts within the life assurance business are accounted for as insurance contracts and the obligations to policy holders presented as Long-term assurance liabilities attributable to policyholders. The value placed on in-force policies includes future investment margins.	IFRS 4 requires life assurance products to be classified between insurance contracts and investment contracts. The latter are accounted for in accordance with IAS 39. Insurance contracts continue to be accounted for using the embedded value methodology. The value of in-force policies excludes any amounts that reflect future investment margins.
(i) Extinguishment of liabilities	
Under UK GAAP, recognition of a financial liability ceases once any transfer of economic benefits to the creditor is no longer likely.	A financial liability is removed from the balance sheet when, and only when, it is legally extinguished i.e. when the obligation specified in the contract is discharged or cancelled or expires.

Abbey

Section 4

Provisional IFRS Accounting Policies of Abbey

1. Adoption of International Accounting Standards

The Consolidated Financial Statements have for the first time, been prepared in accordance with International Financial Reporting Standards ("IFRS") adopted by the International Accounting Standards Board ("IASB"), and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB. The date of transition to IFRS for the Group and the date of its opening IFRS balance sheet was 1 January 2004. On initial adoption of IFRS, the Group applied the following exemptions from the requirements of IFRS and from their retrospective application as permitted by IFRS 1 "First-time Adoption of International Financial Reporting Standards" (IFRS 1).

Business Combinations – the Group has applied IFRS 3 "Business Combinations" to business combinations that occurred on or after 1 January 2004. Business combinations before that date have not been restated. Under previous GAAP ("UK GAAP"), goodwill arising on acquisitions after 1 October 1998 was capitalised and amortised over its estimated useful economic life. Goodwill arising on acquisitions before 1 October 1998 was deducted from equity.

Property, plant and equipment – The Group has adopted the carrying values of all items of property, plant and equipment on the date of transition under UK GAAP as their deemed cost, rather than either reverting to historical cost or carrying out a valuation at the date of transition as permitted by IFRS 1.

Cumulative foreign currency difference – The Group has brought forward a nil opening balance on the cumulative foreign currency translation adjustment arising from the retranslation of foreign operations, which is shown as a separate item in shareholders' equity at the date of transition in accordance with IAS 21 "The Effects of changes in Foreign Exchange Rates".

Derecognition of financial instruments – Financial instruments derecognised before 1 January 2004 have not been re-recognised by the Group under IFRS.

Implementation of IAS 32, IAS 39 and IFRS 4 – As allowed by IFRS 1, the Group has not restated its 2004 consolidated income statements and balance sheets to comply with IAS 32, IAS 39 and IFRS 4.

2. Consolidation

a) Subsidiaries

Subsidiaries, which are those companies and other entities (including Special Purpose Entities) in which the Group, directly or indirectly, has power to govern the financial and operating policies, are consolidated.

The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity.

Provisional IFRS Accounting Policies of Abbey (continued)

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, shares issued or liabilities undertaken at the date of acquisition, plus costs directly attributable to the acquisition. The excess of the cost of acquisition over the fair value of the tangible and intangible assets of the subsidiary acquired is recorded as goodwill. Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless cost cannot be recovered.

The accounting reference date of the Company and its subsidiary undertakings is 31 December, with the exception of those leasing, investment, insurance and funding companies, which, because of commercial considerations, have various accounting reference dates. The financial statements of these subsidiaries have been consolidated on interim financial statements for the period to 31 December.

b) Associates and joint ventures
Investments in associates and joint ventures are accounted for by the equity method of accounting and are initially recognised at cost. Under this method, the Group's share of the post-acquisition profits or losses of associates is recognised in the income statement, and its share of post-acquisition movements in reserves is recognised in reserves. The cumulative post-acquisition movements are adjusted against the cost of the investment.

Associates are entities over which the Group has between 20% and 50% of the voting rights, or over which the Group has significant influence, but which it does not control. Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The Group's investment in associates includes goodwill on acquisition. When the Group's share of losses in an associate equals or exceeds its interest in the associate the Group does not recognise further losses unless the Group has incurred obligations or made payments on behalf of the associates.

Joint ventures are based on contractual arrangements where two or more entities carry out an economic activity that is subject to joint control.

3. Foreign currency translation

Items included in the financial statements of each entity of the Group are measured using the currency that best reflects the economic substance of the underlying events and circumstances relevant to that entity ("the measurement currency"). The consolidated financial statements are presented in Pounds Sterling, which is the measurement currency of the parent.

Income statements and cash flows of foreign entities are translated into the Group's reporting currency at average exchange rates for the year and their balance sheets are translated at the exchange rates ruling on 31 December. Exchange differences arising from the translation of the net investment in foreign entities and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign entity is sold, such exchange differences are recognised in the income statement as part of the gain or loss on sale.

Foreign currency transactions are translated into the measurement currency at the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

4. Revenue recognition

(a) Interest Income and Expense

Interest income on financial assets that are classified as loans and receivables, available for sale or held to maturity and interest expense on financial liabilities other than those at fair value through profit and loss is determined using the effective interest rate method. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the future cash flows are determined are estimated after considering all the contractual terms of the instrument but not future credit losses. The calculation includes all amounts paid or received by the Group that are an integral part of the overall return, direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument and all other premiums or discounts. Once a financial asset or a group of financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(b) Fee and commissions income

Fees and commissions, which are not an integral part of the effective interest rate are generally recognised when the service has been provided.

For the asset management operations, fee and commission income consists principally of investment management fees, distribution fees from mutual funds, commission revenue from the sale of mutual fund shares and transfer agent fees for shareholder record keeping. Revenue from investment management fees, distribution fees and transfer agent fees is recognized as earned when the service has been provided.

Portfolio and other management advisory and service fees are recognised based on the applicable service contracts. Asset management fees related to investment funds are recognised rateably over the period the service is provided. The same principle is applied for wealth management, financial planning and custody services that are continuously provided over an extended period.

(c) Financial assets and liabilities held at fair value

Financial assets and liabilities held for trading and financial assets designated as fair value through profit or loss are recorded at fair value. Changes in fair value are recognised in the income statement as trading income together with dividends and interest receivable and payable.

Provisional IFRS Accounting Policies of Abbey (continued)

5. Pensions and other post retirement benefits

Group companies have various pension schemes. The schemes are generally funded through payments to insurance companies or trustee-administered funds as determined by periodic actuarial calculations. A defined benefit plan is a pension plan that defines an amount of pension benefit to be provided, usually as a function of one or more factors such as age, years of service or compensation. A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity (a fund) and will have no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior periods.

The liability in respect of defined benefit pension plans, is the present value of the defined benefit obligation at the balance sheet date minus the fair value of plan assets. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. Full actuarial valuations of the Group's principal defined benefit schemes are carried out every three years with interim reviews in the intervening years; these valuations are updated to 31 December each year by qualified actuaries. The present value of the defined benefit obligation is determined by the estimated future cash outflows using interest rates of government securities, which have terms to maturity approximating the terms of the related liability.

The Group's income statement includes the current service cost of providing pension benefits, the expected return on schemes' assets, net of expected administration costs, and the interest cost on the schemes' liabilities. Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are taken directly to reserves. Past-service costs are charged immediately to the income statement, unless the charges are conditional on the employees remaining in service for a specified period of time, the vesting period. In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

For defined contribution plans, the company pays contributions to publicly or privately administered pension insurance plans on a mandatory, contractual or voluntary basis. Once the contributions have been paid, the company has no further payment obligations. The regular contributions constitute net periodic costs for the year in which they are due and as such are included in staff costs.

6. Share based payments

The Group engages in cash settled share based payment transactions in respect of services received from certain of its employees. Shares of the Group's parent, Banco Santander Central Hispano, S.A are purchased in the open market to satisfy share options as they vest. Prior to the acquisition of Abbey by Banco Santander Central Hispano, S.A, share options were satisfied by issue of new Abbey shares. These options were accounted for as equity settled share based payments. The fair value of the services received is measured by reference to the fair value of the shares or share options initially on the date of the grant and then subsequently at each reporting date. The cost of the employee services received in respect of the shares or share options granted is recognised in the income statement over the period that the services are received, which is the vesting period. The fair value of the options

Provisional IFRS Accounting Policies of Abbey (continued)

granted is determined using option pricing models, which take into account the exercise price of the option, the current share price, the risk free interest rate, the expected volatility of the Banco Santander Central Hispano, S.A. share price over the life of the option and other relevant factors. Except for those which include terms related to market conditions, vesting conditions included in the terms of the grant are not taken into account in estimating fair value. Non-market vesting conditions are taken into account by adjusting the number of shares or share options included in the measurement of the cost of employee service so that ultimately, the amount recognised in the income statement reflects the number of vested shares or share options. Where vesting conditions are related to market conditions, the charges for the services received are recognised regardless of whether or not the market related vesting conditions are met, provided that, the non-market vesting conditions are met.

7. Intangible assets and goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on the acquisition of subsidiaries is included in "intangible assets". Goodwill on acquisitions of associates is included in "investment in associates". Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Other intangible assets are recognised if they arise from contracted or other legal rights or if they are capable of being separated or divided from the Group and sold, transferred, licensed, rented or exchanged. The value of such intangible assets is amortised over the useful economic life of the assets in question.

8. Property, plant and equipment

Property, plant and equipment, includes owner-occupied properties, office fixtures and equipment and computer software.

Property, plant and equipment are carried at cost less accumulated depreciation and accumulated impairment losses. Items of property, plant and equipment are reviewed for indications of impairment at each reporting date. Gains and losses on disposal of property, plant and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit reported as other operating expenses. Repairs and renewals are charged to the income statement when the expenditure is incurred.

Software development costs are capitalised when they are associated with identifiable and unique software products that are expected to provide economic benefits and the cost of these products can be measured reliably. Internally developed software meeting these criteria and externally purchased software are classified in property, plant and equipment on the balance sheet. Costs associated with maintaining software programmes are expensed as incurred.

Classes of property, plant and equipment are depreciated on a straight-line basis over their useful life as follows:

Provisional IFRS Accounting Policies of Abbey (continued)

Owner-occupied properties	Not exceeding 40 years
Office fixtures and equipment	5 to 8 years
Computer software	3 to 5 years

9. Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit and loss account; loans and receivables and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

(a) Financial assets at fair value through the profit and loss

A financial asset classified in this category may be either held for trading or otherwise designated as held at fair value on inception. The assets are recognised initially at fair value and transaction costs are taken directly to the income statement. Gains and losses arising from changes in fair value are included directly in the income statement. The assets are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

(b) Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments and which are not classified as available for sale. They arise when the Group provides money or services directly to a customer with no intention of trading the loan. Loans and receivables are initially recognised at fair value including direct and incremental transaction costs. They are subsequently valued at amortised cost, using the effective interest method. They are derecognised when the rights to receive cash flows have expired of the Group has transferred substantially all of the risks and rewards of ownership.

(c) Available for sale

Available for sale investments are non-derivative financial investments that are designated as available for sale and are not categorised into any of the other categories described above. They are initially recognised at fair value including direct and incremental transaction costs. They are subsequently held at fair value. Gains and losses arising from changes in fair value are included as a separate component of equity until sale when the cumulative gain or loss is transferred to the income statement. Interest is determined using the effective interest method. Impairment losses and translation differences on monetary items are recognised in the income statement. The investments are derecognised when the rights to receive cash flows have expired or the Group has transferred substantially all the risks and rewards of ownership.

10. Offsetting financial instruments

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

Provisional IFRS Accounting Policies of Abbey (continued)

11. Sale and repurchase agreements (Including stock lending and borrowing)

Securities sold subject to a linked repurchase agreement ('repos') are retained in the financial statements as trading or investment securities and the counterparty liability is included in amounts "Due to other banks" or "Due to customers" as appropriate. Securities purchased under agreements to resell ('reverse repos') are recorded as "Due from banks" or "Loans and advances to customers" as appropriate. The difference between the sale and repurchase price is treated as trading income in the income statement. Securities lent to counterparties are also retained in the financial statements.

Securities borrowing and lending transactions are generally entered into on a collateralised basis with securities used as collateral. Securities borrowed and lent in these transactions are not recognised in the balance sheet.

12. Derivative financial instruments and hedge accounting

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and option pricing models as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Certain derivatives embedded in other financial instruments, such as the conversion option in a convertible bond, are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the hybrid contract is not carried at fair value through profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either: (1) hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge); or, (2) hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge). Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

The Group documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

(a) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

Provisional IFRS Accounting Policies of Abbey (continued)

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of the hedged item for which the effective interest method is used is amortised to profit or loss over the period to maturity. The adjustment to the carrying amount of a hedged equity security remains in retained earnings until the disposal of the equity security.

(b) Cash flow hedges
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled to the income statement in the periods in which the hedged item will affect profit and loss.

When a hedged instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecasted transaction is ultimately recognised in the income statement. When a forecasted transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Derivatives that do not qualify for hedge accounting
Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the income statement.

13. Securitisation transactions

The Group has entered into certain arrangements where undertakings have issued mortgage-backed securities or have entered into funding arrangements with lenders in order to finance specific loans and advances to customers. All such financial instruments continue to be held on the Group balance sheet, and a liability recognised for the proceeds of the funding transaction.

Transactions undertaken prior to 1 January 2004 that were accounted for on the basis of linked presentation under UK GAAP have been represented by separate recognition of the gross assets and related funding from that date.

14. Impairment of financial assets

At each balance sheet date the Group assesses whether, as a result of one or more events occurring after initial recognition, there is objective evidence that a financial asset or group of financial assets has become impaired. Evidence of impairment may include indications that the borrower or group of borrowers have defaulted, are experiencing significant financial difficulty, or the debt has been restructured to reduce the burden to the borrower.

Provisional IFRS Accounting Policies of Abbey (continued)

(a) Financial assets carried at amortised cost
Impairment losses are assessed individually for the financial assets that are individually significant and individually or collectively for assets that are not individually significant.

For individually assessed assets, the Group measures the amount of the loss as the difference between the carrying amount of the asset or group of assets and the present value of the estimated future cash flows from the asset or group of assets discounted at the original effective interest rate of the asset.

In making collective assessment for impairment, financial assets are assessed for each portfolio segmented by similar risk characteristics. Future cash flows from these portfolios are estimated based on historical loss experience. The historical loss experience is adjusted for current observable data, to reflect the effects of current conditions not affecting the period of historical experience. The loss is discounted at the effective interest rate, except where portfolios meet the criteria for short-term receivables. The impact of the discounting is reported through interest receivable within the income statement and represents the unwind of the discount.

Once an impairment loss has been recognised on a financial asset or group of financial assets, interest income is recognised on an effective interest rate basis.

Impairment losses are recognised in profit and loss and the carrying amount of the financial asset or group of financial reduced by establishing an allowance for impairment losses. If in a subsequent period the amount of the impairment loss reduces and the reduction can be ascribed to an event after the impairment was recognised, the previously recognised loss is reversed by adjusting the allowance.

A write off is made when all collection procedures have been completed and is charged against previously established provisions for impairment.

(b) Financial assets carried at Fair Value
The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In assessing whether available for sale assets are impaired, a significant or prolonged decline in the fair value of the security below its cost is considered evidence.

The cumulative loss is measured as the difference between the acquisition cost and the current fair value, less any impairment loss previously reported in the profit and loss account and is removed from equity and recognised in the income statement.

If in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase is due to an event occurring after the impairment loss was recognised in the profit and loss statement (with objective evidence to support this), the impairment loss is reversed through the income statement.

15. Impairment of intangible assets and property, plant and equipment

At each balance sheet date, or more frequently when events or changes in circumstances dictate, property plant and equipment and intangible assets are

Provisional IFRS Accounting Policies of Abbey (continued)

assessed for indicators of impairment. If indications are present, these assets are subject to an impairment review. Goodwill is subject to an impairment review as at the balance sheet date each year. The impairment review comprises a comparison of the carrying amount of the asset with its recoverable amount: the higher of the asset's or the cash-generating unit's net selling price and its value in use. Net selling price is calculated by reference to the amount at which the asset could be disposed of in a binding sale agreement in an arm's length transaction evidenced by an active market or recent transactions for similar assets. Value in use is calculated by discounting the expected future cash flows obtainable as a result of the asset's continued use, including those resulting from its ultimate disposal, at a market based discount rate on a pre tax basis.

The carrying values of fixed assets and goodwill are written down by the amount of any impairment and the loss is recognised in the income statement in the period in which it occurs. A previously recognised impairment loss relating to a fixed asset may be reversed in part or in full when a change in circumstances leads to a change in the estimates used to determine the fixed asset's recoverable amount. The carrying amount of the fixed asset will only be increased up to the amount that would have been had the original impairment not been recognised. Impairment losses on goodwill are not reversed. For conducting impairment reviews, cash generating units are the lowest level at which management monitors the return on investment on assets.

16. Investment property

Property held for long term rental yields and capital appreciation within the long-term assurance funds is classified as investment property. Investment property is stated at fair value, which is determined annually as the open market value. These valuations are reviewed annually by an independent valuation expert. Changes in fair values are recorded in the income statement.

17. Leases

The Group as lessor – Assets leased to customers under agreements which transfer substantially all the risks and rewards identical to ownership, are classified as finance leases. Assets held under finance leases are recognised in the Balance Sheet as a receivable amount equal to the net investment in leases. The net investment in leases represents the present value of the minimum lease payments receivable under finance leases together with any unguaranteed residual value accruing to the lessor discounted at the rates of interest implicit in the leases. Income from finance leases is recognised using the actuarial before tax method to give a constant periodic rate of return on the net investment.

Operating leases are recorded at cost and depreciated over the life of the lease after taking into account anticipated residual values. Operating lease rental income is recognised on a straight-line basis over the life of the lease.

The Group as lessee – The Group principally enters into operating leases for the rental of equipment or real estate. Payments made under such leases are charged to the income statement principally on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment to be made to the lessor by way of penalty is recognized as an expense in the period in which termination takes place.

If the lease agreement transfers the risk and rewards of the asset, the lease is recorded as a finance lease and the related asset is capitalized. At inception, the asset is recorded at the lower of the present value of the minimum lease payments or fair value and depreciated over the estimated useful life. The corresponding rental obligations are recorded as borrowings.

The aggregate benefit of incentives, if any, is recognized as a reduction of rental expense over the lease term on a straight-line basis.

18. Insurance

(1) Insurance and investment contracts - classification

The Group undertakes both life assurance and general insurance business. The life assurance business issues insurance contracts and investment contracts.

Insurance contracts are those contracts, which transfer significant insurance risk. As a general guideline, the Group defines as significant insurance risk the possibility of having to pay benefits on the occurrence of an insured event, which are at least 5% more than the benefits payable if the insured event were not to occur. Investment contracts are those contacts, which carry no significant insurance risk.

A number of insurance and investment contracts contain a discretionary participation feature which entitles the holder to receive, as a supplement to guaranteed benefits, additional benefits or bonuses that are likely to be a significant portion of the total contractual benefits and whose amount or timing is contractually at the discretion of the Group and based on the performance of specified assets. Contracts containing a discretionary participation feature are referred to as participating contracts.

The Group applies UK generally accepted accounting principles for insurance and participating investment contracts modified, as necessary, to comply with the requirements of IFRS. For insurance and participating contracts issued by the life assurance business, this includes continued application of the embedded value basis of accounting although, as described below, the underlying contracts are presented separately from the value of in-force life assurance business in respect of those contracts. Non-participating investment contracts are accounted for as financial instruments.

(2) Insurance contracts and investment contracts with discretionary participation features

The majority of the life assurance contracts issued by the Group are long-term life assurance contracts. The Group also issues life assurance contracts to protect customers from the consequence of events (such as death, critical illness or disability) that would affect the ability of the customer or their dependents to maintain their current level of income. Guaranteed benefits paid on occurrence of the specified insurance event are either fixed or linked to the extent of the economic loss suffered by the policyholder.

Provisional IFRS Accounting Policies of Abbey (continued)

Premiums
Premiums received in respect of life insurance contracts and participating investment contracts are recognised as revenue when due, and are shown before deduction of commission.

Claims
Death claims are recognised on notifications received. Maturities and annuity payments are recorded when due. Surrenders are recorded on the earlier of the date paid or date the policy benefit (or part thereof) ceases to be included within the insurance liabilities. Claims on participating business include bonuses payable. Claims payable include costs of settlement. Reinsurance recoveries are credited to match the relevant gross amounts.

Liabilities – life insurance contracts or participating investment contacts, which are not unit linked
A liability for contractual benefits that are expected to be incurred in the future is recorded when the premium is recognised. The liability is calculated by estimating the future cash flows over the duration of the in-force policies and discounting them back to the valuation date allowing for probabilities of occurrence. The liability will vary with movements in interest rates and with the cost of life assurance and annuity benefits where future mortality is uncertain. Assumptions are made in respect of all material factors affecting future cash flows, including future interest rates, mortality and costs.

Liabilities – life insurance contracts or participating investment contracts, which are unit linked
Allocated premiums in respect of unit linked contacts that are either life assurance contracts or participating investment contracts are recognised as liabilities. These liabilities are increased or reduced by the change in the unit prices and are reduced by policy administration fees, mortality and surrender charges and any withdrawals and include any amounts necessary to compensate the Group for services to be performed over future periods. The mortality charges deducted in each period from the policyholders as a group are considered adequate to cover the expected total death benefits claims in excess of the contract account balances in each period and hence no additional liability is established for these claims in excess of the contract balances in each period and hence no additional liability is established for these claims. Revenue consists of fees deducted for mortality, policy administration and surrender charges. Interest or changes in the unit prices credited to the account balances and excess benefit claims in excess of the account balances incurred in the period are charged as expenses in the income statement.

Value of in-force life assurance business
The Group recognises as an asset the value of in-force life assurance business in respect of life insurance contracts and participating investment contracts. The asset, which represents the present value of future profits expected to arise from these contracts, is determined by projecting the future surpluses and other net cash flows arising from life insurance contract and participating investment contract business written by the balance sheet date, but excluding any future investment margins, using appropriate economic and actuarial assumption, and discounting the result at a rate which reflects the Group's overall risk premium attributable to this business. The asset in the consolidated balance sheet and movements in the asset in the income statement are determined and shown on a gross of tax basis.

Provisional IFRS Accounting Policies of Abbey (continued)

Unallocated surplus
The Group has an obligation to pay policyholders a specified portion of all interest and realisable gains and losses arising from the assets backing participating contracts. Any amounts not yet determined as being due to policyholders are recognised as a liability, which is shown separately from other liabilities.

Realistic liabilities
Liabilities of the Group's with-profits life fund, including guarantees and options embedded within products written by that fund, are stated at their realistic values in accordance with the Financial Services Authority's realistic capital regime.

Liability adequacy test
At each balance sheet date, liability adequacy tests are performed to ensure the adequacy of insurance and participating investment contract liabilities. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities are used. Any deficiency is immediately charged to profit and loss by establishing a provision for losses arising from liability adequacy tests.

Reinsurance
Contracts entered into by the Group with reinsurers under which the Group is compensated for losses on one of more contracts issued by the Group and that meet the classification requirements for insurance contracts are classified as reinsurance contracts held. Insurance contracts entered into by the Group under which the contract holder is another insurer (inwards reinsurance) are included with insurance contacts.

The benefits to which the Group is entitled under its reinsurance contracts held are recognised as reinsurance assets. These assets consist of short-term balances due from reinsurers as well as longer-term receivables that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts. Amounts recoverable from or due to reinsurers are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised as an expense when due.

The Group assesses its reinsurance assets for impairment on the same basis as for financial assets held at amortised cost.

(3) Investment contracts without discretionary participation features

All of the Group's non-participating investment contracts are unit linked. These contracts are accounted for as financial liabilities whose value is contractually linked to the fair values of financial assets within the Group's unitised investment funds. The value of the unit linked financial liabilities is determined using current unit prices multiplied by the number of units attributed to the contract holders at the balance sheet date. Their value is never less than the amount payable on surrender, discounted for the required notice period where applicable.

Provisional IFRS Accounting Policies of Abbey (continued)

The element of premiums and claims in respect of non-participating investment contracts which is invested on behalf of the contract holder is excluded from the income statement, with all movements in the contract holder liability and related assets recorded in the balance sheet. Details of the basis of revenue recognition for the related investment management fees are set out above.

Directly incremental commissions that vary with and are related to either securing new or renewing existing non-participating investment contracts are capitalised as an intangible asset; all other costs are recognised as expenses when incurred. This asset is subsequently amortised over the period of the provision of investment management services and is reviewed for impairment in circumstances where its carrying amount may not be recoverable. If the asset is greater than the recoverable amount it is written down immediately.

19. Income taxes, including deferred income taxes

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

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Currently enacted tax rates are used in the determination of deferred income tax.

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

20. Cash and cash equivalents

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

21. Financial Liabilities

Financial liabilities are measured at amortised cost, except for trading liabilities, which are held at fair value through profit or loss.

22. Borrowings

Borrowings are recognised initially at fair value, being the proceeds (fair value of consideration received) net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Provisional IFRS Accounting Policies of Abbey (continued)

Preference shares, which carry a mandatory coupon, or are redeemable on a specified date or at the option of the shareholder, are classified as financial liabilities and are presented in other borrowed funds. The dividends on these preference shares are recognised in the income statement as interest expense on an amortised cost basis using the effective interest method.

The fair value of the liability portion of a convertible bond is determined using a market interest rate for an equivalent non-convertible bond. This amount is recorded as a liability on an amortised cost basis until extinguished on conversion or maturity of the bonds. The remainder of the proceeds is allocated to the conversion option. This is recognised and included in shareholders' equity, net of income tax effects.

If the Group purchases its own debt, it is removed from the balance sheet, and the difference between the carrying amount of a liability and the consideration paid is included in net trading income.

23. Share capital

(a) Share issue costs

Incremental external costs directly attributable to the issue of new shares, other than on a business combination, are deducted from equity net of any related income taxes.

(b) Treasury shares

Where the Company or its subsidiaries purchases the Company's equity share capital, the consideration paid including any attributable incremental external costs net of income taxes is deducted from total shareholders' equity as treasury shares until they are cancelled. Where such shares are subsequently sold or reissued, any consideration received is included in shareholders' equity.

24. Provisions

Provisions are recognised for present obligations arising as consequences of past events where it is more likely than not that a transfer of economic benefit will be necessary to settle the obligation, and it can be reliably estimated.

When a leasehold property ceases to be used in the business, provision is made where the unavoidable costs of the future obligations relating to the lease are expected to exceed anticipated rental income. The net costs are discounted using market rates of interest to reflect the long-term nature of the cash flows.

Provision is made for the anticipated cost of restructuring, including redundancy costs, when an obligation exists. An obligation exists when the Group has a detailed formal plan for restructuring a business, and has raised valid expectations in those affected by the restructuring and has started to implement the plan or announce its main features.

Contingent liabilities are possible obligations whose existence will be confirmed only by certain future events or present obligations where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised but are disclosed unless they are remote.

25. Dividends

Dividends on ordinary shares are recognised in equity in the period in which they are paid.

Abbey

Appendix 1: Restated Consolidated Balance Sheet at 1 January 2004

Assets	UK GAAP £m	Reclassification £m	Insurance Business £m	New Entities £m	Securitisation £m	Leasing £m	Employee Benefits £m	Software £m	Other Intangibles £m	Goodwill £m	Dividends £m	Other £m	IFRS £m
Cash and balances at central banks	439	-	-	67	-	-	-	-	-	-	-	-	506
Treasury bills and other eligible bills	1,630	(1,630)	-	-	-	-	-	-	-	-	-	-	-
Loans and advances to banks	7,155	-	-	-	-	-	-	-	-	-	-	-	7,155
Loans and advances to customers	93,839	2,573	-	-	14,482	(59)	-	-	-	-	-	-	110,835
Trading securities	28,575	3,263	-	(61)	-	-	-	-	-	-	-	-	31,777
Derivative financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-
Other financial instruments at fair value through P&L	-	-	25,138	298	-	-	-	-	-	-	-	-	25,436
Pledged assets	-	-	-	-	-	-	-	-	-	-	-	-	-
Investment securities	1,753	-	-	70	-	-	-	-	-	-	-	-	1,823
Net Investment in finance leases	2,573	(2,573)	-	-	-	-	-	-	-	-	-	-	–
Debt securities		-	-	-	-	-	-	-	-	-	-	-	-
Equity shares and other variable interest securities	1,633	(1,633)	-	-	-	-	-	-	-	-	-	-	-
Long-term assurance business	2,271	-	(2,271)	-	-	-	-	-	-	-	-	-	-
Investments in associated undertakings	39	-	-	-	-	-	-	-	-	-	-	-	39
Intangible fixed assets	343	-	-	-	-	-	-	-	-	(9)	-	-	334
Value of in force business		-	1,351	-	-	-	-	-	-	-	-	-	1,351
Property plant and equipment	268	-	-	-	-	-	-	109	-	9	-	56	442
Operating lease assets	2,529	-	-	-	-	(92)	-	-	-	-	-	-	2,437
Investment properties	-	-	-	-	-	-	-	-	-	-	-	(44)	(44)
Other assets	4,162	1,229	4,058	30	-	-	-	(1)	-	-	-	-	9,478
Prepayments and accrued income	1,229	(1,229)	-	-	-	-	-	-	-	-	-	-	(0)
Deferred tax assets	-	-	-	-	-	-	-	-	-	-	-	330	330
Assets of long-term assurance funds	28,336	-	(28,336)	-	-	-	-	-	-	-	-	-	-
Total assets	**176,774**	-	**(60)**	**404**	**14,482**	**(151)**	-	**108**	-	–	-	**342**	**191,899**
Liabilities													
Deposits by banks	22,125	-	-	-	220	-	-	-	-	-	-	-	22,345
Customer accounts	74,401	-	-	1	-	-	-	-	-	-	-	-	74,402
Derivative financial instruments and other trading liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Debt securities in issue	24,834	-	-	-	14,262	-	-	-	-	-	-	-	39,096
Other Borrowed Funds		1,296	-	-	-	-	-	-	-	-	-	-	1,296
Accruals and deferred income	1,582	(1,582)	-	-	-	-	-	-	-	-	-	-	-
Subordinated liabilities	6,337	-	-	-	-	-	-	-	-	-	-	-	6,337
Provision for liabilities and charges	836	-	-	-	-	-	-	-	-	-	-	-	836
Other long-term capital instruments	742	(742)	-	-	-	-	-	-	-	-	-	-	-
Insurance and reinsurance liabilities	-	-	25,903	-	-	-	-	-	-	-	-	-	25,903
Investment contract liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Liabilities of Long Term Assurance Funds	28,336	-	(28,336)	-	-	-	-	-	-	-	-	-	-
Other liabilities	11,697	1,582	2,095	2	-	-	-	-	-	-	(242)	21	15,155
Deferred tax liabilities	-	-	278	-	-	-	-	-	-	-	-	76	354
Retirement benefit obligations	-	-	-	-	-	-	1,101	-	-	-	-	-	1,101
Minority interests – non equity	554	(554)	-	-	-	-	-	-	-	-	-	-	–
Total liabilities	**171,444**	-	**(60)**	**4**	**14,482**	-	**1,101**	-	-	-	**(242)**	**97**	**186,825**
Called up share capital – ordinary shares	146	-	-	-	-	-	-	-	-	-	-	-	146
Called up share capital – preference shares	325	-	-	-	-	-	-	-	-	-	-	-	325
Share premium account	2,058	-	-	-	-	-	-	-	-	-	-	-	2,058
Profit and loss account	2,448	-	-	10	-	(151)	-	108	-	-	242	(85)	2,572
Other reserves	353	-	-	-	-	-	(1,101)	-	-	-	-	330	(418)
Total shareholders' equity	**5,330**	-	-	**10**	-	**(151)**	**(1,101)**	**108**	-	-	**242**	**245**	**4,683**
Minority interests	-	-	-	391	-	-	-	-	-	-	-	-	391
Total liabilities and equity	**176,774**	-	**(60)**	**404**	**14,482**	**(151)**	-	**108**	-	-	-	**342**	**191,899**

Abbey

Appendix 2: Restated Consolidated Balance Sheet at 30 June 2004

Assets	UK GAAP	Reclassification	Insurance Business	New Entities	Securitisation	Leasing	Employee Benefits	Software	Other Intangibles	Goodwill	Dividends	Other	IFRS
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Cash and balances at central banks	398	-	-	101	-	-	-	-	-	-	-	-	499
Treasury bills and other eligible bills	1,100	(1,100)	-	-	-	-	-	-	-	-	-	-	-
Loans and advances to banks	4,642	-	-	-	-	-	-	-	-	-	-	-	4,642
Loans and advances to customers	95,402	1,640	-	-	17,348	(50)	-	-	-	-	-	-	114,340
Trading securities	26,434	2,629	-	(64)	-	-	-	-	-	-	-	-	28,999
Derivative financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-
Other financial instruments at fair value through P&L	-	-	22,694	149	-	-	-	-	-	-	-	-	22,843
Pledged assets	-	-	-	-	-	-	-	-	-	-	-	-	-
Investment securities	932	-	-	93	-	-	-	-	-	-	-	-	1,025
Net Investment in finance leases	1,640	(1,640)	-	-	-	-	-	-	-	-	-	-	-
Debt securities		-	-	-	-	-	-	-	-	-	-	-	-
Equity shares and other variable interest securities	1,529	(1,529)	-	-	-	-	-	-	-	-	-	-	-
Long-term assurance business	2,235	-	(2,235)	-	-	-	-	-	-	-	-	-	-
Investments in associated undertakings	22	-	-	-	-	-	-	-	-	-	-	-	22
Intangible fixed assets	327	-	-	-	-	-	-	-	-	–	-	-	327
Value of in force business		-	1,502	-	-	-	-	-	-	-	-	-	1,502
Property plant and equipment	249	-	-	-	-	-	-	87	-	-	-	-	336
Operating lease assets	2,509	-	-	-	-	(106)	-	-	-	-	-	-	2,403
Investment properties	-	-	1,240	-	-	-	-	-	-	-	-	-	1,240
Other assets	4,637	1,065	4,124	40	-	(1)	-	0	-	-	-	-	9,865
Prepayments and accrued income	1,065	(1,065)	-	-	-	-	-	-	-	-	-	-	–
Deferred tax assets	-	-	-	-	-	-	-	-	-	-	-	270	270
Assets of long-term assurance funds	27,850	-	(27,850)	-	-	-	-	-	-	-	-	-	-
Total assets	**170,971**	-	**(525)**	**319**	**17,348**	**(157)**	-	**87**	-	–	-	**270**	**188,313**
Liabilities													
Deposits by banks	17,716	-	-	-	189	-	-	-	-	-	-	-	17,905
customer accounts	75,949	-	-	1	117	-	-	-	-	-	-	-	76,067
Derivative financial instruments and other trading liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Debt securities in issue	24,303	-	-	-	17,042	-	-	-	-	-	-	-	41,345
Other Borrowed Funds		1,284	-	-	-	-	-	-	-	-	-	-	1,284
Accruals and deferred income	1,582	(1,582)	-	-	-	-	-	-	-	-	-	-	-
Subordinated liabilities	5,815	-	-	-	-	-	-	-	-	-	-	-	5,815
Provision for liabilities and charges	140	-	-	-	-	-	-	-	-	-	-	(2)	138
Other long-term capital instruments	738	(738)	-	-	-	-	-	-	-	-	-	-	-
Insurance and reinsurance liabilities	-	-	24,511	-	-	-	-	-	-	-	-	-	24,511
Investment contract liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Liabilities of Long Term Assurance Funds	27,850	-	(27,850)	-	-	-	-	-	-	-	-	-	-
Other liabilities	10,215	1,582	2,632	19	-	-	-	-	-	-	(122)	(4)	14,322
Deferred tax liabilities	649	-	182	-	-	-	-	-	-	-	-	60	891
Retirement benefit obligations	-	-	-	-	-	-	902	-	-	-	-	-	902
Minority interests – non equity	546	(545.6)	-	-	-	-	-	-	-	-	-	-	–
Total liabilities	**165,503**	-	**(525)**	**20**	**17,348**	-	**902**	-	-	-	**(122)**	**54**	**183,180**
Called up share capital – ordinary shares	147	-	-	-	-	-	-	-	-	-	-	-	147
Called up share capital – preference shares	325	-	-	-	-	-	-	-	-	-	-	-	325
Share premium account	2,115	-	-	-	-	-	-	-	-	-	-	-	2,115
Profit and loss account	2,617	-	-	9	-	(157)	-	87	-	-	122	(66)	2,612
Other reserves	264	-	-	(13)	-	-	(902)	-	-	-	-	282	(369)
Total shareholders' equity	**5,468**	-	-	**(4)**	-	**(157)**	**(902)**	**87**	-	-	**122**	**216**	**4,830**
Minority interests	-	-	-	303	-	-	-	-	-	-	-	-	303
Total liabilities and equity	**170,971**	-	**(525)**	**319**	**17,348**	**(157)**	-	**87**	-	-	-	**270**	**188,313**

Appendix 3: Restated Consolidated Balance Sheet at 31 December 2004

	UK GAAP	Reclassification	Insurance Business	New Entities	Securitisation	Leasing	Employee Benefits	Software	Other Intangibles	Goodwill	Dividends	Other	IFRS
Assets	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Cash and balances at central banks	454	-	-	159	-	-	-	-	-	-	-	-	613
Treasury bills and other eligible bills	1,990	(1,990)	-	-	-	-	-	-	-	-	-	-	-
Loans and advances to banks	10,148	-	-	-	-	-	-	-	-	-	-	-	10,148
Loans and advances to customers	93,210	1,148	-	-	15,319	(40)	-	-	-	-	-	-	109,637
Trading securities	22,011	3,166	-	(64)	-	-	-	-	-	-	-	-	25,113
Derivative financial instruments	-	-	-	-	-	-	-	-	-	-	-	-	-
Other financial instruments at fair value through P&L	-	-	21,323	141	-	-	-	-	-	-	-	-	21,464
Pledged assets	-	-	-	-	-	-	-	-	-	-	-	-	-
Investment securities	672	-	-	93	-	-	-	-	-	-	-	-	765
Net Investment in finance leases	1,148	(1,148)	-	-	-	-	-	-	-	-	-	-	-
Debt securities		-	-	-	-	-	-	-	-	-	-	-	-
Equity shares and other variable interest securities	1,176	(1,176)	-	-	-	-	-	-	-	-	-	-	-
Long term assurance business	2,967	-	(2,967)	-	-	-	-	-	-	-	-	-	-
Investments in associated undertakings	25	-	-	-	-	-	-	-	-	-	-	-	25
Intangible fixed assets	317	-	-	-	-	-	-	-	(147)	14	-	-	184
Value of in force business	-	-	1,848	-	-	-	-	-	-	-	-	-	1,848
Property plant and equipment	246	-	-	-	-	-	-	-	-	-	-	-	246
Operating lease assets	2,341	-	-	-	-	(122)	-	-	-	-	-	-	2,219
Investment properties	-	-	1,560	-	-	-	-	-	-	-	-	-	1,560
Other assets	4,661	1,195	5,029	54	-	-	-	(1)	-	-		-	10,938
Prepayments and accrued income	1,195	(1,195)	-	-	-	-	-	-	-	-	-	-	–
Deferred tax assets	-	-	-	-	-	-	-	-	-	-	-	358	358
Assets of long-term assurance funds	27,180	-	(27,180)	-	-	-	-	-	-	-	-	-	-
Total assets	**169,741**	**-**	**(387)**	**383**	**15,319**	**(162)**	**-**	**(1)**	**(147)**	**14**	**-**	**358**	**185,118**
Liabilities													
Deposits by banks	18,412	-	-	-	221	-	-	-	-	-	-	-	18,633
Customer accounts	78,851	-	-	1	-		-	-	-	-	-	-	78,852
Derivative financial instruments and other trading liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Debt securities in issue	21,969	-	-	-	15,098	-	-	-	-	-	-	-	37,067
Other Borrowed Funds		1,234	-	-	-	-	-	-	-	-	-	-	1,234
Accruals and deferred income	1,729	(1,729)	-	-	-	-	-	-	-	-		-	-
Subordinated liabilities	5,360	-	-	-	-	-	-	-	-	-	-	-	5,360
Provision for liabilities and charges	319	-	-	-	-	-	-	-	-	-	-	(4)	315
Other long-term capital instruments	722	(722)	-	-	-	-	-	-	-	-		-	-
Insurance and reinsurance liabilities	-	-	23,599	-	-	-	-	-	-	-	-	-	23,599
Investment contract liabilities	-	-	-	-	-	-	-	-	-	-	-	-	-
Liabilities of Long Term Assurance Funds	27,180	-	(27,180)	-	-	-	-	-	-	-	-	-	-
Other liabilities	9,213	1,729	2,939	94	-	-	45	-	-	-	-	(4)	14,016
Deferred tax liabilities	550	-	255	-	-	-	-	-	-	-	-	23	828
Retirement benefit obligations	-	-	-	-	-	-	1,195	-	-	-	-	-	1,195
Minority interests – non equity	512	(512)	-	-	-	-	-	-	-	-	-	-	–
Total liabilities	**164,817**	**-**	**(387)**	**95**	**15,319**	**-**	**1,240**	**-**	**-**	**-**	**-**	**15**	**181,099**
Called up share capital – ordinary shares	148	-	-	-	-	-	-	-	-	-	-	-	148
Called up share capital – preference shares	325	-	-	-	-	-	-	-	-	-	-	-	325
Share premium account	2,164	-	-	-	-	-	-	-	-	-	-	-	2,164
Profit and loss account	1,981	-	-	9	-	(162)	(45)	(1)	(147)	14		(28)	1,621
Other reserves	306	-	-	(13)	-		(1,195)					371	(531)
Total shareholders' equity	**4,924**	**-**	**-**	**(4)**	**-**	**(162)**	**(1,240)**	**(1)**	**(147)**	**14**	**-**	**343**	**3,727**
Minority interests	-	-	-	292	-	-	-	-	-	-	-	-	292
Total liabilities and equity	**169,741**	**-**	**(387)**	**383**	**15,319**	**(162)**	**-**	**(1)**	**(147)**	**14**	**-**	**358**	**185,118**

Abbey

Appendix 4: Restated Consolidated Income Statement at 30 June 2004

	UK GAAP	Reclassification	Insurance Business	New Entities	Securitisation	Leasing	Employee Benefits	Software	Other Intangibles	Goodwill	Other	IFRS
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Interest receivable	2,482	-	-	(5)	393	-	-	-	-	-	-	**2,870**
Interest payable	(1,652)	-	-	-	(393)	-	(22)	-	-	-	-	**(2,067)**
Net Interest Income	**830**	-	-	**(5)**	-	-	**(22)**	-	-	-	-	**803**
Dividend income	-	-	-	-	-	-	-	-	-	-	-	-
Fees and commissions receivable	345	-	-	-	-	-	-	-	-	-	-	**345**
Fees and commissions payable	(62)	-	-	-	-	-	-	-	-	-	-	**(62)**
Dealing profits	128	(128)	-	-	-	-	-	-	-	-	-	-
Income from long-term assurance business	-	-	-	-	-	-	-	-	-	-	-	-
Net trading income - Banking	-	128	-	6	-	-	-	-	-	-	-	**134**
Operating income from life assurance	-	-	145	-	-	-	-	-	-	-	-	**145**
Other operating income	117	-	(56)	-	-	11	-	(3)	-	-	12	**81**
Total operating income	**1,358**	-	**89**	**1**	-	**11**	**(22)**	**(3)**	-	-	**12**	**1,446**
Administrative expenses	(865)	-	(122)	(2)	-	-	22	5	-	-	-	**(962)**
Depreciation, amortisation and impairment	(125)	-	-	-	-	(16)	-	(23)	-	-	(11)	**(175)**
Provisions and amounts written off fixed asset investments	(55)	-	-	-	-	-	-	-	-	-	2	**(53)**
Operating profit/loss	**313**	-	**(33)**	**(1)**	-	**(5)**	-	**(21)**	-	-	**3**	**256**
Income from associated undertakings	3	-	-	-	-	-	-	-	-	-	-	**3**
Profit on disposals of Group undertakings	34	-	-	-	-	-	-	-	-	-	-	**34**
Loss on sale or termination of a business	-	-	-	-	-	-	-	-	-	-	-	-
Profit on ordinary activities before tax	**350**	-	**(33)**	**(1)**	-	**(5)**	-	**(21)**	-	-	**3**	**293**
Tax on ordinary activities	(113)	-	33	-	-	-	-	-	-	-	16	**(64)**
Profit on ordinary activities after tax	**237**	-	-	**(1)**	-	**(5)**	-	**(21)**	-	-	**19**	**229**
Minority interests – Non equity	(24)	-	-	-	-	-	-	-	-	-	-	**(24)**
Dividends	(24)	-	-	-	-	-	-	-	-	-	-	**(24)**
Retained profit/loss for the period	**189**	-	-	**(1)**	-	**(5)**	-	**(21)**	-	-	**19**	**181**

Appendix 5: Reconciliation of Movement in Shareholders' Funds

	01-Jan 2004 £ m	30-Jun 2004 £ m	31-Dec 2004 £ m	01-Jan 2005 £ m
Ordinary shareholders' funds – UK GAAP	**4,699**	**4,836**	**4,292**	**4,292**
Retrospective (statutory) IFRS adjustments				
Pensions	(1,101)	(902)	(1,195)	(1,195)
Leasing	(151)	(157)	(162)	(162)
Software capitalisation	108	87	(1)	(1)
Intangible assets	-	-	(133)	(133)
Vacant property provision	-	2	4	4
Stock Option expensing	-	-	(46)	(46)
Dividends	242	122	-	-
Deferred taxation	(90)	(80)	(69)	(69)
Tax effect of the above adjustments	345	291	404	404
Shareholders' funds under IFRS	**4,052**	**4,199**	**3,094**	**3,094**
Prospective (proforma) IFRS adjustments				
Life investment products	-	-	-	(114)
Non equity share reclassified to debt	-	-	-	62
Non trading derivatives	-	-	-	(199)
Securities	-	-	-	52
Revenue recognition	-	-	-	(73)
De-recognition of liabilities	-	-	-	(154)
Deferred tax	-	-	-	29
Other	-	-	-	(52)
Tax effect of the above adjustments	-	-	-	123
Shareholders' funds under IFRS	**4,052**	**4,199**	**3,094**	**2,768**