Annual Report and Accounts 2011

www.newcastle.co.uk

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Newcastle
Building Society

Serving our members for over 150 years

CONTENT

OUR VISION

We aim to be an organisation that is friendly, caring and one that values customer loyalty and delivers outstanding customer service. We want to provide secure and rewarding employment to our staff and give recognisable support to the local communities in which we operate. We also aim to provide best in class service for our Solutions business customers.

We acknowledge our members, customers, employees and the communities we serve all have an important part to play in the future of the Society. We believe we can best serve the interests of all stakeholders by remaining a strong, dynamic and independent mutual building society.

Our objectives for each are:

OUR MEMBERS AND CUSTOMERS

- To provide a good range of savings, investment, mortgage and insurance products;
- To provide value for money;
- To be a customer-focused organisation which understands its customers, listens to and acts on what they say;
- To offer expert and trusted advice across a range of services;
- To strive to deliver exceptional service in a prompt, courteous, professional and efficient manner;
- To be straightforward in what we do while being efficient and effective;
- To take personal ownership and care about what we deliver;
- To treat customers fairly and in a way that is consistent with mutuality; and
- To provide a diversified income stream through our savings management Solutions business by sharing our technology and innovation with business partners.

OUR EMPLOYEES

- To provide secure and rewarding long term employment;
- To provide further development of our key resource, our staff;
- To provide our staff with a thorough understanding of our corporate strategy to enable them to pursue it with commitment and passion;
- To be open and honest and do what we say we will do;
- To respect our employees and endeavour to produce an environment of mutual trust and understanding; and
- To provide competitive and fair remuneration packages.

OUR COMMUNITIES

- To be seen to be a major contributor to the economic wellbeing of the areas in which we operate; and
- To support the communities in which we operate, by way of both personal and financial involvement.

David Holborn - Chairman

I am pleased to report the Society has made continued and steady progress in improving operating profits and achieving our revised strategy which focuses on returning to a simpler building society model with a diversified income stream via our Solutions business

Economic Backdrop

In over 40 years of working in the financial sector, I have experienced a number of periods of recessionary conditions. However this has been one of the most protracted periods of economic downturn that I have seen. The problems, which started to emerge in 2007 as financial markets started to freeze up and create the "credit crunch", have continued beyond most commentators' expectations and it appears a sustained recovery may take several years to achieve.

Whilst previous recessions have adversely affected business and employment, the current difficulties have also revealed that many Governments are facing record levels of National Debt against a backdrop of declining national income and related tax revenues. In our inter-related modern world, this has had adverse consequences beyond individual countries; it involves us all. We even see slowdowns in the economies of the previously fast-growing developing nations and close to home we are aware of the difficulties in the Eurozone.

As a regional building society we are not immune to this and our job is to manage effectively against this challenging background. The combined impact of unemployment at a 15-year high, inflation currently exceeding target and higher taxes, is reducing disposable incomes and may start to affect mortgage affordability causing arrears and possessions to increase. Interest rates continue at historically low levels and are expected to remain low for the foreseeable future, this should help borrowers, although many savers would like to see higher rates.

However, despite the challenges of the economic backdrop the Society has made steady progress in delivery of its strategy.

Achieving Our Strategy

We have continued to simplify the business via the sale of the Prepaid Cards business, reduction in legacy mortgage portfolios and unwinding of complex funding structures. At the same time we have improved operating profit before provisions, impairments and exceptional items from a loss of £0.3m in 2010 to a profit of £9.2m in 2011. This has been achieved through our continued efforts to reduce costs and improve efficiency and the ongoing expansion of our Solutions business, which provides a diversified income stream. This income stream helps protect the Society from continuing margin pressures caused by escalating funding costs and reduced levels of activity in mortgage markets. The increased operating profits together with the gain on disposal of the Prepaid Cards business have been offset by commercial mortgage provisions where we see greater pressures for borrowers due to the challenging economic climate.

Our ongoing focus on service quality and staff engagement was evident through the results of our customer and employee satisfaction surveys, which showed very positive trends in 2011.

The Chief Executive's Review on pages 5 and 6 sets out in more detail the progress the Society has made during 2011 in achieving our strategy.

Changes to the Board

It is essential to have a Board with the necessary skills and experience to manage the Society's business and oversee the delivery of our strategy. Changes that took place to the Board in the last year are detailed below.

Ann Cairns, a Non Executive Director, left the Board in June 2011 following an increase in her external international responsibilities which meant she could no longer continue on our Board. It was a pleasure to have Ann's professionalism and vision on our Board and we wish her every success in her continuing career.

Nigel Westwood retired in November after more than 11 years serving the Newcastle and Universal Boards. He worked throughout this time with distinction and commitment and his wise counsel, particularly on property related matters, provided much-valued support to our Executive team and Board as a whole. He leaves with our grateful thanks and best wishes in his retirement.

At the end of October we welcomed two new Non Executive Directors to the Board in John Morris and Phil Moorhouse. John joins as a former Divisional Director of HBOS and brings a wealth of financial services experience from that role and from his time with the former Halifax and Leeds Building Societies. Phil was formerly Managing Director (UK) of Northgate PLC and brings significant experience of running a substantial public limited company and will broaden the overall skills and expertise of the Board.

Going Forward

We shall continue our strategy of simplifying the Society's business operations with the aim of being a respected mutual regional building society serving members' interests and needs. We will focus on core building society products including residential mortgages, savings, investments and insurance, and continue the development of the Solutions business. We recognise that there are undoubted challenges ahead for the financial services sector but we have clear strategic priorities in place and firm foundations from which we can confidently take the Society forward.

DAVID HOLBORN
CHAIRMAN
29 FEBRUARY 2012

Jim Willens - Chief Executive

We entered 2011 holding a view that recovery for the economy would be steady and comparatively slow when compared to that experienced in the past in post recessionary periods, and that further challenges were likely to emerge, and indeed they have

Despite that backdrop, our focus on ensuring long-term delivery to our members, employees, support for local communities and Solutions business customers has meant the Society has continued to build on the successes of 2010, as well as deliver results ahead of our medium-term plans.

2011 was very much a year of two halves. During the first six months of the year, signs were beginning to point towards gradual improvement in general economic conditions. However, market sentiment very quickly deteriorated in the Summer and stayed with us for the rest of the year primarily, but not solely, influenced by uncertainty within the Eurozone.

Approach to Our Business

Our strategy recognises the challenges still facing the economy, financial services generally and individuals. However, it also seeks to optimise opportunities within both our own business and markets generally. Our key strengths lie in the following areas and our strategy therefore continues to be built around these areas of competence:

1. Heartland core building society savings, investments, mortgages and insurance business;
2. Further development of our key resource – employees;
3. Further simplification of our business model;
4. Diversification through our savings management Solutions business; and
5. Clear objectives and a robust corporate agenda, fully understood by employees and pursued with commitment and passion.

Our long-term strategic focus to return the Society to a traditional building society model supported by diversification through our Solutions business and prudent cost management served us well in 2011 and I am confident it will continue to do so in the years ahead.

Building Society Members

We have again enjoyed excellent support from our members. In excess of 25,000 new customers were attracted to the Society reflecting a year when we had excellent products available, such as our five year Fixed Rate Bonds, Online Easy Saver accounts, as well as competitive mortgage products. I was particularly pleased that our first time buyer products were so well received in a market place that needs to encourage more activity amongst those seeking their first home.

Our Penrith branch was reopened during 2011 having spent eight months operating from temporary premises following a flood as a result of the extreme cold weather spell in December 2010. Local needs and involvement of members in the area helped in developing plans for the re-launch, we are grateful to our members for their continuing support. This experience, combined with that gained when we launched our flagship branch in Newcastle city centre during 2010 means we have been able to develop a blueprint for future branch development.

Customer satisfaction improved from 85% to 90% during 2011, which is itself a pleasing result. However, we will always welcome feedback and seek to develop ways in which both delivery of quality products and service levels are improved on a continual basis.

Staff Engagement

Our staff engagement programme, led by a group of staff representatives from across the business, aims to evaluate, develop and build on key areas of the organisation and the day-to-day lives of our staff as we seek to make the Newcastle one of the most rewarding places to work in the region. We have made excellent progress thanks to the hard work and passion of our staff representatives.

We carried out our first annual employee satisfaction survey in December 2010 followed by a second in December 2011. Our staff responded magnificently in offering support and participation to all areas of our employee strategies such as, Reward and Recognition, Communication, HR Policies, Values and Behaviours, Career Paths, and Training and Development. That support has in turn produced a significant improvement in staff satisfaction which was 84% at the end of 2011.

In February 2011, the Society was re-accredited as an 'Investor in People' for the sixteenth year; the Society was the first building society to be accredited as an 'Investor in People'. The Society awarded a pay increase to its staff on 1st April 2011, after a gap of two years, and this was focused on our lower paid staff.

In 2012 the Society plans to introduce a graduate training scheme to provide further support to the region's graduates. By teaming up with North East universities we aim to offer rewarding long-term career opportunities and 'on the job' training to talented graduates. Additionally, we have relaunched a programme to give undergraduates the chance to get hands-on experience of working in a large commercial organisation over a year-long work placement.

I wish to put on record my sincere thanks to all staff for another year during which they have delivered superb results.

Communities
We continue to support the communities we serve through our branch network's engagement with local good causes, the corporate sponsorships we are part of and the Society's corporate charity of the year, which in 2011 was Macmillan Cancer Support. In addition, we have a fund with the Community Foundation, which celebrated its 21st year and this enabled us to give Christmas presents in December to 17 good causes. Our branches also launched a Christmas art competition in local schools; more than 100 winners of which were rewarded with a trip to the theatre. A number of other successful fund raising events have taken place including a family fun day attended by over 350 staff, coffee mornings and a myriad of sponsored activities including the Great North Run.

We launched a financial education programme for schools in our region in 2011; this was kick-started with primary schools in Middlesbrough and Whitley Bay, with positive feedback from all involved, including the 200 11-year-old pupils we presented to. The wider programme is in the process of being rolled out to other regional schools. Corporate Social Responsibility (CSR) remains a focus for us as a mutual organisation. Whilst the Society's ability to provide high levels of financial support has been constrained over the last 18 months, the energy and enthusiasm of our staff to participate and contribute to our CSR activities has not.

Newcastle Strategic Solutions
Solutions had a very successful year in 2011 with 50% growth in the number of accounts under management. Existing and new contracts launched in 2011 also contributed to an excellent year. We enter 2012 with a healthy pipeline of new business from existing and new clients and both present the opportunity for further growth in this part of our operations.

During 2010, the Society carried out a review of key areas of the business. Following this review, we concluded that our Prepaid Cards (PPC) business was not a long-term strategic fit for the Society.

The Society received expressions of interest in PPC from several organisations and after a contract negotiation and consultation period a sale was agreed. The purchaser is part of Wirecard AG, which provides innovative solutions in the fields of corporate banking, prepaid and co-branded cards, along with account products for both business and private customers. Wirecard AG is one of the leading international full-service providers of products and services for electronic payments.

All of the Society's PPC staff were transferred over to the purchaser under the Transfer of Undertakings (Protection of Employment) Regulations (TUPE) and the cards business continues to be based in Newcastle. As part of the sale, it was important to us to secure all the jobs and keep them within the North East.

This is a significant and positive development for our Society. While our PPC business has performed consistently for us over the years we needed to thoroughly assess the feasibility of it forming part of our strategy as a traditional building society going forward.

Business Simplification
Our strategy of returning our business model to that of a traditional building society supported by diversification through Solutions made excellent progress during 2011. The key highlights during 2011 were as follows:

1. The Prepaid card division of the Solutions business was sold in December 2011 with a gain on disposal recognised of £3.9m;
2. The Society completed the unwind of its £500m Covered Bond programme in July 2011 and the repayment of its commercial securitisation programme at the first call date in February 2011; and
3. Reduction in legacy mortgage portfolios accelerated during 2011 with £185m of repayments; including a 22% fall in commercial investment exposures and 17% decrease in Buy to Let loans.

We will continue to pursue a controlled and balanced approach to this strategy thus allowing us to concentrate our efforts further on our key stakeholders.

Financial Performance
Our financial performance during 2011 was much improved particularly in relation to our operating profitability before provisions, impairments and exceptional items. Management expenses continued to fall while operating income increased by 22% giving an improved cost income ratio of 80% compared to 101% in 2010. Our capital and liquidity ratios also improved.

Given the continuing challenges within the economy, we continue to take a prudent view of the potential risk attached to legacy assets held by the Society. As a result, we have made a substantial provisions charge amounting to in excess of £12.3m to protect the business in the years ahead.

We have also recognised a charge of £1.4m in 2011 in relation to the levy imposed by the Financial Services Compensation Scheme (FSCS). The charge reflects a higher funding cost which is expected to arise from the negotiations currently ongoing between HM Treasury and the FSCS around the interest rate applied to the Scheme loans. This levy falls disproportionately on building societies, which are predominantly retail funded. Further details attached to our financial performance are set out in the Business Review.

The Regulatory Landscape in 2012 and Beyond
There is major change on the horizon in terms of regulation covering financial services. Recovery and Resolution Planning becomes a requirement from June 2012. 2013 will see the introduction of the 'twin peaks' style of firm-specific regulation when the Bank of England takes overarching responsibility for financial stability. The Prudential Regulatory Authority (PRA) will be established as a subsidiary of the Bank of England and will have responsibility for prudential oversight of banks and insurers. The Financial Conduct Authority (FCA) will replace the Financial Services Authority and will oversee conduct of markets and the prudential regulation of other firms. 1st January 2013 will also see the introduction of the Retail Distribution Review.

The Society is well advanced with its planning and seeks at all times to work effectively with the regulatory world.

Summary
The Society made exceptional progress during 2011 towards our long-term objectives. Our approach continues to position the Society based on our cautious view of the outlook most likely to prevail in the years ahead. Any upside to this will be a bonus.

Our unrelenting focus will remain entirely fixed on ensuring we deliver the best value possible to our members, Solutions customers and employees, while supporting the communities we serve.

JIM WILLENS
CHIEF EXECUTIVE
29 FEBRUARY 2012

Overview
2011 was another challenging year for the financial services sector and the wider global economy, with some commentators suggesting it was the most difficult 12 months since the onset of the financial crisis. High inflation, higher taxes, rising unemployment and the austerity measures introduced by the Government affected household budgets and the high street through lower disposable incomes and waning confidence to consume. The Eurozone crisis has brought significantly more uncertainty and turbulence to markets. The impact of continued low interest rates coupled with a highly competitive retail savings market maintained pressure on margins. Despite this backdrop the Society has maintained its continued and steady progress.

Operating profit before impairments, provisions and exceptional items improved to £9.2m from a £0.3m loss in 2010. This progress has been achieved by pursuing strategies to return our focus to that of a traditional and simpler building society model, supported by a diversified income stream via the Solutions business, and with a significantly leaner and more efficient cost base. Profit before tax has increased to £0.1m in 2011 compared to a loss of £4.7m in 2010.

The Group balance sheet remains robust with high levels of premium low risk liquid assets, overall well-performing quality mortgage assets, a bigger proportion of funding from retail savers and improving capital ratios with Core Tier 1 ratio improving to 10.0% (2010: 9.1%), and overall Solvency ratio increasing to 15.0% (2010: 14.1%).

A continued focus on business simplification saw completion of the subsidiary rationalisation programme with 22 subsidiaries closed since 2010, repayment of the commercial securitisation programme at the first call date in February 2011 and unwind of the Covered Bond programme in July 2011. The sale of the Society's Prepaid Cards division was completed in December 2011 resulting in a net gain on disposal of £3.9m.

The risk profile of the Society's balance sheet continued to improve with a reduction in legacy portfolios in wind down of £185m including a 22% fall in commercial balances, 17% fall in Buy to Let mortgages and 29% decrease in loans secured on traded endowment policies, which are now at only £28m. The Group recognises the particularly demanding conditions experienced by commercial borrowers and has recognised a charge of £12.3m against loans in arrears or possession, with Law of Property Act 1925 (LPA) receivers or where a trigger event has identified there may be a problem in the future servicing of the loan.

Income Statement Review

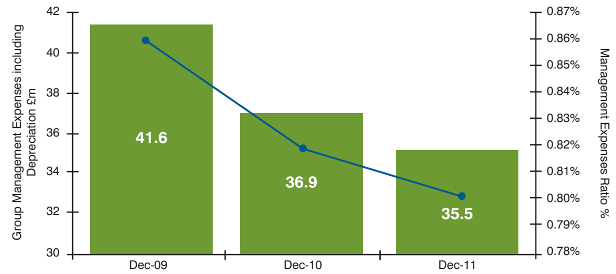
GROUP INCOME STATEMENT	2011 £m	2010 £m	2009 £m
Net interest income	17.5	17.8	20.4
Other income	27.2	18.8	19.4
Total income	**44.7**	**36.6**	**39.8**
Administrative expenses	(32.6)	(33.7)	(38.3)
Depreciation	(2.9)	(3.2)	(3.3)
Operating position before impairments, provisions and exceptional items	**9.2**	**(0.3)**	**(1.8)**
Net gain on disposal	3.9	-	-
Impairment losses - customers	(12.3)	(1.8)	(8.0)
Impairment losses - banks and debt securities	0.7	2.4	9.1
FSCS levy	(1.4)	-	1.3
Repositioning Programme	-	(4.0)	-
Provisions for liabilities and charges	-	(1.0)	(0.5)
Profit/(loss) for the year before taxation	**0.1**	**(4.7)**	**0.1**

Net Interest Income
Net interest margin remained stable at 0.40% in 2011 the same as 2010. Maintaining margin remains a challenge given the continued upward pressure on retail funding costs, reduced returns on liquid assets due to the impact of the Liquidity Standards Regime and a stagnant housing market impacting mortgage lending volumes. The Group will continue to maintain its strategy of considering the longer term impact on margin of new residential lending and will only lend where acceptable returns are achieved for the risk taken.

Other Income and Charges
Other income across the Group rose by £8.4m in 2011 to £27.2m from £18.8m in 2010. The main drivers for the improvement were an increase in Solutions income of £6.6m and higher activity on regulated sales which generated £0.7m of additional income.

In the Solutions business, the full year impact of contributions from a number of savings management contracts was felt on both expanding contracts launched in 2010 and new contracts in 2011. The Solutions division continues to attract new business and the Group will continue with its strategy to strengthen its diversification based on core competencies into 2012 and beyond.

Administrative Expenses and Depreciation
Administrative expenses fell by £1.1m in the year to £32.6m (2010: £33.7m) despite the increased staffing requirement and activity levels required to support the growing Solutions business. When the cost base for 2011 is compared to that of 2009 there has been an overall reduction of £9.1m, after taking into account that 2009 management expenses are stated net of a £3m pension curtailment credit. The overall fall in management expenses reflects the benefits flowing from the Repositioning Programme in 2010 with lower property costs, improved efficiency levels and reduced subsidiary administration costs; this is supplemented with strict control of discretionary expenditure and carefully managed capital investment.



The management expense ratio (administrative expenses plus depreciation as a percentage of mean total assets) improved to 0.80% in 2011 from 0.82% in 2010. As a measure of the Group's improving efficiency the ratio of operating cost to income has improved to 80% from 101% in 2010.

Gain on Disposal of Prepaid Cards Division
The Society legally completed the sale of its Prepaid Cards Division to Wirecard AG Group on 21st December 2011. Cash received on completion amounted to £7.5m and a further £2.5m may be receivable as deferred consideration based on trading performance of the Prepaid Cards Division in 2012 and 2013. The Society has recognised £0.5m of the earn-out in 2011 with any further income being recognised in 2012 and/or 2013 when receipt is more certain. After allowing for costs of £0.7m, assets written off of £0.3m and liabilities recognised of £3.1m (in relation to pre-completion liabilities retained by the Society) the net gain on disposal recognised in 2011 is £3.9m. Further details are given in Note 10 on page 40.

Impairment Losses

Loans and Advances to Customers

The overall net impairment charge for loans and advances to customers has risen to £12.3m in 2011 from £1.8m in 2010. The Society has, and will continue to, pursue its strategy to de-risk the balance sheet by winding down the commercial lending portfolio and providing against loans where an impairment trigger has been reached. The economic climate and uncertainty, particularly in the second half of 2011, have heightened difficulties in the commercial property sector and as a result £12.2m of the £12.3m charge added in the year relates to commercial lending (across specific and collective provisions) following impairment assessments and a revision to the Society's methodology of identifying trigger events. Impairment calculations are carried out by considering future discounted cashflows as per rules laid out in international accounting standard, IAS39. In considering future cashflows the Society estimates the future valuation of the security less anticipated disposal costs, any interest rate hedging unwind required as well as interest rates, payments and charges. The Society considers several factors when deciding if a commercial exposure is impaired including any missed payments, tenant financial position, tenant voids and likelihood of re-letting, and any other potential loan servicing issues arising from assessments or professional advice. In 2011 a provisioning committee was newly formed with the remit to fully and consistently apply the Society's impairment methodology to commercial loans with the best internal and external information available. Further details of commercial arrears and provisions are given in the Directors' Report on page 14.

A charge of £0.5m relates to residential lending; predominantly Buy to Let loans. The incidence of credit losses on the Society's core residential lending portfolio has been negligible. The low level of losses on residential lending, in current circumstances, is a reflection of the good quality of £2.6bn or 86% of the Group's mortgage assets. Impairment of the residential book is considered collectively for loans with 3 month or more arrears, based on an estimation of loss given default and probability of default based on individual loan circumstances. All properties entering possession are provided for specifically based on loan to value and anticipated disposal costs. The Society has created an additional model in 2011 to identify roll rates to possession for loans with previous arrears or where forbearance has previously been granted. An additional small collective provision has been recognised covering loans captured by this model.

The Society's book of loans secured on traded endowment policies is significantly reduced and £0.4m has been credited through impairment charges to reflect a lower provision requirement.

Loans and Advances to Banks and Debt Securities

In 2008 the Society made impairment provisions totalling £32.6m against exposures to Icelandic banks. The Society is provided with information from administrators about the level of recoveries the creditors could expect to recover from the Icelandic banks. The anticipated recoveries for Glitnir and Landsbanki have fallen in 2011 following an adverse ruling on priority of deposits in Iceland. Kaupthing Singer and Friedlander and Heritable recoveries, which are based on latest estimates from the administrators, have been revised upwards following an ongoing improving trend in recoveries, which has been evident over the last year. The overall effect on Newcastle Building Society is that there is a net credit of £0.7m on the impairment provisions as set out in Notes 11 and 12 to the Annual Report and Accounts, and as summarised in the following table.

IMPAIRMENT LOSSES - ICELANDIC BANKS	2011 £m	2010 £m
Balance at 1 January	21.1	23.5
Amounts released in the year	(0.7)	(2.4)
At 31 December	**20.4**	**21.1**

FSCS Levy

The Society's provision for its contribution to the Financial Services Compensation Scheme (FSCS) has been increased by £1.4m in 2011 (2010: £nil). The increase in provision is to enable the Society to cover its estimated liabilities under the rules of the scheme in compliance with international reporting standards and guidance, IAS37 and IFRIC6. The cost of funding the FSCS levy is currently being negotiated between the FSCS and HM Treasury and the final outcome of these discussions will have an impact on the compensation levy passed on to UK regulated deposit takers. Further details of the provision are given in Note 27 on page 52.

Repositioning Costs

The Society established a £4m provision in 2010 to cover costs and fees associated with its programme of business simplification and property rationalisation. At 31 December 2011 £1.1m (2010: £1.7m) of the provision remained, relating to vacant properties that the Society is currently marketing with property agents.

Taxation

The Society's tax charge for the year reflects the impact on deferred tax assets for the change in the enacted corporation tax rate. This amounted to £0.8m for 2011 (2010: £0.5m).

Segment Reporting

The Newcastle Building Society Group prepares segment information under IFRS 8 with activities split into "Member" and "Solutions" businesses. Details are given in Note 9 on page 39. The Member business provides mortgage, savings, investment and insurance products to members and customers. The Solutions business provides business-to-business services through people, processes and technology. The Board assesses performance based on profit before tax after the allocation of all central costs. The presentation in Note 9 highlights the effect that the interest rate margin has on the Member business profitability. In addition, the impact of commercial provisions and the higher FSCS levy has had a pronounced impact on the overall result before tax of the Member business. The improved performance of the Solutions business reflects the full year impact in 2011 of contracts entered into in 2010 and new contracts in 2011. As volumes in the Solutions business increase there is also a greater recovery of the fixed overheads that support this business.

Balance Sheet Review

Liquid Assets

The Society has continued to maintain a high level of quality liquid assets throughout 2011 with a higher liquidity percentage (liquid assets as a percentage of shares and borrowings) of 29.2% at 31 December 2011 (2010: 25.2%). The Society pursues a prudent and careful approach to its liquid asset investments with robust and thorough credit risk assessment. Over 70% of the liquid assets held are AAA-rated.

RATING	2011 %	2010 %
Aaa	70.1	76.1
Aa1 - Aa3	15.5	17.8
A1 - A3	10.8	3.5
Baa1 or below	2.3	1.4
Unrated	1.3	1.2
Total	**100%**	**100%**

Exposures with a rating of A3 or below are all deposits with other building societies and with 2012 maturity dates.

COUNTRY EXPOSURE	2011 %	2010 %
Australia	4.1	3.6
Belgium	-	0.7
Finland	1.5	-
France	-	2.7
Germany	-	2.7
Iceland	0.7	1.4
Netherlands	2.4	-
Spain	0.3	1.1
Switzerland	0.5	-
UK	72.1	70.4
Supranational	16.0	17.4
QMMF*	2.4	-
	100%	**100%**

*Qualifying Money Market Funds (QMMF) exposures are AAA-rated, of overnight duration, and are domiciled in the Republic of Ireland. The Society only invests in QMMF that are members of the Institutional Money Market Funds Association, the trade association for AAA-rated European Money Market Funds.

The Society has no liquid instruments with counterparties based in Greece, Portugal, Italy, France or Belgium. A single Spanish exposure of 0.3% is held with an organisation, which has a major UK high street presence and is due to mature in March 2012. The table below shows the Society's liquid asset profile by asset class at fair value.

	2011 %	2010 %
Cash in hand and balances with the Bank of England	13.8	24.9
Cash with banks and building societies	21.5	20.8
Gilts	17.1	13.2
Certificates of deposit	4.7	4.9
Fixed rate bonds	12.1	15.2
Floating rate notes	11.0	16.9
Residential mortgage backed securities	16.0	4.1
Covered bonds	3.8	-
	100%	**100%**

All of the Society's liquid assets are denominated in UK Sterling; the Society does not invest in instruments denominated in other currencies.

Loans and Advances to Customers

Loans and advances to customers fell by £353m in 2011 as shown below, with over one half of this attributable to the unwinding of portfolios where the Society had ceased new lending and exited the market. The Group has continued its policy of only undertaking new residential lending where it can be done profitably after considering all associated risk, funding and capital costs. 2011 has also seen an increase in residential customers paying off their mortgages in full or making lump sum payments with 55% of the reduction in the prime residential portfolio being attributable to this feature. The residential portfolio contains the Society's Buy to Let mortgage book.

	2011 £m	2011 LTV%	2010 £m	2010 LTV%
Residential Homeowners	1,715	55.8	1,929	55.8
Housing Associations	849	74.8	870	74.7
Commercial	392	93.9	488	78.3
Other	38	66.7	60	62.2
	2,994		3,347	
Provisions	(17)		(22)	
	2,977		**3,325**	

The Group's lending is secured with a first charge registered against the collateral property. Residential loans are shown at indexed loan to value using the quarterly regional Halifax House Price Index, remaining loans are shown without indexing. Further information on security loan to value is provided in Note 34 on page 65 to 67.

The Society's loans of 3 months or more in arrears are measured by both number of loans and balance as a percentage of total number of loans and total balance, respectively. The levels of arrears experienced are satisfactory given the economic backdrop and are below market average as reported by the Council of Mortgage Lenders. The value of commercial loans in arrears of 3 months or more has increased by 1.37% from its 2010 zero base representing 2 loans. The Society works closely with borrowers and regularly assesses the servicing and repayment risk of its exposures.

ARREARS PERFORMANCE 3 months or more arrears	By number of loans 2011 %	By number of loans 2010 %	By balance 2011 %	By balance 2010 %
Residential	0.73	0.75	0.78	0.69
Commercial	0.61	-	1.37	-
Housing Association	-	-	-	-
Other	1.12	1.29	0.86	0.29
Total	**0.75**	**0.78**	**0.64**	**0.40**

The Group's residential portfolio is of good quality with a lower number of loans in arrears at 31 December 2011 than at the 2010 year end.

The Society's policy on forbearance measures is compliant with the detailed requirements of the FSA's Mortgage Code of Business Sourcebook (MCOB). The term forbearance is defined as the granting of a concession, which alters the contractual terms of a loan. The Society will work closely with any homeowner experiencing difficulties, offering help and advice on all aspects of the situation. In an approach which seeks to treat its customers fairly the Society tailors its forbearance measures to reflect the borrower's individual circumstances. The Society can offer measures, including changing the term of the loan, a temporary change to interest only, a reduced subscription, a payment holiday or deferring interest payments. The Society will also consider whether the borrower qualifies for Government initiatives covering Homeowner Mortgage Support Scheme (HMSS) and Homeowner Mortgage Rescue Scheme (HMRS). The Society enters into forbearance agreements on the understanding that concessions are granted in the best interests of the borrower in order to return the loan to performing status over time.

FORBEARANCE CASES	2011	2010
Reduced Payments	95	54
Interest Only Payments	11	29
Conversion to Interest Only	1	26
Extension of Term	2	3
Payment Holiday	19	16
Forbearance Declined	30	54
Total number of cases	**158**	**182**

The forbearance information above is presented in line with the definition used by the FSA in the data gathering exercise for the Financial Policy Committee carried out in the Autumn of 2011. Forbearance data is monitored closely on a monthly basis by the Residential Credit Committee with the levels of concessions granted not considered to be material for the size of the overall book.

At 31 December 2011, the Group had only one commercial loan in possession and two exposures in Law of Property Act 1925 (LPA) receivership with total balances of £2m, after specific provisions. One residential investment loan with a balance of £2.5m had its terms restructured during the year. Residential possessions total 28 (2010: 40) and include properties where the borrower has handed in the keys, properties possessed following court action by a second charge lender and where the Society is assisting the estate of a borrower in the disposal of a property. Only four residential accounts in 2011 had defaulted to the point that required court action by the Society to take possession.

POSSESSIONS	31-Dec-10	Taken in	Sold	31-Dec-11
Equity release managed sale	1	2	1	2
Commercial property	1	-	-	1
BTL property	28	-	8	20
Court action	7	4	7	4
2nd charge mortgagor action	2	4	5	1
Abandoned/surrendered	2	4	5	1
Total	**41**	**14**	**26**	**29**

LPA Receiverships	31-Dec-10	Taken in	Sold	31-Dec-11
BTL property	-	3	1	2
Commercial property	-	4	2	2
Total	**-**	**7**	**3**	**4**

Funding

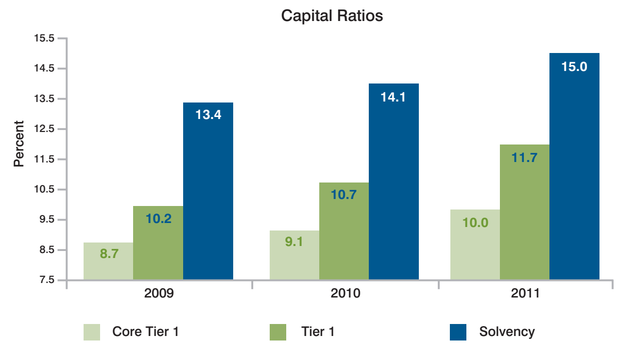
Despite a challenging marketplace, the Society continues to offer its members a range of attractive savings products. This has resulted in an increase in retail savings balances of £170m in 2011 as the Society moved even further away from reliance on treasury markets and wholesale deposits. The wholesale funding ratio reduced over the year from 9.53% to 6.95% with the Society's mortgage portfolio remaining fully funded by retail savings. The Society's £500m Covered Bond programme, which was launched in January 2009 was unwound following repayment of the funding in July 2011. In addition, the Society called the non-recourse finance held in the special purpose vehicle, Bamburgh Finance (No1) PLC, on 1 February 2011. The £65m call saw floating rate notes secured on first-charge commercial loans redeem at par. During the year, the Society notified Moody's that it wished to withdraw its rating and this was withdrawn in October 2011.

Capital

The table below shows the composition of the Group's capital and the capital ratios at the end of the year.

CAPITAL	2011 £m	2010 £m
Tier 1 Capital		
General Reserve	170.8	174.5
Permanent interest bearing shares	29.6	29.6
Regulatory waiver adjustment	-	0.2
	200.4	204.3
Tier 2 Capital		
Subordinated Debt	56.0	58.6
Collective impairment allowance	1.6	6.4
	57.6	65.0
Total Capital	**258.0**	269.3
Risk Weighted Assets		
Liquid Assets	127.4	65.4
Loans and Advances to customers	1,420.4	1,628.6
Other Assets	64.9	86.6
Off Balance Sheet	40.1	59.2
Operational Risk	62.5	73.0
	1,715.3	1,912.8
Capital Ratios	%	%
Core Tier 1 ratio	10.0	9.1
Tier 1 ratio	11.7	10.7
Solvency ratio	15.0	14.1
Tier 2 to Tier 1 ratio	28.7	31.8

All of the capital ratios show improvement in 2011 and demonstrate a strengthening capital base with the total solvency ratio improving to 15.0% (2010:14.1%). The Group complied with Individual Capital Guidance notified by the FSA throughout 2011.



Outlook

It is likely that the economic conditions, and particularly the market turbulence, which prevailed in 2011 could abate to a degree as European governments tackle the issues at hand and attempt to bring stability to the global economy. However, there is also a possibility the UK will enter a second recession given the negative growth figures issued by the Office for National Statistics for Quarter 4 2011. Any further rises in unemployment could see the Society experience a higher rate of mortgage arrears. The Board expects the low interest rate environment to continue throughout 2012. This will maintain pressure on margins when combined with the competitive retail savings market, however household budgets should continue to benefit from lower mortgage interest payments.

The Society will maintain its cautious approach to lending in terms of risk and return with high volume unlikely as there is no planned balance sheet growth. The Board's approach to lending is designed to protect capital and liquidity and means that growth in retail funding will not be required. The commercial wind-down strategy and improving the overall risk profile of the Society's mortgage portfolio will continue to be pursued and the additional provisions recognised in 2011 should support the Society's continued pro-active approach.

Profit will not be the key driver for 2012, but the Society will continue to strengthen its income streams through its Solutions business, as well as reducing further its underlying cost base. The Board is confident that improvement in financial performance will continue in 2012.

ANGELA RUSSELL
FINANCE DIRECTOR
29 FEBRUARY 2012

Our Directors

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1. David Holborn
Chairman

David has spent his entire career as a finance professional. He worked for Lloyds Banking Group for 39 years in a number of Executive roles. He was Director of the Northern Region for 10 years and was responsible for service to customers in business, commercial and personal sectors through 225 branches and 3000 staff. He was also a member of the Lloyds TSB National Retail Board. He was elected to Fellowship of the Chartered Institute Of Financial Services in 1998 for his services to Banking and is a former President of the Bournemouth and Newcastle Centres. Prior to his appointment as Chairman of the Society's Board in January 2011, he built up significant experience of the Society; he was a Non Executive Director for eight years and held the post of Senior Independent Director. David is also the Vice Chairman of Rothley Trust, a post he has held for three years, having previously been a Trustee for four years.

2. Jim Willens
Chief Executive

Jim's expertise in, and commitment to, the building society sector spans more than 30 years. During this time, he has held significant senior posts including Retail Operations Director and Group Services Director at Nationwide. His roles over the years have included strategic responsibility for Branches, Telephony, Internet Services, Technology, Product Development and Central Support Services, which have involved leading teams in excess of 9,000 people. His career started out in the 'field' as a branch manager and he also held a range of retail and sales management positions. Jim has a strong track record of delivery and a passion for developing the people he works with to provide excellent customer service through the mutual business model both of which are key elements to the Society's corporate strategy.

3. Ron McCormick
Deputy Chairman

Ron has established a successful career in the building society sector as an experienced accountant. He is both a Fellow of the Institute of Chartered Accountants and a Fellow of the Chartered Institute of Internal Auditors. He has previously worked as both Group Finance Director then Group Commercial Director at Skipton Building Society, posts which he held for a total of 14 years. In addition, he has more than seven years experience with Guardian Royal Exchange, as well as seven with KPMG, both in the UK and abroad. Following three years on the Newcastle's Board, in January 2011 he was appointed Deputy Chairman and Senior Independent Director. He also is a member of the Society's Audit and Group Risk Committees. He also works as a senior adviser to businesses within a range of sectors.

4. Angela Russell
Finance Director

Angela is a highly experienced Chartered Accountant and Certified Public Accountant with over 20 years experience in finance in the UK and abroad. She has worked in a variety of positions covering finance, risk, audit, project and corporate planning roles. In particular, she has several years experience in finance roles within the building society sector including her current role as Finance Director for the Newcastle, which she has held since 2010, and follows two years with the Society as Group Risk Executive. She also held the post of Finance Director at the Universal Building Society (before its merger with the Society in 2006). Angela also spent 12 years at PricewaterhouseCoopers LLP. She is also a Non Executive Director of a North East based care charity.

5. John Warden
Operations Director

John has worked for over 10 years in financial services. During that time, in addition to operations, he has headed functions covering marketing, corporate planning, business change, project management, finance, IT and HR. He joined the Society in May 2010 as Interim Operations Director before being confirmed in the permanent post in October that year. Prior to that, he held senior roles at both Coventry and Yorkshire Building Societies. John is a Chartered Accountant with over 10 years experience as a Finance Director spanning a number of sectors including financial services, retail, IT and manufacturing. He also spent nine years at PricewaterhouseCoopers LLP.

6. Gillian Tiplady
Business Services Director

Gillian has more than 18 years experience of the legal profession, which includes ten years working in the building society sector. She worked at Universal Building Society for five years before the merger with the Society where she was a Director and Group Secretary. In January 2011, she became a Board member of the Society when she was appointed as Business Services Director. She is a solicitor and spent 13 years at Watson Burton where she specialised in Banking and Insolvency law. She is also a trustee of Seven Stories, the Centre for Children's Books.

7. John Morris
Non Executive Director

John Morris is a Fellow of the Institute of Chartered Accountants and brings to the Society a significant amount of experience of both the banking and building society sectors. He worked for several years as Director of Finance for the Retail Banking Division at HBOS. Prior to that, he held senior posts at Halifax (Halifax Building Society and then Halifax PLC) as General Manager and Leeds Permanent Building Society where he held the post of General Manager Finance. He also worked at KPMG where he started his accountancy career. He is also a member of the Society's Group Risk Committee.

8. Richard Mayland
Non Executive Director

Richard is an experienced accountant who was a partner at Pricewaterhouse Coopers LLP (PwC) for 17 years before his retirement in 2003. During his time with PwC, he specialised in audit and business advisory services. His time as a partner was spent in the North East before being asked to head the financial services audit practice for the North of England. He has significant expertise in the regulatory and accounting matters. He is currently Chief Executive of Norprime Ltd, a post he has held for five years. He brings more than 30 year's experience of the accountancy world to the Society's Board, which he has been a member of for more than six years. He is also Chairman of the Society's Audit Committee and a member of both the Nomination and Remuneration Committees.

9. Catherine Vine-Lott
Non Executive Director

Catherine has a total of 34 year's experience in the financial services sector having spent her entire working life in the industry. This includes 18 years at Barclays where her positions included Chief Executive of Barclays Stock Brokers, as well as Barclays Personal Investment Management. In addition, she has significant experience with Legal and General both at group Board level and in running the wealth management division. This brings an abundance of expertise to Newcastle's Board, which she joined in January 2010. She is also an experienced Non Executive Director and is Chairman of Openwork Holdings Limited, Rathbone Brothers PLC and Cranfield University Advisers Committee. For the Society, she is Chairman of the Remuneration Committee and a member of the Audit Committee.

10. Phil Moorhouse
Non Executive Director

Phil is a highly experienced accountant and is a Fellow of the Chartered Association of Certified Accountants. He has held a number of senior Board positions including that of Managing Director (UK) of Northgate PLC, which he held for more than seven years. This followed six years as Finance Director. He is a Director of the charity Renew (North East), having been Chairman for several years and at Molins PLC he is Chair of Audit and a Senior Independent Director. Additionally, he sits on the Board of Cumbria NHS Partnership Trust. Phil brings his 35 years industry expertise to the Newcastle's Board and also the Society's Audit Committee, of which he is a member.

11. David Buffham
Non Executive Director

David has spent most of his career at the Bank of England. He held a wide variety of banking and other roles, most recently the post of Bank of England Agent for the North East. There he was responsible for reporting to the Bank's Monetary Policy Committee on the region's economy and explaining policy to key stakeholders in the North East. He brings this knowledge and experience to the fore as Chairman of the Group Risk Committee and also as a member of the Nomination and Remuneration Committees. He is an experienced Non Executive Director and, additionally, is a Governor at Northumbria University in Newcastle.

The Directors present their Annual Report and Accounts and Annual Business Statement for the year ended 31 December 2011

Objectives and Activities

The principal objective of Newcastle Building Society is to attract funds, through a competitive range of personal savings and investment products, in order to make available advances secured on land and property, primarily for use of our members. This core activity is supported by offering a range of related financial products and services which are provided by the Society and its subsidiary companies. The principal subsidiary companies which affect the net profits and net assets of the Group are listed in Note 16 on page 44.

It is the intention of the Directors that the Society will continue to remain an independent building society. We believe this status enables us to deliver consistent and fair value and to provide enhanced benefits to all our members and customers through our attractive, innovative products and our increasing network of business partnerships.

Business Review

The Chief Executive's Review and Business Review on pages 5 to 11 report on the business activities and business performance for the year as well as likely future developments.

The Directors have reviewed the Group's capital, liquidity and profit forecasts and considered the risks faced by the Group, including under a stressed scenario. The Directors are satisfied that there are no material uncertainties that cast significant doubt about the Group's ability to continue as a Going Concern and have, therefore, continued to adopt the Going Concern basis in preparing the Annual Accounts. (See Note 1 on page 32.)

Risk Management Objectives and Policies

The Board seeks to manage the key risks faced by the Group in order to minimise any potential adverse impact on performance. The key financial risks faced by the Group include credit risk, liquidity risk, operational risk and market risk which are managed through the Group's documented risk management framework. Further details can be found below and in the Risk Management Report on pages 22 to 24.

Principal Risks and Uncertainties

The principal risks and uncertainties faced by the Group are summarised below.

Credit Risk - Commercial

The Society's commercial lending exposure is made up of larger, more concentrated loans secured on land and non-residential property at a loan to value (LTV) ratio which is higher than more traditional residential lending. The Society ceased commercial lending in 2008 and is actively winding the portfolio down, however, the potential for credit losses continues to be a material risk, despite a reduction in the portfolio of some 22% over 2011. Commercial property values continue to stagnate with values in secondary and tertiary locations continuing to fall. With a backdrop of continuing economic turbulence and in keeping with the Society's desire to protect members' interests in the longer term, provision for an additional £12.2m of commercial credit losses has been made in the 2011 Annual Accounts. The 3 months or more arrears rate on the Society's commercial lending portfolio was 1.37% at 31 December 2011 (2010: 0.00%) representing two loans with a value of £3.6m after provisions. The Society had one possession property at the year end with a value of £0.2m after provisions, and there were two properties held with Law of Property Act 1925 (LPA) receivers with balances totalling £1.8m after provisions.

Credit Risk – Residential

The Group's residential lending portfolio contains mostly well seasoned, well performing, low LTV owner-occupied loans. Throughout the year, the Society continued to see low levels of arrears and possessions on this part of its mortgage portfolio. In 2011, the Society experienced an increase in the number of customers adding to their mortgage payments or making lump sum payments in the challenging economic climate. Average UK house prices have fallen modestly in 2011 and by around 15% compared to the peak in 2007. Unemployment in the UK is rising and although not yet materially affecting the Society's arrears levels, it remains a key factor in the credit risk associated with this type of lending. In 2011 the Society experienced a 40% fall in BTL arrears of 3 months or more. The rental market in 2011 was buoyant and the Society works closely with borrowers experiencing cashflow difficulties. The credit risk inherent in the BTL portfolio remains material and concentrated in a small group of borrowers.

The Society will maintain its strategy to reduce its BTL exposure although the focus remains on larger portfolios rather than smaller borrowers.

The Society's lending policy caps interest only residential borrowing at 75% LTV. At 31 December 2011 33.2% (2010: 34.2%) of the residential book was interest only loans.

Overall the number of 3 month residential arrears cases fell from 0.75% to 0.73% in 2011 with the value of 3 month arrears rising from 0.69% to 0.78%. Further details are given in the Business Review.

Liquidity Risk

The Society monitors on a daily basis the risk it will have insufficient cash to meet its liabilities as they fall due. The Society has throughout the year mitigated this risk by maintaining high quality liquid assets and has further reduced its reliance on treasury markets, with the wholesale funding ratio maintained below 10% throughout the year. The Society undertakes lending only where funding is in place and operates a range of retail savings products to attract and retain customers. Given the increased uncertainty in treasury markets over the latter part of 2011, including a potential Eurozone crisis combined with increasing ratings downgrades, the Society increased its liquidity holdings in Quarter 4 2011 and this is reflected in an increased liquidity ratio of 29.2% at 31 December 2011 (2010: 25.2%).

Operational Risk

Further details on operational risk are given in the Risk Management Report.

Market Risk

The Society's market risk derives from interest rate risk in the banking book and the way interest margin is impacted by a changing rate environment. This includes basis risk as well as the impact of upward and downward movements in interest rates. Sensitivity to, and the effect of, interest rate changes are monitored by the Asset and Liability Committee. The Society actively measures the effect of rate movements in accordance with best practice, and manages the interest rate risk to which it is exposed using interest rate hedges or natural offsetting of asset and liability rate-characteristics. Further details are given in the Risk Management Report.

Group Results for the Year

The Business Review on pages 7 to 11 provides a detailed overview of the Group's results and performance during the year and should be read in conjunction with the following summary, which the Directors consider to be the key performance indicators used to manage the business.

Key Performance Indicators (KPI's)

Profitability

- Group operating profit before impairments, provisions and exceptional items for 2011 was £9.2m, an improvement compared to the previous 2 years where a loss of £0.3m was reported in 2010 and a loss of £1.8m in 2009;
- Profit before tax was for 2011 was £0.1m compared to a loss before tax of £4.7m in 2010;
- Interest margin stable at 0.40% in 2011;
- Solutions income improved from £9m to £15.6m;
- Cost to income ratio in 2011 was 80% improved from 101% in 2010;

Capital

- Solvency ratio improved to 15.0% at 31 December 2011 (2010: 14.1%);
- Tier 1 ratio strengthened to 11.7% at 31 December 2011 (2010: 10.7%);
- Core Tier 1 ratio was 10.0%, up from 9.1% in 2010;
- The Society operated above the Individual Capital Guidance issued by the FSA throughout 2011;

Credit Quality

- There were 29 properties in possession at the end of 2011 (2010: 41) and 4 in LPA receivership (2010: None);
- The number of loans in 3 months or more arrears for the total mortgage portfolio was 0.75% at the end of 2011 compared to 0.78% at the end of 2010. By balance the figure has increased from 0.40% to 0.64%;
- The wind down of legacy portfolios amounted to £185m in 2011 including £107m of Commercial Investment loans and £44m of Buy to Let loans;

- Impairment losses on loans and advances to customers increased from £1.8m to £12.3m and mainly related to higher provisions on the Commercial Investment portfolio;

Liquidity

- Total liquidity represented 29.2% of shares, deposits and liabilities at the end of 2011 compared to 25.2% at the end of 2010; and
- The Society's operated above Individual Liquidity Guidance issued by the FSA throughout 2011.

The Society also uses a number of non-financial KPI's to monitor its performance against target in areas such as customer satisfaction, customer service levels, staff turnover, employee satisfaction and number of new members.

Staff

Newcastle Building Society operates an Equal Opportunities Policy. It is the intention of the Society that no applicant or employee receives less favourable treatment on the grounds of disability, sex, transgender status, sexual orientation, marital status, civil partnership status, race, ethnic origin, colour, age, nationality, national origins, political beliefs or trade union membership, or is disadvantaged by conditions or requirements that cannot be shown to be justifiable.

Staff remuneration reviews are carried out on an annual basis and a variety of performance related bonus schemes are operated in some key business areas to enable individual and branch team efforts to be recognised and rewarded.

The Society takes its responsibilities for staff development very seriously and has held the Investors in People accreditation for more than 16 years. We are committed to effective communication at all levels and the Society was able to build on its Staff Engagement Programme in 2011 taking steps to ensure that employee consultation is ample and ongoing. Unite has negotiating rights on behalf of all staff up to and including senior management level.

Charitable Donations and Political Contributions

The Society made donations to charities amounting to £57,773 in 2011 (2010: £2,244). The Society is very supportive of local and national charities, continuing to offer its "in kind" donations through a programme of fundraising events. There were no political contributions during the year.

Creditor Payment Policy

The Society's policy concerning the payment of suppliers is to negotiate and agree terms and conditions with all suppliers and to pay in accordance with its contractual and other legal obligations. At 31 December 2011, the creditor days' figure was 23 days (2010: 27 days).

Directors

As at 31 December 2011, the members of the Board, who had served throughout the year and continue to act as Directors were as follows:

David Buffham, David Holborn, Richard Mayland, Ron McCormick, Angela Russell*, Catherine Vine-Lott, John Warden* and Jim Willens*

The following Directors were appointed during the year:

- Gillian Tiplady* joined the Board as Business Services Director, with effect from 11th January 2011; and
- Phil Moorhouse and John Morris joined the Board as Non Executive Directors with effect from 31st October 2011.

The following Directors left the Board during 2011:

- Ann Cairns resigned from the Board with effect from 30th June 2011; and
- Nigel Westwood retired from the Board with effect from 28th November 2011.

At the Annual General Meeting, to be held on 25 April 2012, all Directors will now offer themselves up for annual election/re-election.

* Executive Directors

Independent Auditors

A resolution to re-appoint PricewaterhouseCoopers LLP will be proposed at the Annual General Meeting.

Statement of Disclosure to Auditors

So far as each Director is aware, there is no relevant audit information of which the Society's auditors are unaware; and

Each of the Directors, whose names and functions are listed in the Our Directors section on pages 12 and 13 has taken all steps that he or she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Society's auditors are aware of that information.

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The following statement, which should be read in conjunction with the statement of auditors' responsibilities on page 25, is made by the Directors to explain their responsibilities in relation to the preparation of the Annual Report and Accounts, Annual Business Statement and Directors' Report.

The Directors are responsible for preparing the Annual Report and Accounts, Annual Business Statement and Directors Report in accordance with the appropriate law and regulations. The Building Societies Act 1986 ("the Act") requires the Directors to prepare Group and Society Annual Accounts for each financial year. Under the Act they are required to prepare the Group and Society Annual Accounts in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and applicable law.

The Group and Society Annual Accounts are required by law and IFRS as adopted by the EU to give a true and fair view of the state of affairs of the Group and Society as at the end of the financial year and of the income and expenditure of the Group and Society for the financial year, and which provide details of Directors' emoluments in accordance with part VIII of the Act and the regulations made under it.

In preparing each of the Group and Society Annual Accounts, the Directors are required to:

- Select appropriate accounting policies and apply them consistently;
- Make judgements and accounting estimates that are reasonable and prudent;
- State whether applicable accounting standards have been followed subject to any material departures disclosed and explained in the Accounts; and
- Prepare the Annual Accounts on the going concern basis unless it is inappropriate to presume the Group will continue in business.

In addition to the Accounts, the Act requires the Directors to prepare, for each financial year, an Annual Business Statement and a Directors' Report, each containing prescribed information relating to the business of the Group. The Directors are responsible for ensuring that the Group:

- Keeps adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time the financial position of the Group and Society in accordance with the Act; and
- Takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its businesses in accordance with the rules made by the Financial Services Authority under the Financial Services and Markets Act 2000.

They are also responsible for safeguarding the assets of the Society and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the financial information included on the Group's website. Legislation in the UK governing the preparation and dissemination of Annual Accounts may differ from legislation in other jurisdictions.

ON BEHALF OF THE BOARD
DAVID HOLBORN, CHAIRMAN
29 FEBRUARY 2012

Introduction

In discharging its responsibilities to be accountable to the Society's members for the operation of the Society, the Board regards good corporate governance as extremely important. A revised UK Corporate Governance Code (formerly the "Combined Code on Corporate Governance") was issued by the Financial Reporting Council in June 2010 and applies to all accounting periods beginning on or after 29th June 2010. Although the Code is addressed to publicly quoted companies, the Society's Board considers it to be best practice to have regard to the Code when establishing and reviewing corporate governance arrangements.

A small working party was established at the end of 2010 to ensure the corporate governance procedures and processes within the Society are in acknowledgement of the Code. This report outlines the approach taken by the Society and how the Board considers it has demonstrated the principles of the Code.

The Board

The Society recognises that it must be headed by an effective Board which is responsible for the long-term success of the Society. The composition of the Board is detailed on pages 12 and 13. The Board's Terms of Reference were agreed by the Board in September 2011 and are reviewed on an annual basis. Key responsibilities, included within the Terms of Reference are set out below:

- The Board is responsible for agreeing the overall strategy for the Society, with the responsibility for implementing it being delegated to the Executive team. The Board is responsible for monitoring operational and financial performance in pursuit of the strategy;

  At a dedicated Board "Strategy Day" the Board agrees the strategic plan for the Society ensuring that the necessary financial and operational resources are in place so that the Society can meet its objectives and also that appropriate targets are set against which to review management performance;
- The Board is responsible for approving the budgets and forecasts, the adequacy of capital and liquidity plans, the adequacy of the systems of internal control and major capital expenditure. In addition, the Board is responsible for final approval of the interim and annual accounts on a going concern basis;
- In order to oversee the business, the Board receives and reviews various reports and management information from Board Committees and the Executive team;
- The Board is committed to formally review the effectiveness of the Board, on an annual basis, and by 31st October each year. The Board, at its meeting held on 31st October 2011, carried out this task. From time to time the Board will consider whether it would be beneficial to use outside consultants to assist in this review process. The Board also has responsibility for overseeing the evaluation process for all Committees of the Board; and
- The Executive team have been delegated the task of ensuring that the business operates in a compliant fashion and in accordance with the requirements of the Strategic Plan and Budget, Individual Capital Adequacy Assessment Process (ICAAP), Individual Liquidity Adequacy Assessment Process (ILAAP), and also progress action points deriving from the Board meetings, as appropriate.

There is a clear division of responsibilities at the head of the Society, between the running of the Board, and the Executive responsibility for the running of the Society's business. No one individual has unfettered powers of decision and the roles of Chairman and Chief Executive are exercised by different people within the Society.

There is a need for all Non Executive Directors to be deemed to be independent, a task which is carried out by the Nominations Committee (NomCo) as set out on page 17.

An effective Board should not necessarily be a comfortable place, with challenge, as well as teamwork, being an essential feature. Challenge by Non Executive Directors is something which is encouraged by the Chairman. A culture of openness exists within the Society and Non Executive Directors are encouraged to meet with members of the Executive team.

David Holborn was appointed Chairman of the Society on 1st January 2011 having first become a Director on 1st January 2003, and at the time of appointment was considered to be independent by the Board. The Board appointed Ron McCormick as Deputy Chairman and Senior Independent Director on 1st January 2011, who provides a sounding board for the Chairman and serves as an intermediary for the other Directors where necessary.

Board balance and independence is important and the Board should include an appropriate combination of Executive and Non Executive Directors (and in particular independent Non Executive Directors) such that no individual or small group of individuals can dominate the Board's decision taking. The composition of the Board, through NomCo, reflects an appropriate balance of skills, with several changes to the Board having taken place in 2010 and 2011. At the end of 2011 the Board comprised of seven Non Executive Directors and four Executive Directors.

Details of the various Board Committees in existence are set out later in this report.

Board Changes and Elections/Re-elections

It is recognised that changes need to be made to the Board from time to time, and changes during 2011 are set out in the Directors' Report on page 15.

Copies of the Terms of Engagement for all of the Society's Directors are available on request, and at the Annual General Meeting (AGM).

One aspect of the Code provides that all directors of FTSE 350 companies should be subject to annual election by shareholders, and the Building Societies Association considers that this requirement would apply to the twelve largest building societies. Therefore, in line with good corporate governance, and following a recommendation to the Board made by NomCo, all Directors will now offer themselves up for annual election/re-election at the Society's AGM. The biographies of all of the Directors are detailed on page 13.

Management Information

The Chairman is responsible for ensuring that the Directors receive accurate, timely and clear information. Members of the Board receive monthly Board and Management Information packs except in August when there is no meeting although, a Management Information pack is still issued. A rolling Board agenda is tabled at each meeting to ensure all key areas are covered appropriately during the year. Sufficient time is set aside to ensure that constructive discussion and challenge can take place. Once a year, the Board considers whether the regular Management Information which Directors receive is adequate, and this was deemed to be so at the meeting held on 27th April 2011. All Directors have access to independent professional advice, if required, and also access to the services of the Group Secretary.

Board Committees

The Board has Committees, all of which have their own Terms of Reference which are reviewed on an annual basis, further details of which are set out below. The Chairman of each Committee reports to the subsequent Board meeting on the matters discussed at each Committee meeting.

Similar to the Board, each Committee has carried out a review of its effectiveness, and where improvement opportunities have been identified, the individual Committees are responsible for tracking action points. 2011 was the first year that these reviews were performed and going forward they will be carried out on an annual basis. The effectiveness review for each Committee is summarised and presented to the Board for review.

Information concerning Director attendances at meetings is detailed on page 19.

Audit Committee

Members of Audit Committee are:

Richard Mayland (Committee Chairman), Ron McCormick, Phil Moorhouse and Catherine Vine-Lott.

The main responsibilities of the Committee as delegated by the Board:

- Financial reporting: to review the accounting policies, to monitor the integrity of the financial statements of the Group including the interim and annual reports, and any other formal announcements relating to the Group's financial performance, and reviewing significant financial reporting judgements contained therein. This includes ensuring the reports present a balanced and clear assessment of the Society's financial position and outlook;
- Internal control and risk management: to review the effectiveness of the Group's internal controls and risk management systems including those for ensuring compliance with the regulatory environment in which the Group operates. The Committee fulfils its responsibilities by reviewing reports prepared by the business and Group Risk, Internal Audit and External Audit on a regular basis;
- To review the Society's procedures for detecting fraud and irregularities and to ensure that arrangements are in place by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting, financial control or any other matters, and to ensure that arrangements are in place for independent investigation and appropriate follow up action;
- Internal audit: to monitor the effectiveness of the Group's internal audit function, its independence and objectivity. On a regular basis, the Head of Internal Audit has meetings with members of the Audit Committee only;
- External audit: to oversee the Group's relations with the external auditors, including appointment, removal, independence and remuneration. On an annual basis the Audit Committee meets with the External Auditors without management present; and
- The Society has established a policy on the use of the External Auditors for non-audit work which is considered and approved annually by the Audit Committee. The principal purpose of this policy is to ensure the continued independence and objectivity of the External Auditors.

Group Risk Committee

The Society has a separate Group Risk Committee, and further details of the Committee's responsibilities are set out in the Risk Management Report on page 22.

Members of Group Risk Committee are:

David Buffham (Committee Chairman), Ron McCormick, John Morris, Angela Russell and Jim Willens.

Remuneration Committee

The Society has a separate Remuneration Committee comprising only of Non Executive Directors, and further details of the Committee's membership and responsibilities are set out on page 20.

Nominations Committee (NomCo)

The Society has a separate NomCo comprising only of Non Executive Directors, and which operates within the Terms of Reference agreed by the Board. The Terms of Reference are reviewed annually and were last reviewed on 23 January 2012. The effectiveness of NomCo is also reviewed on an annual basis, having last been carried out on 9 December 2011.

The main objectives of NomCo are summarised as follows:

- To oversee the structure of the Board and Board Committees;
- To identify suitable candidates to fill Board vacancies;
- To ensure that the Board has the appropriate balance of skills, experience, independence and knowledge; and
- To oversee the Board's succession plan.

All key decisions of NomCo, for example, Board appointments, must also be ratified by the full Board.

Members of NomCo are:

David Holborn (Committee Chairman), David Buffham and Richard Mayland.

NomCo operates to a rolling agenda in order to ensure it discharges its full responsibilities. It normally meets at least three times each year however, in 2011 it met on six occasions in order to deal with two Board vacancies that occurred during the year.

NomCo is supported by the Chief Executive and Human Resources Executive who attend meetings in an advisory capacity only.

Appointments to the Board

NomCo follows a stringent recruitment process when making appointments to the Board. This process is tailored to meet the requirements of each particular vacancy.

The method of attracting candidates is adapted depending on the nature of the skills required for the vacancy. In 2011, NomCo sought the assistance of professional advisors to identify suitably qualified and experienced candidates to fill the two Board vacancies.

The Board was strengthened during the year by the appointment of two Non Executive Directors: Phil Moorhouse and John Morris. Both of the new Directors underwent the stringent selection process that was overseen by NomCo. This was followed by formal "Significant Influence Function" (SIF) interviews conducted by the Financial Service Authority in order that they become "Approved Persons".

During 2011 NomCo introduced new Role Descriptions and Terms of Engagement for Non Executive Directors to ensure that all Directors fully understand and comply with their role and the responsibilities of being a Non Executive Director of the Society.

Re-election to the Board

During the year NomCo recommended to the Board that all Directors should be required to seek annual re-election. This recommendation was subsequently ratified by the Board and therefore all directors will be seeking re-election at the Annual General Meeting, to be held on 25th April 2012.

Non Executive Directors are usually expected to serve two full three year terms, subject to satisfactory performance evaluations and re-election by members. They may also be proposed for a further third term but only in exceptional circumstances will Non Executive Directors be able to seek re-election when they have served nine years on the Board. During 2011, NomCo introduced a risk based succession plan which is reviewed at each meeting as part of the standing agenda.

Independence of Directors

The Terms of Engagement for Non Executive Directors require that they declare to the Society any other external interests.

NomCo carries out an annual review of the independence of Non Executive Directors, and the last review was carried out on 23rd January 2012. In the opinion of NomCo, and subsequently agreed by the Board, each of its Non Executive Directors is independent in both character and judgement. One of the Non Executive Directors, Catherine Vine-Lott (also known as Kate Avery), is Chairman of Openwork Holdings Limited, which pays commission to Newcastle Financial Services Limited, a wholly owned subsidiary company of Newcastle Building Society. The Board has determined that she is independent, notwithstanding the existence of this relationship, and under the Conflicts of Interest Policy, has undertaken to advise the Board if any conflict arises.

The Society recognises that it is good corporate governance to have a Senior Independent Director. This role has been held by the Society's Deputy Chairman, Ron McCormick since 1st January 2011 and it is intended that, subject to re-election, he continues in this role.

Assessment of Directors

All Directors are subject to a formal appraisal of their performance on an annual basis.

The Chairman conducts the appraisals of the Chief Executive and Non Executive Directors, the Chief Executive conducts the appraisals of the Executive Directors, and the Deputy Chairman/ Senior Independent Director leads the appraisal of the Chairman.

An assessment of the Directors was last undertaken during January and February 2012.

Skills and Continuous Development

All Directors are required, as part of their terms of engagement, to follow a process of continuous development to ensure that their skills and experience meet the needs of the Society and the regulatory environment in which it operates. The training and development plans of Non Executive Directors are reviewed at least annually during their performance appraisal.

The Committee oversees the on-going training and development of Non Executive Directors including a formal induction programme for newly appointed Directors, and this was fully reviewed during 2011. The Chief Executive oversees the programmes for Executive Directors.

In order to ensure that the Committee discharges its duties in this area effectively, a new skills matrix and training menu for Non Executive Directors was introduced during 2011.

Newcastle Strategic Solutions Limited (NSSL)

Members of NSSL are:

Ron McCormick (NSSL Chairman), John Warden, Nigel Wright (Non Executive Director only of NSSL) and Phil Grand (Customer Services Executive).

The main responsibilities of NSSL as delegated by the Board:

- To oversee the strategic direction of NSSL, to ensure this is consistent with the Society's agreed corporate strategy;
- To evaluate and monitor the financial and operational performance of NSSL against pre-determined objectives, which includes assessing performance in terms of sales, profitability, efficiencies, risk and compliance;
- Approval of new contracts where required under the Society's risk appetite and delegation of authorities;
- To ensure that NSSL complies with all relevant legislation and the appropriate regulations relating to its activities;
- To review NSSL's risk appetite statement on a regular basis, including the stressed scenarios for the NSSL business and the requirement for any additional capital;
- To approve the NSSL statutory accounts; and
- To consider and act upon the findings of internal and external audit reviews.

Board and Board Committee Membership Attendance Record

The table below sets out the number of meetings attended by Directors during 2011 with the numbers in brackets representing the maximum number of meetings the Director was eligible to attend.

Director	Board	Audit Committee	Group Risk Committee	Remuneration Committee	Nominations Committee	NSSL
David Holborn	12 (12)	-	-	-	6 (6)	-
Ron McCormick	12 (12)	6 (7)	6 (7)	-	-	5 (5)
Jim Willens	12 (12)	-	7 (7)	-	-	-
David Buffham	12 (12)	-	7 (7)	3 (3)	6 (6)	-
Ann Cairns	5 (7)	-	-	-	-	3 (3)
Richard Mayland	11 (12)	7 (7)	-	3 (3)	5 (6)	-
Phil Moorhouse	3 (3)	-	-	-	-	-
John Morris	3 (3)	-	1 (1)	-	-	-
Angela Russell	12 (12)	-	7 (7)	-	-	-
Gillian Tiplady	12 (12)	-	-	-	-	-
Catherine Vine-Lott	12 (12)	7 (7)	-	3 (3)	-	-
John Warden	12 (12)	-	-	-	-	5 (5)
Nigel Westwood	9 (11)	-	6 (6)	-	-	4 (5)

Relations with Members

Member engagement is at the heart of our strategy and the Society develops relationships with members on a number of different levels. The first and most obvious is through the AGM voting process where we encourage members, as owners of the business, to use their vote and we try to make this process as easy as possible.

Understanding what members think about our products and service is also extremely important. Members are encouraged to join our customer panel and we regularly consult with this group on a range of topics. We also use customer satisfaction surveys extensively and obtain feedback from different types of product holders and from customers who choose to deal with us through our main channels i.e. our branches, over the telephone, by post and via the internet. The information which is collected is used from these sources to help to develop and improve our offering.

Special members' seminars are held on a regular basis and are designed to provide our customers with useful information to help them understand and make sense of what is becoming an increasingly uncertain financial world. These seminars provide an excellent opportunity not only to speak to our members but also to interact and listen to their views.

Through our Corporate Social Responsibility (CSR) activities we are able to engage with both our members and the communities we serve. Whether it is helping to raise money for local worthy causes, or helping to develop financial education in local schools, we try hard to make a difference and improve the well being of people who live within our heartland.

Annual General Meeting

The Annual General Meeting provides an opportunity for members to question the Chairman, Chief Executive, Committee Chairmen and fellow Directors on the resolutions to be proposed at the meeting, the Annual Report and Accounts, and on any other aspect of the Society's business.

All members who are eligible to vote at the Annual General Meeting are encouraged to participate, either in person or by using their proxy voting form. The use of the online voting system is encouraged and for each vote placed online, the Society donates 10p to its charity of the year. All votes are counted by independent scrutineers. As soon as practicable after the AGM, full details of the results of the voting are placed on the Society's website.

ON BEHALF OF THE BOARD
DAVID HOLBORN, CHAIRMAN
29 FEBRUARY 2012

REMUNERATION COMMITTEE REPORT

The Remuneration Committee operates within the Terms of Reference (TOR) agreed by the Board. The TOR are reviewed annually and were last reviewed on 27th February 2012. The effectiveness of the committee is also reviewed on an annual basis and was last reviewed on 28th November 2011.

The main objectives of the committee are summarised as follows:

- To ensure compliance with the FSA Remuneration Code ("the Code");
- To consider and make recommendations to the Board on executive remuneration and conditions of employment; and
- To consider and make recommendations to the Board on the general framework of staff bonus schemes.

Composition of the Committee

The committee consists solely of Non Executive Directors; Catherine Vine-Lott (known as Kate Avery and Chairman of the committee), David Buffham and Richard Mayland. The attendance record of the committee members for 2011 is shown on page 19. The committee operates to a rolling agenda in order to ensure it fully discharges its responsibilities. It normally meets at least three times each year. The committee is supported by the Chief Executive and Human Resources Executive who attend meetings in an advisory capacity only. The Chief Executive does not attend any part of a meeting where his own remuneration is being discussed.

FSA Remuneration Code

On 17th December 2010, the FSA published the final rules for the Code. The Society was governed by the new code with effect from 1st January 2011 but, in view of the short timescale between the announcement and the effective date, the FSA established a transitional period until July 2011 for organisations, such as the Society, to comply fully with the Code. The FSA also issued guidance on the application of the Code throughout the year, as many aspects appeared not applicable to organisations, such as the Society. The Society is categorised as 'Tier 2' for the purposes of the Code (organisations with capital exceeding £100m but not exceeding £750m). The key requirements of the Code affecting the Society are summarised below:

- To establish a Remuneration Committee;
- To maintain a Remuneration Policy Statement;
- To maintain a list of employees whose professional activities have a material impact on its risk profile – such staff are known as 'FSA Code Staff'; and
- To defer parts of variable pay (bonuses) which exceed certain thresholds.

The Remuneration Committee undertook a thorough review of remuneration policies and processes during 2011 and consider that the Society fully complies with the requirements of the Code.

FSA Code Staff

The Committee considered that there were 15 employees that should be categorised as Code Staff and these include:-

- All Executive Directors (4);
- Sales and Marketing Executives (2);
- Executives and senior managers responsible for key control functions (5) – Group Risk Executive, Head of Business Assurance, Head of Compliance, Money Laundering Reporting Officer and Senior Underwriting Manager; and
- All other Executives (4).

A summary of the remuneration of Code Staff during 2011 and the business areas in which they operate is shown on page 21.

Remuneration Strategy

The Society's remuneration Strategy can be summarised as set out below:

Basic Salaries

Remuneration packages are normally set at a level to attract, motivate and retain Executives, Officers and staff of the Society of the calibre necessary to oversee the operations of the Society. Basic salaries are normally set by taking into account salary levels within similar sized financial services organisations and the market as a whole, so as to attract and retain the skills levels that are appropriate to manage the diverse challenges faced by the Society.

General salary increases were not awarded in 2009 or 2010 due to the prevailing economic conditions. A moderate increase of 2.5% was awarded to all staff, except Directors, in April 2011.

Performance Related Bonuses

In light of the continuing difficult trading conditions facing the Society, the payment of bonuses to Executive Directors, Executives and Remuneration Code staff has been suspended since 2007. However, in December 2011 a small bonus of £200 was paid to all staff including four Remuneration Code staff (Senior Managers) but excluding Executive Directors and Executives. Sales related incentive and bonus schemes have continued to be operated for most sales staff. Bonus schemes (when operated) are set in such a way as to ensure that they promote the financial strength of the Society, do not reward failure and that they do not encourage any officer of the Society to take risks outwith the Society's risk appetite.

The Committee introduced a monitoring process during 2011 in order to ensure that all bonus payments comply with the Code and the Society's Remuneration Policy Statement.

The Committee has approved a Corporate Bonus Scheme for 2012 in which all staff, including Code Staff, will participate. The scheme will be based upon the Society achieving the main objectives set by the Board, which will be monitored via Key Performance Indicators. The size of a bonus awarded, if any, will be determined by the Board on the recommendation of the Committee. The Board therefore has total control of the scheme and will ensure that it does not result in inappropriate bonuses being paid.

The performance of all staff, including Code Staff is reviewed at least annually via a formal appraisal process.

Exceptional Items

The Committee is required to report any exceptional items such as 'sign-on' or severance payments made to Code Staff. It is confirmed that there were no such payments made during the year other than relocation expenses for the Chief Executive and Group Risk Executive which were agreed at the times of their appointments.

Pensions

All staff (including Executive Directors and Executives) are eligible for membership of the Newcastle Building Society Group Personal Pension Scheme, which is a defined contribution scheme. The Newcastle Building Society Pension & Assurance Scheme (a 'defined benefit' scheme) has been closed to active membership since November 2010 and had been closed to new entrants since 2000. None of the current directors participated in this particular scheme.

Other Benefits

All Executive Directors and Executives receive a range of taxable benefits, which include a motor vehicle or cash equivalent, private health care and the ability to participate in a concessionary mortgage scheme. Life cover for a lump sum on death in service is also provided. No Executive participated in the concessionary mortgage scheme during the year although some had mortgages with the Society on the same commercial terms as members of the Society.

Service Contracts

It is the Society's policy to provide six months notice of termination for all Executive Directors. All of the current Executive Directors therefore have such notice periods. Five of the longer serving Executives have service agreements, which provide for 12 months notice of termination from the Society. The remaining Executives all have notice periods of 6 months. It is the policy to employ all newly appointed executives with notice periods of 6 months. There are no contracts of employment for Non Executive Directors and no compensatory terms for loss of office.

Policy on Remuneration of Non Executive Directors

Non Executive Directors fees are set at a level appropriate to reflect the skills and time required to oversee the Society's operations and progress. Non Executive Directors receive a base fee and additional fees depending upon the Board Committees on which they sit or chair.

Fees are normally reviewed annually in light of those paid to directors of other similar financial services organisations. The Non Executive Directors do not determine their own fees. The CEO recommends the fees for Non Executive Directors. The Remuneration Committee then agree any such recommendations before they are ratified by the full Board i.e. by Non Executive Directors and Executive Directors. Fees were not subject to a general increase in 2011. Non Executive Directors do not participate in any bonus or pension schemes.

Directors' Emoluments (Audited)

Emoluments of the Society's Directors from the Society and its subsidiary undertakings are detailed below:

	Salary or fees	Annual bonus	Pension contributions to defined contribution scheme Note 1	Other benefits	Increase in accrued pension benefits earned in year (excl. inflation) in defined benefit scheme	Total 2011 contractual benefits	'One off' expenses - relocation costs	Total 2011 including 'one off' expenses	2010 total
	£000	£000	£000	£000	£000	£000	£000	£000	£000
Executive Directors									
C Greaves (resigned 31 July 2010)	-	-	-	-	-	-	-	-	82
W Lee (resigned 31 July 2010)	-	-	-	-	-	-	-	-	90
AM Russell (appointed 1 July 2010) Note 2	145	-	13	10	-	168	-	168	84
CJ Seccombe (retired 12 March 2010)	-	-	-	-	-	-	-	-	57
G Tiplady (appointed 11 January 2011)	120	-	8	11	-	139	-	139	-
JH Warden (appointed 7 October 2010)	140	-	13	11	-	164	-	164	41
G Wilkinson (resigned 9 April 2010)	-	-	-	-	-	-	-	-	21
JH Willens See notes 3 & 4	260	-	-	37	-	297	12	309	362
	665	-	34	69	-	768	12	780	737
Non Executive Directors									
DJ Buffham (appointed 24 May 2010)	38	-	-	-	-	38	-	38	20
AM Cairns (resigned 30 June 2011)	16	-	-	-	-	16	-	16	9
CJ Hilton (retired 31 December 2010)	-	-	-	-	-	-	-	-	64
FD Holborn (appointed Chairman 1 January 2011)	62	-	-	-	-	62	-	62	45
RD Mayland	43	-	-	-	-	43	-	43	40
RJ McCormick (appointed Deputy Chairman/Senior Independent Director 1 January 2011)	50	-	-	2	-	52	-	52	42
J Morris (appointed 31 October 2011)	6	-	-	-	-	6	-	6	-
PJ Moorhouse (appointed 31 October 2011)	6	-	-	-	-	6	-	6	-
JM Pott (retired 31 December 2010)	-	-	-	-	-	-	-	-	33
CRR Vine-Lott (appointed 1 January 2010)	40	-	-	1	-	41	-	41	34
NA Westwood (retired 28 November 2011)	30	-	-	-	-	30	-	30	33
Total for Non Executive Directors	291	-	-	3	-	294	-	294	320
Total for all Directors	956	-	34	72	-	1,062	12	1,074	1,057

Notes:

1. The Society introduced an HMRC approved Pensions Salary Sacrifice Scheme for all staff during 2011. Some of the Executive Directors have elected to participate in the scheme however, their gross salaries and pension contributions (before salary sacrifice is applied) are shown.
2. Mrs A.M. Russell's salary was increased to £150,000 on 1 April 2011 however, Mrs Russell has elected not to accept the increase yet.
3. Mr. J.H. Willens was set a relocation allowance of £90,000 inclusive of tax and national insurance. Mr Willens has now been fully reimbursed for the cost he incurred up to that limit.
4. Mr. J.H. Willens has elected to take his pension contribution amounting to £23,400 as a cash payment. He is liable for his own Tax and National Insurance Contributions on this payment.

Summary of the Remuneration of FSA Code Staff

A summary of the remuneration of Code Staff during 2011 and the business areas in which they operate is shown below. No comparative analysis is available for previous years as the categorisation of FSA Remuneration Code staff was introduced in 2011. Such analysis will be provided in future years.

Category	Typical Functions	Number in Category	*Fixed Remuneration	Variable Remuneration	Deferred Remuneration	Total Remuneration
			£000	£000	£000	£000
Executive Directors	CEO, Finance Director, Operations Director, Business Services Director	4	768	12	-	780
Sales & Marketing Executives		2	212	-	-	212
Control Functions	Business Assurance, Risk Management, Compliance, Underwriting	5	328	15	-	343
Other Executives	Treasury, Information Technology, Operations, Human Resources	4	379	-	-	379
Total		**15**	**1,687**	**27**	**-**	**1,714**

*Includes benefits and pension contributions.

CATHERINE VINE-LOTT
CHAIR - REMUNERATION COMMITTEE
29 FEBRUARY 2012

Overview
Underpinning every well run business is sound corporate governance and a robust risk management framework.

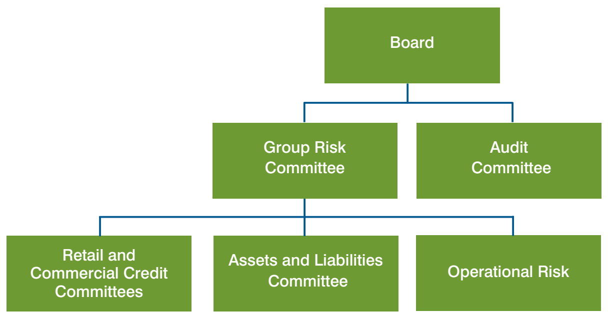
The Society's Group Risk Committee oversees management of risk across the Group and is supported by the Group Risk department and various sub-committees. The Society and Group risk management framework operates under the "three lines of defence" principle.

The first line of defence is within departments, business units and subsidiaries where Executives, Managers and staff have responsibility for risk management and ensuring adequate controls are in place to mitigate risk.

The second line of defence is provided by the Group Risk Committee and supporting sub-committees together with oversight by the Group Risk department.

The third line of defence is provided by Business Assurance and the Audit Committee, which are responsible for reviewing the effectiveness of the first and second lines of defence.

Risk Governance
Risk Governance Structure



The Group Risk Committee is a Board Committee that has responsibility, under its detailed terms of reference, for considering and co-ordinating the approach to risk management across the Group in the following key areas:

- Oversight of risk appetite, risk management strategy and framework;
- Oversight of compliance with risk policy statements and approval of changes to those policies on an annual basis, or more frequently where market conditions require;
- Oversight of the Retail and Commercial Credit Committees;
- Oversight of Operational Risk and the governance of Operational Risk by the Executive;
- Oversight of the Assets & Liabilities Committee;
- Review and assessment of the adequacy of risk management information to monitor and control risks;
- Approval of new initiatives and projects, including risks to which the Group is exposed and the amount of capital required to cover those risks;
- Consideration and approval of the top risks for the Society and Group including low likelihood, high impact risks;
- Approval and recommendation to the Board of the Internal Capital Adequacy Assessment Process (ICAAP);
- Approval and recommendation to the Board of the Individual Liquidity Adequacy Assessment (ILAA); and
- Consideration and approval of stress testing scenarios including reverse stress tests.

The Group Risk Committee normally meets six times a year and is supported by four Executive committees that meet on a monthly basis, as follows:

The Retail Credit Committee is responsible for credit risk across the Group arising from the retail mortgage portfolio as follows:

- Review of lending policy statements and compliance therewith;
- Review of risk metrics and management information for the retail mortgage portfolio;
- Review and approval of arrears and possessions policy (including breach policies) and compliance therewith;
- Monitor compliance with controls and limits set out in the lending policy statements;
- Sanction of larger loans in accordance with the lending policy statement and limits set on higher value loans;
- Review and approval of new types of mortgage products including ensuring return on capital employed meets internal benchmarks and that risks have been effectively considered and mitigated;
- Performance review of underwriters, panel managers and brokers;
- Review of credit risk profile of existing retail mortgage book including trends on arrears (both historical and against the market), losses and capital requirements;
- Review of key economic data impacting credit risk including trends on unemployment, house prices, arrears rates, affordability, inflation and confidence indices;
- Review of credit control activity levels including customer contact volumes, forbearance measures granted, disturbed payment patterns and changes in behavioural scoring. This includes reviewing the effectiveness of forbearance measures granted to customers;
- Review and approval of stress testing assumptions and outputs including monitoring of trends;
- Review of arrears and possessions reports including causal factors and lessons learned; and
- Review of Mortgage Indemnity Guarantee (MIG) policy arrangements.

The Commercial Credit Committee is responsible for credit risk across the Group's non-retail mortgage portfolio as follows:

- Review of non-retail policies and compliance therewith;
- Review of risk metrics and management information for the non-retail mortgage portfolio;
- Monitor compliance with controls and limits set out in the policies;
- Review of credit risk profile of existing mortgage book including trends on arrears, losses and capital requirements;
- Review of key performance indicators in relation to the delivery of the commercial strategy;
- Review of risk indicators and risk factors. This includes review of tenant and borrower watch-lists and sector specific issues;
- Approval of annual reviews, breach reports and loan restructures in accordance with the delegation of authorities;
- Review and approval of stress testing assumptions and outputs including monitoring of trends;
- Review of key trends in commercial property markets including values, yields and levels of activity;

- Approval of changes to the Risk Grade Scorecard and monitoring the effectiveness thereof; and
- Interface with other Committees including Watch Committee, Provisioning Committee and Risk and Recovery Committee.

Operational Risk is overseen by the Executive Committee (see below) and its remit includes:

- Review of operational risk policy and other related risk and compliance policy statements;
- Monitoring compliance with policies;
- Review of risk indicators in risk dashboards including risk events trends across the business, actions being taken on significant risk events, and status of project risks;
- Review of compliance risk indicators, via monthly dashboards, including in relation to Mortgage Conduct of Business (MCOB), Treating Customers Fairly (TCF), Complaints, Information Security and Fraud Risk Policy compliance;
- Approval of corporate insurance policy statement, status of claims and effectiveness of policies at mitigating operational risk; and
- Review of business continuity policy, disaster scenarios and results of annual disaster recovery test.

The Executive Committee includes the Executive Directors and other officers listed on page 70.

The Assets and Liabilities Committee is responsible for all aspects of treasury risk management including liquidity risk, market risk, treasury counterparty credit risk and balance sheet management. The ALCO terms of reference covers the following areas:

- Review of Treasury Policy Statement and compliance therewith;
- Review of treasury dealing strategy and compliance with risk appetite statement;
- Management of balance sheet assets and liabilities;
- Review of risk dashboards covering all aspects of treasury, liquidity, funding and interest rate risk;
- Setting of interest rate view;
- Review of wider treasury markets and economic backdrop to assess the impact on the Society's funding and liquidity requirements;
- Detailed review and agreement of cashflow requirements across the business on a rolling 24 month basis;
- Monitoring of interest rate risk and hedging activity, including profit performance;
- Review of treasury counterparty limits and country limits including assessing the impact of ratings changes;
- Review of funding including sources, mix and compliance with limits;
- Review of liquidity requirements and compliance with limits;
- Review and approval of results of liquidity stress testing scenarios; and
- Review and approval of product pricing including rate changes, mix of new business and maturity defence strategy.

The Group has detailed risk management policies setting out how risk is managed across the Group, including specific risk appetite statements. The risk appetite statement outlines for each risk area the basis on which risks are accepted or excluded. This forms the basis for various limits and key criteria, set out in the policies that must be followed in order to mitigate risk exposures. These limits are embedded into daily, weekly and monthly management and Board reporting in order to monitor compliance with the Society's risk profile.

Other governance structures exist as outlined in the Report of the Directors on Corporate Governance on pages 16 to 19.

Risk Appetite
The Board approved risk appetite statement considers profit and loss in a moderate stress scenario; capital adequacy in a severe stress; and the existence of "tail risks" – low likelihood high impact risks. It also sets out limits in relation to liquidity, Solutions business, credit risk and operational risk. Policies, including credit risk policies, treasury policies and operational risk policies set limits to ensure that the Society complies with its Board approved risk appetite statement. The risk appetite statement is subject to annual review and approval by the Board and performance against the risk appetite is monitored on a quarterly basis by the Board.

Credit Risk
Credit risk is the risk that a treasury counterparty, debtor or borrower will not be able to meet their obligations as they fall due. Credit risk arises primarily on retail and commercial loans, and on treasury assets held for liquidity purposes.

The Group has comprehensive policies in place covering credit risk management that set out criteria that must be followed before funds are advanced and incorporate limits for concentration risk arising from, inter alia, large exposures, geographical areas and sectors. Return on Capital Employed benchmarks are set to ensure that reward is commensurate with the risk taken; once the risk is considered acceptable to the Society.

For retail lending the Group operates manual underwriting procedures to prudent policy criteria, including restrictions on loan to value, income multiples/rental cover, and affordability criteria. The Group does not undertake sub-prime or self-certification lending. The level of Buy to Let (BTL) lending has been capped via the application of portfolio limits that reflect the risk appetite for this type of lending.

The Group no longer undertakes new commercial lending. The Commercial Risk division continues to monitor the performance of the commercial and residential investment portfolios through annual reviews and key risk management information, including tenant and borrower watchlists, arrears trends, breach reports and general market and sector specific information. The Society has a range of Committees established to oversee risk within the Commercial portfolio including Commercial Credit Committee, Risk and Recovery Committee, Watch Committee and the Provisioning Committee.

A specialist collections division operates, which has a more targeted approach to collections and recovery for commercial and BTL portfolio borrowers, featuring a rapid response where difficulties are identified such as late payments, tenant failure, ratings downgrades and general negative market news. The Society has a credit risk management information department that monitors and reports credit risk within the mortgage portfolio, including stress testing.

Credit risk on liquid assets is controlled via the operation of counterparty, sector, instrument, and country limits for treasury assets. Counterparty limits are set with regard to external ratings agency assessments with the Society investing only in highly rated financial institutions or other building societies. The Society supplements ratings agency information with more extensive credit assessment procedures for counterparty limits including market information and movement on credit default swap (CDS) spreads for countries and individual counterparties. Treasury counterparty risk is monitored within Treasury Middle Office in accordance with the Treasury Risk Policy. All treasury counterparty ratings, CDS spreads and market information are monitored real time and prompt action is taken where volatile market conditions require a tightening of criteria.

Liquidity Risk

Liquidity risk is the risk of loss or failure caused by the Group being unable to meet its liabilities or commitments as they fall due, or to be able to do so only at excessive cost. The nature of the business of a building society is to lend longer-term (typically up to 25 years) and fund with short term savings accounts. This leads to a maturity mismatch between assets and liabilities.

The Group's liquidity policy is to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding and enable the Group to meet its financial obligations when they fall due. This is achieved by maintaining a prudent level of liquid assets and ensuring that funding and lending plans are balanced.

The Society has continued to invest in liquidity of the highest quality and further details are provided within the Business Review on page 9.

The Society has complied with the Individual Liquidity Guidance set by the FSA throughout 2011.

Operational Risk

Operational risk is the risk of loss, resulting from inadequate or failed internal processes, people and systems, or from external events. For the Group this definition includes legal risk, strategic risk and reputational risk.

The Group has a well established operational risk framework with a detailed Operational Risk Policy that sets out the framework for operational risk, including the measurement and management of risk, operational risk appetite, tracking of risk events and operational losses, timescales for implementation of action plans and escalation procedures for more serious risk events that require immediate action to mitigate loss.

A key feature of the Group's operational risk framework is that key risks and controls are identified for all areas of the business ranging from the high level risks, discussed at Board level, down to the risks within individual departments. Risk assessments remain the responsibility of the relevant departmental managers and Executives, and are updated regularly for new risks, the results of risk events and following internal audit reviews.

Risks are scored in terms of the impact and probability of the risk arising and are scored before and after considering the impact of controls. The operational risk system is also utilised by Business Assurance with the audit inspection plan based on high scoring risk areas or where there is significant reliance on key controls to mitigate the impact of otherwise significant risks. Group Corporate Insurance policies are also negotiated with full regard to the key risks within the Group requiring greater mitigation. The key risks also dovetail in to stress testing and reverse stress testing scenarios, and production of the ICAAP and ILAA.

Market Risk

The principal market risk to which the Group is exposed is interest rate risk. The Group has no exposure to foreign currency and only a very moderate direct net exposure to equities through a small shareholding in Standard Life arising from the de-mutualisation of the insurance company in 2006. The Group has an indirect exposure to the performance of equities through its defined benefit pension scheme.

Interest rate risk arises on mortgages, savings and treasury instruments due to timing differences on re-pricing of assets and liabilities and the imperfect matching of interest rates between different asset and liability types. This risk is managed using financial instruments including derivatives. Natural hedging strategies are also utilised e.g. matching two year fixed rate mortgages with two-year fixed rate bonds.

The Group's risk appetite for interest rate risk is documented in the Treasury Policy Statement and includes limits for the maximum adverse impact on net interest margin, maximum value at risk, basis risk, as well as limits to minimise gaps in specific time buckets.

The table below describes the activities undertaken by the Group and the derivatives used to manage the associated risks.

ACTIVITY	RISK	TYPE OF HEDGE
Fixed rate savings products and funding instruments	Sensitivity to fall in interest rates	Fair value interest rate swap
Fixed rate mortgage products and funding investment instruments	Sensitivity to rise in interest rates	Fair value interest rate swap
Index-linked savings products	Sensitivity to changes in underlying indices	Fair value hedges with index-linked swaps
General balance sheet management	Sensitivity to different types of interest rates moving in different ways e.g. LIBOR and Base Rate	Basis risk swaps

Derivatives are only used by the Group in accordance with the Building Societies Act 1986. These instruments are not used for trading or speculative purposes and their sole purpose is to mitigate risks arising from movement in interest rates or indices.

Note 34 gives details of the derivative financial instruments held at 31 December 2011.

Capital Management

Capital adequacy is monitored on a monthly basis by the Board and the 3 year capital plan has been updated on a regular basis between ICAAP reviews against the background of changing economic circumstances. The Group maintains its capital at a level in excess of the Individual Capital Guidance notified by the FSA.

Under Basel II Pillar III (disclosure) the Group is required to publish further information about risk exposures. The Group's Pillar III disclosures will be published on the Society's website (www.newcastle.co.uk) shortly after the publication of these accounts.

DAVID BUFFHAM
CHAIR - GROUP RISK COMMITTEE
29 FEBRUARY 2012

We have audited the Group and Society Annual Accounts of Newcastle Building Society for the year ended 31 December 2011 which comprise Group and Society Income Statements, Group and Society Statements of Comprehensive Income, Group and Society Balance Sheet, Group and Society Statements of Movements in Members' Interests and the Group and Society Cash Flow Statements and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Respective Responsibilities of Directors and Auditors

As explained more fully in the Statement of Directors' Responsibilities set out on page 15 of the Annual Report and Accounts. The Directors are responsible for the preparation of the Annual Accounts which give a true and fair view. Our responsibility is to audit and express an opinion on the Annual Accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

This report, including the opinions, has been prepared for, and only for, the Society's Members as a body in accordance with Section 78 of the Building Societies Act 1986 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Scope of the Audit of the Annual Accounts

An audit involves obtaining evidence about the amounts and disclosures in the Annual Accounts sufficient to give reasonable assurance that the Annual Accounts are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and Society's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the Annual Accounts. In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on Annual Accounts

In our opinion the Annual Accounts:

- Give a true and fair view, in accordance with IFRSs as adopted by the European Union, of the state of the Group's and the Society's affairs as at 31 December 2011 and of the Group's and the Society's income and expenditure and cash flows for the year then ended; and
- Have been prepared in accordance with the requirements of the Building Societies Act 1986 and, as regards the Group Annual Accounts, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Building Societies Act 1986

In our opinion:

- The Annual Business Statement and the Directors' Report have been prepared in accordance with the requirements of the Building Societies Act 1986;
- The information given in the Directors' Report for the financial year for which the Annual Accounts are prepared is consistent with the accounting records and the Annual Accounts; and
- The information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Building Societies Act 1986 requires us to report to you if, in our opinion:

- Proper accounting records have not been kept by the Society; or
- The Group and Society Annual Accounts are not in agreement with the accounting records; or
- We have not received all the information and explanations and access to documents we require for our audit.

KARYN LAMONT (SENIOR STATUTORY AUDITOR)
FOR AND ON BEHALF OF PRICEWATERHOUSECOOPERS LLP
CHARTERED ACCOUNTANTS AND STATUTORY AUDITORS
NEWCASTLE UPON TYNE
29 FEBRUARY 2012

Income Statements for the year ended 31 December 2011

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Interest receivable and similar income	2	**103.2**	101.0	**103.7**	100.6
Interest payable and similar charges	3	**(85.7)**	(83.2)	**(85.7)**	(82.1)
Net interest income		**17.5**	17.8	**18.0**	18.5
Other income	4	**27.3**	20.9	**20.6**	15.0
Other charges	4	**(0.7)**	(2.1)	**(0.6)**	(1.6)
Gains less losses on financial instruments and hedge accounting		**0.6**	-	**0.6**	-
Dividend income	5	**-**	-	**3.0**	3.1
Total operating income		**44.7**	36.6	**41.6**	35.0
Administrative expenses	6	**(32.6)**	(33.7)	**(30.1)**	(31.3)
Depreciation	17	**(2.9)**	(3.2)	**(2.7)**	(2.9)
Operating profit / (loss) before impairments, provisions and exceptional items		**9.2**	(0.3)	**8.8**	0.8
Impairment (charge) / credit on loans and advances to banks	11	**(0.2)**	2.1	**(0.2)**	2.1
Impairment credit on debt securities	12	**0.9**	0.3	**0.9**	0.3
Impairment charges on loans and advances to customers	14	**(12.3)**	(1.8)	**(12.3)**	(1.8)
FSCS levy	27	**(1.4)**	-	**(1.4)**	-
Repositioning Programme provision for charges	27	**-**	(4.0)	**-**	(4.0)
Other provisions for liabilities and charges	27	**-**	(1.0)	**-**	(1.0)
Gain on disposal of Prepaid Cards Business	10	**3.9**	-	**3.9**	-
Profit / (loss) for the year before taxation		**0.1**	(4.7)	**(0.3)**	(3.6)
Taxation (expense) / credit	8	**(0.8)**	1.0	**-**	1.5
Loss after taxation for the financial year		**(0.7)**	(3.7)	**(0.3)**	(2.1)

The notes on pages 32 to 68 form part of these Accounts.

Statements of Comprehensive Income for the year ended 31 December 2011

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Loss for the financial year		**(0.7)**	(3.7)	**(0.3)**	(2.1)
Other comprehensive income / (expense)					
Movement on available for sale reserve		**(0.5)**	1.0	**(0.5)**	1.0
Actuarial loss on retirement benefit obligations	32	**(3.9)**	(0.5)	**(3.9)**	(0.5)
Income tax relating to components of other comprehensive income	19	**1.1**	(0.1)	**1.1**	(0.1)
Other comprehensive (expense) / income for the financial year, net of tax		**(3.3)**	0.4	**(3.3)**	0.4
Total comprehensive expense for the financial year		**(4.0)**	(3.3)	**(3.6)**	(1.7)

The notes on pages 32 to 68 form part of these Accounts.

Balance Sheets at 31 December 2011

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
ASSETS					
Cash and balances with the Bank of England		**162.3**	204.6	**162.3**	204.6
Loans and advances to banks	11	**254.1**	172.4	**254.0**	155.0
Debt securities	12	**764.5**	446.9	**764.5**	446.9
Derivative financial instruments	34	**44.3**	34.2	**44.3**	34.2
Loans and advances to customers	14	**2,976.6**	3,325.1	**2,951.0**	3,221.9
Fair value adjustments for hedged risk	15	**57.9**	50.8	**57.9**	48.0
Assets pledged as collateral	13	**85.1**	105.4	**85.1**	105.4
Investment in subsidiaries	16	**-**	-	**47.5**	56.7
Property, plant and equipment	17	**23.9**	26.1	**15.3**	17.1
Investment properties	18	**15.9**	14.3	**-**	-
Deferred tax assets	19	**13.6**	13.3	**13.5**	13.2
Other assets	20	**20.3**	25.7	**30.8**	47.1
TOTAL ASSETS		**4,418.5**	4,418.8	**4,426.2**	4,350.1

The notes on pages 32 to 68 form part of these Accounts.

Balance Sheets at 31 December 2011

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
LIABILITIES					
Due to members	22	**3,761.4**	3,593.0	**3,761.4**	3,593.0
Fair value adjustments for hedged risk	15	**28.7**	20.8	**28.7**	20.8
Due to other customers	23	**157.2**	220.8	**160.3**	224.6
Deposits from banks	24	**107.6**	150.1	**107.6**	150.1
Debt securities in issue	25	**16.0**	86.5	**16.0**	15.5
Derivative financial instruments	34	**57.4**	54.2	**57.4**	51.2
Income tax liabilities		**0.5**	0.6	**0.3**	0.3
Other liabilities	26	**19.0**	21.5	**23.3**	23.2
Provisions for liabilities and charges	27	**8.4**	6.3	**8.4**	6.3
Retirement benefit obligations	32	**1.2**	-	**1.2**	-
Deferred tax liabilities	19	**0.7**	0.7	**-**	-
Subordinated liabilities	28	**58.7**	58.6	**58.7**	58.6
Subscribed capital	29	**29.6**	29.6	**29.6**	29.6
Reserves		**172.1**	176.1	**173.3**	176.9
TOTAL LIABILITIES		**4,418.5**	4,418.8	**4,426.2**	4,350.1

These Accounts were approved by the Board of Directors on 29 February 2012 and signed on its behalf by:

DAVID HOLBORN, CHAIRMAN
RICHARD MAYLAND, CHAIRMAN OF AUDIT COMMITTEE
JIM WILLENS, CHIEF EXECUTIVE

The notes on pages 32 to 68 form part of these Accounts.

Statements of Movement in Members' Interests for the year ended 31 December 2011

GROUP

	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2011	174.6	1.5	176.1
Movement in the year	(3.6)	(0.4)	(4.0)
At 31 December 2011	**171.0**	**1.1**	**172.1**

	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2010	178.6	0.8	179.4
Movement in the year	(4.0)	0.7	(3.3)
At 31 December 2010	**174.6**	**1.5**	**176.1**

SOCIETY

	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2011	175.4	1.5	176.9
Movement in the year	(3.2)	(0.4)	(3.6)
At 31 December 2011	**172.2**	**1.1**	**173.3**

	General reserve £m	Available for sale reserve £m	Total £m
At 1 January 2010	177.8	0.8	178.6
Movement in the year	(2.4)	0.7	(1.7)
At 31 December 2010	**175.4**	**1.5**	**176.9**

Movement in the year reflects changes disclosed in the Statements of Comprehensive Income.

The notes on pages 32 to 68 form part of these Accounts.

Cash Flow Statements for the year ended 31 December 2011

	Note	GROUP		SOCIETY	
		2011 £m	2010 £m	**2011 £m**	2010 £m
Cash inflows / (outflows) from operating activities	30	**314.7**	(92.3)	**318.4**	(93.2)
Payment into defined benefit pension scheme		**(2.4)**	(0.4)	**(2.4)**	(0.4)
Net cash inflows / (outflows) from operating activities		**312.3**	(92.7)	**316.0**	(93.6)
Cash (outflows) / inflows from investing activities					
Purchase of property, plant and equipment		**(1.0)**	(1.4)	**(1.0)**	(1.2)
Purchase of investment properties		**(1.7)**	(0.2)	**-**	-
Sale of property, plant and equipment		**0.4**	1.6	**0.2**	1.6
Increase in loans to subsidiary undertakings		**-**	-	**9.0**	6.9
Purchase of investment securities		**(939.6)**	(832.0)	**(939.6)**	(832.0)
Sale and maturity of investment securities		**645.2**	612.5	**645.2**	612.2
Proceeds on disposal of Prepaid Card Business		**7.5**	-	**7.5**	-
Dividend received		**-**	-	**3.0**	3.1
Net cash outflows from investing activities		**(289.2)**	(219.5)	**(275.7)**	(209.4)
Net cash outflows from financing activities					
Interest paid on subordinated liabilities		**(2.2)**	(1.1)	**(2.2)**	(1.1)
Interest paid on subscribed capital		**(3.6)**	(3.6)	**(3.6)**	(3.6)
Repayments under finance lease agreements		**(0.2)**	(0.2)	**(0.1)**	(0.2)
Net cash outflows from financing activities		**(6.0)**	(4.9)	**(5.9)**	(4.9)
Net increase / (decrease) in cash		**17.1**	(317.1)	**34.4**	(307.9)
Cash and cash equivalents at start of year		**360.9**	678.0	**343.5**	651.4
Cash and cash equivalents at end of year	30	**378.0**	360.9	**377.9**	343.5

The notes on pages 32 to 68 form part of these Accounts.

1 Significant Accounting Policies

Basis of Preparation
The Accounts have been prepared in accordance with International Financial Reporting Standards (IFRSs) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC); as adopted for use in the EU; and with those parts of the Building Societies (Accounts and Related Provisions) 1998 applicable to building societies reporting under IFRSs.

The difficult conditions experienced in global, and particularly European, financial markets have deepened during 2011 with continued pressures on liquidity. The Society has maintained, throughout the year, high levels of liquidity and funding from retail savings, further reducing its requirement for wholesale funding. It is expected that this situation will not change significantly in the foreseeable future.

The Board has reviewed medium and long term plans with particular emphasis on examining the forecast liquidity, capital and profit of the Group and the risks to those forecasts through a variety of stress testing scenarios. The outcome of this review is that the Directors are satisfied that the Society and the Group have adequate resources to continue in business for the foreseeable future. Accordingly, the financial statements of the Society and the Group have been prepared on a going concern basis.

The Accounts have been prepared under the historical cost convention except for those financial assets and hedging instruments which are required by IAS 39 to be carried at fair value. A summary of the Group's principal accounting policies is set out below:

Basis of Consolidation
The Group Accounts include the results of the Society and its subsidiary undertakings, all of which have accounting periods ending 31 December. Subsidiaries are entities over which the Society has the power to control the financial and operating policies so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that control ceases. Upon consolidation, inter-company transactions, balances and unrealised gains on transactions are eliminated. The accounting policies of subsidiaries are consistent with Group accounting policies.

Income Recognition
Interest Income and Expense
Interest receivable and interest payable for all interest-bearing financial instruments are recognised within 'Interest receivable and similar income' and 'Interest payable and similar charges' in the consolidated income statements, using the effective interest rate method.

The effective interest rate method is used to calculate the amortised cost of financial instruments and to recognise interest receivable or payable over the relevant period. The effective interest rate is the rate that exactly discounts estimated cash flows (excluding credit losses) to zero, through the expected life of the instrument. In calculating the effective interest rate all contractual terms of the financial instrument (for example, early redemption charges) are taken into account.

Fees and Commissions
Fees and commissions relating to creating loans and advances to customers are deferred and spread as 'interest receivable', using the effective interest method. Other fees and commissions are recognised as 'Other income' on the accruals basis as services are provided.

Dividend Income
Dividends receivable are recognised in the Income statements in 'Dividend income' when the right to receive payment is established.

Financial Assets
In accordance with IAS 39, Financial Instruments: Recognition and Measurement, the Group classifies its financial assets into the following categories:

Loans and Receivables
The Group's mortgage assets and similar loans are classified as loans and receivables and measured at amortised cost using the effective interest rate method (EIR). In accordance with EIR methodology, incremental up-front costs and fees receivable which are directly related to the loans (including administration and completion fees, arrangement fees, procuration fees and commissions paid to agents) are deferred and released to income over the effective life of the mortgage assets. Historical and forecast mortgage redemption data and management judgement are used to estimate the expected lives of mortgage assets.

At Fair Value through Profit and Loss
The Group enters into derivative financial instruments to hedge its exposures relating to interest rates, index risk relating to savings products (equities, house prices and inflation) and longevity risk on equity release mortgages. At the balance sheet date the Group has only entered into contracts which lead to derivatives designated as fair value hedges. In accordance with the Treasury Policy Statement and the Building Societies Act 1986 the Group does not hold or issue derivative financial instruments for trading purposes.

In accordance with IAS 39, all derivative financial instruments (both assets and liabilities) are initially and on an ongoing basis, assessed to determine whether they are highly effective in offsetting the changes in fair value of hedged items. Derivatives are recognised at fair value on the date the derivative contract is entered into, and subsequently re-measured at their fair value with changes going through the Income Statements along with changes in fair value attributable to the hedged risk of the hedged items. The carrying value of the hedged item is included on the balance sheet under the heading "Fair value adjustments for hedged risk". Any gain or loss arising from an ineffective portion is recognised immediately in the Income Statements under the heading "Gains less losses on financial instruments and hedge accounting".

When a hedging instrument expires, is sold, or no longer meets the criteria for hedge accounting, then hedge accounting is discontinued and any cumulative gain or loss is recognised in the Income Statements.

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risk of the host instrument and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in the fair value of the embedded derivative recognised in the Income Statements.

Fair values are obtained in line with the three tier hierarchy described in IFRS7 from quoted market prices in active markets, valuation techniques using specialist tools and confirmations from counterparties.

Significant Accounting Policies Continued

Available for Sale
These assets are non-derivative financial instruments where the intention is to hold for an indefinite period of time. They are initially measured at fair value, with subsequent fair value movements recognised directly in Members' Interests, until the asset is derecognised or impaired, at which point the cumulative gain or loss previously recognised in Members' Interests is recognised in the Income Statements. Interest received on the asset is recognised immediately in the Income Statements.

Held to Maturity
These are non-derivative financial assets with fixed maturities that the Group has a positive intention and ability to hold until maturity. Held to maturity investments are initially recognised at fair value and are subsequently measured at amortised cost using the effective interest rate method. Interest on held to maturity investments is included in the Income Statements and reported as interest receivable and similar income.

Cash and Cash Equivalents
For the purpose of the Cash Flow Statements, 'Cash and cash equivalents' comprises cash in hand, balances with the Bank of England, loans and advances to banks available on demand or with original maturities of three months or less and investment securities with a maturity period of three months or less i.e. highly liquid assets readily convertible into cash.

Impairment of Financial Assets
Individual assessments are made against all those known loans and advances in arrears, in possession, where an event of default has occurred, where fraud has been identified or where any other potential loan servicing issues arising from assessments or professional advice are known. The value of those loans and advances that are considered to be impaired is reduced on an individual basis. Impairment calculations are carried out by considering future discounted cashflows as per rules laid out in international accounting standard, IAS39. In considering future cashflows the Society estimates the future valuation of the security less anticipated disposal costs, any irrecoverable hedging costs, and other payments and charges, which are then discounted using the original effective interest rate. Collective impairment allowances are also made to reduce the value of those loans and advances where there has been an event which may give rise to impairment but of which the Society is not yet aware at the balance sheet date, with the result that the amount advanced may not be recovered in full. For the purposes of the collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics. Any impairment loss or allowance is recognised in the Income Statements.

Loans are classed as renegotiated when their terms have changed during the year. The Group applies a policy of capitalising arrears on residential loans with the customer's agreement, once the customer has made six contractual monthly mortgage repayments following the instance of non-payments. Capitalisation is only applied where there is no realistic alternative and this is expected to be of long-term benefit to the borrower.

Financial Liabilities
All financial liabilities including shares, deposits, debt securities, subordinated liabilities and Permanent Interest Bearing Shares are recognised initially at fair value, being the issue proceeds, net of premia, discounts and transaction costs incurred. Financial liabilities are subsequently measured at amortised cost, using the EIR method.

Investment Properties
Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the companies included in the consolidated Group, is classed as investment property. This comprises mainly residential properties. Investment property is measured initially at cost, including related transaction costs.

After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specified asset. If this information is not available the Group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. Fair values are determined by the Society's Portfolio Manager with input on methodologies from a RICS qualified valuer.

Subsequent expenditure is included in the carrying amount of the property when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance costs are charged to the income statement during the financial period in which they are incurred. Similarly income is recognised in the financial period in which it arises. Gains or losses arising from changes in the fair value of the Group's investment properties are included in the Income Statements in the period in which they arise.

Property, Plant, Equipment and Depreciation
On transition to IFRS, the Group elected to adopt the exemption in IFRS 1 which permits an entity to use, on transition to IFRS, a value, which is not depreciated cost, as the 'deemed cost' of the asset. Property, plant and equipment are stated at cost (or 'deemed cost') less accumulated depreciation and any provisions for impairment. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Depreciation on assets commences when they are ready for their intended use and is provided at rates calculated to write down the assets to their estimated residual values over the course of their anticipated useful lives, on the following bases:

Freehold buildings and leasehold buildings:

With a residual lease term of greater than fifty years	- 2% per annum straight line
Other leasehold buildings	- over the term of the lease

Equipment, fixtures, fittings and motor vehicles:

Refurbishment expenditure	- 6.67% to 10% per annum, straight line
Equipment, fixtures and fittings	- 10% per annum, straight line
Computer equipment	- 20% per annum, straight line
Motor vehicles	- over the term of the lease

Gains and losses on disposals are determined by comparing the net disposal proceeds with the carrying amount of the asset and are included in the income statement in the period in which they arise.

Significant Accounting Policies Continued

Lease Purchase and Leasing
The Group enters into lease purchase contracts and finance and operating leases. Assets held under lease purchase contracts and finance leases are capitalised in property, plant and equipment at the fair value of the asset at the inception of the lease, with an equivalent liability categorised under other liabilities. Assets are depreciated in accordance with the relevant Group policy, over the lower of the useful life of the asset and the term of the lease. Finance charges are allocated to accounting periods over the life of each lease on a straight line basis or using the sum of digits method, depending on the cash flows attached to the agreement. Rentals under operating leases are charged on a straight line basis over the lease term. Both finance charges and rentals are recognised in administrative expenses in the Income Statements.

Taxation
Corporation tax is charged on profits adjusted for tax purposes.

Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements of the individual entities. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Pension Scheme Costs
The Society operates a defined contribution scheme on behalf of directors and staff. For the defined contribution schemes, contributions are charged to the Income Statements, as they become payable, in accordance with the rules of the Scheme.

The Society previously operated a defined benefit scheme; this was closed to future accrual from 30 November 2010, and was funded by contributions partly from employees and partly from the Society at rates determined by independent actuaries. These contributions are invested separately from the Group's assets. Under IAS 19, the Scheme assets are measured at bid value at each Balance Sheet date and the obligations are measured by independent actuaries using the projected unit valuation method, discounted using a high quality corporate bond rate. The resulting pension scheme surplus or deficit is recognised immediately on the Balance Sheet and any resulting actuarial gains and losses are recognised immediately in the Statements of Comprehensive Income.

Provisions
A provision is recognised when there is a present obligation as a result of a past event, it is probable that the obligation will be settled and it can be reliably estimated. Contingent liabilities have not been recognised.

Segment Information
The operating segments disclosed (Member business and Solutions business) are those used in the Group's management and internal reporting structures (for the Chief Operating Decision Maker) in accordance with IFRS 8. No segment information is presented on geographical lines, because substantially all of the Group's activities are in the United Kingdom.

Accounting Estimates and Judgements in applying Accounting Policies
The Group has to make judgements in applying its accounting policies which affect the amounts recognised in the Accounts. These judgements are based on management's best knowledge but the eventual outcome may differ from them. In addition, estimates and assumptions are made that could affect the reported amounts of assets and liabilities within the following year. The most significant areas where judgements and assumptions are made are as follows:

Pensions
Significant judgements are required in relation to the assumptions for the valuation of the pension scheme surplus or deficit including discount, interest and mortality rates, inflation and future salary increases. The Board receives independent external advice from actuarial consultants in arriving at the assumptions that are outlined in Note 32 to the Accounts.

The impact of a 0.1% increase in the inflation assumption would be to increase the carrying value of the defined benefit obligation by approximately £0.7m (and vice versa). The impact of a 0.1% increase in the assumed discount rate would be to decrease the carrying value of the defined benefit obligation by approximately £1.3m (and vice-versa).

Effective Interest Rate (EIR)
To calculate the appropriate EIR, certain assumptions are made in respect of the expected lives of specific asset portfolios which take into account such factors as the terms of the particular product, historic repayment data and prevailing economic conditions. These estimates are reviewed on a regular basis to ensure they reflect the portfolio's actual performance.

Impairment of Financial Assets
On loans fully secured on residential property the key assumptions in assessing the underlying value of the assets held as security for the loans is based on historic data and prudent expectations around future conditions. An estimate of forced sale adjustments (covering house price falls and disposal costs) has an impact on the level of provisioning for possession and arrears exposures. A forced sale adjustment that was higher by 5% would increase residential provisions by £0.5m.

Loans secured on commercial property or land are more individually significant. Provision is made against loans in arrears, possession or LPA receivership, or where a trigger event raises the likelihood of future problems servicing the loan. The key assumptions used in the discounted future value calculations used to determine the level of impairment required in respect of individual financial assets include:

- Predictions of the future value of underlying assets held as security for loans advanced, based on historic data, professional advice and prudent expectations around future conditions;
- Any sale adjustments, disposal costs, fees or other cash flows applicable;
- Any applicable adjustments arising on hedging instruments relating to the loan as employed by the Society; and
- Timing of cash flows.

Significant Accounting Policies Continued

Impairment of Treasury Assets
Treasury investments are regularly reviewed for objective evidence of impairment. In determining whether objective evidence exists, the Group considers, amongst other factors, financial difficulties of the counterparty, missed payments in breach of contractual arrangements, appointment of an administrator and current market conditions. Provision is made against treasury assets with reference to information provided by administrators on recoverability and also against traded market values. A 1% increase in the average recovery and market value assumption would decrease the current provision by £0.4m (and vice-versa).

Fair Value of Derivatives and Financial Assets
Fair values are determined by the three tier valuation hierarchy as defined within IFRS 7, Financial Instruments: Disclosures.

- Level 1 - quoted market prices in an actively traded market;
- Level 2 - valuations are estimated from observable data where no active market exists; and
- Level 3 - valuation techniques for which one or more significant input is not based on observable market data.

Further details are given in Note 34 to the Accounts.

Financial Services Compensation Scheme Provision
As explained in Note 27, the Society is committed to paying a levy to the Financial Services Compensation Scheme (FSCS). The provision for these costs in this year's accounts relates to payments to be made in future periods. The actual payments to be made are subject to change because they are dependant on the realisation of the assets of the institutions which have triggered the claims against the FSCS and future interest rates. In addition, the cost of funding the FSCS loans from HM Treasury is currently under review and may result in an increased interest rate being payable. The Society has estimated its obligations to the Scheme with reference to currently available external information.

Taxation
The Group is subject to tax in three jurisdictions and, consequently, estimates are required in determining the provision for corporation tax. As shown in Note 19 to the Accounts the Group has deferred tax assets which are considered recoverable given the Society and Group plans over the planning horizon.

Accounting Developments
At the date of approval of these financial statements, there are no new International Financial Reporting Standards or International Financial Reporting Interpretations Committee interpretations that are mandatory for the first time for the financial year beginning 1 January 2011 that have, or would be expected to have, a material impact on the Group.

Developments not effective at 31 December 2011
At the date of approval of these financial statements there are several new standards, amendments to existing standards and new interpretations issued but not effective for the financial year beginning 1 January 2011 and not adopted early by the Group.

The newly issued IFRSs are being assessed by the Group but no material impact is anticipated:

- IFRS 7 'Financial instruments: Disclosures' - promotes transparency in reporting of transfer transactions and the risk exposures from transfer of financial assets, particularly those of securitisations.
- IFRS 10 'Consolidated financial statements' - builds on the existing principals of control for determining entities to be included in a consolidated group.
- IFRS 11 'Joint arrangements' and IFRS12 'Disclosure of interests in other entities' - includes the disclosure requirements for all forms of non-consolidated interests and joint arrangements with other entities.
- IFRS 13 'Fair value measurement' - The new standard replaces guidance on fair value measurement in existing IFRS accounting literature with a single standard. The standard does not change the requirements regarding which items should be measured or disclosed at fair value but may require enhanced disclosures.

Standards not yet issued but being considered
International Financial Reporting Standards (IFRS)
IFRS 9 'Financial Instruments' - the standard set to replace IAS 39 will address the classification and measurement of financial assets and financial liabilities. Financial assets will need to be classified as either at amortised cost or at fair value. Assets designated as held to maturity will need to be reclassified and the available for sale category for financial assets, currently used by the Group, will no longer be available under IFRS 9.

The effective date for IFRS 9 is currently scheduled for 2015. The full impact of IFRS 9 on the Group is still to be assessed.

International Accounting Standards (IAS)
The following amendments to IAS are being assessed by the Group but are not expected to have a material impact.

IAS 12 'Income taxes' - provides a practical approach for measuring deferred tax liabilities and deferred tax assets when investment property is measured using the fair value model in IAS 40 Investment Property.

IAS 19 'Employee benefits' - removes the corridor approach and requires calculation of finance costs on a net funding basis.

IAS 27 'Separate financial statements' - amended to remove the consolidation requirements previously forming part of the standard. Consolidation requirements are now contained in IFRS 10.

IAS 28 'Associates and joint ventures' - amended to conform to the changes arising from the issuance of IFRS 10, IFRS 11 and IFRS 12.

2 Interest receivable and similar income

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
On loans and advances to customers	**127.8**	142.6	**128.2**	137.9
On debt securities				
- interest and other income	**15.9**	13.9	**15.9**	13.9
- profits net of losses on realisation	**4.7**	4.2	**4.7**	4.2
On other liquid assets				
- interest and other income	**2.6**	1.0	**2.7**	2.1
Net expense on derivatives hedging assets	**(47.8)**	(60.7)	**(47.8)**	(57.5)
	103.2	101.0	**103.7**	100.6

3 Interest expense and similar charges

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
On shares held by individuals	**94.6**	93.5	**94.6**	93.5
On subscribed capital	**3.6**	3.6	**3.6**	3.6
On deposits and other borrowings				
- subordinated liabilities	**2.2**	1.1	**2.2**	1.1
- to other depositors and borrowers	**4.5**	6.8	**4.5**	5.7
Net income on derivatives hedging liabilities	**(19.3)**	(22.0)	**(19.3)**	(22.0)
Covered bond costs	**0.1**	0.2	**0.1**	0.2
	85.7	83.2	**85.7**	82.1

4 Other income and charges

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Other income				
Fee and commission income	**10.4**	11.2	**4.5**	6.0
Other operating income	**16.9**	9.7	**16.1**	9.0
	27.3	20.9	**20.6**	15.0

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Other charges					
Fee and commission expense		**0.6**	1.6	**0.6**	1.6
Losses from fair value adjustments to investment properties	18	**0.1**	0.5	**-**	-
		0.7	2.1	**0.6**	1.6

5 Dividend income

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Received from subsidiary undertakings	**-**	-	**3.0**	3.1

6 Administrative expenses

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Staff costs	7	**21.7**	21.5	**19.6**	19.5
Rentals under operating leases for land and buildings					
- payable to third parties		**1.4**	1.6	**1.4**	1.6
- payable to subsidiary undertaking		**-**	-	**0.1**	0.1
Other administrative expenses		**9.5**	10.6	**9.0**	10.1
		32.6	33.7	**30.1**	31.3

During the year the Group and Society obtained the following services from the Group's auditors and these are included in other administrative expenses.

	GROUP and SOCIETY 2011 £m	GROUP and SOCIETY 2010 £m
Fees payable to the Society's auditor for the audit of Society and consolidated financial statements	**0.1**	0.1
Fees payable to the Society's auditor for other services	**0.1**	0.1
	0.2	0.2

7 Staff costs

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Wages and salaries		**19.0**	20.5	**17.2**	18.7
Social security costs		**1.8**	1.9	**1.6**	1.7
Pension costs					
- defined benefit plans		**-**	(1.5)	**-**	(1.5)
- defined contribution plans		**0.9**	0.6	**0.8**	0.6
	6	**21.7**	21.5	**19.6**	19.5

Included within pension costs for 2010 is a curtailment credit following the closure of the 'defined benefit' scheme to future accrual with effect from 30 November 2010. The total credit recognised was £2.0m in 2010.

Directors' emoluments are disclosed in the Remuneration Committee report on page 21.
The monthly average number of persons employed, including Executive Directors, during the year was:

	GROUP 2011	GROUP 2010	SOCIETY 2011	SOCIETY 2010
Full time	**699**	750	**663**	716
Part time	**193**	206	**192**	205
	892	956	**855**	921
Principal Office	**675**	732	**666**	725
Branches	**217**	224	**189**	196
	892	956	**855**	921

8 Taxation expense / (credit)

	Note	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Current tax					
UK corporation tax on profit at 26.5% (2010: 28%) for the year		-	-	-	-
Group relief for the year		-	-	(1.0)	(1.0)
Under provision in respect of previous years		-	-	0.2	-
Total current tax		-	-	(0.8)	(1.0)
Deferred tax					
Current year	19	0.8	(0.6)	0.9	(0.1)
Over provision in respect of previous years		-	(0.4)	(0.1)	(0.4)
Total deferred tax		0.8	(1.0)	0.8	(0.5)
Total taxation expense / (credit) in the Income Statements		0.8	(1.0)	-	(1.5)

Analysis of taxation expense / (credit) for the year

The tax on the Group and Society profit / (loss) before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits as follows:

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Profit / (loss) before taxation	0.1	(4.7)	(0.3)	(3.6)
Loss before taxation at the standard rate of corporation tax in the UK of 26.5% (2010: 28%)	-	(1.3)	(0.1)	(1.0)
Expense / (income) not taxable / deductible for tax purposes:				
Expenses	(0.1)	0.2	(0.2)	0.3
Non-taxable dividend income received	-	-	(0.9)	(0.9)
Rate change	0.9	0.5	1.0	0.5
(Under) / over provision in respect of previous years	-	(0.4)	0.2	(0.4)
Total taxation expense / (credit)	0.8	(1.0)	-	(1.5)

Factors affecting future tax charges

The Society has unrelieved trading losses which are expected to materially affect future taxable profits.

In addition to the changes in rates of Corporation tax disclosed above a number of further changes to the UK Corporation tax system were announced in the March 2011 UK Budget Statement. Further reductions to the main rate are proposed to reduce the rate by 1% per annum to 23% by 1 April 2014. These further changes had not been substantively enacted at the balance sheet date and, therefore, are not included in these financial statements.

The proposed reductions of the main rate of corporation tax by 1% per year to 23% by 1 April 2014 are expected to be enacted separately each year. The overall effect of the further changes from 25% to 23%, if these applied to the deferred tax balance at the balance sheet date, would be to reduce the deferred tax asset by £1.0m (being £0.5m recognised in 2013 and £0.5m recognised in 2014).

9 Segment information

The chief operating decision maker has been identified as the Board of Directors. The Board reviews the Group's internal reporting in order to assess performance and allocate resources. Management has determined the operating segments based on these reports.

Following the management approach of IFRS 8, operating segments are reported in accordance with the internal reporting provided to the Board of Directors. The operating segments used by the Group meet the definition of a reportable segment under IFRS 8.

The 'Member business' segment provides mortgage, savings, investment and insurance products to members and customers. The 'Solutions business' segment provides business to business services through people, processes and technology. The Board assesses performance based on profit before tax after the allocation of all central costs.

No segment information is presented on geographical lines, because substantially all of the Group's activities are in the United Kingdom.

Income and directly attributable costs are allocated to each segment and support costs are apportioned, based on direct salary costs and detailed allocations by budget holders.

Year to 31 December 2011	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	17.5	-	17.5
Other income and charges	11.0	15.6	26.6
Gains less losses from financial instruments and hedge ineffectiveness	0.6	-	0.6
Administrative expenses	(24.0)	(8.6)	(32.6)
Depreciation	(2.1)	(0.8)	(2.9)
Operating profit before impairments, provisions and exceptional items	3.0	6.2	9.2
Impairment charges and provisions for liabilities and charges	(11.6)	-	(11.6)
FSCS levy	(1.4)	-	(1.4)
Exceptional Items	-	3.9	3.9
(Loss) / profit for the year before taxation	(10.0)	10.1	0.1
Taxation expense			(0.8)
Loss after taxation for the financial year			(0.7)
Total assets	4,412.5	6.0	4,418.5

Year to 31 December 2010	Member Business £m	Solutions Business £m	Total £m
Net interest receivable	17.8	-	17.8
Other income and charges	9.8	9.0	18.8
Gains less losses from financial instruments	0.9	-	0.9
Ineffectiveness	(0.9)	-	(0.9)
Administrative expenses	(25.7)	(8.0)	(33.7)
Depreciation	(2.4)	(0.8)	(3.2)
Operating profit before impairments, provisions and exceptional items	(0.5)	0.2	(0.3)
Repositioning Programme provision for charges	(4.0)	-	(4.0)
Impairment charges and provisions for liabilities and charges	0.5	(0.9)	(0.4)
Loss for the year before taxation	(4.0)	(0.7)	(4.7)
Taxation credit			1.0
Loss after taxation for the financial year			(3.7)
Total assets	4,412.4	6.4	4,418.8

10 Gain on Disposal of Prepaid Cards Division

On 21st December 2011 the Society sold its Prepaid Cards division (PPC) to Wirecard AG ("the Buyer"). The net gain on disposal comprises the following elements:-

	£m
Cash consideration	7.5
Deferred consideration	0.5
	8.0
Legal and Professional Fees	(0.7)
Assets written off	(0.3)
Pre-completion liabilities retained	(3.1)
Net Gain on disposal	**3.9**

From the date of Completion the Buyer has all of the risks and rewards of ownership with all profits accruing to the Buyer and liabilities post-completion becoming the responsibility of the Buyer. The Society retains responsibility for PPC liabilities in the pre-completion period; these arise primarily on the close out of historical prepaid card programs that are not being transferred to the Buyer. The Buyer has control of PPC operating and financial policies and business strategy with effect from legal completion. All PPC employees were subject to TUPE on legal completion and are now employees of the Buyer.

The total purchase price is £10m payable as £7.5m in cash on the date of legal completion and £2.5m payable as deferred consideration based on the financial performance of PPC in 2012 and 2013. As the deferred consideration is based solely on financial performance measures this meets the definition of a derivative under IAS39 and is therefore recognised at fair value. The valuation of the derivative is based on a prudent and probability based assessment of expected future performance with the cash receivable discounted back to present value at the year-end.

The Buyer will eventually operate PPC under a separate UK e-money permission, which the Buyer is in the process of obtaining from the Financial Services Authority. Whilst the Buyer already has an existing e-money permission granted by the German regulatory authorities (BaFin) the Buyer continues to operate PPC through the Society's e-money licence. A put option exists within the sale agreement such that in the event the Buyer does not obtain an e-money permission then PPC could be sold back to the Society at a reduced price. The Society believes the likelihood of the Buyer not obtaining an e-money permission is highly remote. The directors consider that control of PPC has been lost and therefore the put option is treated as a derivative under IAS 39 and has been fair valued at £55,000.

The financial performance of PPC for 2011, up to the date of sale, was as follows:

	£m
Net income	2.4
Operating costs	(1.0)
Operating profit	**1.4**

11 Loans and advances to banks

Repayable from the date of the Balance Sheets in the ordinary course of business as follows:

	GROUP		SOCIETY	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Accrued interest	**0.4**	0.1	**0.4**	0.1
On demand	**0.8**	20.0	**0.7**	2.6
In not more than three months	**235.3**	156.5	**235.3**	156.5
In more than three months but not more than one year	**38.0**	15.0	**38.0**	15.0
In more than one year but not more than five years	**-**	1.0	**-**	1.0
Gross loans and advances to banks	**274.5**	192.6	**274.4**	175.2
Less: allowance for losses on loans and advances to banks	**(20.4)**	(20.2)	**(20.4)**	(20.2)
	254.1	172.4	**254.0**	155.0

Allowance for losses on loans and advances to banks

	GROUP and SOCIETY	
	2011 £m	2010 £m
Balance at 1 January	**20.2**	22.3
New provisions during the year	**0.2**	-
Amounts utilised during the year	**-**	-
Amounts released for the year	**-**	(2.1)
At 31 December	**20.4**	20.2

At 31 December 2011 the Society had loans and advances to Icelandic banks totalling **£27.6m** (2010: £30.2m), against which allowance for losses of **£20.4m** (2010: £20.2m) has been made.

Notes to the Accounts for the year ended 31 December 2011

12 Debt securities

	GROUP and SOCIETY	
Transferable debt securities	**2011 £m**	2010 £m
Issued by public bodies - listed	**202.7**	108.4
Issued by other borrowers - unlisted	**561.8**	339.4
Gross debt securities	**764.5**	447.8
Less: allowance for losses on debt securities	**-**	(0.9)
	764.5	446.9
These have remaining maturities as follows:		
Accrued interest	**6.9**	4.2
In not more than one year	**204.1**	95.5
In more than one year but not more than five years	**354.0**	253.0
In more than five years	**199.5**	95.1
Gross debt securities	**764.5**	447.8
Less: allowance for losses on debt securities	**-**	(0.9)
	764.5	446.9

Allowance for losses on debt securities

	GROUP and SOCIETY	
	2011 £m	2010 £m
Balance at 1 January	**0.9**	1.2
Amounts released for the year	**(0.9)**	(0.3)
At 31 December	**-**	0.9

The Directors consider that the primary purpose of holding securities is to comply with prudential requirements. All transferable debt securities are held with the intention of use on a continuing basis in the Group's activities. They are designated by management on initial recognition as being available for sale and are recognised, both initially and subsequently, at fair value with changes recognised directly in equity.

At 31 December 2011, the Society held a debt security issued by an Icelandic bank with a book value of **£nil** (2010: £1.9m), against which an allowance for loss of **£nil** (2010: £0.9m) has been made.

Under IAS 39 as amended, certain financial instruments were reclassified with effect from 1 July 2008. The table below sets out the financial instruments reclassified and their carrying and fair values:

	31 December 2011		31 December 2010	
	Carrying value £m	Fair value £m	Carrying value £m	Fair value £m
Fair value through profit or loss financial instruments reclassified to held to maturity financial instruments	14.8	12.9	42.8	41.3

If the financial assets had not been reclassified, the change in their fair values, after actual reclassification, would have resulted in additional fair value gains of **£nil** (2010: £3.0m) in the Income Statements for the year ended 31 December 2011.

13 Assets pledged as collateral

Assets are pledged as collateral under repurchase agreements with banks. Securities pledged with banks are debt securities with a market value of **£85.1m** (2010: £105.4m). All collateral agreements mature within 1 year.

The nature and carrying amounts of the assets pledged as collateral are as follows:

	Group and Society Asset		Group and Society Related liability	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Debt securities pledged	**85.1**	105.4	**85.1**	102.2

14 Loans and advances to customers

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Loans fully secured on residential property	**2,563.6**	2,799.5	**2,538.0**	2,767.7
Loans fully secured on land	**392.0**	487.5	**392.0**	416.1
Other loans	**38.0**	60.4	**38.0**	60.4
Gross loans and advances	**2,993.6**	3,347.4	**2,968.0**	3,244.2
Less: allowance for losses on loans and advances	**(17.0)**	(22.3)	**(17.0)**	(22.3)
	2,976.6	3,325.1	**2,951.0**	3,221.9

Covered Bonds

The Society's £500m Covered Bond programme which was launched in January 2009 was unwound in July 2011 as part of the restructuring and simplification of the Group's activities and the funding obtained for the purpose which the vehicle was set up for was repaid. At 31 December 2010 loans and advances to customers included £682.0m of loans for both the Group and Society which had been legally transferred to Newcastle Building Society Covered Bond LLP.

Loans and advances to customers have remaining maturities as follows:

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
On demand	**17.1**	17.9	**17.1**	17.9
In not more than three months	**60.6**	50.9	**60.5**	46.3
In more than three months but not more than one year	**185.6**	129.0	**185.3**	120.2
In more than one year but not more than five years	**358.8**	544.1	**357.4**	517.7
In more than five years	**2,371.5**	2,605.5	**2,347.7**	2,542.1
Gross loans and advances	**2,993.6**	3,347.4	**2,968.0**	3,244.2
Less: allowance for losses on loans and advances	**(17.0)**	(22.3)	**(17.0)**	(22.3)
	2,976.6	3,325.1	**2,951.0**	3,221.9

Where a loan is repayable by instalment, each such instalment has been treated as a separate repayment in the maturity analysis set out above. The Group's experience is that in many cases mortgages are redeemed before their scheduled maturity date. As a consequence, the maturity analysis illustrated above may not reflect actual experience.

Notes to the Accounts for the year ended 31 December 2011

14 Loans and advances to customers Continued

Allowance for losses on loans and advances

GROUP and SOCIETY

	Loans fully secured on residential property Individual £m	Collective £m	Loans fully secured on land Individual £m	Collective £m	Other loans Individual £m	Collective £m	Total Individual £m	Collective £m	Total £m
Balance at 1 January 2011	4.4	0.4	11.0	5.6	0.5	0.4	15.9	6.4	22.3
Charge for the year	0.6	(0.1)	17.0	(4.8)	(0.1)	(0.3)	17.5	(5.2)	12.3
Amounts written off during the year	(3.2)	-	(17.3)	-	-	-	(20.5)	-	(20.5)
Interest suspended	0.1	-	2.3	0.5	-	-	2.4	0.5	2.9
At 31 December 2011	**1.9**	**0.3**	**13.0**	**1.3**	**0.4**	**0.1**	**15.3**	**1.7**	**17.0**

	Loans fully secured on residential property Individual £m	Collective £m	Loans fully secured on land Individual £m	Collective £m	Other loans Individual £m	Collective £m	Total Individual £m	Collective £m	Total £m
Balance at 1 January 2010	3.8	1.2	13.6	2.4	0.4	0.7	17.8	4.3	22.1
Charge for the year	1.6	(0.8)	(2.0)	3.2	0.1	(0.3)	(0.3)	2.1	1.8
Amounts written off during the year	(1.2)	-	(0.6)	-	-	-	(1.8)	-	(1.8)
Interest suspended	0.2	-	-	-	-	-	0.2	-	0.2
At 31 December 2010	**4.4**	**0.4**	**11.0**	**5.6**	**0.5**	**0.4**	**15.9**	**6.4**	**22.3**

15 Fair value adjustment for hedged risk

As disclosed in the statement of accounting policies, when specific criteria are met, the Group applies fair value hedge accounting and the adjustments to assets and liabilities are included on the balance sheet under the heading 'Fair value adjustment for hedged risk'. The fair value adjustment for hedged risk for assets for the Group and Society was **£57.9m**, (2010: Group £50.8m, Society £48.0m). The fair value adjustment for hedged risk for liabilities for the Group and Society was **£28.7m**, (2010: Group and Society £20.8m).

16 Investments in subsidiary undertakings

SOCIETY

Investments in subsidiary undertakings	Shares £m	Loans £m	Total £m
Cost			
At 1 January 2011	7.8	52.5	60.3
Additions	-	4.1	4.1
Repayments received	(1.8)	(14.5)	(16.3)
At 31 December 2011	**6.0**	**42.1**	**48.1**
Provisions			
At 1 January 2011	1.8	1.8	3.6
Write Offs	(1.2)	(1.8)	(3.0)
At 31 December 2011	**0.6**	**-**	**0.6**
Net book amount at 31 December 2011	**5.4**	**42.1**	**47.5**

Investments in subsidiary undertakings	Shares £m	Loans £m	Total £m
Cost			
At 1 January 2010	7.8	59.4	67.2
Additions	-	2.4	2.4
Repayments received	-	(9.3)	(9.3)
At 31 December 2010	**7.8**	**52.5**	**60.3**
Provisions			
	1.8	**1.8**	**3.6**
Net book amount at 31 December 2010	**6.0**	**50.7**	**56.7**

The Society directly holds 100% of the issued ordinary share capital of all its subsidiary undertakings.

The Directors believe that the carrying value of the investments in subsidiary undertakings is supported by their underlying net assets.

Name of principal subsidiary undertakings	Principal activity
Kings Manor Properties Limited	Residential property rental
Newcastle Financial Services Limited	Provision of financial services
Newcastle Mortgage Loans (Jersey) Limited	Mortgage lending
Newcastle Portland House Limited	Commercial property rental
Newcastle Strategic Solutions Limited	Provision of specialised products and services
Newton Facilities Management Limited	Provision of managed IT services
Newcastle Card Solutions Limited	Provides prepaid card solutions (dormant)

All the above subsidiary undertakings, except for Newcastle Mortgage Loans (Jersey) Limited, which is incorporated and operates in Jersey, are incorporated in England and Wales and operate in the United Kingdom.

The results of the following special purpose vehicles were consolidated into the Group in 2010 under International Accounting Standard 27: 'Consolidated and separate Financial Statements'.

Name	Principal activity
Bamburgh Finance No. 1 PLC	Securitisation vehicle
Bamburgh Holdings Limited	Holding company
Bamburgh Mortgages Trustee Limited	Securitisation vehicle
Newcastle Building Society Covered Bonds LLP	Acquisition and management of loans

The Society had no shareholdings in any of the companies listed above. Bamburgh Finance No. 1 PLC and Newcastle Building Society Covered Bonds LLP were incorporated in England and Wales and operate in the United Kingdom. The other companies are incorporated and operate in Jersey.

As part of the subsidiary rationalisation programme that commenced in 2010, which was part of the repositioning programme, various subsidiaries have been wound up including dormant companies, companies that no longer trade, Newton Facilities Computer Purchasing Limited and Newton Facilities Computer Leasing Limited. Following the call of the Notes the Bamburgh special purpose vehicle companies are also being wound up and Newcastle Building Society Covered Bond LLP was wound up in 2011.

17 Property, plant and equipment

GROUP

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2011	6.8	12.2	26.3	45.3
Additions	-	-	1.0	1.0
Disposals	(0.1)	-	(0.3)	(0.4)
At 31 December 2011	**6.7**	**12.2**	**27.0**	**45.9**
Accumulated depreciation				
At 1 January 2011	0.6	2.6	16.0	19.2
Charge for the year	0.1	0.2	2.6	2.9
Disposals	-	-	(0.1)	(0.1)
At 31 December 2011	**0.7**	**2.8**	**18.5**	**22.0**
Net book amount at 31 December 2011	**6.0**	**9.4**	**8.5**	**23.9**

GROUP

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2010	6.8	12.2	25.4	44.4
Additions	-	-	1.3	1.3
Disposals	-	-	(0.4)	(0.4)
At 31 December 2010	**6.8**	**12.2**	**26.3**	**45.3**
Accumulated depreciation				
At 1 January 2010	0.5	2.4	13.3	16.2
Charge for the year	0.1	0.2	2.9	3.2
Disposals	-	-	(0.2)	(0.2)
At 31 December 2010	**0.6**	**2.6**	**16.0**	**19.2**
Net book amount at 31 December 2010	**6.2**	**9.6**	**10.3**	**26.1**

17 Property, plant and equipment Continued

SOCIETY

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2011	6.8	0.9	24.0	31.7
Additions	-	-	1.0	1.0
Disposals	(0.1)	-	(0.1)	(0.2)
At 31 December 2011	**6.7**	**0.9**	**24.9**	**32.5**
Accumulated depreciation				
At 1 January 2011	0.6	0.1	13.9	14.6
Charge for the year	0.1	-	2.6	2.7
Disposals	-	-	(0.1)	(0.1)
At 31 December 2011	**0.7**	**0.1**	**16.4**	**17.2**
Net book amount at 31 December 2011	**6.0**	**0.8**	**8.5**	**15.3**

SOCIETY

	Freehold buildings £m	Leasehold land and buildings £m	Equipment, fixtures, fittings and motor vehicles £m	Total £m
Cost				
At 1 January 2010	6.8	0.9	23.2	30.9
Additions	-	-	1.2	1.2
Disposals	-	-	(0.4)	(0.4)
At 31 December 2010	**6.8**	**0.9**	**24.0**	**31.7**
Accumulated depreciation				
At 1 January 2010	0.5	0.1	11.3	11.9
Charge for the year	0.1	-	2.8	2.9
Disposals	-	-	(0.2)	(0.2)
At 31 December 2010	**0.6**	**0.1**	**13.9**	**14.6**
Net book amount at 31 December 2010	**6.2**	**0.8**	**10.1**	**17.1**

Included within Equipment, fixtures, fittings and motor vehicles are assets under finance leases, which comprise motor vehicles and a long lease hold property that have the following net book amounts.

	GROUP and SOCIETY 2011 £m	2010 £m
Cost		
At 1 January	**1.1**	1.2
Accumulated depreciation	**(0.1)**	(0.1)
Net book amount at 31 December	**1.0**	1.1

18 Investment properties

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Fair value				
At 1 January	**14.3**	14.6	**-**	-
Additions from acquisitions	**1.7**	0.2	**-**	-
Net losses from fair value adjustments	**(0.1)**	(0.5)	**-**	-
At 31 December	**15.9**	14.3	**-**	-

The Group has valued all of its investment property as at December 2011 at fair value. The valuation was carried out by reference to open market prices for similar properties, as estimated by management and reviewed by the Directors.

A revaluation deficit of £0.1m has arisen on valuation of investment property to fair value as at December 2011 (2010: £0.5m) and this has been taken to the Income Statements.

The historical cost of the Group's investment property as at 31 December 2011 is £16.5m (2010: £14.8m).

Investment property rental income (included within other income) and direct operating expenses (included within administrative expenses) for the Group are shown below:

	GROUP 2011 £m	GROUP 2010 £m
Income from rental properties	**0.7**	0.7
Operating expenses relating to rental properties	**(0.2)**	(0.1)
Net rental income from rented properties	**0.5**	0.6

The Group leases investment properties to non-commercial individuals under non-cancellable operating leases for a contract period of up to 6 months.

Direct property repair and maintenance costs arising from investment property that generated rental income during the year was £0.2m (2010: £0.1m).

Direct operating expenses arising from investment property that did not generate rental income during the year amounted to £nil (2010: £nil).

19 Deferred tax

Deferred tax is calculated on all temporary differences under the liability method using a tax rate of **25%** (2010: 27%). The movement on the deferred tax account is shown below.

	GROUP		SOCIETY	
	2011 £m	2010 £m	**2011 £m**	2010 £m
At 1 January	**12.6**	11.7	**13.2**	12.8
Income Statements (expense) / credit	**(0.8)**	0.6	**(0.9)**	0.1
Over provision in respect of prior years	**-**	0.4	**0.1**	0.4
Credited / (debited) on items taken directly through reserves	**1.1**	(0.1)	**1.1**	(0.1)
At 31 December	**12.9**	12.6	**13.5**	13.2

Deferred tax assets and liabilities are attributable to the following items.

	GROUP		SOCIETY	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Deferred tax assets				
Short term timing differences	**2.4**	1.8	**2.3**	1.6
Fair value adjustments on adoption of IAS 32 and IAS 39	**0.5**	0.7	**0.5**	0.7
Trading losses	**10.1**	10.8	**10.1**	10.9
Depreciation in excess of capital allowances	**0.6**	-	**0.6**	-
	13.6	13.3	**13.5**	13.2
Deferred tax liabilities				
Accelerated capital allowances	**(0.7)**	(0.7)	**-**	-
	(0.7)	(0.7)	**-**	-
Deferred tax assets				
Deferred tax asset to be recovered in less than 12 months	**0.8**	0.8	**0.7**	0.7
Deferred tax asset to be recovered in more than 12 months	**12.8**	12.5	**12.8**	12.5
	13.6	13.3	**13.5**	13.2
Deferred tax liabilities				
Deferred tax liability to be recovered in less than 12 months	**-**	-	**-**	-
Deferred tax liability to be recovered in more than 12 months	**(0.7)**	(0.7)	**-**	-
	(0.7)	(0.7)	**-**	-

The deferred tax (expense) / credit in the Income Statements comprises the following temporary differences:

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Accelerated capital allowances	**0.6**	0.1	**0.6**	-
Short term timing differences	**(0.9)**	(0.7)	**(0.9)**	(0.8)
Pensions and other post retirement benefits	**-**	(1.0)	**-**	(1.0)
Trading losses	**(0.5)**	2.2	**(0.5)**	1.9
Other	**-**	-	**-**	-
	(0.8)	0.6	**(0.8)**	0.1

Deferred tax assets are recognised for tax losses carried forward only to the extent that realisation of the related tax benefit is probable.

20 Other assets

	GROUP		SOCIETY	
	2011 £m	2010 £m	**2011 £m**	2010 £m
Receivable from subsidiary undertakings	**-**	-	**3.8**	2.9
Interest receivable on financial instruments	**7.6**	5.4	**7.6**	5.4
Prepayments and accrued income	**8.1**	14.4	**14.9**	21.2
Other	**4.6**	5.9	**4.5**	17.6
	20.3	25.7	**30.8**	47.1

21 Non-current assets held for sale

	GROUP and SOCIETY	
	2011 £m	2010 £m
Cost		
At 1 January	**-**	1.5
Disposals	**-**	(1.5)
At 31 December	**-**	-

Net-current assets held for sale comprised a long leasehold property which the Society sold in December 2010.

22 Due to members

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Held by individuals	**3,761.2**	3,592.0	**3,761.2**	3,592.0
Other shares	**0.2**	1.0	**0.2**	1.0
	3,761.4	3,593.0	**3,761.4**	3,593.0

Repayable from the date of the Balance Sheets in the ordinary course of business as follows:

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Accrued interest	**39.0**	44.5	**39.0**	44.5
On demand	**1,541.1**	1,378.0	**1,541.1**	1,378.0
In not more than three months	**1,402.1**	1,308.0	**1,402.1**	1,308.0
In more than three months but not more than one year	**582.3**	637.4	**582.3**	637.4
In more than one year but not more than five years	**196.3**	218.0	**196.3**	218.0
In more than five years	**0.6**	7.1	**0.6**	7.1
	3,761.4	3,593.0	**3,761.4**	3,593.0

Included in the shares balance is the contractual balance of **£211.4m** (2010: £270.9 million) of Capital Protection Bonds with fair values at 31 December 2011 of **£226.1m** (2010: £280.7 million). The fair value adjustments of **£16.9m** (2010: £11.6m) to the carrying value of the bonds are included in the figures above.

All the changes in fair value are attributable to changes in benchmark equity and interest rates. The Society is contractually required to pay only the par value of the shares on maturity.

23 Due to other customers

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Amounts owed to subsidiary undertakings	**-**	-	**3.1**	3.8
Other	**157.2**	220.8	**157.2**	220.8
	157.2	220.8	**160.3**	224.6

Repayable from the date of the Balance Sheet in the ordinary course of business as follows:

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Accrued interest	**1.1**	0.8	**1.1**	0.8
On demand	**5.2**	6.0	**5.2**	6.0
In not more than three months	**98.5**	163.5	**101.6**	167.3
In more than three months but not more than one year	**51.3**	49.3	**51.3**	49.3
In more than one year but not more than five years	**1.1**	1.2	**1.1**	1.2
	157.2	220.8	**160.3**	224.6

24 Deposits from banks

Repayable from the date of the Balance Sheets in the ordinary course of business as follows:

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Accrued interest	**0.3**	0.3	**0.3**	0.3
In not more than three months	**66.0**	41.7	**66.0**	41.7
In more than three months but not more than one year	**41.3**	50.7	**41.3**	50.7
In more than one year but not more than five years	**-**	57.4	**-**	57.4
	107.6	150.1	**107.6**	150.1

25 Debt securities in issue

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Accrued interest	**-**	-	**-**	-
Certificates of deposit	**16.0**	15.5	**16.0**	15.5
Non recourse finance	**-**	71.0	**-**	-
	16.0	86.5	**16.0**	15.5

Debt securities have remaining maturities as follows:

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
In not more than three months	**13.0**	8.0	**13.0**	8.0
In more than three months but not more than one year	**3.0**	7.5	**3.0**	7.5
In more than five years	**-**	71.0	**-**	-
	16.0	86.5	**16.0**	15.5

Non recourse finance repayable after five years comprised:

		GROUP 2011 £m	2010 £m
Class A	Mortgage backed floating rate notes due 2038	**-**	36.0
Class B	Mortgage backed floating rate notes due 2038	**-**	12.6
Class C	Mortgage backed floating rate notes due 2038	**-**	13.3
Class D	Mortgage backed floating rate notes due 2038	**-**	9.1
		-	71.0

The mortgage backed floating rate notes due 2038 (the 'Notes') were secured over a portfolio of mortgage loans secured by first charges over commercial properties in the United Kingdom.

There were four classes of Notes. All classes were subject to interest based on the prevailing three month LIBOR plus an additional margin. The three month LIBOR was revised quarterly and the following margins, subject to revision, applied to the classes of Notes as follows:

	Until 22 Feb 2011	23 Feb 2011 until Dec 2038
Class A	0.45%	0.90%
Class B	0.60%	1.20%
Class C	0.85%	1.70%
Class D	1.85%	2.85%

On 1 February 2011 the Notes were repaid on the first optional call date. The portfolios of commercial mortgage loans moved from the special purpose vehicles, as disclosed in Note 16, to the Society on the same day. The Notes were redeemed at par.

26 Other liabilities

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Amounts payable to subsidiary undertakings	**-**	-	**4.7**	4.0
Third party income tax withheld	**0.7**	0.4	**0.7**	0.4
Obligations under finance leases	**1.1**	1.1	**1.1**	1.1
Other creditors	**9.2**	8.2	**9.1**	8.2
Accruals and deferred income	**8.0**	11.8	**7.7**	9.5
	19.0	21.5	**23.3**	23.2

Obligations under finance leases fall due as follows:

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
Within one year	**0.1**	0.1	**0.1**	0.1
In one to two years	**0.1**	0.1	**0.1**	0.1
In two to five years	**0.1**	0.1	**0.1**	0.1
In more than five years	**0.8**	0.8	**0.8**	0.8
	1.1	1.1	**1.1**	1.1

These liabilities are secured by charges over the assets to which they relate.

There is not a material difference between the minimum lease payment at the balance sheet date and their present value

27 Provisions for liabilities and charges

GROUP and SOCIETY

	Repositioning Programme £m	FSCS Levy Provision £m	Other Provisions £m	Total £m
Opening Provision at 1 January 2011	**1.7**	**3.0**	**1.6**	**6.3**
New Provisions during the year	**-**	**1.4**	**3.1**	**4.5**
Amounts utilised during the year	**(0.6)**	**(1.3)**	**(0.5)**	**(2.4)**
Closing Provision at 31 December 2011	**1.1**	**3.1**	**4.2**	**8.4**

GROUP and SOCIETY

	Repositioning Programme £m	FSCS Levy Provision £m	Other Provisions £m	Total £m
Opening Provision at 1 January 2010	-	4.3	0.6	4.9
New Provisions during the year	4.0	-	1.0	5.0
Amounts utilised during the year	(2.3)	(1.3)	-	(3.6)
Closing Provision at 31 December 2010	1.7	3.0	1.6	6.3

Provision for Financial Services Compensation Scheme Levy

In common with all regulated UK deposit takers, the Society pays a levy to the Financial Services Compensation Scheme (FSCS). The FSCS Levy consists of two parts - a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes, using the rights that have been assigned to it. During the latter part of 2008 claims against the FSCS were triggered by the transfer of Bradford and Bingley's retail deposit business to Abbey National (now Santander) and the defaults of Kaupthing Singer and Friedlander, Heritable Bank and Landsbanki (Icesave). Further defaults arose in relation to London Scottish Bank and Dunfermline Building Society. The FSCS has met these claims by way of loans received from HM Treasury.

The FSCS is liable to pay interest on the loans from HM Treasury and may have a further liability if there are insufficient funds available from the realisation of the assets of the relevant institutions to repay fully the respective HM Treasury loans. Any levies in respect of capital shortfalls would be recognised when they have been communicated by the FSCS and have been triggered at the reporting date.

The Society has recognised a provision of £3.1m at 31 December 2011 for the scheme years 2011/12 and 2012/13 which is calculated with reference to the eligible deposits the Society held at 31 December 2010 and 31 December 2011, and the likely interest payable on the Society's share of overall eligible UK deposits.

HM Treasury and the FSCS are currently in discussions regarding the refinancing of FSCS legacy loans which includes the rate of interest to be charged. These negotiations may impact the charge for interest the Society has recognised in relation to the 2012/13 scheme year based on eligible deposits at 31 December 2011. The charge the Society has recognised in relation to this scheme year is based on the best estimate of the likely outcome of the negotiations having first consulted with relevant external bodies. The charge may be higher based on the final outcome of the negotiations between HM Treasury and the FSCS.

As further information is provided by the FSCS the Society will continue to update its estimate of the amount of FSCS levies it will ultimately be required to pay.

27 Provisions for liabilities and charges

Provision for Repositioning costs

The Society established a £4m provision in 2010 to cover costs and fees associated with its programme of cost reduction, business simplification and property rationalisation. At 31 December 2011 £1.1m (2010: £1.7m) of the provision remained, relating to vacant properties that the Society is currently marketing with property agents.

Other provisions

Other provisions includes amounts deemed irrecoverable on Prepaid Card debtors and settlement liabilities for Prepaid Card programmes, which remain with the Society following the disposal of the Prepaid Cards Division.

Mortgage Payment Protection Insurance (MPPI)

The Society has established a small provision of £25k (2010: £41k) against MPPI mis-selling claims. The provision covers costs of dealing with claims rather than any compensation payable. The Society has never sold single premium policies with interest loaded upfront and the Society has no issues with regard to systematic mis-selling of MPPI.

28 Subordinated liabilities

	GROUP 2011 £m	2010 £m	SOCIETY 2011 £m	2010 £m
7.375% fixed rate subordinated notes 2015	**9.6**	9.6	**9.6**	9.6
7.190% fixed rate subordinated notes 2017	**25.0**	25.0	**25.0**	25.0
6.625% fixed rate subordinated notes 2019	**25.0**	25.0	**25.0**	25.0
Less: unamortised issue costs	**(0.1)**	(0.1)	**(0.1)**	(0.1)
Less: unamortised capital exchange costs	**(0.8)**	(0.9)	**(0.8)**	(0.9)
	58.7	58.6	**58.7**	58.6

On a winding up, the subordinated notes rank behind the claims against the Society of all depositors, creditors and investing members (other than holders of deferred shares i.e. permanent interest bearing shares) of the Society. The notes are repayable at the Society's option and with the prior consent of the Financial Services Authority, on any interest date within five years of the maturity date.

On 10 May 2010 the Society announced that a Capital Agreement had been approved by holders of certain classes of the Society's existing subordinated debt and permanent interest bearing shares. The Capital Agreement involved adding a conversion feature such that the relevant instruments would convert into profit participating deferred shares (PPDS) should the Society's core tier 1 capital ratio fall below 5%. In return for this feature an increase in coupon was agreed as follows:

£11 million 6.375% fixed rate subordinated notes due 2015 (increase in coupon of 1%);

£25 million 6.19% fixed rate subordinated loan due 2017 (increase in coupon of 1%); and

£10 million 12% permanent interest bearing shares (increase in coupon of 0.25%)

The relevant instruments cease to be convertible and the coupon uplift falls away if the Society's core tier 1 capital ratio exceeds 12%.

In the event of conversion, the PPDS would qualify as core tier 1 capital of the Society and be eligible for a dividend payment based on a percentage of the Society's annual post-tax profits. This percentage, which would be determined at the time of conversion, would be equivalent to that proportion of the Society's core tier 1 capital which the PPDS represent immediately after conversion (the "Participation Percentage"). Any such dividend would be at the sole discretion of the Society's board of directors and any dividends would be non-cumulative. The PPDS would be deferred shares for the purposes of Section 119 of the Building Societies Act 1986, as amended, and would be perpetual instruments with no maturity date or right to repayment other than on a winding-up. The PPDS would also absorb the Participation Percentage of any consolidated post-tax losses recorded by the Society, any such amount being debited to a reserve account maintained by the Society for the purpose of the PPDS (the PPDS Reserve Account). Any net profits which are eligible to be paid to holders of PPDS as dividends but which are not so paid would be credited to the PPDS Reserve Account. No dividends may be paid on the PPDS in years where the Society incurs consolidated post-tax losses or where the PPDS Reserve Account is in deficit as a result of previous years' losses.

The conversion feature is considered to be an embedded derivative requiring separate recognition. There was a gain arising on the recognition of the embedded derivative in May 2010 of £0.1m although as this is based on an internal cashflow model with no observable market data, this gain has not been recognised in these financial statements in accordance with IAS 39. The fair value of the embedded derivative has not changed materially as at 31 December 2011 and therefore a market value of £nil has been recorded.

29 Subscribed capital

	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
12.625% permanent interest bearing shares	10.0	10.0	10.0	10.0
10.750% permanent interest bearing shares	10.0	10.0	10.0	10.0
12.250% permanent interest bearing shares	10.0	10.0	10.0	10.0
	30.0	30.0	30.0	30.0
Less: unamortised issue costs	(0.1)	(0.1)	(0.1)	(0.1)
Less: unamortised capital exchange costs	(0.3)	(0.3)	(0.3)	(0.3)
	29.6	29.6	29.6	29.6

The subscribed capital was issued for an indeterminate period and is only repayable in the event of the winding up of the Society.

The £10.0m 12% permanent interest bearing shares were included in the Capital Agreement as described in Note 28.

30 Note to the Cash Flow Statements

Reconciliation of profit / (loss) before taxation to net cash inflow / (outflow) from operating activities	GROUP 2011 £m	GROUP 2010 £m	SOCIETY 2011 £m	SOCIETY 2010 £m
Profit / (loss) before taxation and dividends	0.1	(4.7)	(3.3)	(6.7)
Depreciation	2.9	3.2	2.7	2.9
Interest on subordinated liabilities	2.2	1.1	2.2	1.1
Interest on subscribed capital	3.6	3.6	3.6	3.6
Decrease in derivative financial instruments	(6.9)	(6.5)	(3.9)	(5.6)
Increase / (decrease) in other financial liabilities at fair value through profit or loss	0.8	5.1	(2.0)	4.3
Changes in retirement benefit obligations	3.0	0.5	3.0	0.5
(Gain) / loss on disposal of properties	(0.4)	0.2	(0.4)	0.2
Other non-cash movements	(38.0)	(15.2)	(38.1)	(11.1)
Net cash outflow before changes in operating assets and liabilities	(32.7)	(12.7)	(36.2)	(10.8)
Decrease in loans and advances to customers	353.8	134.8	276.2	101.4
Increase / (decrease) in shares	168.4	(194.2)	168.4	(194.2)
(Decrease) / increase in amounts due to other customers and deposits from banks	(106.1)	16.4	(106.8)	16.4
(Increase) / decrease in debt securities in issue	(70.5)	(31.7)	0.5	(1.0)
Increase / (decrease) in other assets, prepayments and accrued income	2.1	0.4	14.1	(3.7)
(Decrease) / increase in other liabilities	(0.3)	(5.3)	2.2	(1.3)
Net cash inflow / (outflow) from operating activities	314.7	(92.3)	318.4	(93.2)
Cash and cash equivalents				
Cash and balances with the Bank of England	162.3	204.6	162.3	204.6
Loans and advances to banks repayable on demand	0.8	20.0	0.7	2.6
Investment securities	214.9	136.3	214.9	136.3
At 31 December	378.0	360.9	377.9	343.5

Cash and cash equivalents comprise cash in hand, balances with the Bank of England, loans and advances to banks available on demand or with original maturities of three months or less and investment securities with a maturity period of three months or less i.e. highly liquid assets readily convertible into cash.

31 Guarantees, contingent liabilities and commitments

(i) Until 11 June 1996, under Section 22 of the Building Societies Act 1986, the Society had an obligation to discharge the liabilities of its subsidiary undertakings insofar as they were unable to discharge the liabilities out of their own assets. Subsequently, the Society has voluntarily agreed to provide continued support to all of its subsidiary undertakings, insofar as any liabilities are not covered by legislation.

(ii) In common with other financial institutions, the Society has a contingent liability in respect of contributions to the Financial Services Compensation Scheme established under the Financial Services and Markets Act 2000. Details are given in Note 27.

(iii) In 2008, the Society received grant aid of £0.3 million in relation to the premises at Cobalt Business Park. In certain circumstances this grant could become repayable, although it is more likely that further grant will be claimed given the expansion of the Solutions business.

(iv) Commitments

The Society has no capital commitments for the acquisition of property, plant and equipment at 31 December and for which no provision has been made in the Accounts.

	GROUP and SOCIETY 2011 £m	GROUP and SOCIETY 2010 £m
Irrevocable undrawn committed loan facilities	33.5	61.5

Payments under non-cancellable operating lease agreements

Total minimum lease payments:

	GROUP and SOCIETY 2011 £m	GROUP and SOCIETY 2010 £m
Within one year	1.6	1.7
In one to five years	5.6	5.7
Over five years	5.6	7.5
	12.8	14.9

32 Retirement benefit obligations

Group and Society Pension schemes

The Group operates a Final Salary 'defined benefit' scheme, the Newcastle Building Society Pension and Assurance Scheme ("the Scheme"). The Scheme was closed to future benefit accrual with effect from 30 November 2010. Pension benefits for deferred members are based on the members' final pensionable salaries and service at the date accrual ceased (or date of leaving if earlier).

The Group has applied IAS 19 (Revised 2004) to the scheme and the following disclosures relate to this Standard. Any accumulated gains and losses in each period are recognised in the Statements of Comprehensive Income, unless recognised in the Income Statements.

The pension scheme assets do not include assets from Newcastle Building Society.

The amounts recognised in the Balance Sheets are as follows:	2011 £m	2010 £m
Present value of pension obligation	74.5	71.5
Fair value of scheme assets	(73.3)	(71.5)
Net pension liability	1.2	-

The amounts recognised in the Income Statements are as follows:		
Current service cost	-	0.5
Interest on obligation	3.8	3.8
Expected return on scheme assets	(4.2)	(4.0)
Gain on curtailments	-	(2.0)
Total included in staff costs	(0.4)	(1.7)
Actual return on scheme assets	1.3	7.2

Changes in the present value of the defined benefit obligation are as follows:		
Opening defined benefit obligation	71.5	68.8
Current service cost	-	0.5
Interest cost	3.8	3.8
Actuarial losses	1.1	3.8
Contributions by employees	-	0.2
Curtailments	-	(2.0)
Benefits paid	(1.9)	(3.6)
Closing defined benefit obligation	74.5	71.5

Changes in the fair value of scheme assets are as follows:		
Opening fair value of scheme assets	71.5	66.6
Expected return	4.2	4.0
Actuarial (losses) / gains	(2.9)	3.2
Contributions by employer	2.4	1.1
Contributions by employees	-	0.2
Benefits paid	(1.9)	(3.6)
Closing fair value of scheme assets	73.3	71.5

32 Retirement benefit obligations Continued

The major categories of Scheme assets as a percentage of total Scheme assets are as follows:	2011	2010
Equities	53.3%	58.5%
Corporate Bonds	7.5%	7.1%
Government Bonds	36.3%	34.4%
Cash	2.9%	-

Principal actuarial assumptions at the Balance Sheet date (expressed as weighted averages)		
Discount rate	4.95%	5.40%
Future salary increases	-	-
Future pension increases in line with RPI to 5% per annum	3.1%	3.4%
Inflation assumptions - RPI	3.2%	3.6%
- CPI	2.1%	2.8%

Mortality - current pensioners		
Life expectancy at age 62		
Males	24.6 years	23.8 years
Females	26.9 years	26.5 years

Mortality - future pensioners		
Life expectancy at age 62 (aged 42 now):		
Males	26.1 years	25.9 years
Females	28.5 years	28.5 years

At 31 December, the pre and post retirement mortality is assumed based on S1PA CMI 2010 M/F (year of birth) tables with a 1% improvement (2010: S1PAmc (year of birth) with 1% minimum improvement)

100% of members are assumed to commute the maximum pension possible for cash at retirement, in line with current cash commutations. Previously an allowance of 50% of members was made.

Where investments are held in bonds and cash, the expected long-term rate of return is taken to be the yields generally prevailing on such assets at the Balance Sheet date. A higher rate of return is expected on equity investments, which is based more on realistic future expectations than on the returns that have been available historically. The overall expected long term rate of return on assets is then the average of these rates, taking into account the underlying asset portfolio of the pension scheme.

The expected rates of return for each asset class, gross of Scheme expenses, were:	2011	2010
Equities	7.70%	7.50%
Corporate Bonds	4.70%	5.40%
Government Bonds	2.50%	4.00%
Cash	2.00%	0.50%

Amounts for the current and previous four periods are as follows:

	2011 £m	2010 £m	2009 £m	2008 £m	2007 £m
Defined benefit obligation	74.5	71.5	68.8	57.3	66.5
Scheme assets	(73.3)	(71.5)	(66.6)	(49.5)	(63.1)
Deficit	1.2	-	2.2	7.8	3.4
Experience adjustments on plan liabilities	-	-	(2.2)	0.7	0.3
Experience adjustments on plan assets	(2.9)	3.2	5.2	(18.2)	(0.2)

Analysis of amounts recognised in Statements of Comprehensive Income:

	2011 £m	2010 £m
Total amount of actuarial losses recognised in the Statements of Comprehensive Income for the year:	(3.9)	(0.5)
Cumulative amount of actuarial losses recognised in the Statements of Comprehensive Income at the year end:	(18.2)	(14.3)

Future funding obligation

Following the valuation as at 30 June 2010, the Society has agreed to pay annual contributions of £2.0m increasing at 5.0% pa for 10 years with a final payment of £1.65m in 2021. The Society will also contribute 20% of annual profits in excess of £8.5m. The Society expects to pay £2.1m into the Scheme during the accounting year beginning 1 January 2012.

Unfunded pension arrangements

In addition to the Scheme, the Society provides benefits to two members via a separate unfunded arrangement. The value of these benefits on the assumptions given above was £0.1m at 31 December 2011.

33 Related parties

The Group is controlled by Newcastle Building Society which is registered in England and Wales and operates in the United Kingdom. Further details of subsidiary undertakings are disclosed in Note 16 to these Accounts. The Directors are considered to be the only key management personnel as defined by IAS 24.

Transactions with directors and their close family members

Directors and their close family members have entered into the following transactions with Newcastle Building Society in the normal course of business.

Loans outstanding to directors and their close family members

	2011 £000	2010 £000
At 31 December	200	200

These loans were made on normal commercial terms and a register of them is available for inspection at the Principal Office for a period of 15 days up to and including the Annual General Meeting.

Deposits and investments held by directors and their close family members

	2011 £000	2010 £000
At 31 December	491	399

Amounts deposited by Directors and members of their close families earn interest on the same terms and conditions applicable to other customers.

Other transactions

Mrs CRR Vine-Lott is Chairman of Openwork Holdings Limited. During 2011, commission of £5.9m (2010: £5.1m) was received by one of the Society's subsidiary companies, Newcastle Financial Services Limited from Openwork. During the same period Newcastle Financial Services paid £45,102 (2010: £45,485) to Openwork in respect of a franchise fee/regulatory support charges.

33 Related parties Continued

Year ended 31 December 2011

	Interest paid to Society £000	Interest received from Society £000	Rent received from Society £000	Other amounts paid to Society £000	Other amounts received from Society £000
Kings Manor Properties Limited	544	-	-	1,126	-
Newcastle Financial Services Limited	-	-	-	3,000	-
Newcastle Mortgage Loans (Jersey) Limited	1,721	-	-	8,050	-
Newcastle Portland House Limited	-	11	66	-	-
Newton Facilities Management Limited	-	-	-	333	335

Year ended 31 December 2010

	Interest paid to Society £000	Interest received from Society £000	Rent received from Society £000	Other amounts paid to Society £000	Other amounts received from Society £000
Kings Manor Properties Limited	235	-	-	575	-
Newcastle Financial Services Limited	-	1	-	3,000	-
Newcastle Mortgage Loans (Jersey) Limited	2,027	-	-	8,738	-
Newcastle Portland House Limited	-	8	66	-	-
Newton Facilities Computer Purchasing Limited	11	-	-	-	-
Newton Facilities Management Limited	-	-	-	308	310

At the year end the following unsecured balances were outstanding.

	Amounts owed by Society 2011 £000	Amounts owed to Society 2011 £000	Amounts owed by Society 2010 £000	Amounts owed to Society 2010 £000
Adamscastle Limited	-	-	-	1,320
Adamson Newcastle Limited	-	-	36	-
Kings Manor Properties Limited	222	16,857	147	15,168
NBS Financial Services Limited	-	-	81	149
Newcastle Building Society Covered Bonds LLP	-	-	-	3,503
Newcastle Developments Limited	-	-	-	437
Newcastle Mortgage Corporation Limited	-	-	7	-
Newcastle Mortgage Loans (Jersey) Limited	-	25,465	-	31,647
Newcastle Mortgage Services Limited	-	-	5	-
Newcastle Portland House Limited	2,922	4	2,916	7
Newcastle Strategic Solutions Limited	505	487	505	487
Newcastle Financial Services Limited	4,394	3,467	3,620	2,485
Newton Facilities Management Limited	129	71	113	70
Newton Facilities Computer Purchasing Limited	-	-	109	373
Strachans (Newcastle) Limited	-	-	591	5
NBS Mortgage Advisor Limited	-	-	7	21

Transactions with securitisation vehicles

Newcastle Building Society undertook the following transactions with securitisation vehicles up until repayment.

	Interest paid to Society 2011 £000	Interest received from Society 2011 £000	Interest paid to Society 2010 £000	Interest received from Society 2010 £000
Bamburgh Finance No. 1 PLC	-	-	922	-

At the year end the following balances were outstanding with securitisation vehicles.

	Loans owed by Society 2011 £000	Loans owed to Society 2011 £000	Loans owed by Society 2010 £000	Loans owed to Society 2010 £000
Bamburgh Finance No. 1 PLC	-	-	-	10,509

Administration expenses of £7,722 were paid to Newcastle Building Society up to the call date (2010: £131,651).

34 Financial instruments

These disclosures are given on a Group basis, unless otherwise stated, as the risks of the organisation are managed on a Group basis. Society disclosures are given where management information is also reported on that basis.

Categories of financial instruments
Financial assets and liabilities are measured on an on-going basis either at fair value or at amortised cost.

The accounting policies note describes how the classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the financial assets and liabilities in the balance sheet by the class of financial instrument to which they are assigned and by the measurement basis.

		Amortised cost	Available for sale	Held to maturity	Fair value through income statements	Total
Group as at 31 December 2011	Note	£m	£m	£m	£m	£m
Financial assets						
Cash in hand and balances with Bank of England		162.3	-	-	-	162.3
Loans and advances to banks	11	254.1	-	-	-	254.1
Debt securities	12	-	749.7	14.8	-	764.5
Derivative financial instruments	34	-	-	-	44.3	44.3
Fair value adjustments for hedged risk	15	-	-	-	57.9	57.9
Loans and advances to customers	14	2,976.6	-	-	-	2,976.6
Assets pledged as collateral	13	85.1	-	-	-	85.1
Total financial assets		**3,478.1**	**749.7**	**14.8**	**102.2**	**4,344.8**
Financial liabilities						
Due to customers - shares	22	3,744.5	-	-	16.9	3,761.4
Fair value adjustments for hedged risk	15	-	-	-	28.7	28.7
Due to other customers	23	157.2	-	-	-	157.2
Deposits from banks	24	107.6	-	-	-	107.6
Debt securities in issue	25	16.0	-	-	-	16.0
Derivative financial instruments	34	-	-	-	57.4	57.4
Subordinated liabilities	28	58.7	-	-	-	58.7
Subscribed capital	29	29.6	-	-	-	29.6
Total financial liabilities		**4,113.6**	**-**	**-**	**103.0**	**4,216.6**

34 Financial instruments Continued

	Amortised cost	Available for sale	Held to maturity	Fair value through income statements	Total
Group as at 31 December 2010	£m	£m	£m	£m	£m
Financial assets					
Cash in hand and balances with Bank of England	204.6	-	-	-	204.6
Loans and advances to banks	162.6	-	9.8	-	172.4
Debt securities	-	403.0	43.9	-	446.9
Derivative financial instruments	-	-	-	34.2	34.2
Fair value adjustments for hedged risk	-	-	-	50.8	50.8
Loans and advances to customers	3,325.1	-	-	-	3,325.1
Assets pledged as collateral	105.4	-	-	-	105.4
Total financial assets	**3,797.7**	**403.0**	**53.7**	**85.0**	**4,339.4**
Financial liabilities					
Due to customers - shares	3,581.4	-	-	11.6	3,593.0
Fair value adjustments for hedged risk	-	-	-	20.8	20.8
Due to other customers	220.8	-	-	-	220.8
Deposits from banks	150.1	-	-	-	150.1
Debt securities in issue	86.5	-	-	-	86.5
Derivative financial instruments	-	-	-	54.2	54.2
Subordinated liabilities	58.6	-	-	-	58.6
Subscribed capital	29.6	-	-	-	29.6
Total financial liabilities	**4,127.0**	**-**	**-**	**86.6**	**4,213.6**

34 Financial instruments Continued

Fair values of financial assets and liabilities

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not presented on the Group's or Society's Balance Sheet at their fair value.

GROUP

	Note	Carrying value 2011 £m	Carrying value 2010 £m	Fair value 2011 £m	Fair value 2010 £m
Financial assets					
Cash and balances with the Bank of England		162.3	204.6	162.3	204.6
Loans and advances to banks	11	254.1	172.4	254.2	170.9
Debt securities held to maturity	12	14.8	42.8	12.9	41.3
Loans and advances to customers	14	2,976.6	3,325.1	3,354.4	3,460.8
Assets pledged as collateral	13	85.1	105.4	85.1	105.4
Financial liabilities					
Due to customers - shares	22	3,761.4	3,593.0	3,876.1	3,661.7
Due to other customers	23	157.2	220.8	157.6	221.1
Deposits from banks	24	107.6	150.1	107.6	150.1
Debt securities in issue	25	16.0	86.5	16.3	86.8
Subordinated liabilities	28	58.7	58.6	67.3	67.2
Subscribed capital	29	29.6	29.6	31.6	33.5

SOCIETY

	Note	Carrying value 2011 £m	Carrying value 2010 £m	Fair value 2011 £m	Fair value 2010 £m
Financial assets					
Cash and balances with the Bank of England		162.3	204.6	162.3	204.6
Loans and advances to banks	11	254.0	155.0	254.2	153.6
Debt securities held to maturity	12	14.8	42.8	12.9	41.3
Loans and advances to customers	14	2,951.0	3,221.9	3,322.5	3,355.0
Assets pledged as collateral	13	85.1	105.4	85.1	105.4
Financial liabilities					
Due to customers - shares	22	3,761.4	3,593.0	3,876.1	3,661.7
Due to other customers	23	160.3	224.6	160.6	224.8
Deposits from banks	24	107.6	150.1	107.6	150.1
Debt securities in issue	25	16.0	15.5	16.3	15.8
Subordinated liabilities	28	58.7	58.6	67.3	67.2
Subscribed capital	29	29.6	29.6	31.6	33.5

Loans and advances to banks
Loans and advances to banks includes inter-bank placements and items in the course of collection.

The fair value of floating rate and overnight deposits is their carrying amount. The fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and remaining maturity.

Loans and advances to customers
Loans and advances to customers are net of provisions for impairment. The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

Due to customers
The fair value of shares is assumed to approximate to the amount payable at the Balance Sheet date.

Deposits from banks
The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest bearing deposits and other borrowings without market price is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

Debt securities in issue
The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, a discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

34 Financial instruments Continued

Fair value measurement

The following table summarises the fair value measurement basis used for assets and liabilities held on the Balance Sheet at fair value:

2011
GROUP and SOCIETY

	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets				
Debt securities - available for sale	749.7	-	-	749.7
Derivative financial instruments	-	44.3	-	44.3

Derivatives held for hedging

Derivative financial instruments used by the Group have been described previously in the Risk Management Report.
The fair values of the derivative instruments held are set out below:

GROUP	2011 Notional Amount £m	2011 Fair Value Assets £m	2011 Fair Value Liabilities £m	2010 Notional Amount £m	2010 Fair Value Assets £m	2010 Fair Value Liabilities £m
At 31 December						
Interest rate swaps designated as fair value hedges	3,057.0	44.1	(56.4)	3,149.9	31.1	(46.9)
Interest rate swaps	145.3	0.2	(1.0)	389.8	3.1	(7.3)
		44.3	(57.4)		34.2	(54.2)

SOCIETY	2011 Notional Amount £m	2011 Fair Value Assets £m	2011 Fair Value Liabilities £m	2010 Notional Amount £m	2010 Fair Value Assets £m	2010 Fair Value Liabilities £m
At 31 December						
Interest rate swaps designated as fair value hedges	3,057.0	44.1	(56.4)	3,149.9	31.1	(46.9)
Interest rate swaps	145.3	0.2	(1.0)	298.2	3.1	(4.3)
		44.3	(57.4)		34.2	(51.2)

Hedge Ineffectiveness

	2011 £m	2010 £m
Gains on hedging instruments	6.1	6.5
Losses on hedged items attributable to the hedge risk	(5.3)	(7.4)
Net losses representing ineffective portions of the fair value hedges	**0.8**	**(0.9)**

34 Financial instruments Continued

Liquidity risk

For each material category of financial liability a maturity analysis is provided in Notes 24 and 25, which represents the contractual maturities.

The table below analyses the Group's financial liabilities, which will be settled on a net basis, into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying balances as the impact of discounting is not significant.

GROUP

At 31 December 2011	Repayable on demand	Up to 3 months	Between 3 and 12 months	Between 1 and 5 years	Over 5 years	Total
Due to customers - shares	1,580.1	1,402.1	582.3	196.3	0.6	3,761.4
Due to other customers	6.3	98.5	51.3	1.1	-	157.2
Deposits from banks	0.3	66.0	41.3	-	-	107.6
Debt securities in issue	-	-	16.0	-	-	16.0
Derivative financial instruments	-	-	0.9	7.1	49.4	57.4
Fair value adjustments for hedged risk	-	-	1.5	27.2	-	28.7

At 31 December 2010	Repayable on demand	Up to 3 months	Between 3 and 12 months	Between 1 and 5 years	Over 5 years	Total
Due to customers - shares	1,422.5	1,308.0	637.4	218.0	7.1	3,593.0
Due to other customers	6.8	163.5	49.3	1.2	-	220.8
Deposits from banks	0.3	41.7	50.7	57.4	-	150.1
Debt securities in issue	-	-	8.0	7.5	71.0	86.5
Derivative financial instruments	-	0.2	1.7	13.5	38.8	54.2
Fair value adjustments for hedged risk	-	-	2.1	18.7	-	20.8

Equity risk

The Group has no material direct exposure to equity risk. The Group has a number of structured products which have an embedded derivative attached to them i.e. the return payable is derived from the performance of an underlying index. Under IAS 39 both the underlying product and the derivative are fair value accounted through the Income Statements. The fair value amounts are approximately equal and offsetting so there is no material charge or credit in the accounts.

34 Financial instruments Continued

Credit risk

Note 14 of the Accounts on page 42 contains details of total mortgage assets.

The average loan to value (LTV) ratio of the Group's loans and advances to customers is estimated to be **63.4%** (2010: 65.8%). Further LTV and payment performance information is shown below:

Group and Society prime residential mortgage book

The Prime residential mortgage book consists of traditional residential loans. No sub-prime or self-certification lending has been undertaken.

Loan to value (indexed)	2011 £m	2011 %	2010 £m	2010 %
<70%	1,115.6	74.9	1,262.1	76.1
70% - <80%	175.1	11.8	180.7	10.9
80% - <90%	121.0	8.1	120.2	7.3
>90%	77.3	5.2	94.9	5.7
	1,489.0	100.0	1,657.9	100.0

The table below provides further information by payment due status:

	2011 £m	2011 %	2010 £m	2010 %
Neither past due nor impaired	1,456.5	97.8	1,617.0	97.4
Past due up to 3 months but not impaired	19.6	1.3	28.6	1.7
Impaired:				
Past due 3 to 6 months	7.3	0.5	6.7	0.4
Past due over 6 months	4.9	0.3	4.5	0.3
In possession	0.7	0.1	1.2	0.2
	1,489.0	100.0	1,657.9	100.0

Against past due and possession cases, **£211.6m** (2010: £310.1m) of collateral is held.

No loans that would be past due or impaired have had terms renegotiated.

Specialist residential mortgage book

The Specialist residential mortgage book consists of buy-to-let and residential investment loans.

Loan to value (indexed)	2011 £m	2011 %	2010 £m	2010 %
<70%	22.1	9.8	32.6	12.0
70% - <80%	57.2	25.3	25.6	9.4
80% - <90%	57.5	25.4	54.3	19.9
>90%	89.4	39.5	159.7	58.7
	226.2	100.0	272.2	100.0

The table below provides further information by payment due status:

	2011 £m	2011 %	2010 £m	2010 %
Neither past due nor impaired	200.0	88.4	246.9	90.7
Past due up to 3 months but not impaired	5.0	2.2	5.6	2.0
Not passed due but impaired	3.1	1.4	-	-
Impaired and past due 3 to 6 months	0.1	0.1	0.2	0.1
Impaired and past due over 6 months	1.0	0.4	1.9	0.7
LPA receivership	6.1	2.7	-	-
In possession	10.9	4.8	17.6	6.5
	226.2	100.0	272.2	100.0

Against past due, LPA receivership and possession cases, **£27.0m** (2010: £23.0m) collateral is held.

One loan of £2.5m that would be past due or impaired has had terms renegotiated.

34 Financial instruments Continued

Commercial lending book

Following the securitisation call in February 2011, all Group commercial loan exposures are held by the Society.

The commercial lending book comprises:

GROUP	2011 £m	2011 %	2010 £m	2010 %
Loans secured on commercial property	393.3	31.4	489.5	36.0
Loans to Housing Associations	858.8	68.6	869.8	64.0
	1,252.1	100.0	1,359.3	100.0

Loans secured on commercial property **Loan to value**	2011 £m	2011 %	2010 £m	2010 %
<70%	68.2	17.3	115.5	23.6
70% - <80%	95.1	24.2	130.4	26.6
80% - <90%	104.9	26.7	183.6	37.5
>90%	125.1	31.8	60.0	12.3
	393.3	100.0	489.5	100.0

Valuations are carried out on a regular basis and movements into higher LTV bands represent latest valuations, consistent with falls in commercial property values since loan origination.

The table below provides further information by payment due status:

	2011 £m	2011 %	2010 £m	2010 %
Neither past due nor impaired	343.6	87.4	486.1	99.3
Past due but not impaired	4.3	1.1	0.6	0.1
Not past due but impaired	25.3	6.4	-	-
Impaired and past due up to 3 months	11.2	2.8	2.5	0.5
Impaired and past due 3 to 6 months	2.7	0.7	-	-
Impaired and past due over 6 months	2.7	0.7	-	-
LPA receivership	3.1	0.8	-	-
In possession	0.4	0.1	0.3	0.1
	393.3	100.0	489.5	100.0

No loans that would be past due or impaired have had terms renegotiated.

Loans secured on commercial property are diversified by industry type and an analysis is shown below:

	2011 £m	2011 %	2010 £m	2010 %
Retail	193.1	49.1	211.1	43.1
Office	58.3	14.8	68.3	14.0
Industrial	50.2	12.8	79.2	16.2
Hotel / Leisure	74.9	19.0	92.2	18.8
Other	16.8	4.3	38.7	7.9
	393.3	100.0	489.5	100.0

34 Financial instruments Continued

SOCIETY	2011 £m	2011 %	2010 £m	2010 %
Loans secured on commercial property	393.3	31.4	403.4	31.7
Loans to Housing Associations	858.8	68.6	869.8	68.3
	1,252.1	100.0	1,273.2	100.0

Loans secured on commercial property **Loan to value**	2011 £m	2011 %	2010 £m	2010 %
<70%	68.2	17.3	58.9	14.6
70% - <80%	95.1	24.2	120.3	29.8
80% - <90%	104.9	26.7	164.2	40.7
>90%	125.1	31.8	60.0	14.9
	393.3	100.0	403.4	100.0

Valuations are carried out on a regular basis and movements into higher LTV bands represent latest valuations, consistent with falls in commercial property values since loan origination.

The table below provides further information by payment due status:

	2011 £m	2011 %	2010 £m	2010 %
Neither past due nor impaired	343.6	87.4	402.5	99.8
Past due but not impaired	4.3	1.1	0.6	0.1
Not past due but impaired	25.3	6.4	-	-
Impaired and past due up to 3 months	11.2	2.8	-	-
Impaired and past due 3 to 6 months	2.7	0.7	-	-
Impaired and past due over 6 months	2.7	0.7	-	-
LPA receivership	3.1	0.8	-	-
In possession	0.4	0.1	0.3	0.1
	393.3	100.0	403.4	100.0

No loans that would be past due or impaired have had terms renegotiated.

Loans secured on commercial property are diversified by industry type and an analysis is shown below:

	2011 £m	2011 %	2010 £m	2010 %
Retail	193.1	49.1	167.4	41.5
Office	58.3	14.8	54.2	13.4
Industrial	50.2	12.8	65.0	16.1
Hotel / Leisure	74.9	19.0	79.7	19.8
Other	16.8	4.3	37.1	9.2
	393.3	100.0	403.4	100.0

GROUP and SOCIETY

Loans to Housing Associations

Loan to value (unindexed)	2011 £m	2011 %	2010 £m	2010 %
<70%	325.8	37.9	241.1	27.8
70% - <80%	158.9	18.5	190.0	21.8
80% - <90%	273.9	31.9	438.7	50.4
>90%	100.2	11.7	-	-
	858.8	100.0	869.8	100.0

Loans to Housing Associations are secured on residential property.

No Housing Associations Loans are past due or impaired, indeed this has been the case for the last 16 years of lending to the sector.

34 Financial instruments Continued

Interest Rate Risk

Interest rate risk is the exposure of the Group's net interest income to movement in interest rates. This is managed using a combination of limits set by the Board and by use of derivative instruments. The sensitivity to interest rate movements is measured using dynamic stress tests for a series of parallel rate shifts over various time periods.

The table below shows the impact of various interest rate scenarios on Group profit before tax, against the Society's current interest rate view.

	+1% £m	+2% £m	-1% £m	-2% £m
At 31 December 2011				
Next 12 months	**-**	**0.1**	**-**	**-**
Next 2 years	**(0.3)**	**(0.6)**	**-**	**-**
Next 3 years	**(0.9)**	**(1.8)**	**-**	**-**
At 31 December 2010				
Next 12 months	0.1	0.2	-	-
Next 2 years	(0.3)	(0.7)	-	-
Next 3 years	-	-	-	-

The main risk measure used by the Assets and Liabilities Committee (ALCO) is an immediate 2% parallel shift in all interest rates.

Due to the low interest rate environment the interest rate shifts for -1% and -2% are not currently reported to ALCO. This position is reviewed in the light of movements in interest rates.

An immediate 2% upward movement in interest rates would increase Members' Interests by **£5.7m** (2010: £1.9m increase).

The derivative gains less losses for the year in respect of fair value hedges comprise gains on derivatives of **£6.9m** (2010: £11.7m gain) and associated losses on hedged items of **£6.1m** (2010: £10.8m loss).

Interest rate risk in the pension schemes

A reduction of 0.1% in the discount rate would increase the pension deficit by approximately **£1.3m**.

Currency risk

The Group has no exposure to currency risk.

1 Statutory percentages

	2011 %	Statutory %
Lending limit	**18.04**	25.00
Funding limit	**6.95**	50.00

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986 as amended by the Building Societies Act 1997.

The lending limit measures the proportion of business assets not in the form of loans secured on residential property. Business assets are the total assets of the Group plus allowances for losses on loans and advances less liquid assets, investment properties and property, plant and equipment as shown in the Group balance sheet.

	2011 %	2010 %
Lending limit excluding all IAS39 adjustments for derivative financial instruments and fair value adjustments for hedged risk	**15.21**	15.48

The funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals.

The statutory limits are as laid down under the Building Societies Act 1986, as amended by the Building Societies Act 1997, and ensure that the principal purpose of a building society is that of making loans which are fully secured on residential property and are funded substantially by its members.

2 Other percentages

	2011 %	2010 %
As a percentage of shares and borrowings:		
Gross capital	**6.44**	6.65
Free capital	**5.49**	5.79
Liquid assets	**29.18**	25.21
Loss for the year as a percentage of mean total assets	**(0.02)**	(0.08)
Management expenses as a percentage of mean total assets excluding Repositioning Programme	**0.80**	0.82
Management expenses as a percentage of mean total assets including Repositioning Programme	**0.80**	0.91

The above percentages have been prepared from the Group Accounts.

Gross capital represents the aggregate of the general reserve, available for sale reserve, subordinated liabilities and subscribed capital.

Free capital represents gross capital less property, plant and equipment, investment property and non-current assets held for sale.

Liquid assets are as shown in the Group Balance Sheets plus any other liquid assets which qualify as prudential liquidity.

Shares and borrowings represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue but exclude balances owed by special purpose vehicles.

Management expenses represent the aggregate of administrative expenses and depreciation.

Mean total assets is the average of the 2011 and 2010 total assets.

Annual Business Statement for the year ended 31 December 2011

Directors at 31 December 2011

	Date of Birth	Date of Appointment	Business Occupation	
DJ Buffham	**13.08.59**	**24.05.10**	**Company Director**	Directorships: Zytronic PLC; William Leech (Investments) Limited; William Leech Foundation; Governor of Northumbria University.
FD Holborn FCIB	**26.05.47**	**01.01.03**	**Company Director**	Directorships: Newcastle Portland House Limited; Rothley Trust (Vice Chairman).
RD Mayland FCA	**22.05.53**	**27.06.05**	**Company Director**	Directorships: Norprime Limited; Community Services North East Limited.
RJ McCormick FCA, FCIIA	**09.05.49**	**16.08.07**	**Business Consultant**	Directorships: Newcastle Strategic Solutions Limited; Grassington Hub.
PJ Moorhouse FCCA	**18.01.53**	**31.10.11**	**Company Director**	Directorships: Renew (North East); Molins PLC; Cumbria NHS Partnership Foundation Trust.
J Morris BA, FCA	**13.09.56**	**31.10.11**	**Chartered Accountant**	Directorships: Weston Park Hospital Cancer Care and Research Fund (Trustee).
AM Russell BA, FCA, CPA	**18.03.67**	**01.07.10**	**Building Society Finance Director**	Directorships: Bamburgh Finance No 1 PLC; Bamburgh Options Limited; St Cuthberts Care Limited; Newcastle Card Solutions Limited; Newcastle Financial Services Limited; Newcastle Mortgage Loans (Jersey) Limited; Newton Facilities Management Limited; Newcastle Portland House Limited
G Tiplady LLB	**30.09.65**	**11.01.11**	**Building Society Business Services Director**	Directorships: Kings Manor Properties Limited; Newcastle Card Solutions Limited; Newton Facilities Management Limited; Seven Stories, the Centre for Children's Books (Trustee).
JH Warden MBA, ACA, MA, BA	**04.05.61**	**07.10.10**	**Building Society Operations Director**	Directorships: Newcastle Financial Services Limited; Katalysts Limited; Newcastle Strategic Solutions Limited; 22 St. Georges Terrace Limited.
JH Willens MBA, ACIB	**07.06.56**	**04.01.10**	**Building Society Chief Executive**	Directorships: Kings Manor Properties Limited; Brown Shipley and Company Limited.
CRR Vine-Lott MBA, FCISI, FCIM, ACIB	**30.01.60**	**01.01.10**	**Director in Financial Services**	Directorships: Openwork Holdings Limited; Rathbone Brothers PLC; Cranfield University.

Documents may be served on any of the above named Directors: "Newcastle Building Society" c/o Addleshaw Goddard LLP (Ref. GAB), at the following address: Sovereign House, PO Box 8, Sovereign Street, Leeds LS1 1HQ. The Executive Directors have service contracts which are terminable at any time by the Society on six months notice. There are no contracts for Non Executive Directors and no compensatory terms for loss of office.

Other Officers at 31 December 2011

	Business Occupation	
P Ferguson BSc, CA	**Building Society Executive**	Directorships: Newcastle Building Society Pension & Assurance Scheme (Trustee).
PG Grand MCMI, DMS, MBA	**Building Society Executive**	Directorships: Newcastle Strategic Solutions Limited.
PJ Green BA (Hons)	**Building Society Executive**	Directorships: Newcastle Building Society Pension & Assurance Scheme (Trustee).
CW Jopling BA	**Building Society Executive**	
S Marks ACIBS, DMS	**Building Society Executive**	
SA Urwin BSc, DipM	**Building Society Executive**	Directorships: Newcastle Financial Services Limited, Newcastle Mortgage Loans (Jersey) Limited.
S Watchman BSc	**Building Society Executive**	
I Good FMAAT	**Group Secretary**	

Glossary

Set out below are the definitions of the terms used within the Annual Report and Accounts to assist the reader and to facilitate comparison with other financial institutions:

Arrears - A customer is in arrears when they are behind in their mortgage payments with the result that an outstanding loan commitment is overdue.

Administrative expenses - Expenses incurred in running the day to day activities of the Society including staff, property, marketing and technology costs and certain fees and commissions payable.

Basel II - The second of the Basel Accords, issued by the Basel Committee on Banking supervision, which defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. Basel II became law in the EU Capital Requirements Directive, and was implemented in the UK via the FSA Handbook.

Commercial lending / mortgage - Loans secured on commercial property.

Contractual maturity - The final payment date of a loan or other financial instrument, at which point all the remaining outstanding principal and interest is due to be paid.

Core Tier 1 capital - Defined by the FSA as general reserves which for the Society is the accumulation of retained profits.

Covered bonds - Debt securities backed by a portfolio of mortgages that is segregated from the issuer's other on-balance sheet assets solely for the benefit of the holders of the covered bonds.

Credit risk - This is the risk that a customer or counterparty is unable to honour their repayment obligations as they fall due.

Debt securities - Assets representing certificates of indebtedness of credit institutions, public bodies or other undertakings excluding those issued by central banks.

Derivative financial instruments - A derivative financial instrument is a type of financial instrument (or an agreement between two parties) that has a value based on the underlying asset, index or reference rate it is linked to. The Group uses derivative financial instruments to hedge its exposures to interest rate risk.

Effective interest rate method (EIR) - The method used to measure the carrying value of a financial asset or a liability and to allocate associated interest income or expense over the relevant period.

Fair value - Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial Services Compensation Scheme (FSCS) - The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every firm authorised by the FSA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.

Free capital - Represents gross capital less property, plant and equipment and investment property.

Funding limit - Measures the proportion of shares and borrowings not in the form of shares held by individuals.

Gilts - Gilt-edged securities are bonds issued by certain national governments. The Group only classifies debt securities issued by the Bank of England as Gilts.

Gross capital - The aggregate of general reserve, available-for-sale reserve, subscribed capital and subordinated liabilities.

Icelandic treasury investments - Treasury investments in Icelandic banks purchased prior to the collapse of the Icelandic banking system in October 2008, including Glitnir, Landsbanki, Heritable and Kaupthing Singer and Friedlander. Following the Icelandic banking collapse the Society wrote off significant amounts of these exposures in its 2008 accounts.

Impaired loans - Loans where an event has occurred which indicates the Group does not expect to collect all the contractual cash flows due, or expects to collect them later than they are contractually due.

Individually / collectively assessed - Individual assessments are made of all mortgage loans where objective evidence indicates losses are likely or the property is in possession. A collective impairment provision is made against the remaining group of loans and advances where objective evidence indicates that it is likely that losses may be realised.

Internal Capital Adequacy Assessment Process (ICAAP) - The Group's own assessment, as part of Basel II requirements, of the levels of capital that it needs to hold in respect of the risks it faces under a business as usual scenario and a variety of stress scenarios.

Legacy mortgage portfolio - Mortgage loan books where the Group has ceased new lending and is winding down exposures.

Lending limit - Measures the proportion of business assets not in the form of loans fully secured on residential property.

Liquid assets - Total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities.

Liquidity risk - The risk that the Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash inflows and outflows.

Loan-to-value ratio (LTV) - A ratio which expresses the amount of a mortgage as a percentage of the value of the property. The Group calculates UK residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index.

Loans and advances to banks - Treasury investments purchased with banking institutions.

Management expenses - Management expenses represent administrative expense and depreciation. The management expense ratio is management expenses expressed as a percentage of average total assets.

Market risk - The risk that movements in market risk factors, including re-pricing of assets and liabilities and the imperfect matching of interest rates between different asset and liability types.

Mean total assets - Represents the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.

Member - A person who has a share investment or a mortgage loan with the Society.

Net interest income - The difference between interest received on assets and interest paid on liabilities.

Non Executive Director - A member of the Society's Board who does not form part of the executive management team. He or she is not an employee of the Society.

Operational risk - The risk of loss arising from inadequate or failed internal processes, people and systems or from external events.

Other lending - loans and advances secured on traded endowment policies.

Past due - Loans on which payments are overdue including those on which partial payments are being made.

Permanent Interest Bearing Shares (PIBS) - Unsecured, deferred shares that are a form of Tier 1 capital. PIBS rank behind the claims of all subordinated debt holders, depositors, payables and investing members of Newcastle Building Society.

Prepaid cards business - The division of the Society which was licensed to issue cards loaded with electronic money.

Prime - Prime mortgages are those granted to the most credit worthy category of residential borrowers.

Renegotiated loans - Loans are classed as renegotiated with the customer's consent, when their terms have changed during the year. Loans and advances are generally renegotiated either as part of an on-going customer relationship or in response to an adverse change in the circumstances of the borrower.

Repo - Short to medium-term funding agreements which allow a borrower to sell a financial asset, such as Government bonds as security for cash. As part of the agreement the borrower agrees to repurchase the security at a later date. For the party selling the security (and agreeing to repurchase it in the future) it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future), it is a reverse repurchase agreement or reverse repo.

Repositioning Programme - The Board introduced a programme of measures in May 2010 to return the Group to the simplified, core activities of a building society focussing on members, employees and customers.

Residential mortgage backed securities (RMBS) - A category of asset backed securities that represent interests in a group of residential mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and / or principal).

Residential loans - Residential loans are secured against residential property.

Risk appetite - The articulation of the level of risk that the Group is willing to take (or not take) in order to safeguard the interests of the Society's members whilst achieving business objectives.

Risk-weighted asset (RWA) - The value of assets, after adjustment, under Basel II rules to reflect the degree of risk they represent. The Society measures RWA using the standardised approach.

Shares - Funds deposited by a person in a retail savings account with the Society. Such funds are recorded as liabilities for the Society.

Shares and borrowings - The total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue, including accrued interest.

Solutions business - a division of the Society that offers business to business services through people, process and innovative application of technology. Services include complete systems for smaller societies and white-labelled savings management for a range of banks and building societies.

Specialist Lending - Aggregate of the Group's residential investment and buy to let mortgage portfolios. No lending had taken place on this book since 2008 and the exposures are being reduced.

Subordinated debt / liabilities - A form of Tier 2 capital that is unsecured and ranks behind the claims of all depositors, creditors, and investing members (other than holders of PIBS).

Tier 1 capital - Tier 1 capital is divided into Core Tier 1 and other Tier 1 capital. Core Tier 1 capital comprises general reserves from retained profits. Other regulatory adjustments may be made for the purposes of capital adequacy. Qualifying capital instruments such as PIBS are included in other Tier 1 capital (i.e. not Core Tier 1).

Tier 2 capital - Comprises the Group's qualifying subordinated debt and collective impairment allowance (for exposures treated on a Basel II standardised basis). Certain regulatory deductions may be made for the purposes of assessing capital adequacy.

Wholesale funding - The total of amounts owed to credit institutions, amounts owed to other customers and debt securities in issue less balances deposited by offshore customers.