

Lloyds TSB Bank plc

Interim Management Report

For the half-year to 30 June 2010

Member of the Lloyds Banking Group

FORWARD LOOKING STATEMENTS

This announcement contains forward looking statements with respect to the business, strategy and plans of Lloyds TSB Bank plc, its current goals and expectations relating to its future financial condition and performance. Statements that are not historical facts, including statements about the Lloyds TSB Bank Group's or the Lloyds TSB Bank Group's management's beliefs and expectations, are forward looking statements. By their nature, forward looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. The Lloyds TSB Bank Group's actual future business, strategy, plans and/or results may differ materially from those expressed or implied in these forward looking statements as a result of a variety of risks, uncertainties and other factors, including, without limitation, UK domestic and global economic and business conditions; the ability to derive cost savings and other benefits, as well as the ability to integrate HBOS successfully into the Lloyds Banking Group; the ability to access sufficient funding to meet the Lloyds TSB Bank Group's liquidity needs; changes to Lloyds TSB Bank plc's or Lloyds Banking Group plc's credit ratings; risks concerning borrower or counterparty credit quality; market related trends and developments; changing demographic trends; changes in customer preferences; changes to regulation, accounting standards or taxation, including changes to regulatory capital or liquidity requirements; the policies and actions of governmental or regulatory authorities in the UK, the European Union, or jurisdictions outside the UK, including other European countries and the US; the ability to attract and retain senior management and other employees; requirements or limitations imposed on the Lloyds TSB Bank Group as a result of HM Treasury's investment in Lloyds Banking Group plc; the ability to complete satisfactorily the disposal of certain assets as part of Lloyds Banking Group's EU state aid obligations; the extent of any future impairment charges or write-downs caused by depressed asset valuations; exposure to regulatory scrutiny, legal proceedings or complaints, actions of competitors and other factors. Please refer to Lloyds Banking Group plc's latest Annual Report on Form 20-F filed with the US Securities and Exchange Commission for a discussion of such factors together with examples of forward looking statements. The forward looking statements contained in this announcement are made as at the date of this announcement, and the Lloyds TSB Bank Group undertakes no obligation to update any of its forward looking statements.

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FINANCIAL REVIEW

Results

The consolidated income statement on page 7 shows a profit before tax of £790 million and a profit attributable to equity shareholders of £144 million for the half-year ended 30 June 2010.

Principal activities

Lloyds TSB Bank plc (the Bank) and its subsidiaries (together, the Group) provides a range of banking and financial services through branches and offices in the UK and overseas.

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

Corporate structure

Following a reorganisation of Lloyds Banking Group on 1 January 2010, the Bank acquired 100 per cent of the issued ordinary share capital of HBOS plc from Lloyds Banking Group plc; the consideration for this transfer was the issue of 21.4 million shares to Lloyds Banking Group plc for a total value of £21,394 million.

Review of results

Following the transfer of HBOS plc on 1 January 2010, the consolidated results of Lloyds TSB Bank plc include the results of the HBOS group from that date; the comparative figures for 2009 reflect only the Lloyds TSB businesses.

The profit before tax of £790 million for the half-year to 30 June 2010 compares to a profit before tax of £882 million for the half-year to 30 June 2009. A substantial increase in the impairment charge, largely as a result of the transfer of HBOS, and an increase in integration costs has been offset by increased income from the enlarged group and a one-off curtailment gain following changes in the terms of the Group's retirement benefit schemes.

Net interest income increased by £3,924 million to £7,095 million, reflecting the transfer of HBOS and improved margins on lending.

Other income increased by £3,582 million to £8,159 million following the transfer of HBOS, improvements in net fee income and favourable net trading income as a result of relative market conditions, partly offset by a £1,599 million reduction in gains on capital transactions arising from the Lloyds Banking Group's liability management programme.

Overall total income increased by £7,506 million to £15,254 million for the half-year to 30 June 2010 from £7,748 million for the half-year to 30 June 2009.

Insurance claims increased by £1,997 million to £3,189 million as a result of the transfer of HBOS and the improvement in investment returns attributable to policyholders.

FINANCIAL REVIEW (continued)

Total operating expenses increased by £2,364 million to £5,791 million. In addition to the impact of the HBOS transfer there was a £594 million increase in integration costs relating to the combination of the Lloyds TSB and HBOS businesses and a £150 million charge in respect of impairment of tangible fixed assets not related to integration; however these items were offset by the £1,019 million curtailment gain following changes in terms and conditions of the Group's retirement benefit schemes and the non-repetition of the £240 million charge in respect of goodwill impairment which the Group reported in the half-year to 30 June 2009.

Impairment losses increased by £3,175 million to £5,423 million. This item principally reflects impairment charges in respect of loans and advances to customers which increased by £3,266 million to £5,378 million, as a decrease in the charge within the Lloyds TSB businesses following improved credit quality experience in both retail and wholesale lending was more than offset by the impact of the transfer of HBOS.

Profit before tax was £92 million lower at £790 million in the half-year to 30 June 2010 compared to £882 million in the same period last year. Profit after tax, however, decreased by £625 million to £214 million from £839 million. A substantial increase in the tax charge to £576 million reflects the impact of losses generated overseas in the HBOS businesses and movements in policyholder-related tax items (see note 6).

Total assets have increased by £469,990 million to £1,042,970 million at 30 June 2010 from £572,980 million at 31 December 2009 as a result of the transfer of HBOS, with loans and advances to customers increasing by £381,095 million to £612,133 million and customer deposits increasing by £245,780 million to £420,438 million. Shareholders' equity was £30,676 million higher at £44,096 million reflecting £21,394 million from the issue of shares on the transfer of HBOS and a further credit of £6,348 million to the merger reserve arising on the transfer.

The Group's total capital ratio was 12.6 per cent (31 December 2009: 11.8 per cent) with a tier 1 ratio of 10.3 per cent (31 December 2009: 10.4 per cent) and a core tier 1 ratio of 8.5 per cent (31 December 2009: 7.0 per cent). Capital resources for the Lloyds TSB Bank Group have increased in the half year to 30 June 2010 mainly due to the issuance of £21,394 million of shares on the transfer of HBOS plc from Lloyds Banking Group plc together with the credit to reserves of £6,348 million arising on consolidation of HBOS plc. Capital has further been strengthened in the period by the issuance of £2 billion of subordinated debt to the market. Capital requirements have increased as a result of the transfer of HBOS plc.

PRINCIPAL RISKS AND UNCERTAINTIES

The principal risks and uncertainties facing the Group in the second half of 2010 are:

Economy

During the first half of 2010, the global economy has continued to recover from the deepest recession in 80 years. The UK economy has grown in line with its long-term average during the first half of 2010, however consumer confidence has fallen back slightly and the recent rise in house prices has stalled. Nevertheless, some key drivers of the Group's performance have continued to perform better than expected, with UK corporate insolvencies falling in the last three quarters of 2009 and, related to that, employment has held up relatively well. Although the Group expects corporate insolvencies to rise slightly further, the failure rate should peak at around just one third the level reached in the 1990's recession, and consequently unemployment may rise slightly but should already be close to its peak. The Group's central scenario is for the modest recovery in the UK to continue – the projection of 1.3 per cent GDP growth in 2010 and just over 2 per cent in 2011 is close to the consensus. However the risks to this scenario are skewed to the downside. The extent to which simultaneous fiscal tightening across Europe might undermine global and UK growth is unclear. A 'double-dip' scenario – a second recession following closely the one that the economy is just emerging from – would result in further significant increases in corporate failures and unemployment into 2011. Residential and commercial property would suffer a second period of falling prices, tenant defaults would increase and central banks would have limited ability to cushion the downturn.

Liquidity and funding

During the first half of 2010 liquidity and funding has remained a key area of focus for the Group and the industry as a whole. The Group's ability to successfully fund its balance sheet is dependent on the continued functioning of the money and capital markets; successful right-sizing of the Lloyds Banking Group balance sheet; the repayment of public facilities by Lloyds Banking Group in accordance with the terms agreed; limited further deterioration in the UK's, Lloyds Banking Group plc's and the Bank's credit ratings and no significant or sudden withdrawal of deposits.

The Group is reliant on both short-term wholesale funding and public and central bank facilities to support its balance sheet. During the first half of 2010, Lloyds Banking Group has chosen to repay a portion of the amounts drawn from these facilities, replacing them with term debt issuance in the public and private markets as the balance sheet is right-sized. A shortening in maturity risk appetite of investors in the second quarter of 2010 has led to reduced short-term money market liquidity, however, Lloyds Banking Group has funded itself successfully with no material change in its short-term maturity profile.

Lloyds Banking Group has also entered into a number of EU state aid related obligations to achieve reductions in certain parts of its balance sheet by the end of 2014. The requirement to meet this deadline may result in Lloyds Banking Group having to provide funding to support these asset reductions and/or disposals which may also result in a lower price being achieved.

PRINCIPAL RISKS AND UNCERTAINTIES (continued)

Credit risk

The Lloyds Banking Group has seen a significant reduction in impairments in the first half of 2010, following the stabilisation of the wholesale portfolios and good retail affordability and performance. Adjusting for the impact of the transfer of HBOS, the Group's total impairment charge levels have reduced in the first half of 2010 compared with both the first half of 2009 and the second half of 2009.

The Group remains cautious about the economic outlook, and in particular a 'double dip' recession is a key downside risk for the UK economy and consequently the Group. Notwithstanding the improved performance in the first half of the year, the Group's wholesale portfolios continue to be closely monitored, with robust and proactive risk management in place to help ensure timely risk mitigating actions. The Group retains some material single obligor concentrations on weaker credits, which are likely to continue to show vulnerability with the potential for increased impairments. Whilst a high percentage of real estate and real estate related investment lending is in the wholesale portfolio, sustainability of cashflow has been key to the relative resilience seen in the investment market to date. However, the portfolio remains sensitive to a rise in tenant defaults which could impact debt service capability. This could be exacerbated by price falls in the secondary and tertiary assets held in the real estate investment lending portfolio.

The Group expects further stress within certain portfolios as domestically focused names suffer the effects of reduced public sector expenditure, tighter working capital requirements and a weak recovery in demand. Under the Group's economic assumptions, 2010 is expected to continue to be difficult for these portfolios. Some early warning signs of asset deterioration are already evident in some portfolios (for example increasing delinquencies and adverse credit risk rating migrations). Refinancing will be a key issue with significant maturities due in the next few years, especially in the Group's real estate and real estate related portfolios as well as for leveraged loans.

Concerns also exist over the outlook for the Eurozone following the Greek crisis and subsequent contagion to Spain, Portugal and Ireland. This adds further uncertainty in asset valuations and could impede asset disposals. However, the Group has limited exposure to the weaker Eurozone economies and is monitoring them closely.

Market risk

Market uncertainty has continued during the first half of 2010. Equity markets have been volatile. Concerns about the scale of deficits in Ireland and southern European countries resulted in increased credit spreads in the areas affected, and fears of contagion impacted the Euro and widened spreads between official and interbank interest rates.

The environment will continue to be uncertain and the Group will continue to take opportunities to reduce exposures where appropriate. During the first half of 2010 Lloyds Banking Group has hedged some of the equity market risk that arises from the life assurance business and continues to carefully manage risks arising from its pension schemes.

PRINCIPAL RISKS AND UNCERTAINTIES (continued)

Legal and regulatory risk

The Financial Services Act 2010 received Royal Assent on 8 April 2010. The Act establishes a new consumer financial education body, amends the Financial Services and Markets Act to provide the FSA with a new financial stability statutory objective, gives the FSA powers to make rules on remuneration arrangements, short selling, living wills, consumer redress schemes, and extends its enforcement powers. In addition, the government has announced plans to give the Bank of England macro- and micro-prudential supervisory powers over UK regulated banks and to create a new Customer Protection and Markets Authority to take over the FSA's conduct of business supervisory role, together with certain other duties from the FSA and other bodies. The Act and the Bank of England's proposed new supervisory powers could have significant ramifications for the FSA's approach to regulating the Group, particularly regarding the setting of capital and liquidity requirements and also conduct of business regulations.

Evolving capital and liquidity requirements continue to be monitored by the Group. In December 2009, the Basel Committee on Banking Supervision proposed a capital and liquidity reform package (Basel III) which would present a number of challenges to the Group. The UK Government has announced that a bank levy will be imposed on large UK banks and foreign banks operating in the UK from 1 January 2011 and has appointed an independent commission to review possible structural reforms to the banking system. The Treasury Select Committee has also announced its intention to conduct an examination of competition in retail banking and the future of free banking. It is too early to quantify the potential impact of these developments on the Group.

The Group may also be subject to legal and regulatory proceedings and Financial Ombudsman and other complaints brought against it in the UK High Court and elsewhere, and in jurisdictions outside the UK. The outcome of any investigation, proceeding or complaint is inherently uncertain.

A number of changes in regulation will come into effect in the short term that will affect the Group including implementation of new reverse stress testing requirements, the 31 December 2010 delivery deadline for the Single Customer View implementation and the EU's proposed changes to bank remuneration rules. The Group may also be subject to increased EU supervisory influence via the Committee of European Banking Supervisors, the Committee of European Insurance and Occupational Pensions Supervisors and the Committee of European Securities Regulators. From 2011 these bodies will become new EU Supervisory Authorities - the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority respectively.

The Group is currently assessing the impacts of these regulatory developments and is working closely with the Tripartite Authorities and industry associations so that it continues to identify and respond to regulatory and legislative changes.

Customer treatment

The FSA continues to drive focus on conduct of business activities and has established a new approach to supervision of Conduct Risk, particularly in relation to retail customers, in which they will seek to place greater emphasis on product governance. The FSA also published its review of Complaints Handling in Banking Groups in April 2010 in which they have identified a number of concerns across the industry and has indicated that they will complete a thematic review on the sale of packaged current accounts in the third quarter of 2010.

PRINCIPAL RISKS AND UNCERTAINTIES (continued)

People

In the first half of 2010, as integration has continued, the Group has proactively managed the relationship with staff. The Group has published revised proposals to harmonise employee terms and conditions across the Group and is consulting with the various representative unions.

State aid

Lloyds Banking Group has made a number of undertakings to HM Treasury regarding both capital and funding support, including additional lending to certain mortgage and business sectors, corporate governance and staff remuneration.

In addition, Lloyds Banking Group is subject to European state aid obligations in line with the restructuring plan agreed with HM Treasury and the EU College of Commissioners in November 2009, which is designed to support the long-term viability of Lloyds Banking Group and address any competition distortions arising from the benefits of state aid.

CONDENSED INTERIM FINANCIAL STATEMENTS (unaudited)

CONSOLIDATED INCOME STATEMENT

	Note	Half-year to 30 June 2010 £ million	Half-year to 30 June 2009 £ million
Interest and similar income		14,825	6,263
Interest and similar expense		(7,730)	(3,092)
Net interest income		7,095	3,171
Fee and commission income		2,221	1,448
Fee and commission expense		(812)	(480)
Net fee and commission income		1,409	968
Net trading income		853	(707)
Insurance premium income		4,300	2,197
Other operating income		1,597	2,119
Other income	3	8,159	4,577
Total income		15,254	7,748
Insurance claims		(3,189)	(1,192)
Total income, net of insurance claims		12,065	6,556
Operating expenses	4	(5,791)	(3,427)
Trading surplus		6,274	3,129
Impairment	5	(5,423)	(2,248)
Share of results of joint ventures and associates		(61)	1
Profit before tax		790	882
Taxation	6	(576)	(43)
Profit for the period		214	839
Profit attributable to non-controlling interests		70	11
Profit attributable to equity shareholders		144	828
Profit for the period		214	839

CONDENSED INTERIM FINANCIAL STATEMENTS (unaudited)**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**

	Half-year to 30 June 2010 £ million	Half-year to 30 June 2009 £ million
Profit for the period	214	839
Other comprehensive income:		
Movements in revaluation reserve in respect of available-for-sale financial assets:		
Change in fair value	1,255	380
Transferred to income statement in respect of disposals	(147)	(7)
Transferred from income statement in respect of impairment	36	57
Other transfers to income statement	(185)	46
Taxation	(357)	(65)
	602	411
Movement in cash flow hedging reserve:		
Effective portion of changes in fair value taken to other comprehensive income	(535)	8
Net transfers to the income statement	312	(33)
Taxation	73	7
	(150)	(18)
Currency translation differences:		
Currency translation differences, before tax	97	582
Taxation	(1)	(383)
	96	199
Other comprehensive income for the period, net of tax	548	592
Total comprehensive income for the period	762	1,431
Total comprehensive income attributable to non-controlling interests	67	6
Total comprehensive income attributable to equity shareholders	695	1,425
Total comprehensive income for the period	762	1,431

CONDENSED INTERIM FINANCIAL STATEMENTS (unaudited)**CONSOLIDATED BALANCE SHEET**

	Note	As at 30 June 2010 £ million	As at 31 Dec 2009 £ million
Assets			
Cash and balances at central banks		53,035	36,089
Items in course of collection from banks		2,007	1,045
Trading and other financial assets at fair value through profit or loss	7	147,519	48,894
Derivative financial instruments		59,921	18,797
Loans and receivables:			
Loans and advances to customers	8	612,133	231,038
Loans and advances to banks		31,251	25,433
Loans and advances to fellow group undertakings		16,725	164,309
Debt securities		28,713	2,636
		688,822	423,416
Available-for-sale financial assets		47,696	26,089
Investment properties		5,215	2,340
Investments in joint ventures and associates		416	56
Goodwill		2,016	2,016
Value of in-force business		6,478	2,403
Other intangible assets		3,728	205
Tangible fixed assets		8,786	4,125
Current tax recoverable		241	85
Deferred tax assets		4,912	2,438
Retirement benefit asset		727	–
Other assets		11,451	4,982
Total assets		1,042,970	572,980

CONDENSED INTERIM FINANCIAL STATEMENTS (unaudited)

CONSOLIDATED BALANCE SHEET (continued)

	Note	As at 30 June 2010 £ million	As at 31 Dec 2009 ⁽¹⁾ £ million
Equity and liabilities			
Liabilities			
Deposits from banks		69,640	53,045
Customer deposits		420,438	174,658
Deposits from fellow group undertakings		20,178	104,899
Items in course of transmission to banks		1,148	542
Trading and other financial liabilities at fair value through profit or loss		29,384	6,362
Derivative financial instruments		51,695	16,733
Notes in circulation		999	—
Debt securities in issue	11	221,801	120,719
Liabilities arising from insurance contracts and participating investment contracts		74,962	36,960
Liabilities arising from non-participating investment contracts		45,314	15,734
Unallocated surplus within insurance businesses		928	310
Other liabilities		27,855	12,263
Retirement benefit obligations		424	474
Current tax liabilities		57	22
Deferred tax liabilities		195	—
Other provisions		885	547
Subordinated liabilities	12	32,088	15,999
Total liabilities		997,991	559,267
Equity			
Share capital	13	1,571	1,547
Share premium account	14	32,164	8,555
Other reserves	14	5,557	(1,342)
Retained profits	14	4,804	4,660
Shareholders' equity		44,096	13,420
Non-controlling interests		883	293
Total equity		44,979	13,713
Total equity and liabilities		1,042,970	572,980

⁽¹⁾ Restated – see note 2.

CONDENSED INTERIM FINANCIAL STATEMENTS (unaudited)**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**

	Attributable to equity shareholders				Non-controlling interests	Total
	Share capital and premium £ million	Other reserves £ million	Retained profits £ million	Total £ million	£ million	£ million
Balance at 1 January 2009:						
As previously stated	4,502	(2,824)	7,588	9,266	306	9,572
Prior year adjustment (note 2)	–	131	(131)	–	–	–
Restated	4,502	(2,693)	7,457	9,266	306	9,572
Total comprehensive income	–	597	828	1,425	6	1,431
Other movements in non-controlling interests	–	–	–	–	(1)	(1)
Balance at 30 June 2009	4,502	(2,096)	8,285	10,691	311	11,002
Total comprehensive income	–	754	(3,625)	(2,871)	(1)	(2,872)
Capital injection	5,600	–	–	5,600	–	5,600
Dividends	–	–	–	–	(18)	(18)
Other movements in non-controlling interests	–	–	–	–	1	1
Balance at 31 December 2009	10,102	(1,342)	4,660	13,420	293	13,713
Total comprehensive income	–	551	144	695	67	762
Dividends	–	–	–	–	(8)	(8)
Issue of ordinary shares:						
On transfer of HBOS (note 18)	21,394	–	–	21,394	–	21,394
Other	2,239	–	–	2,239	–	2,239
Reserve arising on transfer of HBOS	–	6,348	–	6,348	–	6,348
Adjustment on acquisition	–	–	–	–	1,271	1,271
Extinguishment of non-controlling interests	–	–	–	–	(735)	(735)
Repayment of capital to non-controlling interests	–	–	–	–	(5)	(5)
Balance as at 30 June 2010	33,735	5,557	4,804	44,096	883	44,979

CONDENSED INTERIM FINANCIAL STATEMENTS (unaudited)

CONSOLIDATED CASH FLOW STATEMENT

	Half-year to 30 June 2010 £ million	Half-year to 30 June 2009 £ million
Profit before tax	790	882
Adjustments for:		
Change in operating assets	8,073	(57,735)
Change in operating liabilities	(5,677)	68,491
Non-cash and other items	2,255	892
Tax (paid) received	(143)	4
Net cash provided by operating activities	5,298	12,534
Cash flows from investing activities		
Purchase of available-for-sale financial assets	(17,521)	(425,243)
Proceeds from sale and maturity of available-for-sale financial assets	18,555	460,009
Purchase of fixed assets	(1,812)	(568)
Proceeds from sale of fixed assets	1,667	310
Acquisition of businesses, net of cash acquired	9,077	(15)
Disposal of businesses, net of cash disposed	239	—
Net cash provided by investing activities	10,205	34,493
Cash flows from financing activities		
Dividends paid to non-controlling interests	(8)	—
Interest paid on subordinated liabilities	(945)	(579)
Proceeds from issue of subordinated liabilities	1,968	—
Repayment of subordinated liabilities	—	(486)
Repayment of capital to non-controlling interests	(5)	(1)
Net cash provided by (used in) financing activities	1,010	(1,066)
Effects of exchange rate changes on cash and cash equivalents	181	(335)
Change in cash and cash equivalents	16,694	45,626
Cash and cash equivalents at beginning of period	62,785	32,760
Cash and cash equivalents at end of period	79,479	78,386

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

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1. Basis of preparation

The Directors consider that it is appropriate to continue to adopt the going concern basis in preparing the condensed interim financial statements. In reaching this assessment, the directors have considered projections for the Group's capital and funding position and have had regard to the factors set out in Principal Risks and Uncertainties: Liquidity and funding on page 3.

As explained in note 18, Lloyds Banking Group plc transferred its investment in HBOS plc to Lloyds TSB Bank plc on 1 January 2010. In accordance with the accounting treatment available under IFRS 3 (Revised) for business combinations involving entities under common control, Lloyds TSB Bank plc was not required to fair value the acquired business at the date of transfer. Instead, the assets and liabilities were incorporated at the amounts at which they were recorded within Lloyds Banking Group at that date. The difference between the consolidated net asset value of HBOS plc at the date of transfer and the consideration paid, which was equal to Lloyds Banking Group plc's original cost of investment, has been credited to a merger reserve.

2. Accounting policies, presentation and estimates

These condensed interim financial statements as at and for the half-year to 30 June 2010 have been prepared in accordance with the Disclosure and Transparency Rules of the Financial Services Authority and with International Accounting Standard (IAS) 34 *Interim Financial Reporting*, as adopted by the European Union. They do not include all of the information required for full annual financial statements and should be read in conjunction with the Group's consolidated financial statements as at and for the year ended 31 December 2009 which were prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. Copies of the 2009 annual report and accounts can be found on the Lloyds Banking Group's website, www.lloydsbankinggroup.com, or are available upon request from Group Secretariat, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN.

Accounting policies

The accounting policies are consistent with those applied by the Group in its 2009 annual report and accounts, except as described below.

During 2010, the International Financial Reporting Interpretations Committee clarified the treatment of amounts previously recognised in equity in respect of assets that were transferred from the available-for-sale category to the loans and receivables category. When an impairment loss is recognised in respect of such transferred financial assets, the unamortised balance of any available-for-sale reserve that remains in equity should be transferred to the income statement and recorded as part of the impairment loss.

The Group has changed its accounting policy to reflect this clarification. Under the Group's previous accounting policy, when such a transferred financial asset became impaired, not all of the unamortised amounts previously transferred to equity were recycled to the income statement and therefore continued to be accreted over the expected remaining life of the financial asset. The change is applied retrospectively and the effect has been to reduce retained profits and increase available-for-sale reserves by £131 million at 1 January 2009; shareholders' equity is unchanged. There was no material effect on the Group's income statement in the first half of 2010 or in the first half or second half of 2009.

In accordance with IAS 34, the Group's income tax expense for the six months ended 30 June 2010 is based on the best estimate of the weighted-average annual income tax rate expected for the full financial year. This best estimate does not take into account the impact of changes announced in the June 2010 UK Budget which were not substantively enacted by 30 June 2010.

2. Accounting policies, presentation and estimates (continued)

In accordance with IAS 19 *Employee Benefits* and the Group's normal practice, the valuation of the Group's pension schemes will be formally updated at the year end. During the first half of 2010, the Group's defined benefit pension obligation was adjusted to reflect the effect of the change in the terms of the Group's pension schemes (see note 4). However, no valuation adjustment has been made to the Group's retirement benefit assets and liabilities at 30 June 2010.

The preparation of interim financial statements requires management to make judgements, estimates and assumptions that impact the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Due to the inherent uncertainty in making estimates, actual results reported in future periods may be based upon amounts which differ from those estimates. Estimates, judgements and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. There have been no significant changes in the basis upon which estimates have been determined, compared to those applied at 31 December 2009.

New accounting pronouncements

The Group has adopted the following new standards and amendments to standards which became effective for financial years beginning on or after 1 January 2010. None of these standards or amendments have had a material impact on these condensed interim financial statements.

- (i) IFRS 3 *Business Combinations*. The revised standard continues to require the use of the acquisition method of accounting for business combinations. All payments to purchase a business are to be recorded at fair value at the acquisition date, some contingent payments are subsequently remeasured at fair value through income, goodwill may be calculated based on the parent's share of net assets or it may include goodwill related to the non-controlling interest, and all transaction costs are expensed.
- (ii) IAS 27 *Consolidated and Separate Financial Statements*. Requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control; any remaining interest in an investee is re-measured to fair value in determining the gain or loss recognised in profit or loss where control over the investee is lost.
- (iii) IFRIC 17 *Distributions of Non-cash Assets to Owners*. Provides accounting guidance for non-reciprocal distributions of non-cash assets to owners (and those in which owners may elect to receive a cash alternative).
- (iv) Amendment to IAS 39 *Financial Instruments: Recognition and Measurement* – 'Eligible Hedged Items'. Clarifies how the principles underlying hedge accounting should be applied in particular situations.
- (v) *Improvements to IFRSs* (issued April 2009). Sets out minor amendments to IFRS standards as part of the annual improvements process.

Future accounting developments

The following pronouncements will be relevant to the Group but are not applicable for the year ending 31 December 2010 and have not been applied in preparing these condensed interim financial statements. The full impact of these accounting changes is currently being assessed by the Group.

2. Accounting policies, presentation and estimates (continued)

- (i) IFRS 9 *Financial Instruments*. Replaces those parts of IAS 39 *Financial Instruments: Recognition and Measurement* dealing with the classification and measurement of financial assets. Requires financial assets to be classified into two measurement categories, fair value and amortised cost, on the basis of the objectives of the entity's business model for managing its financial assets and the contractual cash flow characteristics of the instrument. Available-for-sale financial asset and held-to-maturity categories in the existing IAS 39 will be eliminated.

IFRS 9 is the initial stage of the project to replace IAS 39. Future stages are expected to result in amendments to IFRS 9 to deal with changes to the classification and measurement of financial liabilities, impairment of financial assets measured at amortised cost and hedge accounting. Until all stages of the replacement project are complete, it is not possible to determine the overall impact on the financial statements of the replacement of IAS 39. The effective date of the standard is annual periods beginning on or after 1 January 2013.

- (ii) Amendment to IAS 32 *Financial instruments: Presentation – 'Classification of Rights Issues'*. Requires rights issues denominated in a currency other than the functional currency of the issuer to be classified as equity regardless of the currency in which the exercise price is denominated. The amendment is effective for annual periods beginning on or after 1 February 2010.
- (iii) IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*. Clarifies that when an entity renegotiates the terms of its debt with the result that the liability is extinguished by the debtor issuing its own equity instruments to the creditor, a gain or loss is recognised in the income statement representing the difference between the carrying value of the financial liability and the fair value of the equity instruments issued; the fair value of the financial liability is used to measure the gain or loss where the fair value of the equity instruments cannot be reliably measured. The interpretation is effective for annual periods beginning on or after 1 July 2010 and is consistent with the Group's existing accounting policy.
- (iv) *Improvements to IFRSs* (issued May 2010). Sets out minor amendments to IFRS standards as part of the annual improvements process. The effective dates vary on a standard by standard basis but none are effective any earlier than annual periods beginning on or after 1 July 2010.
- (v) Amendment to IFRIC 14 *Prepayments of a Minimum Funding Requirement*. Applies when an entity is subject to minimum funding requirements and makes an early payment of contributions to cover those requirements and permits such an entity to treat the benefit of such an early payment as an asset. The amendment is effective for annual periods beginning on or after 1 January 2011.
- (vi) IAS 24 *Related Party Disclosures*. The revised standard simplifies the definition of a related party and provides a partial exemption from the disclosure requirements for government related entities. The revised standard is effective for annual periods beginning on or after 1 January 2011.

At the date of this report, IFRS 9 and Improvements to IFRSs (issued May 2010) are awaiting EU endorsement.

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

2. Accounting policies, presentation and estimates (continued)*Other matters*

No significant events, other than those disclosed within this document, have occurred between 30 June 2010 and the date of approval of these condensed interim financial statements.

3. Other income

	Half-year to 30 June 2010 £m	Half-year to 30 June 2009 £m
Fee and commission income:		
Current account fees	506	383
Credit and debit card fees	407	277
Other fees and commissions	1,308	788
	2,221	1,448
Fee and commission expense	(812)	(480)
Net fee and commission income	1,409	968
Net trading income	853	(707)
Insurance premium income	4,300	2,197
Gains on capital transactions	176	1,775
Other	1,421	344
Other operating income	1,597	2,119
Total other income	8,159	4,577

During 2010 and 2009, as part of the Lloyds Banking Group's management of capital, the Group exchanged certain existing subordinated debt securities for new securities; these exchanges resulted in a gain on extinguishment of the existing liabilities of £176 million (half-year to 30 June 2009: £1,775 million), being the difference between the carrying amount of the securities extinguished and the fair value of the new securities issued together with related fees and costs.

4. Operating expenses

	Half-year to 30 June 2010 £m	Half-year to 30 June 2009 £m
Administrative expenses:		
Staff costs excluding curtailment gain	3,221	1,703
Curtailment gain ⁽¹⁾	(1,019)	–
Total staff costs	2,202	1,703
Premises and equipment	583	350
Other expenses	1,584	777
	4,369	2,830
Depreciation and amortisation	1,220	357
Impairment of tangible fixed assets	202	–
Impairment of intangible assets	–	240
Total operating expenses	5,791	3,427
Comprising:		
Integration costs ⁽²⁾	804	210
Other operating expenses	4,987	3,217
Total operating expenses	5,791	3,427

⁽¹⁾ During the first half of 2010, the Group implemented a change to the terms of its principal UK defined benefit pension schemes. As a result of this change all future increases to pensionable salary will be capped each year at the lower of: Retail Prices Index inflation; each employee's actual percentage increase in pay; and 2 per cent of pensionable pay. The effect of this change was to reduce the Group's retirement benefit obligations recognised on the balance sheet by £1,019 million with a corresponding curtailment gain recognised in the income statement.

⁽²⁾ Costs incurred in relation to the integration of the Lloyds TSB and HBOS businesses following the acquisition of HBOS by the Lloyds Banking Group in January 2009; these costs in the half-year to 30 June 2010 include £52 million in respect of impairment of tangible fixed assets.

5. Impairment

	Half-year to 30 June 2010 £m	Half-year to 30 June 2009 £m
Impairment losses on:		
Loans and advances to customers	5,378	2,112
Loans and advances to banks	(6)	14
Debt securities classified as loans and receivables	9	78
Impairment losses on loans and receivables (note 9)	5,381	2,204
Impairment of available-for-sale financial assets	45	40
Other credit risk provisions	(3)	4
Total impairment charged to the income statement	5,423	2,248

6. Taxation

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

	Half-year to 30 June 2010 £m	Half-year to 30 June 2009 £m
Profit before tax	790	882
Tax charge thereon at UK corporation tax rate of 28% (2009: 28%)	(221)	(247)
Factors affecting charge:		
Goodwill impairment	–	(67)
Disallowed and non-taxable items	39	157
Overseas tax rate differences	(267)	(9)
Gains exempted or covered by capital losses	22	3
Policyholder interests	(8)	134
Tax losses where no deferred tax provided	(119)	–
Adjustments in respect of previous years	32	(14)
Effect of profit (loss) in joint ventures and associates	(17)	–
Other items	(37)	–
Tax charge	(576)	(43)

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

	As at 30 June 2010 £m	As at 31 Dec 2009 £m
Trading assets	26,486	510
Other financial assets at fair value through profit or loss:		
Loans and advances to customers	139	166
Debt securities	42,685	20,361
Equity shares	78,209	27,857
	121,033	48,384
	147,519	48,894

Included in the above is £117,363 million (2009: £44,843 million) relating to the insurance business.

8. Loans and advances to customers

	As at 30 June 2010 £m	As at 31 Dec 2009 £m
Agriculture, forestry and fishing	5,566	4,457
Energy and water supply	3,306	2,085
Manufacturing	13,227	8,807
Construction	10,354	2,842
Transport, distribution and hotels	34,439	12,280
Postal and communications	1,632	833
Property companies	80,452	23,110
Financial, business and other services	65,646	32,889
Personal:		
Mortgages	360,000	115,349
Other	37,139	23,658
Lease financing	8,905	4,317
Hire purchase	8,155	5,224
	628,821	235,851
Allowance for impairment losses on loans and advances (note 9)	(16,688)	(4,813)
Total loans and advances to customers	612,133	231,038

Loans and advances to customers include advances securitised under the Group's securitisation and covered bond programmes. Further details are given in note 10.

9. Allowance for impairment losses on loans and receivables

	Half-year to 30 June 2010 £m	Year ended 31 Dec 2009 £m
Balance at 1 January	5,207	3,727
Adjustment on transfer of HBOS	10,173	–
Exchange and other adjustments	(97)	4
Advances written off	(3,406)	(2,896)
Recoveries of advances written off in previous years	86	110
Unwinding of discount	(128)	(91)
Charge for the half-year to 30 June (note 5)	5,381	2,204
Charge for the half-year to 31 December		2,149
Charge to the income statement	5,381	4,353
Balance at end of period	17,216	5,207
In respect of:		
Loans and advances to customers (note 8)	16,688	4,813
Loans and advances to banks	94	149
Debt securities	434	245
Balance at end of period	17,216	5,207

10. Securitisations and covered bonds

The Group's principal securitisation and covered bond programmes, together with the balances of the loans subject to securitisation and the carrying value of the notes in issue at 30 June 2010, are listed below.

	As at 30 June 2010		As at 31 December 2009	
	Gross assets securitised £m	Notes in issue £m	Gross assets securitised £m	Notes in issue £m
<i>Securitisation programmes</i>				
UK residential mortgages	150,061	118,608	49,390	36,470
Commercial loans	12,580	8,077	12,173	7,479
Irish residential mortgages	5,826	6,008	—	—
Credit card receivables	4,861	2,168	—	—
Dutch residential mortgages	4,232	4,239	—	—
Personal loans	3,327	2,613	—	—
PPP/PFI and project finance loans ⁽¹⁾	898	42	877	45
Corporate banking loans and revolving credit facilities ⁽¹⁾	—	3	595	7
Motor vehicle loans	338	361	—	—
	182,123	142,119	63,035	44,001
Less held by the Group		(104,589)		(37,438)
Total securitisation programmes (note 11)		37,530		6,563
<i>Covered bond programmes</i>				
Residential mortgage-backed	97,559	75,693	38,753	29,000
Social housing loan-backed	3,286	2,249	—	—
	100,845	77,942	38,753	29,000
Less held by the Group		(49,655)		(29,000)
Total covered bond programmes (note 11)		28,287		—
Total securitisation and covered bond programmes		65,817		6,563

Securitisation programmes

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

Covered bond programmes

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

Cash deposits of £31,853 million (31 December 2009: £7,209 million) held by the Group are restricted in use to repayment of the debt securities issued by the SPEs and other legal obligations.

11. Debt securities in issue

	As at 30 June 2010 £m	As at 31 Dec 2009 £m
Certificates of deposit	40,186	44,508
Medium-term notes issued	83,150	47,786
Covered bonds (note 10)	28,287	–
Commercial paper	32,648	21,862
Securitisation notes (note 10)	37,530	6,563
	<u>221,801</u>	<u>120,719</u>

12. Subordinated liabilities

The movement in subordinated liabilities during the period was as follows:

	Half-year to 30 June 2010 £m
At 1 January 2010	15,999
Adjustment on transfer of HBOS	14,686
Issued during the period	1,968
Repurchases and redemptions during the period	(1,759)
Foreign exchange and other movements	1,194
At 30 June 2010	<u>32,088</u>

13. Share capital

Movements in ordinary share capital were as follows:

	Half-year to 30 June 2010 Number of shares (millions)	Half-year to 30 June 2010 £m
Ordinary shares of £1 each		
At 1 January 2010	1,547	1,547
Issued on transfer of HBOS ⁽¹⁾	21	21
Issued in respect of exchange offers ⁽²⁾	3	3
At 30 June 2010	<u>1,571</u>	<u>1,571</u>

⁽¹⁾ On 1 January 2010 the Bank issued 21 million shares for a total value of £21,394 million in consideration for the transfer of Lloyds Banking Group plc's investment in HBOS plc.

⁽²⁾ During March and April 2010, a total of 3 million shares were issued in exchange for the redemption of capital securities issued by the Bank for an aggregate consideration of £2,239 million.

14. Reserves

	Share premium £m	Other reserves			Total £m	Retained profits £m
		Available- for-sale £m	Cash flow hedging £m	Merger and other £m		
At 1 January 2010:						
As previously stated	8,555	(1,572)	(30)	129	(1,473)	4,791
Prior year adjustment ⁽¹⁾	–	131	–	–	131	(131)
Restated	8,555	(1,441)	(30)	129	(1,342)	4,660
Shares issued in period	2,236	–	–	–	–	–
Issue of ordinary shares on transfer of HBOS	21,373	–	–	–	–	–
Reserve arising on transfer of HBOS	–	–	–	6,348	6,348	–
Profit for the period	–	–	–	–	–	144
Change in fair value of available-for-sale assets (net of tax)	–	808	–	–	808	–
Change in fair value of hedging derivatives (net of tax)	–	–	(388)	–	(388)	–
Transfers to income statement (net of tax)	–	(203)	238	–	35	–
Exchange and other adjustments	–	–	–	96	96	–
At 30 June 2010	32,164	(836)	(180)	6,573	5,557	4,804

⁽¹⁾ See note 2.**15. Contingent liabilities and commitments**

	As at 30 June 2010 £m	As at 31 Dec 2009 £m
Contingent liabilities		
Acceptances and endorsements	60	53
Other:		
Other items serving as direct credit substitutes	1,430	1,395
Performance bonds and other transaction-related contingencies	2,892	3,292
	4,322	4,687
Total contingent liabilities	4,382	4,740
Commitments		
Documentary credits and other short-term trade related transactions	420	219
Forward asset purchases and forward deposits placed	918	758
Undrawn formal standby facilities, credit lines and other commitments to lend:		
Less than 1 year original maturity:		
Mortgage offers	9,256	1,302
Other commitments	61,155	36,206
	70,411	37,508
1 year or over original maturity	47,729	36,020
Total commitments	119,478	74,505

16. Capital ratios

	As at 30 June 2010 £m	As at 31 Dec 2009 ⁽¹⁾ £m
Capital resources		
Core tier 1		
Ordinary share capital and reserves	45,019	13,753
Regulatory post-retirement benefit adjustments	(912)	249
Available-for-sale revaluation reserve and cash flow hedging reserve	1,016	1,471
Other items	289	(1)
	<u>45,412</u>	<u>15,472</u>
Deductions from core tier 1		
Goodwill and other intangible assets	(5,491)	(2,127)
Excess expected loss	(164)	(838)
Other deductions	(209)	(215)
	<u>39,548</u>	<u>12,292</u>
Core tier 1 capital		
	<u>39,548</u>	<u>12,292</u>
Perpetual non-cumulative preference shares		
Preference share capital	1,854	3,030
Innovative tier 1		
Preferred securities	6,155	4,928
Less: restriction in amount eligible	–	(2,097)
	<u>6,155</u>	<u>2,831</u>
Total tier 1 capital	<u>47,557</u>	<u>18,153</u>
Tier 2		
Available-for-sale revaluation reserve in respect of equities	374	6
Undated subordinated debt	4,343	1,914
Innovative capital restricted from tier 1	–	2,097
Eligible provisions	1,775	25
	<u>6,492</u>	<u>4,042</u>
Lower tier 2		
Dated subordinated debt	15,231	4,711
	<u>15,231</u>	<u>4,711</u>
Deductions from tier 2		
Excess expected loss	(164)	(838)
Other deductions	(209)	(215)
	<u>(373)</u>	<u>(1,053)</u>
Total tier 2 capital	<u>15,231</u>	<u>4,711</u>
Supervisory deductions		
Unconsolidated investments – life	(9,333)	(4,586)
– other	(1,256)	(596)
	<u>(10,589)</u>	<u>(5,182)</u>
Total supervisory deductions	<u>(10,589)</u>	<u>(5,182)</u>
Total capital resources	<u>58,318</u>	<u>20,671</u>
Risk-weighted assets⁽²⁾	463,196	174,472
Core tier 1 ratio⁽²⁾	8.5%	7.0%
Tier 1 capital ratio⁽²⁾	10.3%	10.4%
Total capital ratio⁽²⁾	12.6%	11.8%

⁽¹⁾ Restated to reflect a prior year adjustment to available-for-sale revaluation reserves (see note 2).

⁽²⁾ Outside the scope of PricewaterhouseCoopers LLP's independent review report.

17. Legal and regulatory matters

Interchange fees

The European Commission has adopted a formal decision finding that an infringement of European Commission competition laws has arisen from arrangements whereby MasterCard issuers charged a uniform fallback interchange fee in respect of cross border transactions in relation to the use of a MasterCard or Maestro branded payment card. The European Commission has required that the fee be reduced to zero for relevant cross-border transactions within the European Economic Area. This decision has been appealed to the General Court of the European Union (the General Court). Lloyds TSB Bank plc and Bank of Scotland plc (along with certain other MasterCard issuers) have successfully applied to intervene in the appeal in support of MasterCard's position that the arrangements for the charging of a uniform fallback interchange fee are compatible with European Commission competition laws. MasterCard has announced that it has reached an understanding with the European Commission on a new methodology for calculating intra European Economic Area multi-lateral interchange fees on an interim basis pending the outcome of the appeal. Meanwhile, the European Commission and the UK's Office of Fair Trading (OFT) are pursuing investigations with a view to deciding whether arrangements adopted by other payment card schemes for the levying of uniform fallback interchange fees in respect of domestic and/or cross-border payment transactions also infringe European Commission and/or UK competition laws. As part of this initiative, the OFT will also intervene in the General Court appeal supporting the European Commission position and Visa reached an agreement with the European Commission to reduce the level of interchange for cross-border debit card transactions to the interim levels agreed by MasterCard. The ultimate impact of the investigations on the Group can only be known at the conclusion of these investigations and any relevant appeal proceedings.

Unarranged overdraft charges

In April 2007, the OFT commenced an investigation into the fairness of personal current accounts and unarranged overdraft charges. At the same time, it commenced a market study into wider questions about competition and price transparency in the provision of personal current accounts.

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

The OFT however continued to discuss its concerns in relation to the personal current account market with the banks, consumer groups and other organisations under the auspices of its Market Study into personal current accounts. In October 2009, the OFT published voluntary initiatives agreed with the industry and consumer groups to improve transparency of the costs and benefits of personal current accounts and improvements to the switching process. On 16 March 2010 the OFT published a further update announcing several further voluntary industry wide initiatives to improve a customer's ability to control whether they used an unarranged overdraft and to assist those in financial difficulty. However, in light of the progress it noted in the unarranged overdraft market since July 2007 and the progress it expects to see over the next two years, it has decided to take no further action at this time and will review the unarranged overdraft market again in 2012.

17. Legal and regulatory matters (continued)

US sanctions

In January 2009 Lloyds TSB Bank plc announced the settlement it had reached with the US Department of Justice and the New York County District Attorney's Office in relation to their investigations into historic US dollar payment practices involving countries, persons or entities subject to the economic sanctions administered by the US Office of Foreign Assets Control (OFAC). On 22 December 2009 OFAC announced the settlement it had reached with Lloyds TSB Bank plc in relation to its investigation and confirmed that the settlement sum due to OFAC had been fully satisfied by Lloyds TSB Bank plc's payment to the Department of Justice and the New York District Attorney's Office. No further enforcement actions are expected in relation to the matters set out in the settlement agreements.

On 26 February 2009, a purported shareholder filed a derivative civil action in the Supreme Court of New York, Nassau County against certain current and former directors, and nominally against Lloyds TSB Bank plc and Lloyds Banking Group plc, seeking various forms of relief. The derivative action is at an early stage, but the ultimate outcome of the action is not expected to have a material impact on the Group.

Payment protection insurance

In January 2009, the UK Competition Commission (Competition Commission) completed its formal investigation into the supply of Payment Protection Insurance (PPI) services (except store card PPI) to non-business customers in the UK and published its final report setting out its remedies including a prohibition on the active sale of PPI by a distributor to a customer within seven days of the distributor's sale of credit to that customer. Prior to this the Group had made the commercial decision to sell only regular monthly premium PPI to its personal loan customers. Recently the Group ceased to offer PPI products to customers although some existing applications will be honoured for a limited period.

On 16 October 2009, the Competition Appeal Tribunal referred the proposed prohibition back to the Competition Commission. On 14 May 2010, the Competition Commission published its provisional decision retaining in almost all material aspects the proposed point of sale prohibition. A final decision is expected in due course and Lloyds Banking Group continues to liaise with the Competition Commission on this issue.

On 1 July 2008, the Financial Ombudsman Service referred concerns regarding the handling of PPI complaints to the FSA as an issue of wider implication. The Group has been working with other industry members and trade associations in preparing an industry response to address regulatory concerns regarding the handling of PPI complaints.

On 29 September 2009, the FSA issued a consultation paper on PPI complaints handling. The FSA has escalated its regulatory activity in relation to past PPI sales generally and has proposed new guidance on the fair assessment of a complaint and the calculation of redress and a new rule requiring firms to reassess historically rejected complaints. On 9 March 2010, the FSA issued a further consultation paper on this area, the consultation period for which closed on 22 April (the Group has responded to this consultation). The FSA's proposals are materially the same, although it has placed the new rule requiring firms to reassess historically rejected claims on hold for the present. The ultimate impact on the Group of the FSA's complaints handling proposals can only be known on the publication of the FSA's final rules.

17. Legal and regulatory matters (continued)

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

Other legal actions

In the ordinary course of its business, the Group is engaged in discussions with the FSA in relation to a range of conduct of business matters, especially in relation to retail products including packaged bank accounts, mortgages, structured products and pensions. The Group is keen to ensure that any regulatory concerns regarding product governance or contract terms are understood and addressed. The ultimate impact on the Group of these discussions can only be known at the conclusion of such discussions.

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

18. Acquisition of HBOS plc

On 1 January 2010, as part of a restructuring of the Lloyds Banking Group, Lloyds Banking Group plc's investment in 100 per cent of the ordinary share capital of HBOS plc was transferred to Lloyds TSB Bank plc for a consideration of £21,394 million. The consideration was satisfied by the issue of 21.4 million ordinary shares in Lloyds TSB Bank plc to Lloyds Banking Group plc.

19. Related party transactions

There have been no material changes to the related party transaction during the interim period under review.

There were no material transactions between the Group and HM Treasury during the half-year ended 30 June 2010 that were not made in the ordinary course of business or that are unusual in their nature or conditions.

20. June 2010 Budget statement

A number of the measures announced in the UK Government's June 2010 Budget statement will affect the Group.

The Finance (No. 2) Act 2010 includes legislation to reduce the main rate of corporation tax from 28 per cent to 27 per cent with effect from 1 April 2011. The legislation was substantively enacted in July 2010 and as a result it is expected that the Group's deferred tax asset will reduce by approximately £110 million in the second half of the year, resulting in an estimated charge to the income statement of approximately £80 million and a charge to other comprehensive income of approximately £30 million. In addition, following the triggering of relevant tax variation clauses, the reduction in future rental income within the Group's leasing business will result in an additional charge to the income statement which is not expected to be material.

The proposed further reductions in the rate of corporation tax by 1 per cent per annum to 24 per cent by 1 April 2014 are expected to be enacted separately each year starting in 2011. The effect of these further changes upon the Group's deferred tax balances and leasing business cannot be reliably quantified at this stage.

The Government also announced its intention to introduce a bank levy from 1 January 2011. HM Treasury has commenced a consultation to seek views on the detailed implementation of the bank levy prior to drafting legislation to effect the proposed change. At this stage in the process it is not possible to quantify reliably the impact of the introduction of the bank levy upon the Group.

21. Events after the balance sheet date

On 5 July 2010, Lloyds Banking Group plc announced, subject to regulatory approval and certain other conditions, the sale of a portfolio of private equity investments held by the Bank of Scotland Integrated Finance business to a new joint venture. The Group will retain an interest in the private equity investments through a holding of approximately 30 per cent in the joint venture vehicle. The sale is expected to complete in the third quarter of 2010 and values the portfolio at a small premium to the current book value. The impact of the sale on the Group's results is not expected to be material.

22. Ultimate parent undertaking

The Bank's ultimate parent undertaking and controlling party is Lloyds Banking Group plc which is incorporated in Scotland. Lloyds Banking Group plc has published consolidated accounts for the year ended 31 December 2009 and copies may be obtained from Group Secretariat, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN or downloaded via www.lloydsbankinggroup.com.

23. Other information

The financial information included in this news release does not constitute statutory accounts within the meaning of section 434 of the Companies Act 2006. Statutory accounts for the year ended 31 December 2009 were approved by the directors on 25 February 2010 and were delivered to the Registrar of Companies following publication on 27 March 2010. The auditors' report on these accounts was unqualified, did not contain an emphasis of matter paragraph and did not include any statements under section 498 of the Companies Act 2006.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors listed below (being all the directors of Lloyds TSB Bank plc) confirm that to the best of their knowledge these condensed interim financial statements have been prepared in accordance with International Accounting Standard 34, Interim Financial Reporting, as adopted by the European Union. The interim management report includes a fair review of the information required by DTR 4.2.7R, namely:

- an indication of important events that have occurred during the six months ended 30 June 2010 and their impact on the condensed interim financial statements, and a description of the principal risks and uncertainties for the remaining six months of the financial year.

Signed on behalf of the board by

J Eric Daniels
Chief Executive
3 August 2010

Lloyds TSB Bank plc board of directors:

Sir Winfried Bischoff (Chairman)
J Eric Daniels (Chief Executive)
Tim J W Tookey (Finance Director)
Sir Julian Horn-Smith
Archie G Kane
Lord Leitch
Glen R Moreno
David L Roberts
T Timothy Ryan, Jr
Martin A Scicluna
G Truett Tate
Anthony Watson
Helen A Weir

INDEPENDENT REVIEW REPORT TO LLOYDS TSB BANK PLC

Introduction

We have been engaged by the Company to review the condensed interim financial statements in the interim management report for the six months ended 30 June 2010, which comprises the consolidated income statement, consolidated statement of comprehensive income, consolidated balance sheet, consolidated statement of changes in equity, consolidated cash flow statement and related notes. We have read the other information contained in the interim management report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed interim financial statements.

Directors' responsibilities

The interim management report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the interim management report in accordance with the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

As disclosed in note 2, the annual financial statements of the Group are prepared in accordance with International Financial Reporting Standards as adopted by the European Union. The condensed interim financial statements included in the interim management report have been prepared in accordance with International Accounting Standard 34, 'Interim Financial Reporting', as adopted by the European Union.

Our responsibility

Our responsibility is to express to the Company a conclusion on the condensed interim financial statements in the interim management report based on our review. This report, including the conclusion, has been prepared for and only for the Company for the purpose of the Disclosure and Transparency Rules of the Financial Services Authority and for no other purpose. We do not, in producing this report, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity' issued by the Auditing Practices Board for use in the United Kingdom. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

INDEPENDENT REVIEW REPORT TO LLOYDS TSB BANK PLC (continued)

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the condensed interim financial statements in the interim management report for the six months ended 30 June 2010 are not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom's Financial Services Authority.

PricewaterhouseCoopers LLP
Chartered Accountants
Edinburgh
3 August 2010

Notes:

- (a) The maintenance and integrity of the Lloyds Banking Group website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- (b) Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

CONTACTS

For further information please contact:

INVESTORS AND ANALYSTS

Kate O'Neill
Managing Director, Investor Relations
020 7356 3520
email: kate.o'neill@ltsb-finance.co.uk

Michael Oliver
Director of Investor Relations
020 7356 2167
email: michael.oliver@ltsb-finance.co.uk

MEDIA

Brigitte Trafford
Group Communications Director
020 7356 1008
email: brigitte.trafford@lloydsbanking.com

Mark Elliott
Head of Media, City
020 7356 2493
email: mark.elliott2@lloydsbanking.com