Cardnet Merchant Services Limited

Annual report and financial statements

2020

Member of Lloyds Banking Group plc

Strategic report

For the year ended 31 December 2020

The directors present their Strategic report and the audited financial statements of Cardnet Merchant Services Limited (the "Company") for the year ended 31 December 2020.

Business overview

The Company is a private limited company incorporated in the United Kingdom, registered in England and Wales and domiciled in England and Wales (registered number: 00735844). The Directors in office during 2020 are listed in the Directors' report and the Company Secretary is A E Mulholland.

The Company is accounted for as a joint venture between Lloyds Bank plc, FDR Limited, LLC (part of Fiserv Inc. Group) and Lloyds Bank Subsidiaries Limited. The principal activity during the year was the provision of services to merchants enabling the acceptance, authorisation and clearing of plastic card transactions. Lloyds Bank plc and Lloyds Bank Subsidiaries Limited are members of the Lloyds Banking Group ("the Group").

The directors aim to continue the development of the business by recruiting new merchants and leveraging Lloyds Banking Group plc ("LBG") corporate relationships with the existing customer base.

Review of the business

The Company's result for the year shows a Profit before tax of £29m (2019: £60m) and Net fees and commission income of £45m (2019: £74m). Full year income has been adversely affected by the impact of COVID-19 from March 2020, with the restrictions of a UK wide lockdown interrupting normal business activity, and many merchants having to close for long periods at a time. As a result of this, activity levels are down 18% vs prior year.

The Net assets are £53m for 2020 (2019: £30m). £30m relates to deferred Dividend for 2019 which is still not paid, with a further £23m of unpaid Dividend relating to 2020. There was no interim Dividend paid in May 2021. Please see page 8 for further details.

Future outlook

The ongoing impact of COVID-19 continues to cause disruption to normal patterns of business activity in the UK, however, as at May 2021, activity levels have largely reached pre-COVID-19 levels as UK restrictions start to lift with transactions reaching 95m (May 2019 98m).

There remains concern regarding the recommencement of the travel sector, in particular International travel where Government restrictions are still particularly tight and subject to last minute change. Key clients in this sector continue to be monitored for credit risk until normal activity resumes. No significant client chargeback risks have been identified at present.

A further overarching concern remains that any new variant of COVID-19, or a delay in the roll out of the vaccination programme, may have a negative impact and result in tightening of restrictions and an economic impact on business activity.

The effects on the UK, European and global economies following the UK's exit from the EU and the impact of the EU-UK Trade and Cooperation Agreement signed on 30 December 2020 (the "EU-UK TCA") remain difficult to predict but may include economic and financial instability, constitutional instability in the UK and other types of risks that could adversely impact the business of the Cardnet Joint Venture. Risks to profitability remain in the event of any further substantial weakening in the UK's economic growth and reduction in consumer demand. Any business based outside of the UK where activity breaches Brexit regulations has been descoped with minimal impact.

Principal risks and uncertainties

The directors consider that the principal area of risk is counterparty credit risk to chargebacks that must be covered by the business in the event of a client failure and a customer does not receive their goods or service. Counterparty credit risk has been actively managed to reduce exposures where appropriate and client engagement with key risk names has been increased to understand latest business performance, with particular focus on those noted on a watchlist of high risk merchants. Further steps have been taken to ensure robust levels of cash on the balance sheet by deferring the 2019 dividend payment and having an in principle credit line agreed with the LBG group of c.£35m.

As a result of the ongoing global health issues, the potential for operational risks remain, notably in the areas of cyber, fraud, people, technology, operational resilience and where there is reliance on third-party suppliers. From an operational perspective, Cardnet had no material operational failures despite working under significant duress in terms of access to the office and personnel challenges that arose from the health implications that result from operating in a global pandemic.

The other key area of focus is the financial risk from lower business activity due to a material external event, including any further impact of COVID-19. The business did demonstrate a robust performance during the pandemic where it remained profitable throughout.

Details of the Company's risk management policy are contained in note 16 to the financial statements.

Key performance indicators ("KPIs")

The Company's two main KPIs are the number of transactions processed and the sterling (£) aggregate value of those transactions, monitored versus prior year and budget and forecast. Activity can also be monitored separately between Credit cards and Debit cards. This transactional activity is the main driver of the profitability in Cardnet and allows for the monitoring of the financial progress of the business and market share in the UK Acquiring market.

Credit cards

During the year ended 31 December 2020 the Company processed £10,333m (2019: £17,026m) transactions by value, a decrease of 39.31% (2019: a decrease of 0.94%) and 122m (2019: 194m) credit card transactions by volume, a decrease of 37.11% (2019: an increase of 1.16%).

Debit cards

During the year ended 31 December 2020 the Company processed £53,305m (2019: £53,199m) transactions by value, an increase of 0.20% (2019: an increase of 8.00%) and 824m (2019: 961m) debit card transactions by volume, a decrease of 14.26% (2019: an increase of 8.06%).

2020 activity levels have been severely impacted by the onset of COVID-19 since March 2020. Government restrictions, including National lockdowns in March and November, and further Regional restrictions across the devolved Nations have resulted in the temporary closure of a number of key merchants, in particular in the non-essential retail, travel and the entertainment sectors. Travel and airlines have been significantly impacted throughout the year with restrictions still in place.

Section 172(1) Statement

In accordance with the Companies Act 2006 (the 'Act'), for the year ended 31 December 2020, the directors provide the following statement describing how they have had regard to the matters set out in section 172(1) of the Act, when performing their duty to promote the success of the Company under section 172.

Statement of Engagement with Employees and Other Stakeholders

In accordance with the Large and Medium-sized Companies and Groups (Financial statements and Reports) Regulations 2008, the following statement also provides details on how the directors have engaged with, and had regard to, the interest of key stakeholders and employees. The Company is controlled by Lloyds Bank plc, a wholly owned subsidiary of LBG. As such, the Company follows many of the processes and practices of the Group whilst being mindful of the requirements of FDR Limited, LLC which holds approximately 49% of the Company's issued share capital.

Strategic report (continued)

For the year ended 31 December 2020

Customers

The Directors ensure the Company as a joint venture between LBG and FDR Limited, LLC strives to achieve the ambitions and behaviours of both Groups, with an emphasis on treating customers correctly and fairly. The Directors agree customer plans, reviewing customer behaviour and getting feedback to ensure these aims are adhered to. Customer pricing is regularly reviewed and where applicable Scheme changes are passed on to clients. The Company strives to bring innovative Card payment solutions to our clients, working with the major Card Schemes and other payment organisations. The business regularly benchmarks its performance and uses insight along with a range of both internal and external research to ensuring ongoing improvement in client experience.

Shareholders

The Company is owned by Lloyds Bank Plc, Lloyds Bank Subsidiaries Limited (both of which are wholly owned subsidiary of LBG), and by FDR Limited, LLC. The Company and the shareholders are party to a shareholders' agreement which sets out the overall objectives of the arrangement and the respective obligations of each of the parties in terms of meeting those objectives. The directors ensure that the strategy, priorities, processes and practices of the Company are aligned to the requirements of the shareholders' agreement and, where required, to those of LBG as the Company's controlling shareholder.

The directors consider that the principal area of risk is counterparty credit risk to chargebacks that must be covered by the business in the event a client fails and a customer does not receive their goods or service.

Further information in respect of the relationship of LBG with its shareholders is included within the Strategic report within the LBG Annual Report and Financial statements for 2020, which does not form part of this report, available on the LBG website.

Communities and the Environment

Whilst the company has a limited physical presence and direct impact on communities and the environment, it does support initiatives within both parent companies including LBG "Helping Britain Prosper”. Employees take part in many company related charitable activities on a local and national level, benefiting from parent Company initiatives including LBG Matched donations.

The business recruits new clients and leverages from the LBG client base to provide innovative payment solutions with both Face to Face and Online/telephony based options.

Further information in respect of Lloyds Banking Group plc's overall approach to engaging with and contributing to the communities in which it operates is included within the Strategic Report within the Lloyds Banking Group plc's Annual Report and Financial statements for 2020, which does not form part of this report. Additional information on LBG's Helping Britain Prosper Plan is available on the LBG website.

Regulators

The Company is regulated by the FCA as part of its regulation of the broader activity of the Group. As set out within the customer section above, a key focus for the Company is treating customers fairly. The approach of the Group, including that of the Company, to managing regulatory change is detailed on page 34 of the LBG Annual Report and Financial statements for 2020, which does not form part of this report, available on the LBG website.

How stakeholder interest has influenced decision making

The directors acknowledge that one of the primary responsibilities of the Board is to ensure the strategy of the Company, as aligned to the shareholders' agreement, is to effectively manage its customer base to generate sustainable returns, central to which is ensuring engagement with stakeholders, and considering in all instances the long-term implications of decisions made, acting at all times to maintain the highest possible standards of conduct.

A number of changes to the Company's board of directors were made in the year, in order to ensure that the Company benefits from the wider backgrounds and sector experience that exist in the Group and to increase financial control and facilitate transparent reporting.

Additionally in 2020 the decision was made to waive a number of fees in order to support our customers during an unprecedented time of challenges and uncertainties. These fees were waived from 1st April to 31st December. The business appreciated that the impact of this virus was felt across the UK and further extended the waiving of some fees until 30th April 2021 in line with lockdown measures. Our terminal leasing partners also operated a client fee reduction scheme throughout 2020 and extended into 2021.

Strategic report (continued)

For the year ended 31 December 2020

Emerging Risks

The key emerging risks relate to how the economy responds to the ongoing uncertainty from the global pandemic. This also has potential for operational risks materialing in the areas of cyber fraud, people, technology and operational resilience, and where there is reliance on third-party suppliers. The company has developed increased agility and resilience to ensure the continued support of colleagues and customers to minimise disruption to ways of working. Additionally the impacts of the UK's exit from the EU will continue to be monitored as the new EU and non-EU trading relationships develop.

General

The directors do not consider there to be any further material issues which need to be included in the Strategic report.

Approved by the board of directors and signed on its behalf by:

s j everett

15th July 2021

S J Everett
Director

Directors' report

For the year ended 31 December 2020

The directors present their report and the audited financial statements for the year ended 31 December 2020.

Dividends

No dividends were paid or proposed during the year ended 31 December 2020 (2019: £49.3m).

Going concern

The directors are satisfied that it is the intention of LBG and Fiserv Inc that the Company will continue to have access to adequate liquidity and capital resources for the foreseeable future, and, accordingly, the financial statements have been prepared on a going concern basis.

The business continues to operate on a profitable basis with strong operational controls and performance through the COVID-19 pandemic.

Counterparty credit risk has been actively managed to reduce exposures where appropriate and client engagement with key risk names has been increased to understand latest business performance. Further steps have been taken to ensure robust levels of cash on the balance sheet by deferring the 2019 dividend payment. Additional funding, if needed, would be arranged via a credit line facility on Commercial terms from Lloyds Bank Plc.

Directors

The directors of the Company who were in office during the year and up to the date of signing the financial statements are shown below:

G D Gould
S J Everett
M G Pieri
M Shernoff

The following are other changes to directors that have taken place between the beginning of the reporting period and the approval of the Annual report and financial statements:

M Shernoff	(appointed 11 February 2020)
P Stunt	(resigned 13 February 2020)
M G Pieri	(appointed 13 February 2020)
T Nash	(resigned 1 November 2020)
S J Everett	(appointed 1 November 2020)

Registered address

The Company's registered address is 25 Gresham Street, London EC2V 7HN.

Information included in the Strategic report

The disclosures for Principal risks and uncertainties, Future outlook and Key performance indicators that would otherwise be required to be disclosed in the Directors' report can be found in the Strategic report on pages 1-4.

Climate Change

The Company is out of scope of the Streamlined Energy and carbon Reporting ("SECR"), as it does not have to report on SECR in its own Director's report where included in the Group SECR statement of a UK Group report. Further information in respect of SECR is included within the LBG Annual Report and Accounts for 2020, which does not form part of this report, available on the LBG website.

Directors' indemnities

LBG has granted to G D Gould and S J Everett, the LBG directors of the Company appointed by and representing the Group, a deed of indemnity through deed poll which constituted 'qualifying third party indemnity provisions' for the purposes of the Companies Act 2006. The deeds were in force during the whole of the financial year and at the date of approval of the financial statements. LBG directors no longer in office but who served on the board of the Company at any time in the financial year have the benefit of this contract of indemnity during that period of service. The indemnity remains in force for the duration of a director's period of office. The deed indemnifies the LBG directors to the maximum extent permitted by law. The deed for current LBG directors is available for inspection at the registered office of the Group. In addition, the Group has in place appropriate LBG directors and officers liability insurance cover which was in place throughout the financial year.

Fiserv, Inc. has granted to MG Pieri and M Shernoff, the FDR Limited, LLC directors of the Company, appropriate Directors and Officers Liability and Company Reimbursement Liability Insurance. This was in force during the whole of the financial year and at the date of approval of the financial statements.

Directors' report (continued)

For the year ended 31 December 2020

Statement of directors’ responsibilities in respect of the financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulation.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006.

Under company law, directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- state whether applicable international accounting standards in conformity with the requirements of the Companies Act 2006 have been followed, subject to any material departures disclosed and explained in the financial statements;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company’s transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006.

Directors’ confirmations

In the case of each director in office at the date the directors’ report is approved:

- so far as the director is aware, there is no relevant audit information of which the company’s auditors are unaware; and
- they have taken all the steps that they ought to have taken as a director in order to make themselves aware of any relevant audit information and to establish that the company’s auditors are aware of that information.

Independent auditors and disclosure of information to auditors

Pursuant to section 487(2) of the Companies Act 2006, the auditors of the Cardnet Merchant Services Limited are deemed re-appointed for each financial year unless the Directors of the Company resolve to terminate their appointment. Following the completion of a tender process, Deloitte LLP are to be appointed as auditors of the Cardnet Merchant Services Limited for accounting periods ending on or after 31 December 2021.

Approved by the board of directors and signed on its behalf by:

s j everett

15th July 2021

S J Everett
Director

Statement of comprehensive income

For the year ended 31 December 2020

	Note	**2020 £'m**	2019 £'m
Interest income		**9**	12
Interest expense		**(4)**	(6)
Net interest income	3	**5**	6
Fees and commission income		**247**	340
Fees and commission expense		**(202)**	(266)
Net fee and commission income	4	**45**	74
Other operating expenses	5	**(21)**	(20)
Profit before tax		**29**	60
Taxation	8	**(5)**	(11)
Profit for the year, being total comprehensive income		**24**	49

The accompanying notes to the financial statements are an integral part of these financial statements.

Balance sheet

As at 31 December 2020

	Note	**2020**	2019
		£'m	£'m
ASSETS			
Cash and cash equivalents		**7**	5
Trade and other receivables	9	**518**	579
Total assets		**525**	584
LIABILITIES			
Borrowed funds	10	**65**	3
Trade and other payables	11	**401**	539
Provision for liabilities and charges	12	**1**	1
Current tax liability		**5**	11
Total liabilities		**472**	554
EQUITY			
Share capital	13	**-**	-
Retained earnings		**54**	30
Total equity		**54**	30
Total equity and liabilities		**526**	584

The accompanying notes to the financial statements are an integral part of these financial statements.

The financial statements on pages 7-20 were approved by the board of directors and were signed on its behalf by:

s j everett

15th July 2021

S J Everett
Director

Statement of changes in equity

For the year ended 31 December 2020

	Share capital £'m	Retained earnings £'m	Total equity £'m
At 1 January 2019	-	30	30
Profit for the year being total comprehensive income	-	49	49
Dividend paid to equity holders of the Company	-	(49)	(49)
At 31 December 2019	**-**	**30**	**30**
Profit for the year being total comprehensive income	-	24	24
Dividend paid to equity holders of the Company	-	-	-
At 31 December 2020	**-**	**54**	**54**

The accompanying notes to the financial statements are an integral part of these financial statements.

Cash flow statement

For the year ended 31 December 2020

	2020 £'m	2019 £'m
Cash flows (used in)/generated from operating activities		
Profit before tax	**29**	60
Adjustments for:		
- Interest income	**(9)**	(12)
- Interest expense	**4**	6
Changes in operating assets and liabilities:		
- Net (increase)/decrease in Trade and other receivables	**61**	(10)
- Net (decrease)/increase in Trade and other payables	**(138)**	6
Cash (used in)/generated from operations	**(53)**	50
Tax paid	**(11)**	(11)
Net cash (used in)/generated from operating activities	**(64)**	39
Cash flows generated from investing activities		
Interest income	**9**	12
Net cash generated from investing activities	**9**	12
Cash flows used in financing activities		
Interest expense	**(4)**	(6)
Dividends paid	**-**	(49)
Net cash used in financing activities	**(4)**	(55)
Change in Cash and cash equivalents	**(60)**	(4)
Cash and cash equivalents at beginning of year	**2**	6
(Net bank overdrafts)/cash and cash equivalents at end of year	**(58)**	2
(Net bank overdrafts)/cash and cash equivalents comprise		
Cash at bank	**7**	5
Bank overdraft (see note 10)	**(65)**	(3)
(Net bank overdrafts)/cash and cash equivalents	**(58)**	2

The accompanying notes to the financial statements are an integral part of these financial statements.

Notes to the financial statements
For the year ended 31 December 2020

1. Accounting policies

1.1 Basis of preparation

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied in both years presented, unless otherwise stated.

These financial statements have been prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 ('IRFS') and the applicable legal requirements of the Companies Act 2006.

There are no new IFRS pronouncements relevant to the Company requiring adoption in these financial statements.

Details of those pronouncements which will be relevant to the Company but which were not effective at 31 December 2020 and which have not been applied in preparing these financial statements are given in note 20. No standards have been early adopted.
The financial statements have been prepared on a going concern basis as detailed in the Directors' report and under the historical cost convention.

1.2 Income recognition

Foreign currency

The financial statements are presented in Sterling which is the Company's functional and presentation currency. Foreign currency transactions are translated into Sterling at the exchange rate prevailing at the date of the transaction. Exchange gains and losses resulting from the settlement of such transactions are recognised in the Statement of comprehensive income.

Exchange gains and losses arising from the translation of monetary assets and liabilities at the exchange rate prevailing at the Balance sheet date are recognised in the Statement of comprehensive income.

Fees and commission income and expense

Fees and commissions are recognised on an accruals basis when the service has been provided. These services comprise initialisation and ongoing fees for services delivered to merchants. Revenue is recognised net of chargebacks and commission clawbacks.

Expenses directly attributable to merchants acquiring business are recognised through Fees and commission expense. All other expenses are recognised through Other operating expenses.

1. Accounting policies (continued)

1.3 Financial assets and liabilities

Financial assets comprise Cash and cash equivalents, Amounts due from group undertakings, Amounts owed by card schemes, Amounts owed by merchants, Other trade receivables and Accrued income. Financial liabilities comprise Bank overdraft with group undertakings, Amounts owed to merchants, Other creditors and accruals and Amounts owed to related undertakings.

Financial assets and liabilities are recognised when the Company becomes a party to the contractual provisions of the instrument. Financial assets and liabilities are derecognised when the rights to receive cash flows, or obligations to pay cash flows, have expired.

Interest bearing financial assets and financial liabilities are recognised and measured at amortised cost inclusive of transaction costs, using the effective interest rate method.

1.4 Dividends paid

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

1.5 Cash and cash equivalents

For the purposes of the Balance sheet and Cash flow statement, Cash and cash equivalents and Bank overdrafts with group undertakings comprise balances with less than three months' maturity.

1.6 Taxation

Tax expense comprises current and deferred tax. Current and deferred tax are charged or credited in the statement of comprehensive income except to the extent that the tax arises from a transaction or event which is recognised, in the same or a different period, outside the statement of comprehensive income (either in other comprehensive income, directly in equity, or through a business combination), in which case the tax appears in the same statement as the transaction that gave rise to it.

Current tax is the amount of corporate income taxes expected to be payable or recoverable based on the profit for the period as adjusted for items that are not taxable or not deductible, and is calculated using tax rates and laws that were enacted or substantively enacted at the Balance sheet date.

Current tax includes amounts provided in respect of uncertain tax positions when management expects that, upon examination of the uncertainty by Her Majesty's Revenue and Customs ("HMRC") or another tax authority, it is more likely than not that an economic outflow will occur. Provisions reflect management's best estimate of the ultimate liability based on their interpretation of tax law, precedent and guidance, informed by external tax advice as necessary. Changes in facts and circumstances underlying these provisions are reassessed at each Balance sheet date, and the provisions are re-measured as required to reflect current information.

Deferred tax is recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Balance sheet. Deferred tax is calculated using tax rates and laws that have been enacted or substantively enacted at the Balance sheet date, and which are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax liabilities are generally recognised for all taxable temporary differences but not recognised for taxable temporary differences arising on investments in subsidiaries, associates and joint arrangements where the reversal of the temporary difference can be controlled and it is probable that the difference will not reverse in the foreseeable future. Deferred tax liabilities are not recognised on temporary differences that arise from goodwill which is not deductible for tax purposes.

Deferred tax assets are recognised to the extent it is probable that taxable profits will be available against which the deductible temporary differences can be utilised, and are reviewed at each Balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are not recognised in respect of temporary differences that arise on initial recognition of assets and liabilities acquired other than in a business combination. Deferred tax is not discounted.

1.7 Trade and other receivables

Trade and other receivables are measured at amortised cost, less provision for impairment.

1. Accounting policies (continued)

1.8 Trade and other payables

Trade and other payables are measured at amortised cost.

1.9 Provision for liabilities and charges

Provisions are recognised in respect of present obligations arising from past events where it is probable that outflows of resources will be required to settle the obligations and they can be reliably estimated. In line with IAS 37 an event is only considered probable, and therefore a provisions raised in the Cardnet business, if the probability of a loss occurring is deemed 'more likely than not' to happen.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outlaws of resources are uncertain or cannot be measured reliably.

2. Critical accounting estimates and judgements in applying accounting policies

The preparation of financial statements in conformity with the requirements of the Companies Act 2006 ('IFRS') and the applicable legal requirements of the Companies Act 2006 requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although those estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates.

Estimation of income taxes includes the assessment of recoverability of deferred tax assets. Deferred tax assets are only recognised to the extent they are considered more likely than not to be recoverable based on existing tax laws and forecasts of future taxable profits against which the underlying tax deductions can be utilised.

There are no significant estimates or judgements that have been used in the preparation of these financial statements.

3. Net interest income

	2020	2019
	£'m	£'m
Group interest income (see note 15)	**9**	12
Group interest expense (see note 15)	**(4)**	(6)
	5	6

4. Net fee and commission income

	2020	2019
	£'m	£'m
Fee and commission income		
Service charges	**237**	324
Commission receivable	**10**	16
	247	340
Fee and commission expense		
Other fees and commission payable	**(202)**	(266)
	45	74

Included in Other fees and commission payable is £14m (2019: £14m) payable to the related undertaking, FDR Limited, LLC (see note 15).

Notes to the financial statements (continued)

For the year ended 31 December 2020

5. Other operating expenses

	2020 £'m	2019 £'m
Recharges relating to salary and other related costs (see note 6 and 15)	**11**	13
Change in provision, operational losses and fraud	**5**	1
Charge payable to Lloyds Bank plc (see note 15)	**3**	3
Other expenses	**2**	3
	21	20

Charges payable to Lloyds Bank plc are expenses incurred in Lloyds Bank plc on behalf of the Company which are recharged to the Company. Fees payable to the Company's auditors for the audit of the financial statements of £0.03m (2019: £0.03m) have been borne by a fellow group company and are recharged to the Company.

6. Staff costs

The Company did not have any employees during the year (2019: none). Staff who manage the affairs of the Company are employed by two of the shareholders, Lloyds Bank plc and FDR Limited, LLC. The costs of these employees are recharged to the Company.

7. Directors' emoluments

The amounts paid to the directors in respect of services to the Company were £nil (2019: £nil). The amounts paid to the directors in respect of compromise agreements were £nil (2019: £nil). No director received accrued pensions under a defined benefit scheme operated by Lloyds Bank plc (2019: none). No director received shares under long term incentive plans during the year (2019: none). None of the directors exercised share options (2019: none).

8. Taxation

	2020 £'m	2019 £'m
a) Analysis of charge for the year		
UK corporation tax:		
- Current tax on taxable profit for the year	**5**	11

Corporation tax is calculated at a rate of 19.00% (2019: 19.00%) of the taxable profit for the year.

b) Factors affecting the tax charge for the year

A reconciliation of the charge that would result from applying the standard UK corporation tax rate to the profit before tax to the actual tax charge for the year is given below:

	2020 £'m	2019 £'m
Profit before tax	**29**	60
Tax charge thereon at UK corporation tax rate of 19.00% (2019: 19.00%)	**5**	11
Tax charge on profit on ordinary activities	**5**	11
Effective rate	**17.2%**	18.3%

The Finance Act 2016 reduced the main rate of corporation tax to 17% with effect from 1 April 2020. This reduction was superseded by The Finance Act 2020 which was enacted on 22 July 2020, and maintained the main rate of corporation tax at 19% with effect from 1 April 2020.

On 3 March 2021, the UK Government announced its intention to increase the rate of corporation tax from 19% to 25% with effect from 1 April 2023. The effect of this proposed rate change on the Company's deferred tax balances has been assessed and is not significant.

9. Trade and other receivables

	2020 **£'m**	2019 £'m
Amounts due from group undertakings (see note 15)	**315**	323
Amounts owed by card schemes	**176**	227
Amounts owed by merchants	**6**	2
Other trade receivables	**-**	2
Accrued income	**21**	25
	518	579

Amounts due from group undertakings is unsecured, interest bearing and repayable on demand. All Amounts due from group undertakings are included within Stage 1 for IFRS 9 purposes. Any expected credit losses are considered to be immaterial in either year. The average rate of net interest earned during the year was 1.55% (2019: 1.69%). The fair value of Trade and other receivables is equal to its carrying value. No provisions have been recognised in respect of these amounts. Further analysis of Amounts owed by card schemes, Amounts owed by merchants and Other trade receivables is given in note 16.1. All other balances are due within one year.

10. Borrowed funds

	2020 **£'m**	2019 £'m
Bank overdraft with group undertakings (see note 15)	**65**	3

£65m overdrawn position as at 31 December 2020 was cleared in January 2021.

Bank overdraft with group undertakings is unsecured and repayable on demand, although there is no expectation that such a demand would be made. Bank overdraft with group undertakings is interest bearing at variable rates funded over 5 years,

11. Trade and other payables

	2020 **£'m**	2019 £'m
Amounts owed to merchants	**386**	533
Other creditors and accruals	**12**	4
Amounts owed to related undertakings (see note 15)	**3**	2
	401	539

Amounts owed to related undertakings is non-interest bearing, unsecured and repayable on demand, although there is no expectation such a demand would be made. The fair value of Trade and other payables is equal to its carrying value.

12. Provision for liabilities and charges

	Total **£'m**
At 1 January 2019	1
Charge for the year	-
Utilised during the year	-
At 31 December 2019	**1**
Charge for the year	5
Utilised during the year	(5)
At 31 December 2020	**1**

Chargeback losses in 2020 saw a significant uplift due to COVID-19 with one key client loss of £3m, following client failure and subsequent chargebacks received.

Notes to the financial statements (continued)

For the year ended 31 December 2020

13. Share capital

	2020 £'m	2019 £'m
Allotted, issued and fully paid		
650 (2019: 650) "A" ordinary shares of £1 each	**-**	-
651 (2019: 651) "B" ordinary shares of £1 each	**-**	-
1,300 (2019: 1,300) deferred shares of £1 each	**-**	-
	-	-

At 31 December 2020, the authorised share capital of the Company was £2,601 divided into 650 'A' ordinary shares of £1 each and 651 'B' ordinary shares of £1 each and 1,300 deferred shares of £1 each.

On winding up, the deferred shareholders have priority over the ordinary shareholders to receive repayment of capital. The ordinary shareholders have equal voting rights and the deferred shareholders have no voting rights.

FDR Limited, LLC holds 650 'A' ordinary shares, Lloyds Bank plc holds 637 'B' ordinary shares and Lloyds Bank Subsidiaries Limited holds 14 'B' ordinary shares. Lloyds Banking Group plc holds 1,300 deferred shares.

14. Dividends

	2020 £'m	**2020 £ per share**	2019 £'m	2019 £ per share
	-	**-**	49	37,899

The ordinary shareholders (the holders of the 'A' ordinary shares and the 'B' ordinary shares) have priority over the deferred shareholders (the holders of the deferred shares) to receive dividends distributed up to the 'deferred share threshold' as defined in the Company's articles of association.

Dividends above the threshold are to be distributed as follows: 99.00% amongst the ordinary shareholders and 1.00% amongst the deferred shareholders.

15. Related party transactions

A number of transactions are entered into with related parties in the normal course of business. These include loan and fee transactions. A summary of the outstanding balances at the year end and the related income and expense for the year is set out below.

	2020 £'m	2019 £'m
Amounts due from group undertakings		
Lloyds Bank plc (see note 9)	**315**	323
Amounts owed to related undertakings		
FDR Limited (see note 11)	**3**	2
Cash and cash equivalents held with group undertakings		
Lloyds Bank plc	**7**	5
Bank overdraft held with group undertaking		
Lloyds Bank plc (see note 10)	**65**	3
Interest income		
Lloyds Bank plc (see note 3)	**9**	12

15. Related party transactions (continued)

	2020 £'m	2019 £'m
Interest expense		
Lloyds Bank plc (see note 3)	**4**	6
Fees and commission expense		
FDR Limited (see note 4)	**14**	14
Recharge relating to salary and other related costs		
Lloyds Bank plc (see note 5)	**11**	13
Amounts charged by group undertakings		
Lloyds Bank plc (see note 5)	**3**	3
Dividend paid		
FDR Limited, LLC	**-**	24
Lloyds Bank plc	**-**	24
Lloyds Bank Subsidiaries Limited	**-**	1
Total Dividend paid (see note 14)	**-**	49

In 2020 there has been a re-pricing event in respect of LBG businesses who are clients of Cardnet Merchant Services Limited. As a result there has been a £5m reduction to fee and commission income to ensure that pricing remains in line with market rates. The re-pricing was agreed 1st January 2020 and subsequently implemented as such. The re-price involved moving pricing from a blended tariff to an interchange ++ tariff which is used by the majority of Cardnet's larger clients. This was agreed and approved by the Cardnet Board which includes all JV partners.

The above balances are unsecured in nature and are expected to be settled in cash or by cash equivalents. Transactions in the year are those reflected through the Statement of comprehensive income.

Deposits with Lloyds Bank plc are placed on normal commercial terms.

Key management personnel

Key management personnel are those persons having authority and responsibility for planning and controlling the activities of the Company. Accordingly, key management comprises of the directors of the Company, the directors of FDR Limited and the members of the LBG board. There were no transactions between the Company and key management personnel during the current or preceding year. Key management personnel are employed by other companies within the Group or FDR Limited and consider that their services to the Company are incidental to their other activities within those corporations.

16. Financial risk management

The Company's operations expose it to credit risk, liquidity risk, geographical and sector concentrations of risk, business risk and foreign exchange risk; it is not exposed to any significant market risk or interest rate risk.

The directors are responsible for establishing a framework for evaluating, measuring, monitoring and controlling risk. They are responsible for ensuring that the risks within the business are identified, assessed, monitored and controlled. These controls and procedures where relevant comply with Lloyds Banking Group policies and standards. All risk policies are reviewed and authorised by the Company's board of directors, or as appropriate the risk policy owners representing the Company which comprises directors appointed by Lloyds Bank plc and FDR Limited, LLC.

A description of the Company's financial assets/liabilities and associated accounting is provided in note 1.

16.1 Credit risk

Credit risk management

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. Credit risk arises from extending credit in all forms, where there is a possibility that a counterparty may default. The Company is committed to a strong credit culture that recognises the need to ensure that risk assets are of high quality.

16. Financial risk management (continued)

16.1 Credit risk (continued)

Credit risk mitigation

- The Company maintains and adheres to credit policy document in compliance with policies established by the Group Risk Management department within the Group.
- Credit principles and policy: Group Risk sets out the group credit principles and policy according to which credit risk is managed, which in turn is the basis for divisional and business unit credit policy. Principles and policy are reviewed regularly and any changes are subject to a review and approval process. Business unit policy includes lending guidelines, which define the responsibilities of lending officers and provide a disciplined and focused benchmark for credit decisions.
- Credit scoring: Every new merchant is subject to a detailed credit check which includes a review of financial information; a credit reference agency search, review of terms and conditions, associated websites and site visit reports (as necessary). Full Know Your Customers and Know Your Business checks are undertaken in line with the Company's anti-money laundering policies.
- The prime risk for the Company arises from the chargeback rules of the card schemes in which the Company operates, and if the financial strength of the merchant is weak, risk mitigation is considered. This includes taking guarantees (including from Lloyds Bank plc), cash security and deferral of funds to the merchant.
- Stress testing and scenario analysis at a divisional level: The credit portfolio is also subjected to stress testing and scenario analysis, to simulate outcomes and calculate their associated impact.
- Key sectors of concern for Cardnet from a Chargeback perspective are Travel, Tour Operators, Airlines and Cruise-lines.
- Gross exposure that Cardnet has (across all merchants) is seasonal and ranges from £1,500m to £2,500m.
- Total value of guarantees that Cardnet has in place to mitigate the risk of irrecoverable chargebacks is underwritten by Lloyds Bank plc under the Lloyds Bank Credit Risk Responsibility (CRR) arrangement. The credit risk underwritten by Lloyds Bank plc amounted to £40m at 31 December 2020 (£78m in 2019).
- Total value of Cardnet specific cash securities held equates to £33m.
- Cardnet has £40m by way of CRR and £33m by way of cash collateral held, controlled by either Cardnet directly or managed by LBG Commercial Bank.
- Additional funding, if needed, would be arranged via a credit line facility on Commercial terms from Lloyds Bank Plc, the terms of which are principally agreed.

Financial assets subject to credit risk

The maximum exposure to credit risk arising on the Company's financial assets at the reporting date is disclosed in the table below and equates to carrying value.

	2020 £'m	2019 £'m
Cash and cash equivalents	**7**	5
Amounts due from group undertakings	**315**	324
All other Trade and other receivables	**203**	255
	525	584

Credit risk is not considered to be significant to the Company as Cash and cash equivalents represent bank accounts with another Group subsidiary, Lloyds Bank plc, which had a credit rating of A+ (2019:A+) per Standard and Poor's at the end of the year. Amounts due from group undertakings also represent balances owed by Lloyds Bank plc. Given the credit rating of Lloyds Bank plc, management does not expect the counterparty to fail to meet its obligations.

For All other Trade and other receivables, credit risk arises from Amounts owed by card schemes, Amounts owed by merchants, Other trade receivables and Accrued income. The credit risk associated with these balances is considered good quality with a lower probability of default and therefore is categorised as stage 1.

16. Financial risk management (continued)

16.2 Liquidity risk

Liquidity risk is the risk that the Company is unable to meet its obligations as they fall due. This is not considered to be a significant risk to the Company as collection from the scheme is completed before payment to the merchants. This is further supported by the Company being funded by the shareholders (Lloyds Bank plc and FDR Limited, LLC).

The table below sets out the undiscounted cash flows payable by the Company in respect of financial liabilities, according to contractual maturity into relevant maturity groupings based on the remaining period at the balance sheet date.

16.2 Liquidity risk (continued)

As at 31 December 2020

	Up to 1 month	**1-3 months**	**3-12 months**	**1-5 years**	**Total**
	£'m	**£'m**	**£'m**	**£'m**	**£'m**
Amounts owed to merchants	386	-	-	-	386
Other creditors and accruals	7	4	1	-	12
Amounts owed to related parties	3	-	-	-	3
Borrowed funds	65	-	-	-	65
	461	4	1	-	466

As at 31 December 2019

	Up to 1 month	1-3 months	3-12 months	1-5 years	Total
	£'m	£'m	£'m	£'m	£'m
Amounts owed to merchants	533	-	-	-	533
Other creditors and accruals	2	1	2	-	5
Amounts owed to related parties	2	-	-	-	2
Borrowed funds	3	-	-	-	3
	540	1	2	-	543

The Company has sufficient funding to meet liquidity needs as there is a current funding arrangement with Lloyds Bank plc.

16.3 Geographical and sector concentrations of risk

The Company operates primarily within the UK. There is an exposure to particular sectors arising where there is a long period of time elapsing between payment and the provision of goods and services. The resulting risk is closely monitored and controlled with agreed parameters set by the Company's credit policy.

16.4 Business risk

Business risk is the risk that the Company's earnings are adversely impacted by a suboptimal business strategy or the suboptimal implementation of the strategy. In assessing business risk consideration is given to internal and external factors such as products, funding, resource capability and economic, political and regulatory factors.

Through regular reports and oversight business risk is managed by corrective actions to plans and reductions in exposures where necessary.

16.5 Financial strategy

The Company uses financial instruments to mitigate interest rate risk. However, the Company does not trade in financial instruments.

17. Capital disclosures

The Company's objectives when managing capital are to safeguard the entity's ability to continue as a going concern, provide an adequate return to its shareholders through pricing products and services commensurately with the level of risk and, indirectly, to support the Group's regulatory capital requirements.

The Company's parent manages the Company's capital structure and advises the board of directors to consider making adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the board of directors may adjust the amount of dividends to be paid to shareholders, return capital to shareholders, issue new shares, sell assets, or request a revolving credit facility from Lloyds Banking Group Plc.

The Company's capital comprises all components of equity, movements in which appear in the Statement of changes in equity. The Company receives its funding requirements from its fellow group undertakings and does not raise funding externally.

18. Contingent liabilities and capital commitments

There were no contingent liabilities or contracted capital commitments at the Balance sheet date (2019: £nil).

19. Post balance sheet events

There are no post balance sheet events to note.

20. Future developments

The following pronouncements may have a significant effect on the Company's financial statements but are not applicable for the year ending 31 December 2020 and have not been applied in preparing these financial statements. Except as disclosed below, the full impact of these accounting changes is being assessed by the Company, however, the initial view is that this is not expected to cause any material adjustments to the reported numbers in the financial statements.

Pronouncement	Nature of change	Effective date
Interest Rate Benchmark Reform (Amendments to IFRS9, IAS 39 and IFRS 7)	The IASB's Phase 2 amendments in response to issues arising from the planned replacement of interest rate benchmarks in a number of jurisdictions are effective for annual periods beginning on or after 1 January 2021. Under these amendments, an immediate gain or loss is not recognised in the income statement where the contractual cash flows of a financial asset or financial liability are amended as a direct consequence of the rate reform and the revised contractual terms are economically equivalent to the previous terms. In addition, hedge accounting is continued for relationships that are directly affected by the reform. These amendments are not expected to have a significant impact on the Company.	Annual periods beginning on or after 1 January 2020.
Minor amendments to other accounting standards	The IASB has issued a number of minor amendments to IFRSs effective 1 January 2021 and 1 January 2022 (including IFRS 9 Financial Instruments and IAS 37 Provisions, Contingent Liabilities and Contingent Assets). These amendments are not expected to have a significant impact on the Company.	1 January 2021 and 1 January 2022

There are no other standards or interpretations that are not yet effective and that would be expected to have a material impact on the Company.

21. Ultimate parent undertaking and controlling party

The terms of the contractual agreement between the shareholders are such that the Company is accounted for as a joint venture under the requirement of IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities and therefore does not have an ultimate parent undertaking.

Independent auditors’ report to the members of Cardnet Merchant Services Limited

Report on the audit of the financial statements

Opinion

In our opinion, Cardnet Merchant Services Limited’s financial statements:

- give a true and fair view of the state of the company’s affairs as at 31 December 2020 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements, included within the Annual report and financial statements (the “Annual Report”), which comprise: the Balance sheet as at 31 December 2020; the Statement of comprehensive income, the Statement of changes in equity and the Cash flow statement for the year then ended; and the notes to the financial statements, which include a description of the significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (“ISAs (UK)”) and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors’ responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We remained independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC’s Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Conclusions relating to going concern

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the company’s ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In auditing the financial statements, we have concluded that the directors’ use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

However, because not all future events or conditions can be predicted, this conclusion is not a guarantee as to the company's ability to continue as a going concern.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors’ report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic report and Directors' report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on our work undertaken in the course of the audit, the Companies Act 2006 requires us also to report certain opinions and matters as described below.

Strategic report and Directors' report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic report and Directors' report for the year ended 31 December 2020 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic report and Directors' report.

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of directors' responsibilities in respect of the financial statements, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud, is detailed below.

Based on our understanding of the company and industry, we identified that the principal risks of non-compliance with laws and regulations related to breaches of industry laws and regulations such as, but not limited to, regulations relating to the Financial Services and Markets Act 2000 (FSMA), and we considered the extent to which non-compliance might have a material effect on the financial statements. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting manual journal entries to manipulate financial performance. Audit procedures performed by the engagement team included:

- Inquiries of management, including consideration of known or suspected instances of non-compliance with laws and regulations or fraud;
- Performing testing over period end adjustments;
- Incorporating unpredictability into the nature, timing and / or extent of testing;
- Challenging assumptions and judgements made by management; and
- Identifying and testing journal entries, in particular any manual journal entries posted by unexpected or unusual users, posted with descriptions indicating a higher level of risk, and those posted late with a favourable impact on financial performance.

There are inherent limitations in the audit procedures described above. We are less likely to become aware of instances of non-compliance with laws and regulations that are not closely related to events and transactions reflected in the financial statements. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditors' report.

Use of this report

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not obtained all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Christopher J Dalton

Christopher Dalton (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
Edinburgh
16 July 2021