SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20-F

☐ REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g)
OF THE SECURITIES EXCHANGE ACT OF 1934
OR
☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
OR
☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

LLOYDS TSB GROUP plc
(Exact name of Registrant as Specified in Its Charter)

Scotland

(Jurisdiction of Incorporation or Organization)

71 Lombard Street
London EC3P 3BS
United Kingdom
(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Ordinary shares of nominal value 25 pence each, represented by American Depositary Shares.	The New York Stock Exchange.

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the Form 20-F

Ordinary shares, nominal value 25 pence each, as of 31 December 2001 5,564,358,845

Limited voting shares, nominal value 25 pence each, as of 31 December 2001 78,947,368

Preference shares, nominal value 25 pence each, as of 31 December 2001 0

Preference shares, nominal value $.25 cents each, as of 31 December 2001 0

Preference shares, nominal value €.25 cents each, as of 31 December 2001 0

Preference shares, nominal value Japanese ¥25 each, as of 31 December 2001 0

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 ☐ Item 18 ☒

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PRESENTATION OF INFORMATION

In this annual report, references to “Lloyds TSB Group” are to Lloyds TSB Group plc and its subsidiary and associated undertakings; references to “Lloyds TSB Bank” are to Lloyds TSB Bank plc; and references to the “Consolidated Financial Statements” are to Lloyds TSB Group’s Consolidated Financial Statements included in this annual report. References to the “Financial Services Authority” are to the United Kingdom (the “UK”) Financial Services Authority.

Lloyds TSB Group publishes its Consolidated Financial Statements expressed in British pounds (“pounds sterling”, “sterling” or “£”), the lawful currency of the UK. In this annual report, references to “pence” and “p” are to one-hundredth of one pound sterling; references to “US dollars”, “US$” or “$” are to the lawful currency of the United States (the “US”); references to “cent” are to one-hundredth of one US dollar; and references to “euro” or “€” are to the lawful currency of the member states of the European Union that have adopted a single currency in accordance with the Treaty establishing the European Communities, as amended by the Treaty of European Union. Solely for the convenience of the reader, this annual report contains translations of certain pounds sterling amounts into US dollars at specified rates. These translations should not be construed as representations by Lloyds TSB Group plc that the pounds sterling amounts actually represent such US dollar amounts or could be converted into US dollars at the rate indicated or any other rate. Unless otherwise stated, the translations of pounds sterling into US dollars have been made at the noon buying rate in New York City for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York (the “Noon Buying Rate”) in effect on 31 December 2001, which was $1.4543 = £1.00. The Noon Buying Rate on 31 December 2001 differs from certain of the actual rates used in the preparation of the Consolidated Financial Statements, which are expressed in pounds sterling, and therefore US dollar amounts appearing in this annual report may differ significantly from actual US dollar amounts which were translated into pounds sterling in the preparation of the Consolidated Financial Statements in accordance with accounting principles generally accepted in the UK.

RECENT SEC RELEASES

On 12 December 2001, the Securities and Exchange Commission (SEC) issued ‘Cautionary Advice Regarding Disclosure About Critical Accounting Policies’. The disclosures recommended by this advice are set out on pages 17 and 18 under ‘Critical accounting policies’.

On 22 January 2002, the SEC issued ‘Statement about Management's Discussion and Analysis of Financial Condition and Results of Operations’. The disclosures recommended by this Statement have been incorporated into ‘Operating and Financial Review and Prospects’ on pages 63 to 65 in respect of liquidity and capital resources (including off-balance sheet arrangements and disclosures about contractual obligations and commercial commitments) and on page 82 in respect of related party transactions. Lloyds TSB Group does not hold significant non-exchange traded commodity contracts which are accounted for at fair value.

BUSINESS OVERVIEW

Lloyds TSB Group is a leading UK-based financial services group, whose businesses provide a comprehensive range of banking and financial services in the UK and overseas. At 31 December 2001 total Lloyds TSB Group assets were £236,539 million and Lloyds TSB Group had over 81,000 employees. Lloyds TSB Group plc's market capitalisation at that date was some £41,500 million. The profit on ordinary activities before tax for the 12 months to 31 December 2001 was £3,550 million and the risk asset ratios as at that date were 9.2 per cent for total capital and 8.4 per cent for tier 1 capital.

The operations of Lloyds TSB Group in the UK were conducted through approximately 2,300 branches of Lloyds TSB Bank, Lloyds TSB Scotland plc and Cheltenham & Gloucester plc at the end of 2001. International business is conducted mainly in the Americas, New Zealand and continental Europe. Lloyds TSB Group's services in these countries are offered through a combination of branches of Lloyds TSB Bank and subsidiary companies, principally The National Bank of New Zealand Limited, New Zealand's second largest bank measured by assets during 2001, and Losango in Brazil. Lloyds TSB Group also offers offshore banking facilities in a number of countries.

The following table shows the profit before tax of Lloyds TSB Group's UK Operations and its International Operations in each of the last three years.

	2001	2000	1999
	£m	£m	£m
UK Operations	**2,984**	3,427	3,201
International Operations	**566**	433	455
Profit before tax	**3,550**	3,860	3,656

Lloyds TSB Group's activities are organised into three segments: UK Retail Banking and Mortgages, Insurance and Investments and Wholesale Markets and International Banking. Services provided by UK Retail Banking and Mortgages encompass the provision of banking and other financial services to personal and small business customers, private banking, stockbroking and mortgages. Insurance and Investments offers life assurance, pensions and investment products, general insurance and fund management services. Wholesale Markets and International Banking provides banking and related services for major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses, including venture capital finance. It also provides asset finance and share registration services to personal and corporate customers, manages Lloyds TSB Group's activities in financial markets through its Treasury function and provides banking and financial services overseas. Lloyds TSB Group measures the profitability of its segments using the concept of contribution. This concept is explained under "Operating and Financial Review and Prospects - Line of business information - Summary".

The following table shows the contribution of Lloyds TSB Group's UK Retail Banking and Mortgages, Insurance and Investments and Wholesale Markets and International Banking segments and central group items in each of the last three fiscal years.

	2001	2000	1999
	£m	£m	£m
UK Retail Banking and Mortgages	**1,588**	1,665	1,657
Insurance and Investments	**1,601**	1,425	843
Wholesale Markets and International Banking	**1,381**	1,223	1,207
Central group items	**(108)**	(118)	119
Contribution	**4,462**	4,195	3,826

Contribution is defined as profit before tax before taking into account the unusual items set out under "Operating and Financial Review and Prospects - unusual items".

Lloyds TSB Group plc was incorporated as a public limited company and registered in Scotland under the UK Companies Act 1985 on 21 October 1985 with the registered number 95000. Lloyds TSB Group plc's registered office is Henry Duncan House, 120 George Street, Edinburgh EH2 4LH, Scotland, and its principal executive offices in the UK are located at 71 Lombard Street, London EC3P 3BS, United Kingdom, telephone number 011 44 (0) 20 7626 1500.

SELECTED CONSOLIDATED FINANCIAL DATA

The selected consolidated financial information set out in the table below has been derived from the annual reports and accounts of Lloyds TSB Group plc for each of the past five years adjusted for subsequent changes in accounting policy and presentation.

Following the merger in the UK of Price Waterhouse and Coopers & Lybrand, which was completed on 1 July 1998, the resulting partnership has been conducting business under the name of PricewaterhouseCoopers. The Consolidated Financial Statements for the years ended 31 December 2001, 2000, 1999 and 1998 have been audited by PricewaterhouseCoopers, independent accountants. The Consolidated Financial Statements for the year ended 31 December 1997 have been audited by Price Waterhouse, independent accountants.

The Consolidated Financial Statements have been prepared in accordance with UK GAAP, which differ in certain significant respects from US GAAP. A discussion of such differences and a reconciliation of certain UK GAAP amounts to US GAAP is included in Note 48 to the Consolidated Financial Statements.

	2001	2000	1999	1998	1997
Profit and loss account data for the year ended 31 December (£m) [1]					
Net interest income	**4,944**	4,587	4,783	4,398	4,144
Other income	**3,882**	3,937	3,195	2,777	3,247
Trading surplus	**4,502**	4,572	4,561	3,671	3,272
Provisions for bad and doubtful debts	**(747)**	(541)	(615)	(555)	(511)
Profit on ordinary activities before tax	**3,550**	3,860	3,656	3,053	2,790
Profit on ordinary activities after tax	**2,579**	2,755	2,545	2,159	2,044
Profit for the year attributable to shareholders	**2,500**	2,706	2,539	2,146	2,030
Dividends	**1,872**	1,683	1,451	1,204	925
Balance sheet data at 31 December (£m)					
Called-up share capital	**1,411**	1,396	1,389	1,379	1,369
Shareholders' funds (equity)	**10,760**	10,024	8,829	7,563	6,326
Customer accounts	**109,116**	101,989	93,714	90,445	85,688
Undated subordinated loan capital	**3,651**	3,391	3,294	1,518	1,515
Dated subordinated loan capital	**4,006**	4,119	3,199	2,503	2,694
Loans and advances to customers	**122,935**	114,432	102,233	95,243	87,633
Assets[2]	**190,150**	168,028	150,508	144,942	138,757
Total assets	**236,539**	219,113	177,050	168,634	158,803
Share information					
Basic earnings per ordinary share	**45.2p**	49.3p	46.6p	39.7p	38.0p
Diluted earnings per ordinary share	**44.8p**	48.8p	45.8p	39.0p	37.2p
Net asset value per ordinary share	**191p**	180p	159p	137p	116p
Dividends per ordinary share[3]	**33.7p**	30.6p	26.6p	22.2p	17.2p
Equivalent cents per share[3][4]	**49.3c**	44.2c	42.3c	36.7c	28.4c
Market price (year-end)	**746p**	708p	774p	855p	789p
Number of shareholders (thousands)	**981**	1,026	1,024	1,028	1,047
Number of ordinary shares in issue (millions)	**5,564**	5,507	5,475	5,435	5,396
Financial ratios[5]	**%**	%	%	%	%
Dividend payout ratio	**74.9**	62.2	57.1	56.1	45.6
Post-tax return on average shareholders' equity	**23.5**	28.1	30.0	29.7	34.5
Post-tax return on average assets	**1.46**	1.74	1.72	1.55	1.51
Post-tax return on average risk-weighted assets	**2.53**	3.10	3.04	2.70	2.52
Average shareholders' equity to average assets	**6.0**	6.1	5.7	5.2	4.3
Efficiency ratio[6]	**49.0**	46.4	42.8	48.8	55.7
Capital ratios					
Total capital	**9.2**	9.4	15.2	11.4	10.9
Tier 1 capital	**8.4**	8.5	10.2	8.8	8.0

(1) Figures for 2000 and earlier years have been restated to reflect the implementation of FRS 12, "Provisions, Contingent Liabilities and Contingent Assets", FRS 15, "Tangible Fixed Assets", FRS 18, "Accounting Policies", and other minor adjustments.

(2) Assets exclude long-term assurance assets attributable to policyholders.

(3) Annual dividends are comprised of both interim and final dividend payments. Final dividends (which are always paid in the following year) are included in the year to which they relate rather than in the year in which they are paid.

(4) Translated into US dollars at the Noon Buying Rate on the date each payment is made.

(5) Averages are calculated on a monthly basis from the consolidated financ ial data of Lloyds TSB Group.

(6) The efficiency ratio is calculated as total operating expenses as a percentage of total income.

SELECTED US GAAP FINANCIAL DATA	**2001**	2000	1999
Income statement data for the year ended 31 December (£m)			
Total revenues, net of interest expense	**9,180**	10,298	9,715
Policyholder benefits and claims expense	**(2,228)**	(1,735)	(936)
Provision for bad and doubtful debts	**(747)**	(541)	(615)
Income before tax	**2,057**	2,670	3,574
Net income	**1,524**	1,929	2,148
Dividends	**1,738**	1,522	1,285
Balance sheet data at 31 December (£m)			
Shareholders' equity	**13,421**	13,708	13,162
Deposits	**133,419**	117,473	110,545
Loans, net of provisions	**122,485**	110,788	99,120
Total assets	**243,346**	225,872	180,889
Share information (pence per ordinary share)			
Basic earnings	**27.5**	35.2	39.4
Diluted earnings	**27.2**	34.8	38.7
Net asset value	**238**	246	237
Dividends	**31.5**	27.8	23.6
Financial ratios(1)	**%**	%	%
Dividend payout ratio	**114.0**	78.9	59.8
Post-tax return on average shareholders' equity	**11.2**	14.4	16.9
Post-tax return on average assets	**0.67**	0.95	1.21
Average shareholders' equity to average assets	**5.8**	6.6	7.2

(1) Lloyds TSB Group does not have sufficient information to calculate US GAAP average balances on a monthly basis. Where applicable, these financial ratios have been based upon simple averages of the opening and closing balances.

EXCHANGE RATES

In this annual report, unless otherwise indicated, all amounts are expressed in pounds sterling. For the months shown the US dollar high and low Noon Buying Rates per pound sterling were:

	2002				2001	
	April	March	February	January	December	November
	(US dollars per pound sterling)					
High	**1.46**	**1.43**	**1.43**	**1.45**	**1.46**	**1.47**
Low	**1.43**	**1.41**	**1.41**	**1.41**	**1.42**	**1.41**

For the years shown the average of the US dollar Noon Buying Rates per pound sterling on the last day of each month were:

	2001	2000	1999	1998	1997
	(US dollars per pound sterling)				
Average	**1.44**	1.52	1.61	1.66	1.64

On 1 May 2002, the latest practicable date, the US dollar Noon Buying Rate was 1.4621 = £1.00. Lloyds TSB Group makes no representation that amounts in pounds sterling have been, could have been or could be converted into US dollars at that rate or at any of the above rates.

BUSINESS

Management and resources

Lloyds TSB Group recognises that it will create value for its shareholders if it creates value for its customers. Its constant aim is to meet the rapidly changing needs and expectations of its customers. Lloyds TSB Group believes that success depends upon service, consistency and commitment. Nothing is more important to Lloyds TSB Group's business than maintaining the trust and confidence of its customers and Lloyds TSB Group aims, wherever possible, to maintain long-term relationships with its customers. Lloyds TSB Group has an established code of business conduct which is published and available, on request, to the public. The policy defines the standards and values which are used to operate the business and covers Lloyds TSB Group's relationship with customers, suppliers, employees, the community, shareholders and competitors. The code is incorporated within procedures for each area of the business and has been communicated to all employees.

Lloyds TSB Group operates in a marketplace which is continually changing. No organisation can successfully manage change without the support and commitment of its staff. The pace and scope of change will not diminish as competition in the financial services market continues to increase. Lloyds TSB Group recognises that it is the staff of the organisation who have delivered, and will continue to deliver, its success and considers that one of its greatest competitive advantages is the ability of its people to adapt to rapid and far reaching change.

Lloyds TSB Group recognises that long-term success depends on the quality of its management. It is therefore committed to developing the potential of all managers, in particular ensuring that it has the succession management capability to meet future needs for top management. It also believes that the knowledge and skills of its employees is a key element of its organisational success and therefore invests in training, ensuring that it is accessible by everyone in the organisation.

Strategy of Lloyds TSB Group

The governing objective of Lloyds TSB Group is to maximise shareholder value over time. Lloyds TSB Group believe that this objective can only be achieved by having clear strategic aims, plans capable of translating strategy into shareholder value, and the determination and ability to implement those plans. Lloyds TSB Group plans to accomplish this by a combination of organic growth and acquisitions.

Lloyds TSB Group's three strategic aims are to be a leader in our chosen markets, to be the first choice for its customers and to reduce day-to-day operating costs to allow greater scope for investment in better products, enhanced service and multi-channel distribution.

- ***To be a leader in its chosen markets***

  Lloyds TSB Group has pursued its aim to be a leader in its chosen markets by continuing to seek opportunities to consolidate its position in businesses where it is already strong by a combination of organic growth and acquisitions and by divesting businesses in markets where it is not a leader and cannot aspire reasonably to leadership. The acquisition of Scottish Widows in March 2000 has greatly enhanced Lloyds TSB Group's market position in the life assurance market. Based on figures provided by the Association of British Insurers, Lloyds TSB Group's share of the UK life and pensions market in 1999 was 1.5 per cent, excluding Abbey Life. In 2000, following the acquisition of Scottish Widows, this rose to 5.2 per cent. The acquisition of Chartered Trust, a consumer finance and contract hire business, in September 2000 has consolidated Lloyds TSB Group's position as a market leader in the independent provision of motor finance. In 1998, the acquisition of Countrywide Banking Corporation further strengthened Lloyds TSB Group's position in New Zealand. Lloyds TSB Group has also divested businesses such as Mortgage Express, International Factors, Black Horse Agencies, Schröder Münchmeyer Hengst & Co and, in 2001, Lloyds TSB Asset Management S.A. which were either duplicated or were businesses in markets in which Lloyds TSB Group did not wish to become a leader.

- ***To be first choice for its customers***

  Lloyds TSB Group aims to be first choice for its customers by better understanding and meeting their needs. Central to this objective is Lloyds TSB Group's Customer Relationship Management programme, which brings together all the customer information that Lloyds TSB Group holds so that it can build on its relationship with individual customers by providing them with products, services and access suited to their individual requirements.

  Lloyds TSB Group has continued to broaden its product range, which is supported by multiple distribution channels. Lloyds TSB Group continues to extend its telephone banking and internet banking operations offering its customers an extensive choice of when, where and how they want to transact their financial business, be it at a branch, over the telephone or through the internet.

- ***To reduce day-to-day operating costs***

  Reducing day-to-day operating costs allows Lloyds TSB Group greater scope for investment in products, enhanced service and multi-channel distribution. 1999 saw the attainment of the £400 million per annum cost saving target (compared to the 1995 base) which was promised at the time of the merger of Lloyds Bank Plc and TSB Group plc and the integration of Lloyds Abbey Life plc. Building on this achievement, Lloyds TSB Group has identified further opportunities to enable it to continue its focus on tightly controlling costs. The principal vehicle for this is a major efficiency programme which Lloyds TSB Group commenced in 2000, primarily focussed on non-customer facing activities, and subsequently expanded in February 2002. Lloyds TSB Group expects this programme to result in the centralisation of large scale processing activities and the further consolidation and centralisation of support functions. The enhanced efficiency programme is expected to result in a reduction of 5,000 staff in 2002, primarily from central and support areas, whilst staff numbers in customer facing sales and service areas are expected to increase by approximately 2,000, creating a net reduction in headcount of 3,000. The programme is expected to be largely completed by 2004.

Lloyds TSB Group continues to develop new strategies which will leverage the strength of its brands and its multi-channel distribution capability, its enhanced understanding of what its customers want, and its cost advantage to deliver greater value to customers.

Lloyds TSB Group remains alert for opportunities to participate in the further consolidation of the financial services industry, both in the UK and overseas. Management believes that domestic consolidation in many overseas markets, particularly in Europe, is entering its final phase and that, therefore, significant cross border mergers and acquisitions may happen in the coming years. Lloyds TSB Group believes it will be well placed to participate in such cross border consolidation with potential to create value by exploiting its retailing and cost management skills.

Businesses and activities of Lloyds TSB Group

The main businesses and activities of Lloyds TSB Group's three segments are described below.

UK Retail Banking and Mortgages

UK Retail Banking and Mortgages provided banking and financial services to some 15 million customers during 2001. With approximately 2,300 branches of Lloyds TSB Bank, Lloyds TSB Scotland and Cheltenham & Gloucester at the end of 2001, Lloyds TSB Group provides comprehensive geographic branch coverage in England, Scotland and Wales. The contribution, calculated as explained under "Operating and Financial Review and Prospects—Line of business information—Summary", from UK Retail Banking and Mortgages in 2001 was £1,588 million. Lloyds TSB Group has continued to develop alternative distribution channels, through the telephone (PhoneBank and PhoneBank Express, an interactive voice recognition service) and the internet *(lloydstsb.com)*. This enables Lloyds TSB Group to offer a broad range of access points for customers in order to improve service and to enhance revenue growth. During 2001, Lloyds TSB Group completed the implementation of an online real-time personal banking system enabling customers to get up-to-the minute information of their account balances and allowing immediate clearance of personal cheques and immediate transfer of funds between Lloyds TSB accounts.

UK Retail Banking

The contribution, calculated as explained under "Operating and Financial Review and Prospects - Line of business information - Summary", from UK Retail Banking in 2001 was £633 million.

Current accounts, savings and investment accounts, and consumer lending. The retail branches of Lloyds TSB Bank offer a broad range of branded products, and Cheltenham & Gloucester provides retail investments through its branch network and a postal investment centre. Lloyds TSB Group's supermarket banking operation, branded 'easibank', continues to expand and there were 22 branches in ASDA supermarkets or large shopping centres at the end of 2001. Lloyds TSB Group has a relationship with the Post Office to allow Lloyds TSB Group personal customers to undertake banking transactions in post offices in England and Wales.

Business banking. Small businesses were served by dedicated business managers based in 448 locations throughout the UK at the end of 2001. Customers have access to a wide range of tailored business services including money transmission, lending and deposits and insurance and investments. In addition, customers have access to a range of non-financial solutions to their business problems such as Debtor Management service, providing legal support to help customers recover debts and Prospect Finder providing customers with a tailored list of potential customers for their business. Lloyds TSB Group is a leading bank for new business start-ups with around one in five opening accounts with Lloyds TSB Group.

Card services provides a range of card-based products and services, including credit and debit cards and card transaction processing services for retailers. Lloyds TSB Group is a member of both the VISA and MasterCard payment systems and is the third largest credit card issuer in the UK with a 10 per cent share of cards in issue at 31 December 2001.

Cash machines. Lloyds TSB Group has one of the largest cash machine networks of any leading banking group in the UK and, at 31 December 2001, personal customers of Lloyds TSB Bank were able to withdraw cash, check balances and obtain mini statements through 4,350 Cashpoints at branches and external locations around the country. In addition, they had access to a further 32,400 cash machines via LINK in the UK and to cash machines worldwide through the VISA and MasterCard networks.

Telephone banking. Telephone Banking continues to grow and Lloyds TSB Group provides one of the largest telephony services in Europe, in terms of customer numbers. At the end of 2001, 2.5 million customers had registered to use the services of PhoneBank and the automated voice response service PhoneBank Express. PhoneBank and PhoneBank Express handled some 25 million calls during 2001.

Internet banking. Internet Banking provides online banking facilities for personal and business customers and enables them to conduct their financial affairs without the need to use the branch network. Lloyds TSB Group had 1.8 million online customers of *lloydstsb.com* at the end of 2001. *lloydstsb.com* was rated one of the most visited financial websites in Europe by Jupiter MMXI.

UK Wealth Management. Private Banking provides a range of tailor-made wealth management services and products to individuals from 40 offices throughout the UK. In addition to asset management, these include tax and estate planning, executor and trustee services, deposit taking and lending, insurance and personal equity plan and individual savings account (ISA) products. At 31 December 2001, total funds managed and administered totalled some £11,000 million. Lloyds TSB Group's new wealth management brand, Create, was launched in October 2001. This offer aims to meet the specialised banking needs of Lloyds TSB Group's affluent customers who will be the target market for the wealth management services. Lloyds TSB Stockbrokers undertakes retail stockbroking through its Sharedeal Direct telephone service.

Mortgages

Cheltenham & Gloucester is Lloyds TSB Group's specialist residential mortgage provider, providing a range of mortgage products to personal customers through its own branches and those of Lloyds TSB Bank in England and Wales, as well as through the telephone, internet and postal service, C&G TeleDirect. Lloyds TSB Group also provides mortgages through Lloyds TSB Scotland and Scottish Widows Bank. During 2001, the contribution from Mortgages was £955 million. Lloyds TSB Group is the third largest residential mortgage lender in the UK on the basis of outstanding balances, with mortgages outstanding at 31 December 2001 of £56,578 million, representing an estimated market share of 9.5 per cent. Lloyds TSB Group believes that it is one of the most efficient mortgage providers in the UK; since Cheltenham & Gloucester's acquisition by Lloyds TSB Group in 1995, it has consistently had one of the lowest efficiency ratios (total operating expenses expressed as a percentage of total income) compared to its competitors.

Insurance and Investments

The contribution, calculated as explained under "Operating and Financial Review and Prospects - Line of business information - Summary", from Insurance and Investments in 2001 was £1,601 million. This represented an increase of 12 per cent against 2000.

Life assurance, pensions and investment. Scottish Widows is Lloyds TSB Group's specialist provider of life assurance, pensions and investment products, which are distributed through Lloyds TSB Bank's branch network, through independent financial advisers and directly via the telephone and the internet. Before its acquisition in 2000, Scottish Widows was a leading provider of life assurance, pensions and long-term savings products mainly distributed through independent financial advisers. Following the acquisition, the Scottish Widows brand became the sole brand for Lloyds TSB Group's life, pensions, unit trust and other long-term savings products, and Lloyds TSB Group extended the brand's product range to Lloyds TSB Group's retail banking branch network.

In common with other life assurance companies in the UK, the life and pensions business of each of the life assurance companies in the Lloyds TSB Group is written in a long-term business fund. The long-term business fund is divided into a With-Profits and a Non-Participating sub-fund.

With-profits life and pensions products are written from the With-Profits Fund. The benefits accruing from these policies are designed to provide a smoothed return to policyholders who hold their policies to maturity through a mix of annual and final (or terminal) bonuses added to guaranteed basic benefits. The guarantees generally only apply on death or maturity. The actual bonuses declared will reflect the experience of the With-Profits Fund.

Other life and pensions products are generally written from the Non-Participating sub-fund. Examples include unit-linked policies, annuities, term assurances and health insurance (under which a pre-determined amount of benefit is payable in the event of an insured event such as death). The benefits provided by such linked policies are wholly or partly determined by reference to a specific portfolio of assets known as unit-linked funds.

General Insurance. Lloyds TSB General Insurance provides general insurance through the retail branches of Lloyds TSB Bank and Cheltenham & Gloucester, and through a direct telephone operation and the internet. Based on a survey conducted for Lloyds TSB Group, Lloyds TSB General Insurance had a new business market share of 14 per cent of the new household insurance market, selling more policies in the twelve months to December 2001 than any of the other leading distributors. The new household insurance market is defined as those customers switching suppliers, taking out first ever policies and customers re-entering the household insurance market.

Scottish Widows Investment Partnership manages funds for Lloyds TSB Group's retail life, pensions and investment products. Clients also include corporate pension schemes, local authorities and other institutions in the UK and overseas. At 31 December 2001 funds under management amounted to some £78,000 million, compared to some £87,000 million a year earlier. The decline has been primarily caused by the lower stockmarket levels experienced in 2001; Lloyds TSB Group remains a significant player in the asset management business in the UK.

Wholesale Markets and International Banking

Wholesale Markets

The contribution, calculated as explained under "Operating and Financial Review and Prospects - Line of business information - Summary", from Wholesale Markets in 2001 was £937 million.

Lloyds TSB Group's relationships with major UK and multinational companies, banks and institutions, and medium-sized UK businesses, together with its activities in financial markets, are managed through dedicated offices in the UK and a number of locations overseas, including New York.

Treasury is a leading participant in the sterling money market. It is also active in currency money markets, foreign exchange markets and also in certain derivatives markets, primarily to meet the needs of customers. It also plays a central role in funding, cash and liquidity management of Lloyds TSB Group.

Corporate and Commercial provides a wide range of banking and related services, including electronic banking, large value lease finance, share registration, correspondent banking and capital markets services to major UK and multinational companies and financial institutions, and, through a network of dedicated offices, to medium-sized businesses in the UK. The Agricultural Mortgage Corporation provides long-term finance for the agricultural sector and through Lloyds TSB Development Capital, venture capital finance is provided to developing companies.

Asset Finance enables companies to acquire the assets needed to run their businesses through the provision of leasing, hire purchase and contract hire packages. Hire purchase, or instalment credit, is a form of consumer financing where a customer takes possession of goods on payment of an initial deposit but the legal title to the goods does not pass to them until the agreed number of instalments have been paid and the option to purchase has been exercised. Through its invoice discounting and factoring subsidiary Lloyds TSB Commercial Finance, Lloyds TSB Group provides working capital finance for companies by releasing to the company up to 90 per cent of the value of their unpaid invoices, with the balance payable, after deduction of a service fee, once the invoices have been settled. Invoice discounting differs to factoring in that the company retains control of the debt collection and the credit risk. At 31 December 2001, based on information maintained by the Factors and Discounters Association, Lloyds TSB Commercial Finance Limited (which is a subsidiary of Lloyds TSB Bank) was the second largest invoice discounting company in the UK with a market share of 19 per cent and the largest factoring company in the UK, with a market share of 22 per cent.

International Banking

The contribution, calculated as explained under "Operating and Financial Review and Prospects - Line of business information - Summary", from International Banking in 2001 was £444 million.

New Zealand. The National Bank of New Zealand Limited ("NBNZ") was New Zealand's second largest bank measured by assets during 2001 and provides a wide range of banking services through some 159 retail branch outlets. NBNZ serves retail customers' needs for current and savings accounts, credit cards, consumer lending and home loans. NBNZ also has a substantial non-personal business providing working capital, term lending, trade finance and treasury services to the business and agricultural sector.

Europe. International Wealth Management provides services to wealthy individuals outside their country of residence. The business is conducted through branches of Lloyds TSB Bank located in Switzerland, Dubai, Luxembourg, Monaco and Gibraltar. There are also private and corporate banking operations in Spain and France.

Offshore banking comprises Lloyds TSB Group's offices in the Channel Islands and Isle of Man, as well as its operations in Hong Kong, Singapore and Malaysia and representation in Belgium and the US. It provides a wide range of retail banking, private banking and financial services to overseas residents and islanders, together with deposit services offshore for UK residents.

The Americas. Lloyds TSB Group has operated in the Americas for over 130 years and has offices in Brazil, Argentina, Colombia, Ecuador, Guatemala, Honduras, Panama, Paraguay and Uruguay. In addition Lloyds TSB Group has private banking and investment operations in the US and the Bahamas. In Brazil, where Lloyds TSB Bank has 11 corporate banking offices, Lloyds TSB Group's most substantial business is Losango, a consumer lending operation providing three retail products: borrowing at the point of sale in stores, unsecured personal lending and borrowing to fund new and second-hand car purchases. The Losango business is mainly conducted through Banco Lloyds TSB SA a locally incorporated subsidiary of Lloyds TSB

Bank. Through its network of corporate banking offices, Lloyds TSB Bank also provides specialist banking and treasury products to corporate clients in Brazil. In Argentina where Lloyds TSB Bank has 40 branches and Colombia, where Lloyds TSB Bank's subsidiary Lloyds TSB Bank SA has 20 branches, Lloyds TSB Group provides corporate banking services, including trade finance, working capital loans, import finance, term deposits and money transmission. It also provides retail banking services through a network of branches, including current and savings accounts, credit cards, personal loans and mortgages.

Recent developments

In February 2000 Lloyds TSB Group announced a significant efficiency programme designed to support the Group's strategic aim of driving down day-to-day operating costs to improve overall efficiency and finance ongoing high levels of investment in growth businesses. The programme is spread over four years and annualised cost benefits are on track, with the targeted £75 million per annum achieved in 2001.

Lloyds TSB Group announced in February 2002 that a further review had been undertaken to identify all opportunities to extend the efficiency programme to deliver further productivity gains. Annualised benefits from the combined programme are now expected to rise by £190 million to £600 million in 2004. The combined efficiency programme will require total exceptional restructuring costs of approximately £300 million in 2002 and £100 million in 2003, largely to fund severance and infrastructure costs. In 2004 and beyond no further exceptional restructuring costs are anticipated as a result of this efficiency programme. The further expenditure of approximately £170 million, which will now be incurred in 2002, will be covered by additional cost benefits estimated at £155 million by the end of 2002, resulting in a payback of just over one year for these further costs.

	2000	2001	2002	2003	2004
Exceptional restructuring costs	**£m**	**£m**	**£m**	**£m**	**£m**
Initial efficiency programme	188	217	130	60	-
Further initiatives	-	-	170	40	-
Total	188	217	300	100	-
Expected annualised benefits					
Initial efficiency programme (cumulative)	-	75	145	320	410
Further initiatives (cumulative)	-	-	155	180	190
Total	-	75	300	500	600

The enhanced efficiency programme will result in a reduction of approximately 5,000 staff in 2002, primarily from central and support areas, whilst staff numbers in customer facing sales and service areas will increase by approximately 2,000, creating a net reduction in headcount of approximately 3,000. It is expected that the majority of these reductions will be achieved through voluntary redundancy and normal staff turnover.

In December 2000, Lloyds TSB Group contacted Abbey National plc ("Abbey National") concerning a possible combination between the two companies: after discussions between the two parties, Abbey National rejected this proposal. On 31 January 2001, Lloyds TSB Group issued a statement setting out the terms of an offer for Abbey National, which was conditional upon, amongst other things, the proposed transaction being recommended to its shareholders by the board of Abbey National and not being referred to the Competition Commission. However, on 23 February 2001, the Secretary of State for Trade and Industry ("the Secretary of State") requested that the Competition Commission review the transaction. There was concern that the attempted acquisition would lead to the elimination from the market of one of the most significant branch-based competitors to the UK's four largest banks and that this might result in a substantial lessening of competition, particularly in the market for current accounts. Furthermore, the merger would remove a potential competitor in the provision of banking services to small and medium-sized companies. In July 2001, the Secretary of State acting upon the advice of the Competition Commission, announced that the transaction would not be permitted to proceed because of the adverse effects that it would have upon competition in these markets.

Properties

As at 31 December 2001, Lloyds TSB Group occupied 3,693 properties in the UK. Of these, 795 were held as freeholds, 95 as long-term leaseholds and 2,803 as short-term leaseholds. The majority of these properties (2,328) are branches and are widely distributed throughout England, Scotland and Wales. The most significant of these properties are Lloyds TSB Group's head office in London, together with administrative buildings in Bristol, Gloucester and Edinburgh.

In addition, Lloyds TSB Group owns, leases or uses under licence properties for business operations elsewhere in the world, principally in Argentina, Brazil, New Zealand, Spain and Switzerland.

On 14 March 2002, Lloyds TSB Group announced its intention to relocate its head office within the City of London, selling its existing freehold head office and occupying a long-leasehold property.

Legal actions

Lloyds TSB Group and its properties are periodically subject to threatened or filed legal actions in the ordinary course of business. Lloyds TSB Group does not expect the final outcome of any legal proceedings currently known to it to have a material adverse effect, individually or in the aggregate, on its consolidated results of operation or financial condition.

Provisions for redress to past purchasers of pension policies

During the late 1980s, the UK government became concerned about the burden on the state benefit system that will result from the increasing size of the retired population. As a measure to reduce this impact the government introduced, as part of the UK Income and Corporation Taxes Act 1988, legislation aimed at encouraging the working population to make their own private pension arrangements. For several years following the introduction of this legislation, insurance companies and intermediaries advised a large number of private customers to set up their own private pension plans, often by transferring out of, or choosing not to join, occupational pension schemes offered by their employers. As a further way of relieving the possible pensions burden on the state, individuals had been given the option, by the government, to forego their entitlement to the earnings related element of state pension benefits - the State Earnings Related Pension Scheme ("SERPS") - in return for having part of their National Insurance contributions diverted into personal pension plans.

During the early 1990s, the UK government and regulatory authorities became increasingly concerned that many of these customers had been given poor advice and that they would, in fact, have been in a better position if they had remained in, or joined, employer sponsored pension schemes. The regulator of the UK pension industry, then The Securities and Investments Board, carried out an industry-wide investigation into the conduct of business involving the transfer of pensions. The conclusion of this investigation was that a large number of customers had been poorly advised by insurance companies and intermediaries across the industry, such advice resulting in pension misselling: the sale of personal pensions where insufficient consideration was given to the full value of an employer provided occupational pension scheme.

As a result of its investigation, the regulator established an action plan for the UK pensions industry to follow in reviewing all cases of possible misselling as described in the preceding paragraph and determining necessary compensation. For the purposes of this review, all relevant cases were segregated into two classes:

- Phase 1 cases ("priority cases") – these were mainly cases where the customer had retired since taking out the private pension plan, was approaching retirement or had since died.

- Phase 2 cases ("non-priority cases") – these cases primarily relate to younger customers who were not yet approaching their expected retirement dates.

In common with a number of other banks and insurance companies, in January 1997 Lloyds TSB Bank was fined £325,000 by the Investment Management Regulatory Organisation Limited for regulatory breaches and failings in connection with the sale of personal pensions between April 1988 and July 1993. Lloyds TSB Group does not expect any further fines or regulatory investigations in connection with the regulator's action plan for reviewing cases of possible misselling.

The most significant costs are the compensation of past purchasers of pensions. As the review of pension cases in Lloyds TSB Group has progressed, provisions have been established for the cost of compensation to past purchasers of pensions.

Movements in the provisions established by the Lloyds TSB bancassurance business and Abbey Life over the last three years have been as follows:

	2001	2000	1999
	£m	£m	£m
Provision at 1 January	**352**	397	472
Accrual of interest on the provision	**20**	26	22
Additional amounts provided	**70**	100	102
Compensation paid	**(238)**	(173)	(161)
Phase 1 guarantees[1]	**(1)**	3	(38)
Phase 2 guarantees[1]	**-**	(1)	-
Provision at 31 December[2]	**203**	352	397

(1) In some cases, rather than pay cash compensation directly into the customer's private pension plan, Lloyds TSB Group has guaranteed to 'top-up' the customer's pension income, on retirement, to the level that they would have received under the relevant occupational scheme. A separate provision for these amounts is carried in Lloyds TSB Group's balance sheet.

(2) This provision is included within the figure for the long-term assurance business attributable to the shareholder ("embedded value") in Lloyds TSB Group's balance sheet.

At the beginning of 1999 provisions totalling £472 million were held in respect of Phase 1 and Phase 2 cases.

During the second half of 1999, the Financial Services Authority published revised assumptions to be incorporated into the calculations of the continuing cost of redress reflecting the fact that the average life expectancy of pensioners had increased and interest and inflation rates were lower. Applying these guidelines, the cost of redress was forecast to increase by a further £102 million and an additional provision of this amount was raised in the accounts for the year ended 31 December 1999.

Towards the end of 1999, the Financial Services Authority published further revisions to the guidelines, particularly to the way that compensation should be calculated for customers who had opted out of SERPS. At this stage, Lloyds TSB Group had insufficient experience of such cases to be able to establish the need for any additional provisioning. During 2000, the Financial Services Authority required that these revised SERPS guidelines be applied retrospectively to cases settled since the beginning of 1999. By this time Lloyds TSB Group had also gained further experience and improved knowledge as to the number and size of compensation claims to be paid, both standard Phase 2 cases and those affected by the SERPS adjustment. Taking into account all of these factors, the cost of redress was forecast to increase by a further £100 million and a provision of this amount was raised in the year ended 31 December 2000.

A further review of the adequacy of the provision has been carried out as at 31 December 2001. Lower stock market levels have had a significant impact on total redress costs as the cost of restitution into company pension schemes rises as personal pension fund values reduce. As a result of this and the fact that there is now greater clarity as to the number and size of compensation claims to be paid, an additional provision of £70 million has been made.

Following normal actuarial practice, each year the provisions have been increased to recognise the interest accruing upon the assets held to match the liability. The increase in the provision amounted to £20 million in 2001, £26 million in 2000 and £22 million in 1999, although there was no net effect on Lloyds TSB Group's profit and loss account.

Lloyds TSB Group is required to complete the review of all Phase 1 and Phase 2 cases by the end of June 2002. For Free Standing Additional Voluntary Contribution ('FSAVC') pension contracts, all offers of compensation must be made by 31 December 2002. The calculation of the provision is based upon a series of assumptions relating to the number and size of cases requiring compensation, and on guidelines issued by the Financial Services Authority. Lloyds TSB Group was satisfied as to the adequacy of the provision as at 31 December 2001, and believes that the remaining provision will be sufficient to cover its outstanding liabilities. However changes to the guidelines issued by the Financial Services Authority, for example regarding FSAVCs, or new information becoming available may result in adjustments being required to the provision.

Before its acquisition in 2000, Scottish Widows mainly distributed its products through independent financial advisers and for this reason the liability of the business to pay redress to past purchasers of pension policies is less significant. At 31 December 2001 a provision of £11 million (2000: £39 million) was held within the With Profits Fund. Although Lloyds TSB Group was satisfied that no further provision was required to be made at that date, if in the future it should prove necessary to increase this provision for any reason, the cost will be met from assets held in the With Profits Fund and will therefore have no financial impact upon Lloyds TSB Group.

Guaranteed annuity options

A guaranteed annuity option policy is a pension policy that provides a cash benefit at retirement age, which can be converted into an annuity at a specified minimum rate. Under UK GAAP a provision is required when market rates fall below the specified minimum and policyholder funds are not expected to be sufficient to meet the excess cost of the annuity at retirement. In 1998, a provision was made within Abbey Life for liabilities under certain unit-linked products with guaranteed annuity options written from the mid 1960s to the mid 1980s. Unit-linked insurance policies are insurance policies where the policyholder's premiums are used to buy units in a fund run by the insurer. At 31 December 2001 this provision was £79 million; the Group is satisfied that this remains adequate.

Considerable attention has also been given to the implications of guaranteed annuity option contracts for the distribution of profits in the form of bonuses to with-profits policyholders. The House of Lords clarified the position in its judgement on the guaranteed annuities case, *Equitable Life vs Hyman* by ruling that a life company could not use its discretion to undermine or negate a contractual guaranteed annuity rate, and that the cost of funding such rates could not be met by guaranteed annuity option policyholders alone. This ruling raised the issue of how terminal bonuses declared by the directors of a life company can reflect the cost of a guaranteed annuity option.

After an extensive review of its existing practices carried out in the light of this judgement, it was announced that Scottish Widows was revising the way it calculates benefits for guaranteed annuity policies with effect from 1 February 2002. As a result of this change, the terminal bonuses for guaranteed annuity option policies will be increased.

Under the terms of the transfer of Scottish Widows' business, a separate memorandum account was created within the With Profits Fund called the Additional Account. This Account had a value at 31 December 2001 of approximately £1,700 million and is available to meet any additional costs of providing guaranteed benefits on transferred policies, including guaranteed annuity option policies. The assets allocated to the Additional Account include certain hedge assets, which are intended to protect the With Profits Fund against the consequences of a future fall in interest rates.

The eventual cost of providing the enhanced benefits is dependent upon a number of factors, including in particular:

- The proportion of policyholders with a guaranteed annuity option policy who choose to exercise their options;
- The effect of future interest rate and mortality trends on the cost of annuities; and
- The future investment performance of the With Profits Fund.

Having considered a range of possible outcomes, Lloyds TSB Group believes that the most likely outcome is that the balance in the Additional Account available for this purpose will be sufficient to meet the cost of the enhanced benefits payable to the guaranteed annuity option policyholders, as well as other contingencies. This cost, currently estimated to be approximately £1,400 million, will be paid out over many years as policies mature. In the event that the amount in the Additional Account proves, over time, to be insufficient, the shortfall will be met by Lloyds TSB Group. At this time, no provision is considered necessary for such risk.

Competitive environment

General

Lloyds TSB Group operates in a financial services world that is experiencing consolidation at both national and international levels. The last few years have seen the establishment of global players in the industry together with the beginnings of pan-European consolidation and considerable consolidation within the US. Product manufacture and support in markets such as credit cards, mortgages, savings and funds management will increasingly be driven on a global scale.

Globalisation and developments in technology are significantly expanding Lloyds TSB Group's range of competitors, by removing many barriers to entry. These new entrants are expected to put Lloyds TSB Group's margins under increasing pressure with products becoming increasingly simplified and standardised. Nonetheless, Lloyds TSB Group expects competition within the industry to continue to be partially based on service and relationships as well as price, particularly for the core banking services. Furthermore, complex products such as pensions are expected to be more resistant to standardisation and selling across the internet. In addition, Lloyds TSB Group has significant strengths with which to counter the pressure on margins in its portfolio of powerful brands, its existing customer base, its distribution capability and its purchasing power.

The UK

Lloyds TSB Group's key markets are in the UK, predominantly in the retail sector, where the market for basic financial and banking services is relatively mature. The market for life and pensions products is, however, experiencing strong rates of growth with further growth potential. The general insurance market has also exhibited growth in a number of key sectors.

The removal of regulatory and financial barriers in recent years has blurred the traditional financial services industry lines and allowed new competitors into the market. Lloyds TSB Group's competitors include all the major stock and mutual retail financial services and fund management companies operating in the UK. De-mutualised building societies which have become banks and life assurers which have entered the banking market have become direct competitors in the provision of banking products, whilst several UK banks have announced the launch of stand-alone internet banks to complement their existing services. In the mortgage market competitors include the traditional banks and building societies and new entrants to the market, with the market becoming increasingly competitive as both new entrants and incumbents endeavour to gain market share. Lloyds TSB Group's competitors in the credit card market again include both the traditional banks and new entrants, including overseas companies. In the last few years a large share of new business has been acquired by US and new UK competitors. In the provision of life, pensions and investments products Lloyds TSB Group has seen increased competition from new market entrants, such as traditional retailers, primarily in specialist areas. The fragmented nature of the life, pensions and investments market in the UK has resulted in some consolidation within the sector; government regulations on product charges and competitive pressures are likely to drive further consolidation as providers seek to achieve the benefits of economies of scale. In the general insurance sector, the market has seen significant consolidation amongst underwriters but continued fragmentation in distribution and an increasing number of new market entrants including both overseas insurers and direct operators.

In 1998, the UK government commissioned an investigation into competition in the banking industry whose findings were published in March 2000. The investigation specifically examined the levels of innovation, competition and efficiency in various sub-markets within the industry. The investigation found that the small and medium-sized business market was not sufficiently competitive, with barriers to entry existing for new players. The provision of banking services to this sector was referred to the UK Competition Commission under the Fair Trading Act 1973 for a full competition inquiry. Under the Fair Trading Act, a "monopoly situation" is regarded as arising (among other cases) where one firm accounts for the supply of at least one quarter of the reference services, known as a scale monopoly, or where several firms together account for at least one quarter of the reference services and, whether voluntarily or not, and whether by agreement or not, they so conduct their affairs as in any way to prevent, restrict or distort competition in connection with the supply of the reference services, known as a complex monopoly. Since the announcement of the inquiry, there have been several statements by large-scale institutions of their intention to enter this market.

In March 2001, the UK Competition Commission published a statement of its provisional conclusions on some of the questions referred to it. In pursuing its investigation, the UK Competition Commission provisionally decided to regard the small and medium-sized business market to be comprised of sole traders, firms and companies generating an annual turnover of up to £25 million. The statement provisionally identified a scale monopoly in favour of The Royal Bank of Scotland Group plc. The statement provisionally identified a complex monopoly situation in favour of a number of banks; principally Lloyds TSB Group, Abbey National plc, Bank of Scotland plc, Barclays plc, HSBC Bank plc and The Royal Bank of Scotland Group plc. There are a number of operating units within Lloyds TSB Group engaged in the small and medium-sized business market, the largest of which is Business Banking. Business Banking provides services to those businesses with an annual turnover of less than £1 million. Research carried out by City Research Associates in September 2000 showed that Business Banking had a 20 per cent share of this market.

On 14 March 2002, the Competition Commission's report into the competitiveness of banking for small and medium-sized enterprises (SME's) was published by the Government. The Competition Commission concluded that a number of specific practices had the effect of restricting or distorting price competition between the main banks. Particular examples that were identified included the similarity of pricing structures and the fact that in general no interest is paid on current account balances; a pattern of differentiation in the charges made by the main banks, with free banking generally confined to certain categories of SME such as new start-ups or customers switching banks; and the use of negotiation for those considering switching. The Competition Commission also concluded that there were significant barriers to entry, in part caused by the lack of price competition, but also because of the unwillingness of SME's to change banks because of the perceived complexity. In the view of the Competition Commission the restriction and distortion of price competition has led to excessive prices and profits. The Government has accepted in full the recommendations made by the Competition Commission. To remedy this situation one of the most significant proposals is that banks should offer any SME customer operating a current account in England and Wales, either:

- a current account that pays interest of at least the Bank of England Base Rate, minus 2.5 per cent; or
- a current account free of money transmission charges; or
- a choice between the two.

The principal behavioural remedies intended to reduce barriers to entry and expansion are measures to ensure fast error-free switching of accounts between banks. In addition, measures have been proposed limiting the bundling of services and improving market information and transparency. The Competition Commission believes that these measures should not take more than six months to implement. The Competition Commission has also recommended that three years after the implementation of these remedies, the Director General of Fair Trading should review whether further measures are needed or, in light of market developments, whether some or all of the remedies can be discontinued.

The implications for Lloyds TSB Group and its SME customers have not yet been fully assessed. Lloyds TSB Group's position continues to be that it has always supported the principle of competition and believes that the market is extremely competitive. Lloyds TSB Group has already introduced, or is currently introducing, initiatives to address a number of these remedies, such as ease of switching and transparency of charging, either on its own initiative or via the Business Banking Code.

Other markets

Lloyds TSB Group also operates in other countries, principally in New Zealand and Latin America, where it is exposed to different competitive pressures.

Lloyds TSB Group operates in New Zealand through its wholly-owned subsidiary NBNZ. NBNZ's competitors principally comprise the major Australian banks each of which offer retail and wholesale products through branch networks and, more recently, over the telephone and internet. Consolidation in the Australian banking industry would, therefore, have a direct effect upon the competitive environment in New Zealand. The New Zealand economic environment, whilst enjoying a long period of growth and low inflation, has suffered from a volatile currency leading to increasing interest rates. This has depressed business confidence in the country, somewhat balanced by exporters and the agricultural sector enjoying greater prosperity.

In Latin America, Lloyds TSB Group's principal operations are in Brazil, Argentina and Colombia. The competitive environment in each country varies significantly where the number of players, both local and international, is substantially different. In Brazil there are over 200 banks, a third of which are either partially or wholly owned by foreign interests; in addition, there are a number of specialist consumer finance businesses. In Argentina and Colombia the competition is limited to a small number of domestic and foreign banks.

OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The results discussed below are not necessarily indicative of Lloyds TSB Group's results in future periods. The following information contains certain forward-looking statements. For a discussion of certain cautionary statements relating to forward-looking statements, see "Forward-Looking Statements".

The following discussion is based on and should be read in conjunction with the Consolidated Financial Statements and the related notes thereto included elsewhere in this annual report. For a discussion of the accounting policies used in the preparation of the Consolidated Financial Statements, see "Accounting policies" in Note 1 to the Consolidated Financial Statements. The Consolidated Financial Statements are prepared in accordance with UK GAAP, which varies in certain significant respects from US GAAP. A discussion of such differences and a reconciliation of certain UK GAAP amounts to US GAAP is included in Note 48 to the Consolidated Financial Statements.

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Overview

Lloyds TSB Group has operations in both the UK and overseas, however, its earnings are heavily dependent upon its domestic activities. In 2001, 84 per cent of Lloyds TSB Group's profit before tax was derived from its UK operations. The economic outlook in the UK, therefore, has significant implications for the way in which Lloyds TSB Group runs its business. By historical standards, the UK economic outlook is currently one of relatively low growth, low inflation and low interest rates. These conditions have been experienced over the last few years and continue to have significant implications for the development of Lloyds TSB Group particularly in the light of the slowdown in economic growth experienced in the second half of 2001 and into 2002.

Economic stability, low inflation and low interest rates are conditions that usually result in lower net interest margins. During 2001 the effect of these conditions and the increasingly competitive operating environment led to some erosion in the net interest margin of Lloyds TSB Group, although it is anticipated that over the next few years reductions in the overall margin in the UK will not be substantial. The competitive environment is also affecting Lloyds TSB Group's ability to sustain the level of growth achieved in the past in fee income from its core banking activities. For a number of years, Lloyds TSB Group has been anticipating these developments and this has been one of the factors that has led to Lloyds TSB Group's evolution from a banking group to a more diversified financial services group.

Critical accounting policies

Introduction

The reported results of Lloyds TSB Group are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its Consolidated Financial Statements. The accounting policies used in the preparation of the Consolidated Financial Statements are set out in Note 1 to the Consolidated Financial Statements. UK company law and standards require the directors, in preparing these accounts, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. Where UK GAAP allows a choice of policy, Financial Reporting Standard 18 'Accounting Policies' requires Lloyds TSB Group to adopt those policies judged to be most appropriate to its particular circumstances for the purpose of giving a true and fair view.

The judgements and uncertainties involved in Lloyds TSB Group's accounting policies that are most important to the portrayal of its financial condition are discussed below.

Recoverability of loans and investments

Lloyds TSB Group lends money to its customers by means of unsecured lending and secured lending, where collateral is held in respect of some or all of the outstanding balance. In addition, Lloyds TSB Group purchases debt securities and equity shares issued by other companies and governments to provide finance for their operations. In both cases there is a risk that Lloyds TSB Group will not receive full repayment of the amount advanced; provisions are made in the financial statements to reduce the carrying value of loans and advances and investments to the amount expected to be recovered. At 31 December 2001, Lloyds TSB Group held provisions for bad and doubtful debts of £1,468 million against total loans and advances of £139,697 million and provisions of £95 million against investment securities of £11,122 million. These provisions were determined through a combination of specific reviews, statistical modelling and management estimates. Certain aspects of this process require material judgmental evaluations, such as the amounts and timing of future cash flows and the assessment of the value of collateral held (such as guarantees), which may be susceptible to significant variation.

Lloyds TSB Group considers that the provisions for bad and doubtful debts, debt securities and equity shares at 31 December 2001 were adequate based on information available at that time. However, amendments to the provisions may be required in the future as a result of changes in collateral values, the timing and amounts of cash flows or other economic events.

Residual value guarantees

Equipment held by Lloyds TSB Group under operating leases is depreciated over the life of the leases, taking into account anticipated residual values. These values are reviewed regularly and any impairments identified are charged to the profit and loss account as they arise. A material decline in the second-hand market value for the assets being leased may cause these residual value amounts to differ significantly from those assumed at the balance sheet date.

Goodwill

The goodwill arising on the acquisition of Scottish Widows by Lloyds TSB Group is considered to have an indefinite useful life in view of the strength of the Scottish Widows brand and the position of the business as one of the leading providers of life, pensions, unit trust and fund management products and accordingly it is not being amortised. However, it is subject to an annual impairment review, evaluated by comparing the present value of future cash flows (the 'value in use') to the carrying value of the underlying net assets. In the event that the carrying value of the net assets exceeds the value-in-use an impairment is deemed to have occurred resulting in a charge being made to the profit and loss account. Adverse changes in the performance of Scottish Widows, affecting the amount and timing of future cash flows, or changes in the economic environment may lead to the goodwill becoming impaired in future periods.

General insurance provisions

Lloyds TSB Group maintains provisions for outstanding general insurance claims which represent the best estimate of the ultimate cost of settling all claims arising from events which have occurred up to the balance sheet date and these include provisions for the cost of claims notified but not yet settled and claims incurred but not reported. These provisions are calculated using statistical modelling techniques which require certain assumptions to be made in respect of the amount and timing of these claims. Additional provisions may be required as a result of changes in these assumptions or as a result of significant economic or weather related events.

Embedded value

Lloyds TSB Group accounts for the value of the shareholder’s interest in the long-term assurance business using the embedded value basis of accounting, which is UK GAAP for banking groups owning life assurance operations. The embedded value is comprised of the net tangible assets of the life assurance subsidiaries and the present value of the in-force business. The value of the in-force business is calculated by projecting future surpluses and other net cash flows attributable to the shareholder arising from business written by the balance sheet date and discounting the result at a rate which reflects the shareholder’s overall risk premium.

Future surpluses will depend on experience in a number of areas such as investment returns, lapse rates, mortality and investment expenses. Surpluses are projected by making assumptions about future experience, having regard to both actual experience and forecast long-term economic trends. Changes to these assumptions may cause the present value of future surpluses to differ from those assumed at the balance sheet date and could significantly affect the value attributed to the in-force business. The value of the in-force business could also be affected by changes in the amounts, basis of calculation and timing of other net cash flows, principally annual management charges and other fees levied upon the policyholders, which are reflected in the profit and loss account using smoothed fund values. In addition, to the extent that actual experience is different from that assumed, the effect will be recognised in the profit and loss account for the period. The effect of changes in the underlying assumptions and variations between actual and assumed experience on the results of the current and prior periods are disclosed in Note 29 in the Consolidated Financial Statements.

Fair value

Securities and derivatives held by Lloyds TSB Group for trading purposes are carried at fair value. Lloyds TSB Group reflects changes in these values in the profit and loss account. Fair values are based on quoted market prices for their components using appropriate pricing models. Where Lloyds TSB Group’s position is of such a size that the price obtainable would be materially different from the quoted price, Lloyds TSB Group adjusts the quoted price based on management’s estimate of the price that Lloyds TSB Group would realise from the holding in current market conditions.

Where instruments such as over-the-counter derivatives are valued using pricing models, the value of the instrument and changes in that value are determined by the model and its underlying assumptions. The use of different models or other assumptions could result in changes in reported financial results.

Results of operations - 2001 compared with 2000 and 2000 compared with 1999

Summary

	2001 **£m**	2000 £m	1999 £m
Net interest income	**4,944**	4,587	4,783
Other income	**3,882**	3,937	3,195
Total income	**8,826**	8,524	7,978
Operating expenses	**(4,324)**	(3,952)	(3,417)
Trading surplus	**4,502**	4,572	4,561
General insurance claims	**(174)**	(142)	(169)
Provisions for bad and doubtful debts	**(747)**	(541)	(615)
Amounts written off fixed asset investments	**(60)**	(32)	(7)
Operating profit	**3,521**	3,857	3,770
Income from associated undertakings and joint ventures	**(10)**	3	12
Profit (loss) on sale and closure of businesses	**39**	-	(126)
Profit on ordinary activities before tax	**3,550**	3,860	3,656
Tax on profit on ordinary activities	**(971)**	(1,105)	(1,111)
Profit on ordinary activities after tax	**2,579**	2,755	2,545
Minority interests - equity	**(17)**	(13)	(6)
- non-equity	**(62)**	(36)	-
Profit attributable to shareholders	**2,500**	2,706	2,539
Economic profit[(1)]	**1,543**	1,839	1,777

(1) Lloyds TSB Group defines economic profit as the earnings on the equity invested in the business less a notional charge for the cost of the equity invested in that business. See " - Economic Profit".

2001 compared with 2000

Profit on ordinary activities before tax fell by £310 million or 8 per cent to £3,550 million from £3,860 million, driven by a reduction in income from Lloyds TSB Group's insurance businesses caused by the overall fall in stock market values. Shareholders' equity increased by 7 per cent however earnings per share fell by 8 per cent to 45.2p. The post-tax return on average shareholders' equity was 23.5 per cent.

Total income grew by £302 million, or 4 per cent, from £8,524 million in 2000 to £8,826 million in 2001. Net interest income increased by £357 million, or 8 per cent, from £4,587 million to £4,944 million, although after adjusting for the effect of the inclusion of a full year's funding cost relating to the acquisition of Scottish Widows in March 2000, there was an underlying growth of £459 million or 9 per cent. Average interest earning assets increased by £13,923 million or 11 per cent to £144,945 million. Most of this growth was in the UK where average interest earning assets grew by £10,670 million; personal lending and mortgage balances grew by £6,139 million and corporate and commercial balances increased by £4,628 million. Overseas average interest earning assets increased by £3,253 million with growth in New Zealand and Brazil. The effect of this growth was partly offset by a 4 basis point fall in the underlying net interest margin reflecting the increasingly competitive operating conditions and a lower contribution from interest-free liabilities, caused by the lower interest rate environment.

Other income in 2001 fell by £55 million from £3,937 million to £3,882 million. Income from long-term assurance business fell by £422 million as a 15 per cent fall in the FTSE All-Share index during the year caused a sharp reduction in the earnings from the investments held to support Lloyds TSB Group's life and general insurance activities. This was partly offset by a £272 million improvement in other operating income caused mainly by an increase of £178 million in operating lease rental income, reflecting both the inclusion of Chartered Trust for the full year and underlying volume growth, and profits of £57 million from the sale and leaseback of branch and head office premises. There was an increase in net fees and commissions receivable, after deducting fees and commissions payable, of £31 million, dealing profits increased by £35 million and premium income from the general insurance underwriting business grew by £29 million.

Operating expenses in 2001 increased by £372 million, or 9 per cent to £4,324 million from £3,952 million. The efficiency ratio increased from 46.4 per cent to 49.0 per cent. Exceptional restructuring costs of £217 million were incurred in 2001 compared with £188 million in 2000. Of this amount £167 million was incurred in connection with Lloyds TSB Group's efficiency programme, mainly comprising severance, software write-off and consultancy costs, and a further £50 million in respect of the integration of Scottish Widows. Excluding these amounts, there was an underlying increase in costs of £343 million, of which £172 million was due to the inclusion of Scottish Widows and Chartered Trust for a full year. The remainder of the growth was due to increased staff and other costs supporting the improvement in retail banking sales volumes achieved during the year.

The total charge in respect of bad and doubtful debt provisions increased by £206 million or 38 per cent to £747 million from £541 million, although this was adversely affected by an increase in the general provision of £55 million in respect of Lloyds TSB Group's exposures in Argentina. The charge for bad and doubtful debts attributable to UK operations grew by £144 million to £570 million partly reflecting the inclusion of Chartered Trust for a full year, but also as a result of an £83 million increase in the charge against the retail banking and mortgages portfolio due to the growth in the level of outstanding balances and partly as a result of a one-off benefit of £42 million in 2000. Provisions against the corporate and commercial lending portfolios also increased as provisions were required against a small number of large exposures. Overseas provisions, excluding the general provision in respect of Argentina, increased by £7 million as higher charges in Uruguay, Dubai and the Netherlands more than offset improvements in Colombia and New Zealand. Excluding the effect of the additional general provision against Argentina, the charge in respect of bad and doubtful debts expressed as a percentage of average lending increased to 0.57 per cent from 0.50 per cent in 2000.

Amounts written off fixed asset investments increased by £28 million from £32 million to £60 million. In 2001 Lloyds TSB Group provided £45 million against the carrying value of its holding of Argentine Government bonds as a result of the deterioration in the economic environment in that country. The 2000 results include a provision of £18 million against Lloyds TSB Group's holding of Ecuadorian bonds.

The profit on sale of business of £39 million arose as a result of the sale of Lloyds TSB Group's Brazilian Fund management and private banking business including its subsidiary, Lloyds TSB Asset Management S.A., to Banco Itaú S.A.. The sale of this business did not affect Lloyds TSB Group's other Brazilian businesses.

At 31 December 2001, the total capital ratio was reduced to 9.2 per cent and the tier 1 capital ratio was reduced to 8.4 per cent, reflecting a 16 per cent growth in risk-weighted assets from £93,979 million to £108,755 million. Balance sheet assets grew by £17,426 million, or 8 per cent, from £219,113 million to £236,539 million. Loans and advances to customers increased by £8,503 million, or 7 per cent mainly as a result of growth in UK mortgage and personal lending, which increased by £5,565 million, and higher levels of corporate and commercial lending. Debt securities increased by £9,620 million due to higher year-end liquidity requirements and a number of new structured finance transactions which take advantage of tax efficient funding opportunities.

2000 compared with 1999

Profit on ordinary activities before tax rose by £204 million, or 6 per cent, to £3,860 million from £3,656 million in 1999. Earnings per share increased by 6 per cent to 49.3p, shareholders' equity increased by 14 per cent and the post-tax return on average shareholders' equity was 28.1 per cent.

Total income grew by £546 million, or 7 per cent, from £7,978 million in 1999 to £8,524 million in 2000. Net interest income fell by £196 million, or 4 per cent, to £4,587 million reflecting the inclusion of the funding cost of £258 million relating to the acquisition of Scottish Widows; adjusting for this, net interest income increased by £62 million. Average interest earning assets grew by £7,413 million, or 6 per cent, to £131,022 million, adding £276 million to net interest income with growth primarily in UK personal lending and mortgage balances, which increased by £4,186 million. However, this growth was largely offset by an underlying reduction of 17 basis points in the net interest margin, reducing net interest income by £200 million reflecting the competitive market conditions in which Lloyds TSB Group's businesses are operating. Adverse exchange rate movements reduced net interest income by £14 million.

Other income in 2000 grew by £742 million, or 23 per cent, to £3,937 million, with Scottish Widows contributing £317 million of this increase. Net fees and commissions receivable, after deducting fees payable, increased by £218 million or 11 per cent. Insurance broking commission income increased by £71 million in line with sales volumes and there was also growth in retail banking fee income; net income from credit and debit cards increased by £18 million, fees earned from Lloyds TSB Group's Added Value current accounts grew by £17 million after package charges, and arrangement fees increased by £13 million. Private banking and stockbroking income increased by £14 million as a result of higher transaction volumes and fees from large corporate activity grew by £15 million. Income from the long-term assurance businesses increased by £388 million, principally due to the acquisition of Scottish Widows, and other operating income grew by £144 million as a result of an £89 million increase in operating lease rental income, mainly due to the acquisition of Chartered Trust, and a higher level of gains arising on the disposal of fixed asset investments.

Operating expenses in 2000 increased by £535 million, or 16 per cent, to £3,952 million from £3,417 million in 1999. The efficiency ratio increased from 42.8 per cent to 46.4 per cent. Included within operating expenses in 2000 were £188 million of restructuring costs, of which £108 million related to severance and consultancy costs incurred in connection with Lloyds TSB Group's efficiency programme described in "Unusual items – Exceptional restructuring costs". A further £59 million related to the integration of Scottish Widows and a further £21 million to the integration of Chartered Trust. Excluding restructuring costs, expenses grew by £347 million. The acquisitions of Scottish Widows and Chartered Trust resulted in additional costs of £117 million and the investment made by Lloyds TSB Group during the year in its e-commerce, wealth management and customer relationship management programmes added a further £180 million to the cost base. There was also an increase of

£60 million in the depreciation charge, excluding the effect of the acquisition of Chartered Trust, largely due to increased volumes of operating lease assets within Lloyds UDT and Lloyds TSB Leasing and the effect of significant capital expenditure incurred in the second half of 1999 on new computer equipment.

The total Lloyds TSB Group charge for bad and doubtful debts in 2000 was 12 per cent lower at £541 million, compared with £615 million in 1999. The charge for bad and doubtful debts attributable to UK operations decreased to £426 million from £500 million, as a result of a £93 million reduction in the charge in retail banking and mortgages partly reflecting a one-off benefit of £42 million following a change in provisioning methodology. This was partially offset by a higher charge in the motor finance businesses following the acquisition of Chartered Trust. Provisions overseas were unchanged at £115 million: provisions in Colombia were £14 million lower which, together with a £14 million increase in recoveries from the provisions held against the emerging market medium-term debt portfolio, offset a £25 million increase in the charge in Argentina. Lloyds TSB Group's charge for bad and doubtful debts, expressed as a percentage of average lending, was 0.50 per cent in 2000 compared to 0.61 per cent in 1999. During 1999, losses of £126 million were incurred upon the sale of the Abbey Life new business capability and the closure of Lloyds TSB Securities Services. These losses were not repeated in 2000.

At 31 December 2000, the total capital ratio was reduced to 9.4 per cent and the tier 1 capital ratio was reduced to 8.5 per cent largely as a result of the acquisition of Scottish Widows. Balance sheet assets increased by £42,063 million, or 24 per cent, to £219,113 million from £177,050 million at the end of 1999. Of this increase, £24,543 million was attributable to an increase in long-term assurance assets attributable to policyholders following the acquisition of Scottish Widows. Loans and advances to customers increased by £12,199 million, or 12 per cent, mainly as a result of growth in UK mortgage and personal lending, which increased by £6,022 million, and the acquisition of Chartered Trust, which added a further £2,490 million. Risk-weighted assets increased by 11 per cent to £93,979 million from £84,415 million at the end of 1999.

Net interest income

The yields, spreads and margins in the table below are those relating to the banking business only.

	2001	2000	1999
Lloyds TSB Group:			
Net interest income £m	**4,944**	4,587	4,783
Average interest-earning assets £m	**144,945**	131,022	123,609
Average rates			
Gross yield on interest-earning assets %(1)	**7.84**	8.44	8.46
Interest spread %(2)	**3.00**	2.98	3.19
Net interest margin %(3)	**3.41**	3.50	3.87
Domestic:(4)			
Net interest income £m	**4,224**	3,956	4,154
Average interest-earning assets £m	**121,244**	110,574	104,242
Average rates			
Gross yield on interest-earning assets %(1)	**7.38**	8.07	7.69
Interest spread %(2)	**3.12**	3.06	3.38
Net interest margin %(3)	**3.48**	3.58	3.98
International:(4)			
Net interest income £m	**720**	631	629
Average interest-earning assets £m	**23,701**	20,448	19,367
Average rates			
Gross yield on interest-earning assets %(1)	**10.19**	10.40	12.58
Interest spread %(2)	**2.43**	2.58	2.60
Net interest margin %(3)	**3.04**	3.09	3.25

(1) Gross yield is the rate of interest earned on average interest-earning assets.

(2) Lloyds TSB Group interest spread is the difference between the rate of interest earned on total average interest-earning assets and the rate of interest paid on total average interest-bearing liabilities. The domestic interest spread is the difference between the rate of interest earned on domestic average interest-earning assets and the rate of interest paid on domestic average interest-bearing liabilities. The international interest spread is the difference between the rate of interest earned on international average interest-earning assets and the rate of interest paid on international average interest-bearing liabilities.

(3) Net interest margin is net interest income as a percentage of average interest-earning assets.

(4) The analysis of net interest income by domestic and international operations shown above is based on the location of the office recording the transaction, except for lending by the international business booked in London.

2001 compared with 2000

Lloyds TSB Group net interest income increased by £357 million, or 8 per cent, to £4,944 million, representing 56 per cent of total income compared to 54 per cent in 2000. After adjusting for the effect of funding the Scottish Widows' purchase consideration for a full year in 2001 compared to only ten months in 2000, the underlying growth was £459 million, or 9 per cent. Average interest earning assets increased by £13,923 million or 11 per cent to £144,945 million, adding £570 million to net interest income. Personal lending and mortgage balances in the UK grew by £6,139 million as Lloyds TSB Group sought to develop these portfolios prudently, but profitably. Within Wholesale Markets and International Banking, average interest earning assets increased by £7,902 million. The asset finance portfolio grew by £1,074 million, partly reflecting the inclusion of Chartered Trust for a full year and there was an increase of £4,628 million in corporate and commercial lending balances in the UK. There was also growth in structured finance balances in the UK and overseas.

The net interest margin fell by 9 basis points, although after adjusting for the funding cost of Scottish Widows, there was an underlying reduction of 4 basis points reducing net interest income by £52 million. A lower interest rate environment in the UK resulted in a reduced contribution from Lloyds TSB Group's low interest rate and interest free liabilities and this was coupled with lower margins earned on corporate and commercial and some personal lending balances, due to competitive pressures. These factors more than offset the benefits obtained from positive interest rate management within Lloyds TSB Group's treasury and central functions. Adverse exchange rate movements, mainly in Brazil, reduced net interest income by £59 million.

Domestic net interest income in 2001 increased by £268 million, or 7 per cent, to £4,224 million, representing 85 per cent of consolidated net interest income. After adjusting for the effect of the inclusion of a full year's funding cost in respect of the Scottish Widows acquisition in March 2000, there was an underlying increase of £370 million. Average interest earning assets increased by £10,670 million, or 10 per cent, to £121,244 million adding £403 million to net interest income. Personal lending and mortgage balances increased by £6,139 million and corporate and commercial balances increased by £4,628 million.

The domestic net interest margin fell by 10 basis points reflecting the higher funding cost of Scottish Widows, which caused a reduction of 7 basis points. There was an underlying reduction of 3 basis points costing £33 million mainly as a result of a reduced contribution from low interest and interest free liabilities due to the lower interest rate environment. The net interest margin on retail lending products fell 5 basis points and margins on corporate and commercial lending also reduced, although the margin earned on mortgage products was little changed.

Net interest income from international operations increased by £89 million, or 14 per cent, to £720 million, representing 15 per cent of consolidated net interest income. Average interest earning assets increased by 20 per cent on a local currency basis, but this was partly offset by the effect of exchange rate movements. In sterling terms, average interest earning assets increased by £3,253 million, or 16 per cent, to £23,701 million adding £155 million to net interest income. Average interest earning assets in Latin America increased by £592 million with growth in corporate and consumer lending in Brazil, and in New Zealand there was an increase of £574 million due to higher volumes of corporate and commercial lending. Overseas structured finance and government guaranteed export credit transactions resulted in a £1,932 million increase in average interest earning assets.

The net interest margin from international operations decreased by 5 basis points lowering net interest income by £7 million. Lower margins in Lloyds TSB Group's Latin American businesses, more than offset small improvements in New Zealand and the benefits of lower cost funding for the overseas wholesale businesses. Adverse exchange rate movements, mainly in Brazil, reduced net interest income by £59 million.

2000 compared with 1999

Lloyds TSB Group net interest income in 2000 fell by £196 million, or 4 per cent, to £4,587 million, reflecting the impact of the funding cost of Scottish Widows following its acquisition in March 2000. Net interest income represented 54 per cent of total income compared to 60 per cent in 1999.

Scottish Widows was acquired on 3 March 2000. The consideration for the acquisition, which was funded through a combination of cash raised on the money market and loan notes issued to those policyholders who elected to receive them, was paid during August 2000. However, for the period from the date of acquisition to the payment date, Lloyds TSB Group compensated the policyholders for the delay in paying the consideration. This compensation, together with the funding cost of the consideration from the date of payment, totalled £258 million in 2000. Excluding the £258 million funding cost of Scottish Widows in 2000, Lloyds TSB Group net interest income increased by £62 million, or 1 per cent, to £4,845 million, notwithstanding a reduction of £200 million caused by a 17 basis point reduction in the underlying net interest margin. This £200 million reduction in net interest income was more than offset by higher volumes of both customer lending and deposits which resulted in an increase of £276 million. Average interest-earning assets increased by 6 per cent to £131,022 million as a result of further growth in mortgages and other personal lending in the UK, which increased by £4,186 million. The net interest margin decreased to 3.50 per cent, a reduction of 37 basis points. The impact of the funding cost of Scottish Widows represented 20 basis points of this 37 basis point reduction, with the residual 17 basis point decrease in the margin reflecting the increasingly competitive operating environment in the UK and a 16 basis point reduction in the international net interest margin. Adverse exchange rate movements reduced net interest income by £14 million.

Domestic net interest income in 2000 decreased by £198 million, or 5 per cent, to £3,956 million, reflecting the £258 million funding cost of Scottish Widows, and this represents 86 per cent of total group net interest income. Underlying net interest income, therefore, increased by £60 million. Average interest-earning assets from Lloyds TSB Group's domestic operations increased by 6 per cent to £110,574 million resulting in an additional £229 million of net interest income. There was further growth in mortgages and other customer lending. The net interest margin decreased by 40 basis points to 3.58 per cent, again partly reflecting the funding cost of Scottish Widows, which caused a reduction of 23 basis points. The increasingly competitive operating environment, particularly for retail lending, and the higher cost of deposit products in a higher average interest rate environment caused an underlying reduction of 17 basis points in the net interest margin. During the year Lloyds TSB Group had strong growth in a number of lower margin products, particularly mortgages and preferentially priced savings accounts. The reduction in the margin caused a £169 million fall in net interest income.

Net interest income from international operations increased by £2 million to £631 million, representing 14 per cent of total group net interest income. Underlying growth on a local currency basis was largely offset by a £14 million reduction caused by exchange rate movements. Average interest-earning assets on a local currency basis increased by 7 per cent, helped by growth in the New Zealand mortgage portfolio, but this increase was partly offset by the effect of exchange rate movements. Although there was a reduction of 218 basis points in the gross yield as a result of lower interest rates in Latin America, the international net interest margin decreased by only 16 basis points to 3.09 per cent.

Other income

	2001 **£m**	2000 £m	1999 £m
Fees and commissions receivable:			
UK current account fees	**573**	629	663
Other UK fees and commissions	**1,220**	1,171	978
Insurance broking	**528**	398	327
Card services	**332**	304	279
International fees and commissions	**269**	266	250
	2,922	2,768	2,497
Fees and commissions payable	**(602)**	(479)	(426)
Dealing profits (before expenses):			
Foreign exchange trading income	**158**	141	133
Securities and other gains	**75**	57	82
	233	198	215
Income from long-term assurance business	**193**	615	227
General insurance premium income	**428**	399	390
Other operating income	**708**	436	292
Total other income	**3,882**	3,937	3,195

2001 compared with 2000

Other income reduced by £55 million, or 1 per cent, to £3,882 million representing 44 per cent of total income. Excluding the impact of the Chartered Trust acquisition made in September 2000, other income fell by £181 million or 5 per cent.

Fees and commissions receivable increased by £154 million, or 6 per cent, largely reflecting strong growth in income from insurance broking. Other UK fees and commissions increased by £49 million, or 4 per cent, from £1,171 million to £1,220 million mainly due to the inclusion in 2001 of fees earned by Chartered Trust which resulted in fee income from the Asset Finance business increasing by £45 million. There was a £26 million increase in fees from large corporate and factoring activity; and fee income from Lloyds TSB Group's share registration operation increased by £12 million. However, unit trust and asset management fees fell by £20 million and stockbroking income fell by £10 million, as a result of the substantial reduction in stock market activity in the second half of the year. Fees from the retail banking operations also fell following the withdrawal of ATM fees, which reduced income by £29 million, although this was partly offset by the inclusion of £22 million of recharges to Goldfish Bank, Lloyds TSB Group's joint venture with Centrica plc.

Insurance broking commission income increased by £130 million as a result of higher levels of creditor insurance sales which increased income by £98 million and growth in other major product lines. There was also a benefit of £30 million from a one-off change in broking commission arrangements. Income from credit and debit cards increased by £28 million, mainly as a result of higher merchant service charges and fees. However, UK current account fee income fell by £56 million; a £28 million increase in fee income from Added Value accounts was more than offset by a £51 million fall in unauthorised borrowing fees and a £40 million reduction in service charges, as part of the Group's programme to make its customer proposition more competitive.

Fees and commissions payable increased by £123 million compared to 2000 as a result of the impact of the Chartered Trust acquisition, higher reciprocity fees and an increase in package costs relating to a number of products.

Dealing profits increased by £35 million to £233 million, reflecting benefits from opportunities created from managing certain exposures arising within the Group's insurance businesses, an improved performance from the treasury operations in London and higher foreign exchange trading income from The National Bank of New Zealand.

Income from long-term assurance business fell by £422 million from £615 million to £193 million. Income from long-term assurance business in 2000 benefited from a change in the economic assumptions used to calculate the embedded value, which increased income by £127 million, although this was partly offset by a one-off charge of £80 million in respect of stakeholder pensions. Excluding these items there was an underlying decrease of £375 million.

There was growth in new business, in part reflecting successful sales of Lloyds TSB Group's stakeholder pension product and a change in the mix of new business to more profitable regular premium business, which after distribution costs increased income by £43 million. There was a £40 million increase in income from existing business reflecting the growth in the size of the in-force book and a £30 million reduction in provisions for redress to past purchasers of pension policies as the review nears its completion. However these factors were more than offset by a £500 million reduction in the earnings from the investments held to support the life assurance operations largely reflecting the decline in stock market values during the year.

Premium income from insurance underwriting increased by £29 million, or 7 per cent, from £399 million to £428 million. This was due to higher home insurance sales during 2001, which increased by £53 million to £281 million reflecting the success of the home insurance product and improved cross-selling to Lloyds TSB Group's mortgage customers. This has more than offset a £16 million fall in income from creditor insurance, following the outsourcing of the card protection book to Norwich Union in 2000, and small reductions in income from other products.

Other operating income increased to £708 million from £436 million in 2000 reflecting an increase in income from operating lease rentals, partly as a result of the acquisition of Chartered Trust, from £151 million in 2000 to £329 million in 2001. Other significant contributions to other operating income are the realisation of venture capital gains within Lloyds TSB Development Capital of £57 million, earnings on the sale and restructuring of emerging market investments of £109 million and £57 million profit on the sale and leaseback of premises.

2000 compared with 1999

Other income in 2000 increased by £742 million, or 23 per cent, to £3,937 million representing 46 per cent of total income. Scottish Widows contributed £317 million of this increase.

Fees and commissions receivable in 2000 increased by £271 million, or 11 per cent; Scottish Widows contributed £62 million of this increase. UK current account fees fell by £34 million largely as a result of a £14 million reduction in service charges and returned cheque fees and a £31 million reduction in unauthorised overdraft fees following their partial withdrawal as part of a marketing initiative. Unauthorised overdraft fees are charged to those customers who allow their current account to become overdrawn without having organised an agreed overdraft facility in advance. These reductions more than offset a £22 million increase in fees from Lloyds TSB Group's Added Value current accounts reflecting the increased popularity of this product. Depending on the balance in the account, the holder of an Added Value current account pays a monthly fee which allows them access to a range of discounted products and services.

Excluding Scottish Widows, other UK fees and commissions increased by £131 million or 13 per cent, interbank agency and ATM fees increased by £36 million and there was a £13 million increase in loan arrangement fees. Fees from large corporate activity in the UK increased by £15 million and there was a £14 million increase in private banking and stockbroking income as a result of higher transaction volumes and a £9 million increase in income from Lloyds TSB Group's factoring operations. The acquisition of Chartered Trust accounted for a further £17 million of the increase.

Insurance broking commission income increased by £71 million or 22 per cent reflecting a £50 million improvement in income from card and loan protection products, as a result of increased sales volumes, and a £23 million increase in the level of retrospective commissions, which are dependent upon the profitability of policies sold in previous years.

Income from credit and debit cards improved by £25 million as a result of increased late payment charges and merchant commissions. International fees and commissions increased by £16 million or 6 per cent largely due to a £10 million increase in income generated from structured finance transactions entered into in the United States.

Fees and commissions payable in 2000 increased by £53 million against 1999 of which £18 million was attributable to Scottish Widows. The remaining increase of £35 million was largely as a result of a £14 million increase in interchange fees reflecting higher volumes and a £20 million increase in interbank agency fees payable, which more than offset a £15 million reduction in fees paid by Lloyds UDT as a result of lower transaction volumes. The acquisition of Chartered Trust accounted for a further £23 million of the increase.

Dealing profits in 2000 fell by £17 million; a £20 million improvement in the performance of Lloyds TSB Group's Treasury operations was more than offset by a £41 million reduction in the return from the general insurance equities portfolio reflecting the decline in UK stock market values.

Income from long-term assurance business in 2000 increased by £388 million to £615 million, largely as a result of the acquisition of Scottish Widows. Excluding Scottish Widows there was an underlying increase of £120 million reflecting the benefit of changes in the economic assumptions of £127 million and a number of other non-recurring items which more than offset a charge of £80 million in respect of stakeholder pensions. Stakeholder pensions were introduced in the UK in April 2001. Stakeholder pensions aim to provide a low-cost and flexible way for people to save for their retirement. Stakeholder pensions are open only to persons earning less than £30,000 per year. Contributions to a stakeholder pension are capped at £3,600 per year (including tax) and can be cumulated with contributions to an occupational pension scheme. Employers with five or more employees who do not offer any kind of pensions scheme must provide access to a stakeholder pension scheme. Money invested in stakeholder pensions will be managed privately (i.e., outside the state pension system) and will be invested in the stock market. Upon retirement a quarter of the accumulated capital can be taken out as a tax-free cash sum and the remainder must be used to buy an annuity which pays the retirement pension. See "—Results of operations—Unusual items". General insurance premium income on underwritten business in 2000 increased by £9 million, or 2 per cent, against 1999.

Other operating income in 2000 increased by £144 million, largely reflecting the acquisition of Chartered Trust and increased operating lease rentals within Lloyds TSB Leasing and Lloyds UDT which together resulted in an increase in income of £89 million. Gains on the sale of investments increased by £53 million.

Operating expenses

	2001 £m	2000 £m	1999 £m
Administrative expenses			
Staff:			
Salaries and profit sharing	**1,754**	1,626	1,500
National insurance	**140**	131	125
Pensions	**(108)**	(105)	(108)
Restructuring	**8**	47	20
Other staff costs	**191**	189	180
	1,985	1,888	1,717
Premises and equipment:			
Rent and rates	**261**	247	250
Hire of equipment	**18**	26	33
Repairs and maintenance	**110**	115	107
Other	**117**	109	100
	506	497	490
Other expenses:			
Communications and external data processing	**433**	394	406
Advertising and promotion	**152**	167	113
Professional fees	**105**	126	90
Other	**376**	306	324
	1,066	993	933
Administrative expenses	**3,557**	3,378	3,140
Exceptional restructuring costs	**217**	188	-
Total administrative expenses	**3,774**	3,566	3,140
Depreciation	**511**	364	265
Amortisation of goodwill	**39**	22	12
Total operating expenses	**4,324**	3,952	3,417
Efficiency ratio (in %)	**49.0**	46.4	42.8
Efficiency ratio (adjusted) (in %)[1]	**42.9**	43.4	42.6

(1) Excluding short-term fluctuations in investment returns, changes in economic assumptions, exceptional restructuring costs, Abbey National offer costs, provisions for redress to past purchasers of pension policies and stakeholder pension related charge. See "—Unusual items".

2001 compared with 2000

Total operating expenses in 2001 increased by £372 million, or 9 per cent, to £4,324 million from £3,952 million in 2000. There was a further exceptional restructuring charge of £217 million, compared to £188 million in 2000, comprising mainly severance, software write-off and consultancy costs incurred in connection with the Lloyds TSB Group's efficiency programme and the ongoing integration of Scottish Widows. See "Unusual items – Exceptional restructuring costs". Excluding these restructuring charges, there was an underlying growth in costs of £343 million of which £172 million was due to the acquisitions of Scottish Widows and Chartered Trust and £16 million to costs incurred in connection with the unsuccessful offer for Abbey National. Investments in Lloyds TSB Group's revenue growth businesses, e-commerce and real-time banking in 2001 totalled £235 million compared to £224 million in 2000.

Administrative expenses in 2001 increased by £179 million, or 5 per cent, from £3,378 million to £3,557 million. Staff costs grew by £97 million, or 5 per cent, mainly as a result of a £128 million growth in salaries and profit sharing reflecting both the growth in staff numbers and the effect of the annual pay review, and the increased cost of incentive payments to customer facing staff. This has been partly offset by a £39 million reduction in ongoing restructuring costs, as the costs associated with the closure of a number of minor operations in 2000 have not been repeated.

Premises and equipment costs increased by £9 million principally due to higher rental costs on branch and head office properties and losses on the disposal of equipment which more than offset lower IT equipment hire costs. Other costs increased by £73 million. There was a £39 million growth in communications and external data processing costs to support the development of Lloyds TSB Group's e-commerce activities and real-time banking systems and a £23 million increase in charges made by iPSL, Lloyds TSB Group's new clearings joint venture. There was also a £19 million increase in operational losses, partly caused by a higher incidence of credit card fraud.

Depreciation increased by £147 million. There was an increase of £95 million in the charge in respect of operating lease assets, following a reduction of £23 million in the depreciation charge on certain ship leases, of which £82 million was due to the acquisition of Chartered Trust. In addition, there was a £49 million increase in the depreciation charge in respect of equipment reflecting the impact of capital expenditure, in particular on IT equipment, during 2000. Goodwill amortisation increased by £17 million due to the amortisation of the goodwill arising on the acquisition of Chartered Trust.

The efficiency ratio in 2001 was 49.0 per cent compared to 46.4 per cent in 2000.

2000 compared with 1999

Total operating expenses in 2000 increased by £535 million, or 16 per cent, to £3,952 million from £3,417 million in 1999. Expenses in 2000 included exceptional restructuring costs of £188 million, comprising mainly severance and consultancy costs relating to Lloyds TSB Group's efficiency programme and a £21 million provision in respect of the integration of Chartered Trust. See "Unusual items - Exceptional restructuring costs". Administrative expenses in 2000 increased by £238 million, or 8 per cent, to £3,378 million of which £69 million was attributable to the post-acquisition costs of Scottish Widows and Chartered Trust. The remaining increase was due to the investment that Lloyds TSB Group has made in e-commerce, wealth management and customer relationship management programmes which added £180 million to the cost base. This was reflected in increased staff costs, advertising and promotional expenditure and consultancy fees. Depreciation in 2000 increased by £99 million, of which £37 million related to the depreciation in Chartered Trust following its acquisition. The remainder of the increase was due to the growth during the year in operating lease assets which accounted for £21 million of the increase and significant capital expenditure incurred in the second half of 1999 on new computer equipment.

Goodwill amortisation increased by £10 million following the acquisition of Chartered Trust. The goodwill arising upon the acquisition of Scottish Widows amounting to £1,870 million is not being amortised because, in the opinion of the directors, it has an indefinite useful life.

The efficiency ratio in 2000 was 46.4 per cent compared to 42.8 per cent in 1999.

Charge for bad and doubtful debts

	2001	2000	1999
	£m	£m	£m
Domestic	**570**	426	500
International	**177**	115	115
Total charge	**747**	541	615
Specific provisions	**736**	547	615
General provisions	**11**	(6)	-
Total charge	**747**	541	615
Charge as % of average lending:	**%**	%	%
Domestic	**0.54**	0.45	0.57
International	**1.10**	0.80	0.84
Total charge	**0.62**	0.50	0.61

2001 compared with 2000

The total charge for bad and doubtful debts increased by £206 million, or 38 per cent, to £747 million from £541 million. The charge attributable to Lloyds TSB Group's UK operations increased by £144 million to £570 million from £426 million, partly as a result of the acquisition of Chartered Trust which increased the charge during the year by £27 million. During 2000, UK Retail Banking had a one-off benefit of £42 million following the full centralisation of its arrears processing, which was not repeated in 2001. Adjusting for this, provisions in UK Retail Banking increased by £52 million reflecting the growth in the size of the personal loan and credit card portfolios. This was partly offset by a £32 million release of the general provision relating to the Lloyds TSB Group's mortgage portfolio following a change in provisioning methodology.

The charge against the corporate and commercial lending portfolios increased by £53 million largely as a result of provisions being required against a small number of corporate exposures, reflecting the slowdown in economic growth, but also as a result of a £30 million provision made against the Group's loans and advances to one specific corporate customer, which total some £70 million. There was an £18 million reduction in the provisions made against the consumer finance portfolio of Lloyds UDT reflecting improved credit procedures.

Provisions overseas increased by £62 million, from £115 million to £177 million largely as a result of a £55 million increase in the general provision, taken as a measure of prudence, to cover ongoing credit difficulties in Argentina. Increased provisions against specific corporate exposures in Uruguay, Dubai and the Netherlands more than offset improvements in Colombia and New Zealand.

2000 compared with 1999

The total charge for bad and doubtful debts in 2000 decreased by 12 per cent to £541 million. The charge attributable to Lloyds TSB Group's UK operations decreased to £426 million in 2000 from £500 million in 1999 largely due to the continuing benign economic conditions which led to a revision to expected loss rates within the personal lending and card portfolios and a one-off benefit of £42 million arising from a change in methodology in 2000 for retail provisioning to recognise more accurately the amount that Lloyds TSB Group expects to recover. Previously, personal loans transferred to recovery departments were provided against in full and recoveries credited to the profit and loss account when made. Under the revised methodology, provisions are made to write the debt down to its estimated ultimate recoverable value. Recoveries are initially credited against the balance sheet carrying value of the debt and thereafter, to the profit and loss account.

Provisions overseas were unchanged at £115 million. A £14 million reduction in provisions in Colombia as the economy started to recover from the recessionary conditions of the previous year, together with a £14 million increase in recoveries from the provisions held against the emerging markets medium-term debt portfolio, offset a £25 million increase in provisions in Argentina following a deterioration in the economic environment.

Taxation

The rate of tax is influenced by the geographic and business mix of profits. In the absence of special factors, Lloyds TSB Group does not expect the tax rate to vary significantly from the average UK corporation tax rate.

	2001 £m	2000 £m	1999 £m
UK corporation tax			
Current tax on profits for the year	**836**	941	767
Adjustments in respect of prior years	**(14)**	3	21
	822	944	788
Double taxation relief	**(87)**	(72)	(45)
	735	872	743
Foreign tax			
Current tax on profits for the year	**179**	137	110
Adjustments in respect of prior years	**(17)**	(5)	8
	162	132	118
Current tax charge	**897**	1,004	861
Deferred tax	**73**	100	245
Associated undertakings and joint ventures	**1**	1	5
Total charge	**971**	1,105	1,111

2001 compared with 2000

The effective rate of tax in 2001 was 27.4 per cent compared with 28.6 per cent in 2000; the corporation tax rate for both years was 30 per cent. The lower effective tax rate in 2001 is largely due to tax relief on payments to the Lloyds TSB qualifying share ownership trust to satisfy Save As You Earn options which reduced the effective rate by 1.7 per cent and gains on the disposal of investments and properties sheltered by capital losses which reduced the effective rate by 1.1 per cent. See Note 9 to the Consolidated Financial Statements.

2000 compared with 1999

The effective rate of tax in 2000 was 28.6 per cent, compared with 30.4 per cent in 1999. These rates compare with an average UK corporation tax rate for 2000 of 30 per cent and 30.25 per cent in 1999. The lower effective rate of tax in 2000 is largely due to tax relief on payments to the Lloyds TSB qualifying employee share ownership trust to satisfy Save As You Earn options which reduced the effective rate by 1.0 per cent, and gains on disposals of investments sheltered by capital losses which reduced the effective rate by 0.4 per cent.

Economic profit

In pursuit of our aim to maximise shareholder value over time, management has for the last eleven years used a system of value based management as a framework to identify and measure value creation. Management uses economic profit as a measure of performance because it captures both growth in investment and return. Lloyds TSB Group defines economic profit as the earnings on the equity invested in the business less a notional charge for the cost of the equity invested in that business.

Lloyds TSB Group believes that economic profit instils financial discipline in determining investment decisions throughout Lloyds TSB Group and that it enables Lloyds TSB Group to evaluate alternative strategies objectively, with a clear understanding of the value created by each strategy, and then to select the strategy which creates the greatest value. Awards to senior executives under Lloyds TSB Group's annual bonus arrangements are partly determined by the achievement of economic profit targets.

Management only changes its estimates of the cost of equity to reflect significant changes in long-term interest rates and other external market factors which are considered sustainable. The principal factor in estimating the cost of equity is sustainable long-term interest rates. If long-term interest rates increase, management will consider raising its estimate of the cost of equity; if long-term interest rates fall, management will consider reducing its estimate of the cost of equity. The principal other external market factors considered are equity risk premium and Lloyds TSB Group's share price volatility relative to the UK stock market as a whole. Any change to the estimated cost of equity will be disclosed. For the last three years, management has used a cost of equity of 9 per cent to reflect the shareholders' minimum required rate of return on equity invested.

The table below summarises our calculation of economic profit for the periods indicated.

	2001	2000	1999
	£m	£m	£m
Average shareholders' equity	**10,638**	9,638	8,468
Profit attributable to shareholders	**2,500**	2,706	2,539
Less: notional charge	**(957)**	(867)	(762)
Economic profit	**1,543**	1,839	1,777

The notional charge has been calculated by multiplying average shareholders' equity by the cost of equity.

2001 compared with 2000

Economic profit fell by £296 million, or 16 per cent, from £1,839 million in 2000 to £1,543 million in 2001. Profit attributable to shareholders fell by 8 per cent to £2,500 million and there was a higher notional charge on equity resulting from a 10 per cent increase in average equity from £9,638 million to £10,638 million.

2000 compared with 1999

Economic profit rose by £62 million, or 3 per cent, to £1,839 million from £1,777 million in 1999. Profit attributable to shareholders increased by 7 per cent to £2,706 million but this was partly offset by a higher notional charge on equity resulting from a 14 per cent increase in average equity to £9,638 million.

Line of business information

Management analyses the contribution of each line of business to Lloyds TSB Group's overall profit attributable to shareholders and economic profit after adjusting for certain items which either are not expected to recur or which are unusual in nature, thereby hindering management's analysis of trends. Those items, which had a significant impact on Lloyds TSB Group's 2001 results, were:

- short-term fluctuations in investment returns;
- exceptional restructuring costs;
- Abbey National offer costs;
- the provision for redress to past purchasers of pension policies; and
- profit arising on sale of business.

In 2000, changes in the economic assumptions applied to the long-term assurance business and a charge relating to stakeholder pensions were also significant items.

Each of these items is discussed later under "—Unusual items" and is set out separately in the following table:

Summary

	2001 £m	2000 £m	1999 £m
UK Retail Banking and Mortgages	**1,588**	1,665	1,657
Insurance and Investments	**1,601**	1,425	843
Wholesale Markets and International Banking	**1,381**	1,223	1,207
Central group items	**(108)**	(118)	119
Contribution	**4,462**	4,195	3,826
Unusual items:			
Short-term fluctuations in investment returns	**(648)**	(94)	58
Changes in economic assumptions	**-**	127	-
Exceptional restructuring costs	**(217)**	(188)	-
Abbey National offer costs	**(16)**	-	-
Provisions for redress to past purchasers of pension policies	**(70)**	(100)	(102)
Stakeholder pension related charge	**-**	(80)	-
Profit (loss) on sale and closure of businesses	**39**	-	(126)
Profit before tax	**3,550**	3,860	3,656

In the analysis that follows, contribution is defined as profit before tax before taking into account the unusual items set out under " - Unusual items".

UK Retail Banking and Mortgages

The UK retail businesses of Lloyds TSB Group provide banking and financial services to personal and small business customers, private banking and stockbroking. Lloyds TSB Group's UK mortgage business is conducted through Cheltenham & Gloucester, Lloyds TSB Bank, Lloyds TSB Scotland, Scottish Widows Bank and C&G TeleDirect.

	2001 £m	2000 £m	1999 £m
Net interest income	**3,115**	2,951	2,943
Other income	**1,141**	1,143	1,087
Total income	**4,256**	4,094	4,030
Operating expenses	**(2,243)**	(2,099)	(1,951)
Trading surplus	**2,013**	1,995	2,079
Provisions for bad and doubtful debts	**(415)**	(332)	(425)
Income from associated undertakings and joint ventures	**(10)**	2	3
Contribution	**1,588**	1,665	1,657
Unusual items:			
Exceptional restructuring costs	**(150)**	(99)	-
Profit before tax	**1,438**	1,566	1,657
Efficiency ratio	**52.7%**	51.3%	48.4%
Total assets (year-end)	**£77,915m**	£71,292m	£64,346m
Total risk-weighted assets (year-end)	**£48,141m**	£44,009m	£39,703m

2001 compared with 2000

The contribution, calculated as explained under "- Line of business information – Summary" from UK Retail Banking and Mortgages in 2001 fell by £77 million, or 5 per cent, to £1,588 million.

Total income increased by £162 million, or 4 per cent to £4,256 million. Net interest income increased by £164 million to £3,115 million as growth in lending and savings balances, adding £241 million to income, more than offset a 12 basis point fall in the margin, reducing net interest income by £77 million. Compared to 2000, period end personal loan and credit card balances increased by 18 per cent and balances on current accounts and savings and investment accounts grew by 9 per cent. Mortgage balances also increased. A key objective of Lloyds TSB Group is to grow its mortgage lending prudently but profitably. As a result of this focus, net new lending was lower than Lloyds TSB Group's share of outstanding mortgage balances however the net interest margin was little changed. Gross new mortgage lending increased by 21 per cent to £13,986 million compared with

£11,518 million a year ago, however net new lending was £3,919 million compared to £4,627 million in 2000. This resulted in a fall in Lloyds TSB Group's estimated market share of net new lending from 11.3 per cent to 7.1 per cent. Mortgage balances outstanding at the end of 2001 amounted to £56,578 million compared to £52,659 million at the end of 2000, an estimated market share of 9.5 per cent.

The net interest margin on retail lending products was 5 basis points lower, with improved margins on credit cards and overdrafts following base rate cuts, offset by lower margins on personal loans due to a combination of a higher proportion of lending being at concessionary rates offered to attract new business and higher average loan values which are provided at lower interest rates. The retail deposit margin fell by 21 basis points as the lower interest rate environment reduced the benefit from low interest rate and interest free current accounts. The margin on mortgage lending reduced by 1 basis point.

Other income decreased by £2 million to £1,141 million. There was a £21 million improvement in income earned from credit and debit cards and income from added value current accounts increased by £19 million due to increased volumes. In 2001, profits on the sale and leaseback of premises totalled £57 million reflecting Lloyds TSB Group's ongoing strategy, started some years ago, to sell and lease back a number of branches to create greater flexibility in the changing environment for retail sales. This was largely offset by a £76 million decrease in income following the withdrawal of ATM fees and planned reductions in unauthorised borrowing fees; stockbroking income fell by £10 million due to lower transaction volumes.

Operating expenses increased by £144 million, or 7 per cent, to £2,243 million compared to £2,099 million in 2000. Revenue investment expenditure in Lloyds TSB Group's growth businesses, information technology integration and e-commerce amounted to £202 million in 2001 compared to £192 million in 2000. There was an increase in staff costs reflecting the growth in staff numbers during the year as a result of the recruitment of additional service and sales staff into the branch network and the effect of the annual pay review. Communications costs were higher following revisions to network rental charges and the depreciation charge increased reflecting the high levels of capital expenditure, particularly in respect of IT equipment, in 2000. The efficiency ratio increased from 51.3 per cent in 2000 to 52.7 per cent in 2001.

Provisions for bad and doubtful debts increased by £83 million, or 25 per cent, to £415 million. During 2000 there was a one-off benefit of £42 million as a result of a change in provisioning methodology following the centralisation of arrears processing which was not repeated in 2001. There was an underlying increase of £52 million in the provisions charge against personal lending and credit card lending, reflecting the increase in the size of the portfolios. There was a net release from the provisions held against the mortgage portfolio of £24 million as a result of a £32 million reduction in the general provision following a change in provisioning methodology; in 2000 there was a net release of provisions of £13 million.

Lloyds TSB Group's share of the results of its joint venture operations was a loss of £10 million, due to start-up costs incurred by Goldfish Bank.

2000 compared with 1999

The contribution from UK Retail Banking and Mortgages in 2000 rose by £8 million to £1,665 million.

Total income in 2000 increased by £64 million to £4,094 million. Net interest income increased by £8 million to £2,951 million due to a combination of two factors.

Growth in lending and deposit balances increased net interest income by £209 million. Personal lending and credit card balances increased by 9 per cent since the end of 1999 and savings and investment products grew by 10 per cent over the same period; lending to small and medium-sized businesses increased by 13 per cent during 2000 and there was a 14 per cent increase in customer deposits. Despite competitive market conditions, Lloyds TSB Group increased its market share of residential mortgages. Gross new lending increased by 8 per cent to £11,518 million compared with £10,710 million in 1999, and net new lending was £4,627 million compared to £2,791 million in 1999, representing a market share of 11.3 per cent. Mortgages outstanding at the end of 2000 amounted to £52,659 million compared to £47,451 million at the end of 1999, an estimated market share of 9.8 per cent.

The benefit of this balance sheet growth was largely offset by significant erosion in the net interest margin. The net interest margin fell by 33 basis points with reductions in most areas; the mortgage margin fell 23 basis points and the margin for retail lending products was 74 basis points lower largely reflecting the competitive market conditions. Retail deposit margins also fell as there was a continuing switch to higher rate products. The effect of the lower margins has been to reduce net interest income by £201 million.

Other income in 2000 increased by £56 million, or 5 per cent, to £1,143 million. There was a £13 million increase in loan arrangement fees, reflecting lending growth and a revised charging structure introduced in the second half of the year and income from credit and debit cards increased by £18 million principally due to increases in late payment charges and merchant commissions. Fees from Lloyds TSB Group's Added Value current accounts improved by £17 million, net of package costs, as a result of volume growth. ATM charges grew by £16 million following their introduction in late 1999, although these have subsequently been withdrawn. Private banking and stockbroking income increased by £14 million as a result of higher transaction volumes. However, unauthorised overdraft fees fell by £31 million following their withdrawal for certain customers and the benefit of a £6 million increase in mortgage application fees, reflecting the growth in volumes in this business, was offset by a £1 million increase in legal fees incurred setting up the mortgage and not recharged to customers as part of a marketing initiative and the introduction of payments to intermediaries to encourage them to introduce new business to Lloyds TSB Group, which resulted in additional costs of £2 million.

Operating expenses in 2000 increased by £148 million, or 8 per cent. The efficiency ratio increased from 48.4 per cent in 1999 to 51.3 per cent in 2000. The increase in expenses was largely attributable to revenue investment in developing e-commerce, wealth management and customer relationship management programmes, resulting in additional costs of approximately £100 million. Outside of these growth businesses there was an increase in staff costs; although there was a reduction in headcount, this was mainly due to the outsourcing of Lloyds TSB Group's clearing operations in December 2000 and therefore the benefit has yet to appear in the profit and loss account. There was also an increase in depreciation of approximately £30 million as a result of significant capital expenditure on new computer equipment for the branch network in the second half of 1999.

Provisions for bad and doubtful debts in 2000 fell by £93 million, or 22 per cent, to £332 million. This was principally a result of a reduction of £83 million in the charge against the personal lending and credit card portfolios reflecting the continuing benign economic conditions which led to a revision to anticipated loss rates and a one-off benefit of £42 million arising from a change in methodology in 2000 for retail provisioning to recognise more accurately the amount that Lloyds TSB Group expects to recover. There was a net release of provisions held against the mortgage portfolio totalling £13 million reflecting growth in residential house prices which has led to an increase in the value of the security held.

Insurance and Investments

Lloyds TSB Group's insurance and investments activities comprise the life, pensions and unit trust businesses of Scottish Widows and Abbey Life, general insurance underwriting and broking, and Scottish Widows Investment Partnership.

	2001 £m	2000 £m	1999 £m
Contribution by area of business			
Life, pensions and unit trusts			
Scottish Widows (including bancassurance)	**715**	629	222
Abbey Life	**199**	169	138
	914	798	360
General Insurance	**668**	587	461
	1,582	1,385	821
Scottish Widows Investment Partnership	**19**	40	22
Contribution	**1,601**	1,425	843
Unusual items:			
Short-term fluctuations in investment returns	**(648)**	(94)	58
Changes in economic assumptions	**-**	127	-
Exceptional restructuring costs	**(50)**	(59)	-
Provisions for redress to past purchasers of pension policies	**(70)**	(100)	(102)
Stakeholder pension related charge	**-**	(80)	-
Profit before tax	**833**	1,219	799

2001 compared with 2000

The contribution from Insurance and Investments in 2001, calculated as explained under "- Line of business information – Summary", increased by £176 million, or 12 per cent, to £1,601 million from £1,425 million. The contribution from Lloyds TSB Group's life, pensions and unit trusts businesses increased by £116 million, or 15 per cent, to £914 million. The market for medium and long-term investments was adversely affected in the second half of the year, as a consequence of the events of September 11 and the general decline in global stock markets. However, weighted sales (regular premiums plus one-tenth single premiums) increased by 12 per cent helped by the inclusion of Scottish Widows for the full twelve months. See "- Line of business information – Life, pensions and unit trusts."

The contribution from general insurance operations increased by £81 million, or 14 per cent, to £668 million. There was continued growth in sales of card and loan protection products which resulted in an £87 million improvement in profits from broking activities, although there was a £6 million reduction in profits from the underwriting business following a 23 per cent increase in claims expense due to higher property claims. See "- Line of business information – General insurance".

During 2001 Scottish Widows Investment Management and Hill Samuel Asset Management were fully integrated into Scottish Widows Investment Partnership ('SWIP'). A complete overhaul of the management structure has also been undertaken, together with a fundamental review of investment philosophy, processes and systems. The contribution from SWIP in 2001 was

£19 million compared to £40 million in 2000, the reduction in profitability being partly driven by lower stock market levels. At the end of the year SWIP had some £78,000 million of funds under management compared to some £87,000 million at 31 December 2000. The decline has been primarily caused by the lower stock market levels experienced in 2001.

2000 compared with 1999

The contribution from Insurance and Investments in 2000 increased by 69 per cent to £1,425 million from £843 million in 1999, largely as a result of the inclusion, since 3 March 2000, of Scottish Widows. Since that date, the contribution of Scottish Widows was £373 million, before funding costs of £258 million.

The contribution from the life, pensions and unit trusts businesses in 2000 increased by £438 million to £798 million with Scottish Widows contributing £363 million of this increase. Weighted sales (regular premiums plus one-tenth of single premiums) of life, pensions and unit trusts increased by 40 per cent as the sale, on 1 February 2000, of the new business capability of Abbey Life was more than offset by the inclusion, from 3 March 2000, of Scottish Widows. See "—Line of business information—Life, pensions and unit trusts."

The contribution from general insurance operations in 2000 rose by £126 million, or 27 per cent, to £587 million. Increased sales volumes, particularly of creditor insurance products following the outsourcing of the portfolio and higher retrospective commissions led to a £71 million increase in profits from broking activities. Retrospective commissions are a form of profit sharing arrangement between the broking operation and an external underwriter. The profits earned by the underwriter are shared with the broker on the basis of a pre-determined formula. Underwriting profits were £55 million higher, helped by a £27 million reduction in claims costs. See "—Line of business information—General insurance".

The merger of Scottish Widows Investment Management and Hill Samuel Asset Management was completed on 30 June 2000, and the enlarged asset management operation was launched under a new brand, Scottish Widows Investment Partnership. The acquisition of Scottish Widows and the subsequent creation of SWIP, with approximately £87,000 million of funds under management, has enabled Lloyds TSB Group to become a leading player in the UK asset management business. The contribution from Lloyds TSB Group's investment management activities in 2000 was £40 million, up 82 per cent from £22 million in 1999, largely as a result of the inclusion of the Scottish Widows investment management business, which contributed £10 million in 2000.

Life, pensions and unit trusts

The results of the life, pensions and unit trust businesses are analysed in the following table. The basis of this analysis is as follows:

The life and pensions results are split into four elements:

- New business: this represents the value recognised at the end of each financial year from the new business written during that year after taking into account the cost of establishing technical provisions and reserves. This is shown before the significant costs of acquiring that new business, which are shown separately as 'Distribution costs'.

- Existing business: this comprises the following elements:

    - the expected return arising from the unwinding of the discount applied to the expected cash flows at the beginning of a year;

    - experience variances caused by differences between the actual experience during that year and the expected experience; and

    - the effects of changes in assumptions, other than economic assumptions, and other items.

- Investment earnings: this represents the expected return on both the net tangible assets and the value of the shareholder's interest in the long-term business account, based upon the economic assumptions made at the beginning of a year.

- Distribution costs: the costs of acquiring the new business generated in that year are shown separately. These comprise the cost of selling products through Lloyds TSB Bank's branch network, the commissions paid to independent financial advisers and the costs of other direct sales channels.

Unit trust income is shown before the acquisition costs of new business which are separately disclosed.

	2001 £m	2000 £m	1999 £m
New business	**362**	297	148
Existing business:			
- expected return	**374**	334	203
- experience variances	**37**	36	26
- assumption changes and other items	**95**	96	(13)
	506	466	216
Investment earnings	**247**	212	38
Life and pensions distribution costs	**(247)**	(225)	(99)
	868	750	303
Unit trusts	**143**	157	138
Unit trust distribution costs	**(97)**	(109)	(81)
	46	48	57
Contribution of life, pensions and unit trusts	**914**	798	360
Contribution of asset management	**19**	40	22
Unusual items:			
Short-term fluctuations in investment returns	**(602)**	(67)	36
Changes in economic assumptions	**-**	127	-
Exceptional restructuring costs	**(50)**	(59)	-
Provisions for redress to past purchasers of pension policies	**(70)**	(100)	(102)
Stakeholder pension related charge	**-**	(80)	-
Profit before tax	**211**	659	316

The table below shows the level of new business premium income and unit trust sales. Management monitor these figures because they provide an indication of both the rate of growth and the profitability of the business.

	2001 £m	2000 £m	1999 £m
New business premium income and unit trust sales:			
Regular premiums	**282.0**	156.9	129.4
Single premiums	**2,741.0**	2,376.1	796.7
Unit trusts	**1,400.5**	1,993.3	1,770.2

Weighted sales is a UK insurance industry standard which measures the new business volumes; the weighting is made towards regular premium policies to reflect the long-term nature of these contracts. There are three main distribution channels for the sale of Lloyds TSB Group's life, pension and unit trust products and the table below shows the relative importance of each.

	2001 £m	2000 £m	1999 £m
Weighted sales (regular + 1/10 single) by distribution channel:			
Branch network	**376.2**	353.3	355.2
Independent financial advisers	**279.8**	254.9	92.8
Direct	**98.7**	67.6	9.3
	754.7	675.8	457.3

2001 compared with 2000

The contribution in 2001 calculated as explained under "- Line of business information – Summary", of the life, pensions and unit trust businesses increased by £116 million, or 15 per cent, to £914 million from £798 million.

New business income from the life and pensions businesses increased in 2001 by £65 million or 22 per cent, from £297 million to £362 million following a 41 per cent increase in weighted sales, primarily as a result of the inclusion of Scottish Widows for a full year, compared with only ten months in 2000. During the year, the life and pensions new business margin, defined as new business income less distribution costs divided by weighted sales, increased to 20.7 per cent from 18.5 per cent in 2000. This improvement was largely a result of cost efficiencies driven by process enhancements, which limited the increase in distribution costs to 10 per cent, together with an improved product mix.

The growth in the weighted sales of life and pensions products was mainly due to an 80 per cent increase in the sales of regular premium products from £156.9 million to £282.0 million. The inclusion of Scottish Widows for the full year compared to only ten months in 2000 added £17.1 million with the remainder of the growth largely due to the launch of stakeholder pension products in April 2001. During 2001, Scottish Widows became the nominated stakeholder pensions provider for a number of associations and employers which gives access to more than 46,000 employers. Over 20,000 employers have already nominated Scottish Widows as their stakeholder pensions provider resulting in 837,000 employees being offered stakeholder pensions. In 2001, weighted sales of stakeholder pension products totalled £76 million, a market share of 15 per cent based upon management estimates.

Sales of single premium life and pensions products increased by £364.9 million, or 15 per cent, to £2,741.0 million. The inclusion of Scottish Widows for a full year accounted for £174.3 million of this increase, the remainder of the growth being due to higher sales of the Scottish Widows with-profits bond through the branch network distribution channel. With-profits bonds comprise a lump-sum investment into a with-profits fund of a life insurance company. With-profit bonds are designed to be low risk investments which produce growth and allow the investor to take out money when needed. The overall return on the investment varies based on the annual bonuses declared by the life insurance company each year, which in turn will depend upon the performance of its investments. During a period of considerable volatility on the world's stock markets, customers regarded this as a safer investment than unit trusts and Individual Savings Accounts (ISAs).

Existing business earnings increased by 9 per cent from £466 million to £506 million. The expected return from existing business increased by £40 million, or 12 per cent, to £374 million. This reflects the unwinding of the long-term discount rate applied to the expected cash flows from the portfolio of in-force business; the increase reflects the growth in the size of the portfolio.

It is standard practice for life companies to regularly review the underlying assumptions that support the embedded value calculations, taking into account latest experience in respect of lapse rates, expense inflation, investment mix, mortality rates and other items. In 2000, this review, together with some tax-related adjustments, resulted in a benefit of £96 million. In 2001, this review, together with the planned harmonisation of actuarial models between Scottish Widows and other Lloyds TSB Group companies, resulted in a benefit of £95 million.

Investment earnings in 2001, before taking into account short-term fluctuations in investment returns (see "–Unusual items–short-term fluctuations in investment returns") increased by £35 million, due to the inclusion of Scottish Widows for the full year and the growth in the size of the investment portfolio supporting the business.

Profits from the unit trust business fell by £2 million, to £46 million. Continued customer focus upon the Scottish Widows with-profits bond and uncertainty created by global stock market volatility resulted in a 29 per cent fall in weighted sales. However, this was only partly reflected in the decline in profitability of the business because of the income earned from fees charged for managing customers' funds invested in earlier years.

2000 compared with 1999

The contribution of Lloyds TSB Group's life, pensions and unit trusts businesses in 2000 was £438 million higher at £798 million, compared to £360 million in 1999; these results were significantly affected by Lloyds TSB Group's acquisition of Scottish Widows, which was effective 3 March 2000.

In 2000, new business profits increased by £149 million due to the acquisition of Scottish Widows. Excluding the impact of Scottish Widows new business profits were down £15 million largely as a result of the sale of the new business capability of Abbey Life at the beginning of 2000; Abbey Life contributed £11 million of new business profits in 1999. New business profits of the existing Lloyds TSB bancassurance business were £4 million lower at £133 million. Weighted sales through the branch network were little changed from 1999, as considerable time was spent training sales staff on the newly introduced Scottish Widows product line.

Regular premium sales in 2000 increased by £27.5 million largely reflecting two factors. The acquisition of Scottish Widows resulted in an increase of £89.0 million which more than offset the effect of a decrease in sales of £51.8 million caused by the sale of the new business capability of Abbey Life at the beginning of 2000. Sales in the Lloyds TSB bancassurance business were down £9.7 million at £64.6 million principally as a result of the withdrawal of the endowment mortgage product.

Single premium sales rose £1,579.4 million in 2000, with Scottish Widows contributing £1,572.8 million which more than offset a reduction in sales of £264.4 million at Abbey Life following the sale of the new business capability. Sales in the Lloyds TSB bancassurance single premium business grew following the introduction of the new with-profits bond.

Profits from existing business were £250 million higher at £466 million in 2000, and Scottish Widows contributed £152 million of this increase. Excluding the impact of Scottish Widows, existing business profits were up £98 million. Existing business profits at Abbey Life were little changed from 1999 but those in the Lloyds TSB bancassurance business rose by £72 million as a result of the growth in the size of the business and following changes in the underlying actuarial assumptions, and some tax related adjustments.

Investment earnings in 2000, before taking into account short-term fluctuations in investment returns (see "—Short-term fluctuations in investment returns"), increased by £174 million, although excluding Scottish Widows the increase was £17 million. Investment earnings in the Lloyds TSB bancassurance business were £1 million higher than in 1999, and those at Abbey Life rose £16 million reflecting the benefit of the additional funds retained to match annuity liabilities and the higher surplus released following the cessation of new business.

Life and pensions distribution costs in 2000 were £126 million higher at £225 million, although excluding Scottish Widows the increase was £19 million, reflecting the increased cost of branch network sales.

Unit trust profits were down £9 million at £48 million; down £16 million excluding Scottish Widows. Profits at Abbey Life were unchanged from 1999, but those in the Lloyds TSB bancassurance business were down £16 million reflecting a 7 per cent reduction in weighted sales and the increased costs of branch network sales.

Excluding the impact of the acquisition of Scottish Widows, unit trust sales fell by £276.5 million. Sales in the Lloyds TSB bancassurance business fell as a result of the focus of customers' interest on the new with-profits bond product and the fact that sales in 1999 had been high due to the impact of changes to government tax legislation which withdrew Personal Equity Plans (PEPs) and introduced ISAs with effect from 6 April 1999. These are both tax efficient savings schemes however the maximum unit trust investment was reduced from £9,000 to £7,000. The impact of these tax changes resulted in an increase in unit trust sales in 1999, prior to the reduction in the investment limits.

General Insurance

The following table shows premium income from underwriting and commission income from insurance broking.

	2001 £m	2000 £m	1999 £m
Premium income from underwriting			
Creditor	**110**	126	136
Home	**281**	228	203
Health	**45**	50	55
Other	**-**	-	1
Reinsurance premiums	**(8)**	(5)	(5)
	428	399	390
Commissions from insurance broking			
Creditor	**323**	225	175
Home	**41**	34	35
Health	**22**	19	21
Other	**142**	120	96
	528	398	327
Contribution	**668**	587	461
Unusual items:			
Short-term fluctuations in investment returns	**(46)**	(27)	22
Profit before tax	**622**	560	483

2001 compared with 2000

The contribution, calculated as explained under "- Line of business information – Summary", from general insurance operations, comprising both underwriting and broking activities, rose by £81 million, or 14 per cent, to £668 million in 2001.

The contribution from the underwriting business fell in 2001 by £6 million to £224 million. Premium income increased by £29 million, or 7 per cent, due to a £53 million increase in premium income from home insurance partly due to the successful cross-selling of this product by Cheltenham & Gloucester to its mortgage customers. This more than offset a decline of £16 million in income from creditor insurance caused by the transfer of the card protection book to Norwich Union in the second half of 2000. Premiums from health insurance fell by £5 million and reinsurance premiums increased by £3 million.

General insurance claims increased by £32 million or 23 per cent to £174 million. The claims ratio was 39.9 per cent compared to 35.1 per cent in 2000, reflecting higher property claims.

The contribution from the broking business increased by £87 million or 24 per cent to £444 million due to an increase in commission income of £130 million. Creditor insurance sales increased by £98 million as a result of the growth in Lloyds TSB Group's personal lending and credit card portfolios and the success of the branch network selling related income protection products. In addition, there was a £22 million increase in other commissions as a benefit of £30 million resulting from a one-off change in broking arrangements more than offset a fall in the level of retrospective commissions. There was a fall in investment earnings reflecting the lower interest rate environment and costs increased by £28 million to support the higher business volumes.

2000 compared with 1999

The contribution from general insurance operations, comprising underwriting and broking, rose by £126 million, or 27 per cent, to £587 million in 2000.

The contribution from the underwriting business in 2000 increased by £55 million to £230 million. Premium income increased by £9 million, or 2 per cent, as a £25 million growth in income from home insurance policies more than offset a £10 million fall in creditor protection premiums as a result of the transfer of the card protection book to Norwich Union in the second half of 2000. Sales of home insurance policies increased by 10 per cent, with strong growth in both branch network and direct sales. Overall new business sales in 2000 were over 2.4 million, 14 per cent higher than in 1999, of which over 900,000 were home insurance policies.

Investment income in 2000, before taking into account short-term fluctuations in investment returns (see "Short-term fluctuations in investment returns"), increased by £12 million reflecting the growth in the size of the portfolio and expenses were largely unchanged. General insurance claims were £27 million lower benefiting from lower levels of unemployment, resulting in a lower level of claims on loan protection policies, and a reduction in general household perils, particularly theft. The overall claims ratio, calculated as being claims as a proportion of premium income, before reinsurance, was 35.1 per cent compared to 42.8 per cent in 1999.

The contribution from the broking business increased by £71 million to £357 million. Broking commission income increased by £71 million. There was a £19 million increase in card protection income following the transfer of the book to Norwich Union. Card protection insurance is a product which insures the repayment of an outstanding balance on the insured credit card where payments are unable to be met due to sickness, death or unemployment. The underwriting margins on card protection business are small and as a result, in the first half of 2000, Lloyds TSB Group took the decision that in future it would only act as broker and no longer underwrite this business. Responsibility for managing the in-force portfolio was transferred to Norwich Union, a major UK provider of similar protection products. All premiums earned and claims recognised up until the date of transfer were accounted for by Lloyds TSB Group; following the transfer all premiums and claims were accounted for by Norwich Union. No profit or loss was recognised in Lloyds TSB Group's accounts as a result of this transfer. Loan protection income increased by £18 million reflecting increased sales volumes and retrospective commissions which are based on the performance of the policies sold grew by £23 million. Operating expenses were largely unchanged.

Wholesale Markets and International Banking

Lloyds TSB Group's Wholesale Markets and International Banking business comprises banking, treasury, large value lease finance, long-term agricultural finance, share registration, venture capital, factoring and invoice discounting, and other related services for major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses, and other forms of asset finance. It also includes banking and financial services overseas in four main areas (the Americas, New Zealand, Europe, and Offshore Banking) and emerging markets debt.

	2001	2000	1999
	£m	£m	£m
Net interest income	**1,858**	1,653	1,664
Other income	**1,325**	1,065	884
Total income	**3,183**	2,718	2,548
Operating expenses	**(1,410)**	(1,254)	(1,144)
Trading surplus	**1,773**	1,464	1,404
Provisions for bad and doubtful debts	**(332)**	(209)	(190)
Amounts written off fixed asset investments	**(60)**	(32)	(7)
Contribution	**1,381**	1,223	1,207
Unusual items:			
Exceptional restructuring costs	**(17)**	(30)	-
Profit before tax	**1,364**	1,193	1,207
Efficiency ratio	**44.3%**	46.1%	44.9%
Total assets (period-end)	**£101,471m**	£86,030m	£81,922m
Total risk-weighted assets (period-end)	**£59,307m**	£48,858m	£43,522m

2001 compared with 2000

The contribution, calculated as explained under "- Line of business information – Summary", from Wholesale Markets and International Banking in 2001 increased by £158 million, or 13 per cent, to £1,381 million from £1,223 million in 2000. In 2001, the contribution from Chartered Trust was £19 million compared to £1 million during the four months of ownership in 2000.

Total income increased by £465 million, or 17 per cent, from £2,718 million to £3,183 million. Net interest income increased by £205 million to £1,858 million; the inclusion of Chartered Trust for a full year accounted for £85 million of this increase, after funding costs, giving an underlying growth of £120 million, or 7 per cent. This increase resulted primarily from positive interest rate management and asset growth.

Period end assets increased by £15,441 million, or 18 per cent, to £101,471 million. Of this increase, over £9,000 million resulted from a growth in debt securities reflecting an increase in Lloyds TSB Group's asset backed and other investment grade securities, many of which were triple A rated. A high percentage of these assets, which are very liquid and marketable, have low capital weightings and represent a profitable deployment of Lloyds TSB Group's capital at a time when margins in this area are improving. Period end lending to corporate and commercial customers increased by some £3,900 million as a result of a significant growth in term and money market lending and short-term lending to specialist investment funds and UK and US insurance companies. Within International Banking, period end assets grew by £2,427 million primarily as a result of corporate and consumer lending growth in New Zealand and Brazil.

The net interest margin was little changed. The benefits of positive interest rate management in the treasury operations in the UK and improved margins in New Zealand more than offset lower margins earned on corporate and commercial lending balances due to competitive pressures and reductions in the margin in Brazil. Adverse exchange rate movements, mainly in Brazil, reduced net interest income by £59 million.

Other income increased by £260 million; the inclusion of Chartered Trust for a full year accounted for £126 million of this increase giving an underlying growth of £134 million, or 13 per cent. There was a £54 million increase in operating lease rentals from Lloyds UDT and Lloyds TSB Leasing as a result of growth in the portfolio and a £26 million increase in fees from large corporate activity, factoring and following the completion of a number of high quality structured finance transactions. Income from share registration activities increased by £12 million and dealing profits from the treasury operations improved, benefiting from opportunities created from certain exposures arising within Lloyds TSB Group's insurance businesses.

Overseas, other income increased by £19 million as increased profits from the sale of emerging market investments of £51 million and an increase in fee income in New Zealand of £10 million were partly offset by adverse exchange rate movements of £24 million and a reduction of £19 million in fee income from Lloyds TSB Group's overseas wealth management businesses, reflecting lower stock market values.

Operating expenses increased by £156 million; the inclusion of Chartered Trust for a full year added £166 million of costs giving an underlying reduction of £10 million. Operating lease depreciation within Lloyds UDT and Lloyds TSB Leasing increased by £13 million, despite a £23 million reduction in the depreciation charge on certain ship leases. Overseas operating expenses reduced by £26 million; increased operating costs in New Zealand of £13 million and Brazil of £12 million, to support higher business volumes, were more than offset by a £46 million benefit from exchange rate movements.

Provisions for bad and doubtful debts increased by £123 million; the inclusion of Chartered Trust for a full year resulted in an increase of £27 million giving an underlying growth of £96 million. The growth in the charge was mainly attributable to a £55 million increase in the general provision following the recent economic difficulties in Argentina. At 31 December 2001, Lloyds TSB Group's total exposure to Argentina was some £715 million. Lloyds TSB Group's local balance sheet in Argentina had assets totalling £465 million, approximately two-thirds of these were dollar denominated. Some two-thirds of the local balance sheet relates to retail and business customer lending and mortgages, with cash and liquidity, and lending to banks representing the majority of the remainder. In addition, Lloyds TSB Group has offshore loans of some £150 million to subsidiaries of major multinational companies with Argentine operations, and some £100 million of Argentine Government bonds held centrally.

The charge for provisions for bad and doubtful debts relating to the corporate and commercial lending portfolios increased by £53 million largely as a result of new provisions required against a small number of corporate exposures whilst other provisions overseas increased by £7 million. There was an £18 million reduction in the charge against the consumer finance portfolio of Lloyds UDT due to improved credit control procedures.

Amounts written off fixed asset investments increased by £28 million following a provision of £45 million against the carrying value of Argentine Government debt. In 2000, a provision of £18 million was required against part of the emerging market investment portfolio.

2000 compared with 1999

The contribution from Wholesale Markets and International Banking in 2000 increased by £16 million, or 1 per cent, to £1,223 million from £1,207 million in 1999.

Total income increased by £170 million, or 7 per cent, to £2,718 million. Net interest income fell by £11 million to £1,653 million; the acquisition of Chartered Trust resulted in an additional £31 million of income, after funding costs, and therefore the underlying decrease was £42 million, or 3 per cent. Within the UK, net interest income from Lloyds TSB Group's Treasury operations fell by £31 million; the results in 1999 benefited from sterling and US dollar interest rate reductions whilst in 2000 a more stable interest rate environment and higher short dated funding costs resulted in a 16 basis point reduction in the margin. In Lloyds TSB Group's asset finance business lower new business volumes and significant margin erosion resulted in a £57 million fall in net interest income. However, in the Corporate and Commercial businesses higher volumes of both lending and deposits combined to produce a £30 million increase in net interest income.

Overseas, a 15 per cent increase in lending volumes by Lloyds TSB Group's consumer finance business in Brazil and a change in product mix resulting in an improvement in the net interest margin, led to a £27 million increase in net interest income. Net interest income grew by £13 million in New Zealand in local currency terms, largely due to a change in business mix resulting in an improvement in the margin, and by £17 million in the European and offshore banking operations. However, these factors were largely offset by adverse exchange rate movements of £15 million, principally in New Zealand, and lower income from Lloyds TSB Group's other activities in Brazil as volumes and margins have contracted resulting in a £16 million fall in revenues.

Other income increased by £181 million; the acquisition of Chartered Trust resulted in the inclusion of an additional £53 million and therefore the underlying increase was £128 million, or 14 per cent. Venture capital gains were £21 million higher and increased volumes of operating leases resulted in a £36 million increase in rental income. Fee income from large corporate activity in the UK and overseas increased by £15 million as a result of higher transaction volumes and there was a £9 million increase in factoring income. Within Lloyds TSB Group's Treasury operations, dealing profits increased by £20 million largely as a result of increased levels of activity but also reflecting more favourable market conditions for foreign exchange operations following the introduction of the euro at the beginning of 1999. There was also a £15 million reduction in fees paid by Lloyds UDT because of lower transaction volumes. Fee income from Lloyds TSB Group's offshore and European private banking operations increased by £24 million, mainly due to higher transaction volumes in the strong equity markets, however this was offset by reductions in the Latin American operations, reflecting more competitive market conditions in Brazil and the contraction of the businesses in Argentina and Colombia.

Operating expenses increased by £110 million; the acquisition of Chartered Trust added £71 million and therefore the underlying increase was £39 million, or 3 per cent. In the UK, higher volumes of operating lease assets resulted in a £21 million increase in the depreciation charge and there was also a £10 million investment in a number of e-commerce initiatives. Overseas, costs were £12 million higher in the European and offshore banking operations as transaction volumes increased and £7 million higher in Brazil, mainly as a result of increased staff, data processing and telecommunications costs. However, costs in New Zealand were £14 million lower benefiting from the continuing synergies arising from the integration of Countrywide Banking Corporation.

The charge for provisions for bad and doubtful debts increased by £19 million; provisions made by Chartered Trust post-acquisition added £12 million and therefore the underlying increase was £7 million, or 4 per cent. Provisions were £14 million lower in Colombia as the economy started to recover from the recessionary conditions of the previous year and there were increased recoveries of £14 million from the provisions held against the emerging markets medium-term debt portfolio. However, the charge in Argentina increased by £25 million with the continuing effects of the recession impacting the level of both retail and corporate provisions and in the UK there was a £4 million increase in the provisions held against corporate and commercial exposures.

Amounts written off fixed asset investments increased to £32 million from £7 million as Lloyds TSB Group has expanded its venture capital investment portfolio in the UK and a provision of £18 million was required against part of the emerging market investment portfolio.

Central group items

Included within Central group items are the costs of Lloyds TSB Group support functions, the accrual for the annual payment to Lloyds TSB Foundations, the net earnings on that part of Lloyds TSB Group's capital base which is not required to support the operations of the business units and other items of income and expenditure managed centrally.

	2001	2000	1999
	£m	£m	£m
Accrual for payment to Lloyds TSB Foundations	**(36)**	(34)	(31)
Earnings on excess capital, central costs and other unallocated items	**(72)**	(84)	150
Contribution	**(108)**	(118)	119
Unusual items:			
Abbey National offer costs	**(16)**	-	-
Profit(loss) on sale and closure of businesses	**39**	-	(126)
Loss before tax	**(85)**	(118)	(7)

2001 compared with 2000

The four independent Lloyds TSB Foundations support registered charities throughout the UK that enable people, particularly disabled and disadvantaged people, to play a fuller role in society. The Foundations receive one per cent of Lloyds TSB Group's pre-tax profit averaged over three years instead of the dividend on their shareholdings. The increased charge is a reflection of the continued growth in the average profitability of Lloyds TSB Group. See Note 40 to the Consolidated Financial Statements.

Earnings on surplus capital, central costs and other unallocated items, was £12 million better than in 2000. A full year's funding cost of the consideration for the acquisition of Scottish Widows, compared to ten months in 2000, was offset by the gradual build-up of surplus capital and some £30 million of benefits to Lloyds TSB Group capital from changes in interest rate hedging arrangements.

2000 compared with 1999

The increased accrual for the payment to Lloyds TSB Foundations in 2000 is a reflection of the growth in Lloyds TSB Group's profit before tax. The significant fall in the level of earnings on excess capital, central costs and other unallocated items in 2000 reflects the incorporation, for the first time, of the funding cost of the purchase of Scottish Widows. At the end of 2000 Lloyds TSB Group had little excess capital.

Unusual items

In this section of the Operating and Financial Review and Prospects, Lloyds TSB Group discusses in detail certain items that had a significant impact on Lloyds TSB Group's results and which either are not expected to recur or which are unusual in nature, thereby hindering management's analysis of trends. In 2001 these unusual items were:

- short-term fluctuations in investment returns;
- exceptional restructuring costs;
- Abbey National offer costs;
- the provision for redress to past purchasers of pension policies; and
- profit arising on sale of business.

In 2000, changes in the economic assumptions applied to the long-term assurance business and a charge relating to stakeholder pensions were also significant items.

	2001	2000	1999
	£m	£m	£m
Short-term fluctuations in investment returns	**(648)**	(94)	58
Changes in economic assumptions	**-**	127	-
Exceptional restructuring costs	**(217)**	(188)	-
Abbey National offer costs	**(16)**	-	-
Provisions for redress to past purchasers of pension policies	**(70)**	(100)	(102)
Stakeholder pension related charge	**-**	(80)	-
Profit(loss) on sale and closure of businesses	**39**	-	(126)

Short-term fluctuations in investment returns

In accordance with generally accepted accounting practice in the UK, it is Lloyds TSB Group's accounting policy to carry the investments backing the reserves held by its life companies at market value. These investments are substantial and changes in the market value result in significant volatility of Lloyds TSB Group's embedded value earnings. In order to facilitate management's analysis of the underlying performance of the life and pensions business the short-term fluctuations in investment returns have been separately identified by comparing actual investment performance with results calculated using longer-term rates of return. The longer-term rates of return are consistent with those used by Lloyds TSB Group in the calculation of embedded value at the beginning of the period. A similar approach has been adopted for Lloyds TSB Group's general insurance business. For more information concerning the longer-term rates of return used in Lloyds TSB Group's calculation of embedded value, see Note 29 to the Consolidated Financial Statements.

The acquisition of Scottish Widows in March 2000 resulted in a significant increase in the level of assets held by the life companies and as a consequence the short-term fluctuations in investment returns in 2001 and 2000 were much larger than in 1999. In 2001, there were negative short-term fluctuations in investment returns of £648 million reflecting in particular the poor performance of the UK stock market, where the FTSE 100 index of shares fell by more than 15 per cent.

Changes in economic assumptions

The shareholders' interest in the long-term assurance business is calculated using a series of economic assumptions, which are reviewed periodically and changed when necessary to ensure that they remain appropriate in the context of forecast long-term economic trends and changes in the nature of the business being entered into.

Following the acquisition of Scottish Widows in March 2000, the economic assumptions were reviewed to ensure that they remained appropriate for the enlarged life and pensions business. As a result of this review changes were made to the assumptions used by Abbey Life and the bancassurance business of Lloyds TSB in order to make the assumptions used by these businesses consistent with those used by Scottish Widows. The risk adjusted discount rate was reduced from 10.00 per cent to 8.50 per cent and the assumed gross return on equities was reduced from 8.50 per cent to 8.00 per cent leading to a credit of £127 million being recognised in the profit and loss account in 2000.

Exceptional restructuring costs

In February 2000, Lloyds TSB Group announced that after a detailed review, additional opportunities had been identified to reduce the overall cost base. A centralised team was established to co-ordinate the efficiency programme and ensure that the cost savings identified during the planning phase are realised. The principal features of the efficiency programme, which is focussed on non customer-facing activities are:

- the centralisation of computer operations;
- the further consolidation of all Lloyds TSB Group's large scale processing operations and support functions including the complete removal of all back office processing from branches;
- the further streamlining of the branch network, combined with the expansion of lower cost delivery channels such as telephone banking and internet operations;
- the further reduction of Lloyds TSB Group's purchasing costs; and
- the rationalisation of non-personal banking activities, through the progressive sharing and consolidation of operational functions.

In 2001, Lloyds TSB Group incurred restructuring costs of £167 million (2000: £108 million) in connection with the efficiency programme, principally comprising severance, software write-off and consultancy costs.

Following the acquisition of Scottish Widows in March 2000, Lloyds TSB Group has been integrating Scottish Widows businesses with its existing insurance and investments activities and rationalising the processes. During 2001, costs of £50 million (2000: £59 million) were incurred on this integration, principally relating to the integration and centralisation of back office support functions, the streamlining and automation of client service processes and the improvement to front office sales processes.

Following the acquisition of Chartered Trust in September 2000, a provision of £21 million was established to cover the cost of integrating Chartered Trust Group plc and ACL Autolease Holdings Limited with the Lloyds UDT Group, Lloyds TSB Group's existing consumer finance operations. As part of the integration the finance function and certain other back office activities are being relocated from Edinburgh to Cardiff and the vehicle administration function has been relocated from Harrogate to Birmingham. In addition, the contract hire operations have been rebranded as Lloyds TSB autolease, and the motor, caravan, motorcycle and personal lending operations have been rebranded as Black Horse Finance. It is anticipated that the integration will be completed in 2002.

Abbey National offer costs

Lloyds TSB Group incurred costs of £16 million in connection with the proposed acquisition of Abbey National prior to the announcement by the Secretary of State for Trade and Industry that Lloyds TSB Group would not be permitted to proceed with an offer.

Provisions for redress to past purchasers of pension policies

See "Business—Provisions for redress to past purchasers of pension policies".

Stakeholder pension related charge

During 1999, the UK government announced changes intended to encourage more of the population to provide retirement income for themselves through increased rates of private savings. One of these initiatives was the introduction of stakeholder pensions with effect from April 2001.

Stakeholder pensions are intended to provide a source of low cost retirement savings for individuals earning enough to be able to afford to make contributions towards a pension but not currently doing so. A key feature of these products is that charges are transparent and limited to 1 per cent per annum, which is significantly lower than historic charging rates on other personal pension products. In common with other pension providers in the UK, Scottish Widows introduced a stakeholder pension product in April 2001. In anticipation of this, in order not to disadvantage existing pensions customers, Lloyds TSB Group decided during 2000 to reduce charges made on certain existing policies. This had the effect of reducing the projected cash flows in Lloyds TSB Group's embedded value calculation, resulting in a charge of £80 million in the profit and loss account for the year ended 31 December 2000.

Profit(loss) on sale and closure of businesses

In October 2001, Lloyds TSB Group sold its Brazilian fund management and private banking business, including its subsidiary, Lloyds TSB Asset Management S.A. to Banco Itaú S.A. The net asset value of the business sold was less than

£2 million and assets under management were approximately US$2,000 million. The sale of this business did not affect Lloyds TSB Group's other Brazilian businesses. The profit before tax on the sale was £39 million.

In July 1999, Lloyds TSB Group announced its intention to withdraw from the global custody and unit trust trusteeship business. A provision of £28 million was made in the 1999 accounts for the expected operating losses to be incurred over the period that the business was to be run down and closed. In addition, in February 2000, Lloyds TSB Group sold the new business capability of Abbey Life for £100 million, of which £20 million was contingent upon the sales force achieving agreed sales targets over the two year period immediately following the sale. A provision of £98 million was made in the 1999 accounts for the expected loss on sale, including £80 million in respect of goodwill previously written off to reserves, and other asset write-offs.

Future accounting developments

UK

FRS 17—Retirement Benefits

FRS 17 was issued in December 2000 and becomes fully effective no later than for Lloyds TSB Group's 2003 Consolidated Financial Statements. The main requirement of FRS 17 is that it will be necessary to recognise on the balance sheet an asset or liability with respect to the surplus or deficit in Lloyds TSB Group's defined benefit schemes and to recognise immediately actuarial gains and losses in the statement of total recognised gains and losses. The FRS requires transitional disclosures in Lloyds TSB Group's 2001 and 2002 Consolidated Financial Statements, before becoming fully effective in 2003. See Note 43c to the Consolidated Financial Statements.

FRS 19—Deferred Tax

FRS 19 was issued in December 2000 and will be effective for Lloyds TSB Group's 2002 Consolidated Financial Statements. The FRS requires deferred tax to be provided on most types of timing differences. Currently, Lloyds TSB Group recognises deferred tax assets and liabilities only to the extent that it is considered probable that an asset or liability will crystallise. It is not expected that adoption will have a material effect on Lloyds TSB Group's financial statements.

UITF Abstract 33 – Obligations in capital instruments

Urgent Issues Task Force (UITF) Abstract 33 was issued in February 2002 and deals with the classification of various types of capital instruments in the balance sheet, whether as liabilities, shareholders' funds or, in Consolidated Financial Statements, minority interests. The Abstract is effective for periods ending on or after 23 March 2002 and, upon adoption, Lloyds TSB Group will reclassify those instruments affected from minority interests to subordinated debt. At 31 December 2001, the balance sheet amount was £451 million and the related expense, which will be reclassified from minority interests to interest payable, was £22 million.

US

SFAS No. 141—Business Combinations

SFAS No. 141 was issued in July 2001 and requires that the purchase method be used for all business combinations initiated after 30 June 2001. Use of the pooling-of-interests method is no longer permitted. Adoption has not had a material impact on Lloyds TSB Group's US GAAP financial statements.

SFAS No. 142—Goodwill and Other Intangible Assets

SFAS No. 142 was issued in July 2001 and became effective for Lloyds TSB Group on 1 January 2002. Certain provisions are applicable to transactions completed after 30 June 2001. The Statement requires that goodwill should no longer be amortised to earnings, but instead reviewed for impairment and that any losses arising from such a review be charged to income as they arise. Retrospective application is not permitted and certain disclosures will be provided until all reported periods reflect the change in accounting treatment. The impact on Lloyds TSB Group will be to increase US GAAP net income in the periods from 1 January 2002 by the amount of amortisation previously charged to net income on goodwill capitalised under US GAAP. For the year to 31 December 2001, this amounted to £248 million. No impairment of goodwill is anticipated.

SFAS No. 143 – Accounting for Asset Retirement Obligations

SFAS No. 143 was issued in June 2001 and requires the fair value of a liability for an asset retirement obligation to be recorded in the period in which it is incurred. When the liability is initially recorded, the cost is capitalised by increasing the carrying amount of the related long-lived asset. Over time, the liability is increased to its present value and the capitalised cost is depreciated over the useful life of the related asset. Upon settlement of the liability, the obligation is either settled for its recorded amount or a gain or loss is incurred upon settlement. SFAS No. 143 is effective for fiscal years beginning after 15 June 2002, with earlier application encouraged. Adoption is not expected to have a material impact on Lloyds TSB Group's US GAAP financial statements.

SFAS No. 144 – Accounting for the Impairment or Disposal of Long-Lived Assets

SFAS No. 144 was issued in August 2001 and became effective for Lloyds TSB Group from 1 January 2002. The Statement supersedes SFAS No. 121 'Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of' although it maintains many of its requirements. For long-lived assets to be held and used, an impairment is recognised only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows. For a long-lived asset to be disposed of by sale, the asset is measured at the lower of its carrying value or fair value (less costs to sell) and depreciation ceases. This Statement does not apply to goodwill, core deposit intangibles, deferred acquisition costs or deferred tax assets. Adoption is not expected to have a material impact on Lloyds TSB Group's US GAAP financial statements.

UK GAAP compared with US GAAP

Under US GAAP, Lloyds TSB Group's net income in 2001 was £1,524 million and £1,929 million in 2000 compared with £2,500 million in 2001 and £2,706 million in 2000 under UK GAAP. See Note 48 to the Consolidated Financial Statements.

There are a number of areas where differences between UK GAAP and US GAAP have a significant effect on the results of Lloyds TSB Group's operations. Firstly, under UK GAAP applicable to banking groups, life assurance activities are accounted for using the embedded value basis of accounting which requires the recognition of the discounted value of the projected future net cash flows attributable to the shareholder at the point of sale. UK GAAP therefore results in a substantial proportion of the net profit accruing on a portfolio of life assurance policies being recognised at their inception.

Embedded value accounting is not permitted under US GAAP. Under US GAAP income is recognised in the profit and loss account in the period in which it is earned and expenses in the period in which they are incurred. This results in a more even recognition of profit over the life of the related policies.

The second area concerns the treatment of business combinations and the related goodwill. When Lloyds Bank Plc and TSB Group plc combined in 1995 to form Lloyds TSB Group, the transaction was accounted for as a merger, as permitted under UK GAAP at that time, although legally TSB Group plc was deemed to have acquired Lloyds Bank Plc. Under US GAAP the transaction would have been accounted for as a reverse acquisition of TSB Group plc by Lloyds Bank Plc and the resulting goodwill capitalised and amortised through the profit and loss account.

Prior to 1998, in accordance with UK GAAP, goodwill arising on acquisitions by Lloyds TSB Group was written off directly against profit and loss account reserves. As permitted by the transitional provisions of FRS 10, this goodwill was not reinstated in the balance sheet when Lloyds TSB Group changed its accounting policy in 1998 to capitalise goodwill. The goodwill arising upon the acquisition of Scottish Widows in March 2000 was capitalised in the UK GAAP balance sheet in accordance with the requirements of FRS 10. However, in view of the strength of the Scottish Widows brand and the position of the business as one of the leading providers of life, pensions, unit trust and fund management products, the directors of Lloyds TSB Group concluded that the goodwill had an indefinite useful life. Consequently, this goodwill is not amortised, however it is subject to annual impairment reviews.

Under US GAAP all goodwill is capitalised and prior to the full implementation of SFAS No. 142 in 2002, it is amortised through the profit and loss account over periods of up to 40 years. In calculating the goodwill relating to the acquisition of an entity with retail deposit accounts, an asset representing the value of the depositor relationships, termed the core deposit intangible, is capitalised separately and amortised through the profit and loss account over the estimated average life of the retail customer relationships.

Finally, Lloyds TSB Group has elected not to satisfy the more onerous hedging criteria of SFAS No. 133 'Accounting for Derivative Instruments and for Hedging Activities' in respect of derivative contracts; therefore those derivatives that are held for risk management purposes, which are accounted for on an accruals basis under UK GAAP in line with the underlying instruments being hedged, are treated as trading under US GAAP, with the unrealised mark-to-market gains and losses taken to income as they arise and the resulting assets or liabilities recorded on the balance sheet. As Lloyds TSB Group will continue to hold a significant number of derivatives which are hedge accounted under UK GAAP the impact of SFAS No. 133 will mean that net income and shareholders' equity under US GAAP will be subject to increased volatility. In 2001, the effect of this was to reduce US GAAP net income by £315 million.

Average balance sheet and net interest income

The following average balance sheet excludes the long-term assurance business assets and liabilities attributable to policyholders. The interest yields and costs for foreign office assets and liabilities are affected by Lloyds TSB Group's operations in Latin America. The countries in which Lloyds TSB Group operates are periodically subject to comparatively high rates of interest, which in certain instances in the tables below, has had the effect of producing unusually high yields and costs.

	2001			2000			1999		
	Average balance £m	**Interest Income £m**	**Yield %**	Average balance £m	Interest income £m	Yield %	Average balance £m	Interest income £m	Yield %
Assets									
Treasury bills and other eligible bills									
Domestic offices	**1,858**	**91**	**4.90**	836	48	5.74	985	52	5.28
Foreign offices	**1,641**	**423**	**25.78**	1,224	265	21.65	1,000	122	12.20
Loans and advances to banks									
Domestic offices	**12,086**	**692**	**5.73**	13,384	828	6.19	13,606	758	5.57
Foreign offices	**2,308**	**153**	**6.63**	2,332	180	7.72	2,476	221	8.93
Loans and advances to customers									
Domestic offices	**89,802**	**6,876**	**7.66**	80,231	6,815	8.49	74,482	6,081	8.16
Foreign offices	**15,316**	**1,532**	**10.00**	14,009	1,393	9.94	13,387	1,780	13.30
Debt securities									
Domestic offices	**4,394**	**230**	**5.23**	3,882	252	6.49	3,272	200	6.11
Foreign offices	**4,397**	**300**	**6.82**	2,827	271	9.59	2,450	300	12.24
Lease and hire purchase receivables									
Domestic offices	**13,104**	**1,061**	**8.10**	12,241	984	8.04	11,897	924	7.77
Foreign offices	**39**	**6**	**15.38**	56	18	32.14	54	14	25.93
Total interest earning assets of banking book	**144,945**	**11,364**	**7.84**	131,022	11,054	8.44	123,609	10,452	8.46
Total interest earning assets of trading book	**12,252**	**544**	**4.44**	10,189	511	5.02	10,496	500	4.76
Total interest earning assets	**157,197**	**11,908**	**7.58**	141,211	11,565	8.19	134,105	10,952	8.17
Provisions for bad and doubtful debts	**(1,489)**			(1,531)			(1,456)		
Non-interest earning assets									
Domestic offices	**19,282**			16,769			13,140		
Foreign offices	**2,255**			2,121			2,463		
Total average assets and interest income	**177,245**	**11,908**	**6.72**	158,570	11,565	7.29	148,252	10,952	7.39
Percentage of assets applicable to foreign activities (in %)	**14.8**			14.4			15.2		

	2001			2000			1999		
	Average interest earning assets £m	**Net interest income £m**	**Net interest margin %**	Average interest earning assets £m	Net interest income £m	Net interest margin %	Average interest earning assets £m	Net interest income £m	Net interest margin %
Average interest earning assets and net interest income:									
Banking business	**144,945**	**4,944**	**3.41**	131,022	4,587	3.50	123,609	4,783	3.87
Trading business	**12,252**	**-**	**-**	10,189	-	-	10,496	4	0.04
Net yield on interest earning assets	**157,197**	**4,944**	**3.15**	141,211	4,587	3.25	134,105	4,787	3.57

	2001			2000			1999		
	Average balance £m	**Interest expense £m**	**Cost %**	Average balance £m	Interest expense £m	Cost %	Average balance £m	Interest expense £m	Cost %
Liabilities and shareholders' equity									
Deposits by banks									
Domestic offices	**13,452**	**658**	**4.89**	9,057	490	5.41	7,294	320	4.39
Foreign offices	**3,949**	**288**	**7.29**	3,506	247	7.05	3,482	305	8.76
Liabilities to banks under sale and repurchase agreements									
Domestic offices	**1,547**	**74**	**4.78**	2,022	113	5.59	2,544	134	5.27
Foreign offices	**671**	**110**	**16.39**	300	68	22.67	199	57	28.64
Customer accounts									
Domestic offices	**72,633**	**2,724**	**3.75**	72,071	3,232	4.48	67,047	2,534	3.78
Foreign offices	**10,877**	**924**	**8.49**	10,326	801	7.76	10,811	963	8.91
Liabilities to customers under sale and repurchase agreements									
Domestic offices	**1,552**	**73**	**4.70**	551	35	6.35	643	35	5.44
Foreign offices	**128**	**4**	**3.13**	127	4	3.15	128	4	3.13
Debt securities in issue									
Domestic offices	**12,716**	**713**	**5.61**	8,136	620	7.62	6,373	483	7.58
Foreign offices	**6,052**	**359**	**5.93**	4,707	366	7.78	3,327	472	14.19
Subordinated liabilities									
Domestic offices	**9,022**	**484**	**5.36**	7,383	481	6.51	5,614	355	6.32
Foreign offices	**158**	**9**	**5.70**	162	10	6.17	169	7	4.14
Total interest-bearing liabilities of banking book	**132,757**	**6,420**	**4.84**	118,348	6,467	5.46	107,631	5,669	5.27
Total interest-bearing liabilities of trading book	**12,252**	**544**	**4.44**	10,189	511	5.02	10,496	496	4.73
Total interest-bearing liabilities	**145,009**	**6,964**	**4.80**	128,537	6,978	5.43	118,127	6,165	5.22
Interest-free liabilities									
Minority interests and shareholders' funds									
Domestic offices	**9,265**			8,202			6,718		
Foreign offices	**2,225**			1,930			1,778		
Non-interest bearing customer accounts									
Domestic offices	**6,182**			6,058			6,134		
Foreign offices	**595**			635			578		
Other interest-free liabilities									
Domestic offices	**13,005**			12,723			13,964		
Foreign offices	**964**			485			953		
Total liabilities	**177,245**	**6,964**	**3.93**	158,570	6,978	4.40	148,252	6,165	4.16
Percentage of liabilities applicable to foreign activities (in %)	**14.5**			14.1			14.9		

Net interest margin for the banking book

	2001	2000	1999
	%	%	%
Domestic offices	**3.48**	3.58	3.98
Foreign offices	**3.04**	3.09	3.25
Group margin	**3.41**	3.50	3.87

Loans and advances to banks and customers include non-performing loans. Interest receivable on such loans has been included to the extent to which either cash payments have been received or interest has been accrued in accordance with Lloyds TSB Group's policy on income recognition.

Approximately 85 per cent of the value of the balances are calculated on a daily basis with balances held by Lloyds TSB Group's leasing and asset finance businesses averaged on a monthly basis. Management believes that the interest rate trends are substantially the same as they would be if all balances were averaged on the same basis.

Changes in net interest income - volume and rate analysis

The following table allocates changes in net interest income between volume and rate for 2001 compared with 2000 and for 2000 compared with 1999. Where variances have arisen from both changes in volume and rate these are allocated to volume.

	2001 compared with 2000 Increase/(decrease)			2000 compared with 1999 Increase/(decrease)		
	Total change £m	**Volume £m**	**Rate £m**	Total change £m	Volume £m	Rate £m
Interest receivable and similar income						
Treasury bills and other eligible bills						
Domestic offices	**43**	**50**	**(7)**	(4)	(9)	5
Foreign offices	**158**	**107**	**51**	143	48	95
Loans and advances to banks						
Domestic offices	**(136)**	**(74)**	**(62)**	70	(14)	84
Foreign offices	**(27)**	**(2)**	**(25)**	(41)	(11)	(30)
Loans and advances to customers						
Domestic offices	**61**	**733**	**(672)**	734	488	246
Foreign offices	**139**	**131**	**8**	(387)	62	(449)
Debt securities						
Domestic offices	**(22)**	**27**	**(49)**	52	40	12
Foreign offices	**29**	**107**	**(78)**	(29)	36	(65)
Lease and hire purchase receivables						
Domestic offices	**77**	**70**	**7**	60	28	32
Foreign offices	**(12)**	**(3)**	**(9)**	4	1	3
Total banking book interest receivable and similar income	**310**	**1,146**	**(836)**	602	669	(67)
Total trading book interest receivable and similar income	**33**	**92**	**(59)**	11	(15)	26
Total interest receivable and similar income	**343**	**1,238**	**(895)**	613	654	(41)
Interest payable						
Deposits by banks						
Domestic offices	**168**	**215**	**(47)**	170	95	75
Foreign offices	**41**	**32**	**9**	(58)	2	(60)
Liabilities to banks under sale and repurchase agreements						
Domestic offices	**(39)**	**(23)**	**(16)**	(21)	(29)	8
Foreign offices	**42**	**61**	**(19)**	11	23	(12)
Customer accounts						
Domestic offices	**(508)**	**21**	**(529)**	698	225	473
Foreign offices	**123**	**47**	**76**	(162)	(38)	(124)
Liabilities to customers under sale and repurchase agreements						
Domestic offices	**38**	**47**	**(9)**	-	(6)	6
Foreign offices	**-**	**-**	**-**	-	-	-
Debt securities in issue						
Domestic offices	**93**	**257**	**(164)**	137	134	3
Foreign offices	**(7)**	**80**	**(87)**	(106)	107	(213)
Subordinated liabilities						
Domestic offices	**3**	**88**	**(85)**	126	115	11
Foreign offices	**(1)**	**-**	**(1)**	3	-	3
Total banking book interest payable	**(47)**	**825**	**(872)**	798	628	170
Total trading book interest payable	**33**	**39**	**(6)**	15	(15)	30
Total interest payable	**(14)**	**864**	**(878)**	813	613	200

Risk management

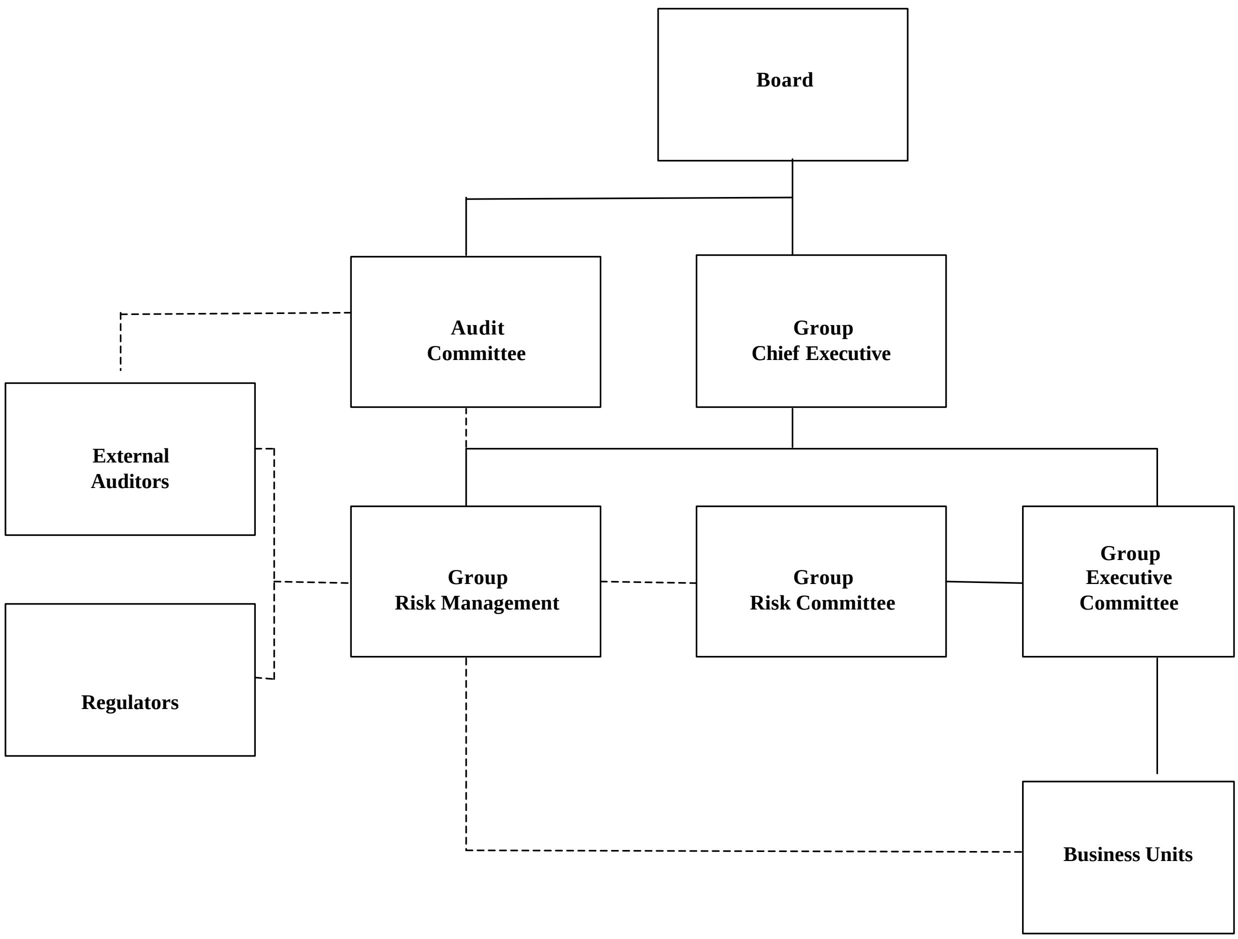
Management of risk

The board is responsible for determining the long-term strategy of the business, the markets in which Lloyds TSB Group will operate and the level of risk acceptable to Lloyds TSB Group in each area of its business.

The Group Risk Committee, established during 2001, is responsible to the Group Executive Committee for the protection of shareholder value through the assessment and control of the high level risks assumed by Lloyds TSB Group, and for ensuring that the requisite culture, practices and systems are in place across the Group to meet internal and external obligations. The Group Risk Committee also reviews the allocation and deployment of capital at risk, taking into account Lloyds TSB Group's risk appetite.

Responsibility for the implementation of risk policy and for ensuring that there is an effective top level control framework is delegated to the Director of Group Risk Management, who reports to the Group Chief Executive and has access to the Chairman and members of senior management. The Audit Committee and the Board in turn receive regular reports on risk issues prepared by Group Risk Management. The Director of Group Risk Management is also responsible for the provision of independent oversight of management actions which impact upon the risk profile of the Lloyds TSB Group.

This risk governance structure is illustrated in the following organogram:



The Director of Group Risk Management implements the policies established by the Board through four principal departments: Group Risk, Group Audit, Group Compliance and Sanctioning & Sovereign Risk. Group Risk's responsibilities include credit risk, market risk, operational risk, insurance risk and environmental risk; the department also sets risk policy, develops risk methodology and undertakes risk evaluation and reporting. Group Risk Management is also responsible for leading the work to assess the impact of the draft proposals for the introduction of the new Basel Capital Accord and to prepare Lloyds TSB Group for its implementation 1 January 2005, at the earliest.

At an operating level, Lloyds TSB Group promotes sound internal risk management practices through the directors of its separate business units, who have primary responsibility for measuring, monitoring and controlling the range of portfolio and operating risk within their specific area of accountability. The directors and management of the business units, as the primary risk managers, are responsible for establishing proper control frameworks within their businesses to ensure that Lloyds TSB

Group's activities are conducted effectively but prudently, and within the parameters defined by Group Risk Management. They are responsible for ensuring that the risks within their business are identified, assessed, controlled and monitored, and that the controls and procedures implemented comply with Lloyds TSB Group policies and standards, which are extensively documented in rule books and procedures manuals.

Credit risk

Credit risk arises from extending credit in all forms in Lloyds TSB Group's banking and trading activities, where there is a possibility that a counterparty may default. Lloyds TSB Group has standards, policies and procedures to control and monitor all such risks.

The Director of Group Risk Management heads Group Risk and reports to the Group Chief Executive. Group Risk's responsibilities in respect of credit risk include the following:

- Formulation of high-level credit policies designed to ensure a balanced and managed approach to the identification and mitigation of credit risk. These policies provide a standard framework within which Lloyds TSB Group businesses structure their individual policies and rules. Group Risk reviews, approves and monitors credit policy documents established for individual Lloyds TSB Group businesses.

- Provision of lending guidelines. These define the responsibilities for lending officers and provide a disciplined and focussed benchmark for sound credit decisions. Clear guidance is provided on Lloyds TSB Group's attitude towards and appetite for credit exposure on different market sectors, industries and products.

- Provision of a Lloyds TSB Group rating system. All business units are required to operate an authorised rating system that complies with Lloyds TSB Group's standard methodology. Lloyds TSB Group uses a 'Master Scale' rating structure with nine ratings, each corresponding to a probability of future default.

- Establishment and maintenance of Lloyds TSB Group's large exposures policy. Exposure to individual counterparties or groups of counterparties is controlled through a tiered hierarchy of delegated sanctioning authorities. Approval requirements for each decision are based on the transaction amount, the customer's aggregate facilities, credit risk ratings and the nature of the risk. Regular reports on significant credit exposures are provided to the Group Executive Committee and Board.

- Control of bank exposures. In-house proprietary rating systems are used to approve bank facilities on a Lloyds TSB Group basis.

- Monitoring of scorecards. Lloyds TSB Group utilises statistically-based decisioning techniques (primarily credit scoring and performance scoring) for its main consumer lending portfolios. Authorisations are determined by scorecards tailored to meet the needs of the particular business. Group Risk reviews and monitors new and material changes to existing scorecards.

- Control of cross-border exposures. Country limits are authorised and managed by a dedicated unit, using an in-house rating system which takes into account economic and political factors.

- Maintenance of a centralised facilities database. Group Risk operates a centralised database of large corporate, sovereign and bank facilities designed to ensure a consistent aggregation policy is maintained throughout Lloyds TSB Group.

- Formulation of concentration limits on certain industries and sectors. Group Risk sets limits and monitors exposures to prevent over-concentration of risk.

- Monitoring and controlling residual value risk exposure. Lloyds TSB Group's appetite for such exposure is communicated to the business by a series of time referenced sector caps, designed to ensure an acceptable distribution of future risk. Methods of mitigating downside risk include obtaining manufacturer's guarantees and deficiency value insurance. For the element of downside risk not covered by such instruments the need for provisions is regularly reviewed. Appropriate industry-specific information sources are used to assess future values and monitor the risk.

- Portfolio analysis. In conjunction with Group Risk, Lloyds TSB Group businesses identify and define portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed in terms of credit risk exposure. This entails the production and analysis of regular portfolio monitoring reports for review by Group Risk.

- Communication and provision of general guidance on all credit-related risk issues, including regulatory changes and environmental risk policy, to promote consistent and best practice throughout Lloyds TSB Group.

Day-to-day credit management and asset quality within each business unit is the primary responsibility of the business unit directors. Each business unit has established credit processes in place involving credit policies, procedures and lending guidelines. Authority to delegate lending discretions within operating divisions rests with officers holding divisional lending delegated authority. All senior management authorities are advised to Group Risk.

Specialist units are established within Lloyds TSB Group business units to provide intensive management and control in order to maximise recoveries of doubtful debts.

Regular independent audits of credit processes are undertaken by Group Audit. Such audits include consideration of the completeness and adequacy of credit manuals and lending guidelines, together with an in-depth analysis of a representative sample of accounts in the portfolio to assess the quality of the loan book and other exposures. Individual accounts are reviewed to ensure that the facility grade is appropriate, that credit procedures have been properly followed and that where an account is non-performing, provisions raised are adequate.

Credit risk also arises from the use of derivatives. Note 45 to the Consolidated Financial Statements shows the total notional principal amount of interest rate and exchange rate contracts outstanding at 31 December 2001. The notional principal amount does not, however, represent the Group's real exposure to credit risk, which is limited to the current cost of replacing contracts with a positive value to the Group, should the counterparty default. This replacement cost is also shown in Note 45.

To reduce credit risk the Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure.

Credit derivatives are a method of transferring credit risk from one counterparty to another and of increasing exposure to selected counterparties. Credit derivatives include credit swaps, credit spread options and credit linked notes. Lloyds TSB Group makes limited use of such instruments.

Loan portfolio

Analysis of loans and advances to customers and banks

The following table analyses loans to banks and customers by geographical area and type of loan at 31 December for each of the five years listed.

	2001	2000	1999	1998	1997
	£m	£m	£m	£m	£m
Domestic:					
Loans and advances to banks	**12,737**	13,165	14,341	15,905	18,650
Loans and advances to customers:					
Mortgages	**56,578**	52,659	47,451	44,660	41,785
Other personal lending	**12,784**	11,138	10,092	9,570	8,735
Agriculture, forestry and fishing	**2,074**	2,026	2,183	2,052	2,009
Manufacturing	**3,321**	3,357	3,262	2,987	2,973
Construction	**1,309**	1,016	754	671	749
Transport, distribution and hotels	**4,440**	3,836	3,540	3,308	3,838
Financial, business and other services	**8,736**	9,295	6,614	5,029	5,952
Property companies	**2,907**	2,470	2,303	2,304	2,297
Lease financing	**7,552**	8,070	8,369	8,165	5,527
Hire purchase	**5,345**	5,172	3,674	3,701	3,523
Other	**2,992**	2,526	2,127	1,921	1,560
Total domestic loans	**120,775**	114,730	104,710	100,273	97,598
Foreign:					
Loans and advances to banks	**2,489**	2,131	2,628	2,606	2,056
Loans and advances to customers:					
Mortgages	**3,467**	3,490	3,558	3,187	2,028
Other personal lending	**1,672**	1,602	1,784	1,832	1,636
Agriculture, forestry and fishing	**1,708**	1,528	1,606	1,703	1,906
Manufacturing	**2,004**	1,730	945	976	1,047
Construction	**304**	190	158	155	171
Transport, distribution and hotels	**2,570**	2,166	1,638	1,082	1,081
Financial, business and other services	**2,631**	2,174	2,553	2,542	1,978
Property companies	**896**	637	470	428	360
Lease financing	**33**	53	79	136	56
Hire purchase	**-**	-	-	19	7
Other	**1,148**	807	581	374	380
Total foreign loans	**18,922**	16,508	16,000	15,040	12,706
Total loans	**139,697**	131,238	120,710	115,313	110,304
Less provision for loan losses	**(1,468)**	(1,426)	(1,414)	(1,462)	(1,771)
Less interest held in suspense	**(70)**	(90)	(100)	(145)	(243)
Total loans and advances net of provisions and interest held in suspense	**138,159**	129,722	119,196	113,706	108,290

	2001	2000	1999	1998	1997
	£m	£m	£m	£m	£m
Analysis of foreign loans by region:					
Loans and advances to customers:					
New Zealand	**8,435**	7,368	7,659	7,310	5,430
Latin America	**2,347**	2,222	1,761	2,120	2,437
Rest of the world	**5,651**	4,787	3,952	3,004	2,783
	16,433	14,377	13,372	12,434	10,650
Loans and advances to banks:					
New Zealand	**534**	357	467	375	283
Latin America	**209**	105	190	148	116
Rest of the world	**1,746**	1,669	1,971	2,083	1,657
	2,489	2,131	2,628	2,606	2,056
Total foreign loans	**18,922**	16,508	16,000	15,040	12,706

The classification of lending as domestic or foreign is based on the location of the office recording the transaction, except for certain lending of the international business booked in London.

Summary of loan loss experience

The following table analyses the movements in the allowance for loan losses for each of the five years listed.

	2001 £m	2000 £m	1999 £m	1998 £m	1997 £m
Balance at beginning of period					
Domestic	**1,129**	1,134	1,126	1,252	1,444
Foreign	**297**	280	336	519	332
Total balance at beginning of period	**1,426**	1,414	1,462	1,771	1,776
Exchange and other adjustments	**(14)**	51	(49)	(30)	22
Advances written off:					
Domestic:					
Loans and advances to customers:					
Mortgages	**(23)**	(35)	(30)	(38)	(41)
Other personal lending	**(438)**	(399)	(364)	(279)	(232)
Agriculture, forestry and fishing	**(9)**	(12)	(14)	(9)	(18)
Manufacturing	**(18)**	(13)	(33)	(33)	(42)
Construction	**(8)**	(9)	(10)	(6)	(13)
Transport, distribution and hotels	**(34)**	(27)	(46)	(108)	(93)
Financial, business and other services	**(44)**	(28)	(40)	(34)	(49)
Property companies	**(21)**	(17)	(24)	(45)	(68)
Lease financing	**(11)**	(12)	(14)	(30)	(32)
Hire purchase	**(86)**	(69)	(29)	(5)	(14)
Other	**(9)**	-	(6)	-	(1)
Total domestic	**(701)**	(621)	(610)	(587)	(603)
Foreign	**(184)**	(124)	(134)	(372)	(60)
Total advances written off	**(885)**	(745)	(744)	(959)	(663)
Recoveries of advances written off:					
Domestic:					
Loans and advances to customers:					
Mortgages	**17**	12	11	9	11
Other personal lending	**80**	63	60	27	17
Agriculture, forestry and fishing	**4**	2	2	4	3
Manufacturing	**5**	6	11	14	9
Construction	**2**	2	1	2	2
Transport, distribution and hotels	**10**	11	7	15	16
Financial, business and other services	**11**	10	6	10	16
Property companies	**6**	5	7	20	35
Lease financing	**4**	5	5	3	4
Hire purchase	**23**	24	10	7	6
Other	**3**	-	1	-	1
Total domestic	**165**	140	121	111	120
Foreign	**29**	25	9	14	5
Total recoveries of advances written off	**194**	165	130	125	125

	2001	2000	1999	1998	1997
	£m	£m	£m	£m	£m
Net advances written off:					
Domestic	**(536)**	(481)	(489)	(476)	(483)
Foreign	**(155)**	(99)	(125)	(358)	(55)
Total net advances written off	**(691)**	(580)	(614)	(834)	(538)
Provision for loan losses charged against income for the year					
Domestic:					
Loans and advances to customers:					
Mortgages	**2**	(4)	9	34	15
Other personal lending	**403**	323	379	201	212
Agriculture, forestry and fishing	**3**	(6)	(4)	31	11
Manufacturing	**40**	21	28	20	21
Construction	**(2)**	1	5	8	6
Transport, distribution and hotels	**28**	3	23	7	63
Financial, business and other services	**39**	12	16	40	10
Property companies	**4**	8	4	(19)	(24)
Lease financing	**5**	8	14	8	20
Hire purchase	**67**	52	31	26	3
Other specific provisions	**23**	15	(5)	14	-
General provisions	**(42)**	(7)	-	(7)	3
Total domestic	**570**	426	500	363	340
Foreign	**177**	115	115	192	171
Total provision for loan losses charged against income for the year	**747**	541	615	555	511
Balance at end of period					
Domestic	**1,162**	1,129	1,134	1,126	1,252
Foreign	**306**	297	280	336	519
Total balance at end of period	**1,468**	1,426	1,414	1,462	1,771
Ratio of net write-offs during the period to average loans outstanding during the period	**0.6%**	0.5%	0.6%	0.9%	0.6%

The following table analyses the coverage of the allowance for loan losses by category of loans.

	2001		2000		1999		1998		1997	
	Allowance £m	**Percentage of loans in each category to total loans %**	Allowance £m	Percentage of loans in each category to total loans %	Allowance £m	Percentage of loans in each category to total loans %	Allowance £m	Percentage of loans in each category to total loans %	Allowance £m	Percentage of loans in each category to total loans %
Balance at period end applicable to:										
Domestic:										
Loans and advances to banks	**-**	**9.1**	-	10.0	-	11.9	-	13.8	-	16.9
Loans and advances to customers:										
Mortgages	**44**	**40.5**	48	40.1	75	39.3	85	38.7	80	37.9
Other personal lending	**407**	**9.2**	362	8.5	358	8.4	283	8.3	346	7.9
Agriculture, forestry and fishing..........	**9**	**1.5**	11	1.5	27	1.8	43	1.8	17	1.8
Manufacturing	**98**	**2.4**	71	2.6	57	2.7	51	2.6	53	2.7
Construction .	**7**	**0.9**	15	0.8	21	0.6	25	0.6	21	0.7
Transport, distribution and hotels	**54**	**3.2**	50	2.9	63	2.9	79	2.9	167	3.5
Financial, business and other services	**65**	**6.3**	59	7.1	65	5.5	83	4.3	65	5.4
Property companies.....	**18**	**2.1**	29	1.9	33	1.9	46	2.0	90	2.1
Lease financing	**18**	**5.4**	20	6.2	16	6.9	11	7.1	30	5.0
Hire purchase	**98**	**3.8**	94	3.9	49	3.0	37	3.2	9	3.2
Other...........	**30**	**2.1**	15	1.9	9	1.8	18	1.7	4	1.4
Total domestic	**848**	**86.5**	774	87.4	773	86.7	761	87.0	882	88.5
Foreign.............	**251**	**13.5**	295	12.6	280	13.3	336	13.0	519	11.5
General provision..........	**369**	**-**	357	-	361	-	365	-	370	-
Total balance at period end	**1,468**	**100.0**	1,426	100.0	1,414	100.0	1,462	100.0	1,771	100.0

Risk elements in the loan portfolio

Non-accrual, past due and restructured loans

The following discussion consists of an analysis of credit risk elements by categories which reflect US lending and accounting practices. These differ from those employed in the UK. In particular:

Suspended interest and non-performing lending

In accordance with the UK British Bankers' Association Statement of Recommended Practice on Advances, Lloyds TSB Group continues to accrue interest, where appropriate, on doubtful debts when there is a realistic prospect of recovery. This accrued interest is charged to the customer's account but it is not applied to income; it is placed on a suspense account and only taken to income if there ceases to be significant doubt about its being paid. Loans are transferred to non-accrual status where the operation of the customer's account has ceased. The lending is managed by specialist recovery departments and is written down to its estimated realisable value. Interest is not added to the lending or placed on a suspense account as its recovery is considered unlikely; it is only taken to income if it is received.

In the US, it is the normal practice to stop accruing interest when payments are 90 days or more past due or when recovery of both principal and interest is doubtful. When the loans are transferred to non-accrual status, accrued interest is reversed from income and no further interest is recognised until it becomes probable that the principal and interest will be repaid in full. Loans on which interest has been accrued but suspended would be included in risk elements as loans accounted for on a non-accrual basis.

In addition, in the US non-performing loans and advances are typically written off more quickly than in the UK. Consequently a UK bank may appear to have a higher level of non-performing loans and advances than a comparable US bank although the reported income is likely to be similar in both the US and the UK.

Troubled debt restructurings

In the US, loans whose terms have been modified due to problems with the borrower are required to be separately disclosed. If the new terms were in line with market conditions at the time of the restructuring and the restructured loan remains current as to repayment of principal and interest then the disclosure can be discontinued at the end of the first year.

There are no similar disclosure requirements in the UK.

Potential problem loans

Potential problem loans are loans where known information about possible credit problems causes management to have concern as to the borrowers' ability to comply with the present loan repayment terms. Interest continues to be accrued to the profit and loss account until, in the opinion of management, its ultimate recoverability becomes doubtful.

Assets acquired in exchange for advances

In most circumstances in the US, title to property securing residential real estate transfers to the lender upon foreclosure. The loan is written off and the property acquired in this way is reported in a separate balance sheet category with any recoveries recorded as an offset to the provision for loan losses recorded in the period. Upon sale of the acquired property, gains or losses are recorded in the income statement as a gain or loss on acquired property.

In the UK, although a bank is entitled to enforce a first charge on a property held as security, it typically does so only to the extent of enforcing its power of sale. In accordance with UK GAAP and industry practice, Lloyds TSB Group takes control of a property held as collateral on a loan at repossession but title does not transfer to it. Loans subject to repossession continue to be reported as loans in the balance sheet although the accrual of interest is suspended. Any gains or losses on sale of the acquired property are recorded within the provision for loan losses during the reporting period.

The difference in practices has no effect on net income reported in the UK compared to that reported in the US but it does result in a difference in classification of losses and recoveries in the income statement. It also has the effect of causing UK banks to report an increased level of non-performing loans compared with US banks.

The following table analyses risk elements in the loan portfolio as at 31 December for the last five years:

	2001	2000	1999	1998	1997
	£m	£m	£m	£m	£m
Loans accounted for on a non-accrual basis:					
Domestic offices	**278**	223	209	287	443
Foreign offices	**101**	181	139	130	108
Total non-accrual loans	**379**	404	348	417	551
Accruing loans on which:					
-interest is being placed in suspense:					
Domestic offices	**637**	617	502	479	966
Foreign offices	**206**	238	217	292	441
Total suspended interest loans	**843**	855	719	771	1,407
-interest is still being accrued and taken to profit, and against which specific provisions have been made:					
Domestic offices	**1,265**	1,713	1,924	2,056	1,633
Foreign offices	**75**	101	74	75	115
Total accruing loans against which specific provisions have been made	**1,340**	1,814	1,998	2,131	1,748
- interest is still being accrued and taken to profit, the lending is contractually past due 90 days or more as to principal or interest, but against which no provisions have been made:					
Domestic offices	**693**	520	506	313	389
Foreign offices	**37**	33	15	-	-
Total accruing loans against which no provisions have been made	**730**	553	521	313	389
Troubled debt restructurings:					
Domestic offices	**1**	2	10	1	2
Foreign offices	**9**	12	10	1	2
Total troubled debt restructurings	**10**	14	20	2	4
Total non-performing lending:					
Domestic offices	**2,874**	3,075	3,151	3,136	3,433
Foreign offices	**428**	565	455	498	666
Total non-performing lending	**3,302**	3,640	3,606	3,634	4,099

Interest foregone on non-performing lending

The table below summarises the interest foregone on loans accounted for on a non-accrual basis and troubled debt restructurings:

	2001 £m
Domestic lending:	
Interest income that would have been recognised under original contract terms	**24**
Interest income included in profit	**17**
Interest foregone	**7**
Foreign lending:	
Interest income that would have been recognised under original contract terms	**21**
Interest income included in profit	**10**
Interest foregone	**11**

Potential problem loans

In addition to the non-performing lending disclosed above, lendings which were current as to payment of interest and principal but where concerns existed about the ability of the borrowers to comply with loan repayment terms in the near future were as follows:

	2001 £m	2000 £m	1999 £m	1998 £m	1997 £m
Potential problem lending	**1,423**	1,142	936	958	1,078

Cross border outstandings

The business of Lloyds TSB Group involves significant exposures in non-local currencies. These cross border outstandings comprise loans (including accrued interest), acceptances, interest-bearing deposits with other banks, other interest-bearing investments and any other monetary assets which are denominated in non-local currency. The following tables analyse, by type of borrower, foreign outstandings which individually represent in excess of 1 per cent of Lloyds TSB Group's total assets.

	% of assets	**Total £m**	**Governments and official institutions £m**	**Banks and other financial institutions £m**	**Commercial, industrial and other £m**
As at 31 December 2001					
Germany	**2.0**	**3,756**	**59**	**2,920**	**777**
United States of America	**1.8**	**3,403**	**151**	**1,290**	**1,962**
Italy	**1.7**	**3,170**	**1,834**	**1,052**	**284**
As at 31 December 2000					
Germany	1.6	2,659	171	2,222	266
United States of America	1.4	2,290	90	907	1,293
As at 31 December 1999					
Belgium	1.7	2,602	-	2,574	28
Germany	1.4	2,156	217	1,794	145
Japan	1.3	1,974	201	1,363	410
France	1.1	1,636	6	1,401	229

As at 31 December 2001, Germany had commitments of £845 million, United States of America had commitments of £818 million and Italy had commitments of £104 million.

As at 31 December 2001, the countries with cross border outstandings of between 0.75 per cent and 1 per cent of assets, amounting to £3,504 million in total were Japan and the Netherlands.

As at 31 December 2000, the countries with cross border outstandings of between 0.75 per cent and 1 per cent of assets, amounting to £4,529 million in total were France, Italy and Japan. As at 31 December 1999 the countries with cross border outstandings of between 0.75 per cent and 1 per cent of assets, amounting to £2,500 million in total were the US and the Netherlands.

Market risk in banking operations

Market risk is the risk of losses being incurred as a result of adverse movements in interest or exchange rates or other market variables. Market risk arises in all areas of Lloyds TSB Group's activities and is managed by a variety of different techniques.

Lloyds TSB Group's activities expose it to the risk of adverse movements in interest rates or exchange rates, with little or no exposure to equity or commodity risks. Trading activities are restricted to a few highly specialist trading centres, authorised by Group Risk, the principal one being Lloyds TSB Group's Treasury department in London. The level of exposure is strictly controlled and monitored within approved limits locally and centrally by Lloyds TSB Group Risk. Most of Lloyds TSB Group's trading activity is to meet the requirements of customers for foreign exchange and interest rate products, from which Lloyds TSB Group is able to earn a spread on the rates charged. However, interest rate and exchange rate positions are taken out using derivatives (forward foreign exchange contracts, interest rate swaps and forward rate agreements) and on-balance sheet instruments (mainly debt securities). The objective of these positions is to earn a profit from favourable movements in market rates. Accordingly, these transactions are reflected in the accounts at their fair value and gains and losses shown in the profit and loss account as dealing profits. Further details on trading derivatives can be found in Note 45 to the Consolidated Financial Statements.

Trading Value at Risk ("VaR")

Trading limits are set by Lloyds TSB Group Risk, up to a total authorised by the board, using a combination of risk measurement techniques, including position limits and sensitivity limits. These are supplemented by a range of value at risk techniques in use in individual businesses, where suitable methodologies have been developed in consultation with Lloyds TSB Group Risk to meet the specific requirements of each centre. At Lloyds TSB Group level, global positions are incorporated into a central VaR model, taking into account natural offset positions between different trading centres, and stress tests are carried out to simulate extreme conditions.

VaR can be calculated using a number of different methodologies and at different confidence intervals. Lloyds TSB Group utilises more than one methodology for comparative purposes, thus avoiding undue reliance on a single measure.

The predominant measure within Lloyds TSB Group is the variance/covariance ('VcV') methodology. Based on the commonly used 95 per cent confidence level, assuming positions are held overnight and using observation periods of the preceding three years, the value at risk based on Lloyds TSB Group's global trading was as detailed in the table below.

The following table shows total, average, maximum and minimum VaR for the years ended 31 December 2001 and 2000.

	31 December 2001				31 December 2000		
	Total £m	**Average £m**	**Maximum £m**	**Minimum £m**	Average £m	Maximum £m	Minimum £m
Interest Rate Risk	**0.6**	**0.6**	**0.9**	**0.4**	0.7	1.2	0.5
Foreign Exchange Risk	**1.0**	**0.6**	**1.0**	**0.3**	0.5	0.9	0.3
Equity Risk	**0.0**	**0.0**	**0.0**	**0.0**	0.1	0.2	0.0
Total VaR	**1.6**	**1.2**	**1.6**	**0.8**	1.3	1.7	1.0

The risk of loss measured by the VaR model is the potential loss in earnings. The total and average trading VaR does not assume any diversification benefit across the three risk types. The maximum and minimum VaR reported for each risk category did not necessarily occur on the same day as the maximum and minimum VaR reported as a whole.

There are some limitations to the VcV methodology which are covered below:

- The model assumes that changes in the underlying asset returns can be modelled by a normal distribution. This assumption is an approximation of reality that may not reflect all circumstances.

- The use of a confidence limit does not convey any information about potential losses on occasions when the confidence limit is exceeded. In times of extreme market movements actual losses may be several times greater than the VaR number. Stress testing is used to supplement VaR to estimate the impact of extreme events.

- Any model that forecasts the future based on historic data is implicitly assuming that the conditions that generated the data will remain true in the future. Stress testing and using more than one VaR methodology for some local markets form part of the wider market risk framework.

- Periods of severe market illiquidity, both in terms of the extent of the illiquidity and the time that it lasts, would mean that it may not be possible to hedge, or close, all positions in the timescales assumed in the VaR model.

- VaR is calculated at the close of business each day, which excludes the profit and loss impact of intra-day trading.

- The variance/covariance approach to VaR is not well suited to options positions. As a result these positions are controlled by additional sensitivity limits.

In summary, although VaR is an important component of Lloyds TSB Group's approach to managing trading market risk, it is supplemented by position and sensitivity limits and stress testing.

Interest rate exposure

Interest rate exposures comprise those originating in treasury trading activities and structural interest rate exposures, which arise from the commercial and retail banking activities of Lloyds TSB Group.

Trading interest rate risk

The VaR relating to interest rate trading positions is set out in "—Market risk in banking operations—Trading Value at Risk (VaR)".

Structural interest rate risk

Structural interest rate risk in Lloyds TSB Group's retail portfolios, including mortgages, and in Lloyds TSB Group's capital funds, arises from the different repricing characteristics of Lloyds TSB Group's banking assets and liabilities and is managed by Lloyds TSB Group's Balance Sheet Management department.

Liabilities arising in the course of business from Lloyds TSB Group's retail banking business fall into two broad categories:

- those which are insensitive to interest rate movements, non-interest bearing liabilities such as shareholders' funds and interest free or very low interest current account deposits; and

- those which are sensitive to interest rate movements, primarily savings deposits bearing interest rates which are varied at Lloyds TSB Group's discretion ("managed rate liabilities") but which for competitive reasons generally reflect changes in the Bank of England's base rate.

There is a relatively small volume of naturally arising banking liabilities whose interest rate is contractually fixed typically for periods of up to two years.

Most banking assets, with the exception of such non-interest earning items as premises, are sensitive to interest rate movements. There is a large volume of managed rate assets such as variable rate mortgage loans, and these may be considered as a natural offset to managed rate liabilities. However many assets, such as personal loans and fixed rate mortgages, bear interest which is contractually fixed for periods of up to five years or longer.

Interest rate risk arises from the mismatch between interest rate insensitive liabilities and interest rate sensitive assets, and between the differing contractual periods for which interest rates are fixed on interest rate sensitive assets and liabilities. Lloyds TSB Group's Balance Sheet Management department manages this risk centrally by:

- offsetting against each other any matching interest rate sensitive assets and liabilities;

- acquiring new financial assets and liabilities as matching hedges against net balances of mismatched interest rate sensitive banking liabilities and assets, respectively; and

- acquiring new financial assets with interest rates contractually fixed for a range of periods up to five years as hedges for net balances of interest rate insensitive liabilities.

The financial assets and liabilities referred to above are acquired by way of internal transactions between Lloyds TSB Group Balance Sheet Management and Lloyds TSB Group Treasury, typically in the form of interest rate swaps and loans or deposits.

Lloyds TSB Group Balance Sheet Management reports to an Asset and Liability Committee under the chairmanship of the Group Finance Director; other members include the Director of Group Risk Management, the Lloyds TSB Group executive director responsible for treasury and the managing directors of the main UK business units. Lloyds TSB Group's policy is to optimise the stability of future net interest income. The risks are monitored using simulation models and other quantitative techniques.

Structural interest rate risk can also arise from the wholesale banking books in the UK, where it is managed by Lloyds TSB Group Treasury, and internationally, where it is managed by an authorised local treasury operation in each overseas centre. The levels of exposure within these books are controlled and monitored within approved limits locally and centrally by Group Risk. Group Risk issues the limits to the international business units on interest rate gaps or, where more appropriate, VaR. Active management of the book is necessary to meet customer requirements and changing market circumstances.

Lloyds TSB Group's non-trading exposure is summarised in the form of an interest rate repricing table, as set out in Note 45 to the Consolidated Financial Statements. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date. However, the table does not take into account the effect of interest rate options used by Lloyds TSB Group to hedge its exposure.

The simulation models used by Lloyds TSB Group include assumptions about the relationships between customer behaviour and the level of interest rates; the anticipated level of future business is also taken into account. The accuracy of these assumptions will impact the efficiency of hedging transactions. The assumptions are regularly updated and the projected exposure is actively managed in accordance with Lloyds TSB Group's Asset and Liability Committee policy.

It is estimated that a hypothetical immediate and sustained 100 basis point increase in interest rates on 1 January 2002 would decrease net interest income by £102.9 million for the 12 months to 31 December 2002, while a hypothetical immediate and sustained 100 basis point decrease in interest rates would increase net interest income by £85.7 million.

	UK £m	**North America £m**	**Asia & Australasia £m**	**Latin America £m**	**Europe & Middle East £m**	**Total 2002 £m**	Total 2001 £m
Change in net interest income from a +100 basis point shift in yield curves	**(71.0)**	**(17.5)**	**(0.3)**	**0.1**	**(14.2)**	**(102.9)**	(26.6)
Change in net interest income from a - 100 basis point shift in yield curves	**53.8**	**17.5**	**0.3**	**(0.1)**	**14.2**	**85.7**	7.3

The analysis above is subject to certain simplifying assumptions including, but not limited to, the following:

- all rates of all maturities worldwide move simultaneously by the same amount;
- all positions in the wholesale books run to maturity; and
- there is no management action in response to movements in interest rates.

In practice, positions in both the retail and wholesale books are actively managed and actual impact on net interest income may be different than the model.

Foreign exchange exposure

Trading foreign exchange risk

The corporate and retail businesses incur foreign exchange risk in the course of providing services to their customers. These risks reside in the authorised trading centres who are allocated exposure limits by Group Risk. The limits are monitored daily by the local centres and reported to Group Risk. Group Risk calculates the associated VaR as shown in the table in "—Market risk in banking operations—Trading Value at Risk (VaR)".

Structural foreign exchange risk

Structural foreign exchange risk arises from Lloyds TSB Group's investments in its overseas operations. Lloyds TSB Group's structural foreign currency exposure is represented by the net asset value of the holding company's foreign currency exchange equity and subordinated debt investments in its subsidiaries and branches. Gains or losses on structural foreign currency exposures are taken to retained earnings.

The structural position is managed by Lloyds TSB Group Capital Funds having regard to the currency composition of Lloyds TSB Group's risk-weighted assets and reported to Lloyds TSB Group Asset and Liability Committee on a monthly basis. The objective is to limit the effect of the exchange rate movements on the published risk asset ratio.

Lloyds TSB Group's structural position at 31 December 2001 is set out in Note 45 to the Consolidated Financial Statements. The position implies that at 31 December 2001 a hypothetical increase of 10 per cent in the value of sterling against all other currencies would have led to a £172 million reduction in reserves, and vice versa. On this basis, there would have been no material impact on Lloyds TSB Group's risk asset ratios.

Equity exposure

A small number of Lloyds TSB Group's authorised centres can incur equity risk in dealings with their retail and commercial customers. Limits on these equity exposures are controlled and monitored by Group Risk. Group Risk calculates VaR on these equities positions as set out in the trading VaR table in "—Market risk in banking operations—Trading Value at Risk (VaR)".

Market risk in insurance operations

Lloyds TSB Group's insurance activities also result in market risk. The market risk within the insurance businesses can be categorised into two broad types: investment market risk and the potential interest rate risk on any mismatch between assets held to support future liabilities in the life business and the actual future liabilities.

Investment market risk is derived from two portfolios: the surplus in the Scottish Widows non-participating fund and an investment portfolio within the General Insurance business.

The surplus in the long-term non-participating fund of Scottish Widows plc exists to provide the long-term funds with liquidity and working capital. The surplus also forms a capital reserve to support the investments managed on behalf of the with-profits policies which were transferred from Scottish Widows Fund and Life Assurance Society. With profits business involves guaranteed benefits; in extreme market conditions the surplus could be called upon to support with profits benefits. As a consequence it is appropriate to invest this fund in a mixture of equities, investment properties, and fixed interest investments that is related to the With Profits Fund. This investment policy maintains the value of the reserve as a proportion of the underlying With Profits Fund. The existence and investment mix of the surplus in the non-participating fund can therefore be considered as structural rather than as a traded portfolio. Under UK GAAP the portfolio is shown at market value and gains and losses are recognised in the profit and loss account.

The General Insurance portfolio comprises funds that form the reserves for that business. These reserves are invested in a mixture of assets: cash, bonds and equities. The size of the equity component allowed and the investment policy are approved by Group Risk.

The composition, and value, of both the non-participating fund and the General Insurance portfolio are reported to Group Risk on a monthly basis and a VaR is calculated. Stress testing is also used to supplement the VaR models.

The risk of loss measured by the VaR model is the potential loss in earnings. The VaR methodology used is a variance/covariance ('VcV') approach which is the same in all respects to that used for the traded risk in the banking book, except that in the case of equity risk, the model maps the portfolio composition onto a series of appropriate indices by region and sector. The figures quoted below are the sum of the two portfolios with no allowance for diversification between portfolios or asset classes and represents the potential loss in earnings.

The following table shows total VaR at 31 December 2001 and 2000:

	31 December 2001	31 December 2000
	£m	£m
Interest Rate Risk	**3.3**	3.8
Foreign Exchange Risk	**2.1**	2.6
Equity Risk	**22.2**	28.1
Total VaR	**27.6**	34.5

The other sources of market risk within the insurance businesses are the matched portfolios (e.g. annuities) that contain long-term liabilities. The aim is to invest in assets such that the cash flows on the investments will match those on the projected future liabilities. Actuarial tools are used to project and match the cash flows.

It is not possible to eliminate risk completely as the timing of mortality is uncertain, and bonds are not available at all of the required maturities. As a result the cash flows cannot be precisely matched and so sensitivity tests are used to test the extent of the mismatch.

Operational risk

Operational risk is the exposure to financial or other damage arising through unforeseen events or failure in the Group's operational processes/systems. Examples include inadequate or failed internal controls and procedures, human error, deliberate or malicious acts including fraud, and business interruptions.

Business units have primary responsibility for identifying and managing their operational risks and internal control techniques to reduce their likelihood or impact include segregation of duties, exception and exposure reporting, business continuity planning, reconciliation, and delegation of authority, and are based on the submission of timely and reliable management reporting. Where appropriate, risk is mitigated by way of insurance with third parties.

Group Risk Management's responsibilities in respect of operational risk are as follows:

Policy & Methodology:

- Formulation of high-level operational risk policies designed to ensure a comprehensive and consistent approach to the identification and management of operational risk. These policies provide a standard framework within which Lloyds TSB Group businesses structure their individual policies and procedures.

- Development of a standard methodology to ensure consistency in the identification, assessment and management of operational risk. This methodology is being implemented by business units throughout the Lloyds TSB Group.

- Communication and provision of general guidance on operational risk related issues, including regulatory changes and developments in the measurement and management of operational risk, to promote best practice throughout the Lloyds TSB Group.

Assurance:

- Approval from a risk perspective of all new products launched throughout the Lloyds TSB Group, to ensure that the risks associated with them are understood by the business.

- Identification of risk through formal Risk Reviews, covering specific risks, activities, business sectors or products, and ensuring that prompt and pre-emptive action is taken to address any actual or perceived risks that may emerge, whether specific to Lloyds TSB Group or to the industry generally.

- Independent verification by Group Audit of the effectiveness of risk control within business units.

A major cause of operational losses is fraud involving credit and debit cards. In common with the rest of the financial services industry, Lloyds TSB Group is investing in technology to combat this problem.

Insurance risk

Lloyds TSB Group offers insurance products to its customers, and Group Risk actively reviews the extent to which the associated risk is underwritten internally or reinsured with external underwriters. The risks associated with long-term savings, investment and insurance products are also evaluated.

The Financial Services Authority sets down minimum requirements for solvency and reserving for all classes of insurance, which are carefully monitored by the relevant business units within Lloyds TSB Group. The retained risk level is carefully controlled and monitored, with close attention being paid to the analysis of underwriting experience, product design, policy wordings, adequacy of reserves, solvency management and regulatory requirements.

Investment strategy is determined by the term and nature of the underwriting liabilities and asset/liability matching positions are actively monitored. General insurance exposure to accumulations of risk and potential catastrophes is reviewed and, where appropriate, mitigated by reinsurance arrangements which are broadly spread over different reinsurers. Appropriate reinsurance arrangements also apply within the life and pensions businesses.

Compliance risk

The Lloyds TSB Group's business is regulated overall by the Financial Services Authority (FSA), and additionally by local regulators in offshore and overseas jurisdictions. Each Lloyds TSB Group business has a nominated individual with 'Compliance Oversight' responsibility under FSA rules. The role of such individuals is to ensure that management have in place within the business a control structure which creates awareness of the rules and regulations to which Lloyds TSB Group is subject, and to monitor and report on adherence to these rules and regulations.

All compliance personnel also have a reporting line to Group Compliance, which sets compliance standards across the Group and provides independent reporting and assessment to Lloyds TSB Group directors and the Board.

Group Compliance includes a dedicated unit, led by the Group Financial Crime Director, which is responsible for ensuring that Lloyds TSB Group has effective processes in place to identify and report on suspicious transactions and customers in support of the world-wide fight against financial crime.

The Group Compliance director has access to the Chairman, Group Chief Executive and members of senior management.

Liquidity and capital resources

Liquidity risk is defined as the risk of a loss arising from Lloyds TSB Group's inability to meet its financial obligations as they fall due. These obligations include the repayment of deposits on demand or at their contractual maturity; the repayment of loan capital and other borrowings as they mature; the payment of insurance policy benefits, claims and surrenders; the payment of lease obligations as they become due; the payment of operating expenses and taxation; the payment of dividends to shareholders; the ability to fund new and existing loan commitments; and the ability to take advantage of new business opportunities, Lloyds TSB Group complies with the Financial Services Authority's liquidity requirements, with similar liquidity policies in place across all trading centres worldwide. Compliance is monitored by regular liquidity returns to Group Risk.

The principal sources of liquidity for Lloyds TSB Group plc are dividends received from its only directly owned subsidiary company, Lloyds TSB Bank and loans from this and other Lloyds TSB Group companies. The ability of Lloyds TSB Bank to pay dividends, or for Lloyds TSB Bank or other Lloyds TSB Group companies to make loans to Lloyds TSB Group plc, depend on a number of factors, including their own regulatory capital requirements, distributable reserves and financial performance. For additional information see "Dividends".

Lloyds TSB Group plc is also able to raise funds by issuing loan capital or equity, although in practice Lloyds TSB Group plc has never issued equity for this purpose and the majority of Lloyds TSB Group's loan capital is issued by Lloyds TSB Bank. As at 31 December 2001, Lloyds TSB Group plc had £413 million of subordinated debt in issuance following the prepayment of £100 million of loan capital during the year, compared with £7,657 million for the consolidated Lloyds TSB Group. The cost and availability of subordinated debt finance are influenced by credit ratings. A reduction in these ratings could increase the cost and could reduce market access. At 31 December 2001, the credit ratings of Lloyds TSB Bank were as follows:

	Senior debt
Moody's	Aaa
Standard & Poor's	AA
Fitch	AA+

The credit ratings of Lloyds TSB Group plc were one notch lower. At 26 February 2002 the Standard & Poor's rating outlook for Lloyds TSB Bank was stable. These credit ratings are not a recommendation to buy, hold or sell any security; and each rating should be evaluated independently of every other rating.

A significant part of the liquidity of Lloyds TSB Group's banking businesses arises from their ability to generate customer deposits. A substantial proportion of the customer deposit base is made up of current and savings accounts which, although repayable on demand, have traditionally provided a stable source of funding. During 2001, amounts deposited by customers increased by £7,127 million from £101,989 million at 31 December 2000 to £109,116 million at 31 December 2001. These customer deposits are supplemented by the issue of subordinated loan capital and wholesale funding sources in the capital markets, as well as from direct customer contracts. Wholesale funding sources include deposits taken on the inter-bank market, certificates of deposit, sale and repurchase agreements, a Euro Medium Term Note programme, of which £996 million had been utilised at 31 December 2001, and a US$5,000 million commercial paper programme, of which US$2,859 million had been utilised at 31 December 2001.

The ability to sell assets quickly is also an important source of liquidity for Lloyds TSB Group's banking businesses. Lloyds TSB Group holds sizeable balances of marketable Treasury and other eligible bills and debt securities which could be disposed of to provide additional funding should the need arise.

Lloyds TSB Group makes limited use of asset securitisation arrangements to provide alternative funding sources. Prior to its acquisition by Lloyds TSB Group, Black Horse Limited (formerly Chartered Trust plc) disposed of its interest in a portfolio of motor vehicles and caravan instalment credit agreements to a special purpose vehicle ('SPV'). Black Horse Limited has no interest in the share capital of this SPV, although it acts as credit manager for the administration of the portfolio and receives a fee for this service. Black Horse Limited has no obligation to the holders of the floating rate notes issued by this SPV to fund the original purchase of the portfolio, or to any other creditors of this SPV. At 31 December 2001, this SPV held £124 million of receivables which are included in Lloyds TSB Group's consolidated balance sheet using a linked presentation; further information is given in Note 14 to the Consolidated Financial Statements.

The following table sets out the amounts and maturities of Lloyds TSB Group's contractual cash obligations at 31 December 2001:

	Within one year £m	One to three years £m	Three to five years £m	Over five years £m	Total £m
Long-term debt – dated	**5**	**567**	**249**	**3,185**	**4,006**
Finance leases	**3**	**-**	**-**	**-**	**3**
Operating leases	**229**	**601**	**186**	**337**	**1,353**
Total	**237**	**1,168**	**435**	**3,522**	**5,362**

At 31 December 2001, Lloyds TSB Group also had £3,651 million of undated long-term debt outstanding.

The following table sets out the amounts and maturities of Lloyds TSB Group's other commercial commitments at 31 December 2001. These commitments are not included in Lloyds TSB Group's consolidated balance sheet.

	Within one year £m	One to three years £m	Three to five years £m	Over five years £m	Total £m
Acceptances	**2,243**	**-**	**-**	**-**	**2,243**
Guarantees	**3,065**	**426**	**27**	**271**	**3,789**
Other contingent liabilities	**1,566**	**271**	**8**	**86**	**1,931**
Total contingent liabilities	**6,874**	**697**	**35**	**357**	**7,963**
Lending commitments	**42,594**	**5,605**	**3,080**	**891**	**52,170**
Other commitments	**834**	**57**	**101**	**180**	**1,172**
Total commitments	**43,428**	**5,662**	**3,181**	**1,071**	**53,342**
Total contingents and commitments	**50,302**	**6,359**	**3,216**	**1,428**	**61,305**

Loan commitments are agreements to lend to customers in accordance with contractual provisions; these are either for a specified period or, as in the case of credit cards, represent a revolving credit facility which can be drawn down at any time, provided that the agreement has not been terminated. The total amounts of unused commitments do not necessarily represent future cash requirements, in that commitments often expire without being drawn upon.

Lloyds TSB Group's banking businesses are also exposed to liquidity risk through the provision of securitisation liabilities to certain corporate customers. Lloyds TSB Group acts as sponsor to two off-balance sheet entities, Monument and Obelisk, which are wholly owned by independent trusts and administered by third parties. These off-balance sheet entities purchase receivables from customers funded by secured lending from third parties, which in turn issue asset-backed commercial paper to investors. Lloyds TSB Group does not sell its own receivables to these entities, and the assets and obligations of Monument and Obelisk are not included in Lloyds TSB Group's consolidated balance sheet. However, Lloyds TSB Group provides short-term asset-backed commercial paper liquidity support facilities on commercial terms to the issuers of the commercial paper, for use in the event of a market disturbance should they be unable to roll-over maturing commercial paper or obtain alternative sources of funding.

During 2001, fee income earned by Lloyds TSB Group in relation to these transactions totalled approximately £650,000. At 31 December 2001, Monument and Obelisk held assets of approximately £2,140 million, primarily loans and investments. The assets are generally of investment grade quality and are typically secured. Based upon the commitments of Monument and Obelisk to their customers as at 31 December 2001, Lloyds TSB Group provided asset-backed commercial paper liquidity support facilities of £2,020 million.

Within Lloyds TSB Group's insurance and investments businesses, the principal sources of liquidity are premiums received from policyholders, charges levied upon policyholders, investment income and the proceeds from the sale and maturity of investments. The investment policies followed by Lloyds TSB Group's life assurance companies take account of anticipated cash flow requirements by matching the cash inflows with projected liabilities. Any liquidity requirements in excess of those anticipated are met from additional funds held to provide solvency margin cover; these include significant short-term cash deposits. As at 31 December 2001, these funds amounted to £2,985 million, representing an excess of £1,831 million over the required minimum solvency margin.

Based upon the levels of resources within the banking and insurance and investments businesses and the ability of Lloyds TSB Group to access the wholesale money markets or issue debt securities should the need arise, Lloyds TSB Group believes that its overall liquidity is sufficient to meet current obligations to customers, policyholders and debt holders, support expectations for future changes in asset and liability levels and carry on normal operations.

Because the principal business of Lloyds TSB Group is banking, it is able to raise substantial amounts of cash in the wholesale money markets to provide funds for acquisitions, should the need arise. In deciding whether Lloyds TSB Group has sufficient resources to be able to make an acquisition the key factor is not the availability of cash, but the ability of Lloyds TSB Group, and the authorised institutions within Lloyds TSB Group, to continue to meet the capital adequacy requirements of the regulatory authorities. There are strict limits imposed by the regulatory authorities as to the proportion of Lloyds TSB Group's regulatory capital base that can be made up of subordinated debt and preferred securities, see – "Liquidity and capital resources – capital ratios". At the end of 2000, following the acquisitions of Scottish Widows and Chartered Trust, Lloyds TSB Group was very close to these limits and only had capacity to raise approximately £200 million of debt capital. However, Lloyds TSB Group's capacity to raise new debt capital for regulatory purposes increases as profits are retained; at 31 December 2001, Lloyds TSB Group had capacity to raise approximately £1,300 million of debt capital.

Capital resources

The total capital resources of Lloyds TSB Group are set out below:

	31 December 2001 £m	31 December 2000 £m	31 December 1999 £m
Minority interests (equity and non-equity)	**997**	552	33
Called-up share capital	**1,411**	1,396	1,389
Share premium account	**959**	595	404
Merger reserve	**343**	343	343
Profit and loss account	**8,047**	7,690	6,693
Shareholders' funds (equity)	**10,760**	10,024	8,829
	11,757	10,576	8,862
Undated loan capital	**3,651**	3,391	3,294
Dated loan capital	**4,006**	4,119	3,199
Total capital resources	**19,414**	18,086	15,355

Lloyds TSB Group's total capital resources increased by £1,328 million during 2001.

Shareholders' funds increased by £736 million, mainly as a result of profit retentions, and loan capital increased by £147 million, due to the issue of additional subordinated loan capital to fund the general activities of Lloyds TSB Group.

There was a further increase in non-equity minority interests during 2001 following the issue of £456 million of non-cumulative perpetual capital securities by Lloyds TSB Bank, to provide capital to support the expansion of Lloyds TSB Group's balance sheet.

Capital ratios

The international standard for measuring capital adequacy is the risk asset ratio, which relates regulatory capital to balance sheet assets and off-balance sheet exposures weighted according to broad categories of risk.

Lloyds TSB Group's regulatory capital is divided into tiers defined by the European Community Own Funds Directive. Tier 1 comprises shareholders' funds and minority interests, after deducting goodwill and intangible assets. Tier 2 comprises general loan loss provisions, and qualifying subordinated loan capital, with restrictions on the amount of general provisions and loan capital which may be included. The amount of qualifying tier 2 capital cannot exceed that of tier 1 capital. Total capital is reduced by deducting investments in subsidiaries and associates which are not consolidated for regulatory purposes and investments in the capital of other credit/financial institutions. In the case of Lloyds TSB Group, this means that the net assets of its life assurance and general insurance businesses are deducted from Lloyds TSB Group's regulatory capital.

Banking operations are categorised as either banking book or trading book (broadly, activities which are accounted for on a mark-to-market basis). Risk-weighted assets are determined according to a broad categorisation of the nature of each asset or exposure and counterparty and, for the trading book, by taking into account market-related risks.

	31 December 2001 £m	31 December 2000 £m	31 December 1999 £m
Capital: tier 1	**9,168**	7,949	8,596
tier 2	**7,831**	7,722	6,838
	16,999	15,671	15,434
Supervisory deductions	**(6,960)**	(6,862)	(2,588)
Total regulatory capital	**10,039**	8,809	12,846
Total risk-weighted assets	**108,755**	93,979	84,415
Post-tax return on average risk weighted assets	**2.53%**	3.10%	3.04%
Risk asset ratios: total capital	**9.2%**	9.4%	15.2%
tier 1	**8.4%**	8.5%	10.2%

At 31 December 2001, the risk asset ratios were 9.2 per cent for total capital and 8.4 per cent for tier 1 capital. The 8.4 per cent tier 1 capital ratio appears higher than would perhaps be expected for Lloyds TSB Group. This reflects the higher level of supervisory deductions resulting from Lloyds TSB Group's significantly increased investment in its life assurance operations as a result of the acquisition of Scottish Widows.

During 2001, total capital for regulatory purposes increased by £1,230 million to £10,039 million. Tier 1 capital was increased by £1,219 million, mainly from retained profits and the issue of tax efficient capital instruments. Tier 2 capital increased by £109 million and supervisory deductions increased by £98 million.

Risk-weighted assets increased to £108,755 million at 31 December 2001 and the post-tax return on average risk-weighted assets, which Lloyds TSB Group considers a key measure of efficient use of capital, was 2.53 per cent.

Corporate social responsibility

Lloyds TSB Group adopts a responsible attitude to social, environmental and ethical (SEE) issues, and publishes a separate annual information pack on its role in the community, its code of business conduct and its environmental performance.

Lloyds TSB Group has a dedicated environmental risk unit which is responsible for the development of environmental policies and procedures, and provides practical advice and guidance on environmental issues to business units. Significant progress has been made in developing Lloyds TSB Group's environmental management system and this is detailed in the environmental report forming part of 'the community and our business'.

Following the recent publication by the Association of British Insurers of guidelines on the disclosure of information on SEE issues in company annual reports, Lloyds TSB Group is reviewing its SEE policies and disclosures.

Investment portfolio

Investment securities and other securities

The following table sets out the book value and valuation of Lloyds TSB Group's investment securities and other securities at 31 December for each of the three years indicated.

	2001		2000		1999	
	Book value £m	**Valuation £m**	Book value £m	Valuation £m	Book value £m	Valuation £m
Investment securities[(1)]						
Bank and building society certificates of deposit	**4,670**	**4,677**	3,034	3,034	4,153	4,145
Corporate debt securities	**613**	**616**	465	466	75	76
Mortgage backed securities	**521**	**527**	18	18	15	15
Other asset backed securities	**2,328**	**2,332**	529	529	49	48
Other debt securities	**1,211**	**1,209**	619	618	540	539
Securities of the US Treasury and US Government agencies	**13**	**13**	12	12	10	10
Other Government securities	**1,633**	**1,829**	1,717	2,136	1,886	2,245
Other public sector securities	**-**	**-**	1	1	4	4
Equity shares	**38**	**66**	41	102	43	79
	11,027	**11,269**	6,436	6,916	6,775	7,161
Other securities						
UK Government securities	**31**	**31**	893	893	1,917	1,917
Securities of the US Treasury and US Government agencies	**-**	**-**	16	16	14	14
Other Government securities	**4,072**	**4,072**	2,151	2,151	1,930	1,930
Other public sector securities	**151**	**151**	131	131	65	65
Bank and building society certificates of deposit	**234**	**234**	105	105	286	286
Corporate debt securities	**7,102**	**7,102**	4,671	4,671	3,873	3,873
Mortgage backed securities	**1,054**	**1,054**	242	242	28	28
Other asset backed securities	**592**	**592**	-	-	-	-
Other debt securities	**-**	**-**	1	1	39	39
Equity shares	**187**	**187**	206	206	170	170
	13,423	**13,423**	8,416	8,416	8,322	8,322

(1) Investment securities are those intended for use on a continuing basis in the activities of Lloyds TSB Group and not for dealing purposes. Investment securities held by Lloyds TSB Group's insurance businesses are not included.

Maturities and weighted average yields of debt securities

The weighted average yield for each range of maturities is calculated by dividing the annualised interest income prevailing at 31 December 2001 by the book value of securities held at that date.

	Maturing within one year		Maturing after one but within five years		Maturing after five but within ten years		Maturing after ten years	
	Amount £m	Yield %	Amount £m	Yield %	Amount £m	Yield %	Amount £m	Yield %
Investment securities								
Securities of the US Treasury and US Government agencies	**-**	**-**	**4**	**5.8**	**5**	**7.1**	**4**	**7.2**
Other Government securities	**254**	**3.2**	**240**	**4.3**	**187**	**5.8**	**952**	**9.9**
Bank and building society certificates of deposit	**4,591**	**4.4**	**79**	**4.7**	**-**	**-**	**-**	**-**
Corporate debt securities	**18**	**5.5**	**377**	**4.7**	**159**	**6.4**	**59**	**3.6**
Mortgage backed securities	**-**	**-**	**174**	**4.6**	**326**	**5.5**	**21**	**6.3**
Other asset backed securities	**17**	**3.6**	**418**	**3.9**	**1,594**	**2.9**	**299**	**5.6**
Other debt securities	**140**	**3.6**	**627**	**4.1**	**444**	**2.9**	**-**	**-**
Total book value	**5,020**	**4.3**	**1,919**	**4.3**	**2,715**	**3.6**	**1,335**	**8.6**

	Maturing within one year		Maturing after one but within five years		Maturing after five but within ten years		Maturing after ten years	
	Amount £m	Yield %	Amount £m	Yield %	Amount £m	Yield %	Amount £m	Yield %
Other securities								
UK Government securities	**31**	**5.8**	**-**	**-**	**-**	**-**	**-**	**-**
Other Government securities	**474**	**3.9**	**1,707**	**3.9**	**1,890**	**5.0**	**1**	**3.7**
Other public sector securities	**59**	**2.9**	**52**	**4.8**	**40**	**5.2**	**-**	**-**
Bank and building society certificates of deposit	**234**	**5.9**	**-**	**-**	**-**	**-**	**-**	**-**
Corporate debt securities	**927**	**3.0**	**5,182**	**3.9**	**964**	**5.0**	**29**	**5.8**
Mortgage backed securities	**-**	**-**	**307**	**4.8**	**495**	**5.1**	**252**	**5.7**
Other asset backed securities	**-**	**-**	**129**	**4.0**	**365**	**5.2**	**98**	**5.8**
Total book value	**1,725**	**3.7**	**7,377**	**4.0**	**3,754**	**5.0**	**380**	**5.7**

Maturity analysis and interest rate sensitivity of loans and advances to customers and banks as at 31 December 2001

The following table analyses the maturity profile and interest rate sensitivity of loans by type on a contractual repayment basis as at 31 December 2001. All amounts are before deduction of provisions and interest in suspense. Demand loans are included in the "maturing in one year or less" category.

	Maturing in one year or less £m	Maturing after one year but not more than five years £m	Maturing after five years £m	Total £m
Domestic:				
Loans and advances to banks	**12,147**	**269**	**321**	**12,737**
Loans and advances to customers:				
Mortgages	**1,364**	**6,693**	**48,521**	**56,578**
Other personal lending	**6,154**	**6,075**	**555**	**12,784**
Financial, business and other services	**4,537**	**1,963**	**2,236**	**8,736**
Lease financing	**638**	**1,651**	**5,263**	**7,552**
Hire purchase	**2,337**	**2,936**	**72**	**5,345**
Others	**8,405**	**4,613**	**4,025**	**17,043**
Total domestic loans	**35,582**	**24,200**	**60,993**	**120,775**
Total foreign loans	**8,814**	**4,418**	**5,690**	**18,922**
Total loans	**44,396**	**28,618**	**66,683**	**139,697**
Of which:				
Fixed interest rate	**29,019**	**14,316**	**28,344**	**71,679**
Variable interest rate	**15,377**	**14,302**	**38,339**	**68,018**

Deposits

The following table shows the details of Lloyds TSB Group's average customer deposits in each of the past three years.

	2001		2000		1999	
	Average balance £m	**Average rate %**	Average balance £m	Average rate %	Average balance £m	Average rate %
Deposits in domestic offices						
Non interest bearing demand deposits	**6,182**	**-**	6,058	-	6,134	-
Interest bearing demand deposits	**18,034**	**0.73**	17,836	1.36	17,050	1.42
Savings deposits	**38,743**	**4.49**	34,468	5.26	34,602	4.06
Time deposits	**15,856**	**5.39**	19,767	5.95	15,395	6.05
Total domestic office deposits	**78,815**	**3.46**	78,129	4.14	73,181	3.52
Deposits in foreign offices						
Non interest bearing demand deposits	**595**	**-**	635	-	578	-
Interest bearing demand deposits	**991**	**2.93**	793	4.04	874	3.09
Savings deposits	**1,842**	**5.16**	1,901	4.58	2,069	3.72
Time deposits	**8,044**	**9.95**	7,632	8.94	7,868	10.92
Total foreign office deposits	**11,472**	**8.05**	10,961	7.31	11,389	8.46
Total average deposits	**90,287**	**4.04**	89,090	4.53	84,570	4.19

Certificates of deposit and other time deposits

The following table gives details of Lloyds TSB Group's certificates of deposit issued and other time deposits as at 31 December 2001 individually in excess of US $100,000 (or equivalent in another currency) by time remaining to maturity.

	3 months or less £m	Over 3 months but within 6 months £m	Over 6 months but within 12 months £m	Over 12 months £m	Total £m
Domestic					
Certificates of deposit	**8,754**	**2,294**	**932**	**20**	**12,000**
Time deposits	**26,087**	**1,902**	**903**	**2,291**	**31,183**
	34,841	**4,196**	**1,835**	**2,311**	**43,183**
Foreign					
Certificates of deposit and other time deposits	**8,875**	**1,370**	**272**	**577**	**11,094**
Total	**43,716**	**5,566**	**2,107**	**2,888**	**54,277**

Short-term borrowings

Short-term borrowings are included within the balance sheet captions "Deposits by banks", "Customer accounts" and "Debt securities in issue" and are not identified separately on the balance sheet. The short-term borrowings of Lloyds TSB Group consist of overdrafts from banks, securities sold under agreements to repurchase, certificates of deposit issued, commercial paper and promissory notes issued and other marketable paper. Securities sold under agreements to repurchase and certificates of deposit issued are the only significant short-term borrowings of Lloyds TSB Group.

The following table gives details of the significant short-term borrowings of Lloyds TSB Group for each of the past three years.

	2001 £m	2000 £m	1999 £m
Liabilities in respect of securities sold under repurchase agreements			
Balance at the period end	**5,516**	4,030	3,933
Average balance for the period	**3,898**	3,000	3,514
Maximum balance during the period	**5,516**	6,158	5,718
Average interest rate during the period	**6.7%**	7.3%	6.6%
Interest rate at the period end	**6.1%**	6.4%	6.3%
Certificates of deposit issued			
Balance at the period end	**17,060**	12,052	8,428
Average balance for the period	**14,643**	11,910	9,471
Maximum balance during the period	**18,160**	13,645	10,853
Average interest rate during the period	**5.0%**	6.3%	8.1%
Interest rate at the period end	**3.7%**	6.3%	5.4%

MANAGEMENT AND EMPLOYEES

Directors and senior management

Lloyds TSB Group plc recognises that good governance is central to achieving the governing objective of maximising shareholder value over time. Lloyds TSB Group plc is led and controlled by a board comprising executive and non-executive directors with wide experience. The appointment of directors is considered by the board and, following the provisions in the articles of association, they must retire by rotation, and may stand for re-election by the shareholders, at least every three years. Executive directors normally retire at age 60 as required by their service agreements. Independent non-executive directors are appointed for a specified term, not exceeding five years, which may be renewed.

The board meets eleven times a year and a programme is prepared and agreed each year, which ensures that the directors are able regularly to review corporate strategy and the operations and results of the business units and to discharge their other duties. The roles of the chairmen, the group chief executive and the board and its governance arrangements are reviewed annually.

The board has a chairman's committee, comprising the chairman, the deputy chairman, the group chief executive and his deputy. The chairman's committee meets to discuss current issues and strategy, examine and test proposals and prepare for board meetings. It also has power to deal with routine matters between board meetings. The board also has audit, nomination and remuneration committees; the chairmen and members of these committees are all non-executive directors.

The chairman, the group chief executive and the group finance director have meetings with representatives of institutional shareholders and all shareholders are encouraged to participate in Lloyds TSB Group's annual general meeting.

Board of directors

Biographical details of the board of directors are given below.

Maarten A van den Bergh ◆
Chairman

Joined Lloyds TSB Group in 2000 as deputy chairman and was appointed chairman in 2001. Joined the Royal Dutch/Shell Group of companies in 1968 and after a number of senior and general management appointments in that group, became group managing director in 1992. Appointed president of Royal Dutch Petroleum Company and vice chairman of the committee of managing directors of the Royal Dutch/Shell Group in 1998 and continued in these roles until 2000. A non-executive director of Royal Dutch Petroleum Company and BT Group. Elected by the shareholders to the board in April 2001. Aged 60.

Alan E Moore CBE ***§**
Deputy Chairman

Joined Lloyds Bank International in 1980. Held a number of senior and general management appointments in that company and in Lloyds Bank before becoming a director of Lloyds Bank in 1989 and deputy chief executive and treasurer in 1994. Following the merger with TSB Group in 1995, became deputy group chief executive of Lloyds TSB Group and then deputy chairman in 1998. Joined Glyn Mills & Co in 1953, holding senior appointments there until his secondment, as director general, to the Bahrain Monetary Agency from 1974 to 1979. Most recently re-elected by the shareholders to the board in April 2000. Aged 65.

Executive directors

Peter B Ellwood CBE
Group Chief Executive

Joined TSB Bank in 1989 as chief executive, retail banking. Appointed a director of TSB Group in 1990 and became group chief executive in 1992. Following the merger with Lloyds Bank in 1995, became deputy group chief executive of Lloyds TSB Group and then group chief executive in 1997. Joined Barclays Bank in 1961 and held a number of senior and general management appointments, including chief executive of Barclaycard from 1985 to 1989. Chairman of the Industrial Society. Former chairman of Visa International. Most recently re-elected by the shareholders to the board in April 2001. Aged 58.

Michael E Fairey
Deputy Group Chief Executive

Joined TSB Group in 1991 and held a number of senior and general management appointments before being appointed to the board in 1997 and deputy group chief executive in 1998. Joined Barclays Bank in 1967 and held a number of senior and general management appointments, including managing director of Barclays Direct Lending Services from 1990 to 1991. Most recently re-elected by the shareholders to the board in April 2002. Aged 53.

Michael D Ross CBE
Deputy Group Chief Executive

Joined the board in 2000. Joined Scottish Widows in 1964 and following a number of senior and general management appointments became group chief executive of that company in 1991. Chairman of the Association of British Insurers. Elected by the shareholders to the board in April 2000. Aged 55.

M Kent Atkinson
Group Finance Director

Joined Bank of London & South America in 1964, which became a Lloyds Bank subsidiary in 1971, and held a number of senior and general management appointments, including positions in Latin America and the Middle East, before being appointed to the board in 1997. A non-executive director of Coca-Cola HBC SA. Most recently re-elected by the shareholders to the board in April 2001. Aged 56.

J Eric Daniels
Group Executive Director, UK Retail Banking

Joined the board in 2001. Served with Citibank from 1975 and held a number of senior and general management appointments in the USA, South America and Europe before becoming chief operating officer of Citibank Consumer Bank in 1998. Following the Citibank/Travelers merger in 1998, he was chairman and chief executive officer of Travelers Life and Annuity until 2000. Chairman and chief executive officer of Zona Financiera from 2000 to 2001. Elected by the shareholders to the board in April 2002. Aged 50.

Archie G Kane
Group Executive Director, IT and Operations

Joined TSB Commercial Holdings in 1986 and held a number of senior and general management appointments in Lloyds TSB Group before being appointed to the board in 2000. After some 10 years in the accountancy profession, joined General Telephone & Electronics Corporation in 1980, serving as finance director in the UK from 1983 to 1985. Chairman of the Council of the Association for Payment Clearing Services. Elected by the shareholders to the board in April 2000. Aged 49.

David P Pritchard
Group Executive Director, Wholesale and International Banking

Joined TSB Group in 1995 as group treasurer. Seconded to the Securities and Investments Board as head of supervision & standards, markets & exchanges, from 1996 to 1998. Appointed to the board in 1998. Held senior and general management appointments with Citicorp from 1978 to 1986 and Royal Bank of Canada from 1986 to 1995. A non-executive director of the London Clearing House. Most recently re-elected by the shareholders to the board in April 2001. Aged 57.

Independent non-executive directors

Ewan Brown CBE FRSE **
Chairman of Lloyds TSB Scotland

A director since 1999. A non-executive director of Lloyds TSB Scotland since 1997. Executive director of Noble Grossart since 1971. Chairman of the Court of Heriot-Watt University and a non-executive director of Stagecoach Holdings. Former Chairman of Dunedin Income Growth Investment Trust. Most recently re-elected by the shareholders to the board in April 2001. Aged 60.

A Clive Butler ✠§▲

A director of TSB Group since 1993. Joined Unilever in 1970 and following a number of senior and general management appointments was appointed an executive director of Unilever in 1992. Most recently re-elected by the shareholders to the board in April 2000. Aged 55.

Sheila M Forbes†

A director of TSB Group since 1994. Chairs the board of governors of Thames Valley University and is a civil service commissioner. Head of personnel for Unigate from 1980 to 1988 and personnel director for Storehouse from 1988 to 1992. Director of human resources at Reed Elsevier (UK) from 1992 to 1996. Most recently re-elected by the shareholders to the board in April 2000. Aged 55.

Gavin J N Gemmell CBE*
Chairman of Scottish Widows

Joined the board on 17 April 2002. A non-executive director of Scottish Widows since 1984. Senior Partner of Baillie Gifford & Co from 1989 to 2001, having held a number of appointments since joining the firm in 1964. A non-executive director of Scottish Enterprise Edinburgh and Lothian. Elected by the shareholders to the board in April 2002. Aged 60.

Christopher S Gibson-Smith†

A director since 1999. Chairman of National Air Traffic Services and a non-executive director of Powergen. Managing director of BP from 1997 to 2001, having held senior and general management appointments in the UK, the USA, Canada and Europe, since joining that company in 1970. Most recently re-elected by the shareholders to the board in April 2002. Aged 56.

DeAnne S Julius CBE†

Joined the board in 2001. Held a number of senior appointments in the UK and the USA with the World Bank, Royal Dutch/Shell Group and British Airways, before membership of the Bank of England Monetary Policy Committee from 1997 to 2001. Chaired HM Treasury's banking services consumer codes review group. A non-executive director of the Bank of England, Serco Group and BP. Elected by the shareholders to the board in April 2002. Aged 53.

Thomas F W McKillop*†

A director since 1999. Joined ICI in 1969 and held a number of senior and general management appointments before the demerger in 1993, when Zeneca was created. Chief executive of Zeneca Pharmaceuticals from 1994 to 1999 and chief executive of AstraZeneca from 1999. Pro-chancellor of Leicester University. Most recently re-elected by the shareholders to the board in April 2002. Aged 59.

The Earl of Selborne KBE FRS§

A director since 1995, having been a director of Lloyds Bank since 1994. Managing director of The Blackmoor Estate, his family business. Chancellor of Southampton University since 1996. President of the Royal Geographical Society from 1997 to 2000. Most recently re-elected by the shareholders to the board in April 2002. Aged 62.

*	Member of the audit committee
**	Chairman of the audit committee
†	Member of the remuneration committee
✠	Chairman of the remuneration committee
§	Member of the nomination committee
◆	Chairman of the nomination committee
▲	Senior independent director

Compensation

Directors' remuneration

The remuneration committee makes recommendations to the board of directors on the executive directors' remuneration and determines, on the board's behalf, specific remuneration packages for the chairman, the deputy chairman and the executive directors. All the non-executive directors receive the minutes of remuneration committee meetings and have the opportunity to comment and have their views taken into account before that committee's decisions are implemented. See also "—Board practices—Remuneration committee".

Executive directors' remuneration policy

Lloyds TSB Group aims to ensure that the executive directors' remuneration arrangements, in line with our overall practice on pay and benefits, are competitive and designed to attract, retain and motivate executive directors of the highest calibre, who are expected to perform to the highest standards. Account is taken of information, from internal and independent sources, on the remuneration for comparable positions in a wide range of FTSE 100 companies.

Reward package. Each year, with the help of external management consultants, the total remuneration package is reviewed, and in 2001 Hay Management Consultants were commissioned by the remuneration committee to conduct the review. In 2001, the package for executive directors comprised the following elements:

Basic salary. The aim is to ensure that the responsibilities of the role are reflected in the salary and that salaries are competitively set in relation to other comparable companies.

Annual incentive. The annual incentive scheme is designed to reflect specific goals linked to the performance of the business. The group chief executive has a maximum incentive opportunity of 100 per cent of his salary, and each of the other executive directors can earn an incentive equal to 75 per cent of their salary. These awards are based on Lloyds TSB Group performance, and for 2001 included the attainment of predetermined targets relating to revenue, business as usual operating profit and economic profit. The remuneration committee reviewed the attainment of targets and agreed the incentive payments.

Medium-term incentive plan

In April 2000, shareholders approved the introduction of a medium-term incentive plan which gives executive directors serving at that time the opportunity of an award, deferred until after the end of 2002 and which is the subject of two performance targets, based on the efficiency ratio and return on equity. For the group chief executive the maximum award will be equal to 50 per cent of aggregate basic salary for the years 2000 - 2002 and for other executive directors, the maximum award will be equal to 25 per cent of aggregate basic salary for these three years.

The two minimum performance targets are a reduction in Lloyds TSB Group's efficiency ratio to 37 per cent by the end of 2002 and a return on equity of 28 per cent by the end of 2002. No payment will be made under the plan unless both these minimum targets are met.

For the year 2001, the efficiency ratio was 49.0 per cent and return on equity was 23.5 per cent.

Share option schemes. Lloyds TSB Group is committed to the governing objective of maximising shareholder value over time. The board believes that the executive share option schemes for senior executives provide an effective method of giving executives the incentive to achieve that objective.

There are two schemes: the approved scheme, under which options over shares with a total market value of up to £30,000 (at the date of grant) may be granted, which has been approved by the UK Inland Revenue (the United Kingdom government department responsible for assessing and collecting United Kingdom tax revenues) and which enjoys certain tax benefits, and the unapproved scheme, which is not subject to such a financial limit and has not been approved by the UK Inland Revenue.

Both schemes are subject to limits relating to the number of shares under option and the price payable on the exercise of options.

In 2001 options were granted to executive directors and senior executives within the limits set by the rules of the schemes and subject to performance conditions set at the time of grant.

In March 2001, options were granted under both schemes subject to performance conditions under which the ranking of Lloyds TSB Group plc, based on total shareholder return (calculated by reference to both dividends and growth in share price over the relevant period), should be in the top 50 companies in the FTSE 100. There must also have been growth in earnings per share at least equal to the aggregate percentage change in the UK retail price index, plus three percentage points for each complete year of the relevant period. The relevant period commenced at the end of the financial year 2000 and continues until the end of the financial year 2003 or, if the conditions have not then been met, at the end of a later financial year.

Under a resolution adopted at the annual general meeting held on 18 April 2001, the rules of the unapproved scheme were amended so that the maximum total price of shares over which options may be granted to an executive in any one year is one and a half times his or her annual base salary (although, in exceptional circumstances, for example on the recruitment of a new executive, this could be increased to four times annual base salary) with a performance multiplier. The maximum performance multiplier is 3.5.

In August 2001, additional options were granted under the amended rules of the unapproved scheme subject to a performance condition linked to the performance of Lloyds TSB Group plc's total shareholder return (calculated by reference to both dividends and growth in share price) relative to a group of seventeen UK and international companies in the banking and insurance sectors, including Lloyds TSB Group plc. The performance condition will be measured over a three year period commencing at the end of the financial year 2000 and continuing until the end of 2003. If the performance condition is not then met it will be measured at the end of 2004. If the condition has not then been met, the options will lapse. A performance multiplier will be applied to calculate the number of shares in respect of which options granted to executive directors will become exercisable, which will be calculated on a sliding scale. If Lloyds TSB Group plc is ranked below median the options will not become exercisable.

Share retention plan. During the year a share retention plan was adopted, specifically to facilitate the recruitment of Mr Daniels, who was based in the USA, as part of the remuneration package considered necessary to attract him to the UK. He is the only participant in the plan and he became eligible to participate in it when he joined Lloyds TSB Group plc on 1 November 2001. On 2 November 2001, an option was granted to him under the plan to acquire 216,763 ordinary shares in Lloyds TSB Group plc (with a value of £1.5 million at the date of grant) for a total price of £1. No further options may be granted to him under the plan.

No new shares will be issued to satisfy the option.

The option is designed to encourage him to remain with Lloyds TSB Group plc and, accordingly, it will normally become exercisable only if he remains as an employee, and has not given notice of resignation, on 31 December 2004, or if he ceases to be an employee before that date in certain circumstances described in his service agreement, in which case it will be exercisable for six months and then lapse. Briefly, these include the following:

- If he were to be entitled to terminate his service agreement without notice by reason of his employer's conduct.
- If he were to be removed as a director or employee otherwise than in accordance with that agreement.
- If there were to be any material diminution of his duties.
- If, within 18 months of his employment, there were to be a change of circumstances of Lloyds TSB Group plc such that there was, in his reasonable judgement, a material and adverse effect on his prospects or a material diminution of his status.

The option may also be exercisable on a takeover or reconstruction of Lloyds TSB Group plc.

The option will lapse if Mr Daniels dies or ceases to be an employee, or gives notice of resignation, before 31 December 2004, except in the circumstances described above.

The number of shares may be adjusted by the board on certain variations in the share capital of Lloyds TSB Group plc.

The benefits conferred by the option are not pensionable and the option is not transferable.

Any change to Mr Daniels' rights in the event of a variation of share capital which would be to his advantage could not generally be made without shareholder approval.

In addition to the executive share option schemes the chairman, deputy chairman and executive directors are entitled to participate in the staff profit sharing and "sharesave" schemes which are open to all UK employees who meet the scheme's eligibility criteria. For 2001 the profit sharing amount was 9 per cent of basic salary.

Pensions. Executive directors are, like most other employees, entitled to pensions based on salary and length of service with Lloyds TSB Group, with a maximum pension of two-thirds of final salary.

Other benefits. Other benefits include the use of a car and medical insurance.

Announcement of appointment of new Group Finance Director

On 30 April 2002 Lloyds TSB Group announced the appointment of Philip Hampton as its Group Finance Director to replace Kent Atkinson, who will remain on the Board as a non-executive director, retiring at the 2003 Annual General Meeting. Mr Hampton will join the Board of Lloyds TSB Group on 1 June 2002.

Directors' emoluments for 2001

	Salaries/fees £000	Other benefits £000	Performance related payments £000	Profit sharing £000	2001 Total £000	2000 £000
Current directors who served during 2001:						
M K Atkinson	**355**	**16**	**185**	**32**	**588**	509
Ewan Brown	**59**				**59**	45
A C Butler	**40**				**40**	33
J E Daniels	**75**	**117**			**192**	-
P B Ellwood	**600**	**23**	**324**	**54**	**1,001**	856
M E Fairey	**415**	**123**	**216**	**37**	**791**	596
S M Forbes	**38**				**38**	34
C S Gibson-Smith	**38**				**38**	30
D S Julius	**9**				**9**	-
A G Kane	**330**	**17**	**171**	**30**	**548**	474
T F W McKillop	**45**				**45**	33
A E Moore	**200**	**11**		**18**	**229**	216
D P Pritchard	**355**	**16**	**185**	**32**	**588**	496
M D Ross	**395**	**15**	**205**	**35**	**650**	468
Lord Selborne	**43**				**43**	42
M A van den Bergh	**355**	**15**		**36**	**406**	68
Former directors who served during 2001:						
Dennis Holt	**220**	**7**			**227**	428
L E Linaker	**12**				**12**	36
Sir Brian Pitman	**120**	**21**		**11**	**152**	488
L M Urquhart	**93**				**93**	70
Former directors who served during 2000						126
	3,797	**381**	**1,286**	**285**	**5,749**	5,048

'Other benefits' include the use of a car, private medical insurance and life insurance cover. Allowances for relocation, housing and legal advice arising from Mr Daniels' service agreement and an additional payment in respect of the contribution to the separate fund relating to Mr Fairey's pension are also included. The separate fund was established to cover pension obligations of those who joined Lloyds TSB Group after 1 June 1989 and who are subject to the Inland Revenue earnings cap relating to pensions, introduced by the Finance Act 1989.

The total for the highest paid director (Mr Fairey), including the gain of £882,000 on the exercise of share options mentioned on page 80, was £1,673,000. (The total for the highest paid director in 2000 (Mr Ellwood) was £856,000). Gains on the exercise of share options arise from increases in the share price since the options were granted. Shareholders who held shares for the same periods would have gained similarly from these increases.

Directors' pensions in 2001

Pension benefits earned by the directors:	(a) Additional pension earned (excluding inflation) during the year ended 31 December 2001 £	(b) Increase in transfer value (excluding inflation) £	(c) Accrued pension entitlement at 31 December 2001 £
M K Atkinson	**27,406**	**416,704**	**227,274**
J E Daniels	**23,750**	**312,504**	**23,750**
P B Ellwood	**39,564**	**698,877**	**336,441**
M E Fairey	**19,888**	**291,267**	**127,183**
Dennis Holt	**19,721**	**256,671**	**189,541**
A G Kane	**18,608**	**235,895**	**118,599**
D P Pritchard	**12,234**	**207,385**	**30,582**
M D Ross	**27,615**	**401,111**	**245,229**

The table above shows the pension earned by the directors during the year and their total entitlement as at 31 December 2001.

The directors are members of one of Lloyds TSB Group's defined benefit schemes. This means that at retirement each director is entitled to receive an annual pension based on salary and service completed at date of leaving.

Column (a) in the table shows the additional pension earned by each director during the year. This is calculated as one year's service at the Scheme's accrual rate multiplied by salary. The calculation is adjusted to take account of inflation and shows the 'real' increase in the entitlement over the year. The figure shown is an annual pension payable from normal retirement date.

Column (b) shows the capital value of the additional pension earned and is intended to illustrate the cost of providing the pension that has accrued over the year. The figure shown is the amount that would be available to transfer to another pension scheme in respect of the one year of accrual if the director left service.

Column (c) shows the total pension that the director has accrued during his membership of the pension scheme. This is the pension to which he would be entitled if he left service at the year-end. This figure is calculated using the relevant scheme's accrual rate, service to the year-end and pensionable salary at that date.

The benefits disclosed in the table are those provided in accordance with the rules of each scheme and for which the employer is responsible for funding. They do not take into account any voluntary provision that the individual director may be making.

The pension provisions in Mr Pritchard's service agreement have been changed, with effect from 1 January 2000, to defined benefit arrangements. He therefore waived entitlement to the £63,045 allocation to the defined contribution section of the separate fund.

Board practices

Audit committee

The audit committee comprises Mr Brown (chairman), Dr McKillop, Mr Moore and Mr Gemmell (who joined the committee when Mr Urquhart retired on 17 April 2002). The audit committee's duties include considering the appointment, resignation or dismissal of the external auditors and their independence and objectivity. The audit committee also reviews all financial statements published in the name of the board and the quality and acceptability of the related accounting policies, practices and financial reporting disclosures; the scope of work of the group risk management division, where duties include internal audit and advising on and monitoring compliance with financial services legislation and regulations, and the adequacy of its resources; the results of the external audit, its cost effectiveness and the audit fee; communications from the external auditors on audit planning and findings on material weaknesses in accounting and internal control systems; the major findings of any relevant internal investigations; and its own efficiency and effectiveness.

Nomination committee

The nomination committee, comprising Mr van den Bergh (chairman), Mr Moore, Mr Butler and The Earl of Selborne, considers potential candidates for appointment as directors and makes recommendations to the board. The group chief executive is invited to attend all meetings of the committee. The committee also makes recommendations to the board concerning the following:

- the re-appointment of any non-executive director by the board at the conclusion of his or her specified term;
- the re-election of any director by the shareholders under the retirement by rotation provisions of the articles of association;
- any matters relating to the continuation in office as a director of any director at any time; and
- the appointment of any director to executive or other office, other than to the positions of chairman and group chief executive where special arrangements apply.

Remuneration committee

The remuneration committee, comprising Mr Butler (chairman), Miss Forbes, Dr Gibson-Smith, Dr Julius and Dr McKillop, reviews and makes recommendations to the board on the framework of executive directors' remuneration and its cost. It also determines, on the board's behalf, specific remuneration packages for each of the chairman, the deputy chairman, the executive directors, and any employee of Lloyds TSB Group plc or any subsidiary whose salary exceeds £300,000 per annum. In addition, it determines proposals for the granting of executive share options.

All the non-executive directors receive the minutes of remuneration committee meetings and have the opportunity to comment and have their views taken into account before that committee's decisions are implemented.

Following the provisions in the articles of association, the shareholders agree an amount of remuneration that may be paid to the non-executive directors in any one year. The chairman's committee makes recommendations to the board on the non-executive directors' remuneration and the board approves the amount within the limit agreed by the shareholders.

Directors' service agreements

Mr Atkinson, Mr Ellwood, Mr Fairey, Mr Kane and Mr Pritchard each has a service agreement which Lloyds TSB Group plc may terminate by giving one year's notice. In connection with the arrangements for the transfer of the business of Scottish Widows to Lloyds TSB Group in March 2000, Mr Ross's service agreement provides for two years' notice for the first two years of employment with the Group, which ended in March 2002. After that, the notice period will decrease by one month for each month of service. In March 2003 therefore, Mr Ross's agreement will provide for one year's notice. Mr Daniels' service agreement provides for two years' notice for the first eighteen months; after that the notice period reduces to one year. None of the other directors has a service agreement with a notice period of one year or more.

The remuneration committee has considered the provisions of the UK listing authority's corporate governance code relating to compensation in the event of early termination of directors' service agreements and a departing director's duty to mitigate loss. The committee reviewed the wording of the executive directors' agreements and felt that, as the notice period did not exceed one year with the exception of Mr Ross and Mr Daniels as mentioned above, there was no need to provide explicitly for compensation payments on early termination. Therefore, none of the directors' service agreements contain provisions for predetermined compensation in the event of the termination of employment in excess of an amount equivalent to the remuneration payable over the notice period, although certain share options may vest upon termination without the need to satisfy the performance conditions. The service agreements provide for a retirement pension provision for each relevant director with a pension upon retirement.

Employees

As at 31 December 2001, Lloyds TSB Group employed 81,400 people (full-time equivalent), compared with 77,540 at 31 December 2000. At 31 December 2001, 69,918 employees were located in the UK, 5,421 in the Americas, 4,413 in New Zealand, and 1,648 in the rest of the world. At the same date, 51,450 people were employed in UK Retail Banking and Mortgages, 6,378 in Insurance and Investments, 21,285 in Wholesale Markets and International Banking, and 2,287 in other functions.

Lloyds TSB Group is committed to employment policies which follow best practice, based on equal opportunities for all employees irrespective of sex, race, national origin, religion, colour, disability, sexual orientation, age or marital status.

In the UK, Lloyds TSB Group supports Opportunity Now and Race for Opportunity, campaigns to improve opportunities for women and ethnic minorities in the workplace. Lloyds TSB Group is a member of the Employers' Forum on Disability in support of employment of people with disabilities. This recognises the need for ensuring fair employment practices in recruitment and selection, and the retention and career development of disabled staff.

Employees are kept closely involved in major changes affecting them through a variety of means. In the UK, Lloyds TSB Group has long standing arrangements with finance sector unions covering both collective and individual representation of staff. Lloyds TSB Group has gone through substantial changes in recent years; adjusting for the effect of acquisitions and disposals underlying staff numbers have reduced by 10,809 since 1995. However, during this time no material strikes or work stoppages have occurred. Additionally staff are kept closely involved in major changes affecting them through such measures as regular briefings, internal communications and opinion surveys as a way of ensuring the views of employees are taken into account in reaching decisions.

Schemes offering share options or the acquisition of shares are available for most staff to encourage their financial involvement in Lloyds TSB Group. Further details are given in "—Compensation—Long-term rewards—Share option schemes".

Share ownership

Directors' interests

The directors' interests in ordinary shares in Lloyds TSB Group plc were:

Shares:	**At 31 December 2001**	At 1 January 2001 (or date of appointment if later)		**At 31 December 2001**	At 1 January 2001 (or date of appointment if later)
M K Atkinson	**124,815**	31,077	A G Kane	**80,120**	78,865
Ewan Brown	**3,402**	3,274	T F W McKillop	**1,000**	1,000
A C Butler	**2,000**	2,000	A E Moore	**1,107,396**	1,043,196
J E Daniels	**1,000**	-	D P Pritchard	**3,367**	2,151
P B Ellwood	**178,751**	177,501	M D Ross	**2,500**	2,500
M E Fairey	**74,158**	72,218	Lord Selborne	**3,372**	3,372
S M Forbes	**2,000**	2,000	L M Urquhart	**2,226**	2,124
C S Gibson-Smith	**3,151**	3,151	M A van den Bergh	**4,000**	4,000
D S Julius	**2,000**	-			

Options to acquire shares of Lloyds TSB Group plc:

		At 1 January 2001 (or date of appointment if later)	Granted during the year	Exercised during the year	At 31 December 2001	Weighted average exercise price at 31 December 2001	Exercise price of share options granted or exercised	Market price at date of exercise	Amount of gain on exercise[2] 2001 £000	2000 £000
M K Atkinson	Exercisable	253,056			147,600	344p				
	Not exercisable	183,377			345,155	710p				
			38,583				655p			
			127,131				733p			
			1,245				591p			
				54,080			129.81p	664p	289	
				27,040			137.94p	664p	142	
				16,224			137.2p	664p	85	
				8,112			197.49p	664p	38	
				5,181			253p	706p	23	
J E Daniels	Exercisable	-			-					
	Not exercisable	-	907,780		907,780	694p	694p			
P B Ellwood[1]	Exercisable	321,340			321,340	358p				
	Not exercisable	311,224			441,725	696p				
			130,501				655p			
M E Fairey[1]	Exercisable	224,556			54,000	510p				
	Not exercisable	203,253			394,138	709p				
			42,884				655p			
			148,618				733p			
				138,556			242.5p	717p	754	
				32,000			321p	717p	127	
				617			632p	730.5p	1	
A G Kane[1]	Exercisable	171,547			171,547	312p				
	Not exercisable	157,784			310,721	715p				
			34,759				655p			
			118,178				733p			20
A E Moore	Exercisable	59,439			-					
	Not exercisable	3,545			-					
				3,545			253p	731p	17	
				59,439			250.37p	694p	264	
D P Pritchard	Exercisable	-			-					
	Not exercisable	176,591			340,096	707p				
			36,374				655p			
			127,131				733p			
M D Ross	Exercisable	-			-					
	Not exercisable	268,941			440,549	615p				
			30,152				655p			
			141,456				733p			
Gain made by Dennis Holt, who left the board on 31 August 2001									53	7
									1,793	27
Share retention plan										
J E Daniels	Not exercisable	-	216,763	-	216,763					

Options were not exercisable because they had not been held for the period required by the relevant scheme or the performance conditions had not been met.

Options may be exercised between 2002 and 2011.

(1) These directors will receive additional Lloyds TSB Group shares on exercising share options held on 28 December 1995. These shares will compensate them for the special dividend of 68.3p per share which was paid to former TSB Group shareholders following the merger with Lloyds Bank, but which was not paid to option holders. In that regard Mr Fairey received 13,511 additional shares when he exercised the 138,556 share options shown above. Following that exercise, Mr Fairey no longer held any share options to which these arrangements apply.

(2) This is the difference between the market price of the shares on the day on which the share option was exercised and the price paid for the shares, and includes the value of shares issued to compensate directors for the special dividend mentioned above.

The market price for a share in Lloyds TSB Group plc at 31 December 2001 was 746p. The range of prices between 1 January 2001 and 31 December 2001 was 590p to 772p.

None of the other directors at 31 December 2001 had options to acquire shares in Lloyds TSB Group plc or its subsidiaries.

Scottish Widows loan capital

At the end of the year, Mr Ross had an interest in £43,194 of Scottish Widows Group Limited floating rate unsecured loan notes 2008 (2000: £57,394).

Directors' non-beneficial interests

Directors had non-beneficial interests as follows:

1. Mr Atkinson, Mr Daniels, Mr Ellwood, Mr Fairey, Mr Kane, Mr Moore, Mr Pritchard, Mr Ross and Mr van den Bergh, together with some 73,000 other employees, were potential beneficiaries in the 2,417,245 and 1,952,179 shares held at the end of the year by the Lloyds TSB qualifying employee share ownership trust and the Lloyds TSB Group employee share ownership trust, respectively. 749,896 and 3,100,000 shares, respectively, were held by these trusts at the beginning of the year. These holdings were 1,719,373 and 1,939,013 respectively on 14 February 2002. In addition, the TSB Group Employee Trust held 66,536 shares at the beginning of the year and none at the end of the year.

2. At the beginning and end of the year, Mr Ellwood also had a non-beneficial interest in 7,000 shares held in another trust.

None of those who were directors at the end of the year had any other interest in the capital of Lloyds TSB Group plc or its subsidiaries.

MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

Major shareholders

Lloyds TSB Group plc does not know of any shareholder owning beneficially, directly or indirectly, five per cent or more of the shares of Lloyds TSB Group plc, or of any shareholder having more than five per cent of the voting rights.

At 31 December 2001, those who were directors of Lloyds TSB Group plc on that day beneficially owned the following ordinary shares, not including options:

Title of Class	Identity of Person or Group	Amount Owned	Per cent of Class
Ordinary shares, nominal value 25 pence each	Directors (17 persons)	1,595,258	0.03%

In addition, those directors held, as at 31 December 2001, options to acquire 4,091,414 shares, all of which were granted pursuant to the executive share option schemes, sharesave share option schemes and share retention plan.

Lloyds TSB Group plc is not owned or controlled directly or indirectly by another corporation or by any government and Lloyds TSB Group plc is unaware of any arrangements which might result in a change in control.

Related party transactions

Lloyds TSB Group, as at 31 December 2001, had related party transactions with seven directors and twenty eight officers. See Note 42 to the Consolidated Financial Statements. The transactions in question were made in the ordinary course of business, were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons, and did not involve more than the normal risk of collectibility or present other unfavourable features.

REGULATION

European Union Directives

European Union ("EU") Directives, which are required to be implemented in member states through national legislation, have a strong influence over the framework for supervision and regulation of banking and financial services in the UK. The banking Directives aim to harmonise banking regulation and supervision throughout member states by setting out minimum standards in key areas such as capital adequacy and deposit and investor compensation schemes. The UK has now largely implemented these minimum requirements. The Directives also require member states to give "mutual recognition" to each other's standards of regulation. Under the Second Banking Co-ordination Directive the concept of mutual recognition has also been extended to create the "passport" concept: this gives a bank which has been authorised in its "home" state the freedom to establish branches in, and to provide cross-border services into, other member states without the need for additional local authorisation.

Whilst credit institutions such as those in Lloyds TSB Group are primarily regulated in their home state by a local regulator, the EU Directives prescribe minimum criteria for the authorisation of credit institutions and the prudential supervision applicable to them. Investment firms are subject to a similar regulatory environment and can obtain a "passport" under the Investment Services Directive. Despite the application of the "passports" a member state can impose certain requirements on the conduct of banking and investment activities in its boundaries (including conduct of business rules).

Credit institutions and investment firms are required to make adequate capital provisions for risks entered into: the Directives set out the deemed quality and acceptable relative proportions of various types of capital. The Directives also regulate permissible counterparty exposures, provide for the supervision of consolidated financial groups' capital adequacy requirements and define permissible exposures to individual or linked counterparties.

During 2001 the Basel Committee on Banking Supervision has issued further consultation documents with the purpose of replacing the Capital Accord of 1988 with a new capital adequacy framework. The outcome of these consultations is likely to result in comprehensive changes to the capital adequacy regulations applicable to Lloyds TSB Group. The proposals for the new framework cover three main areas:

- Minimum capital requirements and methodologies for allocation of regulatory capital for credit and other risks.
- A supervisory review process, including the setting of capital ratios by bank supervisors.
- Improvement in the stability of the financial system by reliable and timely disclosure of risk information.

It is not expected that the eventual framework will be implemented before 2005, at the earliest.

UK regulations

In the UK, the fundamental concepts of constitutional issues, company registration and the format and production of company annual reports and accounts are controlled by the UK Companies Act 1985. In addition, as a company listed on the London Stock Exchange Limited, Lloyds TSB Group plc is obliged to comply with a code of practice known as the Combined Code regarding corporate governance. As part of the continuing obligations of Lloyds TSB Group under the rules of that Exchange it must disclose, through the Exchange, major developments in its sphere of activity which may lead to substantial movement in the price of its securities listed on that Exchange.

The undertaking of certain financial activities in the UK subjects the relevant entity to further regulatory regimes. The UK government has recently implemented major changes to the supervisory regimes affecting financial services businesses. In accordance with the provisions of the Financial Services and Markets Act 2000 ('FSMA') on 1 December 2001, the Financial Services Authority ('FSA') completed the process of assuming responsibility for the regulation and oversight of all financial services activity in the UK, including investment in securities and long term insurance contracts.

Any individual who carries out what is known as a 'controlled function' in a financial services firm now needs to be approved by the FSA. Controlled functions include those of directors, the finance officer, risk management, compliance, anti-money laundering and internal audit. The FSA have established a Code of Practice for Approved Persons; shortfalls in their conduct can lead to sanctions against the individual by the FSA.

The most significant regulatory regimes relevant to Lloyds TSB Group are discussed below.

Banking

Primary responsibility for the prudential supervision of UK banks was transferred from the Bank of England to the FSA under the Bank of England Act 1998. The Bank of England retained its monetary policy role and responsibility for the overall stability of the financial system. The FSA carries out its supervision of the UK banking sector through the collection of information from a series of periodic statistical and prudential returns covering both sterling and non-sterling operations, meetings with the senior management of the banks and reports obtained from skilled persons. The regular reports include operating statements and returns covering (amongst other things) capital adequacy, liquidity, large single exposures and large exposures to related borrowers, lendings by industry sector and geographical area, maturity analyses and foreign exchange activities. A risk-based approach for the supervision of all banks was introduced in 1998; under this approach, the starting point for the FSA's supervision of a bank is based on a systematic analysis of that bank's risk profile. Having determined the level of inherent risk in the bank a minimum capital adequacy requirement is established, which the bank is required to meet at all times.

UK banks are required to maintain, in interest-free accounts at the Bank of England, a non-operational cash balance calculated as a percentage of eligible liabilities, which are, broadly, a measure of the sterling resources available to the banks for lending purposes.

Depositors in the UK are provided with protection for their deposits with authorised institutions. Depositors with a failed institution are entitled to receive 100 per cent of the first £2,000 and 90 per cent of the next £33,000 of their protected deposits from the UK deposit protection fund, subject to a maximum amount of £31,700, including both principal and accrued interest. All authorised institutions are required to be members of the deposit protection scheme and are subject to a levy in proportion to their deposit base, which includes deposits in sterling, other European Economic Area currencies and euro, to finance the deposit protection fund.

The Banking Code (the "Code") is a voluntary code agreed by UK banks and building societies which became effective in 1992, with subsequent revisions in 1994, 1997 and 2000, and which has been adopted by Lloyds TSB Group. The Code defines the responsibilities of the banks and building societies to their personal customers in connection with the operation of their accounts and sets out minimum standards of service that these customers can expect from institutions which subscribe to the Code. Compliance with the Code is monitored by the Banking Code Standards Board.

The Business Banking Code is a voluntary code agreed by UK banks which became effective at the end of March 2002 and which has been adopted by Lloyds TSB Group. The Business Banking Code defines the responsibilities of the banks to their smaller business customers in connection with UK operation of their accounts and sets out minimum standards of service that such customers can expect from institutions which subscribe to the Business Banking Code. Compliance with the Business Banking Code is monitored by the Banking Code Standards Board.

Investment business

The FSA is responsible for the authorisation and supervision of those firms which are engaged in investment business as defined in the FSMA. As part of the authorisation process, the FSA reviews applicants to ensure that they satisfy the necessary criteria including honesty, competence and financial soundness, to engage in regulated activity. Lloyds TSB Group's investment businesses became authorised by the FSA through being "grandfathered" as having been authorised under previous legislation to carry on investment business.

The FSA's regulatory approach aims to focus and reinforce the responsibility of the management of each authorised person to ensure that it takes reasonable care to organise and control its affairs responsibly and effectively and that it develops and maintains adequate risk management systems. The FSA Handbook of Rules and Guidance ('the Handbook') sets out the principles of market conduct and the rules to which investment businesses are required to adhere.

Under the FSMA a compulsory single, industry wide, investor's compensation scheme, the Financial Services Compensation Scheme has been set up. The Scheme is financed by a levy system and the FSMA allows for the establishment of different funds for different kinds of business and for different maximum amounts of claim. The limit for investment business compensation is £48,000.

"Listed money market institutions" are regulated by the FSA which expects such entities to observe the "London Code of Conduct" and other regulations contained in the paper entitled "The Regulation of the Wholesale Cash and OTC Derivatives Markets" which was originally issued by the Bank of England to regulate the operation of the wholesale money markets. Lloyds TSB Bank has been granted listed money market institution status.

Insurance

The insurance companies within the Lloyds TSB Group became authorised by the FSA through being "grandfathered" as having been authorised under previous legislation. While the authorisation and supervision of insurance companies is subject to the same FSA regulatory approach as other investment companies, rules exist to:

- Restrict the carrying out of insurance business in the UK to persons authorised by the FSA.
- Require the separation of the long-term business assets of an insurance company from the assets attributable to shareholders.
- Require, and define the role of, an appointed actuary for each insurance company carrying out long-term business in the UK. The appointed actuary is responsible for monitoring the financial health of the company.

- Require the directors to prepare an annual report on the solvency position of the insurer. The valuation basis for assets is defined and there are limits on the extent to which certain categories of assets are allowable in determining the solvency position. The appointed actuary must calculate the value of long-term liabilities and details of his investigations are contained in the directors' solvency report. In determining the value of long-term liabilities the appointed actuary must use a method and valuation basis permitted by the Handbook.

- Require the maintenance of a prescribed solvency margin at all times. The amount of the solvency margin depends upon the amount and type of business an insurance company writes. Failure to maintain the required solvency margin gives the regulator grounds for intervention.

- Prevent an insurer, and its parent, from declaring a dividend when long-term business assets do not exceed long-term liabilities. Furthermore, surplus assets in the long-term fund can only be transferred out once the appointed actuary has completed an investigation.

- Prevent the use of the long-term business assets for purposes other than supporting long-term business.

The Financial Services Compensation Scheme also applies to insurance business written by an insurer authorised by the FSA or by the UK branch of an EEA firm carrying on "home state regulated activity". The limit of compensation in respect of long-term insurance contracts is 90 per cent of the value of the contact and is unlimited.

Other relevant legislation and regulation

The Consumer Credit Act 1974 regulates both brokerage and lending activities in the provision of personal secured and unsecured lending. The Data Protection Acts 1984 and 1998 regulate, among other things, the retention and use of data relating to individual customers. The Unfair Terms in Consumer Contracts Regulations 1994 came into force in July 1995. These Regulations together with the Unfair Contract Terms Act 1977 apply to certain contracts for goods and services entered into with customers. The main effect of the Regulations is that a contractual term covered by the Regulations which is "unfair" will not be enforceable against a consumer. These Regulations apply, among other things, to mortgages and related products and services.

The Mortgage Code is a voluntary code followed by lenders and mortgage intermediaries dealing with customers in the UK who want a loan secured on their home. It sets standards of good mortgage practice, which are followed as a minimum standard by those subscribing to it. Compliance with the Mortgage Code is monitored by the Mortgage Code Compliance Board.

Rest of the world

Lloyds TSB Group operates in many countries around the world and its overseas branches, subsidiaries and associate companies are subject to reporting and reserve requirements and controls imposed by the relevant central banks and regulatory authorities.

LISTING INFORMATION

The information in this section has been extracted from publicly available documents from various sources, including officially prepared materials from the London Stock Exchange, and has not been prepared or independently verified by us.

The ordinary shares of Lloyds TSB Group plc are listed and traded on the London Stock Exchange under the symbol "LLOY.L". The prices for shares as quoted in the official list of the London Stock Exchange are in pounds sterling. The following table shows the reported high and low closing prices for the ordinary shares on the London Stock Exchange.

	Price per share (in pence)	
	High	**Low**
Annual prices:		
2001	**772.0**	**590.0**
2000	774.5	517.0
1999	1,060.0	725.0
1998	1,070.5	575.5
1997	850.5	428.0
Quarterly prices:		
2002:		
First quarter	**775.0**	**680.0**
2001:		
Fourth quarter	**757.0**	**644.0**
Third quarter	**742.0**	**590.0**
Second quarter	**772.0**	**684.5**
First quarter	**751.0**	**610.0**
2000:		
Fourth quarter	725.0	614.5
Third quarter	660.0	576.5
Second quarter	742.5	598.0
First quarter	774.5	517.0
Monthly prices:		
April 2002	789.0	708.0
March 2002	742.0	698.0
February 2002	775.0	680.0
January 2002	765.0	710.0
December 2001	754.0	705.0
November 2001	757.0	692.0

On 1 May 2002, the closing price of shares on the London Stock Exchange was 781 pence, equivalent to $11.42 per share translated at the Noon Buying Rate of $1.4621 per £1.00 on 1 May 2002.

Lloyds TSB Group plc's ADRs have been traded on the over-the-counter market in the US under the symbol "LLDTY" since March 2000. Since 27 November 2001 Lloyds TSB Group plc ADSs have been listed on The New York Stock Exchange under the symbol "LYG". The prices for Lloyds TSB Group plc's ADRs, as quoted below are in US dollars. Each ADS represents four ordinary shares. The following table shows the reported high and low closing prices for the ADRs in the over-the-counter market in the US.

	Price per ADR (in US dollars)	
	High	**Low**
Annual prices:		
2001 (to 26 November 2001)	**46.00**	**34.75**
2000	45.27	33.50
Quarterly prices:		
2001:		
Fourth quarter (to 26 November 2001)	**43.88**	**38.25**
Third quarter	**44.00**	**35.50**
Second quarter	**43.94**	**38.94**
First quarter	**46.00**	**34.75**
2000:		
Fourth quarter	43.75	35.75
Third quarter	38.75	33.50
Second quarter	45.27	37.53
Monthly prices:		
November 2001 (to 26 November 2001)	43.88	40.50
October 2001	42.38	38.25
September 2001	42.25	35.50
August 2001	44.00	40.52
July 2001	41.07	36.86
June 2001	41.66	38.94

The following table shows the reported high and low closing prices for ADSs on the New York Stock Exchange:

	Price per ADS (in US dollars)	
	High	**Low**
Annual prices:		
2001 (from 27 November 2001)	**45.00**	**40.75**
Quarterly prices:		
2002:		
First quarter	**45.35**	**39.10**
2001:		
Fourth quarter (from 27 November 2001)	**45.00**	**40.75**
Monthly prices:		
April 2002	46.51	40.85
March 2002	43.10	40.50
February 2002	45.35	39.10
January 2002	44.10	41.50
December 2001	45.00	40.75
November 2001 (from 27 November 2001)	42.10	41.25

On 1 May 2002, the closing price of ADSs on the New York Stock Exchange was $45.95.

DIVIDENDS

Lloyds TSB Group plc has paid an interim and final dividend each year since the merger of TSB Group plc and Lloyds Bank Plc in 1995. Dividends are paid in May and October and the record date for purposes of determining the shareholders who will be entitled to a dividend is approximately 10 weeks before the dividend payment date. TSB Group plc, which was re-named Lloyds TSB Group plc after the merger, has paid an interim and final dividend every year after its flotation on the London Stock Exchange in September 1986, with the exception of 1986 when no final dividend was paid. Lloyds TSB Bank has paid a dividend every year since its incorporation as Lloyds Banking Company Limited in 1865.

Lloyds TSB Group plc's ability to pay dividends is restricted under UK company law. Dividends may only be paid if distributable profits are available for that purpose. In the case of a public limited company, a dividend may only be paid if the amount of net assets is not less than the aggregate of the called-up share capital and undistributable reserves and if the payment of the dividend will not reduce the amount of the net assets to less than that aggregate. In addition, a company cannot pay a dividend if any of its UK insurance subsidiaries is insolvent on a regulatory valuation basis or in the case of regulated entities, if the payment of a dividend results in regulatory capital requirements not being met. Similar restrictions exist over the ability of Lloyds TSB Group plc's subsidiary companies to pay dividends to their immediate parent companies. Furthermore, in the case of Lloyds TSB Group plc, dividends may only be paid if sufficient distributable profits are available for distributions due in the financial year on certain preferred securities. The board of directors has the discretion to decide whether to pay a dividend and the amount of any dividend. Dividends are paid through The Bank of New York which acts as paying and transfer agent for the American Depositary Shares.

The table below sets out the interim and final dividends which were declared in respect of the ordinary shares for fiscal years 1996 through 2001. The sterling amounts have been converted into US dollars at the Noon Buying Rate in effect on each payment date.

	Interim dividend per share £	**Interim dividend per share $**	**Final dividend per share £**	**Final dividend per share $**
1997	0.053	0.086	0.119	0.198
1998	0.067	0.114	0.155	0.253
1999	0.081	0.134	0.185	0.289
2000	0.093	0.136	0.213	0.306
2001	**0.102**	**0.149**	**0.235**	**0.344**

There are no UK governmental laws, decrees or regulations that affect the remittance of dividends or other shareholder payments to non-residents of the UK who hold shares of Lloyds TSB Group plc.

MEMORANDUM AND ARTICLES OF ASSOCIATION OF LLOYDS TSB GROUP PLC

A summary of the material provisions of Lloyds TSB Group plc's memorandum and articles of association was incorporated into Lloyds TSB Group plc's registration statement filed with the SEC on 25 September 2001 and is therefore incorporated into this annual report by reference to that statement.

EXCHANGE CONTROLS

There are no UK laws, decrees or regulations that restrict Lloyds TSB Group plc's export or import of capital, including the availability of cash and cash equivalents for use by Lloyds TSB Group, or that affect the remittance of dividends or other shareholder payments to non-UK holders of Lloyds TSB Group plc shares, except as otherwise set out in "Taxation".

TAXATION

UK Taxation

The following discussion is intended only as a general guide to current UK tax legislation, what is understood to be current UK Inland Revenue practice and the terms of the current UK/US income tax treaty (the "Treaty") and the New Treaty (as defined below), all of which are subject to change at any time, possibly with retroactive effect. On 24 July, 2001, the UK and the US entered into a new income tax treaty (the "New Treaty"), which has still to be ratified by both the UK Parliament and the US Senate before its provisions enter into force. It is not known when these procedures will be completed. The UK Inland Revenue is the UK government department responsible for assessing and collecting UK tax revenues. The discussion is intended as a general guide and only applies to persons who are the beneficial owners of their ordinary shares or ADSs. References below to a US Holder are to that term as defined, and subject to the exclusions described in the introduction, below under "—US Federal Income Tax Considerations". It may not apply to certain shareholders or ADS holders, such as dealers in securities. Any person who is in any doubt as to his tax position should consult his own professional adviser.

Taxation of chargeable gains

UK residents

A disposal (or deemed disposal) of ordinary shares or ADSs by a shareholder or holder of ADSs resident or (in the case of an individual) ordinarily resident for tax purposes in the UK may, depending on the shareholder's or ADS holder's particular circumstances, and subject to any available exemption or relief, give rise to a chargeable gain or an allowable loss for the purposes of UK taxation on chargeable gains.

Persons, other than US Holders, temporarily non-resident in the UK

A shareholder or ADS holder who is an individual and who has, on or after 17 March 1998, ceased to be resident and ordinarily resident for tax purposes in the UK for a period of less than five years of assessment and who disposes of ordinary shares or ADSs during that period may be liable, on return to the UK, to UK taxation on chargeable gains arising during the period of absence, subject to any available exemption or relief.

US Holders

Subject to the provisions set out in the next paragraph in relation to temporary non-residents, US Holders will not normally be liable for UK tax on chargeable gains unless they carry on a trade, profession or vocation in the UK through a branch or agency and the ordinary shares or ADSs are or have been used or held by or for the purposes of the branch or agency, in which case such US Holder might, depending on individual circumstances, be liable to UK tax on chargeable gains on any disposition of ordinary shares or ADSs. A US Holder who is only temporarily not resident in the UK may, under anti-avoidance legislation, still be liable for UK tax on chargeable gains realised, subject to any available exemption or relief.

A US Holder who is an individual and who has, on or after 17 March 1998, ceased to be resident or ordinarily resident for tax purposes in the UK for a period of less than five years of assessment and who disposes of ordinary shares or ADSs during that period may be liable, on return to the UK, to UK taxation on chargeable gains arising during the period of absence, subject to any available exemption or relief.

Other non-UK resident persons

Subject to the provisions set out above under "—Persons, other than US Holders, temporarily non-resident in the UK", shareholders or ADS holders who are neither resident nor ordinarily resident in the UK will not normally be liable for UK tax on chargeable gains unless they carry on a trade, profession or vocation in the UK through a branch or agency and the ordinary shares or ADSs are or have been used or held by or for the purposes of the branch or agency, in which case such shareholder or ADS holder might, depending on individual circumstances, be liable to UK tax on chargeable gains on any disposition of ordinary shares or ADSs. An individual holder of ordinary shares or ADSs who is only temporarily not resident in the UK may, under anti-avoidance legislation, still be liable for UK tax on chargeable gains realised, subject to any available exemption or relief.

Taxation of dividends

UK residents

Lloyds TSB Group will not be required to withhold tax at source when paying a dividend on the ordinary shares or ADSs.

An individual shareholder or ADS holder who is resident in the UK for tax purposes will be entitled to a tax credit in respect of any dividend received from us and will be taxable on the gross dividend, which is the aggregate of the dividend received and related tax credit. The value of the tax credit will be equal to one-ninth of the dividend received (and, therefore, 10 per cent of the gross dividend). The gross dividend will be treated as an individual's marginal income. The tax credit will, however, be treated as discharging the individual's liability to income tax in respect of the gross dividend, unless and except to the extent that the gross dividend falls above the threshold for the higher rate of income tax. A UK resident individual shareholder or ADS holder who is liable to income tax at the higher rate will be subject to tax at the rate applicable to dividends for such shareholders or ADS holders (currently 32.5 per cent) on the gross dividend. The tax credit will be set against but will not fully discharge such shareholder's or ADS holder's tax liability on the gross dividend and he will have to pay additional tax equal to 22.5 per cent of the gross dividend, being 25 per cent of the dividend received, to the extent that such sum, when treated as marginal income, falls above the threshold for the higher rate of income tax.

There will be no payment of the tax credit or any part of it to an individual whose liability to income tax on the dividend and the related tax credit is less than the tax credit, except where the individual holds the relevant shares through a personal equity plan or individual savings account and the dividend is received into such plan or account on or before 5 April 2004.

UK resident shareholders or ADS holders which are not liable to UK tax on dividends, including pension funds and charities, will not be entitled to reclaim the tax credits in respect of dividends although charities will be entitled to a payment by the UK Inland Revenue of a specified proportion of any dividend paid by us to the charities on or before 5 April 2004, that proportion declining on a year by year basis.

Subject to an exception for some insurance companies with overseas business, UK resident corporate shareholders or ADS holders will generally not be subject to corporation tax in respect of dividends received from us, but will not be entitled to the payment of any tax credit with respect to the dividends.

US Holders

Lloyds TSB Group will not be required to withhold tax at source when paying a dividend on the ordinary shares or ADSs to a US Holder.

A US Holder is entitled under the terms of the Treaty, in principle, to receive a payment from the UK Inland Revenue in respect of a dividend from us in an amount equal to the tax credit (the "Tax Credit Amount") to which a UK resident individual is generally entitled in respect of the dividend. This is an amount equal to one-ninth of the dividend received. However, that entitlement is subject to a deduction withheld under the Treaty. The amount of such deduction will equal the Tax Credit Amount, i.e. one-ninth of the dividend. Therefore, a US Holder will not be able to claim any payment from the UK Inland Revenue in respect of a dividend from us.

When the New Treaty comes into effect (and the Treaty ceases to apply), a US Holder will not be entitled to claim a payment from the UK Inland Revenue in respect of a dividend from us an amount equal to the Tax Credit Amount because the New Treaty does not provide for that entitlement.

Other non-UK resident persons

Lloyds TSB Group will not be required to withhold tax at source when paying a dividend on the ordinary shares or ADSs to a holder, other than a US Holder, who is not resident for tax purposes in the UK.

Holders of ordinary shares or ADSs, other than US Holders, who are not resident for tax purposes in the UK and who receive a dividend from us will not have any further UK tax to pay in respect of the dividend, but will not normally be able to claim any additional payment in respect of the dividend from the UK Inland Revenue under any applicable double tax treaty.

Stamp duty and stamp duty reserve tax

UK residents, US Holders and other non-UK resident persons

Any conveyance or transfer on sale of ordinary shares (whether effected using the CREST settlement system or not) will be subject to UK stamp duty or stamp duty reserve tax ("SDRT"). The transfer on sale of ordinary shares will be liable to ad valorem UK stamp duty or SDRT, generally at the rate of 0.5 per cent of the consideration paid (rounded up to the next multiple of £5 in the case of stamp duty). Stamp duty is usually the liability of the purchaser or transferee of the ordinary shares. An unconditional agreement to transfer such ordinary shares will be liable to SDRT, generally at the rate of 0.5 per cent of the consideration paid, but such liability will be cancelled, or, if already paid, refunded, if the agreement is completed by a duly-stamped transfer within six years of the agreement having become unconditional. SDRT is normally the liability of the purchaser or transferee of the ordinary shares.

Where Lloyds TSB Group issue ordinary shares or a holder of ordinary shares transfers such shares to the custodian or nominee for the depositary to facilitate the issue of ADSs to him representing the ordinary shares or to a person providing clearance services (or their nominee or agent), a liability to UK stamp duty or SDRT at the rate of 1.5 per cent (rounded up to the next multiple of £5 in the case of the stamp duty) of either the issue price or, in the case of transfer, the listed price of the ordinary shares, calculated in sterling, will arise. Where a holder of ordinary shares transfers such shares to the custodian or nominee for the depositary or clearance service this charge will generally be payable by the person receiving the ADSs or transferring the ordinary shares into the clearance service.

A liability to stamp duty at the fixed rate of £5 will arise as a result of the cancellation of any ADSs with the ordinary shares that they represent being transferred to the ADS holder.

No liability to UK stamp duty or SDRT will arise on a transfer of ADSs provided that any document that effects such transfer is not executed in the UK and that it remains at all subsequent times outside the UK. An agreement to transfer ADSs will not give rise to a liability to SDRT.

US federal income tax considerations

The following summary describes certain US federal income tax consequences of the acquisition, ownership and disposition of ADSs or ordinary shares, but it does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a decision to acquire such securities. The summary applies only to holders that hold ADSs or ordinary shares as capital assets and does not address special classes of holders, such as:

- certain financial institutions;
- insurance companies;
- dealers in securities or foreign currencies;
- holders holding ADSs or ordinary shares as part of a hedge, straddle or other conversion transaction;
- holders whose "functional currency" is not the US dollar;
- holders liable for alternative minimum tax;
- partnerships or other entities classified as partnerships for US federal income tax purposes; or
- a holder that owns 10 per cent or more of the voting shares of Lloyds TSB Group plc.

In addition, the summary is based in part on representations of the Depositary and assumes that each obligation provided for in or otherwise contemplated by the Deposit Agreement or any other related document will be performed in accordance with its terms. The US Treasury has expressed concerns that parties to whom ADSs are pre-released may be taking actions that are inconsistent with the claiming of foreign tax credits for US Holders of ADSs. Accordingly, the analysis of the creditability of UK taxes described below could be affected by future actions that may be taken by the US Treasury.

The summary is based upon tax laws of the US including the Internal Revenue Code of 1986, as amended to the date hereof (the "Code"), administrative pronouncements, judicial decisions and final, temporary and proposed Treasury Regulations, as well as upon the Treaty and the New Treaty, as appropriate, changes to any of which may affect the tax consequences described herein possibly with retroactive effect. On 24 July, 2001, the US and the UK entered into the New Treaty, which will enter into force at such time as it is ratified. Except as discussed under "—Taxation of Distributions", application of the New Treaty will not affect this summary. Prospective purchasers of the ADSs or ordinary shares should consult their own tax advisers as to the US, UK or other tax consequences of the purchase, ownership and disposition of such securities in their particular circumstances, including the effect of any state or local tax laws.

As used herein, a "US Holder" is a beneficial owner of ADSs or shares that is, for US federal income tax purposes:

- a citizen or resident of the US;
- a corporation created or organized in or under the laws of the US or of any political subdivision thereof; or
- an estate or trust the income of which is subject to US federal income taxation regardless of its source.

For US federal income tax purposes, US Holders of ADSs will be treated as the owners of the underlying ordinary shares.

Taxation of distributions

To the extent paid out of current or accumulated earnings and profits of Lloyds TSB Group plc (as determined in accordance with US federal income tax principles), distributions made with respect to ADSs or ordinary shares (other than certain distributions of capital stock of Lloyds TSB Group plc or rights to subscribe for shares of capital stock of Lloyds TSB Group plc) will be includible in the income of a US Holder as ordinary dividend income. Such dividends will not be eligible for the "dividends received deduction" generally allowed to corporations under the Code. To the extent that a distribution exceeds Lloyds TSB Group plc's current and accumulated earnings and profits, it will be treated as a nontaxable return of capital to the extent of the US Holder's tax basis in the ADSs or ordinary shares, and thereafter as capital gain. The amount of the distribution will equal the US dollar value of the pounds sterling received, calculated by reference to the exchange rate in effect on the date such distribution is received (which, for holders of ADSs, will be the date such distribution is received by the Depositary), whether or not the Depositary or US Holder in fact converts any pounds sterling received into US dollars at that time. Any gains or losses resulting from the conversion of pounds sterling into US dollars will be treated as ordinary income or loss, as the case may be, of the US Holder and will be US source.

A US Holder may, under the Treaty, elect to claim a foreign tax credit in respect of the Tax Credit Amount. A US Holder who so elects must include the Tax Credit Amount in income. Under the New Treaty no such election would be available.

The limitation of foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For this purpose, any dividends paid by Lloyds TSB Group plc on ADSs or ordinary shares will generally constitute "passive income" or, in the case of US financial service providers, may be "financial services income".

Taxation of capital gains

Gain or loss realised by a US Holder on (i) the sale or exchange of ADSs or ordinary shares or (ii) the Depositary's sale or exchange of ordinary shares received as distributions on the ADSs will be subject to US federal income tax as capital gain or loss in an amount equal to the difference between the US Holder's tax basis in the ADSs or ordinary shares and the amount realised on the disposition. Gain or loss, if any, will be US source. US Holders should consult their tax advisers regarding the US federal tax treatment of capital gains, which may be taxed at lower rates than ordinary income for individuals, and losses, the deductibility of which is subject to limitations.

Deposits and withdrawals of ordinary shares in exchange for ADSs will not result in taxable gain or loss for US federal income tax purposes.

Information reporting and backup withholding

Dividends paid on ADSs or ordinary shares to a US Holder may be subject to information reporting requirements of the Code. Such dividends may also be subject to backup withholding unless the US Holder:

- is a corporation or comes within certain other exempt categories and, when required, demonstrates this fact, or
- provides a taxpayer identification number on a properly completed Form W-9 or a substitute form and certifies that no loss of exemption from backup withholding has occurred and that such holder is a US person.

Any amount withheld under these rules will be creditable against the US Holder's federal income tax liability. A US Holder who does not provide a correct taxpayer identification number may be subject to certain penalties.

WHERE YOU CAN FIND MORE INFORMATION

The documents concerning us which are referred to herein may be inspected at the Securities and Exchange Commission. You may read and copy any document filed or furnished by us at the Securities and Exchange Commission's public reference rooms in Washington D.C., New York and Chicago, Illinois. Please call the Securities and Exchange Commission at 1-800-SEC-0330 for further information on the reference rooms.

ENFORCEABILITY OF CIVIL LIABILITIES

Lloyds TSB Group plc is a public limited company incorporated under the laws of Scotland. Most of Lloyds TSB Group plc's directors and executive officers and certain of the experts named herein are residents of the United Kingdom. A substantial portion of the assets of Lloyds TSB Group plc, and a substantial portion of the assets of such persons, are located outside the United States. As a result, it may not be possible for investors to effect service of process within the United States upon such persons or to enforce against them judgements of US courts, including judgements predicated upon the civil liability provisions of the federal securities laws of the United States. Furthermore, Lloyds TSB Group plc has been advised by its English solicitors, that there is doubt as to the enforceability in the United Kingdom, in original actions or in actions for enforcement of judgements of US courts, of civil liabilities, including those predicated solely upon the federal securities laws of the United States.

RISK FACTORS

An investment in Lloyds TSB Group plc's ordinary shares involves a number of risks, including credit, market, operational, regulatory, competitive and acquisition risks, some of which could be substantial and are inherent in Lloyds TSB Group's business.

Lloyds TSB Group's businesses are subject to inherent risks concerning borrower credit quality as well as the UK unemployment rate and general UK and international economic conditions. Development of adverse conditions in the UK or in other major economies, could cause profitability to decline.

Lloyds TSB Group's businesses are subject to inherent risks regarding borrower credit quality as well as the UK unemployment rate and general UK economic conditions, each of which can change the level of demand for Lloyds TSB Group's products and services. Changes in the credit quality of Lloyds TSB Group's UK or international borrowers and counterparties could reduce the value of Lloyds TSB Group's assets, and increase provisions for bad and doubtful debt. Any significant increase in the UK unemployment rate would reduce profits from the insurance business. Furthermore, a general deterioration in the UK economy would also reduce Lloyds TSB Group's profit margins for both its UK banking and financial services businesses. A general deterioration in any other major world economy could also adversely impact Group profitability.

Lloyds TSB Group's businesses are inherently subject to the risk of market fluctuations, which could reduce profitability.

Lloyds TSB Group's businesses are inherently subject to the risk of market fluctuations. The most significant market risks Lloyds TSB Group faces are interest rate risk and foreign exchange risk in its banking businesses and equity risk in its insurance businesses. See "Operating and Financial Review and Prospects—Risk management" for a discussion of these risks.

Lloyds TSB Group's insurance business is subject to inherent risks concerning changing demographic developments, catastrophic weather and similar contingencies outside its control. Development of adverse conditions could reduce profitability margins.

Lloyds TSB Group's insurance business is subject to inherent risk regarding changing demographic developments, catastrophic weather and similar contingencies outside its control, both in the UK and overseas. Such contingencies can change the risk profile and profitability of such products and services.

Adverse experience in the operational risks inherent in Lloyds TSB Group's businesses could have a negative impact on its results of operations.

Operational risks are present in Lloyds TSB Group's businesses, including the risk of direct or indirect loss resulting from inadequate or failed internal and external processes, people and systems or from external events. Lloyds TSB Group's businesses are dependent on their ability to process very efficiently a very large number of complex transactions across numerous and diverse products and services, in different currencies and subject to a number of different legal and regulatory regimes. Lloyds TSB Group's systems and processes are designed to ensure that the operational risks associated with its activities are appropriately controlled, but Lloyds TSB Group realises that any weakness in these systems could have a negative impact on its results of operations during the affected period. See "Operating and Financial Review and Prospects—Risk management—Other risks—Operational risks" and "Operating and Financial Review and Prospects—Other risks—Compliance risk".

Lloyds TSB Group operates its businesses subject to substantial regulation, regulatory and governmental oversight. Any significant adverse regulatory developments or changes in government policies or economic controls could have a negative impact on Lloyds TSB Group's results of operations.

Lloyds TSB Group conducts its businesses subject to ongoing regulation and associated regulatory risks, including the effects of changes in the laws, regulations, policies, voluntary codes of practice and interpretations in the UK and the other markets where it operates. Future changes in regulation, fiscal or other policies are unpredictable and beyond the control of Lloyds TSB Group. For additional information, see "Regulation".

The resolution of a number of issues affecting the UK financial services industry, including Lloyds TSB Group, could have a negative impact on Lloyds TSB Group's results of operations or on its relations with some of its customers and potential customers.

These issues involve the possible misselling of pension and other life assurance policies and matters arising from the treatment of guaranteed annuity options. There is a risk that further provisions may be required as a result of these issues. See "Business—Provisions for redress to past purchasers of pension policies" and "Business—Guaranteed Annuity Options".

Lloyds TSB Group's businesses are conducted in highly competitive environments and management's ability to create an appropriate return for shareholders depends upon management's ability to respond effectively to competitive pressures.

The market for UK financial services and the other markets within which Lloyds TSB Group operates are highly competitive and management expects such competition to intensify in response to consumer demand, technological changes, the impact of consolidation, regulatory actions and other factors, which could result in a reduction in profit margins. Lloyds TSB Group's ability to generate an appropriate return for its shareholders depends significantly upon the competitive environment and management's response to it. See "Business—Competitive environment".

Lloyds TSB Group is devoting considerable time and resources to securing new customers and developing more business from existing customers. If Lloyds TSB Group is unsuccessful, its organic growth prospects and results of operations may decline.

Lloyds TSB Group seeks to achieve further organic growth by securing new customers and developing more business from existing customers. Lloyds TSB Group is currently expending significant resources and effort to bring about this growth, particularly with respect to its UK retail financial services business. If these expenditures and efforts do not meet with success, its operating results could grow more slowly or decline.

Lloyds TSB Group's businesses are conducted in a market place that is rapidly consolidating, significant cross-border mergers and acquisitions may happen in the coming years and Lloyds TSB Group's ability to generate an appropriate return for its shareholders over the long term will depend upon whether management is able or permitted by either regulatory bodies or its shareholders to achieve value-creating mergers and/or acquisitions at the appropriate times and prices.

In addition to its important strategy of organic growth, one of Lloyds TSB Group's aims is to remain alert for opportunities to participate in the further consolidation of the financial services industry, both in the UK and overseas. In light of the Secretary of State's decision to prohibit the attempted acquisition of Abbey National, management believes that under current conditions Lloyds TSB Group may find it difficult to be able to make a significant acquisition in the UK in any business line where it already has a significant market share. Management also believes that domestic consolidation in many overseas markets, particularly in Europe, is entering its final phase and that therefore, significant cross border mergers and acquisitions may happen in the coming years. Lloyds TSB Group's ability to generate an appropriate return for its shareholders over the long term may depend upon whether management is able to achieve value-creating mergers and/or acquisitions at the appropriate times and prices. Lloyds TSB Group cannot be sure that it will ultimately be able to make any such mergers or acquisitions.

Any acquisition or merger made by Lloyds TSB Group could strain existing resources and disrupt existing businesses.

In the event of any future merger or acquisition, Lloyds TSB Group could:

- effect share issuances which might prove dilutive of Lloyds TSB Group's profits per ordinary share and which would dilute the percentage ownership of existing shareholders;
- incur debt;
- assume liabilities; and
- incur significant expenses relating to integration of the acquired business, including integration of information systems, employee compensation schemes and rebranding.

Any acquisition or merger would also involve numerous integration risks, including:

- problems combining and integrating the acquired operations, technologies or products;
- unanticipated costs or liabilities;
- diversion of management's attention from existing business operations;
- possible adverse effects on existing business relationships with suppliers, counterparties and customers;
- risks associated with cultural issues;
- risks associated with entering markets in which Lloyds TSB Group has limited or no experience; and
- potential loss of key employees, particularly those of acquired organizations.

There is a risk that Lloyds TSB Group will not be able to integrate successfully any acquired or merged business, products, technologies or personnel.

FORWARD LOOKING STATEMENTS

This annual report includes certain forward looking statements with respect to the business, strategy and plans of Lloyds TSB Group and its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about Lloyds TSB Group's or management's beliefs and expectations, are forward looking statements. Words such as "believes", "anticipates", "estimates", "expects", "intends", "aims", "potential", "will", "could", "considered", "likely", "estimate" and variations of these words and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend upon circumstances that will occur in the future.

Examples of such forward-looking statements include, but are not limited to:

- projections or expectations of profit attributable to shareholders, provisions, economic profit, dividends, capital structure or any other financial items or ratios;
- statements of plans, objectives or goals of Lloyds TSB Group or its management;
- statements about the future trends in interest rates, stock market levels and demographic trends and any impact on Lloyds TSB Group;
- statements concerning any future UK or other economic environment or performance, including in particular any such statements included in this registration statement in "Operating and Financial Review and Prospects";
- statements about strategic goals, competition, regulation, dispositions and consolidation or technological developments in the financial services industry; and
- statements of assumptions underlying such statements.

Lloyds TSB Group plc may also make or disclose written and/or oral forward looking statements in reports filed with or furnished to the US Securities and Exchange Commission, Lloyds TSB Group plc's annual report and accounts to shareholders, proxy statements, offering circulars, registration statements and prospectuses, press releases and other written materials and in oral statements made by the directors, officers or employees of Lloyds TSB Group plc to third parties, including financial analysts. The forward looking statements contained in this annual report are made as of the date hereof, and Lloyds TSB Group undertakes no obligation to update any of its forward looking statements.

LLOYDS TSB GROUP STRUCTURE

The following is a list of the principal subsidiaries of Lloyds TSB Group plc at 31 December 2001. The audited consolidated accounts of Lloyds TSB Group plc for the year ended 31 December 2001 include the audited accounts of each of these companies.

Name of subsidiary undertaking	Country of registration/ incorporation	Percentage of equity share capital and voting rights held	Nature of business	Registered office
Lloyds TSB Bank plc	England	100%	Banking and financial services	71 Lombard Street, London EC3P 3BS England
Cheltenham & Gloucester plc	England	*100%	Mortgage lending and retail investments	Barnett Way, Gloucester GL4 3RL England
Lloyds Bank (BLSA) Limited	England	*100%	Banking and financial services	71 Lombard Street, London EC3P 3BS England
Lloyds TSB Commercial Finance Limited	England	*100%	Credit factoring	Beaumont House, Beaumont Road, Banbury, Oxfordshire OX16 7RN England
Lloyds TSB Leasing Limited	England	*100%	Financial leasing	71 Lombard Street, London EC3P 3BS England
Lloyds TSB Private Banking Limited	England	*100%	Private banking	71 Lombard Street, London EC3P 3BS England
The Agricultural Mortgage Corporation PLC	England	*100%	Long-term agricultural finance	AMC House, Chantry Street, Andover, Hants SP10 1DD England
The National Bank of New Zealand Limited	New Zealand	*100%	Banking and financial services	National Bank House 170-186 Featherston Street, Wellington, New Zealand
Lloyds TSB Bank (Jersey) Limited	Jersey	*100%	Banking and financial services	25 New Street, St. Helier JE4 8RG Jersey
Lloyds TSB Scotland plc	Scotland	*100%	Banking and financial services	Henry Duncan House, 120 George Street Edinburgh EH2 4LH Scotland
Lloyds TSB General Insurance Limited	England	*100%	General insurance	71 Lombard Street, London EC3P 3BS England
Scottish Widows Investment Partnership Group Limited	England	*100%	Investment management	10 Fleet Place, London EC4M 7RH England

Name of subsidiary undertaking	Country of registration/ incorporation	Percentage of equity share capital and voting rights held	Nature of business	Registered office
Abbey Life Assurance Company Limited	England	*100%	Life assurance	80 Holdenhurst Road, Bournemouth BH8 8ZQ England
Lloyds TSB Insurance Services Limited	England	*100%	Insurance broking	71 Lombard Street, London EC3P 3BS England
Lloyds TSB Life Assurance Company Limited	England	*100%	Life assurance and other financial services	71 Lombard Street, London EC3P 3BS England
Lloyds TSB Asset Finance Division Limited	England	*100%	Consumer credit, leasing and related services	71 Lombard Street, London EC3P 3BS England
Black Horse Limited	England	*100%	Consumer credit, leasing and related services	71 Lombard Street London EC3P 3BS England
Scottish Widows plc	Scotland	*100%	Life assurance	69 Morrison Street, Edinburgh EH3 8YF Scotland
Scottish Widows Annuities Limited	Scotland	*100%	Life assurance	69 Morrison Street, Edinburgh EH3 8YF Scotland

* Indirect interest

INDEX TO THE CONSOLIDATED FINANCIAL STATEMENTS

Report of Independent Accountants

To the Shareholders of Lloyds TSB Group plc:

We have audited the accompanying consolidated balance sheets of Lloyds TSB Group plc and its subsidiaries as of 31 December 2001 and 31 December 2000, and the related consolidated profit and loss account, consolidated statement of total recognised gains and losses, reconciliation of movement in shareholders' funds and consolidated cash flow statement for each of the three years in the period ended 31 December 2001 which, as described in Note 1, have been prepared on the basis of accounting principles generally accepted in United Kingdom. These financial statements are the responsibility of the directors of Lloyds TSB Group plc. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lloyds TSB Group plc and its subsidiary undertakings at 31 December 2001 and 31 December 2000, and the results of their operations and their cash flows, for each of the three years in the period ended 31 December 2001 in conformity with accounting principles generally accepted in the United Kingdom.

Accounting principles generally accepted in the United Kingdom vary in certain material respects from accounting principles in the United States. The application of the latter would have affected the determination of consolidated net income expressed in pounds sterling for each of the three years in the period ended 31 December 2001 and the determination of consolidated shareholders' equity also expressed in pounds sterling at 31 December 2001 and 2000 to the extent summarised in Note 48 to the consolidated financial statements.

PricewaterhouseCoopers
Southampton, England
14 February 2002

Consolidated profit and loss account

for the year ended 31 December 2001

	Note	**2001 £ million**	2000 £ million	1999 £ million
Interest receivable:				
Interest receivable and similar income arising from debt securities		**530**	443	430
Other interest receivable and similar income		**10,834**	10,611	10,022
Interest payable		**6,420**	6,467	5,669
Net interest income		**4,944**	4,587	4,783
Other income				
Fees and commissions receivable		**2,922**	2,768	2,497
Fees and commissions payable		**(602)**	(479)	(426)
Dealing profits (before expenses)	3	**233**	198	215
Income from long-term assurance business	29	**193**	615	227
General insurance premium income		**428**	399	390
Other operating income		**708**	436	292
		3,882	3,937	3,195
Total income		**8,826**	8,524	7,978
Operating expenses				
Administrative expenses	4	**3,557**	3,378	3,140
Exceptional restructuring costs	5	**217**	188	-
Total administrative expenses		**3,774**	3,566	3,140
Depreciation	23	**511**	364	265
Amortisation of goodwill	22	**39**	22	12
Depreciation and amortisation		**550**	386	277
Total operating expenses		**4,324**	3,952	3,417
Trading surplus		**4,502**	4,572	4,561
General insurance claims		**174**	142	169
Provisions for bad and doubtful debts	15			
Specific		**736**	547	615
General		**11**	(6)	-
		747	541	615
Amounts written off fixed asset investments	6	**60**	32	7
Operating profit		**3,521**	3,857	3,770
Income from associated undertakings and joint ventures	20	**(10)**	3	12
Profit(loss) on sale and closure of businesses	7	**39**	-	(126)
Profit on ordinary activities before tax	8	**3,550**	3,860	3,656
Tax on profit on ordinary activities	9	**971**	1,105	1,111
Profit on ordinary activities after tax		**2,579**	2,755	2,545
Minority interests : equity		**17**	13	6
: non-equity	39	**62**	36	-
Profit for the year attributable to shareholders		**2,500**	2,706	2,539
Dividends	10	**1,872**	1,683	1,451
Retained profit	41	**628**	1,023	1,088
Earnings per share	11	**45.2p**	49.3p	46.6p
Diluted earnings per share	11	**44.8p**	48.8p	45.8p

The accompanying notes are an integral part of the Consolidated Financial Statements.

Consolidated balance sheet
at 31 December 2001

	Note	**2001 £ million**	2000* £ million
Assets			
Cash and balances at central banks		**1,240**	1,027
Items in course of collection from banks		**1,664**	1,533
Treasury bills and other eligible bills	12	**4,412**	1,709
Loans and advances to banks	13	**15,224**	15,290
Loans and advances to customers		**123,059**	114,832
Non-returnable finance		**(124)**	(400)
	14	**122,935**	114,432
Debt securities	17	**24,225**	14,605
Equity shares	18	**225**	247
Interests in associated undertakings and joint ventures:	20		
Share of gross assets		**281**	14
Share of gross liabilities		**(242)**	(5)
		39	9
Intangible fixed assets	22	**2,566**	2,599
Tangible fixed assets	23	**3,365**	3,037
Own shares	26	**23**	28
Other assets	27	**4,468**	3,998
Prepayments and accrued income	28	**3,190**	2,965
Long-term assurance business attributable to the shareholder	29	**6,574**	6,549
		190,150	168,028
Long-term assurance assets attributable to policyholders	29	**46,389**	51,085
Total assets		**236,539**	219,113

The accompanying notes are an integral part of the Consolidated Financial Statements.

* restated (see note 1)

	Note	**2001 £ million**	2000* £ million
Liabilities			
Deposits by banks	31	**24,310**	16,735
Customer accounts	32	**109,116**	101,989
Items in course of transmission to banks		**534**	420
Debt securities in issue	33	**24,420**	17,899
Other liabilities	34	**6,673**	6,600
Accruals and deferred income	35	**3,563**	4,174
Provisions for liabilities and charges:			
Deferred tax	36	**1,719**	1,683
Other provisions for liabilities and charges	37	**401**	442
Subordinated liabilities:			
Undated loan capital	38	**3,651**	3,391
Dated loan capital	38	**4,006**	4,119
Minority interests:			
Equity		**37**	37
Non-equity	39	**960**	515
		997	552
Called-up share capital	40	**1,411**	1,396
Share premium account	41	**959**	595
Merger reserve	41	**343**	343
Profit and loss account	41	**8,047**	7,690
Shareholders' funds (equity)		**10,760**	10,024
		190,150	168,028
Long-term assurance liabilities to policyholders		**46,389**	51,085
Total liabilities		**236,539**	219,113
Memorandum items	44		
Contingent liabilities:			
Acceptances and endorsements		**2,243**	357
Guarantees and assets pledged as collateral security		**3,789**	3,249
Other contingent liabilities		**1,931**	1,541
		7,963	5,147
Commitments:			
Commitments arising out of sale and option to resell transactions		**-**	3
Other commitments		**53,342**	42,586
		53,342	42,589

The accompanying notes are an integral part of the Consolidated Financial Statements.

* restated (see note 1)

Other statements

Statement of total recognised gains and losses
for the year ended 31 December 2001

	2001 £ million	2000 £ million	1999 £ million
Profit attributable to shareholders	**2,500**	2,706	2,539
Currency translation differences on foreign currency net investments	**(86)**	(11)	(10)
Total recognised gains and losses relating to the year	**2,414**	2,695	2,529
Prior year adjustment in respect of the adoption of FRS 18 (note 1)	**248**	-	
Prior year adjustment in respect of the adoption of FRS 15	**-**	(112)	
Total gains and losses recognised during the year	**2,662**	2,583	

Historical cost profits and losses
for the year ended 31 December 2001

There was no material difference between the results as reported and the results that would have been reported on an unmodified historical cost basis. Accordingly, no note of historical cost profits and losses has been included.

Reconciliation of movements in shareholders' funds
for the year ended 31 December 2001

	2001 £ million	2000 £ million	1999 £ million
Profit attributable to shareholders	**2,500**	2,706	2,539
Dividends	**(1,872)**	(1,683)	(1,451)
Retained profit	**628**	1,023	1,088
Currency translation differences on foreign currency net investments	**(86)**	(11)	(10)
Issue of shares	**194**	74	108
Goodwill written back on sale and closure of businesses	**-**	109	80
Net increase in shareholders' funds	**736**	1,195	1,266
Shareholders' funds at beginning of year	**10,024**	8,829	7,563
Shareholders' funds at end of year	**10,760**	10,024	8,829

The accompanying notes are an integral part of the Consolidated Financial Statements.

Consolidated cash flow statement

for the year ended 31 December 2001

	2001	2000	1999
	£ million	£ million	£ million
Net cash inflow from operating activities (note 47a)	**9,927**	7,474	1,213
Dividends received from associated undertakings	**2**	2	-
Returns on investments and servicing of finance:			
Dividends paid to equity minority interests	**(17)**	(12)	(11)
Payments made to non-equity minority interests	**(62)**	(36)	-
Interest paid on subordinated liabilities (loan capital)	**(492)**	(442)	(270)
Interest element of finance lease rental payments	**(1)**	(1)	-
Net cash outflow from returns on investments and servicing of finance	**(572)**	(491)	(281)
Taxation:			
UK corporation tax	**(682)**	(723)	(670)
Overseas tax	**(147)**	(141)	(137)
Total taxation	**(829)**	(864)	(807)
Capital expenditure and financial investment:			
Additions to fixed asset investments	**(47,049)**	(23,564)	(23,147)
Disposals of fixed asset investments	**40,530**	24,850	21,969
Additions to tangible fixed assets	**(1,157)**	(1,006)	(595)
Disposals of tangible fixed assets	**285**	78	83
Capital injection to long-term assurance business	**(100)**	-	(220)
Net cash (outflow) inflow from capital expenditure and financial investment	**(7,491)**	358	(1,910)
Acquisitions and disposals:			
Additions to interests in joint ventures	**(44)**	-	-
Acquisition of group undertakings (note 47e)	**(180)**	(5,110)	(27)
Disposal of group undertakings and businesses (note 47g)	**40**	83	3
Net cash outflow from acquisitions and disposals	**(184)**	(5,027)	(24)
Equity dividends paid	**(1,738)**	(1,522)	(1,285)
Net cash outflow before financing	**(885)**	(70)	(3,094)
Financing:			
Issue of subordinated liabilities (loan capital)	**286**	952	2,769
Issue of capital securities by subsidiary undertakings	**456**	509	-
Issue of ordinary share capital net of £185 million (2000: £124 million; 1999: £205 million) contribution to the QUEST (note 26)	**194**	74	108
Repayments of subordinated liabilities (loan capital)	**(131)**	(55)	(228)
Capital element of finance lease rental payments	**(20)**	(4)	(3)
Net cash inflow from financing	**785**	1,476	2,646
(Decrease) increase in cash (note 47c)	**(100)**	1,406	(448)

The accompanying notes are an integral part of the Consolidated Financial Statements.

1 Accounting policies

Accounting policies are unchanged from 2000. In accordance with the requirements of Financial Reporting Standard 3 ‘Reporting Financial Performance’ a gain of £248 million in 2001 has been recognised in the Statement of Recognised Gains and Losses in connection with the implementation of the requirements of Financial Reporting Standard 18 ‘Accounting Policies’ in the consolidated financial statements for the year ended 31 December 2000.

During the year the Group adopted Financial Reporting Standard 17 ‘Retirement Benefits’. In accordance with the transitional arrangements of the standard in accounts for the year ended 31 December 2001, supplementary disclosures only are required and these are set out in note 43c. The Group has also implemented the requirements of the British Bankers’ Association’s revised Statement of Recommended Practice on Derivatives, although the effect has not been significant. Certain assets and liabilities have been reclassified and 2000 and 1999 comparative figures have been restated accordingly.

The Group has also adopted the requirements of the Urgent Issues Task Force’s Abstract 32 ‘Employee benefit trusts and other intermediate payment arrangements’. This has had no effect on the consolidated Group figures.

a Accounting convention

The consolidated financial statements are prepared under the historical cost convention as modified by the revaluation of debt securities and equity shares held for dealing purposes (see g) and assets held in the long-term assurance business (see n) in compliance with Section 255A, Schedule 9 and other requirements of the Companies Act 1985 except as described below (see c), in accordance with applicable accounting standards, pronouncements of the Urgent Issues Task Force and with the Statements of Recommended Practice issued by the British Bankers’ Association and the Finance & Leasing Association.

The Group continues to take advantage of the dispensation in the Urgent Issues Task Force’s Abstract 17 ‘Employee Share Schemes’ not to apply that Abstract to the Group’s Inland Revenue approved Save As You Earn (‘SAYE’) share option schemes.

b Basis of consolidation

Assets, liabilities and results of group undertakings and joint ventures are included in the consolidated accounts on the basis of accounts made up to 31 December. Details of the principal group undertakings and joint ventures can be found in note 20 and note 21. In order to reflect the different nature of the shareholder’s and policyholders’ interests in the long-term assurance business, the value of long-term assurance business attributable to the shareholder and the assets and liabilities attributable to policyholders are classified under separate headings in the consolidated balance sheet (see n). Details of transactions entered into by the Group which are not eliminated on consolidation are given in note 42.

c Goodwill

Goodwill arising on acquisitions of or by group undertakings is capitalised. For acquisitions prior to 1 January 1998, goodwill was taken direct to reserves in the year of acquisition. As permitted by the transitional arrangements of Financial Reporting Standard 10, this goodwill was not reinstated when the Group adopted the standard in 1998.

The useful economic life of the goodwill arising on each acquisition is determined at the time of the acquisition. The directors consider that it is appropriate to assign an indefinite life to the goodwill which arose on the acquisition of Scottish Widows during 2000 in view of the strength of the Scottish Widows brand, developed through over 185 years of trading, and the position of the business as one of the leading providers of life, pensions, unit trust and fund management products. Both of these attributes are deemed to have indefinite durability, which has been determined based on the following factors: the nature of the business; the stability of the industry; the typical lifespans of the products; the extent to which the acquisition overcomes market entry barriers; and the expected future impact of competition on the business.

The Scottish Widows goodwill is not being amortised through the profit and loss account; however, it is subjected to annual impairment reviews in accordance with Financial Reporting Standard 11. Impairment of the goodwill is evaluated by comparing the present value of the expected future cash flows of the business, excluding financing and tax, (the ‘value-in-use’) to the carrying value of the underlying net assets. If the net assets were to exceed the value-in-use, an impairment would be deemed to have occurred and the resulting write-down in the goodwill would be charged to the profit and loss account immediately.

Paragraph 28 of Schedule 9 to the Companies Act 1985 requires that all goodwill carried on the balance sheet should be amortised. In the case of the goodwill arising on the acquisition of Scottish Widows, the directors consider that it is appropriate to depart from this requirement in order to comply with the over-riding requirement for the accounts to show a true and fair view. If this goodwill was amortised over a period of 20 years, profit before tax for the year ended 31 December 2001 would be £94 million lower (2000: £78 million lower), with a corresponding reduction in reserves of £172 million (2000: £78 million); intangible assets on the balance sheet would also be £172 million lower (2000: £78 million lower).

Goodwill arising on all other acquisitions after 1 January 1998 is amortised on a straight line basis over its estimated useful economic life, which does not exceed 20 years.

1 Accounting policies (continued)

c Goodwill (continued)

At the date of the disposal of group or associated undertakings, any unamortised goodwill, or goodwill taken directly to reserves prior to 1 January 1998, is included in the Group's share of the net assets of the undertaking in the calculation of the profit or loss on disposal.

d Income recognition

Interest income is recognised in the profit and loss account as it accrues, with the exception of interest on non-performing lending which is taken to income either when it is received or when there ceases to be any significant doubt about its ultimate receipt (see e).

Fees and commissions receivable from customers to reimburse the Group for costs incurred are taken to income when due. Fees and commissions relating to the ongoing provision of a service or risk borne for a customer are taken to income in proportion to the service provided or risk borne in each accounting period. Fees and commissions charged in lieu of interest are taken to income on a level yield basis over the period of the loan. Other fees and commissions receivable are accounted for as they fall due.

e Provisions for bad and doubtful debts and non-performing lending

Provisions for bad and doubtful debts
It is the Group's policy to make provisions for bad and doubtful debts, by way of a charge to the profit and loss account, to reflect the losses inherent in the loan portfolio at the balance sheet date. There are two types of provision, specific and general, and these are discussed further below.

Specific provisions
Specific provisions relate to identified risk advances and are raised when the Group considers that recovery of the whole of the outstanding balance is in serious doubt. The amount of the provision is equivalent to the amount necessary to reduce the carrying value of the advance to its expected ultimate net realisable value.

For the Group's portfolios of smaller balance homogeneous loans, such as the residential mortgage, personal lending and credit card portfolios, specific provisions are calculated using a formulae driven approach. These formulae take into account factors such as the length of time that payments from the customer are overdue, the value of any collateral held and the level of past and expected losses, in order to derive an appropriate provision.

For the Group's other lending portfolios, specific provisions are calculated on a case-by-case basis. In establishing an appropriate provision, factors such as the financial condition of the customer, the nature and value of any collateral held and the costs associated with obtaining repayment and realisation of the collateral are taken into consideration.

General provisions
General provisions are raised to cover latent bad and doubtful debts which are present in any portfolio of advances but have not been specifically identified. The Group holds general provisions against each of its principal lending portfolios, which are calculated after having regard to a number of factors; in particular, the level of watchlist or potential problem debt and the observed propensity for such debt to deteriorate and become impaired and prior period loss rates. The level of general provision held is reviewed on a regular basis to ensure that it remains appropriate in the context of the perceived risk inherent in the related portfolio and the prevailing economic climate.

Non-performing lending
An advance becomes non-performing when interest ceases to be credited to the profit and loss account. There are two types of non-performing lending which are discussed further below.

Accruing loans on which interest is being placed in suspense
Where the customer continues to operate the account, but where there is doubt about the payment of interest, interest continues to be charged to the customer's account, but it is not applied to income. Interest is placed on a suspense account and only taken to income if there ceases to be significant doubt about its being paid.

Loans accounted for on a non-accrual basis
In those cases where the operation of the customer's account has ceased and it has been transferred to a specialist recovery department, the advance is written down to its estimated realisable value and interest is no longer charged to the customer's account as its recovery is considered unlikely. Interest is only taken to income if it is received.

1 Accounting policies (continued)

f Mortgage incentives

Payments made under cash gift and discount mortgage schemes, which are granted to customers as incentives to take out loans and are recoverable from the customer in the event of early redemption, are amortised as an adjustment to net interest income over the early redemption charge period. Payments cease to be deferred and are charged to the profit and loss account in the event that the related loan is redeemed or becomes impaired.

g Debt securities and equity shares

Debt securities, apart from those held for dealing purposes, are stated at cost as adjusted for the amortisation of any premiums and discounts arising on acquisition, which are amortised from purchase to maturity in equal annual instalments, less amounts written off for any permanent diminution in their value. Debt securities acquired in exchange for advances to countries experiencing payment difficulties are included in the Group's portfolio of investment securities at an amount based on the market value at the date of exchange as adjusted for the amortisation of discount on acquisition. Equity shares, apart from those held for dealing purposes, are stated at cost less amounts written off for any permanent diminution in their value.

Debt securities and equity shares held for dealing purposes are included at market value.

h Tangible fixed assets

Tangible fixed assets are included at cost less depreciation.

Land is not depreciated. Leasehold premises with unexpired lease terms of 50 years or less are depreciated by equal annual instalments over the remaining period of the lease. Freehold and long leasehold buildings are depreciated over 50 years. The costs of adapting premises for the use of the Group are separately identified and depreciated over 10 years, or over the term of the lease if less; such costs are included within premises in the balance sheet total of tangible fixed assets. Equipment is depreciated by equal annual instalments over the estimated useful lives of the assets, which for fixtures and furnishings are 10-20 years and for computer hardware, operating software and application software and the related development costs relating to separable new systems, motor vehicles and other equipment are 3-8 years.

Premises and equipment held for letting to customers under operating leases are depreciated over the life of the lease to give a constant rate of return on the net investment, taking into account anticipated residual values. Anticipated residual values are reviewed regularly and any impairments identified are charged to the profit and loss account.

i Vacant leasehold property

When a leasehold property ceases to be used in the business or a commitment is entered into which would cause this to occur, provision is made to the extent that the recoverable amount of the interest in the property is expected to be insufficient to cover future obligations relating to the lease.

j Leasing and instalment credit transactions

Assets leased to customers are classified as finance leases if the lease agreements transfer substantially all of the risks and rewards of ownership to the lessee; all other leases are classified as operating leases.

Income from both finance and operating leases is credited to the profit and loss account in proportion to the net cash invested so as to give a constant rate of return over each period after taking account of tax. Income from instalment credit transactions is credited to the profit and loss account using the sum of the digits method.

In those cases where the Group is the lessee, operating lease costs are charged to the profit and loss account in equal annual instalments over the life of the lease.

k Deferred tax

Deferred tax is provided at the appropriate rates of tax where there is a reasonable probability that a liability or asset will crystallise in the foreseeable future.

l Pensions and other post-retirement benefits

The cost of providing pension benefits is charged to the profit and loss account so as to spread the expected cost of pensions, calculated in accordance with actuarial advice, on a systematic basis over employees' working lives. The pension cost is assessed in accordance with the advice of qualified actuaries, using the projected unit method. Variations from the regular cost are allocated by equal annual instalments over the average remaining service lives of current employees.

1 Accounting policies (continued)

l Pensions and other post-retirement benefits (continued)

The cost of providing post-retirement benefits other than pensions is charged to the profit and loss account on a systematic basis over employees' working lives. The unfunded liability is included as a provision in the balance sheet.

m Foreign currency translation

Assets, liabilities and results in foreign currencies are expressed in sterling at the rates of exchange ruling on the dates of the respective balance sheets. Exchange adjustments on the translation of opening net assets held overseas are taken direct to reserves. All other exchange profits or losses, which arise from normal trading activities, are included in the profit and loss account.

n Long-term assurance business

A number of the Group's subsidiary undertakings are engaged in writing long-term assurance business, including the provision of life assurance, pensions, annuities and permanent health insurance contracts. In common with other life assurance companies in the UK, these companies are structured into one or more long-term business funds, depending upon the nature of the products being written, and a shareholder's fund. All premiums received, investment returns, claims and expenses, and changes in liabilities to policyholders are accounted for within the related long-term business fund. Any surplus, which is determined annually by the Appointed Actuary after taking account of these items, may either be distributed between the shareholder and the policyholders according to a predetermined formula or retained within the long-term business fund. The shareholder will also levy investment management and administration charges upon the long-term business fund.

The Group accounts for its interest in long-term assurance business using the embedded value basis of accounting. The value of the shareholder's interest in the long-term assurance business ('the embedded value') included in the Group's balance sheet is an actuarially determined estimate of the economic value of the Group's life assurance subsidiaries, excluding any value which may be attributed to future new business. The embedded value is comprised of the net tangible assets of the life assurance subsidiaries, including any surplus retained within the long-term business funds, which could be transferred to the shareholder, and the present value of the in-force business. The value of the in-force business is calculated by projecting the future surpluses and other net cash flows attributable to the shareholder arising from business written by the balance sheet date, using appropriate economic and actuarial assumptions, and discounting the result at a rate which reflects the shareholder's overall risk premium.

Changes in the embedded value, which are determined on a post-tax basis, are included in the profit and loss account. For the purpose of presentation, the change in this value is grossed up at the underlying rate of corporation tax.

The assets held within the long-term business funds are legally owned by the life assurance companies, however the shareholder will only benefit from ownership of these assets to the extent that surpluses are declared or from other cash flows attributable to the shareholder. Reflecting the different nature of these assets, they are classified separately on the Group's balance sheet as 'Long-term assurance assets attributable to policyholders', with a corresponding liability to the policyholders also shown. Investments held within the long-term business funds are included on the following basis: equity shares, debt securities and unit trusts held for unit linked funds are valued in accordance with policy conditions at market prices; other equity shares and debt securities are valued at middle market price and other unit trusts at bid price; investment properties are included at valuation by independent valuers at existing use value at the balance sheet date, and mortgages and loans are at cost less amounts written off.

o General insurance business

The Group both underwrites and acts as intermediary in the sale of general insurance products. Underwriting premiums are included, net of refunds, in the period in which insurance cover is provided to the customer; premiums received relating to future periods are deferred and only credited to the profit and loss account when earned. Where the Group acts as intermediary, commission income is included in the profit and loss account at the time that the underwriter accepts the risk of providing insurance cover to the customer. Where appropriate, provision is made for the effect of future policy terminations based upon past experience.

The underwriting business makes provision for the estimated cost of claims notified but not settled and claims incurred but not reported at the balance sheet date. The provision for the cost of claims notified but not settled is based upon a best estimate of the cost of settling the outstanding claims after taking into account all known facts. In those cases where there is insufficient information to determine the required provision, statistical techniques are used which take into account the cost of claims that have recently been settled and make assumptions about the future development of the outstanding cases. Similar statistical techniques are used to determine the provision for claims incurred but not reported at the balance sheet date. Claims equalisation provisions are calculated in accordance with the relevant legislative requirements.

1 Accounting policies (continued)

p Derivatives

Derivatives are used in the Group's trading activities to meet the financial needs of customers, for proprietary purposes and to manage risk in the Group's trading portfolios. Such instruments include exchange rate forwards and futures, currency swaps and options together with interest rate swaps, forward rate agreements, interest rate options and futures. These derivatives are carried at fair value and all changes in fair value are reported within dealing profits in the profit and loss account. Fair values are normally determined by reference to quoted market prices; internal models are used to determine fair value in instances where no market price is available. The unrealised gains and losses on trading derivatives are included within other assets and other liabilities respectively. These items are reported gross except in instances where the Group has entered into legally binding netting agreements, where the Group has a right to insist on net settlement that would survive the insolvency of the counterparty; in these cases the positive and negative fair values of trading derivatives with the relevant counterparties are offset within the balance sheet totals.

Derivatives used in the Group's non-trading activities are taken out to reduce exposures to fluctuations in interest and exchange rates and include exchange rate forwards and futures, currency options together with interest rate swaps, forward rate agreements and options. These derivatives are accounted for on an accruals basis, in line with the treatment of the underlying items which they are hedging. Interest receipts and payments on hedging interest derivatives are included in the profit and loss account so as to match the interest payable or receivable on the hedged item.

A derivative will only be classified as a hedge in circumstances where there was adequate evidence of the intention to hedge at the outset of the transaction and the derivative substantially matches or eliminates the exposure being hedged.

Where a hedge transaction is superseded, ceases to be effective or is terminated early the derivative is measured at fair value. Any profit or loss arising is then amortised to the profit and loss account over the remaining life of the item which it was originally hedging. When the underlying asset, liability or position that was being hedged is terminated, the hedging derivative is measured at fair value and any profit or loss arising is recognised immediately.

2 Segmental analysis

The Group's activities are organised into three segments: UK Retail Banking and Mortgages, Insurance and Investments and Wholesale Markets and International Banking. Services provided by UK Retail Banking and Mortgages encompass the provision of banking and other financial services to personal and small business customers, private banking, stockbroking and mortgages. Insurance and Investments offers life assurance, pensions and savings products, general insurance and fund management services. Wholesale Markets and International Banking provides banking and related services for major UK and multinational companies, banks and financial institutions, and medium-sized UK businesses. It also provides asset finance to personal and corporate customers, manages the Group's activities in financial markets through its Treasury function and provides banking and financial services overseas.

Year ended 31 December 2001	**UK Retail Banking and Mortgages £m**	**General insurance £m**	**Life, pensions, unit trusts and asset management £m**	**Insurance and Investments £m**	**Wholesale Markets and International Banking £m**	**Central group items £m**	**Total £m**
Net interest income	**3,115**	**48**	**32**	**80**	**1,858**	**(109)**	**4,944**
Income from long-term assurance business	**-**	**-**	**181**	**181**	**12**	**-**	**193**
Other operating income	**1,141**	**900**	**286**	**1,186**	**1,313**	**49**	**3,689**
Total income	**4,256**	**948**	**499**	**1,447**	**3,183**	**(60)**	**8,826**
Exceptional restructuring costs	**(150)**	**-**	**(50)**	**(50)**	**(17)**	**-**	**(217)**
Other operating expenses	**(2,243)**	**(152)**	**(238)**	**(390)**	**(1,410)**	**(64)**	**(4,107)**
Trading surplus	**1,863**	**796**	**211**	**1,007**	**1,756**	**(124)**	**4,502**
General insurance claims	**-**	**(174)**	**-**	**(174)**	**-**	**-**	**(174)**
Provisions for bad and doubtful debts	**(415)**	**-**	**-**	**-**	**(332)**	**-**	**(747)**
Amounts written off fixed asset investments	**-**	**-**	**-**	**-**	**(60)**	**-**	**(60)**
Income from associated undertakings and joint ventures	**(10)**	**-**	**-**	**-**	**-**	**-**	**(10)**
Profit on sale of businesses	**-**	**-**	**-**	**-**	**-**	**39**	**39**
Profit (loss) before tax	**1,438**	**622**	**211**	**833**	**1,364**	**(85)**	**3,550**

Year ended 31 December 2000*	UK Retail Banking and Mortgages £m	General insurance £m	Life, pensions, unit trusts and asset management £m	Insurance and Investments £m	Wholesale Markets and International Banking £m	Central group items £m	Total £m
Net interest income	2,951	57	31	88	1,653	(105)	4,587
Income from long-term assurance business	-	-	607	607	8	-	615
Other operating income	1,143	774	315	1,089	1,057	33	3,322
Total income	4,094	831	953	1,784	2,718	(72)	8,524
Exceptional restructuring costs	(99)	-	(59)	(59)	(30)	-	(188)
Other operating expenses	(2,099)	(129)	(236)	(365)	(1,254)	(46)	(3,764)
Trading surplus	1,896	702	658	1,360	1,434	(118)	4,572
General insurance claims	-	(142)	-	(142)	-	-	(142)
Provisions for bad and doubtful debts	(332)	-	-	-	(209)	-	(541)
Amounts written off fixed asset investments	-	-	-	-	(32)	-	(32)
Income from associated undertakings and joint ventures	2	-	1	1	-	-	3
Profit (loss) before tax	1,566	560	659	1,219	1,193	(118)	3,860

2 Segmental analysis (continued)

Year ended 31 December 1999	UK Retail Banking and Mortgages £m	General insurance £m	Life, pensions, unit trusts and asset management £m	Insurance and Investments £m	Wholesale Markets and International Banking £m	Central group items £m	Total £m
Net interest income	2,943	50	10	60	1,664	116	4,783
Income from long-term assurance business	-	-	219	219	8	-	227
Other operating income	1,087	702	271	973	876	32	2,968
Total income	4,030	752	500	1,252	2,548	148	7,978
Operating expenses	(1,951)	(100)	(193)	(293)	(1,144)	(29)	(3,417)
Trading surplus	2,079	652	307	959	1,404	119	4,561
General insurance claims	-	(169)	-	(169)	-	-	(169)
Provisions for bad and doubtful debts	(425)	-	-	-	(190)	-	(615)
Amounts written off fixed asset investments	-	-	-	-	(7)	-	(7)
Income from associated undertakings and joint ventures	3	-	9	9	-	-	12
Loss on sale and closure of businesses	-	-	-	-	-	(126)	(126)
Profit (loss) before tax	1,657	483	316	799	1,207	(7)	3,656

Geographical area: **	**Domestic 2001 £m**	**International 2001 £m**	**Total 2001 £m**	Domestic 2000 £m	International 2000 £m	Total 2000 £m	Domestic 1999 £m	International 1999 £m	Total 1999 £m
Interest receivable	**8,950**	**2,414**	**11,364**	8,927	2,127	11,054	8,015	2,437	10,452
Fees and commissions receivable	**2,636**	**286**	**2,922**	2,480	288	2,768	2,227	270	2,497
Dealing profits (before expenses)	**138**	**95**	**233**	149	49	198	154	61	215
Income from long-term assurance business	**181**	**12**	**193**	607	8	615	219	8	227
General insurance premium income	**428**	**-**	**428**	399	-	399	390	-	390
Other operating income	**538**	**170**	**708**	269	167	436	138	154	292
Total gross income	**12,871**	**2,977**	**15,848**	12,831	2,639	15,470	11,143	2,930	14,073
Profit on ordinary activities before tax	**2,984**	**566**	**3,550**	3,427	433	3,860	3,201	455	3,656

2 Segmental analysis (continued)

	Net assets †		Assets ‡	
	2001	2000	**2001**	2000*
	£m	£m	**£m**	£m
Class of business:				
UK Retail Banking and Mortgages	**2,437**	2,235	**77,915**	71,292
Insurance and Investments				
- General insurance	**339**	361	**825**	755
- Life, pensions, unit trusts and asset management	**6,680**	6,147	**8,653**	8,682
	7,019	6,508	**9,478**	9,437
UK Retail Financial Services	**9,456**	8,743	**87,393**	80,729
Wholesale Markets and International Banking	**3,965**	3,377	**101,471**	86,030
Central group items	**(2,624)**	(2,059)	**1,286**	1,269
	10,797	10,061	**190,150**	168,028
Geographical area: **				
Domestic	**9,723**	9,129	**161,542**	144,898
International	**1,074**	932	**28,608**	23,130
	10,797	10,061	**190,150**	168,028

* Figures for 2000 have been restated to take account of changes in internal transfer pricing and the reclassification of certain assets and liabilities (note 1); the impact of the changes in internal transfer pricing for the year ended 31 December 1999 was not material.

** The geographical distribution of gross income sources, profit on ordinary activities before tax and assets by domestic and international operations is based on the location of the office recording the transaction, except for lending by the international business booked in London.

† Net assets represent shareholders' funds plus equity minority interests. Disclosure of information on net assets is an accounting standard requirement (SSAP25); it is not appropriate to relate it directly to the segmental profits above because the business is not managed by the allocation of net assets to business units.

‡ Assets exclude long-term assurance assets attributable to policyholders.

As the business of the Group is mainly that of banking and insurance, no segmental analysis of turnover is given.

3 Dealing profits (before expenses)

	2001	2000	1999
	£m	£m	£m
Foreign exchange trading income	**158**	141	133
Securities and other gains	**75**	57	82
	233	198	215

Dealing profits include the profits and losses arising both on the purchase and sale of trading instruments and from the year-end revaluation to market value, together with the interest income earned from these instruments and the related funding cost.

4 Administrative expenses

	2001	2000	1999
	£m	£m	£m
Salaries and profit sharing	**1,953**	1,862	1,700
Social security costs	**140**	131	125
Other pension costs (note 43)	**(108)**	(105)	(108)
Staff costs	**1,985**	1,888	1,717
Other administrative expenses	**1,572**	1,490	1,423
	3,557	3,378	3,140

4 Administrative expenses (continued)

	2001	2000	1999
The average number of persons on a headcount basis employed by the Group during the year was as follows:			
UK	**71,184**	67,848	67,576
Overseas	**11,768**	11,847	12,599
	82,952	79,695	80,175

The above staff numbers exclude 5,450 (2000: 6,152; 1999: 4,938) staff employed in the long-term assurance business. Costs of £168 million (2000: £199 million; 1999: £141 million) in relation to those staff are reflected in the valuation of the shareholder's interest in the long-term assurance business.

Details of directors' emoluments, pensions and interests are given on pages 76, 77 and 79 to 81.

During the year PricewaterhouseCoopers, the Group's independent financial accountants, earned the following fees:

	2001 £m	2000 £m	1999 £m
Statutory audit	**4**	4	4
Due diligence and other audit-related work	**13**	7	4
Audit and similar services	**17**	11	8
Consultancy and advisory services	**4**	25	25
Total fees	**21**	36	33

The auditors' remuneration for the holding company was £50,000 (2000: £50,000; 1999: £50,000).

The increase in due diligence and other audit-related work in 2001 comprises principally work in relation to the Group's listing on the New York Stock Exchange and in connection with the bid for Abbey National.

It is the Group's policy to employ PricewaterhouseCoopers on assignments additional to their statutory audit duties, where their expertise and experience with the Group are important, principally relating to tax advice and due diligence reporting on acquisitions, or where they are selected on a competitive basis.

It is the Group's policy to seek competitive tenders for all consultancy projects.

5 Exceptional restructuring costs

In February 2000 the Group announced an efficiency initiative aimed at reducing its overall cost base which continued during 2001. The initiative focuses on improving the Group's infrastructure, consolidation of large scale processing operations and support functions, and streamlining of the branch network combined with the expansion of lower cost delivery channels all of which contributes towards an enhancement in organisational efficiency and customer service. Costs of £167 million (2000: £108 million) were incurred in connection with this programme, mainly comprising severance, software write-off and consultancy costs.

Following completion of the acquisition of Scottish Widows in March 2000, the Group has been progressively integrating its businesses with its existing insurance and investments activities and rationalising the processes. During 2001 costs of £50 million (2000: £59 million) were incurred, principally relating to the integration and centralisation of back office support functions, the streamlining and automation of client service processes and the redefinition of the sales process.

A provision of £21 million was made in 2000 to cover the cost of integrating Chartered Trust Group plc and ACL Autolease Holdings Limited following their acquisition in September 2000.

6 Amounts written off fixed asset investments

	2001 £m	2000 £m	1999 £m
Debt securities	**58**	27	7
Equity shares	**2**	5	-
	60	32	7

7 Profit (loss) before tax on sale and closure of businesses

	2001 £m	2000 £m	1999 £m
Profit on sale of Brazilian fund management and private banking business (tax: £11 million)	**39**	-	-
Provision for closure of Lloyds TSB Securities Services (tax: nil)	**-**	-	(28)
Provision for sale of Abbey Life new business capability (including £80 million in respect of goodwill previously written off to reserves) (tax: nil)	**-**	-	(98)
	39	-	(126)

During 1999 the Group announced its decision to withdraw from the global custody and unit trust trusteeship business and the consequential run-down and closure of Lloyds TSB Securities Services. A provision was raised in 1999 for the expected operating losses up to the date of closure and this provision was released as the operating losses were incurred over 2000; the closure of Lloyds TSB Securities Services was completed during 2000.

The new business capability of Abbey Life was sold on 1 February 2000. A provision of £98 million was made for the loss on sale in 1999; this loss included £80 million in respect of goodwill previously written off to reserves and other asset write-downs.

8 Profit on ordinary activities before tax

	2001 £m	2000 £m	1999 £m
Profit on ordinary activities before tax is stated after taking account of:			
Income from:			
Aggregate amounts receivable in respect of assets leased to customers and banks under:			
Finance leases and hire purchase contracts	**3,250**	3,295	3,578
Operating leases	**329**	151	62
Profit less losses on disposal of investment securities	**160**	127	74
Charges:			
Rental of premises	**203**	193	195
Hire of equipment	**18**	26	33
Interest on subordinated liabilities (loan capital)	**493**	490	362

9 Tax on profit on ordinary activities

	2001 £m	2000 £m	1999 £m
UK corporation tax			
Current tax on profits for the year	**836**	941	767
Adjustments in respect of prior years	**(14)**	3	21
	822	944	788
Double taxation relief	**(87)**	(72)	(45)
	735	872	743
Foreign tax			
Current tax on profits for the year	**179**	137	110
Adjustments in respect of prior years	**(17)**	(5)	8
	162	132	118
Current tax charge	**897**	1,004	861
Deferred tax	**73**	100	245
Associated undertakings and joint ventures	**1**	1	5
	971	1,105	1,111

9 Tax on profit on ordinary activities (continued)

The charge for tax on the profit for the year is based on an average UK corporation tax rate of 30 per cent (2000: 30 per cent; 1999: 30.25 per cent).

The UK corporation tax charge includes £74 million (2000: £171 million; 1999: £67 million) in respect of notional tax on the shareholder's interest in the increase in the value of the long-term assurance business.

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

	2001 £m	2000 £m	1999 £m
Tax charge at average UK corporation tax rate of 30% (2000: 30%; 1999: 30.25%)	**1,065**	1,158	1,106
Change in non-allowable provisions	**(14)**	3	3
Goodwill amortisation	**8**	10	37
Overseas tax rate differences	**21**	14	8
Non-allowable items	**17**	13	9
Gains covered by capital losses brought forward	**(39)**	(14)	(7)
Tier 1 capital	**(19)**	(12)	-
Payment to employee trust	**(60)**	(37)	(64)
Other items	**(8)**	(30)	19
Tax on profit on ordinary activities	**971**	1,105	1,111
Effective rate	**27.4%**	28.6%	30.4%

10 Ordinary dividends

	2001 pence per share	2000 pence per share	1999 pence per share	**2001 £m**	2000 £m	1999 £m
Interim: paid	**10.2**	9.3	8.1	**566**	511	440
Final: proposed	**23.5**	21.3	18.5	**1,306**	1,172	1,011
	33.7	30.6	26.6	**1,872**	1,683	1,451

11 Earnings per share

	2001	2000	1999
Profit attributable to shareholders*	**£2,500m**	£2,706m	£2,539m
Weighted average number of ordinary shares in issue during the year**	**5,533m**	5,487m	5,445m
Dilutive effect of options outstanding	**50m**	58m	101m
Diluted weighted average number of ordinary shares in issue during the year	**5,583m**	5,545m	5,546m
Earnings per share	**45.2p**	49.3p	46.6p
Diluted earnings per share	**44.8p**	48.8p	45.8p

* No adjustment was made to profit attributable to shareholders in calculating diluted earnings per share.

** The weighted average number of shares for the year has been calculated after deducting 15 million (2000: 9 million; 1999: 11 million) ordinary shares held by Lloyds TSB Group Holdings (Jersey) Limited, and the trustees of the TSB Group Employee Trust, the Lloyds TSB Group Employee Share Ownership Trust and the Lloyds TSB Qualifying Employee Share Ownership Trust, on which dividends have been waived (note 26).

12 Treasury bills and other eligible bills

	2001 Balance sheet £m	2001 Valuation £m	2000 Balance sheet £m	2000 Valuation £m
Banking securities:				
Treasury bills and similar securities	**748**	**748**	121	119
Other eligible bills	**2,034**	**2,032**	509	508
	2,782	**2,780**	630	627
Trading securities:				
Treasury bills and similar securities	**1,630**		1,032	
Other eligible bills	**-**		47	
	1,630		1,079	
	4,412		1,709	
Included above:				
Unamortised discounts net of premiums on banking securities	**6**		2	

Movements in banking securities comprise:	Cost £m	Premiums and discounts £m	Total £m
At 1 January 2001	**626**	**4**	**630**
Exchange and other adjustments	**(3)**	**-**	**(3)**
Additions	**28,367**	**-**	**28,367**
Bills sold or matured	**(26,213)**	**(80)**	**(26,293)**
Amortisation of premiums and discounts	**-**	**81**	**81**
At 31 December 2001	**2,777**	**5**	**2,782**

Banking securities are those intended for use on a continuing basis in the activities of the Group and not for dealing purposes.

The difference between the cost of trading securities and market value, where the market value is higher than the cost, is not disclosed as its determination is not practicable.

13 Loans and advances to banks

	2001 £m	2000 £m
Lending to banks	**1,616**	565
Deposits placed with banks	**13,610**	14,731
Total loans and advances to banks	**15,226**	15,296
Provisions for bad and doubtful debts	**(2)**	(6)
	15,224	15,290
Repayable on demand	**2,443**	2,794
Other loans and advances by residual maturity repayable:		
3 months or less	**8,995**	10,352
1 year or less but over 3 months	**2,698**	1,365
5 years or less but over 1 year	**708**	478
Over 5 years	**382**	307
Provisions for bad and doubtful debts	**(2)**	(6)
	15,224	15,290

14 Loans and advances to customers	**2001 £m**	2000* £m
Lending to customers	**111,541**	102,648
Hire purchase debtors	**5,345**	5,172
Equipment leased to customers	**7,585**	8,122
Total loans and advances to customers	**124,471**	115,942
Provisions for bad and doubtful debts	**(1,466)**	(1,420)
Interest held in suspense	**(70)**	(90)
	122,935	114,432
Loans and advances by residual maturity repayable:		
3 months or less	**20,468**	20,968
1 year or less but over 3 months	**9,792**	8,216
5 years or less but over 1 year	**27,910**	24,313
Over 5 years	**66,301**	62,445
Provisions for bad and doubtful debts	**(1,466)**	(1,420)
Interest held in suspense	**(70)**	(90)
	122,935	114,432
Of which repayable on demand or at short notice	**7,804**	9,342

* restated (see note 1)

The cost of assets acquired during the year for letting to customers under finance leases and hire purchase contracts amounted to £3,166 million (2000: £2,754 million).

Equipment leased to customers, which is stated after deducting £5,905 million (2000: £6,007 million) of unearned charges, is repayable as follows:

	2001 £m	2000 £m
3 months or less	**157**	212
1 year or less but over 3 months	**511**	493
5 years or less but over 1 year	**1,653**	1,803
Over 5 years	**5,264**	5,614
	7,585	8,122

Securitisations

Certain instalment credit receivables have been securitised and are subject to non-returnable financing arrangements. In accordance with Financial Reporting Standard 5, these items have been shown under the linked presentation method.

The Group's subsidiary, Black Horse Limited (formerly Chartered Trust plc), entered into transactions whereby it disposed of its interest in portfolios of motor vehicle and caravan instalment credit agreements for a total of £980 million to Cardiff Automobile Receivables Securitisation (UK) No 4 plc ('CARS 4'). CARS Trustee (UK) No 4 Limited is responsible for the collection and onward payment of all amounts falling due under the terms of the receivables sold to CARS 4. Principal receipts up to 10 December 2000 were used to purchase further receivables; subsequent to this date they are being used to redeem floating rate notes. Income receipts are applied in the following order of priority: interest due on the floating rate notes; credit manager fees; payments under swaps; amounts due to third parties; dividends; and residual income to Black Horse Limited. Black Horse Limited has been appointed by CARS Trustee (UK) No 4 Limited as credit manager and receives a fee for fulfilling this function. It has no liability to the noteholders or any creditor of CARS 4 or CARS Trustee (UK) No 4 Limited other than through failure to meet its obligations as credit manager or for breach of warranties given. Black Horse Limited has no interest in the share capital of CARS 4 or CARS Trustee (UK) No 4 Limited.

Black Horse Limited and CARS 4 have also entered into interest rate swaps in respect of this transaction, the interest rates payable and receivable under these swaps are set by reference to market rates of interest on an arm's length basis.

At 31 December 2001 CARS 4 held £124 million (2000: £400 million) of receivables, matched by non-returnable finance of the same amount.

15 Provisions for bad and doubtful debts and non-performing lending

	2001 Specific £m	**2001 General £m**	2000 Specific £m	2000 General £m	1999 Specific £m	1999 General £m
At 1 January	**1,069**	**357**	1,053	361	1,097	365
Exchange and other adjustments	**(15)**	**1**	4	(2)	(45)	(4)
Adjustments on acquisition	**-**	**-**	45	4	-	-
Advances written off	**(885)**	**-**	(745)	-	(744)	-
Recoveries of advances written off in previous years	**194**	**-**	165	-	130	-
Charge (release) to profit and loss account:						
New and additional provisions						
- normal coverage	**1,310**	**9**	1,093	7	1,087	7
- credit difficulties in Argentina	**-**	**55**	-	-	-	-
Releases and recoveries	**(574)**	**(53)**	(546)	(13)	(472)	(7)
	736	**11**	547	(6)	615	-
At 31 December	**1,099**	**369**	1,069	357	1,053	361

	2001	2000	1999
	1,468	1,426	1,414
In respect of:			
Loans and advances to banks	**2**	6	6
Loans and advances to customers	**1,466**	1,420	1,408
	1,468	1,426	1,414

	2001 £m	2000 £m
Non-performing lending comprises:		
Accruing loans on which interest is being placed in suspense	**843**	855
Loans accounted for on a non-accrual basis	**379**	404
	1,222	1,259
Provisions	**(829)**	(807)
Interest held in suspense	**(70)**	(90)
	323	362

16 Concentrations of exposure

	2001 £m	2000* £m
Loans and advances to customers		
Domestic:		
Agriculture, forestry and fishing	**2,074**	2,026
Manufacturing	**3,321**	3,357
Construction	**1,309**	1,016
Transport, distribution and hotels	**4,440**	3,836
Property companies	**2,907**	2,470
Financial, business and other services	**8,736**	9,295
Personal : mortgages	**56,578**	52,659
: other	**12,784**	11,138
Lease financing	**7,552**	8,070
Hire purchase	**5,345**	5,172
Other	**2,992**	2,526
Total domestic	**108,038**	101,565
International:		
Latin America	**2,347**	2,222
New Zealand	**8,435**	7,368
Rest of the world	**5,651**	4,787
Total international	**16,433**	14,377
	124,471	115,942
Provisions for bad and doubtful debts**	**(1,466)**	(1,420)
Interest held in suspense **	**(70)**	(90)
	122,935	114,432

* restated (see note 1)

** Figures exclude provisions and interest held in suspense relating to loans and advances to banks.

The classification of lending as domestic or international is based on the location of the office recording the transaction, except for certain lending of the international business booked in London.

17 Debt securities	**2001 Balance sheet £m**	**2001 Valuation £m**	2000 Balance sheet £m	2000 Valuation £m
Investment securities:				
Government securities	**1,646**	**1,842**	1,729	2,148
Other public sector securities	**-**	**-**	1	1
Bank and building society certificates of deposit	**4,670**	**4,677**	3,034	3,034
Other debt securities	**4,673**	**4,684**	1,631	1,631
	10,989	**11,203**	6,395	6,814
Other securities:				
Government securities	**4,103**	**4,103**	3,060	3,060
Other public sector securities	**151**	**151**	131	131
Bank and building society certificates of deposit	**234**	**234**	105	105
Other debt securities	**8,748**	**8,748**	4,914	4,914
	24,225	**24,439**	14,605	15,024
Due within 1 year	**6,745**		5,405	
Due 1 year and over	**17,480**		9,200	
	24,225		14,605	
Unamortised discounts net of premiums on investment securities	**622**		904	
Investment securities:				
Listed	**4,703**	**4,900**	2,644	3,063
Unlisted	**6,286**	**6,303**	3,751	3,751
	10,989	**11,203**	6,395	6,814
Other securities:				
Listed	**11,543**	**11,543**	7,289	7,289
Unlisted	**1,693**	**1,693**	921	921
	13,236	**13,236**	8,210	8,210

	Cost £m	**Premiums and discounts £m**	**Provisions £m**	**Total £m**
Movements in investment securities comprise:				
At 1 January 2001	**5,881**	**543**	**29**	**6,395**
Exchange and other adjustments	**33**	**8**	**-**	**41**
Additions	**18,672**	**-**	**-**	**18,672**
Transfers	**(46)**	**(10)**	**-**	**(56)**
Securities sold or matured	**(13,987)**	**(84)**	**(4)**	**(14,067)**
Charge for the year	**-**	**-**	**58**	**(58)**
Amortisation of premiums and discounts	**-**	**62**	**-**	**62**
At 31 December 2001	**10,553**	**519**	**83**	**10,989**

Investment securities are those intended for use on a continuing basis in the activities of the Group and not for dealing purposes.

The difference between the cost of other securities and market value, where the market value is higher than the cost, is not disclosed as its determination is not practicable.

18 Equity shares

	2001 Balance sheet £m	2001 Valuation £m	2000 Balance sheet £m	2000 Valuation £m
Investment securities:				
Listed	**4**	**14**	7	45
Unlisted	**34**	**52**	34	57
	38	**66**	41	102
Other securities:				
Listed	**187**		204	
Unlisted	**-**		2	
	187		206	
	225		247	

	Cost £m	Provisions £m	Total £m
Movements in investment securities comprise:			
At 1 January 2001	**54**	**13**	**41**
Exchange and other adjustments	**(1)**	**-**	**(1)**
Additions	**10**	**-**	**10**
Disposals	**(13)**	**(3)**	**(10)**
Charge for the year	**-**	**2**	**(2)**
At 31 December 2001	**50**	**12**	**38**

Investment securities are those intended for use on a continuing basis in the activities of the Group and not for dealing purposes.

The difference between the cost of other securities and market value, where the market value is higher than the cost, is not disclosed as its determination is not practicable.

19 Assets transferred under sale and repurchase transactions

Included in the Group's balance sheet are assets subject to sale and repurchase agreements as follows:

	2001 £m	2000 £m
Treasury bills and other eligible bills	**1,036**	546
Debt securities	**4,498**	3,543
	5,534	4,089

These investments have been sold to third parties but, since the Group is committed to reacquire them at a future date and at a predetermined price, they are shown in the balance sheet.

20 Interests in associated undertakings and joint ventures

	£m
At 1 January 2001	**9**
Additions	**44**
Disposals	**(1)**
Retained profits	**(13)**
At 31 December 2001	**39**

The Group's principal investments are in two joint ventures:

	Group interest	Nature of business
iPSL	19.5% of issued ordinary share capital	Cheque processing
Goldfish Holdings Limited	25.0% of issued ordinary share capital	Financial services

During 2001 the Group established Goldfish Holdings Limited, a joint venture with Centrica plc for the provision of a broad range of financial services products through Goldfish Holdings Limited's wholly owned subsidiary, Goldfish Bank Limited. By 31 December 2001, the Group had contributed £44 million of capital to the venture.

In the year ended 31 December 2001 £27 million (2000: £4 million; 1999: nil) of fees payable to iPSL have been included in the Group's administrative expenses and £6 million (2000: £1 million; 1999: nil) of charges to iPSL have been included in the Group's income. The Group has also prepaid £8 million (2000: £7 million) of fees in respect of 2002 and this amount is included in prepayments and accrued income; in addition at 31 December 2001 iPSL owed £1 million (2000: £2 million) to the Group, which is included in other assets.

In the year ended 31 December 2001 £1 million of interest receivable from Goldfish Bank Limited and £22 million of charges to Goldfish Bank Limited in respect of administrative costs have been included in the Group's income. At 31 December 2001 Goldfish Bank Limited owed £611 million to the Group, which is included in loans and advances to banks.

21 Interests in group undertakings

The principal group undertakings, all of which have prepared accounts to 31 December and whose results are included in the consolidated accounts of Lloyds TSB Group plc, are:

	Country of registration/ incorporation	Percentage of equity share capital and voting rights held	Nature of business
Lloyds TSB Bank plc	England	100%	Banking and financial services
Cheltenham & Gloucester plc	England	†100%	Mortgage lending and retail investments
Lloyds Bank (BLSA) Limited	England	†100%	Banking and financial services
Lloyds TSB Commercial Finance Limited	England	†100%	Credit factoring
Lloyds TSB Leasing Limited	England	†100%	Financial leasing
Lloyds TSB Private Banking Limited	England	†100%	Private banking
The Agricultural Mortgage Corporation PLC	England	†100%	Long-term agricultural finance
The National Bank of New Zealand Limited	New Zealand	†100%	Banking and financial services
Lloyds TSB Bank (Jersey) Limited	Jersey	†100%	Banking and financial services
Lloyds TSB Scotland plc	Scotland	†100%	Banking and financial services
Lloyds TSB General Insurance Limited	England	†100%	General insurance
Scottish Widows Investment Partnership Group Limited	England	†100%	Investment management
Abbey Life Assurance Company Limited	England	†100%	Life assurance
Lloyds TSB Insurance Services Limited	England	†100%	Insurance broking
Lloyds TSB Life Assurance Company Limited	England	†100%	Life assurance and other financial services
Lloyds TSB Asset Finance Division Limited	England	†100%	Consumer credit, leasing and related services
Black Horse Limited	England	†100%	Consumer credit, leasing and related services
Scottish Widows plc	Scotland	†100%	Life assurance
Scottish Widows Annuities Limited	Scotland	†100%	Life assurance

† Indirect interest

The country of registration/incorporation is also the principal area of operation for each of the above group undertakings except as follows:

Lloyds TSB Bank plc operates principally in the UK but also through branches in Argentina, Belgium, Brazil, Dubai, Gibraltar, Guatemala, Hong Kong, Honduras, Japan, Luxembourg, Malaysia, Monaco, Netherlands, Panama, Paraguay, Singapore, Spain, Switzerland, Uruguay, the USA and a representative office in Iran. Lloyds Bank (BLSA) Limited operates in Ecuador. The National Bank of New Zealand Limited also operates through a representative office in Hong Kong.

22 Intangible fixed assets

	Cost £m	**Amortisation £m**	**Net book value £m**
Goodwill			
At 1 January 2001	**2,635**	**36**	**2,599**
Exchange and other adjustments	**(3)**	**(1)**	**(2)**
Acquisition (note 46)	**8**	**-**	**8**
Charge for the year	**-**	**39**	**(39)**
At 31 December 2001	**2,640**	**74**	**2,566**

23 Tangible fixed assets

	Premises £m	Equipment £m	Operating lease assets £m
Cost:			
At 1 January 2001	**1,052**	**2,343**	**1,411**
Exchange and other adjustments	**(14)**	**(22)**	**8**
Additions	**91**	**310**	**680**
Disposals	**(55)**	**(361)**	**(328)**
At 31 December 2001	**1,074**	**2,270**	**1,771**
Depreciation:			
At 1 January 2001	**284**	**1,354**	**131**
Exchange and other adjustments	**(4)**	**(10)**	**-**
Charge for the year	**61**	**253**	**197**
Disposals	**(7)**	**(319)**	**(190)**
At 31 December 2001	**334**	**1,278**	**138**
Balance sheet amount at 31 December 2001	**740**	**992**	**1,633**
		3,365	
Balance sheet amount at 31 December 2000	768	989	1,280
		3,037	

	2001 £m	2000 £m
Balance sheet amount of premises comprises:		
Freeholds	**436**	490
Leaseholds 50 years and over unexpired	**36**	22
Leaseholds less than 50 years unexpired	**268**	256
	740	768
Land and buildings occupied for own activities	**664**	691

The Group's residual value exposure in respect of operating lease assets, all of which are expected to be disposed of at the end of the lease terms, was as follows:

	2001 £m	2000 £m
Residual value expected to be recovered in:		
1 year or less	**156**	134
2 years or less but over 1 year	**119**	108
5 years or less but over 2 years	**388**	367
Over 5 years	**482**	301
Total exposure	**1,145**	910

24 Lease commitments

At 31 December 2001, the Group was committed to various non-cancellable operating leases, which require aggregate future rental payments as follows:

	Premises £m	**Equipment £m**
Payable within one year	**221**	**8**
1 to 2 years	**212**	**3**
2 to 3 years	**196**	**1**
3 to 4 years	**189**	**-**
4 to 5 years	**186**	**-**
Over 5 years	**337**	**-**
	1,341	**12**

Annual commitments under non-cancellable operating leases were:

	2001 Premises £m	**2001 Equipment £m**	2000 Premises £m	2000 Equipment £m
Leases on which the commitment is due to expire in:				
1 year or less	**7**	**5**	3	1
5 years or less but over 1 year	**33**	**3**	18	2
Over 5 years	**181**	**-**	184	-
	221	**8**	205	3

Obligations under finance leases were:	**2001 Equipment £m**	2000 Equipment £m
Amounts payable in:		
1 year or less	**3**	20
5 years or less but over 1 year	**-**	3
	3	23

25 Capital commitments

Capital expenditure contracted but not provided for at 31 December 2001 amounted to £137 million (2000: £33 million) of which £125 million (2000: £28 million) relates to assets to be leased to customers under operating leases.

26 Own shares

Lloyds TSB Group plc sponsors the Lloyds TSB Group Employee Share Ownership Trust, a discretionary trust for the benefit of employees and former employees of the Lloyds TSB Group. Lloyds TSB Group plc has lent £22 million to the trustees, interest free, to enable them to purchase Lloyds TSB Group plc ordinary shares, which are used to satisfy options granted by Lloyds TSB Group plc or to meet commitments arising under other employee share schemes. Under the terms of the trust, the trustees have waived all but a nominal dividend on the shares they hold. The cost of providing these shares is charged to the profit and loss account on a systematic basis over the period that the employees are expected to benefit. At 31 December 2001, 2 million shares were held by the trustees with a book value of £15 million and a market value of £15 million (2000: 3 million shares with a book value of £24 million and a market value of £22 million).

Lloyds TSB Group plc also sponsored the TSB Group Employee Trust, a further discretionary trust for the benefit of employees and former employees of the Lloyds TSB Group. The shares in this trust were exhausted during 2001; at 31 December 2000, 0.1 million shares were held by the trustees with a book value of £0.2 million and a market value of £0.5 million. The trust currently holds no assets and full provision has been made against the outstanding amount of Lloyds TSB Group plc's loan to the trust.

26 Own shares (continued)

The Group has also established the Lloyds TSB Qualifying Employee Share Ownership Trust ('the QUEST') for the purpose of delivering shares on the exercise of options under certain of the Group's Save As You Earn (SAYE) share option schemes. During 2001, Lloyds TSB Group plc contributed £200 million to the QUEST, and the trustees subscribed for 47 million shares in Lloyds TSB Group plc for a consideration of £316 million. During 2000, Lloyds TSB Group plc contributed £122 million and the trustees subscribed for 30 million shares for a consideration of £193 million. At 31 December 2001, 2 million shares were held by the QUEST with a book value of £8 million (2000: 1 million shares with a book value of £4 million) reflecting the exercise price of the options the shares are expected to be used to satisfy. Under the terms of the QUEST's trust deed, the trustees have waived all but a nominal dividend on the shares they hold. The difference between the amount contributed by Lloyds TSB Group plc and the book value of the shares held by the QUEST at 31 December 2001 has been charged to profit and loss account reserves.

In addition, a further 0.5 million ordinary shares were held by Lloyds TSB Group Holdings (Jersey) Limited at 31 December 2001 (2000: 0.8 million shares). These shares, on which the dividend entitlement has been waived, were gifted to the Group some years ago at nil cost and are used to satisfy outstanding options or to meet commitments arising under other employee share schemes.

27 Other assets

	2001 **£m**	2000* £m
Foreign exchange and interest rate contracts (note 45a)	**2,090**	2,688
Balances arising from derivatives used for hedging purposes	**931**	431
Settlement balances	**570**	121
Other assets	**877**	758
	4,468	3,998

* restated (see note 1)

28 Prepayments and accrued income

	2001 **£m**	2000 £m
Interest receivable	**843**	875
Pensions prepayment	**894**	768
Deferred expenditure incurred under cash gift and discount mortgage schemes	**256**	242
Other debtors and prepayments	**1,197**	1,080
	3,190	2,965

29 Long-term assurance business

a Methodology

The value of the shareholder's interest in the long-term assurance business ("the embedded value") is comprised of the net tangible assets of the life assurance subsidiaries, including any surplus retained in the long-term business funds, which could be transferred to shareholders, and the present value of the in-force business. The value of the in-force business is calculated by projecting future surpluses and other net cash flows attributable to the shareholder arising from business written by the balance sheet date and discounting the result at a rate which reflects the shareholder's overall risk premium.

Surpluses arise following annual actuarial valuations of the long-term business funds, which are carried out in accordance with the statutory requirements designed to ensure and demonstrate the solvency of the funds. Future surpluses will depend upon experience in a number of areas such as investment returns, lapse rates, mortality and administrative expenses. Surpluses can be projected by making realistic assumptions about future experience, having regard to both actual experience and forecast long-term economic trends. Other net cash flows principally comprise annual management charges and other fees levied upon the policyholders by the life assurance subsidiaries.

Changes in the embedded value, which are determined on a post-tax basis, are included in the profit and loss account and described as income from long-term assurance business. For the purpose of presentation the change in this value is grossed up at the underlying rate of corporation tax.

b Analysis of embedded value

The embedded value included in the consolidated balance sheet comprises:

	2001	2000
	£m	£m
Net tangible assets of life companies including surplus	**3,985**	4,128
Value of other shareholder's interests in the long-term assurance business	**2,589**	2,421
	6,574	6,549

Movements in the embedded value balance have been as follows:

	2001	2000
	£m	£m
At 1 January	**6,549**	2,274
Exchange and other adjustments	**(35)**	(92)
Profit after tax	**115**	441
Capital injection	**100**	-
Dividends	**(155)**	(126)
Acquisitions	**-**	4,052
	6,574	6,549

c Analysis of income from long-term assurance business

Income from long-term assurance business included in the profit and loss account can be divided into those items comprising the operating profit of the business and other items. Included within operating profit are the following items:

New business contribution: this represents the value recognised at the end of the year from new business written during the year after taking into account the cost of establishing technical provisions and reserves.

Contribution from existing business: this comprises the following elements:

- the expected return arising from the unwinding of the discount applied to the expected cash flows at the beginning of the year;
- experience variances caused by the differences between the actual experience during the year and the expected experience; and
- the effects of changes in assumptions other than economic assumptions, and other items.

Investment earnings: this represents the expected investment return on both the net tangible assets and the value of the shareholder's interest in the long-term business account, based upon the economic assumptions made at the beginning of the year.

29 Long-term assurance business (continued)

c Analysis of income from long-term assurance business (continued)

Distribution costs: this represents the actual cost of acquiring new business during the year and includes commissions paid to independent financial advisors and other direct sales costs.

Included within other items are:

Short-term fluctuations in investment returns: this represents (a) the difference between the actual investment return in the year on investments backing shareholder funds and the expected return based upon the economic assumptions made at the beginning of the year: this is recognised immediately; and (b) the effect of these fluctuations on the value of in-force business which is recognised using smoothed fund values.

Changes in economic assumptions: this represents the effect of changes in the economic assumptions referred to in f.

Exceptional items: this includes any other items which, by virtue of their size or incidence, are considered not to form part of the ongoing operating profit.

Income from long-term assurance business is set out below:

	2001 £m	2000 £m	1999 £m
New business contribution	**374**	305	156
Contribution from existing business			
- expected return	**359**	311	185
- experience variances	**37**	36	26
- changes in assumptions and other items	**95**	96	(13)
Investment earnings	**247**	212	38
Distribution costs	**(247)**	(225)	(99)
Operating profit	**865**	735	293
Short-term fluctuations in investment returns	**(602)**	(67)	36
Changes in economic assumptions	**-**	127	-
Exceptional items			
- Pension provisions (see d)	**(70)**	(100)	(102)
- Stakeholder pension related charge (see e)	**-**	(80)	-
Income from long-term assurance business before tax	**193**	615	227
Tax	**(78)**	(174)	(69)
Income from long-term assurance business after tax	**115**	441	158

Income before tax from long-term assurance business can also be analysed as follows:

	2001 £m	2000 £m	1999 £m
Income net of claims and technical provisions	**636**	937	621
Pension provisions	**(70)**	(100)	(102)
Operating expenses	**(557)**	(471)	(291)
Tax charged to technical account	**(62)**	(191)	(159)
(Deficit retained) surplus emerging	**(53)**	175	69
Value of in-force business	**168**	266	89
Income from long-term assurance business after tax	**115**	441	158
Tax	**78**	174	69
Income from long-term assurance business before tax	**193**	615	227

29 Long-term assurance business (continued)

d Pension provisions

During the early 1990's, there was increasing concern in the UK that many customers had been given poor advice when they were advised to set up their own personal pension plan and that they would, in fact, have been in a better position if they had remained in, or joined, employer sponsored pension schemes. The regulator of the UK pension industry (now the responsibility of the Financial Services Authority) carried out an industry wide investigation into the conduct of business involving the transfer of pensions. The conclusion of the investigation was that a large number of customers had been poorly advised, by insurance companies and intermediaries across the industry. As a result of this investigation the regulator established an action plan for the UK pensions industry to follow in reviewing all cases of possible misselling and determining the necessary compensation. As the review of pension cases in the Group has progressed, provisions have been established for the estimated cost of compensation.

Movements in the provision over the last three years have been as follows:

	2001	2000	1999
	£m	£m	£m
At 1 January	**352**	397	472
Accrual of interest on the provision	**20**	26	22
Charge for the year	**70**	100	102
Compensation paid	**(238)**	(173)	(161)
Guarantees*	**(1)**	2	(38)
At 31 December	**203**	352	397

*In some cases, rather than pay cash compensation directly into the customer's personal pension plan, the Group has guaranteed to 'top up' the customer's pension income on retirement, to the level that they would have received under the relevant occupational scheme.

During the second half of 1999, the Financial Services Authority published revised assumptions to be incorporated into the calculations of the continuing cost of redress reflecting the fact that the average life expectancy of pensioners had increased and interest and inflation rates were lower. Applying these guidelines, the cost of redress was forecast to increase by £102 million and an additional provision of this amount was raised in the accounts for the year ended 31 December 1999.

By the end of 2000, the Group had gained further experience as to the number and size of claims likely to require compensation, in particular those affected by the revised guidelines issued towards the end of 1999 dealing with the way in which compensation should be calculated for those customers who had opted out of the State Earnings Related Pension Scheme. After taking this into account, the cost of redress was forecast to increase by £100 million and a provision of this amount was made.

A further review of the adequacy of the provision has been carried out as at 31 December 2001. Lower stock market levels have had a significant impact on total redress costs as the cost of restitution into company pension schemes rises as personal pension fund values reduce. As a result of this and the fact that there is now greater certainty as to the number and size of compensation claims to be paid, an additional provision of £70 million has been made.

e Stakeholder pension related charge

During 1999, the government announced changes intended to encourage more of the population to provide retirement income for themselves through increased rates of savings. One of these initiatives was the introduction of stakeholder pensions with effect from April 2001; a key feature of these products is that charges are limited to 1 per cent per annum, which is significantly lower than historic charging rates on other personal pension products. In anticipation of the introduction of stakeholder pension products in 2001, during 2000 the Group decided to reduce the charges made on certain existing policies, resulting in a cost of £80 million.

29 Long-term assurance business (continued)

f Assumptions

The economic assumptions are based upon a long-term view of economic activity and are therefore not adjusted for market movements which are considered to be short-term. This approach is considered to be the most appropriate given the long-term nature of the portfolio of products. The principal economic assumptions which have been used are as follows:

	2001	2000	1999
	%	%	%
Risk-adjusted discount rate (net of tax)	**8.50**	8.50	10.00
Return on equities (gross of tax)	**8.00**	8.00	8.50
Return on fixed interest securities (gross of tax)	**5.25**	5.25	5.25
Expenses inflation	**3.00**	3.00	3.00

Following the acquisition of the business of Scottish Widows in 2000, a review of the economic assumptions used in the embedded value calculation was carried out, to ensure that these assumptions remained appropriate for the enlarged life and pensions business in the context of forecast long-term economic trends. As a result of this review certain economic assumptions were amended, including the risk-adjusted discount rate which was reduced from 10 per cent to 8.5 per cent. The adoption of the revised assumptions, which were used with effect from 1 January 2000 for Abbey Life and the bancassurance operation of Lloyds TSB Life resulted in a credit to the profit and loss account of £127 million in 2000. The same assumptions were used for the Scottish Widows business from the date of acquisition.

Other assumptions used to derive the embedded value are as follows:

- Assumed rates of mortality and morbidity are taken from published tables adjusted for demographic differences. Assumptions in respect of lapse rates reflect the recent actual experience of the companies concerned.

- Current tax legislation and rates have been assumed to continue unaltered, except where future changes have been announced. The UK corporation tax rate used for grossing up was 30% (2000: 30%; 1999: 30.25%). The investment earnings have been grossed up at a composite longer term tax rate of 17% (2000: 17%; 1999: 30.25%).

- The value of the in-force business does not allow for future premiums under recurring single premium business or non-contractual increments, which are included in new business when the premium is received. Department of Social Security rebates have been treated as recurring single premiums.

- Future bonus rates on with-profits business are set at levels which would fully utilise the assets supporting the with-profits business. The proportion of profits derived from with-profits business allocated to the shareholder has been assumed to continue at the current rate of one-ninth of the cost of the bonus.

g Balance sheet

The long-term assurance assets attributable to policyholders comprise:

	2001	2000
	£m	£m
Investments	**47,910**	52,683
Premises and equipment	**16**	20
Other assets	**2,448**	2,510
	50,374	55,213
Net tangible assets of life companies including surplus	**(3,985)**	(4,128)
	46,389	51,085

Investments shown above comprise:

Fixed interest securities	**12,642**	14,512
Stocks, shares and unit trusts	**27,018**	31,885
Investment properties	**3,722**	3,098
Other properties	**121**	10
Mortgages and loans	**102**	117
Deposits	**4,305**	3,061
	47,910	52,683

29 Long-term assurance business (continued)

g Balance sheet (continued)

	2001 £m	2000 £m
The liabilities to policyholders comprise:		
Technical provisions:		
Long-term business provision (net of reinsurance)	**24,151**	23,514
Claims outstanding (net of reinsurance)	**211**	172
Technical provisions for linked liabilities	**21,083**	24,413
Fund for future appropriations	**95**	1,667
Other liabilities	**849**	1,319
	46,389	51,085

30 Assets and liabilities denominated in foreign currencies

		2001 £m	2000* £m
Assets	: denominated in sterling	**133,558**	126,753
	: denominated in other currencies	**56,592**	41,275
		190,150	168,028
Liabilities	: denominated in sterling	**133,661**	127,267
	: denominated in other currencies	**56,489**	40,761
		190,150	168,028

* restated (see note 1)

31 Deposits by banks

	2001 £m	2000 £m
Repayable on demand	**6,634**	4,330
Other deposits by banks with agreed maturity dates or periods of notice by residual maturity repayable:		
3 months or less	**14,227**	9,712
1 year or less but over 3 months	**2,529**	1,790
5 years or less but over 1 year	**751**	695
Over 5 years	**169**	208
	24,310	16,735

The breakdown of deposits by banks between the domestic and international offices of the Group is set out below:

	2001 £m	2000 £m
Domestic		
Non-interest bearing	**601**	612
Interest bearing	**18,535**	11,816
	19,136	12,428
International		
Non-interest bearing	**80**	177
Interest bearing	**5,094**	4,130
	5,174	4,307
Total	**24,310**	16,735

32 Customer accounts

	2001 £m	2000* £m
Repayable on demand	**80,635**	74,404
Other customer accounts with agreed maturity dates or periods of notice by residual maturity repayable:		
3 months or less	**19,902**	21,064
1 year or less but over 3 months	**2,889**	3,522
5 years or less but over 1 year	**3,369**	2,582
Over 5 years	**2,321**	417
	109,116	101,989

The breakdown of customer accounts between the domestic and international offices of the Group is set out below:

	2001 £m	2000* £m
Domestic		
Non-interest bearing	**6,874**	5,522
Interest bearing	**92,920**	87,698
	99,794	93,220
International		
Non-interest bearing	**758**	619
Interest bearing	**8,564**	8,150
	9,322	8,769
Total	**109,116**	101,989

* restated (see note 1)

33 Debt securities in issue

	2001 £m	2000 £m
Bonds and medium-term notes by residual maturity repayable:		
1 year or less	**589**	538
2 years or less but over 1 year	**178**	169
5 years or less but over 2 years	**405**	472
Over 5 years	**928**	1,413
	2,100	2,592
Other debt securities by residual maturity repayable:		
3 months or less	**17,070**	8,574
1 year or less but over 3 months	**4,931**	6,476
5 years or less but over 1 year	**104**	241
Over 5 years	**215**	16
	22,320	15,307
	24,420	17,899

Debt securities in issue includes certificates of deposit of £17,060 million (2000: £12,052 million) and commercial paper of £1,966 million (2000: £1,850 million). An amount of £996 million (2000: £929 million) relating to debt securities issued under the Group's Euro Medium Term Note programme is included in these figures.

34 Other liabilities

	2001 £m	2000* £m
Foreign exchange and interest rate contracts (note 45a)	**2,288**	2,346
Balances arising from derivatives used for hedging purposes	**475**	1,071
Current tax	**598**	631
Dividends	**1,306**	1,172
Settlement balances	**542**	232
Other liabilities	**1,464**	1,148
	6,673	6,600

* restated (see note 1)

35 Accruals and deferred income

	2001 **£m**	2000* £m
Interest payable	**1,310**	1,670
Other creditors and accruals	**2,253**	2,504
	3,563	4,174

* restated (see note 1)

36 Deferred tax

	2001 **£m**	2000 £m
Short-term timing differences	**(89)**	(59)
Pensions prepayment	**268**	230
Emerging Markets Debt securities	**(70)**	(74)
Accelerated depreciation allowances	**1,610**	1,586
	1,719	1,683

	£m
At 1 January 2001	**1,683**
Exchange and other adjustments	**7**
Adjustments on disposal	**(44)**
Tax provided	**73**
At 31 December 2001	**1,719**

	2001 **£m**	2000 £m
Potential tax for which no provision has been made relating to accelerated depreciation allowances on equipment leased to customers	**72**	72

Provision has been made for the liability to tax on overseas earnings which are expected to be remitted to the UK. No provision has been made for the liability to tax which could arise if premises, to the extent that the tax base cost has been reduced by rollover relief, were disposed of at their balance sheet amounts. It is expected that the majority of these assets will be retained in the business and that, in view of the substantial number of assets involved and the law relating to rollover relief, the likelihood of any such material tax liability arising is remote; no useful purpose would be served by attempting to quantify it. If deferred tax were to be provided in respect of general bad debt provisions the deferred tax asset would be £90 million.

37 Other provisions for liabilities and charges

	Pension obligations £m	Insurance provisions £m	Post-retirement healthcare £m	Vacant leasehold property £m	Other £m	Total £m
At 1 January 2001	**34**	**202**	**76**	**96**	**34**	**442**
Exchange and other adjustments	**-**	**6**	**-**	**-**	**(1)**	**5**
Provisions applied	**(1)**	**(178)**	**(4)**	**(17)**	**(17)**	**(217)**
Charge for the year	**1**	**174**	**3**	**(10)**	**3**	**171**
At 31 December 2001	**34**	**204**	**75**	**69**	**19**	**401**

Pension obligations

A description of the Group's pension arrangements is provided in note 43a.

Insurance provisions

The Group's general insurance subsidiary maintains provisions for outstanding claims which represent the ultimate cost of settling all claims arising from events which have occurred up to the balance sheet date and these include provisions for the cost of claims notified but not settled and for claims incurred but not yet reported. In addition, in line with the requirements of the Insurance Companies (Reserves) Act 1995, claims equalisation provisions are maintained in relation to property, credit and suretyship business. The majority of provisions in respect of claims will be settled in the following year, although new provisions will then be required in respect of claims arising from that year. The level of the claims equalisation provision will be adjusted annually, taking into account the guidelines contained in the legislation, and such provisions will be held for as long as the Group continues to write the relevant types of general insurance business.

Post-retirement healthcare

A description of the Group's post-retirement healthcare obligations is provided in note 43b.

Vacant leasehold property

Whenever the Group ceases to occupy a property, or commits itself to doing so, it is the Group's policy to raise a provision to cover any anticipated shortfall when comparing the recoverable amount of its interest in the property to the future rental and other payments that the Group is obligated to make over the remaining term of the lease. These provisions are made by reference to a prudent estimate of expected sub-let income and the possibility of disposing of the Group's interest in the lease, taking into account conditions in the property market. These provisions are reassessed on an annual basis and will normally run off over the remaining life of the leases concerned, currently averaging six years; where a property is disposed of earlier than anticipated, any remaining balance in the provision relating to that property is released.

38 Subordinated liabilities

	2001 £m	2000 £m
* *Undated loan capital:*		
† Primary Capital Undated Floating Rate Notes:		
Series 1 (US$750 million)	**516**	502
Series 2 (US$500 million)	**344**	335
Series 3 (US$600 million)	**412**	401
11¾% Perpetual Subordinated Bonds	**100**	100
■ 5? % Undated Subordinated Step-up Notes callable 2009 (€1,250 million)	**757**	774
† Undated Step-up Floating Rate Notes callable 2009 (€150 million)	**91**	94
¶ 6? % Undated Subordinated Step-up Notes callable 2010	**406**	405
✜ 5.57% Undated Subordinated Step-up Coupon Notes callable 2015 (¥20 billion)	**105**	117
¶ 6½% Undated Subordinated Step-up Notes callable 2019	**266**	266
¶ 8% Undated Subordinated Step-up Notes callable 2023	**199**	199
? ¶6½% Undated Subordinated Step-up Notes callable 2029	**455**	198
	3,651	3,391
Dated loan capital:		
Eurocurrency Zero Coupon Bonds 2003 (¥3 billion)	**15**	15
§ Subordinated Fixed Rate Bonds 2003 (NZ$151 million)	**43**	49
† Subordinated Floating Rate Notes 2004	**15**	20
7? % Subordinated Bonds 2004	**399**	399
†❖ Subordinated Floating Rate Notes 2004	**100**	100
§ Subordinated Fixed Rate Bonds 2006	**-**	22
† Subordinated Floating Rate Notes 2006	**-**	100
8½% Subordinated Bonds 2006	**249**	249
7¾% Subordinated Bonds 2007	**299**	298
§ Subordinated Fixed Rate Bonds 2007 (NZ$150 million)	**43**	44
5¼% Subordinated Notes 2008 (DM 750 million)	**234**	240
10? % Guaranteed Subordinated Loan Stock 2008	**100**	100
9½% Subordinated Bonds 2009	**99**	99
† Subordinated Step-up Floating Rate Notes 2009 callable 2004 (US$500 million)	**343**	334
Subordinated Fixed Rate Bonds 2010 (NZ$100 million)	**29**	30
6¼% Subordinated Notes 2010 (€400 million)	**244**	250
† Subordinated Floating Rate Notes 2010 (US$400 million)	**274**	267
12% Guaranteed Subordinated Bonds 2011	**100**	100
9? % Subordinated Bonds 2011	**149**	148
4¾% Subordinated Notes 2011 (€850 million)	**498**	508
✠§ Subordinated Fixed Rate Bonds 2011 (NZ $100 million)	**28**	-
6? % Subordinated Notes 2015	**343**	343
† Subordinated Floating Rate Notes 2020 (€100 million)	**61**	62
9? % Subordinated Bonds 2023	**341**	342
	4,006	4,119
Total subordinated liabilities	**7,657**	7,510

These liabilities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer.

* In certain circumstances, these notes and bonds would acquire the characteristics of preference share capital.
† These notes bear interest at rates fixed periodically in advance based on London Interbank rates.
¶ At the callable date the coupon on these Notes will be reset by reference to the applicable five year benchmark gilt rate.
§ These bonds bear interest, to be reset 5 years before redemption date, at a fixed margin over New Zealand Government stocks.
■ In the event that these Notes are not redeemed at the callable date, the coupon will be reset to a floating rate.
✜ In the event that these Notes are not redeemed at the callable date, the coupon will be reset to a fixed margin over the then 5 year Yen swap rate.
❖ Exchangeable at the election of the Group for further subordinated floating rate notes.
? A further £257 million was issued during 2001 primarily to finance the general business of the Group.
✠ Issued during 2001 primarily to finance the general business of the Group.

38 Subordinated liabilities (continued)

Dated subordinated liabilities are repayable as follows:

	2001 £m	2000 £m
1 year or less	**5**	5
2 years or less but over 1 year	**63**	5
5 years or less but over 2 years	**753**	573
Over 5 years	**3,185**	3,536
	4,006	4,119

39 Non-equity minority interests

Non-equity minority interests comprise:

	2001 £m	2000 £m
Euro Step-up Non-Voting Non-Cumulative Preferred Securities callable 2012 (€430 million) *	**261**	267
Sterling Step-up Non-Voting Non-Cumulative Preferred Securities callable 2015 †	**248**	248
6.625% Perpetual Capital Securities (€750 million) §	**451**	-
	960	515

* These securities constitute limited partnership interests in Lloyds TSB Capital 1 L.P., a Jersey limited partnership in which Lloyds TSB (General Partner) Limited, a wholly owned subsidiary, is the general partner. Non-cumulative income distributions accrue at a fixed rate of 7.375 per cent per annum up to 7 February 2012; thereafter they will accrue at a rate of 2.33 per cent above EURIBOR, to be set annually.

† These securities constitute limited partnership interests in Lloyds TSB Capital 2 L.P., a Jersey limited partnership in which Lloyds TSB (General Partner) Limited, a wholly owned subsidiary of the Group, is the general partner. Non-cumulative income distributions accrue at a fixed rate of 7.834 per cent per annum up to 7 February 2015; thereafter they will accrue at a rate of 3.50 per cent above a rate based on the yield of specified UK government stock.

Both of the above issues were made under the limited subordinated guarantee of Lloyds TSB Bank plc. In certain circumstances these preferred securities will be mandatorily exchanged for preference shares in Lloyds TSB Group plc. Lloyds TSB Group plc has entered into an agreement whereby dividends may only be paid on its ordinary shares if sufficient distributable profits are available for distributions due in the financial year on these preferred securities.

§ These securities were issued during 2001, by Lloyds TSB Bank plc, primarily to finance the general business of the Group. Interest payments accrue at the rate of 6.625 per cent per annum; in certain circumstances these payments can be deferred although in this case neither Lloyds TSB Bank plc nor Lloyds TSB Group plc can declare or pay a dividend until any deferred payments have been made. In the event of a winding up of Lloyds TSB Bank plc, these securities will acquire the characteristics of preference shares. The securities can be redeemed at par at the option of Lloyds TSB Bank plc on or after 25 October 2006.

40 Called-up share capital

	2001	2000	1999
	£m	£m	£m
Authorised:			
Sterling			
6,911 million Ordinary shares of 25p each	**1,728**	1,728	1,728
79 million Limited voting ordinary shares of 25p each	**20**	20	20
300 million Limited voting preference shares of £1 each	**-**	-	300
175 million Preference shares of 25p each	**44**	44	-
	1,792	1,792	2,048
US dollars	**US$m**	US$m	US$m
160 million Preference shares of US25 cents each	**40**	40	-
Euro	**€m**	€m	€m
160 million Preference shares of €25 cents each	**40**	40	-
Japanese yen	**¥m**	¥m	¥m
50 million Preference shares of ¥25 each	**1,250**	1,250	-

	2001	2000	1999
	£m	£m	£m
Issued and fully paid:			
Ordinary shares of 25p each			
At 1 January	**1,376**	1,369	1,359
Issued to the QUEST (note 26)	**12**	7	7
Issued under employee share schemes	**3**	-	3
At 31 December	**1,391**	1,376	1,369
Limited voting ordinary shares of 25p each			
At 1 January and 31 December	**20**	20	20
Total	**1,411**	1,396	1,389
Number of shares in issue (millions):			
Ordinary shares of 25p each	**5,564**	5,507	5,475
Limited voting ordinary shares of 25p each	**79**	79	79

The limited voting ordinary shares are held by the Lloyds TSB Foundations. These shares carry no rights to dividends but rank pari passu with the ordinary shares in respect of other distributions and in the event of winding up. These shares do not have any right to vote at general meetings other than on resolutions concerning acquisitions or disposals of such importance that they require shareholder consent, or for the winding up of Lloyds TSB Group plc, or for a variation in the class rights of the limited voting ordinary shares.

At 31 December 2001, options to acquire 123 million Lloyds TSB Group ordinary shares of 25p each were outstanding under executive share option schemes, the share retention plan, and the staff sharesave share option schemes exercisable up to 2011. These include the option, described on page 74, to acquire 216,763 shares under the share retention plan: otherwise the options are exercisable at prices ranging from 124p to 888p per share.

41 Reserves

	2001 £m	2000 £m	1999 £m
Share premium account:			
At 1 January	**595**	404	101
Premium arising on issue of shares	**364**	191	303
At 31 December	**959**	595	404
Merger reserve:			
At 1 January and 31 December	**343**	343	343
Profit and loss account:			
At 1 January	**7,690**	6,693	5,740
Exchange and other adjustments	**(86)**	(11)	(10)
Shares issued to the QUEST (note 26)	**(185)**	(124)	(205)
Goodwill written back on sale and closure of businesses	**-**	109	80
Retained profit	**628**	1,023	1,088
At 31 December	**8,047**	7,690	6,693

The Group profit and loss account reserves at 31 December 2001 include £1,564 million (2000: £1,396 million; 1999: £1,165 million) not presently available for distribution representing the Group's share of the value of long-term assurance business in force and the surplus retained within the long-term assurance funds.

The cumulative amount of premiums on acquisitions written off against reserves during previous years amounts to £2,271 million of which £1,817 million was within the last 10 years.

The accumulated foreign exchange translation adjustment as at 31 December 2001 reduced the Group's reserves by £259 million (2000: £173 million; 1999: £162 million).

42 Related party transactions

a Transactions, arrangements and agreements involving directors and others

At 31 December 2001, transactions, arrangements and agreements entered into by the Group's banking subsidiaries with directors and connected persons and with officers included:

	2001 Number of persons	**2001 Total £000**	2000 Number of Persons	2000 Total £000
Loans and credit card transactions:				
Directors and connected persons	**7**	**1,343**	10	119
Officers	**28**	**4,113**	36	4,993

b Group undertakings

Details of the principal group undertakings are given in note 21. In accordance with FRS 8, transactions or balances with group entities that have been eliminated on consolidation are not reported.

c Associated undertakings and joint ventures

Details of the Group's associated undertakings and joint ventures are provided in note 20. Information relating to transactions entered into between Group undertakings and the joint ventures and details of outstanding balances at 31 December 2001 are also shown in note 20.

42 Related party transactions (continue)

d Long-term assurance business

The Group enters into certain transactions with its long-term assurance businesses which cannot be eliminated in the consolidated accounts because of the embedded value basis of accounting used for the Group's long-term assurance businesses. After taking into account legally enforceable netting agreements, at 31 December 2001 Group entities owed £1,186 million (2000: £1,251 million) and were owed £299 million (2000: £289 million); these amounts are included in customer accounts and loans and advances to customers respectively. In addition, fees of £62 million (2000: £68 million; 1999: £42 million) were received, and fees of £28 million (2000: £29 million; 1999: £30 million) were paid, in respect of asset management services.

In addition, certain administrative properties used by Scottish Widows are owned by the long-term assurance funds. During 2001 Scottish Widows paid rent to the long-term assurance funds amounting to £4 million (2000: £3 million). In addition, at 31 December 2001, the long-term assurance funds owned 31 million ordinary shares in Lloyds TSB Group plc (2000: 31 million shares).

e Pension funds

Group entities provide a number of banking and other services to the Group's pension funds, which are conducted on similar terms to third party transactions. At 31 December 2001, the Group's pension funds had call deposits with Lloyds TSB Bank plc amounting to £572 million (2000: £344 million).

43 Pensions and other post-retirement benefits

a Pension costs in the consolidated accounts

There was a net credit in respect of pension costs for the Group in 2001 of £108 million (2000: credit of £105 million; 1999: credit of £108 million), which included a credit of £126 million (2000: credit of £121 million; 1999: credit of £121 million) relating to Lloyds TSB Group Pension Schemes No's 1 and 2.

Pension arrangements for most of the staff in the UK and the majority of those overseas are operated through defined benefit schemes funded by Group companies. The principal schemes in operation are Lloyds TSB Group Pension Schemes No's 1 and 2. The defined benefit sections of these schemes are now closed to new members. Pension arrangements for staff joining Lloyds TSB Group Pension Scheme No.1 after 1 January 1996 and Lloyds TSB Group Pension Scheme No. 2 after 1 January 1998 are through money purchase elements of these schemes. Arrangements for pensions of certain staff employed overseas who are not included in funded schemes are made in accordance with local regulations and custom.

Full actuarial valuations of Lloyds TSB Group Pension Schemes No's l and 2 are carried out every three years with interim reviews in the intervening years. At 30 June 1999, the date of the latest full actuarial valuations, the principal actuarial assumptions adopted were that, over the long term, the annual real rate of return on new investments would be 3 per cent higher than the annual increase in pensionable remuneration, 4 per cent higher than the annual increase in present and future pensions in payment, and 3 per cent higher than the annual increase in dividends receivable. The market value of the assets of the schemes at this date was £11,748 million. The actuarial value of the assets represented 125 per cent of the accrued liabilities allowing for future increases in pensions and pensionable remuneration. For funding purposes, the surpluses in the two schemes are being eliminated by means of a contribution holiday.

Contribution rates to other schemes have been adjusted to take account of surpluses and deficiencies.

The following balances relating to the Group's pension schemes are included in the consolidated balance sheet:

	2001	2000
	£m	£m
Pension asset related to Lloyds TSB Group Pension Schemes No's 1 and 2	**894**	768
Pension obligation relating to certain overseas schemes	**(34)**	(34)
Deferred tax	**(268)**	(230)
Net asset	**592**	504

43 Pensions and other post-retirement benefits (continued)

b Post-retirement healthcare costs in the consolidated accounts

The Group operates a number of schemes which provide post-retirement healthcare benefits to certain employees, retired employees and their dependent relatives. The principal scheme relates to former Lloyds Bank staff and under this scheme the Group has undertaken to meet the cost of post-retirement healthcare for all eligible former employees (and their dependants) who retired prior to 1 January 1996. For retirements subsequent to this date, the Group will meet a reducing proportion of the cost until 31 December 2004, after which date the only obligation will be in respect of the pre 1 January 1996 retirements. The cost of providing all post-retirement healthcare benefits is charged to the profit and loss account on a systematic basis over the employees' working lives; the provision represents the unfunded obligation and is based on valuations of the Group's liability by qualified actuaries.

The total cost for the Group in 2001 was £3 million (2000: £3 million; 1999: £17 million). For the principal scheme, the latest actuarial valuation of the liability was carried out at 31 December 2000. This valuation showed the Group's liability to be £72 million, which had been fully provided for at that date. The principal actuarial assumptions adopted were that, over the long term, the valuation discount rate and the rate of increase in medical costs would be 4 per cent and 3 per cent respectively higher than annual price inflation.

c Disclosures made in accordance with Financial Reporting Standard 17

As explained in note 1, the Group has adopted the requirements of Financial Reporting Standard 17 "Retirement Benefits" during the year. Under the transitional arrangements of this accounting standard the Group continues to account for pension costs in accordance with Statement of Standard Accounting Practice 24, but the following additional disclosures are required.

The majority of the Group's employees are members of the defined benefit sections of Lloyds TSB Group Pension Schemes No's 1 and 2. During the year ended 31 December 2001, the Group made no contributions to these schemes. Since the defined benefit sections of these schemes are now closed to new members and the age profile of the active members is increasing, under the projected unit method, the current service cost will increase as the members of the schemes approach retirement.

The last full valuations of the schemes were carried out as at 30 June 1999; interim reviews were performed at 30 June 2001 and these have been updated to 31 December 2001 by qualified independent actuaries. The last full valuations of other Group schemes were carried out on a number of different dates; these have been updated to 31 December 2001 by qualified independent actuaries or, in the case of Scottish Widows Retirement Benefits Scheme, by a qualified actuary employed by Scottish Widows.

The principal assumptions used in these updated valuations were as follows:

	%
Rate of inflation	**2.50**
Rate of salary increases	**4.04**
Rate of increase for pensions in payment and deferred pensions	**2.50**
Discount rate	**6.00**

The assets of the Group's defined benefit schemes and the expected rates of return are summarised as follows:

	Fair value at 31 December 2001 £m	**Expected long-term rate of return at 31 December 2001 % pa**
Market values of scheme assets:		
Equities	**7,779**	**8.0**
Fixed interest securities	**1,835**	**5.1**
Property	**798**	**7.1**
Other	**714**	**4.1**
Total fair value of scheme assets	**11,126**	

43 Pensions and other post-retirement benefits (continued)

c Disclosures made in accordance with Financial Reporting Standard 17 (continued)

The following amounts at 31 December 2001 were measured in accordance with the requirements of FRS 17:

	£m
Market value of assets	**11,126**
Present value of scheme liabilities	**(10,618)**
Surplus in the schemes	**508**
Related deferred tax liability	**(152)**
Net pension asset	**356**

If these amounts had been recognised in the financial statements, the Group's net assets and profit and loss account reserve at 31 December 2001 would have been as follows:

	£m
Net assets excluding net pension asset	**10,168**
Net pension asset	**356**
Net assets including net pension asset	**10,524**
Profit and loss reserve excluding net pension asset	**7,455**
Net pension asset	**356**
Profit and loss reserve including net pension asset	**7,811**

44 Contingent liabilities and commitments

a Contingent liabilities and commitments arising out of banking transactions

	2001 £m	2000 £m
Contingent liabilities:		
Acceptances and endorsements	**2,243**	357
Guarantees	**3,789**	3,249
Other:		
Other items serving as direct credit substitutes	**460**	266
Performance bonds and other transaction-related contingencies	**1,469**	1,271
Other contingent liabilities	**2**	4
	1,931	1,541
	7,963	5,147
Commitments:		
Documentary credits and other short-term trade-related transactions	**354**	238
Forward asset purchases and forward forward deposits placed	**783**	779
Undrawn note issuing and revolving underwriting facilities	**35**	53
Undrawn formal standby facilities, credit lines and other commitments to lend:		
Less than 1 year maturity	**42,594**	33,815
1 year or over maturity	**9,576**	7,701
Commitments arising out of sale and option to resell transactions	**-**	3
	53,342	42,589

b Limited voting ordinary shares (see note 40)

The limited voting ordinary shares are held by the Lloyds TSB Foundations for England & Wales, Scotland, Northern Ireland and the Channel Islands; these shares do not carry any entitlement to dividends. Lloyds TSB Group plc has entered into deeds of covenant with the four foundations, under the terms of which Lloyds TSB Group plc makes annual donations to the foundations equal, in total, to 1% of the Group's pre-tax profits (after certain adjustments) averaged over three years. The deeds of covenant can be cancelled by the Group at nine years notice.

44 Contingent liabilities and commitments (continued)

c Guaranteed annuity options

After an extensive review of its existing practices carried out in the light of the judgement of the House of Lords in the guaranteed annuities case *Equitable Life vs Hyman*, it was announced that Scottish Widows was revising the way it calculates benefits for guaranteed annuity policies with effect from 1 February 2002. As a result of this change, the terminal bonuses for guaranteed annuity option policies will be increased.

Under the terms of the transfer of the Scottish Widows' business, a separate memorandum account was created within the With Profits Fund called the Additional Account. This Account had a value at 31 December 2001 of approximately £1.7 billion, and is available to meet any additional costs of providing guaranteed benefits on transferred policies, including guaranteed annuity option policies. The assets allocated to the Additional Account include certain hedge assets, to provide protection to the With Profits Fund against the consequences of a future fall in interest rates.

The eventual cost of providing the enhanced benefits is dependent upon a number of factors, including in particular:

- the proportion of policyholders with a guaranteed annuity option policy who choose to exercise their options;
- the effect of future interest rate and mortality trends on the cost of annuities; and
- the future investment performance of the With Profits Fund

Having considered a range of possible outcomes, the Group currently expects that the most likely outcome is that the balance in the Additional Account available for this purpose will be sufficient to meet the cost of the enhanced benefits payable to the guaranteed annuity option policyholders, as well as other contingencies. This cost, currently estimated to be approximately £1.4 billion, will be paid out over many years as policies mature. In the event that the amount in the Additional Account proves, over time, to be insufficient, the shortfall will be met by the Group. At this time, no provision is considered necessary for such risk.

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45 Derivatives and other financial instruments

Information about the Group's use of financial instruments and management of the associated risks is given on pages 58 to 60.

a Derivatives

Derivatives are used to meet the financial needs of customers, as part of the Group's trading activities and to reduce its own exposure to fluctuations in interest and exchange rates. The principal derivatives used by the Group are interest rate and exchange rate contracts; particular attention is paid to the liquidity of the markets and products in which the Group trades to ensure that there are no undue concentrations of activity and risk.

Interest rate related contracts include interest rate swaps, forward rate agreements and options. An interest rate swap is an agreement between two parties to exchange fixed and floating interest payments, based upon interest rates defined in the contract, without the exchange of the underlying principal amounts. Forward rate agreements are contracts for the payment of the difference between a specified rate of interest and a reference rate, applied to a notional principal amount at a specific date in the future. An interest rate option gives the buyer, on payment of a premium, the right, but not the obligation, to fix the rate of interest on a future loan or deposit, for a specified period and commencing on a specified future date.

Exchange rate related contracts include forward foreign exchange contracts, currency swaps and options. A forward foreign exchange contract is an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate. Currency swaps generally involve the exchange of interest payment obligations denominated in different currencies; the exchange of principal can be notional or actual. A currency option gives the buyer, on payment of a premium, the right, but not the obligation, to sell specified amounts of currency at agreed rates of exchange on or before a specified future date.

Equity derivatives are also used by the Group as part of its equity based retail product activity to eliminate the Group's exposure to fluctuations in various international stock exchange indices. Index-linked equity options are purchased which give the Group the right, but not the obligation, to buy or sell a specified amount of equities, or basket of equities in the form of published indices on or before a specified future date.

Derivatives contracts expose the Group to both market risk and credit risk. Only a few highly specialist trading centres within the Group are permitted to enter into derivative contracts and the level of exposure to interest rate and exchange rate movements and other market variables is strictly controlled and monitored within approved limits.

45 Derivatives and other financial instruments (continued)

a Derivatives (continued)

Unlike on-balance sheet instruments the principal amount of the contract does not represent the Group's real exposure to credit risk which is limited to the current cost of replacing contracts with a positive value to the Group, should the counterparty default. To reduce credit risk the Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure.

Trading

The notional principal amounts and fair values (which, after netting, are the carrying values) of trading instruments entered into with third parties were as follows:

31 December 2001	**Notional principal amount**	**Fair values**	
		Assets	**Liabilities**
	£m	**£m**	**£m**
Exchange rate contracts:			
Spot, forwards and futures	**95,895**	**1,035**	**1,038**
Currency swaps	**6,737**	**223**	**152**
Options purchased	**3,825**	**11**	**-**
Options written	**3,492**	**-**	**9**
	109,949	**1,269**	**1,199**
Interest rate contracts:			
Interest rate swaps	**286,617**	**4,085**	**4,535**
Forward rate agreements	**54,171**	**78**	**84**
Options purchased	**8,887**	**73**	**-**
Options written	**3,993**	**-**	**58**
Futures	**35,112**	**-**	**-**
	388,780	**4,236**	**4,677**
Equity contracts	**4,580**	**428**	**255**
Effect of netting		**(3,843)**	**(3,843)**
Balances arising from off-balance sheet financial instruments		**2,090**	**2,288**

31 December 2000	Notional principal amount	Fair values	
		Assets	Liabilities
	£m	£m	£m
Exchange rate contracts:			
Spot, forwards and futures	86,423	1,742	1,940
Currency swaps	6,049	304	206
Options purchased	1,208	23	-
Options written	1,023	-	19
	94,703	2,069	2,165
Interest rate contracts:			
Interest rate swaps	290,129	3,484	3,438
Forward rate agreements	48,002	57	64
Options purchased	3,539	17	-
Options written	2,229	-	8
Futures	34,390	6	-
	378,289	3,564	3,510
Equity contracts	2,768	443	59
Effect of netting		(3,388)	(3,388)
Balances arising from off-balance sheet financial instruments		2,688	2,346

45 Derivatives and other financial instruments (continued)

a Derivatives (continued)

Non-trading

Through intra company and intra group transactions the Group establishes non-trading derivatives positions with the Group's independent trading operations. Similar positions are also established with third parties. The notional principal amounts and fair values of non-trading instruments entered into with third parties were as follows:

31 December 2001	**Notional principal amount £m**	**Fair values Positive £m**	**Fair values Negative £m**
Exchange rate contracts:			
Spot, forwards and futures	**146**	**3**	**1**
Currency swaps	**70**	**9**	**1**
	216	**12**	**2**
Interest rate contracts:			
Interest rate swaps	**2,919**	**164**	**68**
Forward rate agreements	**62**	**-**	**-**
	2,981	**164**	**68**
Effect of netting		**(39)**	**(39)**
		137	**31**

31 December 2000	Notional principal amount £m	Fair values Positive £m	Fair values Negative £m
Exchange rate contracts:			
Spot, forwards and futures	296	4	4
Currency swaps	78	5	7
	374	9	11
Interest rate contracts:			
Interest rate swaps	2,466	96	35
Forward rate agreements	134	-	-
	2,600	96	35
Effect of netting		-	-
		105	46

The aggregate carrying value of non-trading derivatives with a positive fair value was an asset of £18 million (2000: an asset of £23 million) and with a negative fair value was an asset of £1 million (2000: a liability of £1 million).

45 Derivatives and other financial instruments (continued)

a Derivatives (continued)

The maturity of the notional principal amounts and net replacement cost of both trading and non-trading instruments entered into with third parties was:

	Under 1 year £m	1 to 5 years £m	Over 5 years £m	Total £m
31 December 2001				
Exchange rate contracts:				
Notional principal amount	**102,130**	**6,260**	**1,775**	**110,165**
Net replacement cost	**663**	**132**	**42**	**837**
Interest rate contracts:				
Notional principal amount	**187,570**	**155,079**	**49,112**	**391,761**
Net replacement cost	**545**	**229**	**188**	**962**
Equity contracts:				
Notional principal amount	**738**	**3,394**	**448**	**4,580**
Net replacement cost	**75**	**330**	**23**	**428**
Total:				
Notional principal amount	**290,438**	**164,733**	**51,335**	**506,506**
Net replacement cost	**1,283**	**691**	**253**	**2,227**
31 December 2000				
Exchange rate contracts:				
Notional principal amount	88,288	4,973	1,816	95,077
Net replacement cost	1,094	183	39	1,316
Interest rate contracts:				
Notional principal amount	177,684	159,422	43,783	380,889
Net replacement cost	731	146	157	1,034
Equity contracts:				
Notional principal amount	506	2,054	208	2,768
Net replacement cost	68	343	32	443
Total:				
Notional principal amount	266,478	166,449	45,807	478,734
Net replacement cost	1,893	672	228	2,793

The notional principal amount does not represent the Group’s real exposure to credit risk, which is limited to the current cost of replacing contracts at current market rates should the counterparties default.

Net replacement cost represents the total positive fair value of all derivative contracts at the balance sheet date, after allowing for the offset of all negative fair values where the Group has a legal right of set-off with the counterparty concerned.

An analysis of the net replacement cost of both trading and non-trading instruments entered into with third parties by counterparty type is set out below; the Group’s exposure is further reduced by qualifying collateral held.

	2001 £m	2000 £m
OECD banks	**1,425**	2,244
Other	**802**	549
Net replacement cost	**2,227**	2,793
Qualifying collateral held	**(339)**	(643)
Potential credit risk exposure	**1,888**	2,150

45 Derivatives and other financial instruments (continued)

b Interest rate sensitivity gap analysis for the non-trading book

The table below summarises the repricing mismatches of the Group's non-trading assets and liabilities. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date. The table does not take into account the effect of interest rate options used by the Group to hedge its exposure; details of options are given in note 45a.

As at 31 December 2001	**3 months or less £m**	**6 months or less but over 3 months £m**	**1 year or less but over 6 months £m**	**5 years or less but over 1 year £m**	**Over 5 years £m**	**Non-interest bearing £m**	**Trading book £m**	**Total £m**
Assets:								
Treasury bills and other eligible bills	**2,709**	**37**	**26**	**4**	**6**	**-**	**1,630**	**4,412**
Loans and advances to banks	**11,311**	**1,621**	**1,076**	**142**	**289**	**452**	**333**	**15,224**
Loans and advances to customers	**74,361**	**5,252**	**8,798**	**28,497**	**7,108**	**(1,353)**	**272**	**122,935**
Debt securities and equity shares	**2,545**	**1,662**	**718**	**1,940**	**4,168**	**(6)**	**13,423**	**24,450**
Other assets	**154**	**9**	**8**	**4**	**15**	**17,291**	**5,648**	**23,129**
Total assets	**91,080**	**8,581**	**10,626**	**30,587**	**11,586**	**16,384**	**21,306**	**190,150**
Liabilities:								
Deposits by banks	**19,226**	**1,859**	**666**	**512**	**90**	**681**	**1,276**	**24,310**
Customer accounts	**92,834**	**1,644**	**1,172**	**3,228**	**2,299**	**7,633**	**306**	**109,116**
Debt securities in issue	**16,453**	**3,957**	**1,333**	**600**	**890**	**-**	**1,187**	**24,420**
Other liabilities	**350**	**-**	**3**	**-**	**5**	**7,180**	**5,352**	**12,890**
Subordinated liabilities – loan capital	**1,069**	**714**	**-**	**641**	**5,233**	**-**	**-**	**7,657**
Minority interests and shareholders' funds	**-**	**-**	**-**	**-**	**-**	**11,655**	**102**	**11,757**
Internal funding of trading business	**(3,736)**	**(741)**	**(1,171)**	**(6,051)**	**(1,384)**	**-**	**13,083**	**-**
Total liabilities	**126,196**	**7,433**	**2,003**	**(1,070)**	**7,133**	**27,149**	**21,306**	**190,150**
Off-balance sheet items	**21,937**	**(10,861)**	**(7,509)**	**(2,896)**	**(671)**	**-**	**-**	**-**
Interest rate repricing gap	**(13,179)**	**(9,713)**	**1,114**	**28,761**	**3,782**	**(10,765)**	**-**	**-**
Cumulative interest rate repricing gap	**(13,179)**	**(22,892)**	**(21,778)**	**6,983**	**10,765**	**-**	**-**	**-**

As at 31 December 2000*	3 months or less £m	6 months or less but over 3 months £m	1 year or less but over 6 months £m	5 years or less but over 1 year £m	Over 5 years £m	Non-interest bearing £m	Trading book £m	Total £m
Assets:								
Treasury bills and other eligible bills	534	40	46	9	1	-	1,079	1,709
Loans and advances to banks	13,034	1,184	392	112	191	185	192	15,290
Loans and advances to customers	69,150	4,206	6,109	30,673	5,542	(1,378)	130	114,432
Debt securities and equity shares	2,497	475	464	1,202	1,747	51	8,416	14,852
Other assets	251	22	47	5	22	16,603	4,795	21,745
Total assets	85,466	5,927	7,058	32,001	7,503	15,461	14,612	168,028
Liabilities:								
Deposits by banks	12,854	1,090	604	396	92	789	910	16,735
Customer accounts	89,194	1,955	1,508	2,506	394	6,141	291	101,989
Debt securities in issue	8,519	5,950	1,769	623	82	-	956	17,899
Other liabilities	159	-	3	91	2	8,289	4,775	13,319
Subordinated liabilities – loan capital	1,727	509	-	637	4,637	-	-	7,510
Minority interests and shareholders' funds	-	-	-	-	-	10,556	20	10,576
Internal funding of trading business	148	(982)	(264)	(6,188)	(374)	-	7,660	-
Total liabilities	112,601	8,522	3,620	(1,935)	4,833	25,775	14,612	168,028
Off-balance sheet items	12,229	(766)	170	(10,612)	(1,021)	-	-	-
Interest rate repricing gap	(14,906)	(3,361)	3,608	23,324	1,649	(10,314)	-	-
Cumulative interest rate repricing gap	(14,906)	(18,267)	(14,659)	8,665	10,314	-	-	-

* restated (see note 1)

45 Derivatives and other financial instruments (continued)

c Fair value analysis (continued)

Financial instruments include both financial assets and financial liabilities and also derivatives. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Wherever possible, fair values have been estimated using market prices for instruments held by the Group. Where market prices are not available, fair values have been estimated using quoted values for instruments with characteristics either identical or similar to those of the instruments held by the Group. In certain cases, where no ready markets currently exist, various techniques have been developed to estimate what the approximate fair value of such instruments might be. These estimation techniques are necessarily subjective in nature and involve several assumptions.

The fair values presented in the following table are at a specific date and may be significantly different from the amounts which will be actually be paid or received on the maturity or settlement date. In many cases, the estimated fair values could not be realised immediately and accordingly do not represent the value of these financial instruments to the Group as a going concern.

Because a variety of estimation techniques are employed and significant estimates made, comparisons of fair values between financial institutions may not be meaningful. Readers of these accounts are thus advised to use caution when using this data to evaluate the Group's financial position.

Fair value information is not provided for items that do not meet the definitions of a financial instrument. These items include intangible assets, such as the value of the Group's branch network, the long-term relationships with depositors and credit card relationships, premises and equipment and shareholders' equity. These items are material and accordingly the Group believes that the fair value information presented does not represent the underlying value of the Group.

The valuation technique for each major category of financial instrument is discussed below:

Treasury bills and other eligible bills
Fair value is estimated using market prices, where available.

Loans and advances to banks and customers
The Group provides loans and advances to commercial, corporate and personal customers at both fixed and variable rates. The carrying value of the variable rate loans and those relating to lease financing is assumed to be their fair value. For fixed rate lending, several different techniques are used to estimate fair value, as considered appropriate. For commercial and personal customers, fair value is principally estimated by discounting anticipated cash flows (including interest at contractual rates) at market rates for similar loans offered by the Group and other financial institutions. The fair value for corporate loans was estimated by discounting anticipated cash flows at a rate which reflects the effects of interest rate changes, adjusted for changes in credit risk. Certain loans secured on residential properties are made at a fixed rate for a limited period, typically two to five years, after which the loans revert to the relevant variable rate. The fair value of such loans has been estimated by reference to the market rates for similar loans of maturity equal to the remaining fixed interest rate period.

Debt securities and equity shares held for investment purposes
Listed investment securities are valued at quoted mid-market prices. Unlisted securities and equity shares are valued based on discounted cash flows, market prices of similar securities and other appropriate valuation techniques.

Deposits by banks and customer accounts
The fair value of deposits repayable on demand is considered to be equal to their carrying value. The fair value for all other deposits and customer accounts was estimated using discounted cash flows applying either market rates, where applicable, or current rates for deposits of similar remaining maturities.

Debt securities in issue and subordinated liabilities
The fair value of short-term debt securities in issue is approximately equal to their carrying value. Fair value for other debt securities and for subordinated liabilities is estimated using quoted market prices.

Financial commitments and contingent liabilities
The Group considers that, given the lack of an established market, the diversity of fee structures and the difficulty of separating the value of the instruments from the value of the overall transaction, it is not meaningful to provide an estimate of the fair value of financial commitments and contingent liabilities. These are therefore excluded from the following table.

The carrying and fair values of non-trading derivative financial instruments are disclosed in note 45a.

45 Derivatives and other financial instruments (continued)

c Fair value analysis (continued)

The table below shows a comparison by category of book values and fair values of the Group's on-balance sheet financial assets and liabilities.

As at 31 December 2001	**Trading book**		**Non-trading book**	
	Book value £m	**Fair value £m**	**Book value £m**	**Fair value £m**
Assets:				
Treasury bills and other eligible bills	**1,630**	**1,630**	**2,782**	**2,780**
Loans and advances to banks and customers	**605**	**605**	**137,554**	**138,287**
Debt securities and equity shares	**13,423**	**13,423**	**11,027**	**11,269**
Liabilities:				
Deposits by banks and customers	**1,582**	**1,582**	**131,844**	**131,813**
Debt securities in issue	**1,187**	**1,187**	**23,233**	**23,266**
Subordinated liabilities	**-**	**-**	**7,657**	**8,084**

As at 31 December 2000*	Trading book		Non-trading book	
	Book value £m	Fair value £m	Book value £m	Fair value £m
Assets:				
Treasury bills and other eligible bills	1,079	1,079	630	627
Loans and advances to banks and customers	322	322	129,400	130,300
Debt securities and equity shares	8,416	8,416	6,436	6,916
Liabilities:				
Deposits by banks and customers	1,201	1,201	117,523	117,369
Debt securities in issue	956	956	16,943	16,982
Subordinated liabilities	-	-	7,510	7,692

* restated (see note 1)

d Currency exposures

Structural currency exposures

The Group's main overseas operations are in New Zealand, the Americas and Europe. Details of the Group's structural foreign currency exposures are as follows:

Functional currency of Group operation	**2001 £m**	2000 £m
New Zealand dollar	**748**	703
Euro (and component former currencies)	**286**	289
US dollar	**147**	194
Swiss franc	**104**	120
Other non-sterling	**438**	397
Total	**1,723**	1,703

Non-structural currency exposures

All foreign exchange exposures in the non-trading book are transferred to the trading area where they are monitored and controlled.

Information about the management of market risk in the Group's trading activities is given on pages 58 to 60.

45 Derivatives and other financial instruments (continued)

e Unrecognised gains and losses on hedging instruments

The Group uses a variety of financial instruments to hedge exposures in its banking book; these hedges are accounted for on an accruals basis, in line with the underlying instruments being hedged. Any gains or losses that would occur if these instruments were carried at market value are therefore not recognised.

At 31 December 2001, the unrecognised gains on financial instruments used for hedging were £242 million (2000: £200 million) and unrecognised losses were £820 million (2000: £457 million).

The net losses arising in 2000 and earlier years and recognised in 2001 amounted to £88 million. Net losses of £403 million arose in 2001 but were not recognised in the year.

Of the net losses of £578 million at 31 December 2001, £342 million of net losses are expected to be recognised in the year ending 31 December 2002 and £236 million of net losses in later years.

f Value at risk in trading activities

Details of the value at risk in the Group's global trading activities are given on page 58.

46 Acquisitions

On 21 November 2001 the Group's subsidiary, Lloyds TSB Commercial Finance Limited, acquired the issued share capital of CashFriday Limited, a provider of funding and payroll services to the UK temporary recruitment sector. The consideration was approximately £10 million, satisfied by £1 million of cash and the issue of £9 million short-term loan notes. The premium on acquisition of £8 million has been capitalised and will be written off to the profit and loss account over its estimated useful life of 20 years. There were no fair value adjustments made to the assets acquired. The results of this business have been consolidated in full from the date of acquisition, the effect on the results of the Group is not material.

47 Consolidated cash flow statement

The cash flow statement reflects cash flows attributable to the banking, life and general insurance businesses. Cash flows from long-term assurance business attributable to shareholders include the surplus emerging from the life and pension businesses; 'Income from long-term assurance business' reflects the movement in the value of long-term assurance business attributable to shareholders (see Note 29) as adjusted for capital injections and acquisitions, which are reflected within the 'Capital expenditure and financial investment' and 'Acquisitions and disposals' sections of the cash flow statement. Cash flows relating to the long-term assurance business attributable to policyholders are not reflected within this statement.

47 Consolidated cash flow statement (continued)

a Reconciliation of operating profit to net cash inflow from operating activities

	2001 £m	2000* £m	1999* £m
Operating profit	**3,521**	3,857	3,770
Increase in prepayments and accrued income	**(411)**	(121)	(231)
(Decrease) increase in accruals and deferred income	**(439)**	830	183
Provisions for bad and doubtful debts	**747**	541	615
Net advances written off	**(691)**	(580)	(614)
General insurance claims	**174**	142	169
General insurance claims paid	**(178)**	(146)	(145)
Amounts written off fixed asset investments	**60**	32	7
Income from long-term assurance business	**(193)**	(615)	(227)
Transfer from long-term assurance business	**155**	104	162
Interest on subordinated liabilities (loan capital)	**493**	490	362
Interest element of finance lease rental payments	**1**	1	-
Depreciation and amortisation	**550**	386	277
Other non-cash movements	**(395)**	(266)	(300)
Net cash inflow from trading activities	**3,394**	4,655	4,028
Net increase in loans and advances	**(9,340)**	(6,350)	(6,389)
Net (increase) decrease in investments other than investment securities	**(5,664)**	(355)	461
Net (increase) decrease in other assets	**(327)**	(124)	1,565
Net increase (decrease) in deposits by banks	**7,689**	(2,794)	827
Net increase in customer accounts	**7,525**	7,469	3,299
Net increase in debt securities in issue	**6,557**	4,738	551
Net increase (decrease) in other liabilities	**109**	185	(2,961)
Net increase in items in course of collection/transmission	**(17)**	(126)	(60)
Other non-cash movements	**1**	176	(108)
Net cash inflow from operating activities	**9,927**	7,474	1,213

* restated (see note 1)

b Analysis of cash as shown in the balance sheet

	2001 £m	2000 £m	1999 £m
Cash and balances with central banks	**1,240**	1,027	1,276
Loans and advances to banks repayable on demand	**2,443**	2,794	1,132
	3,683	3,821	2,408

The Group is required to maintain balances with the Bank of England which, at 31 December 2001, amounted to £156 million (2000: £142 million; 1999: £128 million).

c Analysis of changes in cash during the year

	2001 £m	2000 £m	1999 £m
At 1 January	**3,821**	2,408	2,856
Net cash (outflow) inflow before adjustments for the effect of foreign exchange movements	**(100)**	1,406	(448)
Effect of foreign exchange movements	**(38)**	7	-
At 31 December	**3,683**	3,821	2,408

d Analysis of changes in financing during the year

	Share capital (including premium and merger reserve)		
	2001 £m	2000 £m	1999 £m
At 1 January	**2,334**	2,136	1,823
Cash inflow from financing	**379**	198	313
At 31 December	**2,713**	2,334	2,136

47 Consolidated cash flow statement (continued)

d Analysis of changes in financing during the year (continued)

	Capital securities issued by subsidiary undertakings		
	2001	2000	1999
	£m	£m	£m
At 1 January	**515**	-	-
Effect of foreign exchange movements	**(11)**	6	-
Cash inflow from financing	**456**	509	-
At 31 December	**960**	515	-

	Subordinated liabilities and finance leases		
	2001	2000	1999
	£m	£m	£m
At 1 January	**7,533**	6,497	4,028
Effect of foreign exchange movements	**(8)**	120	(69)
Cash inflow from financing	**155**	897	2,541
Capital repayments	**(20)**	(4)	(3)
Adjustments on acquisition	**-**	23	-
At 31 December	**7,660**	7,533	6,497

e Analysis of the net cash outflow in respect of the acquisition of group undertakings

	2001	2000	1999
	£m	£m	£m
Cash consideration paid (see f)	**1**	5,110	27
Payments to former members of Scottish Widows Fund and Life Assurance Society acquired during 2000	**179**	-	-
Net cash outflow	**180**	5,110	27

f Acquisition of group undertakings

	2001	2000	1999
	£m	£m	£m
Net assets acquired:			
Loans and advances	**-**	2,827	-
Long-term assurance business	**-**	4,052	-
Other assets	**15**	168	1
Tangible fixed assets	**-**	375	-
Deposits by banks, customer accounts and other liabilities	**(13)**	(3,239)	4
	2	4,183	5
Goodwill arising on consolidation	**8**	2,405	22
	10	6,588	27
Satisfied by:			
Issue of loan notes	**9**	1,077	-
Cash	**1**	5,110	27
Payments pending settlement	**-**	401	-
	10	6,588	27

g Disposal of group undertakings and businesses

	2001	2000	1999
	£m	£m	£m
Net assets disposed of:			
Interests in associated undertakings	**-**	-	2
Other net assets	**1**	2	-
Goodwill written back on disposal	**-**	93	-
	1	95	2
Profit (loss) on sale	**39**	(12)	1
Cash consideration received	**40**	83	3

48 Differences between UK GAAP and US GAAP

The accounts presented in this report have been prepared in accordance with accounting principles generally accepted in the United Kingdom (UK GAAP). These differ in significant respects to the accounting principles generally accepted in the United States (US GAAP). The following is a summary of significant differences applicable to the Group.

UK GAAP	US GAAP
Business combinations	
For accounting periods beginning before 23 December 1994, UK GAAP permitted merger accounting for business combinations wherein the offeror acquired at least 90 per cent of all equity shares in issue and that equity shares comprised not less than 90 per cent of the fair value of the consideration.	Under Accounting Principles Board (APB) Opinion No. 16 'Business Combinations', a business combination should be accounted for as a pooling-of-interests if two previously independent entities combine as a result of one entity issuing common stock in exchange for substantially all the common stock of the second entity. Whilst the offer may include provisions to distribute cash for fractional shares or those held by dissenting shareholders, the offer may not include a pro rata distribution of cash or other consideration. In addition, no changes in the equity interests of the common stock may be made prior to the merger in contemplation of the transaction and neither may the ratio of the interest of the individual common stockholder to those of other common stockholders in a combining company change as a result of the exchange of stock.
Goodwill / core deposit intangibles	
Following the implementation of Financial Reporting Standard (FRS) 10 'Goodwill and intangible assets' in 1998 goodwill arising on acquisitions of or by group and associated undertakings is capitalised and amortised over its estimated life. There is a presumption that the estimated life is limited to 20 years or less, although this may be rebutted and a longer or indefinite useful life considered. Goodwill is written off when judged to be irrecoverable. For acquisitions prior to 1 January 1998 goodwill was charged directly against reserves as permitted by Statement of Standard Accounting Practice 22. This goodwill was not reinstated following the implementation of FRS 10, but in the event of a subsequent disposal it will be written back and included in the calculation of the profit or loss on disposal.	APB No. 17 'Intangible Assets' requires that goodwill arising on acquisitions by group and associated undertakings be capitalised and amortised over its estimated life, which should not exceed 40 years. The Group amortises goodwill over periods of up to 20 years. Under the transition requirements of Statement of Financial Accounting Standards (SFAS) No. 142 'Goodwill and Other Intangible Assets' goodwill acquired after 30 June 2001 is capitalised but not amortised and is subject to review for impairment in accordance with APB 17 or SFAS No. 121 'Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of' as appropriate until SFAS No. 142 is applied in its entirety (from 1 January 2002).
UK GAAP does not require a value to be placed upon the retail depositor relationship in an acquired financial institution.	SFAS No. 72 'Accounting for Certain Transactions of Banking and Thrift Institutions' requires that, when assessing the fair value of the assets of an acquired financial institution, certain identifiable intangible assets must be recognised. These include the asset representing the value of retail depositor relationships, termed the core deposit intangible, which is capitalised separately and amortised through the profit and loss account over the estimated average life of the retail depositor relationships.

48 Differences between UK GAAP and US GAAP (continued)

UK GAAP	US GAAP
Pension costs	
Pension costs relating to defined benefit schemes, calculated using actuarial assumptions and methods, are charged so as to allocate the cost of providing benefits over the average remaining service lives of employees. Variations from regular cost are spread in equal annual amounts over the average remaining service lives of current employees.	SFAS No. 87 'Employers' Accounting for Pensions' prescribes a similar method of actuarial valuation but requires assets to be assessed at fair value and the assessment of liabilities to be based on current settlement rates. Certain variations from regular cost are allocated in equal amounts over the average remaining service lives of current employees.
Leasing	
Finance lease income is recognised in proportion to the funds invested in the lease using a method that results in a constant rate of return on the net cash investment, which takes into account tax payments and receipts.	The application of SFAS No.13 'Accounting for Leases' gives rise to a level rate of return on the investment in the lease, but without taking into account tax payments and receipts. This results in income being recognised in different periods than under UK GAAP.
Operating lease assets are depreciated such that rentals less depreciation are recognised at a constant periodic rate of return on the net cash invested in that asset.	Operating lease assets are depreciated such that the depreciation charge is at least equal to that which would arise on a straight line basis.
Profits or losses arising on sale and leasebacks are taken to profit as they arise.	Under SFAS No. 28 'Accounting for Sales with Leasebacks' profits or losses arising on a sale and leaseback are deferred and amortised. For leasebacks resulting in a finance lease, the amounts are amortised in proportion to the amortisation of the leased asset; for leasebacks resulting in an operating lease, the amounts are amortised in proportion to the gross rental charged to expense over the lease term.
Property	
Depreciation is charged on the cost of freehold and long leasehold properties over their estimated useful economic lives. Following the adoption of FRS 15, the Group reassessed the useful economic lives and residual values of its freehold and long-leasehold premises and, with effect from 1 January 2000, the cost of these properties, after deducting the value of the land, is being depreciated over 50 years. Previously it was considered that the residual values were such that depreciation was not significant.	Freehold and long leasehold properties are included in the balance sheet at historical cost and depreciated over their estimated useful economic lives.
Share compensation schemes	
Where shares are purchased to satisfy an actual, or anticipated, requirement created by the exercise of options under either the Group's Executive or Save-As-You-Earn option schemes, the difference between the purchase price and exercise price is charged to the profit and loss account on a systematic basis over the period that the employees are expected to benefit. Where shares are issued, no charge is made to the profit and loss account.	The Group accounts for share compensation schemes based on their estimated fair values at the date of the grant in accordance with SFAS No. 123 'Accounting for Stock Based Compensation'.

48 Differences between UK GAAP and US GAAP (continued)

UK GAAP	US GAAP
Computer software developed or obtained for internal use	
All computer software costs are expensed as incurred except for operating software and application software relating to separable new systems, which are capitalised and depreciated over their estimated useful lives.	The American Institute of Certified Public Accountants' Statement of Position 98-1 'Accounting for the costs of computer software developed or obtained for internal use' requires certain costs incurred from 1 January 1999 in respect of software developed for internal use to be capitalised and subsequently amortised.
Derivative instruments held for risk management purposes	
Derivatives used in the Group's trading activities are carried at fair value and all changes in fair value are reported within dealing profits in the profit and loss account. Derivatives used in the group's non-trading activities are accounted for on an accruals basis, in line with the treatment of the underlying items which they are hedging. A derivative will only be classified as a hedge in circumstances where there was adequate evidence of the intention to hedge at the outset of the transaction and the derivative substantially matches or eliminates the exposure being hedged.	SFAS No. 133 'Accounting for Derivative Instruments and for Hedging Activities' requires that all derivatives be recognised on-balance sheet at fair value. Changes in the fair value of derivatives that are not hedges are reported in the income statement. For derivatives which are hedges, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognised in other comprehensive income until the hedged item is recognised in earnings. The ineffectiveness portion of a hedge's change in fair value is immediately recognised in earnings.
Foreign currency translation	
The assets, liabilities and results of the Group's overseas operations are translated into sterling at the rate of exchange prevailing at the balance sheet date, as permitted under UK GAAP.	Under SFAS No. 52 'Foreign Currency Translation', foreign currency assets and liabilities are translated at the year-end rate; however, results are translated at the average rate for the year.
Investment securities	
Debt securities and equity shares intended for use on a continuing basis by the Group are treated as investment securities and included in the balance sheet at cost as adjusted for the amortisation of any premiums and discounts arising upon acquisition, less provision for any permanent diminution in value.	SFAS No. 115 'Accounting for Certain Investments in Debt and Equity Securities' requires that debt securities which are "available-for-sale" (where there is the absence of either the intent or the ability to hold them to maturity) and equity shares with a readily determinable market value should be recorded at fair value with unrealised gains and losses reflected in shareholders' equity. All debt securities held as available-for-sale are subject to assessment for other than temporary impairment in accordance with SFAS No. 115 and, for asset backed securities, in accordance with the Emerging Issues Task Force (EITF) Abstract No. 99-20 'Recognition of Interest Income and Impairment on Purchased and Retained Beneficial Interests in Securitized Financial Assets'.
Dividend payable	
Dividends declared after the period end are recorded in the period to which they relate.	Dividends are recorded in the period in which they are declared.

48 Differences between UK GAAP and US GAAP (continued)

UK GAAP	US GAAP
Own shares	
Own shares held are included within equity and are reported as an asset on the balance sheet.	Own shares held are reclassified as Treasury stock and deducted from shareholders' equity in accordance with Accounting Research Bulletin (ARB) No. 51 'Consolidated Financial Statements'.
Deferred tax	
Deferred tax is provided using the liability method on timing differences where there is a reasonable probability that a liability or asset will crystallise in the foreseeable future. No deferred asset is created in respect of the general provision for bad and doubtful debts which is not deductible in arriving at UK taxable profits.	Under SFAS No. 109 'Accounting for Income Taxes', the liability method is also used, but deferred tax assets and liabilities are recorded for all temporary differences, including the general provision for bad and doubtful debts. A valuation allowance is recorded against a deferred tax asset where it is more likely than not that some portion of the deferred tax asset will not be realised.
Provision for credit losses	
A specific provision is made to cover the estimated loss as soon as the recovery of an outstanding loan is considered doubtful. General provisions are raised to cover losses incurred but not yet identified as of the balance sheet date.	SFAS No. 114 'Accounting by Creditors for Impairment of a Loan' requires the overall credit risk provision to be determined based upon the present value of expected future cash flows, discounted at the loan's effective interest rate or, as a practical expedient, on the loan's observable market value, or the fair value of the collateral if the loan is collateral dependent. Smaller balance homogeneous consumer loans that are collectively valued for impairment are outside the scope of SFAS No. 114, as are debt securities and leases. General provisions are made against such loans when losses have been incurred but not yet identified as of the balance sheet date.
Acceptances	
Acceptances are not recorded on the balance sheet.	Acceptances and the related customer liabilities are recorded on the balance sheet.
Insurance activities	
The shareholder's interest in the long-term assurance fund is valued at the net present value of the profits inherent in such policies.	The net present value of the profits inherent in the policies of the long-term assurance fund is not recognised. An adjustment is made for the amortisation of acquisition costs and fees.
	Additional information on the differences between the UK and US accounting for insurance activities is provided within the Insurance section of this note on pages F-80 to F-83.

48 Differences between UK GAAP and US GAAP (continued)

<u>Recent developments</u>

United Kingdom

FRS 17 'Retirement Benefits'

FRS 17 was issued in December 2000 and becomes fully effective no later than for Lloyds TSB Group's 2003 financial statements. The main requirement of FRS 17 is that it will be necessary to recognise on the balance sheet an asset or liability with respect to the surplus or deficit on the Group's defined benefit schemes and to recognise immediately actuarial gains and losses in the statement of total recognised gains and losses. The FRS requires transitional disclosures in the Group's 2001 and 2002 financial statements, before becoming fully effective in 2003.

FRS 19 'Deferred Tax'

FRS 19 was issued in December 2000 and will be effective for the Group's 2002 financial statements. The FRS requires deferred tax to be provided on most types of timing differences. Currently, the Group recognises deferred tax assets and liabilities only to the extent that it is considered probable that an asset or liability will crystallise. It is not expected that adoption will have a material effect on Lloyds TSB Group's financial statements.

UITF Abstract 33 'Obligations in capital instruments'

Urgent Issues Task Force (UITF) Abstract 33 was issued in February 2002 and deals with the classification of various types of capital instruments in the balance sheet, whether as liabilities, shareholders' funds or, in consolidated financial statements, minority interests. The Abstract is effective for periods ending on or after 23 March 2002 and, upon adoption, Lloyds TSB Group will reclassify those instruments affected from minority interests to subordinated debt. At 31 December 2001, the balance sheet amount was £451 million and the related expense, which will be reclassified from minority interests to interest payable, was £22 million.

United States

SFAS No. 141 'Business Combinations'

SFAS No. 141 was issued in July 2001 and requires that the purchase method be used for all business combinations initiated after 30 June 2001. Use of the pooling-of-interests method is no longer permitted. Adoption has not had a material impact on the Lloyds TSB Group's US GAAP financial statements.

SFAS No. 142 'Goodwill and Other Intangible Assets'

SFAS No. 142 was issued in July 2001 and became effective for the Lloyds TSB Group on 1 January 2002. Certain provisions are applicable to transactions completed after 30 June 2001. The Statement requires that goodwill should no longer be amortised to earnings, but instead reviewed for impairment and that any losses arising from such a review be charged to income as they arise. Retrospective application is not permitted and certain disclosures will be provided until all reported periods reflect the change in accounting treatment. The impact on the Lloyds TSB Group will be to increase US GAAP net income in the periods from 1 January 2002 by the amount of amortisation previously charged to net income on goodwill capitalised under US GAAP. For the year ended 31 December 2001, this amounted to £248 million. No impairment of goodwill is anticipated

SFAS No. 143 'Accounting for Asset Retirement Obligations'

SFAS No. 143 was issued in June 2001 and requires the fair value of a liability for an asset retirement obligation to be recorded in the period in which it is incurred. When the liability is initially recorded, the cost is capitalised by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalised cost is depreciated over the useful life of the related asset. Upon settlement of the liability, the obligation is either settled for its recorded amount or a gain or loss is incurred upon settlement. SFAS No. 143 is effective for fiscal years beginning after 15 June 2002, with earlier application encouraged. Adoption is not expected to have a material impact on the Lloyds TSB Group's US GAAP financial statements.

SFAS No. 144 'Accounting for the Impairment or Disposal of Long-Lived Assets'

SFAS No. 144 was issued in August 2001 and became effective for the Lloyds TSB Group on 1 January 2002. The Statement supersedes SFAS No. 121 'Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of' although it maintains many of its requirements. For long-lived assets to be held and used, an impairment is recognised only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows. For a long-lived asset to be disposed of by sale, the asset is measured at the lower of its carrying value or fair value (less costs to sell) and depreciation ceases. This Statement does not apply to goodwill, core deposit intangibles, deferred acquisition costs or deferred tax assets. Adoption is not expected to have a material impact on the Lloyds TSB Group's US GAAP financial statements.

48 Differences between UK GAAP and US GAAP (continued)

The following tables summarise the adjustments to net income and shareholders' equity which would arise from the application of US GAAP:

Reconciliation of net income	Note	**2001 £m**	2000 £m	1999 £m
Profit for the year attributable to shareholders under UK GAAP		**2,500**	2,706	2,539
Insurance activities, before tax (see page F-80)		**(550)**	(528)	119
Banking and Group activities:				
Goodwill amortisation	(a)	**(209)**	(188)	(118)
Profit/loss on sale and closure of businesses	(b)	**-**	12	21
Amortisation of core deposit intangibles	(a)	**(219)**	(219)	(219)
Pension costs	(c)	**(16)**	(36)	(39)
Leasing		**(131)**	(47)	(20)
Property depreciation		**3**	3	(7)
Share compensation schemes	(d)	**(46)**	(31)	(37)
Internal software costs		**16**	10	37
Derivative instruments held for risk management purposes	(f)	**(315)**	(168)	178
Foreign currency translation differences		**(4)**	2	3
Total Banking and Group activities, before tax		**(921)**	(662)	(201)
Taxation				
- deferred taxation	(i)	**38**	(75)	(107)
- deferred taxation on GAAP differences	(i)	**457**	488	(202)
Total Taxation		**495**	413	(309)
Total adjustments, after tax		**(976)**	(777)	(391)
Net income under US GAAP		**1,524**	1,929	2,148

Reconciliation of shareholders' equity	Note	**2001 £m**	2000 £m
Shareholders' funds under UK GAAP		**10,760**	10,024
Insurance activities, before tax (see page F-80)		**(274)**	399
Banking and Group activities:			
Goodwill	(a)	**1,312**	1,533
Core deposit intangibles	(a)	**772**	991
Pension Costs	(c)	**1,687**	1,703
Leasing		**(274)**	(143)
Property depreciation		**(53)**	(56)
Internal software		**63**	47
Derivative instruments held for risk management purposes	(f)	**(578)**	(257)
Net unrealised gain on available-for-sale investment securities	(g)	**242**	480
Dividend payable		**1,306**	1,172
Own shares	(h)	**(251)**	(247)
Total Banking and Group activities, before tax		**4,226**	5,223
Taxation			
- deferred taxation	(i)	**(45)**	(83)
- deferred taxation on GAAP differences	(i)	**(1,246)**	(1,855)
Total Taxation		**(1,291)**	(1,938)
Total adjustments, after tax		**2,661**	3,684
Shareholders' equity under US GAAP		**13,421**	13,708

48 Differences between UK GAAP and US GAAP (continued)

Reconciliation of movements in shareholders' equity under US GAAP	**2001 £m**	2000 £m	1999 £m
Net income in period	**1,524**	1,929	2,148
Dividends	**(1,738)**	(1,522)	(1,285)
	(214)	407	863
New share capital subscribed	**194**	74	108
Movement in own shares	**(4)**	(41)	(14)
Share compensation schemes	**46**	31	37
Change in the fair value of available-for-sale securities – Insurance activities	**(46)**	21	(50)
Change in the fair value of available-for-sale securities – Banking activities	**(165)**	67	4
Exchange differences	**(98)**	(13)	(58)
	(287)	546	890
Shareholders' equity at beginning of period	**13,708**	13,162	12,272
Shareholders' equity at end of period	**13,421**	13,708	13,162

Accumulated other comprehensive income	**2001 £m**	2000 £m	1999 £m
Exchange translation differences	**(321)**	(223)	(210)
Available-for-sale securities:			
Net unrealised gains – Insurance activities	**49**	98	68
Related amortisation of deferred acquisition costs	**(23)**	(7)	(9)
Net unrealised gains – Banking activities	**242**	480	386
Taxation	**(81)**	(173)	(135)
	187	398	310
Accumulated other comprehensive income under US GAAP	**(134)**	175	100

48 Differences between UK GAAP and US GAAP (continued)

Condensed US GAAP Profit and loss account

The following table provides a condensed profit and loss account for the Group, incorporating the US GAAP adjustments arising.

	2001 £m	2000 £m	1999 £m
Loan interest, including fees	**10,317**	10,218	9,778
Other interest and dividends	**2,077**	2,539	1,541
Insurance premiums	**1,671**	1,604	1,230
Commissions and fees	**2,248**	2,118	1,982
Realised gains from sales of investments	**183**	139	102
Foreign exchange trading income	**158**	141	133
Securities and other trading (losses)gains	**(2,307)**	(253)	328
Other income	**1,260**	838	880
Total revenues	**15,607**	17,344	15,974
Interest expense	**6,427**	7,046	6,259
Total revenues, net of interest expense	**9,180**	10,298	9,715
Policyholder benefits and claims expense	**2,228**	1,735	936
Movement in undistributed earnings to policyholders	**(2,427)**	(317)	3
Provisions for bad and doubtful debts	**747**	541	615
Amounts written off fixed asset investments	**60**	32	7
Total benefits, claims and provisions	**608**	1,991	1,561
Non-insurance compensation and benefits	**2,014**	1,870	1,715
Insurance underwriting, operating and acquisition expenses	**511**	552	345
Other operating expenses	**2,418**	1,899	1,781
Exceptional restructuring costs	**217**	188	-
Depreciation	**622**	414	284
Amortisation of intangible fixed assets			
Goodwill	**248**	210	130
Core deposit intangibles	**219**	219	219
Value of long-term assurance business acquired	**305**	285	1
	772	714	350
	6,554	5,637	4,475
Profit (loss) on sale and closure of businesses	**39**	-	(105)
Income before tax	**2,057**	2,670	3,574
Provision for income taxes*	**476**	692	1,420
Minority interests, net of income taxes	**57**	49	6
Net income under US GAAP	**1,524**	1,929	2,148
Exchange translation differences	**(98)**	(13)	(58)
Available-for-sale securities:			
Net unrealised (losses) gains – Insurance activities	**(49)**	30	(144)
Related amortisation of deferred acquisition costs	**(16)**	2	72
Net unrealised (losses) gains – Banking activities	**(238)**	94	5
Taxation	**92**	(38)	21
	(211)	88	(46)
Comprehensive income under US GAAP	**1,215**	2,004	2,044
Earnings per share (pence)	**27.5p**	35.2p	39.4p
Diluted earnings per share (pence)	**27.2p**	34.8p	38.7p

* Significant items affecting the Group's effective tax rate under US GAAP include the fact that tax is levied on UK life assurance and pension businesses under specialised rules not based on the profit and loss account. In addition, under US GAAP a tax provision is required for unrealised gains that are attributable to the policyholders. The amount provided will vary depending upon the fluctuations of the stock market and this movement can result in significant changes in the effective rate of tax.

48 Differences between UK GAAP and US GAAP (continued)

Condensed US GAAP Balance sheet

The following table provides a condensed balance sheet for the Group, incorporating the US GAAP adjustments arising.

	2001	2000
	£m	£m
Assets		
Cash and due from banks	**7,388**	6,478
Deposits at interest with banks	**11,709**	10,799
Securities purchased under resale agreements	**1,383**	4,937
Treasury bills and other eligible bills	**2,782**	630
Trading account assets	**38,714**	36,872
Investments	**15,126**	10,626
Loans, net of provisions	**122,485**	110,788
Tangible fixed assets	**3,429**	3,146
Intangible fixed assets – goodwill	**3,878**	4,132
– core deposit intangibles	**772**	991
– value of long-term assurance business acquired	**3,007**	3,312
Deferred acquisition costs	**795**	698
Separate account assets	**22,068**	25,559
Other assets	**9,810**	6,904
Total assets	**243,346**	225,872
Liabilities		
Deposits	**133,419**	117,473
Trading account liabilities	**3,476**	3,302
Debt securities in issue	**23,233**	16,943
Policyholder liabilities	**23,465**	22,182
Undistributed policyholder allocations	**3,478**	5,905
Commitments and contingencies	**251**	291
Deferred tax	**3,105**	3,719
Long-term debt	**8,108**	7,510
Separate account liabilities	**22,068**	25,559
Other liabilities	**8,776**	8,728
Minority interests	**546**	552
Total liabilities	**229,925**	212,164
Shareholders' equity:		
Common stock	**1,411**	1,396
Additional paid-in capital	**4,670**	4,260
Retained earnings	**7,725**	8,124
Treasury stock	**(251)**	(247)
Accumulated other comprehensive income	**(134)**	175
Total shareholders' equity	**13,421**	13,708
Total liabilities and shareholders' equity	**243,346**	225,872

48 Differences between UK GAAP and US GAAP (continued)

Condensed Consolidated Statement of Cash flows in accordance with SFAS No. 95

	2001 £m	2000 £m	1999 £m
Cash flows from operating activities			
Net income before minority interests	**1,581**	1,978	2,154
Adjustments required to reconcile net income to net cash provided by operating activities:			
Amortisation of intangible fixed assets	**772**	714	350
Depreciation of tangible fixed assets	**622**	414	284
Provision for bad and doubtful debts	**56**	(39)	1
Change in trading account assets	**(2,004)**	861	2,176
Change in trading account liabilities	**174**	38	(2,242)
Change in deferred acquisition costs	**(97)**	(60)	(74)
Change in other assets	**(2,910)**	658	1,179
Change in policyholder liabilities	**583**	310	488
Change in undistributed policyholder allocations	**(2,427)**	(164)	24
Change in other liabilities	**279**	(367)	(1,336)
Net gain on sale of investment securities	**(183)**	(139)	(102)
(Profit) loss on disposal of tangible fixed assets	**(67)**	(6)	2
Other, net	**(725)**	(50)	515
Total adjustments	**(5,927)**	2,170	1,265
Net cash (used in) provided by operating activities	**(4,346)**	4,148	3,419
Cash flows from investing activities			
Change in deposits at interest with banks	**(986)**	474	3,448
Change in securities purchased under resale agreements	**3,554**	2,912	(4,816)
Change in loans and advances to customers	**(12,211)**	(9,510)	(5,146)
Purchases of investment securities	**(48,842)**	(24,659)	(25,871)
Proceeds from sale and maturity of investment securities	**42,282**	25,731	22,800
Purchases of tangible fixed assets	**(1,140)**	(1,031)	(639)
Proceeds from sale of tangible fixed assets	**293**	87	83
Additions to interests in joint ventures	**(44)**	-	-
Acquisition of subsidiary undertakings	**(180)**	(5,110)	(27)
Disposal of subsidiary undertakings	**40**	83	3
Net cash used in investing activities	**(17,234)**	(11,023)	(10,165)
Cash flows from financing activities			
Dividends paid - equity	**(1,738)**	(1,522)	(1,285)
Dividends paid to minorities - equity	**(17)**	(12)	(11)
Dividends paid to minorities - non-equity	**(40)**	(36)	-
Issue of ordinary shares	**194**	74	108
Purchase of treasury stock	**(4)**	(41)	(14)
Issue of preferred securities	**-**	509	-
Issue of long-term debt	**742**	952	2,769
Redemption of long-term debt	**(131)**	(55)	(228)
Change in deposits	**16,458**	4,287	3,975
Change in short-term borrowings	**6,326**	5,065	851
Policyholders’ deposits	**1,987**	1,978	314
Policyholders’ withdrawals	**(1,287)**	(1,499)	(752)
Net cash provided by financing activities	**22,490**	9,700	5,727
Change in cash and cash equivalents	**910**	2,825	(1,019)
Cash and cash equivalents at beginning of period	**6,478**	3,653	4,672
Cash and cash equivalents at end of period	**7,388**	6,478	3,653
Cash paid during the year for income taxes	**829**	864	807
Cash paid during the year for interest	**6,755**	6,102	5,935
Non-cash investing and financing activities:			
Loan notes issued in respect of acquisitions	**9**	1,077	-

48 Differences between UK GAAP and US GAAP (continued)

Balance sheet presentation

Certain classification differences exist in financial reporting under UK GAAP and US GAAP. For the Group, such differences primarily arise in the balance sheet and the following comparison lists the line items in which such differences occur.

UK GAAP	US GAAP
Cash and balances at central banks	Cash and due from banks
Items in course of collection from banks	Cash and due from banks
Treasury bills and other eligible bills	Classified as “Trading account assets” where appropriate
Loans and advances to banks	Loans to banks due on demand classified as “Cash and due from banks”; Reverse repos classified as “Securities purchased under resale agreements”
Loans and advances to customers	Reverse repos classified as “Securities purchased under resale agreements”
Debt securities	Classified as “Trading account assets” and “Investments” where appropriate
Equity shares	Classified as “Trading account assets” and “Investments” where appropriate
Other assets	Classified as “Trading account assets” where appropriate
Prepayments and accrued income	Other assets
Items in course of transmission to banks	Cash and due from banks
Debt securities in issue	Classified as “Trading account liabilities” where appropriate
Other liabilities	Classified as “Trading account liabilities” where appropriate
Accruals and deferred income	Other liabilities
Other provisions for liabilities and charges	Commitments and contingencies
Subordinated liabilities	Long-term debt
Minority interests	Classified as “Long-term debt” where appropriate
Merger reserve	Classified as “Additional paid-in capital”
Long-term assurance business	Classifications are discussed on pages F-81 to F-83

Consolidated Statement of Cash flows

The Group’s UK GAAP cash flow statement on page F- 7 is prepared under the provisions of FRS 1(Revised). This is similar in many respects to SFAS No. 95 ‘Statement of Cash Flows’, as amended by SFAS No. 104 ‘Statement of Cash Flows - Net Reporting of Certain Cash Receipts and Cash Payments and Classification of Cash Flows from Hedging Transactions’. Two principal differences arise between the standards with regard to the definition of cash and the classification of items within the cash flow statement.

48 Differences between UK GAAP and US GAAP (continued)

FRS 1 (Revised) defines cash as cash in hand and repayable on demand. Under SFAS No. 95, cash and cash equivalents are defined as short term, highly liquid investments that are both readily convertible to known amounts of cash; and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates.

For the purposes of SFAS No. 95, the Group's cash and cash equivalents of £7,388 million (2000: £6,478 million; 1999: £3,653 million) comprise items reported under the following UK balance sheet categories: cash and balances at central banks; items in the course of collection from banks; loans and advances to banks repayable on demand and items in the course of transmission to banks. Under UK GAAP the results, assets and liabilities of the long-term assurance business are presented on a one-line basis and accordingly movements in cash flows are aggregated into one line within the reconciliation of operating profit. Under US GAAP, the insurance activities have been disaggregated and accordingly the cash flows have been allocated to the appropriate line items within the cash flow statement. Cash attributable to the long-term assurance business is included within cash and cash equivalents above.

Differences between UK and US GAAP with regard to classification of items within the cash flow statement are summarised below:

Cash flow	Classification under FRS 1 (Revised)	Classification under SFAS No. 95
Net change in loans and advances, including lease financing	Operating activities	Investing activities
Net change in deposits and debt securities in issue	Operating activities	Financing activities
Dividends paid to equity and non-equity minority interests	Returns on investments and servicing of finance	Financing activities
Tax paid	Taxation	Operating activities
Capital expenditure and financial investment	Capital expenditure and financial investment	Investing activities
Purchases/proceeds from disposal of subsidiary and associated undertakings	Acquisitions and disposals	Investing activities
Dividends paid – equity	Equity dividends paid	Financing activities

Under FRS 1 (Revised), transactions designated as hedges are reported under the same heading as the related assets or liabilities. Details of withdrawal and usage restrictions in respect of cash and balances at central banks are discussed on pages 84 and F-52.

Notes to the UK/US GAAP reconciliation

a Goodwill and core deposit intangible assets

Under UK GAAP, on 1 January 1998, the Group adopted FRS 10, 'Goodwill and Intangible Assets'. In respect of acquisitions since 1 January 1998, goodwill is included in the consolidated balance sheet under intangible fixed assets and amortised over its estimated useful economic life on a straight-line basis. Prior to 1 January 1998, the Group charged goodwill directly against reserves. In the case of the acquisition of Scottish Widows in 2000, in view of the strength of the Scottish Widows brand and the position of the business as one of the leading providers of life, pensions, unit trust and fund management products, the directors consider that it is appropriate to assign an indefinite life to the goodwill. This goodwill is not being amortised through the profit and loss account; however it is subjected to annual impairment reviews in accordance with FRS 11 'Impairment of Fixed Assets and Goodwill'. Should any impairment be identified, it would be charged to the profit and loss account immediately.

Under US GAAP, all goodwill arising in respect of acquisitions before 30 June 2001 is capitalised and amortised over periods of up to 40 years; goodwill arising after 30 June 2001 is capitalised but not amortised in accordance with the transition provisions of SFAS No. 142. The Group amortises all goodwill arising before 30 June 2001, including that for Scottish Widows, over periods of up to 20 years.

48 Differences between UK GAAP and US GAAP (continued)

a Goodwill and core deposit intangible assets (continued)

The treatment of the Group's major acquisitions is detailed below:

Abbey Life
In 1988, Lloyds Bank Plc transferred a minority interest in five businesses to Abbey Life Group plc, a life insurance company, in return for a majority interest in the enlarged Abbey Life Group. Under UK GAAP, this transaction was accounted for as a merger. Under US GAAP, the same transaction would be accounted for as an acquisition. Accordingly the net assets of Abbey Life Group plc (later renamed Lloyds Abbey Life plc) have been fair valued in accordance with US GAAP and a purchase price determined based on the fair value of the minority interest transferred.

In 1996, Lloyds TSB Group plc acquired the remaining minority interest in Lloyds Abbey Life plc. Under UK and US GAAP the transaction is treated as an acquisition. However, certain differences arise under US GAAP regarding the determination of fair value of life insurance companies and accordingly an adjustment has been made for the items affected. The goodwill arising is being amortised over 20 years.

Cheltenham & Gloucester
Under UK and US GAAP, the purchase of the business of Cheltenham & Gloucester Building Society by Lloyds Bank Plc in August 1995 is treated as an acquisition. Certain differences arise under US GAAP regarding the fair value of the net assets. In addition, the net assets acquired include £521 million relating to core deposit intangibles, which is being amortised over 7 years. The goodwill arising is being amortised over 20 years.

TSB Group plc
The business combination of Lloyds Bank Plc and TSB Group plc in December 1995 was accounted for as a merger as permitted under UK GAAP at that time, although legally TSB Group plc was deemed to have acquired Lloyds Bank Plc. Under US GAAP, the same transaction would have been accounted for as an acquisition of TSB Group plc by Lloyds Bank Plc. Accordingly, for US GAAP, the net assets of TSB Group plc have been fair valued as at the date of the business combination and a purchase price determined based on the value of TSB Group plc shares at that time. The net assets include £1,596 million relating to core deposit intangibles, which is being amortised over 11 years. The resulting goodwill of £601 million is being amortised over 20 years.

Scottish Widows
In March 2000, the Group acquired the business of Scottish Widows' Fund and Life Assurance Society, a life insurance and pensions provider. Under UK and US GAAP, the purchase is treated as an acquisition. However certain differences arise under US GAAP regarding the determination of fair value of the life insurance business. Accordingly adjustments have been made for these items. Under US GAAP, the resulting goodwill is being amortised over 20 years.

The movement in US GAAP goodwill is summarised as follows:

		2001			2000	
	UK GAAP £m	**US GAAP adjustment £m**	**US GAAP £m**	UK GAAP £m	US GAAP adjustment £m	US GAAP £m
Cost						
Balance at 1 January	**2,635**	**2,363**	**4,998**	247	2,486	2,733
Exchange and other adjustments	**(3)**	**(15)**	**(18)**	(17)	(1)	(18)
Acquisitions	**8**	**-**	**8**	2,405	67	2,472
Disposals	**-**	**-**	**-**	-	(189)	(189)
Balance at 31 December	**2,640**	**2,348**	**4,988**	2,635	2,363	4,998
Amortisation						
Balance at 1 January	**(36)**	**(830)**	**(866)**	(16)	(734)	(750)
Exchange and other adjustments	**1**	**3**	**4**	2	-	2
Charge for the year	**(39)**	**(209)**	**(248)**	(22)	(188)	(210)
Disposals	**-**	**-**	**-**	-	92	92
Balance at 31 December	**(74)**	**(1,036)**	**(1,110)**	(36)	(830)	(866)
Net book value	**2,566**	**1,312**	**3,878**	2,599	1,533	4,132

48 Differences between UK GAAP and US GAAP (continued)

a Goodwill and core deposit intangible assets (continued)

Under US GAAP, the asset representing the value of retail depositor relationships associated with an acquisition of a savings entity, termed the core deposit intangible, is capitalised separately and amortised in the consolidated statement of income over the estimated average life of the retail depositor relationships. The average life of the retail depositor relationships is estimated at between 7 and 11 years.

	2001	2000
	£m	£m
Core deposit intangibles		
Balance at 1 January	**991**	1,210
Amortisation	**(219)**	(219)
Balance at 31 December	**772**	991

b Profit/loss on sale and closure of businesses

Under UK GAAP, upon disposal of a business or undertaking, goodwill written-off directly against reserves prior to the implementation FRS 10 “Goodwill and Intangible Assets”, is included in the Group’s share of the net assets of the business or undertaking in the calculation of the profit or loss on disposal.

Under US GAAP, all goodwill is capitalised and amortised over its estimated useful life. Upon disposal of a business or undertaking, the unamortised goodwill is included in the calculation of the profit or loss on disposal. Compared to the treatment under UK GAAP, the effect of this is to increase the profits, and reduce the losses, arising on the sale and closure of those businesses acquired before the implementation of FRS 10.

On 1 February 2000 the Group announced the sale of Abbey Life’s new business capability. In the Group’s 1999 results calculated under UK GAAP a provision of £98 million was made for asset impairment, of which £80 million related to the impairment of goodwill previously written-off against reserves and £18 million to other asset write-offs. Under US GAAP this provision would have been £21 million lower reflecting the cumulative effect of goodwill amortisation.

c Pension costs

The measurement of the US GAAP pension cost is undertaken in accordance with the requirements of SFAS No. 87 and SFAS No. 109. The disclosures reflect the amendments arising from SFAS No. 132 ‘Employers’ Disclosures about Pensions and Other Postretirement Benefits’.

For the reconciliations below, the Group has applied SFAS No. 87 to the Lloyds TSB Group Pension Schemes No’s 1 and 2 with effect from 31 December 1997 as it was not feasible to apply it as of January 1989, the date specified in the standard. The Scottish Widows pension scheme has been included from 3 March 2000, the date of acquisition.

The components of the pension expense which arise under US GAAP are estimated as:

	2001	2000	1999
	£m	£m	£m
Service cost	**212**	211	226
Interest cost	**545**	516	472
Expected return on plan assets	**(778)**	(720)	(688)
Net amortisation and deferral	**(89)**	(92)	(92)
Net pension credit	**(110)**	(85)	(82)

48 Differences between UK GAAP and US GAAP (continued)

c Pension costs (continued)

Change in projected benefit obligation

	2001 £m	2000 £m	1999 £m
Projected benefit obligation as at 1 January	**9,222**	8,527	7,861
Acquisition of Scottish Widows	**-**	278	-
Service cost	**212**	211	226
Interest cost	**545**	516	472
Employee contributions	**-**	-	1
Amendments	**67**	-	120
Net actuarial loss (gain)	**1,014**	(7)	84
Benefits paid	**(121)**	(303)	(237)
Projected benefit obligation as at 31 December	**10,939**	9,222	8,527

Change in plan assets

	2001 £m	2000 £m
Plan assets at fair value as at 1 January	**13,047**	11,601
Acquisition of Scottish Widows	**-**	499
Actual return on plan assets	**(1,597)**	1,250
Benefits paid	**(121)**	(303)
Plan assets at fair value at 31 December	**11,329**	13,047

	2001 £m	2000 £m
Funded status	**390**	3,825
Unrecognised net actuarial loss (gain)	**2,248**	(1,141)
Unrecognised prior service cost	**182**	132
Unrecognised transition asset	**(213)**	(319)
Prepaid benefit cost	**2,607**	2,497
Recognised under UK GAAP	**(920)**	(768)
Recognised on acquisition of Scottish Widows under UK GAAP	**-**	(26)
US GAAP adjustment recognised	**1,687**	1,703

The assets of the pension schemes are invested primarily in equities and fixed interest securities.

In accordance with SFAS No. 87, the excess of the plan assets over the projected benefit obligation at the transition date (1 January 1998) is recognised as a reduction to pension expense on a prospective basis over approximately 15 years, which was the average remaining services period of employees expected to receive benefits under the plans.

The financial assumptions used to calculate the projected benefit obligation at 31 December 2000 and 2001 are as follows:

	2001	2000
Discount rate	**6.0%**	6.0%
Return on assets	**6.6%**	6.6%
Rate of pay increase	**4.0%**	3.5%

48 Differences between UK GAAP and US GAAP (continued)

d Share compensation schemes

In accordance with SFAS No. 123 the Group accounts for share compensation schemes based on their estimated fair value at the date of grant. The following disclosures only reflect options granted from 1 January 1995 onwards. In the initial phase-in period, the amounts will not be representative of the effect on reported net income for future years. The SFAS No. 123 charge for the fair value of share options issued since 1 January 1996 is:

	2001 £m	2000 £m	1999 £m
Balance at 1 January	**(118)**	(87)	(50)
Charge for options granted in year	**(9)**	(13)	(4)
Charge for options granted in prior years	**(37)**	(18)	(33)
Total charge for the year	**(46)**	(31)	(37)
Balance at 31 December	**(164)**	(118)	(87)

During the period from 1 January 1995 to 31 December 2001 the Group operated the following stock compensation plans:

Executive scheme

The Executive share option schemes are long-term incentive schemes and are available to certain senior executives of the Group, with grants usually made annually. Options are granted within limits set by the rules of the schemes. These limits relate to the number of shares under option and the price payable on the exercise of options. From 18 April 2001, the aggregate value of the award based upon the market price at the date of grant must not exceed four times the executive's annual remuneration and, normally, the limit for the grant of options to an executive in any one year would be equal to one and a half year's remuneration with a maximum performance multiplier of three and a half. Prior to 18 April 2001, the normal limit was equal to one year's remuneration and no performance multiplier was applied.

Options are normally exercisable between three and ten years from the date of grant. However, the exercise of the options is subject to the satisfaction of the following performance conditions:

For options granted after March 2001

The performance condition is linked to the performance of Lloyds TSB Group plc's total shareholder return (calculated by reference to both dividends and growth in share price) against a comparator group of sixteen companies.

The performance condition is measured over a three year period commencing at the end of the financial year preceding the grant of the option and continuing until the end of the third subsequent year. If the performance condition is not then met, it will be measured at the end of the fourth financial year. If the condition has not then been met, the options will lapse.

To meet the performance conditions, the Group's ranking against the comparator group must be at least ninth. The full grant of options will only become exercisable if the Group is ranked first. A performance multiplier will be applied below this level to calculate the number of shares in respect of which options granted to executive directors will become exercisable, and will be calculated on a sliding scale. If Lloyds TSB Group plc is ranked below median the options will not become exercisable.

Options granted to senior executives other than executive directors will not be so highly leveraged and as a result, different performance multipliers may be applied to their options. For the majority of executives, options will be granted with the performance condition but no performance multiplier.

For options granted between 1997 and March 2001

(i) the company's ranking, based on total shareholder return (calculated by reference to both dividends and growth in share price) over the relevant period, should be in the top fifty companies listed in the FTSE 100; and

(ii) there must have been growth in earnings per share which is at least equal to the aggregate percentage change in the Retail Price Index plus three percentage points for each complete year of the relevant period. For options granted between 1997 and 1999 there must have been growth in earnings per share which is at least equal to the aggregate percentage change in the Retail Price Index plus two percentage points for each complete year of the relevant period.

48 Differences between UK GAAP and US GAAP (continued)

d Share compensation schemes (continued)

Options granted in 1996 are only exercisable if there has been growth in earnings per share which is at least equal to the aggregate percentage change in the Retail Price Index, plus two percentage points for each complete year of the relevant period.

In respect of options granted between 1996 and March 2001, the relevant period for the performance conditions begins at the end of the financial year of the date of grant and will continue until the end of the third financial year following commencement or, if not met, the end of such later year in which the conditions are met. Once the conditions have been satisfied the options will remain exercisable without further conditions. If they are not satisfied by the tenth anniversary of the grant the option will lapse.

For options granted in 1995, no performance conditions were attached to the exercise of options.

The effect of the performance conditions on the value of the executive share options has been determined by assuming that the earnings per share condition will be satisfied at all times and by using a stochastic projection model to determine the effect of the market-based condition. The compensation cost accrued in the US GAAP financial statements has therefore been based on a best estimate of the number of options that are likely to vest. To the extent that actual forfeitures are different from the estimate, the calculation of the compensation cost will be revised as appropriate.

As at 31 December 2001, no options granted under the Executive share scheme have lapsed as a result of a failure to satisfy the performance conditions.

Executive scheme	**2001**		2000		1999	
	Number of options	**Weighted average exercise price (pence)**	Number of options	Weighted average exercise price (pence)	Number of options	Weighted average exercise price (pence)
Outstanding at 1 January	**11,216,636**	**615.23**	8,472,746	623.44	9,828,305	489.52
Granted	**6,067,500**	**687.22**	4,260,747	553.92	1,677,700	870.67
Exercised	**(1,196,024)**	**387.11**	(1,065,674)	435.46	(2,836,443)	315.15
Forfeited	**(934,616)**	**793.48**	(451,183)	614.97	(196,816)	486.64
Outstanding at 31 December	**15,153,496**	**651.07**	11,216,636	615.23	8,472,746	623.44

The weighted average fair value of options granted in the year was £1.50 (2000: £1.29; 1999: £1.98)

Share retention plan

During the year, the Group adopted the Lloyds TSB Group plc Share Retention Plan. Options granted under this scheme are not subject to any performance conditions and are exercisable between 3 and 10 years from the date of grant. The option granted in 2001 was made specifically to facilitate the recruitment of Mr Daniels and has a total exercise price of £1.

Share retention plan	**2001 Number of shares**
Outstanding at 1 January	**-**
Granted in the year	**216,763**
Outstanding at 31 December	**216,763**

The weighted average remaining vesting period as at 31 December 2001 was 3 years.

48 Differences between UK GAAP and US GAAP (continued)

d Share compensation schemes (continued)

Save-As-You-Earn scheme

Eligible employees may enter into contracts through the Save-As-You-Earn (SAYE) Scheme to save up to £250 per month and, at the expiry of a fixed term of three, five or seven years, have the option to use these savings to acquire shares in the Group at a discount, which is currently 20 per cent of the market price at the date the options were granted.

SAYE scheme	**2001**		2000		1999	
	Number of options	**Weighted average exercise price (pence)**	Number of options	Weighted average exercise price (pence)	Number of options	Weighted average exercise price (pence)
Outstanding at 1 January	**136,169,743**	**404.03**	141,451,803	393.90	133,795,429	354.86
Granted	**23,850,747**	**548.29**	55,205,646	455.64	16,045,457	718.44
Exercised	**(44,897,336)**	**283.69**	(26,567,632)	179.71	(2,140,791)	279.97
Forfeited	**(8,316,661)**	**500.73**	(33,920,074)	621.48	(6,248,292)	430.38
Outstanding at 31 December	**106,806,493**	**479.30**	136,169,743	404.03	141,451,803	393.90

The weighted average fair value of options granted in the year was £2.24 (2000: £1.65; 1999: £2.52).

The ranges of exercise prices, weighted average fair values and weighted average contractual life for the options granted under the Executive and SAYE schemes outstanding at 31 December 1999, 2000 and 2001 are shown in the table below:

	2001		2000		1999	
	Executive	**SAYE**	Executive	SAYE	Executive	SAYE
Exercise price (pence)	**242.50-887.50**	**160.40-768.00**	242.50-887.50	160.40-768.00	242.50-887.50	160.40-768.00
Fair value (pence)	**64-209**	**67-295**	64-209	63-295	64-209	63-295
Weighted average remaining life (years)	**7.9**	**2.3**	7.6	2.1	8.3	2.6

48 Differences between UK GAAP and US GAAP (continued)

d Share compensation schemes (continued)

The ranges of exercise prices, weighted average exercise prices, weighted average remaining contractual life and number of options outstanding at 31 December 2001 for the Executive and SAYE schemes are as follows:

	Executive scheme			SAYE Scheme		
Exercise price range	Weighted average exercise price (pence)	Weighted average remaining life (years)	Number of options	Weighted average exercise price (pence)	Weighted average remaining life (years)	Number of options
£1 to £2	-	-	-	182.66	0.3	1,182,609
£2 to £3	244.83	3.2	452,412	266.40	1.1	5,738,021
£3 to £4	321.00	4.2	518,378	-	-	-
£4 to £5	-	-	-	434.61	2.0	55,331,066
£5 to £6	539.74	7.4	4,906,437	546.06	3.2	36,629,370
£6 to £7	661.32	9.3	4,159,217	632.00	1.7	4,023,108
£7 to £8	732.91	9.6	1,996,752	731.96	1.9	3,902,319
£8 to £9	873.82	6.7	3,120,300	-	-	-

The fair value calculations are based on the following assumptions:

	Executive	Share Retention Plan	SAYE
Risk-free interest rate	5.0%	4.2%	5.0%
Expected life	5 years	3 years	3, 5 or 7 years
Expected volatility	38-40%	40%	38-40%
Expected dividend yield	4.4%	4.4%	4.4%

Details of options outstanding in respect of stock compensation plans operated prior to 1 January 1995 are as follows:

2001	Number of options at 31 December	Weighted average option price at 31 December (pence)	Number of shares as to which options were exercisable at 31 December	Number of options lapsed during year	Number of options exercised during year	Weighted average exercise prices (pence)
Lloyds TSB Group Staff Share Save Scheme (1989)	-	-	-	10,839	476,580	210.6
Lloyds TSB Group Staff Share Save Scheme	65,955	161.0	65,955	7,190	755,460	161.0
Lloyds TSB Group plc Executive Share Option Scheme (1989)	89,246	177.3	89,246	-	95,070	203.3
Lloyds TSB Group plc Executive Share Option Scheme	137,568	282.5	137,568	-	17,344	282.5
Lloyds Bank Plc Senior Executives' UK Share Option Scheme 1987	123,032	200.7	123,032	2,704	200,096	161.5
Lloyds TSB Group Rollover Scheme (formerly Lloyds Abbey Life)	18,678	139.0	18,678	258,099	37,540	146.6
	434,479		434,479	278,832	1,582,090	

48 Differences between UK GAAP and US GAAP (continued)

d Share compensation schemes (continued)

2000	Number of options at 31 December	Weighted average option price at 31 December (pence)	Number of shares as to which options were exercisable at 31 December	Number of options lapsed during year	Number of options exercised during year	Weighted average exercise prices (pence)
Lloyds TSB Group Staff Share Save Scheme (1989)	487,419	210.7	27,550	311,687	1,263,356	139.9
Lloyds TSB Group Staff Share Save Scheme	828,605	161.0	-	2,556	14,153	161.0
Lloyds Bank Plc Staff Savings-Related Share Option Scheme 1990	-	-	-	230,388	363,503	169.4
Lloyds TSB Group plc Executive Share Option Scheme (1989)	184,316	190.7	184,316	-	41,942	140.7
Lloyds TSB Group plc Executive Share Option Scheme	154,912	282.5	154,912	-	56,712	282.5
Lloyds Bank Plc Senior Executives' UK Share Option Scheme 1987	325,832	176.6	325,832	-	148,720	185.1
Lloyds TSB Group Rollover Scheme (formerly Lloyds Abbey Life)	314,317	135.7	314,317	-	-	-
	2,295,401		1,006,927	544,631	1,888,386	

e Earnings per share

Basic earnings per share under US GAAP differs from UK GAAP (see Note 11) only to the extent that income calculated under US GAAP differs from UK GAAP.

Diluted earnings per share measures the effect that existing share options would have on the basic earnings per share if they were to be exercised, by increasing the number of ordinary shares although any options that are anti-dilutive are excluded from this calculation. An option is considered anti-dilutive when the value of the exercise price exceeds the market price. Under US GAAP certain incentive plan shares, for which the trustees have waived all dividend and voting rights, have been included in the calculation of diluted earnings per share.

	2001	2000	1999
Basic			
Net income (US GAAP)	**£1,524m**	£1,929m	£2,148m
Weighted average number of ordinary shares in issue	**5,533m**	5,487m	5,445m
Earnings per share	**27.5p**	35.2p	39.4p
Diluted			
Net income (US GAAP)	**£1,524m**	£1,929m	£2,148m
Weighted average number of ordinary shares in issue	**5,595m**	5,548m	5,549m
Earnings per share	**27.2p**	34.8p	38.7p

The weighted average number of anti-dilutive shares excluded from the calculation of diluted earnings per share was 9 million at 31 December 2001 (2000: 14 million; 1999: 3 million).

48 Differences between UK GAAP and US GAAP (continued)

f Derivatives held for risk management purposes

Under UK GAAP, the Group uses a variety of financial instruments to hedge exposures in its banking book; these hedges are accounted for on an accruals basis, in line with the underlying instruments being hedged. Any gains or losses that would occur if these instruments were carried at market value are therefore not recognised.

For the purposes of US GAAP, the Group believes that derivatives that are hedges under UK GAAP do not qualify for hedge accounting under the provisions of SFAS No. 133; however prior to the adoption of SFAS No. 133, such exposures did not qualify for hedge accounting under US GAAP either and therefore there is no transition adjustment in respect of SFAS No. 133. Accordingly these exposures have been marked to market, with the resulting gains and losses taken directly to income. The movement in the US GAAP adjustment arising is summarised below:

	2001 £m	2000 £m	1999 £m
Balance at 1 January	**(257)**	(92)	(272)
Exchange and other adjustments	**(6)**	3	2
Net losses recognised in the year	**88**	32	136
Unrecognised (losses) gains arising during the year	**(403)**	(200)	42
	(315)	(168)	178
Balance at 31 December	**(578)**	(257)	(92)

These activities are discussed more fully on pages 58 to 60 and in Note 45e on page F-51.

g Investment securities

Under UK GAAP investment securities are held at amortised cost except within the long-term insurance businesses where the securities are held at market value, with unrealised gains and losses taken to the income statement in the period to which they relate.

Under SFAS No. 115 all debt securities and equity shares are classified and disclosed as either held-to-maturity, available-for-sale or trading. Those classified as held-to-maturity are measured at amortised cost. Available-for-sale securities are measured at fair value with unrealised gains and losses excluded from the income statement and reported net of tax and minority interests as a separate component of other comprehensive income. Trading securities are measured at fair value with unrealised gains and losses included in the income statement. Debt securities and equity shares categorised as available-for-sale under US GAAP give rise to an adjustment to accumulated other comprehensive income as detailed on page F-60.

The disclosures for investment securities in the tables below include those held within the banking business as reported in Notes 17 and 18 and those held within the insurance business. Securities held by the general insurance business are included within Notes 17 and 18 under UK GAAP; for the purposes of US GAAP they have been reclassified into insurance activities. At 31 December 2001, the book and market values of these securities was £273 million (2000: £191 million). The Group had no held-to-maturity securities at 31 December 2001 or 31 December 2000.

	2001 £m	2000 £m
Proceeds from sales of available-for-sale investment debt securities	**15,989**	17,349
Gross realised gains	**(210)**	(170)
Gross realised losses	**27**	31
Net amount sold	**15,806**	17,210

Realised gains and losses are computed using the weighted average cost method. There were no material gains recorded on securities transferred from available-for-sale to trading.

48 Differences between UK GAAP and US GAAP (continued)

g Investment securities (continued)

2001	**Amortised cost £m**	**Gross unrealised gains £m**	**Gross unrealised losses £m**	**Carrying value £m**
Available-for-sale investment securities:				
UK Government	**516**	**24**	**(3)**	**537**
Securities of the US Treasury and US government agencies	**13**	**-**	**-**	**13**
European governments	**105**	**-**	**-**	**105**
Other Government securities	**2,045**	**256**	**(53)**	**2,248**
Other public sector securities	**54**	**1**	**(2)**	**53**
Bank and building society certificates of deposit	**4,670**	**8**	**(1)**	**4,677**
Corporate debt securities	**3,214**	**64**	**(41)**	**3,237**
Mortgage backed securities	**521**	**6**	**-**	**527**
Other asset backed securities	**2,328**	**6**	**(2)**	**2,332**
Other debt securities	**1,326**	**3**	**(4)**	**1,325**
Debt securities	**14,792**	**368**	**(106)**	**15,054**
Equity shares	**41**	**29**	**-**	**70**
	14,833	**397**	**(106)**	**15,124**
Of which:				
Banking	**10,754**	**298**	**(56)**	**10,996**
Insurance	**4,079**	**99**	**(50)**	**4,128**
	14,833	**397**	**(106)**	**15,124**

2000	Amortised cost £m	Gross unrealised gains £m	Gross unrealised losses £m	Carrying value £m
Available-for-sale investment securities:				
UK Government	886	58	(4)	940
Securities of the US Treasury and US Government agencies	12	-	-	12
European governments	112	1	-	113
Other Government securities	1,792	430	(3)	2,219
Other public sector securities	58	-	(1)	57
Bank and building society certificates of deposit	3,035	1	(1)	3,035
Corporate debt securities	2,297	41	(25)	2,313
Mortgage backed securities	18	-	-	18
Other asset backed securities	574	1	(1)	574
Other debt securities	1,213	17	(2)	1,228
Debt securities	9,997	549	(37)	10,509
Equity shares	51	71	(5)	117
	10,048	620	(42)	10,626
Of which:				
Banking	6,245	490	(10)	6,725
Insurance	3,803	130	(32)	3,901
	10,048	620	(42)	10,626

48 Differences between UK GAAP and US GAAP (continued)

g Investment securities (continued)

Maturity of investment debt securities:

	Due within 1 year £m	Due between 1 and 5 years £m	Due between 5 and 10 years £m	Due over 10 years £m	No fixed maturity £m	Total £m
2001						
Available-for-sale						
Amortised cost	**5,068**	**2,189**	**3,213**	**4,145**	**177**	**14,792**
Fair value	**5,081**	**2,185**	**3,250**	**4,358**	**180**	**15,054**
2000						
Available-for-sale						
Amortised cost	3,409	1,508	1,237	3,710	133	9,997
Fair value	3,426	1,576	1,382	3,995	130	10,509

h Own shares

Own shares held of £251 million at 31 December 2001 (2000: £247 million) have been netted off against Additional Paid-in Capital within Shareholders' equity in accordance with ARB No. 51.

i Deferred taxation

In accordance with the provisions of SFAS No. 109, the US GAAP deferred tax liability is:

	2001 £m	2000 £m
Deferred tax liabilities:		
Assets used in the business	**2**	76
Assets leased to customers	**1,596**	1,538
Pension schemes	**776**	758
Value of business acquired	**728**	799
Deferred acquisition costs	**190**	174
Pension profit recognition	**102**	268
Unrealised gains on trading securities	**149**	491
Other	**353**	334
Total liabilities	**3,896**	4,438
Deferred tax assets:		
Goodwill	**(333)**	(260)
General loan loss allowance	**(106)**	(108)
Tax losses - pensions business	**(1,230)**	(1,061)
- other	**(367)**	(299)
Specific loan loss allowance	**(92)**	(50)
Other	**(354)**	(316)
Total assets	**(2,482)**	(2,094)
Valuation allowance	**1,691**	1,375
	3,105	3,719

48 Differences between UK GAAP and US GAAP (continued)

i Deferred taxation (continued)

Valuation allowance

Scottish Widows has a significant with-profits pensions business. This business is subject to UK corporation tax on the basis of a notional return determined by the UK taxation authorities. To the extent that the actual return from the business is less than the notional return, tax losses accumulate which may be carried forward and offset against excess returns in future years. The value of these losses at 31 December 2001 was £1,230 million (2000: £1,061 million). Excess returns have only occurred once in the thirteen years since this basis of taxation was introduced and are only likely to be triggered in the future if interest rates increase significantly or the actuarial valuation basis alters significantly. Given the current low interest rate environment and in view of the fact that the actuarial valuation basis is currently considered unlikely to alter significantly, in the opinion of management it is more likely than not that these losses will not be realised and therefore a full valuation allowance has been established against this balance.

A further valuation allowance of £128 million (2000: £54 million) has been established against other tax losses which are not expected to be utilised in the foreseeable future. Under UK tax legislation, certain capital losses may only be offset against taxable gains of a particular type and consequently the associated deferred tax assets are less certain of realisation. Assessments have been made as to the likelihood of gains arising that can be offset against these losses and, to the extent that it is more likely than not that these losses will not be realised, appropriate valuation allowances have been established. In relation to other tax losses, the pattern of utilisation of losses over previous years has been reviewed together with gains that may be realised in the foreseeable future and an appropriate valuation allowance established to the extent that it is more likely than not that these losses will not be realised.

A deferred tax asset of £333 million (2000: £260 million) has been recognised as a result of the different accounting and tax treatments for goodwill arising upon acquisition of companies and businesses. There is currently no expectation that these businesses will be disposed of and therefore in the opinion of management it is more likely than not that these losses will not be realised. Accordingly, a full valuation allowance has been established against this balance.

Tax losses

The Group has the following tax losses available to be carried forward and offset against the future taxable profits of certain subsidiaries. The majority of the losses may be carried forward indefinitely.

	2001 £m	2000 £m
Trading losses	**403**	289
Capital losses	**447**	488
Pensions business	**4,100**	3,370
	4,950	4,147

US GAAP reconciliation

The following tables reconcile the UK GAAP tax charge and deferred tax liability to the US GAAP tax charge and deferred tax liability as disclosed on pages F-61 and F-62.

	2001 £m	2000 £m	1999 £m
UK GAAP Profit and loss tax charge	**971**	1,105	1,111
Deferred tax – US GAAP	**(38)**	75	107
Deferred tax – US GAAP reconciling items	**(457)**	(488)	202
US GAAP Profit and loss tax charge	**476**	692	1,420

48 Differences between UK GAAP and US GAAP (continued)

i Deferred taxation (continued)

	2001 **£m**	2000 £m
UK GAAP Deferred tax liability	**1,719**	1,683
Deferred tax – US GAAP	**45**	83
Deferred tax - US GAAP reconciling items	**1,246**	1,855
Other items *	**95**	98
US GAAP Deferred tax liability	**3,105**	3,719

* Under UK GAAP applicable to banking groups, the Group accounts for its life assurance operations using the embedded value basis of accounting and the shareholder's and policyholders' interests are accounted for as one-line items. Under US GAAP the constituent parts of the shareholder's and policyholders' interests are separately disclosed and as a result of this reclassification the total deferred tax liability has been increased. There is no impact on the underlying shareholder's equity.

j Loan impairment

At 31 December 2001, the Group estimated that there was no difference between the carrying value of its loan portfolio on the basis of SFAS No. 114 and its value in the UK GAAP financial statements. Impaired loans are those reported as non-performing on page F-21, less those loans which are outside the scope of SFAS No. 114, and amounted to £472 million (2000: £477 million). The impairment reserve in respect of these loans estimated in accordance with the provisions of SFAS No. 114 was £249 million (2000: £235 million). During the year ended 31 December 2001, impaired loans, including those excluded from SFAS No. 114, averaged £1,198 million (2000: £1,159 million) and interest income recognised on these loans was £27 million (2000: £11 million).

k Significant Group concentrations of credit risk

SFAS No. 105 'Disclosure of Information about Financial Instruments with Off-Balance Sheet Risk and Financial Instruments with Concentrations of Credit Risk' states that concentrations of credit risk exist if a number of counterparties are engaged in similar activities and have similar economic characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. The Group's exposure to credit risk is concentrated in the United Kingdom where the majority of the Group's activities are conducted and is detailed further in Note 16.

l Repos and reverse repos

The Group enters into reverse repo transactions which are accounted for as collateralised loans. It is the Group's policy to seek collateral which is at least equal to the amount loaned. At 31 December 2001, the fair value of collateral accepted under reverse repo transactions that the Group is permitted by contract or custom to sell or repledge was £1,042 million (2000: £4,673 million). Of this, £230 million (2000: £3,488 million) was sold or repledged as at 31 December 2001. The remainder has been held for continuing use within the business.

The Group also enters into repos which are accounted for as secured borrowings. As at 31 December 2001, the carrying value of assets that have been pledged as collateral under repo transactions where the secured party is permitted by contract or custom to sell or repledge was £1,408 million (2000: £3,803 million).

m Segmental analysis

Under UK GAAP, if an entity has two or more classes of business, or operates in two or more geographical segments which differ substantially from each other, Statement of Standard Accounting Practice No 25 "Segmental Reporting" requires that information concerning the results and net assets of the different classes of business and geographical segments should be given in the accounts. In determining whether an entity has different classes of business the accounting standard recommends that a number of factors should be taken into account, including the nature of products and services, the markets in which they are sold, the distribution channels for the products and the manner in which the entity's activities are organised. Ultimately, however, SSAP 25 states that the determination of an entity's classes of business depends upon the judgement of the directors. The Group's segmental analysis prepared in accordance with UK GAAP is shown in Note 2 on pages F-13 to F-15.

In order to give a more meaningful presentation of the performance of the Group's operations and to take into account the similarities of products and services, customer bases, distribution channels and regulatory regimes, the results of a small number of businesses have been reflected in different reporting segments for financial reporting purposes compared with the management accounts. The effect of this is shown below.

48 Differences between UK GAAP and US GAAP (continued)

m Segmental analysis (continued)

Under US GAAP, SFAS No. 131 “Disclosure about Segments of an Enterprise and Related Information” defines an operating segment as a component of the business that engages in business activities from which it may earn income or incur expenses and whose operating results are regularly reviewed by the enterprise’s chief operating decision maker to make decisions about resource allocation and to assess its performance. SFAS No. 131 permits the aggregation of operating segments if the segments demonstrate similar economic characteristics and if the segments are similar in the following respects: the nature of the products and services offered; the nature of the production processes; the type or class of customer for their products or services; the distribution channels; and the nature of the regulatory environment.

UK Retail Banking and Mortgages	**2001**			2000			1999		
	Figures based on management accounts £m	**Businesses transferred £m**	**Figures disclosed in segmental analysis £m**	Figures based on management accounts £m	Businesses transferred £m	Figures disclosed in segmental analysis £m	Figures based on management accounts £m	Businesses transferred £m	Figures disclosed in segmental analysis £m
Net interest income	**2,765**	**350**	**3,115**	2,634	317	2,951	2,660	283	2,943
Other operating income	**953**	**188**	**1,141**	1,045	98	1,143	983	104	1,087
Total income	**3,718**	**538**	**4,256**	3,679	415	4,094	3,643	387	4,030
Exceptional restructuring costs	**(150)**	**-**	**(150)**	(99)	-	(99)	-	-	-
Other operating expenses	**(1,994)**	**(249)**	**(2,243)**	(1,921)	(178)	(2,099)	(1,810)	(141)	(1,951)
Trading surplus	**1,574**	**289**	**1,863**	1,659	237	1,896	1,833	246	2,079
Provisions for bad and doubtful debts	**(357)**	**(58)**	**(415)**	(288)	(44)	(332)	(379)	(46)	(425)
Income from associated undertakings and joint ventures	**(10)**	**-**	**(10)**	2	-	2	3	-	3
Profit before tax	**1,207**	**231**	**1,438**	1,373	193	1,566	1,457	200	1,657

Wholesale Markets and International Banking	**2001**			2000			1999		
	Figures based on management accounts £m	**Businesses transferred £m**	**Figures disclosed in segmental analysis £m**	Figures based on management accounts £m	Businesses transferred £m	Figures disclosed in segmental analysis £m	Figures based on management accounts £m	Businesses transferred £m	Figures disclosed in segmental analysis £m
Net interest income	**2,205**	**(347)**	**1,858**	1,970	(317)	1,653	1,947	(283)	1,664
Income from long-term assurance business	**12**	**-**	**12**	8	-	8	8	-	8
Other operating income	**1,448**	**(135)**	**1,313**	1,156	(99)	1,057	980	(104)	876
Total income	**3,665**	**(482)**	**3,183**	3,134	(416)	2,718	2,935	(387)	2,548
Exceptional restructuring costs	**(17)**	**-**	**(17)**	(30)	-	(30)	-	-	-
Other operating expenses	**(1,667)**	**257**	**(1,410)**	(1,442)	188	(1,254)	(1,285)	141	(1,144)
Trading surplus	**1,981**	**(225)**	**1,756**	1,662	(228)	1,434	1,650	(246)	1,404
Provisions for bad and doubtful debts	**(390)**	**58**	**(332)**	(253)	44	(209)	(236)	46	(190)
Amounts written-off fixed asset investments	**(60)**	**-**	**(60)**	(32)	-	(32)	(7)	-	(7)
Profit before tax	**1,531**	**(167)**	**1,364**	1,377	(184)	1,193	1,407	(200)	1,207

48 Differences between UK GAAP and US GAAP (continued)

Insurance activities

The following tables summarise the adjustments to the profit and loss account and balance sheet which would arise from the application of US GAAP to the Group's insurance business.

Profit and loss account	Note	**2001 Life £m**	**2001 General £m**	**2001 Total £m**	2000 Life £m	2000 General £m	2000 Total £m	1999 Life £m	1999 General £m	1999 Total £m
Income from long-term assurance business	(i)	**(193)**	**-**	**(193)**	(615)	-	(615)	(227)	-	(227)
Other interest and dividends	(i)	**1,019**	**-**	**1,019**	948	-	948	191	-	191
Insurance premiums	(i)	**1,232**	**-**	**1,232**	1,205	-	1,205	840	-	840
Other income	(i)	**(2,005)**	**-**	**(2,005)**	258	-	258	363	-	363
Policyholder benefits and claims expense	(i)	**(2,033)**	**-**	**(2,033)**	(1,585)	(12)	(1,597)	(759)	(11)	(770)
Movement in the undistributed policyholders liabilities		**2,427**	**-**	**2,427**	317	-	317	(3)	-	(3)
Insurance underwriting, operating and acquisition expenses	(i)	**(697)**	**(4)**	**(701)**	(734)	13	(721)	(287)	8	(279)
Depreciation	(i)	**(23)**	**-**	**(23)**	(16)	-	(16)	(9)	-	(9)
Amortisation of value of long-term assurance business acquired	(ii)	**(305)**	**-**	**(305)**	(285)	-	(285)	(1)	-	(1)
Revenue and expense recognition		**-**	**24**	**24**	-	(26)	(26)	-	11	11
Equalisation provision		**-**	**8**	**8**	-	4	4	-	3	3
Total adjustments before tax		**(578)**	**28**	**(550)**	(507)	(21)	(528)	108	11	119

Balance sheet	Note	**2001 Life £m**	**2001 General £m**	**2001 Total £m**	2000 Life £m	2000 General £m	2000 Total £m
Long-term assurance business attributable to shareholders	(ii)	**(6,574)**	**-**	**(6,574)**	(6,549)	-	(6,549)
Long-term assurance assets attributable to policyholders	(iii)	**(46,389)**	**-**	**(46,389)**	(51,085)	-	(51,085)
Cash and due from banks		**2,604**	**-**	**2,604**	1,569	-	1,569
Trading account assets	(iv)	**25,620**	**-**	**25,620**	28,591	-	28,591
Tangible fixed assets		**163**	**-**	**163**	156	-	156
Deferred acquisition costs	(v)	**660**	**(15)**	**645**	572	(11)	561
Value of long-term assurance business acquired	(ii)	**3,007**	**-**	**3,007**	3,312	-	3,312
Separate account assets	(viii)	**22,067**	**-**	**22,067**	25,559	-	25,559
Other assets		**1,190**	**36**	**1,226**	872	24	896
Indebtedness of related parties		**1,919**	**-**	**1,919**	1,478	-	1,478
Long-term assurance liabilities to policyholders	(iii)	**46,389**	**-**	**46,389**	51,085	-	51,085
Debt securities in issue		**(99)**	**-**	**(99)**	(31)	-	(31)
Policyholder liabilities	(vi)	**(23,346)**	**-**	**(23,346)**	(22,059)	-	(22,059)
Undistributed policyholder allocations	(vii)	**(3,478)**	**-**	**(3,478)**	(5,905)	-	(5,905)
Equalisation provision		**-**	**31**	**31**	-	23	23
Other liabilities		**(969)**	**-**	**(969)**	(824)	(12)	(836)
Separate account liabilities	(viii)	**(22,067)**	**-**	**(22,067)**	(25,559)	-	(25,559)
Indebtedness to related parties		**(1,023)**	**-**	**(1,023)**	(807)	-	(807)
Total adjustments before tax		**(326)**	**52**	**(274)**	375	24	399

48 Differences between UK GAAP and US GAAP (continued)

(i) Revenue recognition

Under UK GAAP applicable to banking groups, the Group accounts for its life assurance operations using the embedded value basis of accounting. An embedded value is an actuarially determined estimate of the economic value of a life assurance company, excluding any value which may be attributed to future new business. The embedded value is the sum of the net assets of the life assurance company and the present value of the in-force business. The value of the in-force business is calculated by projecting future net cash flows using appropriate economic and actuarial assumptions and the result discounted at a rate which reflects the shareholders' overall risk premium. The change in the embedded value during any reporting period adjusted for any dividends declared or capital injected, and grossed up at the underlying rate of corporation tax, is reflected in the Group's profit and loss account as income from long-term assurance business.

US GAAP requires that results of the life assurance business should be reported on a gross basis and reflected in appropriate captions in the income statement. Premiums from conventional with-profits policies and other protection-type life insurance policies are recognised as revenue when due from the policyholder. Premiums from unitised with-profits life insurance policies and investment contracts, which have minimal mortality risk, are reported as increases in policyholder account balances when received. Revenues derived from these policies consist of mortality charges, policy administration charges, investment management fees and surrender charges that are deducted from policyholders' accounts and are disclosed within other income.

Under US GAAP, premiums and policy charges received that relate to future periods are deferred until the period to which they relate. For limited payment annuities, the excess of the gross premium over the US GAAP net benefit premium is deferred and amortised in relation to the expected future benefit payments. For investment contracts, policy charges that benefit future periods are deferred and amortised in relation to expected gross profits.

(ii) Value of long term assurance business acquired

Under US GAAP the value of the long-term assurance business acquired ('VOBA') is calculated at acquisition by discounting future earnings to a present value. In subsequent years the VOBA is amortised over the premium recognition period for with-profits life insurance and other protection-type insurance policies using assumptions consistent with those used in computing policyholder benefit provisions. VOBA for investment-type policies and unitised insurance policies is amortised in relation to expected gross profits. Expected gross profits are evaluated regularly against actual experience and revisions made to allow for the effect of any changes.

	2001 £m	2000 £m
Balance at 1 January	**3,312**	701
Acquisition	**-**	2,896
Interest accrued on unamortised balance	**(92)**	120
Amortisation	**(213)**	(405)
Balance at 31 December	**3,007**	3,312

Over the next 5 years the amount of VOBA expected to be amortised prior to interest accruals is:

2002	£225m
2003	£216m
2004	£207m
2005	£203m
2006	£196m

48 Differences between UK GAAP and US GAAP (continued)

(iii) Balance sheet

Under UK GAAP applicable to banking groups, in order to reflect the different nature of the shareholder's and policyholders' interests in the long-term assurance business these are shown separately as one-line items in the Group's balance sheet. The value of the long-term assurance business attributable to shareholders comprises the net assets of the life assurance companies and the value of the in-force business. The assets attributable to policyholders mainly comprise the investments held in the long-term assurance funds either on behalf of policyholders, or which have not yet been allocated to either the policyholders or the shareholder. Liabilities to policyholders mainly comprise policyholder benefit provisions.

Under US GAAP the constituent parts of the shareholder's and policyholders' interests in the long-term assurance business are separately disclosed. Significant differences also arise regarding the valuation of the constituent assets and liabilities, which are discussed further in the notes which follow.

(iv) Investments

Under UK GAAP applicable to banking groups, debt securities and equity shares held within the long-term assurance funds are included in the Group's balance sheet at market value; investment properties are included at existing use value.

Under US GAAP, debt securities are classified as trading, available-for-sale or held-to-maturity; equity shares may only be classified as trading or available-for-sale. Securities classified as trading are carried at current market value. Securities classified as available-for-sale are carried at current market value, and unrealised gains and losses arising are held as a separate component of shareholders' equity. Securities classified as held-to-maturity are carried at amortised cost. In addition, US GAAP requires that all freehold and long leasehold properties should be carried at depreciated historic cost.

For those securities classified as available-for-sale, the disclosures required under SFAS No. 115 are presented in aggregate with the banking business on pages F-74 to F-76.

(v) Deferred acquisition costs

Under UK GAAP applicable to banking groups, the cost of acquiring new and renewal life assurance business is recognised in the embedded value calculation as incurred.

Under US GAAP the costs incurred by the Group in the acquisition of new and renewal life insurance business are capitalised. These consist of the acquisition costs, principally commissions, marketing and advertising and the administration costs associated with the processing and policy issuance, typically underwriting, together these are capitalised as an asset and amortised in relation to the profit margin of the policies acquired.

Deferred acquisition costs for conventional with-profits life insurance and other protection type insurance policies are amortised in relation to premium income using assumptions consistent with those used in computing policyholder benefits provisions. Investment, universal life, and separate account contracts are amortised in proportion to the estimated gross profits arising from the contracts.

(vi) Policyholder liabilities

Under UK GAAP applicable to banking groups, future policyholder benefit provisions included in the Group's balance sheet are calculated using net premium methods for conventional with-profits life insurance and other protection-type policies and are based on fund value for unitised with-profits insurance policies and investment-type policies. Net premiums are calculated using assumptions for interest, mortality, morbidity and expenses. These assumptions are determined as prudent best estimates at the date of valuation. Liabilities are not established for future annual and terminal bonus declarations.

Under US GAAP, for unitised with-profits insurance and other investment-type policies, the liability is represented by the policyholder's account balance before any applicable surrender charges. Policyholder benefit liabilities for conventional with-profits life insurance and other protection-type insurance policies are developed using the net level premiums method. Assumptions for interest, mortality, morbidity, withdrawals and expenses were prepared using best estimates at date of policy issue (or date of company acquisition by the Group, if later) plus a provision for adverse deviation based on Group experience. Interest assumptions range from 5 per cent to 11 per cent.

48 Differences between UK GAAP and US GAAP (continued)

(vii) With profits business

With-profits policies entitle the policyholder to participate in the surplus within the with-profits life fund of the insurance company which issued the policy. Regular bonuses are determined annually by the issuing company's Appointed Actuary and its board of directors. The bonuses that may be declared are highly correlated to the overall performance of the underlying assets and liabilities of the fund in which the contracts participate and are the subject of normal variability and volatility. Terminal bonuses are paid on maturity of the contract and are designed to provide policyholders with a share of the total performance of the issuing company during the period of the contract.

The contract for conventional with-profits business written into the with-profits fund provides that approximately 90 per cent of the surplus arising from the net assets of the fund are allocated to policyholders in the form of annual bonuses. For unitised with-profits business written into the with-profits fund all of the surplus is allocated to policyholders as bonus.

Under UK GAAP all amounts in the with-profits fund not yet allocated to policyholders or shareholders are recorded in the liabilities attributable to policyholders on the Group's balance sheet.

Under US GAAP a liability is established for undistributed policyholder allocations. The excess of assets over liabilities in the with-profits fund is allocated to the policyholders and shareholders in accordance with the proportions prescribed by the contracts. The remaining liability comprises the obligation of the insurance company to the policyholders.

(viii) Separate account assets and liabilities

Under UK GAAP, segregated accounts are established for policyholder business for which policyholder benefits are wholly or partly determined by reference to specific investments or to an investment-related index. This is referred to as linked business. Linked business can either be unit-linked, property-linked or index-linked. In the case of the unit-linked and property-linked business the policyholders bear the investment risk. The Group bears the investment risk relating to the index-linked business.

Under US GAAP only those assets where the policyholder bears the investment risk are reported as separate account assets and liabilities.

49 Parent company disclosures

a Company profit and loss account

	2001 £m	2000 £m	1999 £m
Net interest income	**6**	8	8
Dividends received from group undertakings	**1,872**	1,685	1,300
Total income	**1,878**	1,693	1,308
Operating expenses	**(60)**	(39)	(35)
Profit on ordinary activities before tax	**1,818**	1,654	1,273
Taxation credit	**75**	45	71
Profit on ordinary activities after tax	**1,893**	1,699	1,344
Dividends	**(1,872)**	(1,683)	(1,451)
Profit (loss) for the year	**21**	16	(107)

b Company balance sheet

	2001 £m	2000 £m
Fixed assets		
Investments		
Shares in group undertakings	**11,960**	11,152
Loans to group undertakings	**759**	759
Own shares	**23**	24
	12,742	11,935
Current assets		
Debtors falling due within one year		
Amounts owed by group undertakings	**1,369**	1,233
Other debtors	**47**	42
Tax recoverable	**29**	16
Cash balances with group undertakings	**114**	66
	1,559	1,357
Current liabilities		
Amounts falling due within one year		
Short-term borrowings	**-**	1
Amounts owed to group undertakings	**1,760**	1,811
Other creditors	**62**	62
Dividend payable	**1,306**	1,172
	3,128	3,046
Net current liabilities	**(1,569)**	(1,689)
Total assets less current liabilities	**11,173**	10,246
Creditors: amounts falling due after more than one year		
Dated loan capital	**413**	512
Net assets	**10,760**	9,734
Capital and reserves		
Called-up share capital	**1,411**	1,396
Share premium account	**959**	595
Revaluation reserve	**5,894**	5,086
Profit and loss account	**2,496**	2,657
Shareholders' funds (equity)	**10,760**	9,734

49 Parent company disclosures (continued)

c Company cash flow statement

	2001 £m	2000 £m	1999 £m
Net cash outflow from operating activities	**(68)**	(149)	(815)
Returns on investments and servicing of finance:			
Dividends received from group undertakings	**1,736**	1,375	1,340
Interest paid on subordinated liabilities (loan capital)	**(41)**	(34)	(25)
Net cash inflow from returns on investments and servicing of finance	**1,695**	1,341	1,315
Taxation:			
UK corporation tax received	**62**	64	98
Capital expenditure and financial investment:			
Capital lending to subsidiaries	**(100)**	-	(150)
Repayments of capital lending by subsidiaries	**100**	-	740
Net cash inflow from capital expenditure and financial investment	**-**	-	590
Acquisitions and disposals:			
Acquisition of group undertakings	**-**	-	(3,714)
Disposal of group undertakings	**-**	-	3,920
Net cash inflow from acquisitions and disposals	**-**	-	206
Equity dividends paid	**(1,738)**	(1,522)	(1,285)
Net cash (outflow) inflow before financing	**(49)**	(266)	109
Financing:			
Issue of ordinary share capital net of £182million (2000: £128 million;1999: £205 million) contribution to the QUEST	**197**	70	108
Repayments of subordinated liabilities (loan capital)	**(100)**	-	-
Net cash inflow from financing	**97**	70	108
Increase (decrease) in cash	**48**	(196)	217

d Reconciliation to US GAAP

	2001 £m	2000 £m
Shareholders' funds (UK GAAP)	**10,760**	9,734
Dividends	**1,306**	1,172
Own shares	**(23)**	(24)
Revaluation of shares in group undertakings	**1,378**	2,708
Shareholders' equity (US GAAP)	**13,421**	13,590

e Reconciliation of the movements in shareholders' equity under US GAAP

	2001 £m	2000 £m	1999 £m
Profit after tax (UK GAAP)	**1,893**	1,699	1,344
Share compensation schemes	**(46)**	(31)	(37)
Net income (US GAAP)	**1,847**	1,668	1,307
Dividends paid	**(1,738)**	(1,522)	(1,285)
	109	146	22
Issue of shares	**194**	70	108
Movement in own shares	**1**	11	(14)
Share compensation schemes	**46**	31	37
Revaluation of shares in group undertakings	**(519)**	383	709
	(169)	641	862
Shareholders' equity at 1 January	**13,590**	12,949	12,087
Shareholders' equity at 31 December	**13,421**	13,590	12,949

GLOSSARY

Term Used	US Equivalent or Brief Description
Accounts	Financial statements.
Associates	Long-term equity investments accounted for by the equity method.
ATM	Automatic Teller Machine.
Attributable profit	Net income.
Broking	Brokerage.
Building society	A building society is a mutual institution set up to lend money to its members for house purchases. See also "Demutualisation".
Called-up share capital	Ordinary shares, issued and fully paid.
Contract hire	Leasing.
Cashpoint	Automatic Teller Machine
Contribution	Profit before tax before taking into account the unusual items.
Creditors	Payables.
Dealing	Trading.
Debtors	Receivables.
Demutualisation	Process by which a mutual society is converted into a public limited company.
Economic profit	See definition under "Operating and Financial Review and Prospects - Economic profit".
Embedded value	See definition under "Operating and Financial Review and Prospects - Overview".
Endowment mortgage	An interest-only mortgage to be repaid by the proceeds of an endowment insurance policy which is assigned to the lender providing the mortgage. The sum insured, which is payable on maturity or upon the death of the policyholder, is used to repay the mortgage.
Estate agency	Real estate agent.
Fees and commissions payable	Fees and commissions expense.
Fees and commissions receivable	Fees and commissions income.
Finance lease	Capital lease.
Freehold	Ownership with absolute rights in perpetuity.
Guaranteed annuity	See "Business - Guaranteed Annuity Options".
Guaranteed annuity option	See "Business - Guaranteed Annuity Options".
Hire purchase	See "Business - Wholesale Markets and International Banking–Asset finance".
Interchange	System allowing customers of different Automatic Teller Machine (ATM) operators to use any ATM that is part of the system. The LINK network is an interchange in the UK.

Term Used	US Equivalent or Brief Description
Interest payable	Interest expense.
Interest receivable	Interest income.
ISA	Individual Savings Account.
Leasehold	Land or property which is rented from the owner for a specified term under a lease. At the expiry of the term the land or property reverts back to the owner.
Lien	Under UK law, a right to retain possession pending payment.
Life assurance	Life insurance.
LINK network	See “Interchange”.
Loan capital	Long-term debt.
Members	Shareholders.
Memorandum and articles of association	Articles and bylaws.
National Insurance	A form of taxation payable in the UK by employees, employers and the self-employed, used to fund benefits at the national level including state pensions, medical benefits through the National Health System (NHS), unemployment and maternity. It is part of the UK’s national social security system and ultimately controlled by the Department of Social Security.
NBNZ	The National Bank of New Zealand Limited.
Nominal value	Par value.
One-off	Non-recurring.
Ordinary shares	Common stock.
Overdraft	A line of credit, contractually repayable on demand unless a fixed-term has been agreed, established through a customer’s current account.
Preference shares	Preferred stock.
Premises	Real estate.
Profit & loss account	Income statement.
Profit & loss account reserve	Retained earnings.
Provisions	Reserves.
Recurring premium	Premiums which are payable throughout the duration of a policy or for some shorter fixed period.
Reinsurance	The insuring again by an insurer of the whole or part of a risk that it has already insured with another insurer called a reinsurer.
SERPS	State Earnings Related Pension Scheme, a UK government pension scheme.
Share capital	Capital stock.
Shareholders’ funds	Stockholders’ equity.
Share premium account	Additional paid-in capital.
Shares in issue	Shares outstanding.

Term Used	US Equivalent or Brief Description
Single premium	A premium in relation to an insurance policy payable once at the commencement of the policy.
Stakeholder pension	See “Operating and Financial Review and Prospects - Other Income - 2000 compared with 1999”.
Superannuation	An occupational pension scheme.
Tangible fixed assets	Property and equipment.
Undistributable reserves	Restricted surplus.
Unit-linked products	See “Business - Guaranteed Annuity Options”.
Unit trust	Mutual fund.
VaR	Value at Risk, see definition under “Operating and Financial Review and Prospects - Market risk in banking operations - Trading Value at Risk (VaR)”.
VcV	Variance/covariance methodology, see definition under “Operating and Financial Review and Prospects–Market risk in banking operations–Trading Value at Risk (VaR)”.
Weighted sales	The sum of regular premiums plus one-tenth of single premiums paid by customers on life insurance, pensions and unit trusts.
With-profits bond	See “Operating and Financial Review and Prospects-Life, Pensions (and unit trusts-2000 compared to 1999”.
With-profits fund	See “Operating and Financial Review and Prospects - Liquidity and capital resources - Insurance and investments businesses”.

FORM 20-F CROSS-REFERENCE SHEET

LIST OF EXHIBITS

1 Memorandum and articles of association of Lloyds TSB Group plc.*

2 (i) Limited Partnership Agreements dated 4 February 2000, relating to the preference securities.*

(ii) Trust Deed dated 25 April 2001, relating to the perpetual capital securities.*

4 (a)(i) Transfer Agreement between Scottish Widows' Fund and Life Assurance Society and Lloyds TSB Group plc dated 23 June 1999, relating to the transfer of the business of Scottish Widows Fund and Life Assurance Society.*

(ii) Deed of Amendment between Scottish Widows' Fund and Life Assurance Society and Lloyds TSB Group plc dated 17 November 1999, amending the Transfer Agreement dated 23 June 1999, relating to the transfer of the business of Scottish Widows Fund and Life Assurance Society.*

(iii) Share Purchase Agreement among Lloyds TSB Bank plc, Chartered Trust Holdings plc and others dated 31 August 2000, relating to the acquisition of the Chartered Trust Group plc.*

(b)(i) Service agreement dated 2 February 1999, as amended, between Lloyds TSB Group plc and M Kent Atkinson.*

(ii) Service agreement dated 19 June 1989, as amended, between Lloyds TSB Group plc and Peter B. Ellwood.*

(iii) Service agreement dated 6 September 1991, as amended, between Lloyds TSB Group plc and Michael E. Fairey.*

(iv) Service agreement dated 9 February 2000, as amended, between Lloyds TSB Group plc and Archie G. Kane.*

(v) Service agreement dated 13 February 1998, as amended, between Lloyds TSB Group plc and David P. Pritchard.*

(vi) Service agreement dated 7 March 2000, as amended, between Lloyds TSB Group plc and Michael D. Ross.*

(vii) Service agreement dated 19 October 2001 between Lloyds TSB Group plc and J Eric Daniels.

8 List of subsidiaries, their jurisdiction of incorporation and the names under which they conduct business.

* Previously filed with the SEC, together with Lloyds TSB Group's registration statement, on 25 September 2001.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorised the undersigned to sign this annual report.

LLOYDS TSB GROUP plc

By: /s/ M Kent Atkinson

Name: M. Kent Atkinson

Title: Group Finance Director

Dated: 3 May 2002