ANNUAL REPORT AND ACCOUNTS 2010

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CHAIRMAN'S STATEMENT

I am pleased to report that in 2010 Coventry Building Society maintained the excellent performance achieved throughout the economic downturn, delivering strong increases in the volume of mortgage and savings balances while adding to its capital reserves. In addition, in September, the Society completed the merger with the Stroud & Swindon Building Society and is well on the way to full integration of that Society's branches, products and systems with those of the Coventry.

These impressive results were delivered against a difficult economic background. Although the UK economy emerged from recession at the end of 2009, the recovery remained fragile. The scale of the UK's national debt and budget deficit revealed fundamental issues, exacerbated by the crisis in financial services, and it remains to be seen whether the private sector can offset any reduction in demand resulting from public sector cuts, the reduction in welfare benefits and increased taxes.

The realisation that the UK faced a new age of austerity impacted the housing market in 2010. Many financial organisations restricted lending in order to rebuild balance sheets and capital strength. As a result the housing market remained subdued with the total number of transactions approximately half that of pre-credit crunch trading.

In contrast, in this diminishing market, the Society increased the volume of net lending from £0.9 billion in 2009 to £1.6 billion in 2010, beating the previous highest share of the mortgage market that it achieved last year. With the addition of Stroud & Swindon, mortgage balances increased by £3.5 billion. After excluding the balances acquired on merger, the Society accounted for 19.0% of the growth in the UK mortgage market, up from the record 8% it achieved in 2009 and substantially more than its share of opening stock of 1.1%.

The capability to continue lending was built on success in securing funding, both retail and wholesale.

On retail funding, the Society achieved another outstanding performance in 2010. Savings balances grew by £2.2 billion, exceeding comfortably the substantial growth in net lending. This excludes the £2.2 billion of balances transferred in from Stroud & Swindon. This performance enabled the Society to post another record – that of the highest increase in savings balances ever recorded, well above the previous records set in 2007 and 2008. As a result, the Society was able to fund all of its mortgage growth through members' savings, capital and reserves.

On the wholesale side, the Society repeated the success of 2009 by securing further long-term funding. The transaction in September 2010 of a £400 million 12 year unsecured bond was again oversubscribed and showed the confidence investors have in Coventry's asset quality and long-term strength.

Another landmark for the Society was the successful merger with Stroud & Swindon Building Society.

The merger was announced formally on 23 March 2010 and was supported by nearly 90% of Stroud & Swindon members voting in June. It became effective on 1 September at which point the interest rates on many similar savings and mortgage accounts were aligned, immediately benefiting over 185,000 former Stroud members. This merger has resulted in a larger combined branch network and will provide additional efficiencies resulting from the increased scale of the new Group.

The major refurbishment programme of all 22 Stroud branches will be completed in early 2011 and we are ahead of schedule in our plans to enable the combined membership to transact at all branches across the extended network.

The ability to manage projects of this sensitivity and scope, whilst maintaining a very strong overall performance and with no degradation in service to members, is testament to the hard work and professionalism of all involved in both Coventry and Stroud.

The Society also maintained its sector leading management expense ratio, which demonstrates once again the importance we attach to spending members' money wisely which is why Coventry remains the most efficient building society in the UK.

The combination of growth in assets, prudent lending and continued cost efficiency enabled the Society to achieve a profit before tax of £100.6 million. After provision for tax, the sum of £84.9 million has been added to reserves.

The consistency of our financial performance has helped maintain the confidence of credit rating agencies, investors and members and the Society has retained 'A' ratings from the leading credit rating agencies throughout the financial crisis.

In summary, Coventry has once again achieved an exceptionally strong performance based on putting members' interests first. This performance spans all aspects of the Society's activities including the support we give to national charities and local communities. These achievements will be covered in more detail elsewhere in this report but I must mention one contribution of which I am particularly proud – the £4.6 million Coventry Building Society has donated, with the support of our members, to the Poppy Appeal since 2008.

The consistency with which the Society has delivered outstanding results since the onset of the credit crisis in 2007 reflects the strength of the traditional building society model and the very successful execution of a simple, member focused strategy. It will therefore be no surprise to members that the board of directors, which must consider formally each year the status of the Society, remains unanimous in believing that Coventry should stay an independent, mutual building society.

As I look forward to 2011 I am struck once again by the uncertainties that face us all over the coming months. The last year may well come to be regarded, on reflection, as a year of relative calm as budget reduction plans are implemented in the UK and sovereign debt issues cross international borders.

I remain confident, however, that Coventry Building Society is not only financially strong but that it has the right strategy, leadership and capability to meet the coming challenges.

I should like to thank the management team and every member of staff for their continued commitment and achievements in what has been another extremely successful year.

David Harding
Chairman

CHIEF EXECUTIVE'S REVIEW

I am delighted to confirm that 2010 was another extremely successful year for Coventry Building Society, building on the very strong performance the Society has achieved throughout the financial crisis that began in 2007.

The results show an increase in profitability, a record share of the mortgage market which was funded entirely by a significant growth in savings balances, and a further reduction in our cost to mean asset ratio – a consistent feature of our performance for more than ten years.

In addition, we completed a merger with Stroud & Swindon Building Society on 1 September and remain ahead of timescales in our plans to integrate fully the two societies for the benefit of the combined membership. I would like to welcome all former Stroud & Swindon members to Coventry and hope that those reading this report will appreciate that the strength of the Society is very much based on serving members' interests.

This strong performance has once again been achieved against a backdrop of continued economic uncertainty, and a mortgage market in which activity levels have remained low.

In the 2007 Annual Report, at the start of the credit crisis, I said that Coventry had the right model to succeed in the difficult times to come, and our performance over the last three years supports this view. I believe that Coventry's ability to prosper in such an environment is due to the simple and consistent member-focused approach that has guided it throughout its 126 year history.

The traditional building society has a number of attributes that enable it to compete successfully in both favourable and challenging markets.

An unambiguous responsibility to act in the interests of members tempers risk-taking and encourages a long-term view. It supports fairness and sustainable levels of profitability. It also underlines the need for budget restraint and efficiency, whilst striving to meet the service expectations of the membership.

Coventry is a traditional building society. Our consistent performance is due to the effective implementation of this simple model, described on occasions as 'cautious' and 'reassuringly boring'.

The increase in our share of the mortgage market means that our results may be regarded differently because of the market context. Our continued growth marks us out as somewhat different. However, it is actually the case that the Society has pursued a very consistent growth strategy over many years and what is striking to me is the extent to which our activity levels have been relatively unaffected by external events.

The strength of the Society is that our past growth was consistently achieved without taking on new or higher levels of risk, and therefore that it has been sustainable throughout the economic downturn.

The Society's lending performance, whilst remarkable in terms of our share of net lending, simply reflects a consistently active presence in the mortgage market and steady underlying organic growth. In many ways it really has been business as usual.

In 2010 Coventry advanced £3.5 billion (2009 – £2.7 billion). This equates to a market share of new lending of 2.6%, once again significantly more than our natural market share and 17.1% of all building society and mutual lender advances. In terms of net lending the Society achieved 19.0% of the total UK market, an increase on the record position we achieved last year.

The addition of Stroud & Swindon in September added a further £1.9 billion of mortgage balances but it is the year on year organic growth which highlights the core strength of Coventry Building Society and underlines our consistent success in fulfilling our traditional role of helping people to buy their homes.

In a reduced housing market, characterised by the withdrawal of lending capacity by a number of financial institutions, it is essential that our lending continues to be of the highest quality. I can confirm that this is the case and that all lending undertaken in 2010 has been in low risk sectors.

This responsible approach is demonstrated by our arrears performance which remains significantly better than for the industry as a whole. As at 31 December 2010, only 0.73% of mortgage balances originated by Coventry Building Society were 2.5% or more in arrears, below the equivalent figure of 0.80% in December 2009. At the time of the latest available data (30 September 2010), Coventry's arrears were only 39% of the average of all lenders (1.94% source: FSA).

The equivalent figure for Stroud & Swindon 2010 originated or acquired mortgages as at 31 December was 1.64%, resulting in combined mortgage balances 2.5% or more in arrears of 0.82% (2009: 0.93%). At the time of the latest available data (30 September 2010), the combined arrears were only 44% of the average of all lenders.

The same picture is revealed in terms of numbers of accounts rather than balances. Just 0.51% of Coventry originated mortgages were more than six months in arrears, substantially less than the industry average (Council of Mortgage Lenders' (CML) average of 1.23%) and less than reported in 2009. The figure for Stroud & Swindon was 1.25%, showing the combined figure of 0.60% to be substantially less than average.

The number of properties held by the combined Society reduced slightly in 2010 from the extremely low number reported at the end of 2009. The total of 107 properties in possession (of which 25 were originated or acquired by Stroud & Swindon) represents just 0.06% of more than 170,000 mortgage accounts.

The overall performance of the mortgage book is highlighted by impairment charges which are certain to remain amongst the lowest reported by any of the larger UK lenders. As a result the Society's strong underlying profitability has again been protected against significant credit losses.

The ability to maintain high quality lending, at levels which stand out in the market, obviously requires funding. For many years Coventry has had an enviable record of attracting and retaining retail funds, but the performance since the collapse of the wholesale markets in 2007 has been particularly noteworthy.

In 2010, a new record was set by the Society with an overall increase in retail savings balances of £2.2 billion – a figure which excludes a further £2.2 billion added by the merger with Stroud & Swindon. This exceptional performance was based on offering a wide range of competitive, valued products supported by an organisational capability that delivers good service, flexibility and speed of action.

The strength of the Society's performance in 2010 is particularly highlighted by the fact that total savings balances held by NS&I and other banks and building societies fell by £1.4 billion (Bank of England) in that period.

Although the wholesale markets continue to be restricted, Coventry remains one of only two building societies to have issued an unsecured long term wholesale bond since the onset of the financial crisis in 2007. In 2010 we successfully issued a 12 year instrument that confirmed Coventry's position as a strong, secure and high performing building society. As was the case for our 10 year issuance in 2009, the 2010 issue was oversubscribed.

The Society's traditional business model and consistent application of a member focused strategy is also shown by the continued progress we make in improving efficiency and cost-effectiveness. This has been a strength of Coventry for many years and supports the delivery of good value products and sustainable profits.

In 2010 we continued a trend that has been sustained for well over a decade by reducing our management expenses as a percentage of average assets to 0.37%. This is a key measure of cost-efficiency and our ability to improve our sector-leading position shows the commitment we have to maintaining this competitive advantage. The cost to income ratio also fell to just 47.0%, a figure that compares favourably with banking competitors, notwithstanding our focus on offering the best possible interest rates for the benefit of members, reflected in our narrow interest margin.

The result of this outstanding performance is a record level of profit. Reported profit before tax increased by 79% to £100.6 million, although it should be noted that this includes a net £32.6 million of accounting adjustments as a result of merging with Stroud & Swindon together with the costs associated with this project and other exceptional items of £7.3 million.

More importantly, the underlying profit[1] of £75.3 million was also more than in any previous year, exceeding the record set in 2007 of £67.0 million. After provisions for tax of £15.7 million, we were able to transfer £84.9 million to the Society's reserves, further increasing our long term capital strength.

It is worthy of note that at a time when the capital strength of financial organisations is being scrutinised ever more closely, Coventry's core tier 1 ratio of 22.0% remains the highest reported by any building society.

With the primary source of capital for building societies being retained earnings, this performance confirms the Society's ability to generate the capital necessary to support our growth as well as underlining the quality of our assets and low risk nature of our operations.

It also reaffirms our commitment to the financial security of our members. The profits we have transferred to the Society's reserves are appropriate considering the size of the organisation, the challenging economic conditions and the need to maintain the Society's strength for the future.

We do not, however, exist to maximise profits. Many building society members rely on the interest they earn from savings accounts to supplement their income and the historically low Bank of England Base Rate continues to put pressure on many members, particularly our older savers.

Since October 2008, when it began its downward path to 0.5%, the Society has improved interest rates on 95% of

[1] Underlying profit is defined as operating profit after impairments and before exceptional items

variable rate savings accounts relative to the Bank of England Base Rate. During 2010 the Society received over 650 savings & mortgages mentions in the best buy tables.

This ability to maintain sustainable profitability whilst protecting members' interests underlines not only the strength of Coventry Building Society but the relevance of the traditional mutual model to a modern financial sector.

Although recent events may have had a major impact on those of us who work in financial services, more important has been the effect they have had on society as a whole and in particular people who are in some way disadvantaged. In this environment, those of us who are in a position to do so, have an increased responsibility to put something back into the community.

Against this background, I would like to highlight the broader agenda through which staff and members contribute to the communities in which we work, and in which the Society was again very active in 2010.

Our ongoing programme of work to promote greater financial literacy is proving successful at all levels. We have increased the numbers of staff volunteers who regularly spend time working with children in schools on projects from basic reading and numeracy skills to learning about personal budgets, how to save and managing borrowing.

Our relationship with Age Concern, now entering its third year, has benefited both partners, as staff and members have not only raised significant funds for the charity but have also gained greater understanding of the challenges faced by older people.

Behind all the activities we support lies the enthusiasm and energy of our staff. All told, we supported over 150 charities in 2010, raising over £100,000, together with a further £50,000 donated by the Society to local community groups through the Coventry Building Society Charitable Foundation. These activities were in addition to the very successful partnership we have with The Royal British Legion, for which we raised a further £1.7 million in 2010, bringing the total donated to the Poppy Appeal since 2008 to £4.6 million.

It is clear that 2010 has been an exceptional year for Coventry Building Society and one that follows sustained strong performances over a number of years.

In many ways this should not be a surprise. The Society has a simple business model and executes it well. The traditional mutual building society model can be as relevant today as it was in the very different environment that led to its creation in the first place.

Looking forward, I believe that the differences in ownership, objective, scope and risk that exist between banks and building societies should be reflected in their regulation.

It is right that events over the last few years have raised concerns about the effectiveness of existing financial regulations, but there is also a danger of adding controls that restrict the ability of smaller players in general, and the mutual sector in particular to compete and grow.

Throughout 2010, proposals relating to capital requirements and, more parochially, the development of the mortgage market have been raised and discussed. With the need to maintain economic growth beginning to shape the debate, it is to be hoped that overbearing mortgage regulation will be avoided.

However, it is largely economic necessities that seem to be driving this debate rather than the need to create an appropriate and sustainable regulatory framework which supports the differences that exist between different financial organisations. I believe Coventry's performance shows that the regulatory framework for building societies may not need fundamental change.

It is still impossible to predict what will happen to the UK economy in 2011. Not only are there serious issues to face at home as attempts to reduce the budget deficit are implemented, but the international situation remains uncertain.

The future path of interest rates is hard to predict. Most likely they will remain low by historic standards, despite inflationary pressure, and restrictions in the financial markets will continue with attendant downward pressure on margins. The housing market is likely to remain depressed in terms of volumes and prices.

This is not a new situation. Rather, it is one which we have experienced over the past four years, and in which the Society has achieved a record-breaking performance. Coventry is well funded, we continue to earn an adequate return on our assets, the integration of Stroud & Swindon is ahead of schedule, and our performance on arrears and impairments is very strong.

I remain confident that Coventry has the right business model to maintain its outstanding record of achievement and remains well placed to report further progress in 2011 and beyond.

David Stewart
Chief Executive

THE DIRECTORS AND SECRETARY

BRIDGET BLOW, DEPUTY CHAIRMAN AND SENIOR INDEPENDENT DIRECTOR (61)

Bridget Blow joined the Board as a non-executive director in 2007. Between 2000 and 2005 Bridget was a non-executive director of the Bank of England.

Bridget is an experienced company director with a strong information technology background, having been Chief Executive of ITNET plc. Bridget is a past president of the Birmingham Chamber of Commerce and Industry and a non-executive director of Birmingham Hippodrome.

She is chairman of Trustmarque Group and Harvard International plc and also chairs the Development Board of the Local Enterprise Partnership for Birmingham and Solihull with East Staffordshire, Lichfield and Tamworth.

Bridget became the Society's Deputy Chairman in 2009. She is also Senior Independent Director, Chairman of the Society's Remuneration Committee and a member of the Board Audit Committee.

ROGER BURNELL (60)

Roger Burnell joined the Board as a non-executive director in 2008 and is a Chartered Accountant with over 25 years' senior executive experience. He worked as Finance Director and Managing Director of several businesses within the Thomson Travel Group before becoming Group Chief Operating Officer in 1998.

Since retiring from his executive roles Roger has continued to work at Board level through a number of non-executive directorships, including previously as Chairman of International Life Leisure Group, Chairman of The First Resort and Chairman of HomeForm Group.

Roger is currently Senior Independent Director of Thomas Cook Group plc and a member of the Society's Board Audit Committee and the Remuneration Committee.

COLIN FRANKLIN (55)

Colin has been with the Society for over 30 years during which time he has held line management responsibility for a number of areas including the branch network, operations and sales.

Colin joined the Society's executive team in 2005 and in 2009 he was appointed to the board as Director of Sales and Marketing with responsibility for sales operations, distribution, product development and marketing. He is also Managing Director of Godiva Mortgages, the Society's intermediary lending subsidiary.

IAN GEDEN (57)

Ian Geden joined the Board as a non-executive director in 2008. He has over 30 years' financial services experience in the mutual sector, working for most of his career with NFU Mutual where he was Chief Executive before retiring at the end of 2008.

Ian is a non-executive director of The Police Mutual and a member of the Society's Board Audit Committee and the Remuneration Committee.

DAVID HARDING, CHAIRMAN (63)

David Harding joined the Board as a non-executive director in 1996, becoming Deputy Chairman in 1999 and Chairman in 2005.

David holds a degree in Economics from the University of Nottingham and a Masters degree from Nottingham University Business School. He is a Fellow of the Chartered Institute of Management Accountants and has experienced a wide career in finance. His executive career included Board positions with several major listed companies, including Railtrack plc, Rugby Group Plc and T&N plc. He was also Chairman of PD Ports Plc until 2006.

David is Senior Independent Director of Enterprise Inns plc and a non-executive director of the Royal Mint. He is a local magistrate and Deputy Chairman of the Bench.

JOHN LOWE (38)

John Lowe was appointed to the role of Finance Director in 2010. He joined the Society in 2007, initially to manage its Corporate Planning and Product Development functions, before assuming the role of Deputy Finance Director in 2009.

A graduate of Oxford University and a Chartered Accountant, having qualified with Deloitte, John has over 14 years' experience of financial services gained across a broad range of businesses.

THE DIRECTORS AND SECRETARY

(continued)

IAN PICKERING (55)

Ian Pickering was appointed to the Board as a non-executive director in 2005. He is a qualified Chartered Accountant.

Ian holds a degree in mathematics from the University of Cambridge. An experienced company director, having worked for much of the last 20 years in the engineering industry, Ian is a former Chief Executive of Manganese Bronze Holdings plc. Prior to this he was a director of the Dennis Group plc.

Ian is a non-executive director of Bedford Hospital NHS Trust, whose Audit Committee he chairs, and a member of the Council of Cranfield University. He is a member of the Auditing Practices Board of the Financial Reporting Council.

Ian is Chairman of the Society's Board Audit Committee and a member of the Remuneration Committee and Ratings System Committee.

NAILESH RAMBHAI, SECRETARY AND SOLICITOR (36)

Nailesh Rambhai is a Solicitor. He joined the Society in 2006, having qualified at Linklaters and then working for another major international law firm in the City of London.

Nailesh is the principal legal advisor for the Society. He is a member of the legal panel of the Council of Mortgage Lenders and, in his spare time, is a non-executive director of the Belgrade Theatre in Coventry where he is Chairman of the theatre's community and education company.

FIONA SMITH (52)

Fiona Smith joined the Board as a non-executive director in 2002. Fiona is a Solicitor and has been General Counsel and Company Secretary of Severn Trent plc since 2006. She was previously General Counsel and Company Secretary at National Grid plc, where she worked for 15 years, and then at Transport for London.

Fiona is a trustee of the Coventry Building Society Staff Superannuation Fund and a member of the Society's Remuneration Committee.

GLYN SMITH (58)

Glyn Smith is a graduate of the University of Cambridge and joined the Board in 2010. He is a Chartered Accountant with over 30 years' experience in the financial services sector, most notably as a senior executive at Barclays Bank PLC and as Finance Director of Portman Building Society.

He is a current member of the Institute of Chartered Accountants in England and Wales examinations team and also a non-executive director and chairman of the Audit Committee of the Covent Garden Market Authority and a Primary Care Trust. Other recent non-executive directorships include Domestic & General Group PLC and Stroud & Swindon Building Society, where latterly he also acted as Finance Director until the merger with the Coventry.

Glyn is a member of the Society's Board Audit Committee and Remuneration Committee.

DAVID STEWART, CHIEF EXECUTIVE (45)

David Stewart is a graduate of Warwick University and a Chartered Accountant, having qualified with KPMG. He joined the Board in 2002 as Finance Director, assumed Board responsibility for the sales and marketing functions in 2004 and was appointed Chief Executive in 2006.

Prior to joining the Society, David gained financial services experience at DBS Management plc where he was Group Finance Director and then Group Chief Executive.

David is a member of the Council of the Building Societies Association and of the Executive Committee of the Council of Mortgage Lenders. He is also a member of the Financial Ombudsman Service Steering Group.

PHIL VAUGHAN (46)

Phil Vaughan joined the Society in 2006 as Chief Operating Officer and was appointed to the Board in 2009. He holds responsibility for the Society's information systems infrastructure and its customer service centre including the telephone call centre and mortgage and savings processing functions.

Previously Phil was Finance Director for Group Operations and Technology at Barclays Bank plc. Phil joined the Society from American Express where he was Vice-President for Business Management and Global Re-engineering.

DIRECTORS' REPORT

BUSINESS OBJECTIVES AND ACTIVITIES

The Society's principal objective is the provision of a range of personal financial services including mortgage finance for house purchase and improvements, savings, investment products and insurance.

The directors consider that all activities carried out during the year were within the powers set out in the Memorandum of the Society.

BUSINESS REVIEW

The Society recorded another outstanding performance in 2010, following several years of sustained success achieved during a period of unprecedented financial and economic crisis.

The year was marked by a record performance in acquiring and retaining retail savings balances, enabling the Society to fully fund further growth in responsible lending. The ability of the Society to do this shows the strength of the traditional mutual model. By maintaining a consistent focus on serving the interests of members, the Society provides savings and mortgage products that offer long-term value, whilst retaining award-winning service and sector-leading cost efficiency.

Importantly, in a period of ongoing uncertainty, Coventry Building Society remains strongly profitable, adding further capital to the Society's reserves and maintaining 'A' ratings with Fitch and Moody's, the credit rating agencies that monitor most of the building society sector.

This performance provides reassurance for members and industry commentators alike that Coventry Building Society continues to offer security, choice and value in an uncertain economy.

The Society's business performance is reviewed by the Chairman and Chief Executive on pages 2 to 6.

External environment

The UK economy emerged from recession at the start of 2010. However, the recovery remained fragile throughout the year as concerns focused on the potential impact of budget deficit reduction measures introduced by the new coalition government.

Although many of these measures will not come into effect until 2011, consumer confidence was impacted during 2010 by the realisation of the extent of the deficit, as well as the steps being implemented to address it.

The external context in 2010 and beyond is defined by the challenge to reduce the level of public borrowing whilst protecting the recovery. During 2010 the Monetary Policy Committee maintained the Bank of England Base Rate at its historically low level of 0.5% and consideration was given to further quantitative easing.

However, towards the end of the year, concerns regarding the level of inflation, under pressure as a result of rising commodity prices and the increase in VAT, have caused some to believe that a rise in Base Rate may happen earlier than previously anticipated. The outlook for the Base Rate remains unclear.

Unemployment in the early part of 2010 reduced as the UK emerged from recession led by a stronger manufacturing sector. However, figures began to creep up towards the end of the year and there remains some concern that public sector cuts could accelerate this in 2011.

The housing market remained subdued throughout 2010 with activity levels approximately half of what was considered commonplace prior to the financial crisis. The low levels of consumer confidence were partly responsible for this, but also relevant was the restriction in mortgage lending capacity as many financial organisations continued to rebuild balance sheets.

House prices, which had recovered during the second half of 2009, continued to rise during the early part of 2010 boosted by a lack of supply. However, by the end of the year this trend had reversed and house prices ended 2010 at a similar level to where they started.

Impact on Coventry Building Society

The Society has once again prospered in what to all financial organisations has been an extremely difficult environment, adding an exceptional year's results to previous strong performances.

The reason for the continued success of Coventry Building Society is the consistent execution of a simple traditional business model, based on acquiring and retaining savings balances to support responsible lending.

The Society's tight control of costs, its emphasis on operational efficiency and its ability to maintain an appropriate margin has meant that it has avoided the requirement to take on higher levels of risk. As a result the Society has retained 'A' ratings from both Moody's and Fitch credit rating agencies. It is noteworthy that the business as usual performance has not been impacted by the merger with and integration of the Stroud & Swindon Building Society.

DIRECTORS' REPORT
(continued)

The Society has remained strongly profitable throughout the economic downturn and is very well placed to continue to grow and add to its capital strength for the benefit of current and future members.

FUTURE DEVELOPMENTS

As 2011 dawns the UK economy continues to be marked by uncertainty. Concerns about the rate of inflation have led to calls for an early rise in the Bank of England Base Rate. However, these concerns are countered by a need to support growth within a faltering economy, particularly as budget deficit reduction measures are implemented.

Consumer confidence is likely to remain brittle, with fears of public sector cuts, unemployment, rising interest rates and inflation restricting supply and demand in the housing market. The overall availability of mortgage finance will remain constrained as wholesale markets continue to operate at much reduced levels, and retail savings will be correspondingly competitive. The pressure will be increased by the withdrawal in 2011 and 2012 of the special liquidity support mechanisms put in place by the Bank of England at the onset of the financial crisis.

Whilst this is a developing situation, the existence of considerable uncertainties and restrictions are not new. It is the same environment in which the Society has been succeeding for the last four years.

It has been a theme of this Annual Report and Accounts, and of the ones that have preceded it, that the Society has the right business model for the challenges it faces. The Board believes that Coventry is well placed to continue the track record of success which it has established over many years, and has demonstrated without equal during the economic downturn.

GROUP ACCOUNTS

The Accounts show the consolidated Group results of the Society and its subsidiaries, and the Society as a single entity.

PROFIT AND CAPITAL

The Group's profit after tax amounted to £84.9 million (2009 – £43.5 million), which was added to reserves.

The Group holds capital to protect its depositors, to cover inherent risks, to support the development of the business and to provide a cushion for unexpected losses. In assessing the adequacy of its capital, the Group considers its risk appetite and the material risks to which it is exposed. Capital adequacy and capital resources are monitored on the basis of the framework developed by the Basel Committee on Banking Supervision and subsequently implemented in the UK by the UK regulator, the Financial Services Authority (FSA).

Prior to 1 January 2008, the Group followed the requirements of the Capital Accord (Basel I). Since 1 January 2008 the Group has complied with the EU Capital Requirements Directive (Basel II). From this date the FSA granted the Group permission to use the Basel II Internal Ratings Based (IRB) approach to retail credit risk and capital management. This permission reflects the Group's detailed analysis of its customer base and control of its credit risk profile. In 2010, Coventry Building Society merged with the Stroud & Swindon Building Society, which used the standardised approach to retail credit risk management. The Group intends to adopt the IRB approach for these mortgages in due course. It allows the Group to set capital levels using internally developed models that reflect the credit quality of the Group's mortgage book rather than through standardised percentages set by the FSA.

The table opposite summarises the composition of regulatory capital for the Group as at 31 December 2009 and 31 December 2010. At 31 December 2010, and throughout the year, the Group complied with the capital requirements that were in force. Further information on how the Group manages capital can be found on page 20. The Group calculates its capital requirement under Basel II using the IRB approach for prime residential and buy-to-let mortgage exposures (excluding those transferred from the Stroud & Swindon merger), and the standardised approach in calculating the capital requirements for other risk areas.

Capital structure

	Notes	2010 £m	2009 £m
Tier 1			
General reserve		**704.5**	616.0
Pension fund surplus adjustment		**(7.2)**	(6.9)
Intangible assets		**(12.2)**	(9.9)
Deductions from tier 1 capital	1	**(15.3)**	(19.2)
Core tier 1 capital		**669.8**	580.0
Permanent interest bearing shares	2	**160.0**	160.0
Total tier 1 capital		**829.8**	740.0
Tier 2			
Collective provisions for impairment	3	**0.8**	0.3
Subordinated debt	2	**67.0**	70.0
Deductions from tier 2 capital	1	**(15.3)**	(19.2)
Total tier 2 capital		**52.5**	51.1
Total capital		**882.3**	791.1
Risk-weighted assets		**3,043.9**	2,078.5
Core tier 1 ratio (%)		**22.0**	27.9

1. Under Basel II a deduction is made for the excess of expected losses on loans and advances to customers, calculated on an IRB basis, over accounting provisions, and are allocated 50% to tier 1 and 50% to tier 2 capital.
2. Principal amount outstanding only.
3. Under Basel II collective provisions for impairment relating to loans and advances to customers, calculated on a standardised basis, are included as tier 2 capital.

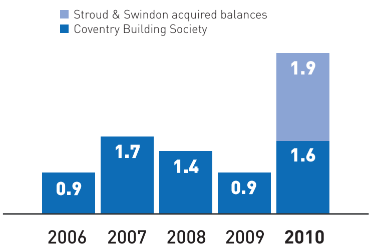
Core tier 1 ratio

The Society retains a strong capital position with a core tier 1 ratio of 22.0% (2009 – 27.9%).

DIRECTORS' REPORT
(continued)

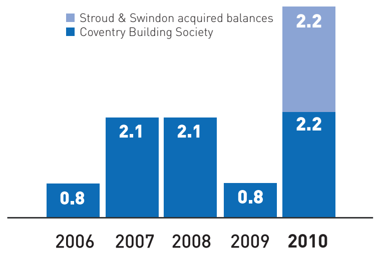
KEY PERFORMANCE INDICATORS

GROWTH IN MORTGAGE BALANCES (£bn)



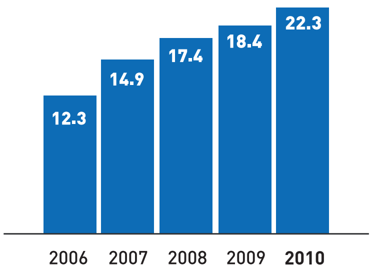
- The Society beat the previous highest share of the new mortgage market achieved in 2009, accounting for approximately 2.6% of all lending in the UK*.
- Excluding the balances acquired on merger, the Society's net lending represented 19.0% of the total growth in the UK mortgage market*.

GROWTH IN SAVINGS BALANCES (£bn)



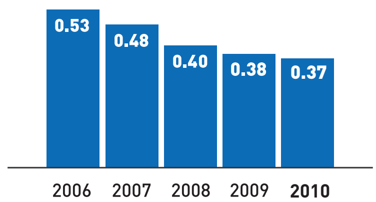
- Savings balances grew by £4.4 billion (including £2.2 billion of balances transferred in from Stroud & Swindon), exceeding comfortably the substantial growth in mortgage assets.
- Excluding Stroud & Swindon balances, the organic growth of £2.2 billion is the highest increase in savings balances ever recorded by the Society, exceeding the previous records set in 2007 and 2008.

ASSETS (£bn)



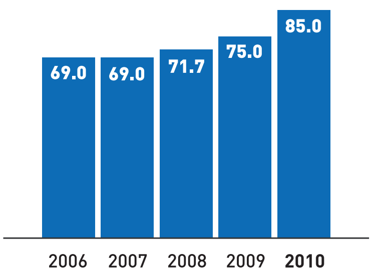
- Total assets grew by £3.9 billion or 21%.
- Of this growth, £2.6 billion represent assets acquired as a result of the merger with Stroud & Swindon.

MANAGEMENT EXPENSES RATIO (%)



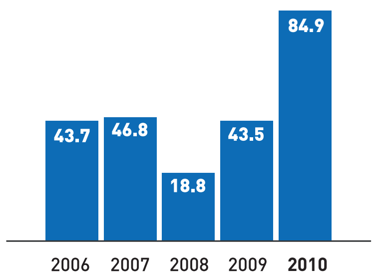
- This ratio measures management expenses as a percentage of average assets.
- At 0.37% of average assets, Coventry's ratio is the lowest reported by a UK building society.

OPERATING PROFIT BEFORE IMPAIRMENTS AND EXCEPTIONAL ITEMS (£m)



- Profitability increased by 13%, despite the pressure on margin arising from a low base rate environment.

PROFIT AFTER TAX (£m)



- Profit after tax represents the amount of capital that has been generated during the year.
- £84.9 million was transferred to the Society's reserves, further increasing its capital strength.

* Source: Council of Mortgage Lenders' Statistical Release December 2010

ASSETS

The assets of the Group increased by £3.9 billion to £22.3 billion at 31 December 2010, representing growth of 21%.

Changes in intangible assets and property, plant and equipment are detailed in notes 24 and 25 to the Accounts.

Advances during the year amounted to £3.5 billion, contributing to total loan balances of £17.6 billion.

At 31 December 2010, there were 336 mortgage accounts (Coventry – 204, former Stroud & Swindon – 132) 12 months or more in arrears (2009 – 174, excluding Stroud & Swindon). The balances on these accounts totalled £38.7 million (Coventry – £26.3 million, former Stroud & Swindon – £12.4 million) (2009 – £22.2 million, excluding Stroud & Swindon) and the value of these arrears was £8.3 million (Coventry – £1.6 million, former Stroud & Swindon – £6.7 million) (2009 – £1.1 million, excluding Stroud & Swindon). The increase in arrears is mainly due to the transfer of a small subset of mortgages (£25.4 million) from Stroud & Swindon which have high arrears balances, but have a low average LTV (19%).

CREDITOR PAYMENT POLICY

The Society's policy is to agree the terms of payment at the start of trading with the supplier and to pay in accordance with its contractual and other legal obligations.

CHARITABLE AND POLITICAL DONATIONS

The Society provided for donations of £1.8 million (2009 – £1.4 million) to charitable organisations during the year. This included a provision for £1.7 million (2009 – £1.3 million) to The Royal British Legion's Poppy Appeal and £50,000 (2009 – £50,000) to the Coventry Building Society Charitable Foundation. The Coventry Building Society Charitable Foundation, now in its 12th year of operation, continues to support many small, locally based community groups, and the £700,000 it has donated since its launch has made a difference to hundreds of charities in that time.

The amount donated to The Royal British Legion shows the strength and value of the ongoing relationship with The Legion for which the Society has developed a portfolio of products. The total support given to the Poppy Appeal since the launch of the first Poppy Bond in October 2008 is £4.6 million. The number of members holding accounts which support The Legion now totals over 51,000.

No contributions were made for political purposes. However as a result of the Political Parties, Elections and Referendums Act 2000, time allowed for employees to carry out civic duties and political activity can amount to a donation. The Society supports a very small number of employees in this way.

CORPORATE RESPONSIBILITY, ENVIRONMENTAL AND EMPLOYEE FACTORS

Staff

The directors welcome the opportunity to recognise the commitment and professionalism of all staff in enabling the Society to record such an outstanding performance in 2010.

One of the fundamental strengths of the Society is the ability to move quickly to identify opportunities and deliver a range of competitive products and the quality of service that members expect.

This is made possible by the experience and flexibility of staff throughout the Society and it is through their endeavours that the Society wins awards for both operational efficiency and quality of service.

Although 2010 has been more stable, with few of the shocks to the financial system witnessed in the previous three years, staff have continued to play a vital role in reassuring and supporting members in what remains an uncertain time. In particular the Society's exemplary record in managing issues that members raise highlights the importance that staff place on its mission to 'Put Members First'.

Not only has the Society performed exceptionally well in its core business as usual activities, but the merger with Stroud & Swindon and the work to integrate the two societies has been undertaken with great skill and commitment by all those involved. The Board recognises the efforts of the many Coventry staff who worked diligently on the project, but would also like to put on record its thanks to the former Stroud & Swindon staff for the professionalism they have demonstrated throughout. It is a reassuring footnote to the project that 'Investors in People' conducted a review of the way in which the Society handled the 'people issues' associated with the merger and concluded that it was a model of its type.

As the Society continues to grow, the directors are pleased to report that it remains a priority to recruit new members of staff who share its values. All staff continue to benefit from extensive training and development opportunities, with many building long-term careers with the Society – an aspect of the Society's commitment to members of staff that has enabled it to retain its Investors in People status.

This commitment to the Society is matched by an ongoing programme of support for staff, for which the Society continues to be recognised in the Coventry and Warwickshire Employer of Choice awards. In 2010, as in previous years, the Society showed itself amongst the best employers in the region, including both larger and smaller organisations.

DIRECTORS' REPORT
(continued)

The Society will continue to invest to provide the right environment and opportunities for members of staff to achieve their potential and both meet their expectations and those of the Society's membership.

Community
The directors are pleased to report that the Society has continued to make a very significant contribution to local communities and national charities alike, through the commitment and enthusiasm of many members of staff.

The success of an approach which has focused in recent years on areas of particular strength has been clearly evident and the Society received a number of independent accolades for the work it carries out (see Awards below).

Of particular note has been the ongoing development of the Society's financial literacy programme which includes a number of initiatives ranging from supporting numeracy and literacy in primary schools to working with specialist finance academies. The number of staff who volunteer to take part in these activities continues to increase, with over 75 people actively involved in delivering courses, mentoring students and supporting skills development in schools and colleges across Coventry and Warwickshire. That this support makes a real difference is shown by the experience of pupils at Stoke Park, a Coventry school where many have taken the opportunity to gain a specialist GCSE in personal finance as a result of the involvement of Coventry staff.

The directors recognise that educational initiatives like this are important in helping children develop skills to prepare for adult life. In addition the Society continues to work with debt-advice charities, assisting those currently experiencing financial difficulties.

The Society's work with Age UK, the charity that resulted from the merger of Age Concern and Help the Aged, is now entering its third year. The partnership continues to meet its twin objectives of raising both funds and awareness. To date, staff, supported by the generosity of members, have raised over £85,000 for the charity. As important has been the opportunity to learn about the issues facing the UK's elderly and support some of the awareness campaigns that Age UK has organised. It is an unfortunate reality that the abuse of the elderly often has a financial element and those members of staff working in customer-facing roles have benefited from an increased understanding of the issues involved.

Further details of the Society's donations to charity are noted within the section on Charitable and Political Donations on page 13.

For the last three years the environment in which the Society operates has been characterised by economic turmoil, and difficult conditions are expected to continue. In this climate, the Board believes it is right that the Society continues to support local communities and in 2010 this support was extended to more groups than in any previous year. Over 150 separate organisations were supported through fund-raising, direct volunteering or by using the skills and resources present at the Society.

Environment
The Society is committed to reducing the environmental impact of its activities, in particular the amount of energy used and waste created, through working more efficiently and the recycling or re-using of raw materials.

The Society has made good progress in a number of areas. All paper used within Coventry Building Society is recycled via a secure facility which brings both an environmental and a security benefit. In addition, over 95% of all literature produced by the Society is printed on recycled paper.

In 2010 a programme to install smart meters in all branches was initiated, following a successful pilot in 2009. The overall objective is to identify and correct any anomalies whilst supporting the change of behaviour required to drive down energy use. The indications are that this will deliver potentially significant savings, enabling greater cost efficiencies as well as environmental benefits.

In addition the Society maintains a proactive approach to energy procurement which has enabled renewable energy to be sourced cost effectively for use at head office sites. An additional office at the Binley Business Park site in Coventry is currently undergoing a refurbishment prior to full occupation later in 2011. This work includes an energy efficiency programme designed to minimise ongoing energy consumption.

Awards
The directors are pleased to report that the Society has achieved independent recognition, and in 2010 it received numerous awards across a wide range of activities.

One example was the Moneywise Customer Service Awards. The Society featured prominently in a number of categories including: Most Trusted Mortgage Provider, Most Trusted Savings Provider and Most Trusted Current Account Provider. Indeed, in 2010 the Society won, was highly commended, or was shortlisted in eleven of those awards, despite its relatively narrow mortgage range.

Coventry also featured highly in the Which? annual round-up of member satisfaction surveys for financial companies, coming fifth in the overall satisfaction table of 31 organisations, with the first three positions being taken by direct-only brands. Coventry was the highest rated building society in the satisfaction table.

The directors were particularly pleased that the work of the Society was recognised by The Royal British Legion in naming Coventry Building Society as their 'Corporate Partner of the Year'. The contribution made to the Poppy Appeal since the relationship with The Royal British Legion began in October 2008 now exceeds £4.6 million, showing the deep commitment felt by many to the work undertaken by The Legion.

Finally, although technically not an award, it is appropriate to mention the ongoing performance of the Society in its handling of member issues. Since 2009, the Financial Ombudsman Service (FOS) has published tables of the complaints that had been referred to it having failed to be resolved by the individual organisation. Having referred significantly fewer than the minimum thirty complaints required for inclusion in the FOS tables in each of the six month reporting periods, the Society is the largest mortgage lender never to have appeared in these tables.

GOING CONCERN

In preparing the financial statements the directors must satisfy themselves that it is reasonable for them to conclude it is appropriate to adopt the going concern basis.

The Society meets its day-to-day liquidity requirements, through managing both its retail and wholesale funding sources and is required to maintain sufficient liquid assets to comply with regulatory requirements, in order to continue to be authorised to carry on its business.

The Society's business activities, together with the factors likely to affect its future development, performance, position, liquidity and capital structure are set out in the Chairman's Statement, Chief Executive's Review and this Directors' Report. In addition, the Risk Management Report and note 42 to the financial statements includes further information on the Society's objectives, policies and processes for managing its exposure to liquidity, credit, market and operational risk, along with details of its financial instruments and hedging activities.

The directors believe that the Society is well placed to manage its business risks, despite the current uncertain economic outlook. After considering factors including default rates on loans, house price movements and the Society's capital and liquidity position including the use of stress testing, the directors are confident that the Society has adequate resources for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report & Accounts.

PRINCIPAL RISKS AND UNCERTANTIES

The principal risks and uncertainties faced by the Society are set out in the Risk Management Report on pages 16 to 20.

CORPORATE GOVERNANCE

The Directors' Report on Corporate Governance can be found on pages 21 to 25.

DIRECTORS' STATEMENT PURSUANT TO THE DISCLOSURE AND TRANSPARENCY RULES

The directors confirm that, to the best of each person's knowledge and belief:

- The financial statements, prepared in accordance with IFRS as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the Group and Society; and
- The management report contained in this Directors' Report and the Risk Management Report includes a fair review of the development and performance of the business and the position of the Group and Society, together with a description of the principal risks and uncertainties that they face.

AUDITORS

Following a review by the Board Audit Committee, the Board has agreed that a resolution proposing the re-appointment of Ernst & Young LLP as auditors of the Society will be submitted at the Society's 2011 AGM.

On behalf of the Board

David Harding
Chairman
28 February 2011

RISK MANAGEMENT REPORT

OVERVIEW

The Society is a mutual organisation run for the long term benefit of its members. This objective is known throughout the Society as 'Members First'. In keeping with this mutual status, the Board adopts a prudent approach to managing risk geared towards long-term value creation for the benefit of members. This low risk appetite is monitored and enforced through the Society's risk management structure described below.

GOVERNANCE AND OVERSIGHT

Risk management structure

The Society's risk management structure is based on a three lines of defence model:

- First line of defence – risk management is primarily the responsibility of all managers and staff of the Society. Management have a responsibility to understand how risk impacts their area of the business and for putting in place controls or mitigating activities.
- Second line of defence – policies and oversight are required to effectively challenge managers and staff in their performance of risk management activities and to provide risk management expertise. This is provided through risk support functions and risk committees. The Head of Risk reports to the Chief Executive and has an independent reporting line directly to the Chairman of the Board Risk Committee.
- Third line of defence – the Society's internal audit function is responsible for independently reviewing the effectiveness of the Society's risk management structure and adherence to processes. The Head of Internal Audit reports to the Chief Executive but has an independent reporting line directly to the Chairman of the Board Audit Committee. The Board Audit Committee approves the work programme of internal audit and receives reports of the results on the work performed.

The structure and responsibility of management and board committees are set out below:

BOARD COMMITTEES

Details of the board committees can be found in the Directors' Report on Corporate Governance on pages 21 to 25.

SENIOR MANAGEMENT COMMITTEES

Executive Committee

Chaired by the Chief Executive and comprised of executive directors and senior management.

Committee members work closely day-to-day and the committee oversee the operational and business performance of the Society.

Risk Management Committee

Chaired by the Chief Executive and comprised of the executive directors and senior management, with non-executive directors in attendance by rotation and the external auditors in attendance by invitation.

The committee ensures that risk is being managed efficiently across the Society, in accordance with the corporate plan. The minutes of the committee are presented to the Board Risk Committee.

The Society also has a number of sub-committees that report to the Risk Management Committee. The details of these committees are as follows:

Asset and Liability Committee (ALCO)

Chaired by the Finance Director and comprised of executive directors and senior management, including the Chief Executive. The committee oversees the management of the Society's asset and liability strategy. The minutes of the committee are presented to the Board Risk Committee.

Credit Risk and Lending Committee

Chaired by the Finance Director and comprised of the Sales and Marketing Director and senior management. The committee monitors the performance of the Society's mortgage book to ensure compliance with limits approved by the Board. This committee is also responsible for revising and amending lending policy in response to changes in the market.

Operational Risk and Compliance Committee

Chaired by the Chief Operating Officer and comprised of senior management. The committee monitors operational risk, financial crime, regulatory compliance and business continuity in the Society.

Rating System Committee

Chaired by a non-executive director (Ian Pickering) and comprised of executive directors and senior management. The committee monitors the performance of the Society's Basel II credit risk rating system.

Security and Safety Committee

Chaired by the Sales and Marketing Director and comprised of executive directors and senior management. The committee oversees security and health and safety issues as they apply to staff and customers.

PRINCIPAL RISKS AND UNCERTAINTIES

The Society seeks to understand and manage the various risks that arise from its operations. The Society classifies the principal risks it faces according to four broad categories. These are credit risk, market risk, liquidity risk, and operational risk (including compliance and financial crime). The procedures put in place to manage these risks are described below:

Credit risk

Credit risk is the risk that customers or counterparties will not meet their financial obligations to the Society as they fall due. For a building society, this risk is most likely to present itself in the potential inability of borrowers to repay their mortgage (retail credit risk). The Society's exposure to this risk is overseen by a specialist department that reports to the Credit Risk and Lending Committee.

Retail credit risk is managed through a combination of an automated decision system and statistical modelling that seeks to identify those customers who pose a greater risk of not repaying their mortgage (including the use of credit scoring), and the Society's underwriting process which considers loans that require individual underwriting and which seeks to ensure that customers only assume a debt that they can afford to repay, thereby safeguarding both themselves and the Society.

Lending policy is monitored by the Credit Risk and Lending Committee, which meets twice monthly. The committee is a sub-committee of the Risk Management Committee and is tasked with ensuring that the quality of new business and overall exposures are within the prudent limits set by the Board (principally low LTV lending on owner occupied properties), and that the performance of the book is being monitored and trends identified. In this respect, regular stress testing is undertaken that seeks to establish the extent to which losses may emerge in a variety of scenarios, including severe stresses. Should customers find themselves in financial difficulty, the Society has established procedures to ensure that it responds appropriately.

Typically, this involves working with the customer to clear arrears or making other arrangements commensurate with the customer's circumstances; should the situation deteriorate significantly, it can involve the Society taking possession of the underlying property. Regular reviews of the Society's arrears management function is undertaken to ensure that customers are being treated fairly and in line with established policies and procedures that reflect our mutual status and regulatory best practice.

Credit risk within the treasury function arises from the risk that counterparties will be unable to repay loans and other financial instruments that the Society holds as part of its liquidity portfolio (see Liquidity Risk on page 19). This risk is monitored on a weekly basis by the Treasury Credit Committee which is chaired by either the Finance Director or the Chief Executive. The Society has restrictions on the type of assets it holds, undertakes assessments of the credit-worthiness of counterparties, and works strictly within exposure limits for each counterparty, that are set by the Board. These limits require a formal review annually but in practice are reviewed by the Society's specialist credit analyst and reported to the Treasury Credit Committee as required in response to changing economic conditions. The treasury risk management team and the Treasury Credit Committee report through ALCO to the Risk Management Committee and to the Board Risk Committee.

Details of the Society's exposure to credit risk are contained in note 42 to the Accounts.

Market risk

Market risk is the risk that the value of income derived from the Society's assets and liabilities may change adversely as a result of changes in interest rates, foreign exchange rates or house prices. The Society's policy is to manage these risks prudently, which is ensured through the setting of limits by the Board. The Society ensures compliance with these limits through a combination of matching assets and liabilities with off-setting interest rate or currency characteristics, and by the use of derivative financial instruments such as interest rate swaps and caps, foreign exchange swaps and foreign exchange forward purchase contracts. Control of market risk exposure is managed by ALCO, which makes regular reports to the Risk Management Committee and the Board Risk Committee. The most significant elements of market risk for the Society are interest rate risk, foreign currency risk and house price risk, each of which are described below.

Interest rate risk

Interest rate risk arises from the different interest rate characteristics of the Society's mortgages and savings products and from other financial instruments. In particular, the issue of fixed and capped rate mortgages and fixed rate savings products exposes an organisation that principally operates within a variable rate environment (such as the Society) to the risk that interest rate fluctuations could cause either a reduction in interest income or an increase in interest expense relative to other interest flows.

Where the Society has issued fixed rate mortgages, the risk is that a general increase in interest rates would leave the Society facing higher interest expense, but without a compensating increase in interest income. In these circumstances, the Society would typically take out an interest rate swap with a counterparty bank under which the Society's fixed rate income is exchanged for one based on a variable rate which would be expected to follow the general pattern of interest rate movements and thereby reduce the Society's exposure. Similarly, in cases of issuing fixed rate savings products, the Society would typically take out an interest rate swap under which the Society receives a fixed rate of interest and pays a variable rate. With capped rate mortgages, the risk is that if the rates increase above a pre-determined level, the Society will be unable to increase its mortgage rate on these products to compensate. In these circumstances, the Society would typically purchase a rate cap that will pay a variable rate if an agreed index rate (for example, LIBOR) exceeds a certain level. In addition, the Society regularly forecasts the impact of movements in the Bank of England Base Rate on the Society's balance sheet to ensure any potential adverse impact can be anticipated. This information is reported to ALCO.

The Society does not trade or take speculative positions on derivatives.

Foreign currency risk

Foreign currency risk arises as a result of the Society's activities in raising funds and making investments in foreign currencies. This is undertaken to ensure wholesale funds are obtained cost effectively across a wide pool of potential providers, but exposes the Society to the risk of an appreciation in the value of foreign currency denominated liabilities or a deterioration in the value of the foreign currency denominated assets. The risk is managed through the use of currency swaps and foreign currency forward contracts and also, where appropriate, by the matching of foreign currency liabilities with assets denominated in the same currency.

Details of the Society's exposure to interest rate and foreign currency risk are contained in note 42 to the Accounts.

House price risk

House price risk is present in two forms. Most significantly this risk arises from the value of the property forming the security for a mortgage being insufficient to repay the loan in the event of default and subsequent repossession. The Society manages this risk through a combination of prudent loan-to-value limits at inception and ongoing monitoring to ensure that bad debt provisions are sufficient to cover the potential losses that may arise in repossession situations.

With respect to lifetime mortgages, house price risk also arises from the 'no negative equity' guarantee, whereby the borrower is guaranteed that the amount recoverable by the Society at the end of the mortgage will not exceed the value of the property.

Under these loans, the borrower receives an advance but makes no payments of interest or principal until the loan is redeemed. The interest is added to the loan and recovered by the Society when the loan is redeemed. The 'no negative equity' guarantee therefore exposes the Society to the risk that the value of the property at the time of redemption is lower than the loan plus accumulated interest. The Society manages this risk by granting loans only at relatively low loan to value ratios, subject to the age of the borrower, and through the use of statistical modelling to stress potential exposures within acceptable prudent limits. Only 2% of the Society's outstanding mortgage balances have been advanced on this type of product. The Society does not currently offer these products to new applicants.

The risks presented by house price movements are evaluated through stress testing and monitored by the Credit Risk and Lending Committee and ALCO and, through these committees, by the Risk Management Committee and the Board Risk Committee.

Liquidity risk

Liquidity risk is the risk that the Society will be unable to meet its financial obligations as they fall due or can do so only at excessive cost. The risk is managed principally by holding funds in cash accounts and other easily realisable liquid assets. The amount and composition of liquid assets held is subject to guidance from the FSA and to regular stress testing. The stress testing programme, and other policies addressing liquidity risk, have been updated in accordance with an Internal Liquidity Adequacy Assessment ('ILAA') undertaken by the Society. The ILAA reflects the new liquidity regime introduced by the FSA in 2010, and has resulted in a greater proportion of the liquidity book being represented by Government securities or invested with the Bank of England via a current account. Whilst these assets realise a relatively low yield, this reflects the very low credit risk represented by a AAA rated sovereign entity, such as the UK Government, and ensures the assets can readily be converted into cash to meet liabilities, as they fall due. Day-to-day management of the Society's liquidity position is the responsibility of the treasury and balance sheet management functions and is monitored by ALCO and, through this committee, by the Risk Management Committee and the Board Risk Committee.

Details of the Society's exposure to liquidity risk are contained in note 42 to the Accounts.

Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems or from external events, including legal risks. These risks are managed as an integral part of the operation of each of the Society's business units. Management has a responsibility to understand how operational risk impacts the area of the business for which they are responsible, and for putting in place controls or mitigating activities. The operational risk department ensures co-ordination of the Society's risk assessment and resulting control activities, reporting to the Operational Risk and Compliance Committee and, through this committee, to the Risk Management Committee and the Board Risk Committee.

New operational risks arose in 2010 following the merger with Stroud & Swindon from the integration work required to migrate the information stored on Stroud and Swindon systems onto the framework used by the Society. There are risks both in undertaking this exercise, for example, data errors on transfer, and also a risk that as a result of the scale of work required, resource will be distracted from managing the ongoing operation of the Society in a challenging external environment. The Society has a strong track record in undertaking major change programmes and has considerable project expertise. In addition an experienced Managing Director has been appointed to manage the operations at Stroud & Swindon until the migration is complete. A dedicated steering group has been set up to manage this project with responsibility of also highlighting the impact on business as usual activity. This steering group is chaired by the Chief Operating Officer and members include the Chief Executive, Sales and Marketing Director and the Managing Director of Stroud & Swindon. Updates from this steering group are provided monthly to the Risk Management Committee and Board.

Financial crime is also recognised by the Society as an evolving and substantial threat to the security and the safe operation of all financial institutions. The Society continues to invest in monitoring and control systems to prevent increasingly sophisticated criminal attacks, and has an excellent track record in this area.

The Society has a duty of care to its staff, members and visitors whilst present on Society premises. The Society has in place comprehensive health and safety polices and a compliance regime which includes internal and external inspection, the maintenance and testing of equipment as well as appropriate training programmes; these are reviewed regularly. This work is overseen by the Security and Safety Committee which reports to the Risk Management Committee and Board each month.

In addition the Society has developed Business Continuity Plans to manage situations in which buildings, systems or significant staff are unavailable, for example, in the event of a flu pandemic or the loss of utilities. The Society's Business Continuity Plan is overseen by the Operational Risk and Compliance Committee and, through this, by the Risk Management Committee and the Board Risk Committee.

Business risk

Business risk encompasses those aspects of the external environment that have the potential to affect the Society's business model. This is particularly relevant in the context of the multiple major regulatory initiatives currently being proposed or implemented, including ones which cover liquidity, capital, governance, the special resolution regime, reform of the Financial Services Compensation Scheme and conduct of business, including a review of the mortgage market and retail distribution. Some of these have the potential to affect significantly the Society's business model. The regulatory agenda is considered to be of strategic importance and as such it is actively considered by all directors and senior management with the support of the compliance function.

Further details of risk exposures are available in our Pillar 3 Disclosures on the Society's website: http://www.thecoventry.co.uk/pillar3

CAPITAL

The Board determines the level of capital required to support the Society's business objectives through its Internal Capital Adequacy Assessment Process (ICAAP).

The ICAAP evaluates the Group's risk management framework, together with financial projections contained in the corporate plan, in order to assess the significant risks to which it is exposed and the capital resources it needs to support its risk exposure over a five year horizon.

The ICAAP incorporates expected future capital requirements from changes in business volumes, mix of assets and activities within the context of current and anticipated future risks, and market stress scenarios. The ICAAP is used by the FSA in its Supervisory Review and Evaluation Process (SREP) through which it sets the Group's capital requirements as Individual Capital Guidance (ICG). The amount, composition and adequacy of the Group's capital requirement is determined by assessing the Basel II minimum capital requirement, the impact of stress and scenario tests and the Group's ICG.

The ICAAP is reviewed by ALCO before submission to the Board for formal approval as part of the corporate planning process. The Society's internal audit function reviews the accuracy and consistency of the financial information included within the ICAAP document.

Capital levels for the Group are reported to and monitored by the Board on a monthly basis. The Group continues to be strongly capitalised and manages its capital substantially above the ICG and Basel II transitional floors at all times. The Group's core tier 1 capital ratio is the highest reported of any Building Society.

Further details of the Group's capital can be found on page 11.

DIRECTORS' REPORT ON CORPORATE GOVERNANCE

The Board is accountable to the Society's members for the operation of the Society and places the highest priority on good corporate governance.

In June 2010, the Financial Reporting Council (FRC) issued the new UK Corporate Governance Code (the Code). This included many of the recommendations in the Walker Review of Governance in Banks and Other Financial Institutions, which was published in November 2009. The Code is applicable for financial years beginning on or after 29 June 2010. The Board has considered the requirements of the new Code and the recommendations in the Walker Review and will continue to seek compliance in a manner which is proportionate to the size, scale and relative simplicity of the Society's operations and its business model.

All listed companies are required to explain their governance policies in light of the principles contained in the Code and to confirm that they comply with the Code's provisions or provide an explanation where they do not comply. Whilst the Society does not have to comply with the Code, as it is not a listed company, the FSA requires building societies to have regard to the principles of the Code. The Board's objective is to adhere to the principles and provisions of the Code that are relevant to the Society and explain to members where this is not the case. The Board believes that the Society complies fully with the Code, unless stated otherwise.

Insofar as it is applicable, the Society is also compliant with the 8th EU Company Law Directive.

THE BOARD OF DIRECTORS

The Board currently comprises a Chairman, six other independent non-executive directors and four executive directors.

The following persons served as directors of the Society during the year: Bridget Blow, Roger Burnell, Colin Franklin, Ian Geden, Rob Green (resigned 14 October 2010), David Harding, John Lowe (appointed 14 October 2010), Ian Pickering, Fiona Smith, Glyn Smith (appointed 22 September 2010), David Stewart, and Phil Vaughan.

No director has any interest in the shares or debentures of any associated body of the Society.

The role of the Board is to determine long term strategy, approve major operational projects, maintain systems of internal control, consider significant financial matters and the appointment of executive directors and senior management. Risk management is viewed as an integral part of the Board's decision making process and also of the Society's corporate planning process which is overseen by the Board. In addition, in 2010 the Board established a dedicated Board Risk Committee to consider risk strategy in the Society.

The Board has a formal schedule of matters that are reserved to it, and it has also delegated authority in other matters to a number of Board committees, as described below. The Board has set clear terms of reference for these committees and has clearly documented delegated authority to the executive directors and senior management.

The Board applies principles of good governance by adopting the following procedures:

- the Board's role is to set the Society's strategy, review performance and ensure that the necessary resources are in place for it to meet its objectives. It is also responsible for ensuring that financial controls and systems of risk management are robust. In particular the Board's role is to provide overall direction to the Society and to safeguard the interests of its members;
- the Board retains specific powers in relation to the approval of the Society's strategic aims and policies and other matters which must be approved by it under applicable legislation and the Society's Rules. The Board is also responsible for the recruitment and terms of employment of executive directors and senior management within the Society. Other powers are devolved to the executive directors and senior management;
- the size and composition of the Board and the senior management team is kept under review to ensure that there is adequate succession planning for executive and non-executive directors and that the Board has the appropriate skills and experience for the direction of the Society's activities;
- directors receive accurate, timely and clear information and it is the responsibility of the Chairman to ensure that this information is considered by the Board;
- the Chairman also ensures that, on appointment, non-executive directors receive a comprehensive tailored induction programme that covers the Society's business and regulatory environment. Non-executive directors update their skills, knowledge and familiarity with the Society through presentations by senior managers and by attending relevant bespoke internal and external courses; and

DIRECTORS' REPORT ON CORPORATE GOVERNANCE
(continued)

- all directors have access to the advice and services of the Secretary and Solicitor who is responsible for ensuring compliance with Board procedures and advising the Board, through the Chairman, on governance related matters.

The Society maintains liability insurance cover for directors and officers as permitted by the Building Societies Act 1986.

Set out in the table below are details of the directors during 2010 and their attendance record at Board meetings and relevant Board committee meetings during the year.

BOARD COMMITTEES AND MEETINGS 2010

Name	Title	Number of Board Meetings – 12	Number of Board Audit Committee Meetings – 5	Number of Board Risk Committee Meetings – 6	Number of Nominations and Governance Committee Meetings – 2	Number of Remuneration Committee Meetings – 4
David Harding	Chairman	12		6	2	3
Bridget Blow	Deputy Chairman	12	5	6	2	4
Roger Burnell	Non-executive director	11	5	5		4
Colin Franklin	Sales and Marketing Director	12				
Ian Geden	Non-executive director	11	5	6		4
John Lowe	Finance Director (appointed 14 October 2010)	3[1]				
Ian Pickering	Non-executive director	12	5	6		4
Fiona Smith	Non-executive director	12		6		4
Glyn Smith	Non-executive director (appointed 22 September 2010)	4[2]	–[3]	3[4]		2[5]
David Stewart	Chief Executive	11			2	
Phil Vaughan	Chief Operating Officer	12				

[1] Maximum number of Board Meetings is 3.
[2] Maximum number of Board Meetings is 4.
[3] Glyn Smith was appointed a member of the Board Audit Committee on 1 January 2011.
[4] Maximum number of Board Risk Committee Meetings is 3.
[5] Maximum number of Remuneration Committee Meetings is 2.

NON-EXECUTIVE DIRECTORS

In the opinion of the Board, Bridget Blow, Roger Burnell, Ian Geden, Ian Pickering, Fiona Smith and Glyn Smith are independent in character and judgement.

Bridget Blow fulfils the role of Senior Independent Director insofar as this role is relevant to the nature and scale of the Society's operations.

CHAIRMAN AND CHIEF EXECUTIVE

The roles of the Chairman and Chief Executive are held by different people and are distinct in their purpose.

The Chairman is responsible for leading the Board and ensuring that it acts effectively. The Chief Executive has overall responsibility for managing the Society and for implementing the strategies and policies agreed by the Board.

David Harding was re-elected Chairman on 25 May 2010.

PERFORMANCE EVALUATION

The performance of the non-executive directors and each of the Board committees is appraised by the Nominations and Governance Committee, and the Chairman's performance is reviewed by the rest of the Board, in the absence of the Chairman.

The Board also periodically reviews its own performance, and in 2010 the FSA conducted a pilot board effectiveness review of the Board. An externally facilitated evaluation of the Board is under active consideration and is expected to be held in 2011.

In addition, all directors have open and direct access to the Chairman and to the Senior Independent Director in order to raise any issues of concern.

APPOINTMENTS TO THE BOARD

The appointment of new directors is considered by the Nominations and Governance Committee which makes recommendations to the Board. In accordance with Rule 25 of the Society's Rules, all directors are subject to election by members at the AGM following their appointment or, where applicable, at the next following AGM. In addition, all directors must receive approval from the FSA as an approved person in order to fulfil their controlled function as a director.

Under Rule 26, directors have to submit themselves for re-election at least once every three years.

Glyn Smith and John Lowe were appointed to the Board on 22 September 2010 and 14 October 2010 respectively. They retire under Rule 25 and, being eligible, offer themselves for election in accordance with that Rule.

The directors retiring by rotation are Bridget Blow, Ian Pickering, Fiona Smith and David Harding.

David Harding joined the Board in 1996, becoming Chairman in 2005. Historically governance codes have recommended that non-executive directors should only serve a term of more than nine years in exceptional circumstances, although comments in the Walker Review of Governance in Banks and Other Financial Institutions have recognised the importance of retaining experience in the sector.

In 2008, 2009 and again in 2010 the Board, excluding, for this purpose, the Chairman, conducted a thorough review to assess David Harding's performance as Chairman. They confirmed that he has led the Board effectively through a period of transition and difficult market conditions during which time the Society has performed extremely well.

The Board has therefore decided unanimously to recommend David Harding for re-election by the members at this year's AGM.

Therefore, Bridget Blow, Ian Pickering, Fiona Smith and David Harding, being eligible, offer themselves for re-election in accordance with Rule 26.

As noted above, although it is not obliged to do so, the Society complies with and has regard to the Code insofar as it is appropriate. In this connection the Board has considered the provisions of the Code and does not feel that it would be appropriate, at present, to submit the entire Board for annual re-election by the members.

BOARD COMMITTEES

The Board has established a number of committees that have their own terms of reference. Details of the principal Board committees, including their membership, are set out below.

In addition to attendance at Board and committee meetings, meetings with senior management and branch visits, non-executive directors are required to complete a detailed induction programme (on appointment) and to participate in a structured programme of director training in order to keep abreast with new regulatory requirements and some of the more technical aspects of the role. Non-executive directors are also encouraged to engage with the Society's members through the AGM process, the Society's Members' Council Meetings and the Society's programme of member roadshows.

BOARD RISK COMMITTEE

The Board Risk Committee was formed in June 2010. The Board Risk Committee is a board committee, chaired by the Society's Chairman, and is made up of the Society's non-executive directors and the Head of Risk. The committee meets on a monthly basis and consists of:

David Harding, Chairman of the Society and Chairman of the committee
Bridget Blow, non-executive director
Roger Burnell, non-executive director
Ian Geden, non-executive director
Ian Pickering, non-executive director
Fiona Smith, non-executive director
Glyn Smith, non-executive director
Sheryl Lawrence, Head of Risk

The Society's executive directors and the Secretary and Solicitor attend Board Risk Committee meetings.

The committee has the responsibility for overseeing risk strategy, risk policies and risk appetite and making recommendations to the Board. The main function of the committee is to assist the Board in fulfilling its responsibilities with specific regard to risk by:

- reviewing and challenging material risks in relation to the Board's risk appetite and the Society's liquidity and capital adequacy;

DIRECTORS' REPORT ON CORPORATE GOVERNANCE
(continued)

- reviewing and challenging the Society's rating systems; and
- reviewing and challenging material breaches and control weaknesses and responses.

In 2010 the Committee met six times and considered a number of areas including:

- a review of the Society's risk management culture and framework;
- detailed and regular reviews of the Society's top down risk register and discussion of emerging risks in the Society's operating and the wider economic environment;
- risk governance matters;
- mortgage fraud;
- interest only mortgages;
- settlement systems and risks; and
- implementation of regulatory developments, including the new liquidity regime (ILAA) and the Building Societies Sourcebook (BSOCS).

BOARD AUDIT COMMITTEE

The committee consists of:

Ian Pickering, Chairman of the committee
Bridget Blow, non-executive director
Roger Burnell, non-executive director
Ian Geden, non-executive director
Glyn Smith, non-executive director (appointed to the committee on 1 January 2011)

The Society's external auditors, the Chief Executive, Finance Director, Secretary and Solicitor, Head of Risk, Head of Internal Audit and also certain senior managers (if required) attend Audit Committee meetings. In addition, the external auditors meet members of the committee in a private session.

The Chairman of the committee, Ian Pickering, has recent and relevant financial experience and is a Chartered Accountant.

The responsibilities of the committee comply with the provisions of the Smith Guidance on Audit Committees. The main function of the committee is to assist the Board in fulfilling its oversight responsibilities with specific regard to:

- monitoring the integrity of the half-year and annual financial statements and any formal announcements relating to financial performance, focusing particularly on the financial reporting judgements contained in them;
- reviewing the adequacy of systems of internal control and risk management processes;
- assessing the effectiveness of internal audit;
- considering compliance with relevant laws and regulations, including the Financial Services and Markets Act 2000;
- reviewing the performance of external auditors and overseeing the appointment by the Society of the external auditors for non audit work; and
- making recommendations to the Board on the appointment, re-appointment or removal of external auditors and the amount of their remuneration.

During 2010 the committee met five times and, amongst other things, considered reports on:

- the Society's risk management framework and systems of internal control;
- the integrity of financial statements;
- operational risk related matters;
- compliance with laws and regulations, including adherence to Money Laundering Regulations; and
- the activities and performance of the internal and external auditors.

Reports were provided by the finance, internal audit, operational risk and compliance functions and the external auditors.

The committee ran a tender in relation to the Society's external audit work in 2007 and plan to run a similar exercise in due course.

The committee undertakes an annual evaluation to assess the independence and objectivity of the external auditors and the effectiveness of the audit process, taking into consideration relevant professional and regulatory requirements. Noting the significant non audit fees incurred by the external auditors in 2010, as a result of the advice and support given by Ernst & Young on the Society's merger with Stroud & Swindon, the committee undertook a thorough evaluation of the continued independence of the firm. The review concluded that the firm remained independent and that it therefore remained appropriate for Ernst & Young to continue to act as the Society's auditors.

The outcome of this evaluation feeds into the committee's recommendation to the Board on the re-appointment of the external auditors. The final decision on the recommendation to the members is reserved for the Board.

The committee also completed a self appraisal exercise in 2010 and considers that it has met its responsibilities and performed its duties with appropriate levels of care and expertise.

NOMINATIONS AND GOVERNANCE COMMITTEE

The committee consists of:

David Harding, Chairman of the Society and Chairman of the committee
Bridget Blow, Deputy Chairman
David Stewart, Chief Executive

The committee is responsible for making recommendations to the Board on matters relating to the composition of the Board (including Board succession planning, the appointment of new directors, the re-appointment of retiring directors, the appointment of non-executive directors to committees of the Board and executive director and senior management succession planning).

The committee is responsible for appraising the performance of the Board and its committees as well as of individual directors. The performance of the Chairman is reviewed by the Board excluding, for this purpose, the Chairman.

In 2010 the Committee met two times and considered, amongst other things, the appointment of a new non-executive director and the appointment of a new Finance Director of the Society.

In addition, through the AGM process the Society issues a standing invitation to members to apply for the position of non-executive director. Through this process a large number of candidates were interviewed by members of the Committee in 2010, and previous appointments to the Board through this process include the appointments in 2008 of two new non-executive directors. External consultants and recruitment specialists are also employed by the Society in considering director and senior management succession planning.

REMUNERATION COMMITTEE

The committee consists of the non-executive directors of the Society and is chaired by Bridget Blow, Deputy Chairman and Senior Independent Director.

The committee is responsible for considering and approving the remuneration of executive directors and senior management and also sets targets for the Society's performance related bonus scheme in which all staff members participate. In 2010 the committee met four times. Further details of the committee, the remuneration policy and directors' service contracts can be found in the Directors' Remuneration Report on pages 26 to 28.

The UK Governance Code states that the Remuneration Committee should set the remuneration of the Chairman. However, the Board believes that it is more appropriate for the remuneration of the Chairman to be set and reviewed in the same manner as that used to determine the remuneration for the other non-executive directors. It is therefore dealt with by the Board, acting upon a recommendation from the executive directors and excluding, for this purpose, the Chairman. No director takes part in the discussion of his/her own remuneration.

The terms of reference of the Board Risk Committee, Audit Committee, the Nominations and Governance Committee and the Remuneration Committee, and the letters of appointment for non-executive directors, are available on request from the Secretary and Solicitor.

RELATIONS WITH MEMBERS

The Society's members comprise its shareholding investors and borrowers. The majority of its customers are therefore members and the Society encourages feedback from them on all aspects of the Society's activities.

All members who are eligible are also encouraged to exercise their vote at the AGM either by attending in person or by voting by proxy, for which purpose they are sent a proxy voting form and reply-paid envelope, or they can vote in any branch or online. All proxy votes are counted. All resolutions are taken on a poll and the Chairman indicates the level of proxies lodged on each resolution by announcing the numbers for and against the resolution. A separate resolution is proposed on each item including a resolution on the Annual Report & Accounts. The Society employs Electoral Reform Services Limited to act as independent scrutineers and ensure the votes are properly received and recorded.

INTERNAL CONTROLS

Responsibility for implementing sound and effective systems of internal control has been delegated by the Board to senior management. The internal audit function provides independent assurance to the Board on the effectiveness of the systems of internal control through the Audit Committee.

The information received and considered by the Audit Committee provided assurance that, during 2010, there were no material breaches of control or regulatory requirements and that, overall, the Society maintained adequate systems of internal control.

AUDITORS

The Society has a policy on the use of the external auditors for non-audit work which has been approved by the Audit Committee. The purpose of this policy, which stipulates when prior approval is required from the Audit Committee for any ancillary services, is to ensure the continued independence and objectivity of the external auditors.

DIRECTORS' REMUNERATION REPORT

INTRODUCTION

This report informs members of the Society of the policy for the remuneration of directors, executive and non-executive, who are equally responsible in law for directing the Society's affairs.

POLICY FOR EXECUTIVE DIRECTORS

Executive directors are employed by the Society and are required to devote substantially the whole of their time to its affairs. The policy of the Board is to recruit and retain high calibre executive directors and to ensure that their remuneration reflects their responsibilities, experience and performance.

The level of remuneration for the executive directors is set by the Remuneration Committee. The Committee consists of the non-executive directors only and is chaired by Bridget Blow, the Society's Deputy Chairman and Senior Independent Director.

The Remuneration Committee is responsible for setting and reviewing the individual elements that comprise the remuneration package for executive directors. These currently consist of a base salary, performance related bonuses, pension arrangements and other benefits. In fulfilling this responsibility the Remuneration Committee has considered recommendations made by the Financial Services Authority, independent advisors, as well as the remuneration policies of the Society's peer group. The Members' Council, a voluntary group of Society members, has also reviewed and supported the Society's approach to executive remuneration.

The Remuneration Committee is aware of concern expressed about the role that bonuses have played in encouraging inappropriate behaviours at some financial institutions. The Committee shares that concern and has designed the Society's remuneration policy for all staff accordingly.

The Remuneration Committee has taken full account of best practice in corporate governance. The UK Corporate Governance Code states 'a significant proportion of executive directors remuneration should be structured so as to link rewards to corporate and individual performance'. It continues that performance related elements should be 'stretching and designed to promote the long term success of the company'.

The Remuneration Committee strongly believes that performance related bonuses enable a flexible approach to remuneration which means payments are accurately aligned to results, as well as providing transparency and clarity of objective. It also ensures that the Society's costs are reduced if for any reason financial performance deteriorates. The Remuneration Committee has considered alternatives but continues to believe that carefully controlled performance related bonuses are in the best interests of the Society and its members.

The principal elements of the executive directors' remuneration packages are described in the following sections.

a) Base salary

The Society's reward strategy for executive directors aims to pay competitive market salaries and to recognise individual development and progression through the annual salary and personal review processes.

Base salary levels are reviewed annually, taking into account comparative data from other building societies. The latest review of remuneration policy found that base salaries for the executive directors remain below median levels relative to other societies of a comparable size.

b) Annual performance related bonus

All eligible Coventry Building Society staff participate in an annual performance related bonus scheme. Eligibility is dependent upon satisfactory individual performance. The executive directors are eligible to participate in this scheme, on the same terms as other members of staff.

In 2010, as has been the case throughout the economic downturn, Coventry Building Society achieved an outstanding performance. The Society retained 'A' ratings from Fitch and Moody's, two of the credit rating agencies that monitor the building society sector, highlighting the financial security provided to members. The Society has achieved sustainable profits, building additional capital reserves to strengthen its financial position and enable future growth. The Society attracted £2.2 billion of additional retail balances through an expanding portfolio of savings offering long term value to members and achieved a record share of the mortgage market by maintaining its capability to lend responsibly. The Society was recognised for its performance in Treating Customers Fairly and is the largest mortgage lender not to appear in complaint league tables issued by the Financial Ombudsman Service.

The strong performance of the Society during 2010 gave rise to a calculated bonus for all 1,501 eligible members of staff equivalent to 11% of base salary. The bonus percentage payable to each of the executive directors of 11% of base salary is identical to that of all other eligible staff.

c) Long Term Incentive Plan

In order to ensure that the remuneration package of executive directors reflects the long-term performance of the Society and members' interests, the Remuneration Committee operates a Long Term Incentive Plan (LTIP) for executive directors.

The primary objective of this plan is to align remuneration with the longer term goals of the Society. The LTIP also helps the Society to recruit and retain executives of the calibre required to promote the interests of members.

Under the LTIP, the executive directors are eligible to receive a performance related payment based on the financial performance of the Society over rolling three year periods.

The plan is designed to make payments in the early part of the year following the end of the three year period providing that strong performance is achieved against the current three year plan. An on-plan performance over each of the three year periods would provide a 20% of salary cash payment, with a current maximum of 40% (which is below the 50% of salary maximum permitted under the Society's Rules) for consistent over-performance over the three year period. The Committee however can award a lower salary cash payment if appropriate.

To protect the interests of members, the Committee may amend any payment if it considers it appropriate in light of either the Society's overall performance or economic conditions. In assessing this, the Committee will take account of a range of factors such as customer and member satisfaction, the impact of 'one-off' exceptional items, the performance of competitors, the Society's health and safety record, and the individual performance of participants.

All payments under the LTIP are subject to approval by the Remuneration Committee and are not pensionable.

During the period 2008 – 2010 the Society increased its total assets by £7.4 billion. Mortgage balances rose by £5.8 billion (49%) at a time of significant market contraction with many lenders unwilling or unable to maintain their lending. This mortgage growth was fully funded by a £7.3 billion (71%) increase in retail savings balances. The Society maintained its 'A' rating from both Moody's and Fitch credit rating agencies and the core tier 1 capital ratio was the highest of any building society, highlighting the security of members' investment in the Society. A correspondingly strong performance was recorded in terms of efficiency improvements with the Society achieving the lowest cost to mean asset ratio of any building society, a reduction from 0.48% to 0.37% in the period.

In addition, the Society won numerous awards for its products, service and is the largest UK mortgage lender not to be included in any league table of complaints issued by the Financial Ombudsman Service. The Society was also independently recognised in 2009 and 2010 for 'Treating Customers Fairly'.

At its last inspection conducted in 2009, Coventry was identified as one of the top 100 UK organisations by Investors in People, and has expanded its support provided to local charities and community groups to over 150 organisations by 2010. These included a ground-breaking partnership with The Royal British Legion that has raised over £4.6 million for the Poppy Appeal since it began in October 2008 and recognition as The Legion's leading corporate partner in 2010.

Taking into account the overall performance detailed above and the performance against the LTIP profit targets, the Remuneration Committee approved a payment for each participant equivalent to 15% of base salary at 1 January 2008. The Committee is satisfied that this reflects management performance over the period.

As for base salaries, bonus and LTIP payments are also benchmarked on a regular basis. Total bonuses earned by executive directors remain significantly below median levels relative to the comparison group of large building societies.

DIRECTORS' REMUNERATION REPORT
(continued)

d) Pension arrangements
Coventry Building Society closed its final salary pension scheme to new entrants in December 2001, replacing it with a defined contribution pension scheme.

No special arrangements have been put in place for executive directors since this change was implemented and consequently the Chief Operating Officer and Finance Director, who both joined subsequent to 2002, are active members of the Society's funded defined contribution pension scheme.

The Sales and Marketing Director, whose long service at the Society pre dates 2002 by a number of years, continues to be a member of the Society's contributory final salary pension scheme.

David Stewart, although a member of the final salary pension scheme on joining the Society, voluntarily left this scheme on being appointed Chief Executive in 2006.

The Remuneration Committee has reviewed the pension arrangements offered by a comparator group of building societies and in the majority of cases, their executive directors continue to benefit from participation in final salary pension schemes.

e) Other benefits
Each executive director is provided with a fully expensed car or a cash alternative, and membership of a private medical insurance scheme.

POLICY FOR NON-EXECUTIVE DIRECTORS
Non-executive directors are independent of the Society's management and are not required to devote the whole of their time to its affairs.

After considering recommendations from the executive directors, the Board (chaired for this purpose by the chief executive) determines the remuneration of all non-executive directors. No director takes part in the discussion of his or her own remuneration. Fees of non-executive directors are reviewed annually in light of their responsibilities and comparative information from other building societies. In keeping with the Society's approach to executive compensation, fees for non-executive directors are below median levels reported by the competitor group at its last inspection of large societies.

Non-executive directors do not participate in any performance related pay or bonus scheme, pension arrangements or other benefits; nor do they have service contracts.

DIRECTORS' REMUNERATION
Full details of directors' remuneration for 2010 and prior year comparatives, all of which form part of this report, can be found in note 11 to the Accounts.

EXECUTIVE DIRECTORS' PENSIONS
Full details of executive directors' pension benefits can be found in note 11 to the Accounts.

DIRECTORS' SERVICE CONTRACTS
In 2006 the Society entered into a service contract with David Stewart. The contract expires at the age of 60, but is terminable by David Stewart on six months' notice and by the Society on one year's notice.

In 2009 the Society appointed Colin Franklin (Sales and Marketing Director) and Phil Vaughan (Chief Operating Officer) to the Board. Service contracts were entered into which are terminable by the individual on six months' notice and by the Society on one year's notice.

In 2010 the Society appointed John Lowe (Finance Director) to the Board. A service contract was entered into, which is terminable by John Lowe on six months' notice and by the Society on one year's notice.

On behalf of the Board

Bridget Blow
Chairman of the Remuneration Committee
28 February 2011

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The following statement, which should be read in conjunction with the statement of the auditors' responsibilities on page 30, is made by the directors to explain their responsibilities in relation to the preparation of the Annual Accounts, Annual Business Statement and Directors' Report.

The directors are responsible for preparing the Annual Report, Annual Business Statement, Directors' Report and the Annual Accounts in accordance with applicable 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 that law they are required to prepare the Group Annual Accounts in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and applicable law and have elected to prepare the Society Accounts on the same basis.

The Group and Society Annual Accounts are required by law and IFRS as adopted by the EU to present fairly the financial position and the performance of the Group and the Society; the Building Societies Act 1986 provides in relation to such Annual Accounts that references in the relevant part of that Act to Annual Accounts giving a true and fair view are references to their achieving a fair presentation.

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

- select suitable accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the Annual Accounts on the going concern basis, unless it is inappropriate to presume that the Group and Society will continue in business.

In addition to the Annual 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 proper accounting records that 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 business (in accordance with the rules made by FSA under the Financial Services and Markets Act 2000).

The directors have general responsibility for safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future. For this reason, the Annual Accounts continue to be prepared on the going concern basis.

INDEPENDENT AUDITORS' REPORT

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF COVENTRY BUILDING SOCIETY

We have audited the Group and Society financial statements of Coventry Building Society for the year ended 31 December 2010 which comprise Group and Society Income Statements, Group and Society Statements of Other Comprehensive Income, Group and Society Statements of Financial Position, the Group and Society Statements of Changes in Members' Interests, the Group and Society Statements of Cash Flows, and the related notes 1 to 45. 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.

This report is made solely to the Society's members, as a body, in accordance with Section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As explained more fully in the Directors' Responsibilities Statement set out on page 29, the directors are responsible for the preparation of the financial statements which give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements 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 Ethical Standards for Auditors.

SCOPE OF THE AUDIT OF THE FINANCIAL STATEMENTS

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements 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 financial statements.

OPINION ON FINANCIAL STATEMENTS

In our opinion the financial statements:

- 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 2010 and of the Group's and the Society's income and expenditure 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 financial statements, 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 financial statements are prepared is consistent with the accounting records and the financial statements; 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 Society financial statements 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.

Peter Wallace (Senior statutory auditor)
for and on behalf of Ernst & Young LLP, Statutory Auditor
London

28 February 2011

INCOME STATEMENTS

for the year ended 31 December 2010

	Notes	Group 2010 £m	Society 2010 £m	Group 2009 £m	Society 2009 £m
Interest receivable and similar income	3	**599.5**	**678.0**	545.5	642.3
Interest payable and similar charges	4	**(453.5)**	**(557.3)**	(420.5)	(529.5)
Net interest income		**146.0**	**120.7**	125.0	112.8
Fees and commissions receivable	5	**15.9**	**15.1**	17.4	16.9
Fees and commissions payable	6	**(1.5)**	**(1.4)**	(1.1)	(1.1)
Other operating income	7	**0.6**	**0.5**	0.7	0.7
Net (losses)/gains from derivative financial instruments	8	**(0.7)**	**(0.7)**	1.3	1.3
Total income		**160.3**	**134.2**	143.3	130.6
Administrative expenses	9	**(68.0)**	**(65.6)**	(61.6)	(59.8)
Amortisation of intangible assets	24	**(3.0)**	**(3.0)**	(2.7)	(2.7)
Depreciation of tangible fixed assets	25,26	**(4.3)**	**(4.3)**	(4.0)	(4.0)
Operating profit before impairments and exceptional items		**85.0**	**61.3**	75.0	64.1
Impairment losses on loans and advances to customers	13	**(11.8)**	**(8.9)**	(19.9)	(14.3)
Release of provision for impairment of debt securities	15	**2.1**	**2.1**	1.5	1.5
Release of provisions	35	**–**	**–**	2.9	2.9
Operating profit after impairment and before exceptional items		**75.3**	**54.5**	59.5	54.2
Provision for FSCS levies	14,35	**(5.6)**	**(5.6)**	(2.0)	(2.0)
Stroud & Swindon integration and merger related costs	45	**(11.2)**	**(11.2)**	–	–
Operating profit after impairments and exceptional items		**58.5**	**37.7**	57.5	52.2
Gain on business combination	45	**43.8**	**70.7**	–	–
Charitable donation to Poppy Appeal	16	**(1.7)**	**(1.7)**	(1.3)	(1.3)
Profit before tax		**100.6**	**106.7**	56.2	50.9
Taxation	17	**(15.7)**	**(10.0)**	(12.7)	(11.7)
Profit for the financial year		**84.9**	**96.7**	43.5	39.2

Profit for the financial year arises from continuing operations and is attributable to the members of the Society.

STATEMENTS OF OTHER COMPREHENSIVE INCOME

for the year ended 31 December 2010

	Notes	Group 2010 £m	Society 2010 £m	Group 2009 £m	Society 2009 £m
Profit for the financial year		**84.9**	**96.7**	43.5	39.2
Other comprehensive income					
Actuarial gain/(loss) on defined benefit pension plans	12	**5.0**	**5.0**	(3.3)	(3.3)
Tax on actuarial gain/loss on defined benefit pension plans	12,17	**(1.4)**	**(1.4)**	0.9	0.9
Fair value movements on Available-for-sale assets taken to reserves	39	**19.0**	**19.0**	(11.1)	(11.1)
Tax on fair value movements taken to reserves	17,39	**(5.3)**	**(5.3)**	3.1	3.1
Other comprehensive income for the year, net of tax		**17.3**	**17.3**	(10.4)	(10.4)
Total comprehensive income for the year, net of tax		**102.2**	**114.0**	33.1	28.8

The accounting policies and notes on pages 36 to 81 form part of these Accounts.

STATEMENTS OF FINANCIAL POSITION

as at 31 December 2010

	Notes	Group 2010 £m	Society 2010 £m	Group 2009 £m	Society 2009 £m
Assets					
Cash in hand and balances with the Bank of England	18	**1,444.2**	**1,443.8**	302.2	300.0
Loans and advances to credit institutions	19	**193.4**	**193.4**	325.2	325.2
Debt securities	20	**2,864.0**	**2,864.0**	3,538.0	3,538.0
Other liquid assets		**30.3**	**30.3**	-	-
		4,531.9	**4,531.5**	4,165.4	4,163.2
Derivative financial instruments	21	**73.4**	**73.4**	29.3	29.3
Loans and advances to customers	22	**17,573.7**	**13,523.7**	14,074.7	11,397.2
Hedge accounting adjustment		**40.6**	**40.6**	76.1	76.1
Pension benefit surplus	12	**7.2**	**7.2**	6.9	6.9
Prepayments and accrued income		**6.1**	**5.7**	5.6	5.6
Investments in subsidiary undertakings	23	**–**	**7,217.3**	–	5,313.5
Intangible assets	24	**12.2**	**12.2**	9.9	9.9
Property, plant and equipment	25	**28.1**	**28.1**	24.9	24.9
Investment properties	26	**5.8**	**0.6**	0.6	0.6
Current tax asset		**–**	**–**	6.5	8.2
Deferred tax assets	27	**19.4**	**8.2**	2.1	2.0
Non-current assets held for sale	28	**3.9**	**3.9**	–	–
Total assets		**22,302.3**	**25,452.4**	18,402.0	21,037.4
Liabilities					
Shares	29	**17,637.6**	**17,637.6**	13,218.8	13,218.8
Deposits from banks	30	**1,315.4**	**1,315.4**	1,370.3	1,370.3
Other deposits	31	**34.1**	**34.1**	18.0	18.0
Amounts owed to other customers	32	**645.2**	**645.2**	856.2	856.2
Derivative financial instruments	21	**139.4**	**139.4**	108.9	108.9
Debt securities in issue	33	**1,551.3**	**1,551.3**	1,969.8	1,969.8
Other liabilities	34	**16.6**	**3,167.5**	19.3	2,661.7
Current tax liabilities		**10.1**	**6.4**	–	–
Deferred tax liabilities	27	**5.6**	**5.6**	5.3	5.3
Pension benefit obligations	12	**3.1**	**3.1**	–	–
Provisions for liabilities and charges	35	**15.9**	**15.9**	10.1	10.1
Accruals and deferred income		**12.1**	**9.7**	9.2	8.7
Subordinated liabilities	36	**68.2**	**68.2**	70.7	70.7
Subscribed capital	37	**161.3**	**161.3**	161.2	161.2
Total liabilities		**21,615.9**	**24,760.7**	17,817.8	20,459.7
Equity					
General reserve	38	**704.5**	**709.8**	616.0	609.5
Available-for-sale reserve	39	**(18.1)**	**(18.1)**	(31.8)	(31.8)
Total liabilities and equity		**22,302.3**	**25,452.4**	18,402.0	21,037.4
Memorandum item					
Financial commitments	40	**152.4**	**108.0**	56.0	5.0

The accounting policies and notes on pages 36 to 81 form part of these Accounts.

Approved by the board of directors on 28 February 2011.

David Harding
Chairman

David Stewart
Chief Executive

John Lowe
Finance Director

STATEMENTS OF CHANGES IN MEMBERS' INTERESTS

for the year ended 31 December 2010

Group	Notes	General reserve £m	Available-for-sale reserve £m	Total £m
As at 1 January 2010	38,39	**616.0**	**(31.8)**	**584.2**
Profit for the financial year		**84.9**	**–**	**84.9**
Actuarial gain on defined benefit pension plans	12	**5.0**	**–**	**5.0**
Tax on actuarial gain on defined benefit pension plans	12,17	**(1.4)**	**–**	**(1.4)**
Fair value movements on Available-for-sale assets taken to reserves	39	**–**	**19.0**	**19.0**
Tax on fair value movements taken to reserves	17,39	**–**	**(5.3)**	**(5.3)**
As at 31 December 2010		**704.5**	**(18.1)**	**686.4**
As at 1 January 2009	38,39	574.9	(23.8)	551.1
Profit for the financial year		43.5	–	43.5
Actuarial loss on defined benefit pension plan	12	(3.3)	–	(3.3)
Tax on actuarial loss on defined benefit pension plan	12,17	0.9	–	0.9
Fair value movements on Available-for-sale assets taken to reserves	39	–	(11.1)	(11.1)
Tax on fair value movements taken to reserves	17,39	–	3.1	3.1
As at 31 December 2009		616.0	(31.8)	584.2

Society	Notes	General reserve £m	Available-for-sale reserve £m	Total £m
As at 1 January 2010	38,39	**609.5**	**(31.8)**	**577.7**
Profit for the financial year		**96.7**	**–**	**96.7**
Actuarial gain on defined benefit pension plans	12	**5.0**	**–**	**5.0**
Tax on actuarial gain on defined benefit pension plans	12,17	**(1.4)**	**–**	**(1.4)**
Fair value movements on Available-for-sale assets taken to reserves	39	**–**	**19.0**	**19.0**
Tax on fair value movements taken to reserves	17,39	**–**	**(5.3)**	**(5.3)**
As at 31 December 2010		**709.8**	**(18.1)**	**691.7**
As at 1 January 2009	38,39	572.7	(23.8)	548.9
Profit for the financial year		39.2	–	39.2
Actuarial loss on defined benefit pension plan	12	(3.3)	–	(3.3)
Tax on actuarial loss on defined benefit pension plan	12,17	0.9	–	0.9
Fair value movements on Available-for-sale assets taken to reserves	39	–	(11.1)	(11.1)
Tax on fair value movements taken to reserves	17,39	–	3.1	3.1
As at 31 December 2009		609.5	(31.8)	577.7

The accounting policies and notes on pages 36 to 81 form part of these Accounts.

STATEMENTS OF CASH FLOWS

for the year ended 31 December 2010

	Notes	Group 2010 £m	Society 2010 £m	Group 2009 £m	Society 2009 £m
Cash flows from operating activities					
Profit before tax		**100.6**	**106.7**	56.2	50.9
Adjustments for:					
Non-cash items included in profit before tax	44	**(5.0)**	**(29.8)**	164.0	158.6
Changes in operating assets	44	**(1,235.6)**	**(407.9)**	(865.2)	(152.0)
Changes in operating liabilities	44	**1,545.7**	**1,546.6**	691.1	690.9
Interest paid on subordinated liabilities		**(3.9)**	**(3.9)**	(4.0)	(4.0)
Interest paid on subscribed capital		**(12.3)**	**(12.3)**	(12.2)	(12.2)
Taxation		**(7.1)**	**(7.1)**	(5.2)	(5.0)
Net cash flows from operating activities		**382.4**	**1,192.3**	24.7	727.2
Cash flows from investing activities					
Purchase of investment securities		**(5,687.0)**	**(5,687.0)**	(12,479.9)	(12,479.9)
Sale and maturity of investment securities		**6,796.2**	**6,796.2**	12,084.0	12,084.0
Purchase of property, plant and equipment		**(5.6)**	**(5.6)**	(3.4)	(3.4)
Purchase of intangible assets		**(3.1)**	**(3.1)**	(4.4)	(4.4)
Cash and cash equivalents acquired on transfer of engagements		**10.8**	**9.7**	-	-
Net cash flows from investing activities		**1,111.3**	**1,110.2**	(403.7)	(403.7)
Cash flows from financing activities					
Loans from connected undertakings		**–**	**508.6**	–	158.8
Loans to connected undertakings		**–**	**(1,315.6)**	–	(861.6)
Repurchase of subordinated liabilities		**(55.0)**	**(55.0)**	–	–
Repurchase of debt securities		**(629.0)**	**(629.0)**	–	–
Issue of debt securities		**400.0**	**400.0**	346.6	346.6
Net cash flows from financing activities		**(284.0)**	**(1,091.0)**	346.6	(356.2)
Net increase/(decrease) in cash		**1,209.7**	**1,211.5**	(32.4)	(32.7)
Cash and cash equivalents at start of year		**328.1**	**325.9**	360.5	358.6
Cash and cash equivalents at end of year	44	**1,537.8**	**1,537.4**	328.1	325.9

The accounting policies and notes on pages 36 to 81 form part of these Accounts.

NOTES TO THE ACCOUNTS

1. ACCOUNTING POLICIES

The following accounting policies have been applied consistently in dealing with items that were considered material in relation to the Accounts.

BASIS OF PREPARATION

These Accounts have been prepared in accordance with IFRS as adopted by the EU; interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC); and with those parts of the Building Societies (Accounts and Related Provisions) Regulations 1998 applicable to organisations reporting under IFRS.

The Accounts have been prepared on an historical cost basis, as modified by the revaluation of Available-for-sale debt securities and certain financial instruments which are measured at fair value. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges and are otherwise carried at cost are adjusted to record changes in the fair values attributable to the risks that are being hedged.

BUSINESS COMBINATIONS

The Society merged with Stroud & Swindon Building Society on 1 September 2010. This business combination has been accounted for using the acquisition method (see note 45), following the requirements of IFRS 3 (2008 Revised) 'Business Combinations' which was endorsed by the EU in June 2009. Results relating to the merger with Stroud & Swindon Building Society are included within the Society's results effective from the date of completion of the merger, 1 September 2010.

CHANGES IN ACCOUNTING POLICY

The following standards and interpretations have been released since 1 January 2010. The Society has not early adopted any of these IFRSs. The expected impact on the Society is detailed below:

IFRS 7 Financial Instruments: Disclosures (Amendment)

The amendments to IFRS 7 shall be effective for annual periods beginning on or after 1 July 2011. These amendments ensure sufficient information is disclosed to allow users of financial statements to evaluate the risk exposures relating to transfers of financial assets and the effect of those risks on an entity's financial position. The Society does not expect any significant impact on its financial position or performance.

IFRS 9 Financial Instruments: Classification and Measurement

IFRS 9 as issued, reflects the first phase of the Board's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities. The standard is effective for annual periods beginning on or after 1 January 2013. In subsequent phases, the Board will address hedge accounting, impairment and derecognition. The adoption of IFRS 9 will have an effect on the classification and measurement of the Society's financial assets and financial liabilities. However, the Society has determined that the effect shall be quantified in conjunction with the other phases when issued, to present a comprehensive picture.

IAS 24 Related Party Disclosures (Amendment)

The amended standard is effective for annual periods beginning on or after 1 January 2011. It clarifies the definition of a related party to simplify the identification of such relationships and to eliminate inconsistencies in its application. The revised standard introduced a partial exemption of disclosure requirements for government-related entities. Early adoption is permitted for either the partial exemption for government-related entities or for the entire standard. The Society does not expect any significant impact on its financial position or performance.

IFRIC 14 Prepayments of a minimum funding requirement (Amendment)

The amendment to IFRIC 14 is effective for annual periods beginning on or after 1 January 2011 with retrospective application. The amendment provides guidance on assessing the recoverable amount of a net pension asset. The amendment permits an entity to treat the prepayment of a minimum funding requirement as an asset. The amendment is not expected to have any significant impact on the financial statements of the Society.

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments

IFRIC 19 is effective for annual periods beginning on or after 1 July 2010. The interpretation clarifies that equity instruments issued to a creditor to extinguish a financial liability qualify as consideration paid. The equity instruments issued are measured at their fair value. In case this cannot be reliably measured, they are measured at the fair value of the liability extinguished. Any gain or loss is recognised immediately in profit or loss. The adoption of this interpretation will have no effect on the financial statements of the Society.

Improvements to IFRSs
The IASB issued Improvements to IFRSs in April 2009 and May 2010, an omnibus of amendments to its existing standards. The Society has considered the impact of these improvements and, where necessary, has made adjustments to the disclosure in the financial statements.

The preparation of financial statements that conform with IFRS requires the use of certain critical judgements and estimates, a summary of which is presented in note 2. The areas involving estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under current or normal operating circumstances.

BASIS OF CONSOLIDATION

The Group Accounts consolidate the assets, liabilities and results of the Society and all its subsidiary companies.

The financial statements are presented in sterling millions (£m), and are rounded to the nearest hundred thousand except where otherwise indicated.

Subsidiaries are all entities, including special purpose entities, controlled by the Society. Control exists when the Society has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The carrying value of the investment in the subsidiaries in the Society's balance sheet is at cost. Intragroup transactions, balances and unrealised gains on transactions between Group companies are eliminated in the consolidated accounts.

INTEREST RECEIVABLE AND INTEREST EXPENSE

For instruments measured at amortised cost the effective interest rate method is 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. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset.

In calculating the effective interest rate, the Society estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes the spread of various incentives, fees and charges, both paid and received by the Society, across the expected life of the loan account. Items spread in this way include:

- initial interest rate discounts;
- cash backs and other customer incentives; and
- certain fees and charges paid and received by the Society.

The purpose of using the effective interest rate method is to recognise interest income at a more level yield across the expected life of the product than would be obtained by recognising income as it is received.

Interest income on Available-for-sale debt securities is included in interest receivable and similar income.

FEES AND COMMISSIONS

Fees and commissions receivable and payable that are not spread across expected asset lives under the effective interest rate method are taken to income on an accruals basis as services are provided, or on the completion of an act to which the fee relates.

SEGMENTAL REPORTING

The Society operates solely within the retail financial services sector and within the United Kingdom. As such, no detailed segmental analysis is required.

INTANGIBLE FIXED ASSETS

Intangible assets consist of software development costs and other intangible assets. Software development costs and purchased software that is not an integral part of a related hardware purchase is recognised as an intangible asset. Amortisation of such assets is charged to the income statement on a straight line basis over the useful life of the asset. The useful life of computer software is between three and eight years, depending on the nature of the asset.

Other intangible assets arise from retail deposits acquired by the Society. These are amortised using the straight line method over the estimated useful life of 16 months. The amortisation period is reviewed annually.

NOTES TO THE ACCOUNTS
(continued)

LEASES AND CONTRACT PURCHASE AGREEMENTS

The determination of whether an arrangement is, or contains, a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Where the Society enters into a lease that entails taking substantially all the risks and rewards of ownership of an asset, the agreement is treated as a finance lease. The asset is recorded in the balance sheet within property, plant and equipment and is depreciated over its estimated useful life. If there is no reasonable certainty that the Society will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the lease term and its useful life. Future instalments under such leases, net of finance charges, are included within creditors. Rentals payable are apportioned between the finance element, which is charged to the income statement at a constant annual rate, and the capital element which reduces the outstanding obligation for future instalments.

All other leases are accounted for as operating leases and payments are charged to administrative expenses on a straight line basis over the period of the lease. Rents receivable are credited to other operating income on a straight line basis over the period of the lease.

TAXATION INCLUDING DEFERRED TAX

Income tax on the profits for the year comprises current and deferred taxation.

Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates and laws that are enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements, with the exception that deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, carried forward tax credits or tax losses can be utilised.

Deferred tax assets and liabilities are measured on an non-discounted basis at the tax rates that are expected to apply when the related asset is realised or liability settled, based on tax rates and laws enacted or substantively enacted by the balance sheet date.

Income tax is charged or credited directly to equity if it relates to items that are credited or charged to equity. Otherwise income tax is recognised in the income statement.

INVESTMENT PROPERTIES, PROPERTY, PLANT AND EQUIPMENT

Investment property is property held to earn rentals or for capital appreciation or for both, rather than for sale or use in the business. The Society recognises investment properties at cost less accumulated depreciation and any accumulated impairment. The carrying values of investment properties are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment. As permitted by IFRS 1, the Society treated previous valuations of certain properties as the deemed cost of those properties on transition to IFRS. The carrying values of property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

An asset's carrying value is written down immediately to its recoverable amount if the asset's carrying value is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the net disposal proceeds with the carrying value of the asset and are included within the income statement.

Depreciation is provided on a straight line basis over the anticipated useful life of the asset as follows:

• Freehold buildings (including investment properties)	Over a period of 50 years
• Leasehold buildings	Shorter of remaining term of the lease and useful life
• Equipment, fixtures, fittings and vehicles	Three to eight years

NON-CURRENT ASSETS HELD FOR SALE

A non-current asset is classified as held for sale if the Society will recover the carrying amount principally through a sale transaction rather than through continuing use. A non-current asset classified as held for sale is measured at the lower of the carrying amount and fair value less costs to sell. If the asset is acquired as part of a business combination it is initially measured at fair value less costs to sell. Assets classified as held for sale are shown separately on the face of the statement of financial position.

FINANCIAL LIABILITIES

Financial liabilities, including shares, bank and other deposits, amounts owed to other customers, debt securities in issue, subordinated liabilities and subscribed capital are initially measured at fair value plus (for items not subsequently measured at fair value through the income statement), transaction costs directly attributable to the acquisition or issue.

Financial liabilities are subsequently measured at amortised cost, adjusted for the amortisation of any transaction costs, premiums and discounts. The amortisation is recognised in interest payable and similar charges using the effective interest rate method.

Permanent Interest Bearing Shares (subscribed capital), which are redeemable at specific dates at the option of the Society, are classed as financial liabilities.

Financial liabilities are derecognised when the obligation is discharged, cancelled or has expired. Financial liabilities that are designated as hedged items are subject to measurement under the hedge accounting requirements described in the derivatives and hedge accounting policy note. The impact of hedging on the measurement of financial liabilities is detailed in the derivatives and hedge accounting policy note.

Purchases and sales of financial assets are accounted for at trade date.

FINANCIAL ASSETS

All financial assets are measured initially at their fair value plus transaction costs, except in the case of financial assets recorded at fair value through profit or loss. The Society classifies its financial assets at inception into the following categories:

Financial assets at fair value through profit or loss

This category consists of derivative financial assets. Derivative financial assets are carried at fair value. The fair values are quoted market prices where there is an active market, or are based on valuation techniques where there is not.

Gains and losses arising from changes in the fair values are recognised in the income statement.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Society's residential mortgage loans, unsecured lending and loans to credit institutions are classified as loans and receivables.

Loans are recognised when the funds are advanced to customers. Loans and receivables are carried at amortised cost using the effective interest rate method.

Available-for-sale

Available-for-sale assets are non-derivative financial assets that are designated as such or not classified into either of the two categories above.

Available-for-sale assets are initially measured at fair value. Subsequently, Available-for-sale assets are carried at fair value. The fair values, in the majority of cases, are based on quoted market prices or prices obtained from counterparties. In cases where quoted market prices are not available, discounted cash flow valuations are used.

Unrealised gains and losses arising from changes in the fair values are recognised directly in the Available-for-sale reserve, except for impairment losses and foreign exchange gains and losses, which are recognised in the income statement. Gains and losses arising on the sale of Available-for-sale assets, including any cumulative gains or losses previously recognised in the Available-for-sale reserve, are recognised in the income statement.

NOTES TO THE ACCOUNTS
(continued)

Financial assets are derecognised when the rights to receive cash flows have expired or where substantially all of the risks and rewards of ownership have been transferred. In respect of the Group's secured funding structure, the Society sells to another entity, Coventry Building Society Covered Bonds LLP, the right to receive the cash flows arising on the loans which have been transferred. However, other than in a default or insolvency scenario, the Society receives substantially all of the profit of that entity, and hence retains substantially all of the risks and rewards of the transferred loans. Hence the transferred loans are retained on the Society's balance sheet.

The impact of hedging on the measurement of financial assets is detailed in the derivatives and hedge accounting policy note.

IMPAIRMENT OF LOANS AND ADVANCES TO CUSTOMERS

The Society assesses its loans and advances to customers for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event (or events) that has occurred after initial recognition and before the balance sheet date and has a reliably measurable impact on the estimated future cash flows of the loan amount.

Impairment is categorised as either individual impairment (where individual assets have been assessed for loss) or collective impairment (where losses are assessed as being present in a portfolio of loans, but they cannot be identified to individual accounts).

If there is objective evidence that an impairment loss on loans and advances to customers has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred). The carrying amount of the asset is reduced through the use of an impairment allowance and the amount of the loss is recognised in the income statement.

When a loan is not collectable, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recorded in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the customer's credit rating), the previously recognised impairment loss is reversed by adjusting the impairment allowance. The amount of the reversal is recognised in the income statement.

SALE AND REPURCHASE AGREEMENTS

Securities lent or sold subject to a commitment to repurchase them (a 'repo') are retained on the balance sheet when substantially all the risks and rewards of ownership remain within the Group. The counterparty liability is included separately in the balance sheet, as appropriate. The difference between the sale and repurchase price is accrued over the life of the agreements using the effective interest rate method.

DERIVATIVE FINANCIAL INSTRUMENTS

The Society holds derivative financial instruments for the purposes of managing the risks associated with its various fixed and capped rate assets, its fixed rate liabilities and its foreign currency transactions. In accordance with legislation and its treasury policy, the Society holds derivative financial instruments only for risk management and not for speculative or trading purposes.

All derivative financial instruments are stated in the accounts at fair value, with movements in fair value taken through the income statement under 'net (losses)/gains from derivative financial instruments' in the period in which the movement occurred. Fair values are calculated by discounted cash flow models using yield curves that are based on observable market data or are based on valuations from counterparties.

HEDGE ACCOUNTING

All derivatives entered into by the Society are for the purpose of providing an economic hedge. Full details of hedging activities are contained in note 21. Hedge accounting is an optional treatment, subject to the satisfaction of specific rules and conditions set out in IAS 39. The Group periodically tests hedge effectiveness and applies fair value hedge accounting, so that changes in the fair value of the underlying asset or liability that are attributable to the hedged risk are recorded in the income statement to offset the fair value movement of the related derivative.

PENSION COSTS

The Society operates two defined benefit pension schemes and two defined contribution schemes for members of staff.

Contributions to the defined contribution pension schemes are recognised as an expense in the income statement as incurred, on an accruals basis.

The Society's net obligation under the defined benefit pension schemes is assessed annually by an independent qualified actuary. The net obligation is calculated as the difference between the fair value of the schemes' assets and the amount of future entitlements earned by scheme members from service in the current and prior periods, discounted back to present values using a rate based on an index of long dated AA rated corporate bonds. This calculation allows the net obligations of the schemes to be expressed as either a surplus or deficit, which is recognised as respectively either an asset or liability in the Society's accounts at the balance sheet date.

Pension costs for service in the period are assessed in accordance with advice from a qualified actuary and are recognised in the income statement. Pension fund actuarial gains or losses are recognised in full in the year they occur in the statement of other comprehensive income.

FOREIGN CURRENCY TRANSLATION

The consolidated financial statements are presented in sterling, which is the functional currency of the Group.

Foreign currency transactions are translated into sterling using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are retranslated at the rate prevailing at the year end. Foreign exchange gains and losses resulting from the retranslation and settlement of these items are recognised in the income statement.

LIQUID ASSETS

Liquid assets consist of cash in hand and balances with the Bank of England, loans and advances to credit institutions, debt securities and other liquid assets. Other liquid assets consists of amounts advanced to other non-credit institutions.

The Society uses various debt securities (certificates of deposit, gilts, etc) to maintain its liquidity position. These debt securities are classified as Available-for-sale under the terms of IAS 39 and, as such, are recorded in the accounts at fair value, with changes in fair value taken to the Available-for-sale reserve within equity reserves.

If debt securities are sold, the gain or loss on sale is measured as the difference between sale proceeds and original cost (net of any discount or premium on acquisition). Any fair value adjustments already recognised are released from reserves at the time of the sale and offset against the gain or loss.

When a decline in the fair value of an Available-for-sale financial asset has been recognised directly in equity reserves and there is objective evidence that the asset is impaired, the cumulative loss recognised in equity reserves is removed and recognised in the income statement.

CASH AND CASH EQUIVALENTS

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash and non-restricted balances with central banks and loans and advances to credit institutions.

PROVISIONS AND CONTINGENT LIABILITIES

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 the amount can be estimated reliably.

Contingent liabilities are potential obligations from past events which shall be confirmed by future events. Contingent liabilities are not recognised within the balance sheet.

EXCEPTIONAL ITEMS

Exceptional items are items of income and expenditure that are disclosed separately on the basis that they are material, either by their nature or their size, to the understanding of the Society's financial performance, and they significantly distort the comparability of financial performance between periods. During 2010 this included costs relating directly to the merger with Stroud & Swindon Building Society, which comprise of deal costs, integrations costs, and Stroud & Swindon Building Society operating costs incurred prior to the year end, which will conclude within the next twelve months when integration has completed.

'Gain on business combination' has been recognised below 'operating profit after impairment and exceptional items', as the gain does not form part of operating activities, and to enable appropriate comparison with the prior year comparatives.

2. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

JUDGEMENTS

In the process of applying the Society's accounting policies, the directors have made the following judgements and estimates that have the most significant effect on the amounts recognised in the financial statements.

The treatment of derivative financial instruments

The Society uses derivative financial instruments. All such instruments are used to mitigate the interest rate risk and foreign currency risk that arises from the Society's lending and funding activities. All derivatives used for such purposes are treated as fair value hedges. This treatment is consistent with the economic purpose of using the derivative instruments, which is to provide a hedge against the movement in the fair value of fixed rate and foreign currency assets and liabilities. It also enables the Society to take advantage of the fair value hedge accounting provisions of IAS 39, which allow the recognition of movements in the hedged portion of the fair values of the underlying assets and liabilities that should materially offset the volatility that may arise from recognising the fair value movements of the derivatives themselves.

Debt securities

The Society maintains a portfolio of liquid assets to ensure it has sufficient funds available to meet its financial commitments as they fall due. A large part of this portfolio is made up of debt securities, for which there are various accounting treatments permitted under IAS 39. The Society has adopted the 'Available-for-sale' treatment as this most closely matches the way debt securities are used within the business, with a portfolio of assets maintained for continuing use, and individual assets available to be sold depending on particular requirements for funding or the maintenance of interest yields. This treatment requires that debt securities are recognised at fair value with movements in fair value taken to equity reserves.

The determination of whether Available-for-sale instruments are impaired is assessed based on similar criteria to financial assets carried at amortised cost.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the balance sheet cannot be derived from active markets, they are determined using interest rate yield curves and other relevant market data. These are judged to be the most appropriate valuation tools. The valuation of financial instruments is disclosed in more detail in note 42.

Deferred tax

The Society recognises deferred tax on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available to utilise the asset. The Society considers that sufficient future taxable profit will, in fact, be available to utilise all the Society's deferred tax assets and the Society has therefore recognised deferred tax assets where they have arisen.

Pension schemes

The Society's defined contribution and defined benefit pension schemes are accounted for under the terms of IAS 19. The standard requires the calculation of the net assets or liabilities of the defined benefit schemes and their inclusion in the statement of financial position. The result is dependent in part on the interest rate used to discount scheme liabilities back to present value. IAS 19 requires that this should equate to a rate available on an AA rated corporate bond. In practice, the rates available on such bonds cover a wide range and there is therefore a range of possible outcomes that could be disclosed as the pension schemes' net position. In order to avoid this uncertainty, the directors have selected a rate from within a narrow range recommended by the Society's professional pension scheme advisors. This range has been based on an index of related corporate bond yields.

ESTIMATION UNCERTAINTY

The key assumptions regarding the future and other key sources of estimation uncertainty at the balance sheet date that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year are discussed below.

Loan impairment and other provisions

IAS 39 requires that loan losses are only recognised where there is objective evidence of impairment. The Society has applied this requirement in determining the level of losses present in its loans and advances to customers, but has been required to apply management judgement in determining the financial impact of this impairment. IAS 39 makes a distinction between individual and collective impairment. Individual impairment relates to situations where individual assets are assessed for loss. The Society has used this approach on loans in possession and those in arrears. Estimates that have been applied include assessing the likelihood of the loan going into possession for those cases currently in arrears, the length of time expected to be required to complete the sale of properties in possession, and the expected costs of realisation. Collective impairment relates to cases where losses are assessed as being present in a loan portfolio, but they cannot be identified to individual accounts. This approach has been used to calculate a value of incurred but not reported losses, where statistical analysis has been used to determine a value for losses where a loss event has already impacted an account, but has not yet manifested itself in arrears data. A portfolio approach is also used on sections of the loan book where there are known problems but individual accounts are again as yet not identifiable. This method has been applied to loans advanced on city centre buy-to-let flats where a problem of oversupply is having a negative effect on prices and ease of sale, with the result that the Society has made an impairment provision against these assets.

Estimated asset lives

The Society recognises interest on loans and advances to customers on the basis of their effective interest rate. This is a constant rate that averages out the effect of incentives and fees across the expected life of the loan account. A critical assumption in the calculation is the expected life, as this determines the assumed period over which customers may be paying various differentiated interest rates. The calculation of the effective interest rate uses assumptions on expected life that are based on the historic experience of similar products. These assumptions are monitored to ensure their ongoing appropriateness. Changes in the amortised cost balance arising from actual product life experience differing from the assumed life, are periodically calculated and an adjustment made to the loan balance, with a corresponding adjustment to interest income. Also within the calculations, provision has been made for the uncertainty of the estimates in order to reduce the risk of overstatement of interest income.

Valuation of derivatives and Available-for-sale assets

The fair values of derivative financial instruments and Available-for-sale assets are based on open market prices, where available. If open market prices are not available, the Society uses valuation techniques which comprise discounted cash flow valuation models. The assumptions in these models are periodically reviewed to ensure that they remain relevant.

FSCS levy provision

The Society is committed to paying levy charges of the UK Financial Services Compensation Scheme (FSCS) (see note 14).

All deposit-taking institutions who are members of the FSCS are required to contribute to the administrative and capital costs of the FSCS in safeguarding the deposits of savers in failed financial institutions. The Society is, and continues to be, a member of the FSCS.

Contributions to the FSCS are calculated according to a prescribed formula using the retail savings balances of all deposit-taking institutions that are members of the 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 based on estimations of the repayments by failed institutions and future interest rates.

NOTES TO THE ACCOUNTS
(continued)

3. INTEREST RECEIVABLE AND SIMILAR INCOME

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
On loans fully secured on residential property	635.6	483.8	554.9	448.4
On other loans				
Connected undertakings	–	154.1	–	129.6
Other	5.2	3.8	6.2	4.6
	640.8	641.7	561.1	582.6
Interest and other income on debt securities	59.4	59.4	81.0	81.0
Interest and other income on other liquid assets	4.4	4.4	9.0	9.0
Net expense on hedging instruments	(105.1)	(27.5)	(105.6)	(30.3)
Total	599.5	678.0	545.5	642.3

Included within 'Interest receivable and similar income' is interest accrued on impaired financial assets of Group £8.7 million (2009 - £7.5 million) and Society £6.3 million (2009 - £6.1 million).

The Society believes that interest receivable and similar income comprises revenue for the purposes of IAS 1.

4. INTEREST PAYABLE AND SIMILAR CHARGES

	Group 2010	Society 2010	Group 2009	Society 2009
Bank and customer				
Subordinated liabilities	3.9	3.9	4.0	4.0
Other	21.4	21.4	56.1	56.1
Debt securities in issue	43.8	43.8	2.8	2.8
Other borrowed funds				
On shares held by individuals	423.1	423.1	411.0	411.0
On other shares	0.1	0.1	0.2	0.2
On subscribed capital	12.3	12.3	12.2	12.2
On loans from connected undertakings	–	26.2	–	33.7
Net (income)/expense from hedging instruments	(51.1)	26.5	(65.8)	9.5
Total	453.5	557.3	420.5	529.5

5. FEES AND COMMISSIONS RECEIVABLE

	Group 2010	Society 2010	Group 2009	Society 2009
Mortgage related fees	3.3	2.5	2.9	2.5
General insurance fees	5.8	5.8	5.7	5.6
Other fees and commissions	6.8	6.8	8.8	8.8
Total	15.9	15.1	17.4	16.9

6. FEES AND COMMISSIONS PAYABLE

	Group 2010	Society 2010	Group 2009	Society 2009
Funding related fees	0.6	0.6	0.3	0.3
Other fees and commissions	0.9	0.8	0.8	0.8
Total	1.5	1.4	1.1	1.1

7. OTHER OPERATING INCOME

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Rents receivable	0.4	0.3	0.3	0.3
Other	0.2	0.2	0.4	0.4
Total	0.6	0.5	0.7	0.7

8. NET (LOSSES)/GAINS FROM DERIVATIVE FINANCIAL INSTRUMENTS

Gains less losses on derivatives:				
Derivatives designated as fair value hedges	27.8	27.8	(22.6)	(22.6)
Movement in fair value of hedged items attributable to hedged risk	(29.2)	(29.2)	24.5	24.5
	(1.4)	(1.4)	1.9	1.9
Other derivatives	0.7	0.7	(0.5)	(0.5)
On other assets and liabilities	–	–	(0.1)	(0.1)
Total	(0.7)	(0.7)	1.3	1.3

9. ADMINISTRATIVE EXPENSES

Employee costs				
Wages and salaries	34.7	34.7	31.3	31.3
Social security costs	3.4	3.4	3.0	3.0
Pension costs (note 12)				
Defined benefit plans	1.2	1.2	0.8	0.8
Defined contribution plans	0.7	0.7	0.6	0.6
	40.0	40.0	35.7	35.7
Other expenses				
Finance lease charges	0.4	0.4	0.4	0.4
Other	27.6	25.2	25.5	23.7
Total	68.0	65.6	61.6	59.8

The remuneration of the auditors, Ernst & Young LLP, is set out below.

Audit fees for the statutory audit	0.3	0.3	0.2	0.2
Fees payable for other services:				
Other services in relation to taxation	0.3	0.3	–	–
All other services	0.3	0.3	0.1	0.1
Total	0.9	0.9	0.3	0.3

The Society's policy in relation to the use of its auditors on non-audit engagements sets out the nature of services they are generally precluded from performing. All non-audit engagements provided by the Society's auditors, are subject to pre-approval by either the Audit Committee or the Finance Director, depending upon the nature of the non-audit engagement. Amounts included within other services include additional work in respect of the merger with Stroud & Swindon Building Society.

NOTES TO THE ACCOUNTS
(continued)

10. STAFF NUMBERS

	Group and Society 2010		Group and Society 2009	
	Full-time	**Part-time**	Full-time	Part-time
The average number of persons employed during the year (including executive directors) was:				
Head office and administrative centres	**741**	**262**	641	239
Branches	**341**	**219**	324	203
Total	**1,082**	**481**	965	442

11. DIRECTORS' EMOLUMENTS

	2010	2009
	£000	£000
Directors' emoluments		
For services as directors	**305**	285
For executive services	**1,283**	890
Increase in accrued pension	**13**	–
Total	**1,601**	1,175

The emoluments of the Society's directors are listed below:

Non-executive directors		
David Harding (Chairman)	**77**	75
Bridget Blow (Deputy Chairman, Senior Independent Director and Chair of the Remuneration Committee)	**50**	48
Roger Burnell	**39**	38
Ian Geden	**39**	38
Ian Pickering (Chair of the Audit Committee)	**50**	48
Fiona Smith	**39**	38
Glyn Smith (appointed 22.09.2010)	**11**	–
Total	**305**	285

No pension contributions were made for non-executive directors.

11. DIRECTORS' EMOLUMENTS (continued)

Executive directors	Salary £000	Annual bonus £000	Long Term Incentive Plan £000	Pension contributions £000	Increase in accrued pension £000	Taxable benefits £000	Total £000
2010							
David Stewart	**314**	**35**[1]	**44**[2]	**78**	**1**	**15**	**487**
Colin Franklin	**136**	**15**[1]	**18**[2]	**31**	**12**	**16**	**228**
Rob Green (resigned 14.10.2010)	**204**	**–**	**–**	**19**	**–**	**19**	**242**
John Lowe (appointed 14.10.2010)	**39**	**20**[1]	**–**	**2**	**–**	**3**	**64**
Phil Vaughan	**193**	**21**[1]	**28**[2]	**19**	**–**	**14**	**275**
Total	**886**	**91**	**90**	**149**	**13**	**67**	**1,296**
2009							
David Stewart	294	24[3]	–	76	–	15	409
Colin Franklin (appointed 07.07.2009)	66	11[1]	–	14	–	8	99
Rob Green	199	17[1]	–	19	–	21	256
Phil Vaughan (appointed 07.07.2009)	95	15[1]	–	9	–	7	126
Total	654	67	–	118	–	51	890

1. All eligible Coventry Building Society staff participate in an annual performance related bonus scheme. Eligibility is dependent upon satisfactory individual performance. The executive directors are eligible to receive an annual performance related payment which, in 2010, was calculated by reference to the Society's financial performance. The performance of the Society during 2010 gave rise to a calculated bonus for all 1,501 eligible members of Coventry staff (2009 – 1,350) equivalent to 11% (2009 – 8%) of basic salary. The bonus percentage payable to each of the executive directors of 11% (2009 – 8%) of basic salary was identical to that of all other eligible staff. The annual performance bonus for John Lowe represents the amount payable for the full year. The 2009 annual performance bonus for Colin Franklin and Phil Vaughan represents the amount payable for the full year.
2. Payments made under the Long Term Incentive Plan are in relation to the performance of the three financial years 2008, 2009 and 2010. The Remuneration Committee approved a payment of 15% (2009 – nil) of base salary at 1 January 2008 to participants in the scheme at that date, reflecting the Society's performance over this period.
3. In view of the continuing difficult economic environment and its impact on members, David Stewart elected to waive his bonus payment for 2009 of £24,000 which was awarded and approved by the Remuneration Committee and has been included in the comparatives above.

DEFINED BENEFIT SCHEME[4]

Pension benefits earned by directors	Director's contribution £000	Accrued pension per annum at 31.12.2010 £000	Transfer value of accrued benefits 31.12.2009 £000	Transfer value of accrued benefits 31.12.2010 £000	Difference in transfer value less contributions £000
David Stewart[5]	–	39	567	600	33
Colin Franklin	10	52	814	1,114	290

4. The Chief Executive, the Finance Director and the Chief Operating Officer are all active members of the Society's funded defined contribution pension scheme.
5. The Chief Executive is also a deferred member of the Society's contributory final salary pension scheme. In light of concerns over the cost of providing such final salary benefits, David Stewart voluntarily left the final salary pension scheme in July 2006 on being appointed Chief Executive.

Details of the executive directors' service contracts are contained in section 3 of the Annual Business Statement.

NOTES TO THE ACCOUNTS
(continued)

12. PENSION SCHEME

The Society operates funded defined benefit and funded defined contribution pension schemes for employees and executive directors. The Coventry defined benefit scheme has been closed to new members since December 2001. The defined benefit schemes provide benefits based on final pensionable salary with assets held in separate trustee-administered funds.

The cost of a defined benefit scheme is assessed in accordance with the advice of a qualified actuary on the basis of valuations using the projected unit method. The main assumptions used in the valuations were:

i) an investment return pre-retirement of 1.2% (2009 – 1.0%) per annum in excess of projected salary increases;
ii) for the Coventry Building Society Superannuation Fund an investment return post-retirement of 2.1% (2009 – 2.5%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued prior to 6 April 2006 and 3.1% (2009 – 3.5%) per annum in excess of guaranteed pension increases in respect of pensionable service accrued after 6 April 2006; and
iii) for the Stroud & Swindon Building Society Retirement Benefit Plan, an investment return post-retirement of 2.5% (2009 – n/a) per annum in excess of guaranteed pension increases in respect of pensionable service accrued prior to 6 April 1997, 1.8% (2009 – n/a) per annum in excess of guaranteed pension increases in respect of pensionable service accrued from 6 April 1997 to 31 July 2002, 2.1% (2009 – n/a) per annum in excess of guaranteed pension increases in respect of pensionable service accrued from 1 August 2002 to 5 April 2006 and 3.1% (2009 – n/a) per annum in excess of guaranteed pension increases in respect of pensionable service accrued after 6 April 2006.

The Society contributed 24.5% (2009 – 24.5%) of members' pensionable salaries over the year to 31 December 2010 into the Coventry Building Society Staff Superannuation Fund, and estimates its contribution to the fund in the following twelve months to be £2.1 million (2009 – £2.1 million). The Society contributed 28.9% (2009 – n/a) into the Stroud & Swindon Building Society Retirement Benefit Plan from 1 September 2010 (the effective date of the merger) to 31 December 2010 and estimates its contribution to the plan in the following twelve months to be £0.5 million (2009 – n/a).

	2010	2009
Group and Society	**£m**	£m
The amounts recognised in the balance sheet		
Coventry Building Society Staff Superannuation Fund	**7.2**	6.9
Stroud & Swindon Building Society Retirement Benefit Plan	**(3.1)**	–
Funded status/Defined benefit asset	**4.1**	6.9
Present value of funded obligations	**(133.8)**	(89.0)
Fair value of plan assets	**137.9**	95.9
Funded status/Defined benefit asset	**4.1**	6.9
The amounts recognised in the income statement		
Current service cost	**1.8**	1.5
Interest cost on benefit obligations	**5.9**	4.3
Expected return on plan assets	**(6.5)**	(5.0)
Total (charged within administrative expenses)	**1.2**	0.8
Actual return on plan assets	**11.4**	14.5
Changes in the present value of the defined benefit obligations		
Defined benefit obligation at 1 January	**89.0**	71.5
Acquired on transfer of engagements	**38.9**	–
Current service cost	**1.8**	1.5
Interest cost	**5.9**	4.3
Employee contributions	**0.7**	0.7
Actuarial (gains)/losses	**(0.2)**	12.8
Benefits paid	**(2.3)**	(1.8)
Defined benefit obligation at 31 December	**133.8**	89.0

12. PENSION SCHEME (continued)

	2010	2009
Group and Society	**£m**	£m
Changes in the fair value of plan assets		
Fair value of plan assets at 1 January	**95.9**	80.4
Acquired on transfer of engagements	**30.1**	–
Expected return on plan assets	**6.5**	5.0
Actuarial gains	**4.8**	9.5
Contributions by employer	**2.2**	2.1
Employee contributions	**0.7**	0.7
Benefits paid	**(2.3)**	(1.8)
Fair value of plan assets at 31 December	**137.9**	95.9
The amount recognised in the statement of other comprehensive income		
Actuarial gain/(loss)	**5.0**	(3.3)
Tax (charge)/credit on actuarial loss at 27% (2009 – 28%)	**(1.4)**	0.9
Actuarial gain/(loss) net of tax	**3.6**	(2.4)

The major categories of plan assets as a percentage of the fair value of total plan assets, and their expected rates of return are:

	Expected return at balance sheet date	**Plan assets at 31.12.2010**	Expected return at balance sheet date	Plan assets at 31.12.2009
	%	**%**	%	%
Equities	**8.2**	**25**	8.0	33
Corporate bonds	**5.5**	**20**	5.7	25
Government bonds	**4.2**	**21**	4.5	13
Alternatives	**5.7**	**34**	6.5	29
		100		100

At 31 December 2010, the Stroud & Swindon Building Society Retirement Benefits Plan held assets totalling £0.5 million which were invested in Coventry Building Society Permanent Interest Bearing Shares (PIBS) (2009 – £nil).

To develop the expected long term rate of return on assets assumption, the Society considered the current level of expected returns on risk free investments (primarily Government bonds), the historical level of the risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each asset class. The expected return for each asset class, as shown above, was then weighted based on the asset allocation to develop the expected long term rate of return on assets assumption for the portfolio and then a deduction of 0.14% (2009 – 0.14%) made for expenses. This resulted in the selection of 5.8% (2009 – 6.2%).

12. PENSION SCHEME (continued)

The principal actuarial assumptions used are as follows:

Weighted average assumptions used to determine benefit obligations at	**31.12.2010**	31.12.2009
	%	%
Discount rate	**5.5**	5.8
Rate of pensionable salary increase	**4.3**	4.8
Weighted average assumptions used to determine net pension cost		
Discount rate	**5.5**	6.1
Expected long term return on fund assets	**6.2**	6.2
Rate of pensionable salary increase	**4.6**	4.3
Rates of inflation	**3.2**	2.8

Weighted average life expectancy for mortality tables used to determine benefit obligations at

	31.12.2010		31.12.2009	
	Male	**Female**	Male	Female
Member age 60 (current life expectancy)	**26.1**	**28.8**	25.4	28.0
Member age 45 (life expectancy at age 60)	**28.2**	**30.8**	26.8	29.1

The assumptions on mortality are determined by the actuarial tables known as S1PXA (YOB) medium cohort 1% underpin for current and future pensioners (2009 – S1PXA (YOB) medium cohort for current and future pensioners).

	Financial year ending				
Fund history	**2010**	2009	2008	2007	2006
Fair value of fund assets at end of year (£m)	**137.9**	95.9	80.4	94.1	88.7
Benefit obligation at end of year (£m)	**133.8**	89.0	71.5	82.5	87.8
Surplus (£m)	**4.1**	6.9	8.9	11.6	0.9
Difference between expected and actual return on fund assets					
Amount (£m)	**4.9**	9.5	(20.8)	(1.2)	0.6
Percentage of fund assets (%)	**3.6**	9.9	(25.9)	(1.3)	0.7
Actuarial (gains)/losses on fund liabilities					
Amount (£m)	**(0.2)**	12.8	(16.4)	(11.1)	0.3
Percentage of fund liabilities (%)	**(0.1)**	14.4	(22.9)	(13.5)	0.3

13. IMPAIRMENT PROVISIONS ON LOANS AND ADVANCES TO CUSTOMERS

	Loans fully secured on residential property	Other loans	Total
Group	£m	£m	£m
At 1 January 2010			
Individual impairment	15.3	2.5	17.8
Collective impairment	5.3	0.3	5.6
	20.6	2.8	23.4
Charge for the year			
Individual impairment	7.7	3.5	11.2
Collective impairment	0.1	0.5	0.6
	7.8	4.0	11.8
Amounts written off individual impairment	(8.7)	(5.4)	(14.1)
At 31 December 2010			
Individual impairment	14.3	0.6	14.9
Collective impairment	5.4	0.8	6.2
Total	19.7	1.4	21.1
Society			
At 1 January 2010			
Individual impairment	11.7	2.2	13.9
Collective impairment	3.6	0.3	3.9
	15.3	2.5	17.8
Charge for the year			
Individual impairment	5.5	2.8	8.3
Collective impairment	0.3	0.3	0.6
	5.8	3.1	8.9
Amounts written off individual impairment	(6.7)	(4.5)	(11.2)
At 31 December 2010			
Individual impairment	10.5	0.5	11.0
Collective impairment	3.9	0.6	4.5
Total	14.4	1.1	15.5

13. IMPAIRMENT PROVISIONS ON LOANS AND ADVANCES TO CUSTOMERS (continued)

	Loans fully secured on residential property	Other loans	Total
Group	£m	£m	£m
At 1 January 2009			
Individual impairment	11.5	3.9	15.4
Collective impairment	4.7	0.8	5.5
	16.2	4.7	20.9
Charge for the year			
Individual impairment	15.8	4.0	19.8
Collective impairment	0.6	(0.5)	0.1
	16.4	3.5	19.9
Amounts written off individual impairment	(12.0)	(5.4)	(17.4)
At 31 December 2009			
Individual impairment	15.3	2.5	17.8
Collective impairment	5.3	0.3	5.6
Total	20.6	2.8	23.4
Society			
At 1 January 2009			
Individual impairment	9.8	3.5	13.3
Collective impairment	4.3	0.7	5.0
	14.1	4.2	18.3
Charge for the year			
Individual impairment	12.1	3.3	15.4
Collective impairment	(0.7)	(0.4)	(1.1)
	11.4	2.9	14.3
Amounts written off individual impairment	(10.2)	(4.6)	(14.8)
At 31 December 2009			
Individual impairment	11.7	2.2	13.9
Collective impairment	3.6	0.3	3.9
Total	15.3	2.5	17.8

The provisions above have been deducted from the appropriate asset values in the balance sheet.

14. PROVISION FOR FSCS LEVIES

All deposit-taking institutions that are members of the UK Financial Services Compensation Scheme (FSCS) are required to contribute to the costs of the FSCS in safeguarding the deposits of savers in failed financial institutions. The Society is, and continues to be, a member of the FSCS.

Contributions to the FSCS are calculated according to a prescribed formula using the retail savings balances of all deposit-taking institutions who are members of the FSCS.

FSCS rules require the Society to provide for £5.6 million in its 2010 accounts with respect to the estimated levies for the period 2011/12 and revisions for the levy estimate for the period 2010/11 previously provided in its 2009 accounts (2009 – £2.0 million for the period 2010/11 and revisions for the period 2009/10).

These costs are 'exceptional' because they are outside of the Society's control and are dependent upon the extent of failures of other deposit-taking institutions who are members of the FSCS.

15. PROVISION FOR IMPAIRMENT OF DEBT SECURITIES

The Society has recovered a further £2.1 million (2009 – £1.5 million) from the administrators of Kaupthing, Singer & Friedlander.

16. CHARITABLE DONATION TO POPPY APPEAL

During 2010 the Society again partnered with The Royal British Legion to raise funds for the annual Poppy Appeal. The Society has provided for a donation of £1.7 million (2009 – £1.3 million) to the Poppy Appeal in addition to paying a fixed rate of interest to members on a related savings bond and variable rate on a related savings account.

17. TAXATION

	Group 2010	**Society 2010**	Group 2009	Society 2009
	£m	**£m**	£m	£m
Current tax				
UK corporation tax at 28%	**15.6**	**10.4**	15.3	13.8
UK corporation tax – adjustment in respect of prior years	**(0.6)**	**(0.6)**	(4.9)	(4.4)
Total current tax	**15.0**	**9.8**	10.4	9.4
Deferred tax				
Current year	**0.3**	**(0.2)**	0.6	0.6
Adjustment in respect of prior years	**0.4**	**0.4**	1.7	1.7
Total deferred tax	**0.7**	**0.2**	2.3	2.3
Total	**15.7**	**10.0**	12.7	11.7

The effective tax rate for the year is 15.6% for the Group and 9.4% for the Society (2009 – 22.6% for the Group and 23.0% for the Society). Further information relating to deferred tax is presented in note 27.

NOTES TO THE ACCOUNTS
(continued)

17. TAXATION (continued)

The tax on items reported through other comprehensive income is as follows:

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Statement of other comprehensive income				
Tax charge/(credit) on actuarial gain/(loss) on defined benefit pension plan	1.4	1.4	(0.9)	(0.9)
Tax on fair value movements taken to reserves	5.3	5.3	(3.1)	(3.1)
Total	6.7	6.7	(4.0)	(4.0)

The actual tax charge for the period differs from the UK standard corporation tax rate of 28%. The differences are explained below:

	Group 2010	Society 2010	Group 2009	Society 2009
Profit before tax (PBT)	100.6	106.7	56.2	50.9
Tax at UK standard rate of corporation tax on PBT of 28%	28.2	29.9	15.7	14.2
Adjustments in respect of prior years	(0.2)	(0.2)	(3.2)	(2.7)
Gain on business combination	(12.3)	(19.8)	–	–
Effect of rate change	(0.1)	(0.1)	–	–
Expenses not deductible for tax purposes	0.1	0.2	0.2	0.2
Total	15.7	10.0	12.7	11.7

Following the emergency budget on 2 June 2010, a reduction in the corporation income tax rate was announced from 28% to 24% to be phased in over four years. For the 2010 accounts all deferred tax balances have been restated to a rate of 27%. It has been estimated that a further 3% reduction in the corporation tax rate will reduce net deferred tax by £0.6 million over the next three years. The adjustment will be recognised through both income and reserves.

18. CASH IN HAND AND BALANCES WITH THE BANK OF ENGLAND

	Group 2010	Society 2010	Group 2009	Society 2009
Cash in hand and balances with the Bank of England other than mandatory reserve deposits	1,427.9	1,427.5	287.6	285.4
Mandatory reserve with the Bank of England	16.3	16.3	14.6	14.6
Total	1,444.2	1,443.8	302.2	300.0

The mandatory reserve deposits with the Bank of England of £16.3 million (2009 – £14.6 million) are not available for use in the Society's day-to-day operations. All other balances with the Bank of England are not mandatory and are readily accessible.

19. LOANS AND ADVANCES TO CREDIT INSTITUTIONS

Loans and advances to credit institutions have remaining maturities as follows:

	Group 2010	Society 2010	Group 2009	Society 2009
Accrued interest	1.0	1.0	0.8	0.8
Repayable on demand	70.6	70.6	40.5	40.5
Other loans and advances by residual maturity repayable				
In not more than three months	106.0	106.0	128.1	128.1
In more than three months but not more than one year	15.8	15.8	83.5	83.5
In more than one year but not more than five years	-	-	72.3	72.3
Total	193.4	193.4	325.2	325.2

20. DEBT SECURITIES

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	**£m**	£m	£m
Available-for-sale:				
Government investment securities	**1,019.4**	**1,019.4**	778.4	778.4
Analysis of transferable debt securities				
Listed	**1,165.2**	**1,165.2**	1,486.0	1,486.0
Unlisted	**679.4**	**679.4**	1,273.6	1,273.6
Total	**2,864.0**	**2,864.0**	3,538.0	3,538.0
Debt securities have remaining maturities as follows:				
In not more than one year	**905.3**	**905.3**	1,669.8	1,669.8
In more than one year	**1,958.7**	**1,958.7**	1,868.2	1,868.2
Total	**2,864.0**	**2,864.0**	3,538.0	3,538.0
Movements during the year of transferable securities are analysed below:				
At 1 January	**3,538.0**	**3,538.0**	3,155.8	3,155.8
Acquired on transfer of engagements	**398.9**	**398.9**	–	–
Additions	**5,687.0**	**5,687.0**	12,479.9	12,479.9
Maturities and disposals	**(6,796.2)**	**(6,796.2)**	(12,084.0)	(12,084.0)
Gains/(losses) from changes in fair value	**36.3**	**36.3**	(13.7)	(13.7)
At 31 December	**2,864.0**	**2,864.0**	3,538.0	3,538.0

21. DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS

	2010 Contract/ notional amount	2010 Fair value assets	2010 Fair value liabilities	2009 Contract/ notional amount	2009 Fair value assets	2009 Fair value liabilities
Group and Society	**£m**	**£m**	**£m**	£m	£m	£m
Derivatives designated as fair value hedges						
Interest rate caps	**343.0**	**0.1**	**–**	392.0	3.8	–
Interest rate swaps	**9,857.9**	**71.2**	**138.3**	7,498.2	24.0	107.9
Other derivatives						
Interest rate floors	**40.0**	**1.1**	**–**	–	–	–
Currency swaps	**164.2**	**1.0**	**1.1**	665.8	1.5	–
Interest rate basis swaps	**–**	**–**	**–**	300.0	–	1.0
Total derivatives	**10,405.1**	**73.4**	**139.4**	8,856.0	29.3	108.9

Contract/notional amount indicates the amount outstanding at the balance sheet date and does not represent amounts at risk.

All derivative counterparties are rated A1 or better.

Group and Society

	2010 Contract/ notional amount	2010 Fair value assets	2010 Fair value liabilities	2009 Contract/ notional amount	2009 Fair value assets	2009 Fair value liabilities
Derivatives have remaining maturities as follows:						
In not more than one year	**3,717.9**	**13.9**	**20.3**	3,407.2	9.9	31.3
In more than one year	**6,687.2**	**59.5**	**119.1**	5,448.8	19.4	77.6
Total derivatives	**10,405.1**	**73.4**	**139.4**	8,856.0	29.3	108.9

HEDGING ACTIVITIES

Fair value hedges
At 31 December 2010 the Society held the following interest rate derivative contracts which qualify for hedge accounting:

- Interest rate swap agreements under which the Society pays a fixed rate of interest and receives interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate mortgage assets as a result of changes in market interest rates. These swaps have a nominal principal amount of £3,531.9 million (2009 – £3,612.4 million) and a net negative fair value of £80.1 million (2009 – net negative £88.6 million).

- Interest rate swap agreements under which the Society receives a fixed rate of interest and pays interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of the fixed rate shares liabilities as a result of changes in market interest rates. These swaps have a nominal principal amount of £4,180.0 million (2009 – £2,200.0 million) and a net positive fair value of £12.0 million (2009 – net positive £1.7 million).

- Interest rate swap agreements under which the Society pays a fixed rate of interest and receives interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate gilts or Government guaranteed bonds purchased in the wholesale market as a result of changes in market interest rates. These swaps have a nominal principal amount of £737.0 million (2009 – £582.0 million) and a net negative fair value of £30.0 million (2009 – net negative £5.6 million).

- Interest rate swap agreements under which the Society receives a fixed rate of interest and pays interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of fixed rate bonds or liabilities issued in the wholesale market as a result of changes in market interest rates. These swaps have a nominal principal amount of £1,409.0 million (2009 – £1,103.8 million) and a net positive fair value of £31.0 million (2009 – net positive £8.6 million).

21. DERIVATIVES AND OTHER FINANCIAL INSTRUMENTS (continued)

Fair value hedges (continued)

- Interest rate cap agreements under which the Society pays an initial premium and is subsequently compensated to the extent that LIBOR exceeds the cap strike rate. These caps are used to hedge changes in the fair value of exposure to the risk that market rates exceed the cap on capped rate mortgage assets. These caps have a nominal principal amount of £343.0 million (2009 – £392.0 million) and a net positive fair value of £0.1 million (2009 – £3.8 million).

- The derivative gains and losses for the year in respect of fair value hedges comprise gains on derivatives of £27.8 million (2009 - losses of £22.6 million) and associated losses on hedged items of £29.2 million (2009 – gains of £24.5 million).

Hedges not qualifying for hedge accounting

Interest rate floor agreements under which the Society pays an initial premium and is subsequently compensated to the extent that LIBOR falls below the floor strike rate. These floors are used to hedge the risk of long-term low rates of interest. These floors have a nominal principal amount of £40.0 million (2009 – £nil) and a net positive fair value of £1.1 million (2009 – £nil).

Cross currency swaps under which the Society receives interest at EURIBOR and pays interest based on LIBOR. These swaps are used to hedge the exposure to changes in the fair value of Euro denominated bonds issued in the wholesale market as a result of changes in market interest rates and exchange rates. These cross currency swaps have a nominal principal amount of £82.0 million (2009 – £665.8 million) and a net positive fair value of £1.0 million (2009 – net positive £1.5 million).

Foreign exchange swaps under which the Society has sold Euros for Pounds Sterling at the exchange rate current to the deal and has agreed that at a future date it will sell at an agreed exchange rate Pounds Sterling for the same value of Euros that was originally exchanged. The swaps are used to hedge the exposure to changes in the values of future cash flows on Euro denominated bonds issued in the wholesale market as a result of changes in exchange rates. These foreign exchange swaps have a nominal principal amount of £82.2 million (2009 – £nil) and a net negative fair value of £1.1 million (2009 – £nil).

The derivative gains and losses for the year in respect of hedges that do not qualify for hedge accounting comprise gains on derivatives of £0.7 million (2009 – losses of £0.5 million).

22. LOANS AND ADVANCES TO CUSTOMERS

	Group 2010	**Society 2010**	Group 2009	Society 2009
	£m	**£m**	£m	£m
Loans fully secured on residential property	**17,485.7**	**13,470.2**	13,991.2	11,337.3
Other loans				
Loans fully secured on land	**14.5**	**2.0**	0.1	0.1
Other loans	**73.5**	**51.5**	83.4	59.8
	88.0	**53.5**	83.5	59.9
Total	**17,573.7**	**13,523.7**	14,074.7	11,397.2

Other loans incorporate £1.0 million (2009 – £1.3 million) of loans that are fully secured on residential property and that were made to corporate bodies such as Housing Associations prior to 1 July 1998, the date upon which the Society adopted the powers of the Building Societies Act 1997. Although the classification of these assets is not consistent with similar loans made after 1 July 1998 that are included in 'loans fully secured on residential property', this treatment has been adopted in order to comply with the requirements of the Building Societies Act 1997.

22. LOANS AND ADVANCES TO CUSTOMERS (continued)

Maturity analysis
The remaining maturity of loans and advances to customers at the balance sheet date is as follows:

		Group 2010	Society 2010	Group 2009	Society 2009
		£m	£m	£m	£m
In not more than one year		111.9	91.5	56.5	50.9
In more than one year		17,482.9	13,447.7	14,041.6	11,364.1
		17,594.8	13,539.2	14,098.1	11,415.0
Impairment	(note 13)	(21.1)	(15.5)	(23.4)	(17.8)
Total		17,573.7	13,523.7	14,074.7	11,397.2

The maturity analysis is based on contractual maturity not actual redemption levels experienced by the Group or Society.

Covered bonds
On 21 April 2008, the Bank of England launched its Special Liquidity Scheme (SLS) which allows financial institutions to swap their high quality mortgage-backed and other securities for UK Treasury Bills for a defined period. In common with many banks and building societies, the Society has used this facility as an efficient way of maintaining a high level of liquidity.

In 2008, the Society accessed the SLS by issuing a covered bond and swapping this with the Bank of England for UK Treasury Bills. To establish this structure the Society created a new entity, Coventry Building Society Covered Bonds LLP, which is consolidated by the Group. The SLS scheme will end on 31 January 2012.

Loans and advances to customers include £3,051.7 million (2009 – £2,602.6 million) for both the Group and Society which have been transferred from the Society to Coventry Building Society Covered Bonds LLP. The loans secure £2,000.0 million (2009 – £2,000.0 million) of covered bonds issued by the Society. The loans are retained on the Society's balance sheet as the Society retains substantially all the risks and rewards relating to the loans.

23. INVESTMENTS IN SUBSIDIARY UNDERTAKINGS

	Shares	Loans	Total 2010
Society	£m	£m	£m
Cost and net book value			
At 1 January	–	5,313.5	5,313.5
Acquired on transfer of engagements	13.2	575.0	588.2
Additions	–	1,315.6	1,315.6
At 31 December	13.2	7,204.1	7,217.3

23. INVESTMENTS IN SUBSIDIARY UNDERTAKINGS (continued)

The Society has the following subsidiary undertakings all of which are consolidated:

Subsidiary undertakings	Principal activity
Godiva Mortgages Limited	Mortgage lending
ITL Mortgages Limited	Mortgage lending and mortgage acquisition vehicle
Stroud and Swindon Funding Company	Funding company for mortgage acquisitions
Stroud and Swindon Funding Company (No.2) Limited	Funding company for mortgage acquisitions
Five Valleys Property Company Limited	Investment properties holding company
Coventry Financial Services Limited	Non-trading
Coventry Property Services Limited	Non-trading
Godiva Financial Services Limited	Non-trading
Godiva Housing Developments Limited	Non-trading
Godiva Savings Limited	Non-trading
Godiva Securities and Investments Limited	Non-trading
Coventry Building Society Covered Bonds LLP	Intra-group mortgage acquisition and guarantor of covered bonds

All of the above subsidiaries are 100% directly or indirectly owned by Coventry Building Society. The subsidiaries are wholly owned subsidiaries incorporated in England and Wales and operate in the UK. All of the subsidiaries have an accounting reference date of 31 December and are included in the Group's consolidated Financial Statements.

24. INTANGIBLE ASSETS

	Software expenditure 2010	**Other intangible assets 2010**	**Total 2010**	Software expenditure 2009	Other intangible assets 2009	Total 2009
Group	**£m**	**£m**	**£m**	£m	£m	£m
Cost						
At 1 January	**11.4**	**–**	**11.4**	10.2	–	10.2
Additions	**3.1**	**–**	**3.1**	4.4	–	4.4
Acquired on transfer of engagement	**–**	**3.0**	**3.0**	–	–	-
Disposals	**(1.1)**	**–**	**(1.1)**	(3.2)	–	(3.2)
At 31 December	**13.4**	**3.0**	**16.4**	11.4	–	11.4
Amortisation						
At 1 January	**1.5**	**–**	**1.5**	1.7	–	1.7
Charge for the year[1]	**3.0**	**0.7**	**3.7**	2.7	–	2.7
Disposals	**(1.0)**	**–**	**(1.0)**	(2.9)	–	(2.9)
At 31 December	**3.5**	**0.7**	**4.2**	1.5	–	1.5
Net book value at 31 December	**9.9**	**2.3**	**12.2**	9.9	–	9.9

[1] The amortisation charge of other intangible assets has been included within Stroud & Swindon integration and merger related costs within the income statement.

Other intangible assets are in respect of retail deposits and customer relationships arising on the merger with Stroud & Swindon Building Society.

NOTES TO THE ACCOUNTS
(continued)

24. INTANGIBLE ASSETS (continued)

Society	Software expenditure 2010 £m	Other intangible assets 2010 £m	Total 2010 £m	Software expenditure 2009 £m	Other intangible assets 2009 £m	Total 2009 £m
Cost						
At 1 January	10.9	–	10.9	9.7	–	9.7
Additions	3.1	–	3.1	4.4	–	4.4
Acquired on transfer of engagement	–	3.0	3.0	–	–	–
Disposals	(1.1)	–	(1.1)	(3.2)	–	(3.2)
At 31 December	12.9	3.0	15.9	10.9	–	10.9
Amortisation						
At 1 January	1.0	–	1.0	1.2	–	1.2
Charge for the year[1]	3.0	0.7	3.7	2.7	–	2.7
Disposals	(1.0)	–	(1.0)	(2.9)	–	(2.9)
At 31 December	3.0	0.7	3.7	1.0	–	1.0
Net book value at 31 December	9.9	2.3	12.2	9.9	–	9.9

25. PROPERTY, PLANT AND EQUIPMENT

		Land and buildings			
	Freehold	Long leasehold	Short leasehold	Equipment, fixtures, fittings & vehicles	Total
Group and Society	£m	£m	£m	£m	£m
Cost					
At 1 January 2010[1]	6.4	3.5	3.2	40.1	53.2
Acquired on transfer of engagements	1.5	0.4	–	–	1.9
Additions	–	–	–	5.6	5.6
Disposals	–	–	–	(2.7)	(2.7)
At 31 December 2010	7.9	3.9	3.2	43.0	58.0
Depreciation					
At 1 January 2010[1]	1.0	0.3	2.0	25.0	28.3
Charge for the year	0.1	0.1	0.1	4.0	4.3
Depreciation on disposals	–	–	–	(2.7)	(2.7)
At 31 December 2010	1.1	0.4	2.1	26.3	29.9
Net book value at 31 December 2010	6.8	3.5	1.1	16.7	28.1

25. PROPERTY, PLANT AND EQUIPMENT (continued)

	Land and buildings			Equipment, fixtures, fittings & vehicles	
	Freehold	Long leasehold	Short leasehold		Total
Group and Society	£m	£m	£m	£m	£m
Cost					
At 1 January 2009[1]	6.4	3.5	3.2	39.1	52.2
Additions	–	–	–	3.4	3.4
Disposals	–	–	–	(2.4)	(2.4)
At 31 December 2009	6.4	3.5	3.2	40.1	53.2
Depreciation					
At 1 January 2009[1]	0.9	0.2	2.0	23.5	26.6
Charge for the year	0.1	0.1	-	3.8	4.0
Depreciation on disposals	-	-	-	(2.3)	(2.3)
At 31 December 2009	1.0	0.3	2.0	25.0	28.3
Net book value at 31 December 2009	5.4	3.2	1.2	15.1	24.9

[1] Freehold property has been restated and now excludes freehold property held for investment purposes. See note 26 for details on the freehold properties held for investment purposes.

Equipment, fixtures, fittings and vehicles includes assets held under finance leases as follows:

	2010	2009
Group and Society	**£m**	£m
Net book value	**1.1**	0.9
Accumulated depreciation	**0.7**	0.6

The net book value of land and buildings occupied by the Society for its own activities is as follows:

Group and Society		
At 31 December	**10.5**	9.6

26. INVESTMENT PROPERTIES

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Cost				
At 1 January	0.7	0.7	0.7	0.7
Acquired on transfer of engagements	5.2	–	–	–
At 31 December	5.9	0.7	0.7	0.7
Amortisation				
At 1 January	0.1	0.1	0.1	0.1
Charge for the year	–	–	–	–
At 31 December	0.1	0.1	0.1	0.1
Net book value at 31 December	5.8	0.6	0.6	0.6
Fair value at 31 December	6.5	1.3	1.3	1.3

Investment properties generally include residential properties and offices ancillary to branch premises which are not occupied by the Group.

Depreciation is provided by the Group to write off the cost less the estimated residual value of investment properties (excluding land) by equal instalments over their useful economic life of 50 years. Land is not depreciated. Any impairment in the value of properties is dealt with through the income statement as it arises.

The investment properties were valued by qualified independent chartered surveyors, who are members of the Royal Institute of Chartered Surveyors (RICS). The properties were valued on the basis of market value, and the valuation was carried out in accordance with the RICS Appraisal and Valuation Standards. As the investment properties are held at depreciated historical cost, this valuation has not been reflected in the carrying value of the assets.

27. DEFERRED TAX

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

	Group 2010	Society 2010	Group 2009	Society 2009
Deferred tax assets				
Mortgage book impairment and other provisions	0.3	0.3	0.4	0.4
Pension scheme benefit from special contribution	0.1	0.1	–	–
IFRS transitional fair value adjustments	1.3	1.3	1.6	1.6
Excess of depreciation over capital allowances	0.1	0.1	0.1	–
Defined benefit pension plan deficit	0.8	0.8	–	–
Transfer of engagements – fair value adjustments	16.8	5.6	–	–
Total	19.4	8.2	2.1	2.0
Deferred tax liabilities				
Excess of capital allowances over depreciation	1.0	1.0	1.0	1.0
IFRS transitional fair value adjustments	2.0	2.0	2.4	2.4
Defined benefit pension plan surplus	2.0	2.0	1.9	1.9
Transfer of engagements – fair value adjustments	0.6	0.6	–	–
Total	5.6	5.6	5.3	5.3

28. NON-CURRENT ASSETS HELD FOR SALE

Assets held for sale consist of freehold properties which were acquired as a result of the merger with Stroud & Swindon Building Society. The properties are expected to be sold in the financial year beginning 1 January 2011.

29. SHARES

	Group 2010	**Society 2010**	Group 2009	Society 2009
	£m	**£m**	£m	£m
Held by individuals	**17,626.5**	**17,626.5**	13,210.3	13,210.3
Other shares	**7.8**	**7.8**	7.9	7.9
Hedge accounting adjustment	**3.3**	**3.3**	0.6	0.6
Total	**17,637.6**	**17,637.6**	13,218.8	13,218.8

Shares are repayable from the balance sheet date in the ordinary course of business as follows:

Accrued interest	**167.6**	**167.6**	111.3	111.3
Repayable on demand	**13,843.3**	**13,843.3**	12,724.1	12,724.1
Shares with residual maturity repayable:				
In more than three months but not more than one year	**865.0**	**865.0**	–	–
In more than one year but not more than five years	**2,761.7**	**2,761.7**	383.4	383.4
Total	**17,637.6**	**17,637.6**	13,218.8	13,218.8

30. DEPOSITS FROM BANKS

Deposits from banks are repayable from the balance sheet date in the ordinary course of business as follows:

Accrued interest	**0.7**	**0.7**	0.7	0.7
Repayable on demand	**8.6**	**8.6**	38.1	38.1
Other amounts owed to banks with residual maturity repayable:				
In not more than three months	**1,306.1**	**1,306.1**	969.6	969.6
In more than three months but not more than one year	**–**	**–**	–	–
In more than one year but not more than five years	**–**	**–**	361.9	361.9
Total	**1,315.4**	**1,315.4**	1,370.3	1,370.3

Deposits from banks include £1,294 million (2009 – £1,327 million) in respect of sale and repurchase agreements.

NOTES TO THE ACCOUNTS
(continued)

31. OTHER DEPOSITS

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Other deposits are repayable from the balance sheet date in the ordinary course of business as follows:				
Accrued interest	0.1	0.1	–	–
Repayable on demand	–	–	–	–
Other amounts owed to depositors with residual maturity repayable:				
In not more than three months	25.0	25.0	–	–
In more than three months but not more than one year	9.0	9.0	18.0	18.0
Total	34.1	34.1	18.0	18.0

32. AMOUNTS OWED TO OTHER CUSTOMERS

Amounts owed to other customers are repayable from the balance sheet date in the ordinary course of business as follows:

	Group 2010	Society 2010	Group 2009	Society 2009
Accrued interest	2.8	2.8	5.5	5.5
Repayable on demand	40.8	40.8	58.3	58.3
Other amounts due to customers with residual maturity repayable:				
In not more than three months	428.2	428.2	577.6	577.6
In more than three months but not more than one year	159.1	159.1	186.2	186.2
In more than one year but not more than five years	14.3	14.3	28.6	28.6
Total	645.2	645.2	856.2	856.2

33. DEBT SECURITIES IN ISSUE

	Group 2010	Society 2010	Group 2009	Society 2009
Certificates of deposit	134.2	134.2	101.2	101.2
Fixed rate notes	1,262.1	1,262.1	1,009.3	1,009.3
Floating rate notes	137.0	137.0	854.6	854.6
	1,533.3	1,533.3	1,965.1	1,965.1
Hedge accounting adjustment	18.0	18.0	4.7	4.7
Total	1,551.3	1,551.3	1,969.8	1,969.8

Debt securities in issue are repayable from the balance sheet date in the ordinary course of business as follows:

	Group 2010	Society 2010	Group 2009	Society 2009
Accrued interest	12.4	12.4	2.3	2.3
Other debt securities in issue with residual maturity repayable:				
In not more than one year	178.9	178.9	972.9	972.9
In more than one year	1,342.0	1,342.0	989.9	989.9
	1,533.3	1,533.3	1,965.1	1,965.1
Hedge accounting adjustment	18.0	18.0	4.7	4.7
Total	1,551.3	1,551.3	1,969.8	1,969.8

34. OTHER LIABILITIES

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Other liabilities falling due within one year are as follows:				
Amounts due to connected undertakings	–	3,150.9	–	2,642.3
Tax deducted at source from interest paid	11.2	11.2	14.5	14.5
Other taxation and social security	1.8	1.8	1.3	1.3
Finance leases	0.6	0.6	0.6	0.6
Other creditors	2.5	2.5	2.5	2.6
	16.1	3,167.0	18.9	2,661.3
Other liabilities falling due after more than one year but in less than five years:				
Finance leases	0.5	0.5	0.4	0.4
Total	16.6	3,167.5	19.3	2,661.7

35. PROVISIONS FOR LIABILITIES AND CHARGES

	FSCS 2010	Other provisions 2010	Total 2010	FSCS 2009	Other provisions 2009	Total 2009
Group and Society	£m	£m	£m	£m	£m	£m
At 1 January	8.8	1.3	10.1	11.4	4.3	15.7
Acquired on transfer of engagement	0.8	–	0.8	–	–	–
Charge/(release) for the year	5.6	4.2	9.8	2.0	(2.9)	(0.9)
Provisions utilised	(4.7)	(0.1)	(4.8)	(4.6)	(0.1)	(4.7)
At 31 December	10.5	5.4	15.9	8.8	1.3	10.1

Details of the FSCS charge are detailed in note 14.

Other provisions include the restructuring provision relating to the merger with Stroud & Swindon Building Society. Other provisions have also been recognised in respect of circumstances that may give rise to various customer claims. It is expected that the liability will mainly crystallise over the next five years.

The Society has no contingent liabilities to report.

NOTES TO THE ACCOUNTS
(continued)

36. SUBORDINATED LIABILITIES

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	**£m**	£m	£m
Subordinated liabilities owed to note holders are as follows:				
Fixed rate subordinated notes 2015 – 5.875%	**–**	**–**	30.0	30.0
Fixed rate subordinated notes 2015 – 5.25%	**–**	**–**	25.2	25.2
Fixed rate subordinated notes 2016 – 12.25%	**7.0**	**7.0**	–	–
Fixed rate subordinated notes 2017 – 8.37%	**10.0**	**10.0**	–	–
Fixed rate subordinated notes 2021 – 6.12%	**10.1**	**10.1**	–	–
Fixed rate subordinated notes 2022 – 6.469%	**15.5**	**15.5**	15.5	15.5
Fixed rate subordinated notes 2026 – 6.33%	**10.2**	**10.2**	–	–
Fixed rate subordinated notes 2032 – 7.54%	**15.4**	**15.4**	–	–
Total	**68.2**	**68.2**	70.7	70.7

All the subordinated liabilities are denominated in sterling. The notes are repayable at the dates stated, or earlier in accordance with their terms at the option of the Society, with the prior consent of FSA.

During the year ended 31 December 2010 the Society, with the consent of the FSA, redeemed early £25.0 million of the 5.25% subordinated loan due on 8 November 2015 and £30.0 million of the 5.875% subordinated loan due on 16 December 2015. The Society acquired subordinated liabilities maturing in 2016, 2017, 2021, 2026 and 2032 as a result of the merger with Stroud & Swindon Building Society.

The rights of repayment of the holders of the notes are subordinated to the claims of all depositors, creditors and shareholders in the Society, as regards the principal of the notes and accrued interest.

37. SUBSCRIBED CAPITAL

Subscribed capital owed to permanent interest holding members is as follows:

Permanent interest bearing shares	**161.3**	**161.3**	161.2	161.2

Interest is paid in arrears on £40 million permanent interest bearing shares at the rate of 12 1/8% p.a. in half-yearly instalments, and on £120 million permanent interest bearing shares at the rate of 6.092% p.a. in half-yearly instalments. The shares are repayable only in the event of a winding up of the Society or otherwise with the consent of FSA. In a winding up or dissolution of the Society the claims of the holders of permanent interest bearing shares would rank behind all other creditors of the Society and the claims of members holding shares as to principal and interest. The holders of permanent interest bearing shares are not entitled to any share in any final surplus upon a winding up or final dissolution of the Society.

38. GENERAL RESERVE

Movements in general reserves were as follows:

As at 1 January	**616.0**	**609.5**	574.9	572.7
Actuarial gain/(loss) on defined benefit pension plans (net of tax at 27%) (2009 – 28%)	**3.6**	**3.6**	(2.4)	(2.4)
Net profit for the financial year	**84.9**	**96.7**	43.5	39.2
As at 31 December	**704.5**	**709.8**	616.0	609.5

39. AVAILABLE-FOR-SALE RESERVE

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Movements in Available-for-sale reserves were as follows:				
As at 1 January	(31.8)	(31.8)	(23.8)	(23.8)
Fair value gains/(losses) taken to reserves (net of tax at 28%)	13.7	13.7	(8.0)	(8.0)
As at 31 December	(18.1)	(18.1)	(31.8)	(31.8)

During the year £9.4 million (2009 – £24.0 million) of fair value gains were recycled through the income statement due to the disposal of Available-for-sale assets. A further £23.7 million of fair value gains (2009 – £2.6 million fair value losses) were transferred to the income statement in respect of hedged Available-for-sale assets.

40. FINANCIAL COMMITMENTS

	Group 2010	Society 2010	Group 2009	Society 2009
Undrawn mortgage loan facilities	152.4	108.0	55.0	4.0
Other undrawn loan facilities	–	–	1.0	1.0
Total	152.4	108.0	56.0	5.0

Undrawn mortgage loan facilities

Subject to the satisfaction of previously agreed loan to value ratios, the Group is committed to £152.4 million (2009 – £55.0 million) of undrawn mortgage loan facilities (Society £108.0 million, 2009 – £4.0 million) relating to its lifetime and flexible mortgage products.

Other undrawn loan facilities

Other undrawn loan facilities relate to the Group and Society commitment of standby loan facilities to other financial institutions (2010 – £nil, 2009 – £1.0 million).

41. CAPITAL AND LEASING COMMITMENTS

	Group 2010	Society 2010	Group 2009	Society 2009
Capital commitments				
Capital expenditure contracted for but not provided for	1.6	1.6	–	–

Leasing commitments

Future minimum lease payments under non-cancellable operating leases relating to land and buildings were as follows:

	Group 2010	Society 2010	Group 2009	Society 2009
Amounts falling due:				
Within one year	3.1	3.1	2.3	2.3
Between one and five years	10.3	10.3	7.3	7.3
After five years	9.8	9.8	4.7	4.7
Total	23.2	23.2	14.3	14.3
Lease payments recognised as an expense in the period	3.1	3.1	2.7	2.7
Leasing payments due as lessor				
At the balance sheet date, future minimum subleasing payments receivable under non-cancellable subleases	1.0	1.0	0.7	0.7
At the balance sheet date, future minimum lease payments receivable under non-cancellable subleases were as follows:				
Within one year	0.2	0.2	0.1	0.1
Between one and five years	0.3	0.3	0.3	0.3
After five years	0.2	0.2	0.3	0.3
Total	0.7	0.7	0.7	0.7

42. FINANCIAL INSTRUMENTS

Use of financial instruments
The risks of the organisation are managed on a Group basis and therefore all risk disclosures in this note have been presented on a consolidated basis. The term 'Group' is used in the remainder of this note to cover the activities of both Group and Society.

Deposits are accepted from customers at both fixed and floating interest rates for various periods. The Group earns interest margin on these deposits by investing in mortgages.

The Group holds derivative financial instruments for the purposes of managing the risks associated with its various fixed and capped rate assets and liabilities and its foreign currency transactions. In accordance with its treasury policy, and the Building Societies Act 1986, the Group holds derivative financial instruments only for risk management and not for speculative or trading purposes.

The Group's policy is to manage its exposure to these risks within prudent limits. It does this through a combination of matching assets and liabilities with off-setting interest rate or exchange rate characteristics and by the use of derivative financial instruments such as interest rate swaps, forward rate agreements, interest rate options, cross currency interest rate swaps and foreign exchange contracts.

The accounting policy for derivatives and hedge accounting is described in the Accounting Policies in note 1.

Control and monitoring procedures
ALCO sets limits over the use of derivative products for managing exposure to interest rates and foreign exchange rates, sets Group non-retail credit policy and regularly monitors and reviews exposures. ALCO reports through the Risk Management Committee to the Board Risk Committee.

The Credit Risk and Lending Committee sets Group retail credit policy and regularly monitors and reviews exposures in this area. The Credit Risk and Lending Committee reports through the Risk Management Committee to the Board Risk Committee.

The principal risks the Group faces are interest rate, credit, foreign currency and liquidity risk. Each risk, and the control procedures surrounding its management, are described in detail in the Risk Management Report (see page 16).

Interest rate risk
The Group evaluates the impact on margin of various interest rate scenarios to monitor interest rate risk. The Group uses basis point sensitivity analysis to assess the change in the value of the Group's balance sheet net worth against a 100 basis point (1.0%) parallel shock to interest rates.

Details of this sensitivity analysis are on page 69. The limits around these scenarios are proposed by ALCO and approved by the Board. The Society's policies surrounding the management of interest rate risk are detailed within the Risk Management Report (see page 18).

All exposures include investment of the Group's reserves.

42. FINANCIAL INSTRUMENTS (continued)

Interest rate risk (continued)

The following table shows the impact on net worth through the reporting period:

	+100bps 2010	**-100bps 2010**	+100bps 2009	-100bps 2009
	£m	**£m**	£m	£m
Impact on equity reserves	**(18.7)**	**18.8**	(39.8)	38.7
Impact on profit and loss	**11.8**	**(8.3)**	5.4	(1.6)

The following table sets out the carrying amount of the Group's financial instruments that are exposed to interest rate risk and the expected interest reset date of those instruments.

	Three months or less	**More than three months less than six months**	**More than six months less than one year**	**More than one year less than five years**	**More than five years**	**Non-interest bearing**	**Total**
At 31 December 2010	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Assets							
Liquid assets	**3,244**	**78**	**17**	**515**	**605**	**73**	**4,532**
Loans and advances to customers	**10,781**	**925**	**847**	**4,342**	**647**	**32**	**17,574**
Fixed assets	**–**	**–**	**–**	**–**	**–**	**46**	**46**
Other assets and adjustments	**–**	**–**	**–**	**–**	**–**	**150**	**150**
Total assets	**14,025**	**1,003**	**864**	**4,857**	**1,252**	**301**	**22,302**
Liabilities and equity							
Shares	**(9,466)**	**(1,442)**	**(1,944)**	**(4,532)**	**(96)**	**(158)**	**(17,638)**
Deposits, amounts owed to customers and debt securities	**(2,090)**	**(72)**	**(47)**	**(512)**	**(750)**	**(75)**	**(3,546)**
Other liabilities and adjustments	**–**	**–**	**–**	**–**	**–**	**(203)**	**(203)**
Subordinated liabilities	**–**	**–**	**–**	**–**	**(68)**	**–**	**(68)**
Subscribed capital	**–**	**–**	**–**	**–**	**(161)**	**–**	**(161)**
Reserves	**–**	**–**	**–**	**–**	**–**	**(686)**	**(686)**
Total liabilities and equity	**(11,556)**	**(1,514)**	**(1,991)**	**(5,044)**	**(1,075)**	**(1,122)**	**(22,302)**
Derivative financial instruments	**(709)**	**277**	**555**	**(314)**	**340**	**(149)**	**–**
Interest rate sensitivity gap	**1,760**	**(234)**	**(572)**	**(501)**	**517**	**(970)**	**–**

NOTES TO THE ACCOUNTS
(continued)

42. FINANCIAL INSTRUMENTS (continued)

Interest rate risk (continued)

	Three months or less	More than three months less than six months	More than six months less than one year	More than one year less than five years	More than five years	Non-interest bearing	Total
At 31 December 2009	£m	£m	£m	£m	£m	£m	£m
Assets							
Liquid assets	2,341	460	274	610	452	28	4,165
Loans and advances to customers	8,715	592	491	3,777	478	22	14,075
Fixed assets	–	–	–	–	–	35	35
Other assets and adjustments	–	–	–	–	–	127	127
Total assets	11,056	1,052	765	4,387	930	212	18,402
Liabilities and equity							
Shares	(8,789)	(56)	(790)	(3,473)	–	(111)	(13,219)
Deposits, amounts owed to customers and debt securities	(3,106)	(162)	(58)	(526)	(350)	(12)	(4,214)
Other liabilities and adjustments	–	–	–	–	–	(153)	(153)
Subordinated liabilities	–	–	–	–	(71)	–	(71)
Subscribed capital	–	–	–	–	(161)	–	(161)
Reserves	–	–	–	–	–	(584)	(584)
Total liabilities and equity	(11,895)	(218)	(848)	(3,999)	(582)	(860)	(18,402)
Derivative financial instruments	913	(590)	147	(454)	25	(41)	–
Interest rate sensitivity gap	74	244	64	(66)	373	(689)	–

Credit risk

Credit risk is the risk that customers or counterparties will be unable to meet their financial obligations to the Society as they fall due. Impairment provisions are provided for losses that have been incurred at the balance sheet date (see note 13). The Society's policies in respect of managing credit risk are detailed in the Risk Management Report (see page 17).

Maximum credit risk exposure at 31 December 2010 approximates to the carrying value for all assets and loan commitments.

Of the £17,573.7 million 'loans and advances to customers', £17,500.2 million (99.6%) (2009 – 99.4%) is fully secured on residential property and land and £73.5 million (0.4%) (2009 – 0.6%) related to unsecured personal loans.

The average current loan to value ratio of the Group's loans and advances to customers is 50% (2009 – 51%).

The Group's number of customers in arrears as a percentage of loans and advances to customers compared to the Council of Mortgage Lenders' (CML) data is shown below:

42. FINANCIAL INSTRUMENTS (continued)

Credit risk (continued)

	2010		2009	
	Group	**CML***	Group	CML
	%	**%**	%	%
Greater than three months	**1.17**	**2.11**	1.18	2.38
Greater than six months	**0.59**	**1.23**	0.55	1.40
Greater than one year	**0.18**	**0.55**	0.12	0.60
In possession	**0.06**	**0.11**	0.06	0.14

*Council of Mortgage Lenders' data (as at 31 December 2010)

The table below provides further information by payment due status:

	2010		2009	
	£m	**%**	£m	%
Not impaired				
Neither past due nor impaired	**16,588.5**	**94.40**	13,376.7	95.04
Past due up to three months but not impaired	**736.7**	**4.19**	484.5	3.44
Impaired				
Past due over three to six months	**120.2**	**0.68**	104.4	0.74
Past due over six months or in litigation	**117.2**	**0.67**	96.6	0.69
In possession	**11.1**	**0.06**	12.5	0.09
Total	**17,573.7**	**100.00**	14,074.7	100.00

The Group held properties totalling £13.3 million pending their sale (2009 – £12.5 million) as collateral against loan repossession cases which are classified in 'loans and advances to customers' in the balance sheet. £0.5 million (2009 – £0.4 million) of loans that would be past due or impaired have had their terms renegotiated or capitalised in the last 12 months.

Credit risk – treasury liquidity book

	Exposure value by Moody's rating				
	Aaa–Aa3	**A1–A3**	**Baa1-Baa3**	**Unrated**	**Total**
At 31 December 2010	**£m**	**£m**	**£m**	**£m**	**£m**
Central banks and sovereigns	**2,817.6**	**–**	**–**	**–**	**2,817.6**
Multilateral development banks (supranational bonds)	**108.4**	**–**	**–**	**–**	**108.4**
Financial institutions	**1,014.8**	**91.2**	**28.7**	**79.9**	**1,214.6**
Mortgage-backed securities	**361.0**	**–**	**–**	**–**	**361.0**
Local authorities	**–**	**–**	**–**	**30.3**	**30.3**
Total	**4,301.8**	**91.2**	**28.7**	**110.2**	**4,531.9**

Unrated institutions are all smaller building societies and local authorities.

42. FINANCIAL INSTRUMENTS (continued)

Credit risk – treasury liquidity book (continued)

	Exposure value by Moody's rating				
	Aaa–Aa3	A1–A3	Baa1–Baa3	Unrated	Total
At 31 December 2009	£m	£m	£m	£m	£m
Central banks and sovereigns	1,705.8	–	–	–	1,705.8
Financial institutions	1,515.9	273.4	120.0	170.2	2,079.5
Mortgage-backed securities	380.1	–	–	–	380.1
Total	3,601.8	273.4	120.0	170.2	4,165.4

Foreign currency risk

Foreign currency risk arises as a result of the Group's activities in raising funds and making investments in foreign currencies. This is done to ensure wholesale funds are obtained cost effectively across a wide pool of potential providers, but exposes the Group to the risk of an appreciation in the value of foreign currency denominated liabilities or a deterioration in the value of the foreign currency denominated assets.

The risk is managed through the use of currency swaps and foreign currency forward contracts and also, where appropriate, by the matching of foreign currency liabilities with assets denominated in the same currency.

After taking into account the effects of cross currency swaps, the Group has no material net exposure to foreign exchange risk fluctuations or changes in foreign currency interest rates. ALCO sets limits on the level of exposure by currency which are monitored daily.

House price risk

House price risk arises from the value of the property forming the security for the mortgage being insufficient to repay the loan in the event of default and subsequent repossession. The Society manages this risk through a combination of prudent loan-to-value limits at inception and constant monitoring to ensure that bad debt provisions are sufficient to cover the potential losses that may arise in repossession situations. Further details of the Society's policies for managing house price risk are set out within the Risk Management Report (see page 19).

Liquidity risk

Liquidity risk is the risk that the Group has insufficient funds to meet its financial obligations as they fall due. This could manifest itself in extreme scenarios such as an inability to raise new wholesale funding to replace existing funding as it matures, or a run on retail funds. Details of the Society's policies for managing liquidity risk are detailed in the Risk Management Report (see page 19).

The liquidity ratio measures the Group's liquid assets as a percentage of the Group's shares and borrowings. The ratio during the year was as follows:

	Group 2010	Group 2009
	%	%
Liquidity ratio	**21.4**	23.9

For each material class of financial liability the contractual maturity analysis is provided in notes 29 to 34. In practice, customer deposits will be repaid later than on the contractual date on which the repayment can be required.

42. FINANCIAL INSTRUMENTS (continued)

Liquidity risk (continued)

The following is an analysis of gross contractual cash flows payable under financial liabilities:

	Repayable on demand	Up to three months	More than three months less than six months	More than six months less than one year	More than one year less than five years	More than five years	Total
At 31 December 2010	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Liabilities							
Shares	**13,641**	**102**	**129**	**1,086**	**2,879**	**–**	**17,837**
Deposits, amounts owed to customers and debt securities	**50**	**1,903**	**109**	**105**	**555**	**845**	**3,567**
Other liabilities and adjustments	**–**	**34**	**27**	**51**	**87**	**11**	**210**
Cross currency swaps	**–**	**–**	**–**	**–**	**6**	**1**	**7**
Subordinated liabilities	**–**	**–**	**–**	**5**	**28**	**83**	**116**
Subscribed capital	**–**	**2**	**4**	**6**	**49**	**162**	**223**
Total liabilities	**13,691**	**2,041**	**269**	**1,253**	**3,604**	**1,102**	**21,960**
Undrawn loan facilities	**152**	**–**	**–**	**–**	**–**	**–**	**152**
Leasing commitments	**–**	**1**	**1**	**2**	**10**	**10**	**24**
At 31 December 2009							
Liabilities							
Shares	12,836	1	1	1	414	–	13,253
Deposits, amounts owed to customers and debt securities	95	1,645	1,041	67	995	441	4,284
Other liabilities and adjustments	116	8	7	13	8	1	153
Cross currency swaps	–	1	1	1	11	3	17
Subordinated liabilities	–	–	–	4	17	85	106
Subscribed capital	–	2	4	6	49	162	223
Total liabilities	13,047	1,657	1,054	92	1,494	692	18,036
Undrawn loan facilities	56	–	–	–	–	–	56
Leasing commitments	–	–	1	1	7	5	14

Repayments of shares which are subject to notice are treated as if the notice were to be given immediately. In practice, deposits in the form of fixed bonds, notice accounts, regular savings accounts and some other transactional accounts are held by customers over the longer term and for this reason the table does not reflect the expected cash flows indicated by the Society's deposit retention history.

The tables above exclude cash flows beyond five years (other than the repayment of principal) that relate to subscribed capital.

NOTES TO THE ACCOUNTS
(continued)

42. FINANCIAL INSTRUMENTS (continued)

Capital management
The Society's approach to capital management is detailed in the Directors' Report.

Fair values
Set out below is a comparison by category of the carrying amounts and the fair values of all the Group's, and shown separately the Society's, non-derivative financial instruments.

	2010 Carrying amount	**2010 Fair value**	2009 Carrying amount	2009 Fair value
Group	**£m**	**£m**	£m	£m
Financial assets				
Cash	**1,444.2**	**1,444.2**	302.2	302.2
Debt securities - Available-for-sale:				
Government investment securities	**1,019.4**	**1,019.4**	778.4	778.4
Analysis of transferable debt securities				
Listed	**1,165.2**	**1,165.2**	1,486.0	1,486.0
Unlisted	**679.4**	**679.4**	1,273.6	1,273.6
Total	**2,864.0**	**2,864.0**	3,538.0	3,538.0
Loans and advances at amortised cost				
Loans and advances to credit institutions	**193.4**	**193.5**	325.5	325.6
Loans and advances to customers	**17,573.7**	**18,470.9**	14,074.7	15,161.6
Other liquid assets	**30.3**	**30.3**	-	-
Total	**17,797.4**	**18,694.7**	14,400.2	15,487.2
Financial liabilities at amortised cost				
Shares	**17,637.6**	**17,781.5**	13,218.8	13,629.9
Deposits, amounts owed to customers and debt securities	**3,546.0**	**3,588.2**	4,214.3	4,233.3
Subordinated liabilities	**68.2**	**91.7**	70.7	79.3
Permanent interest bearing shares	**161.3**	**214.9**	161.2	205.6

42. FINANCIAL INSTRUMENTS (continued)

Fair values (continued)

	2010 Carrying amount	**2010 Fair value**	2009 Carrying amount	2009 Fair value
Society	**£m**	**£m**	£m	£m
Financial assets				
Cash	**1,443.8**	**1,443.8**	300.0	300.0
Debt securities – Available-for-sale:				
Government investment securities	**1,019.4**	**1,019.4**	778.4	778.4
Analysis of transferable debt securities				
Listed	**1,165.2**	**1,165.2**	1,486.0	1,486.0
Unlisted	**679.4**	**679.4**	1,273.6	1,273.6
Total	**2,864.0**	**2,864.0**	3,538.0	3,538.0
Loans and advances at amortised cost				
Loans and advances to credit institutions	**193.4**	**193.5**	325.2	325.6
Loans and advances to customers	**13,523.7**	**14,444.8**	11,397.2	12,685.2
Other liquid assets	**30.3**	**30.3**	–	–
Total	**13,747.4**	**14,668.6**	11,722.4	13,010.8
Financial liabilities at amortised cost				
Shares	**17,637.6**	**17,781.5**	13,218.80	13,629.9
Deposits, amounts owed to customers and debt securities	**3,546.0**	**3,588.2**	4,214.3	4,233.3
Subordinated liabilities	**68.2**	**91.7**	70.7	79.3
Permanent interest bearing shares	**161.3**	**214.9**	161.2	205.6

Determination of fair value and fair value hierarchy

The Society uses the following hierarchy for determining and disclosing financial instruments which are carried at fair value:

- Level 1: quoted prices in active markets for the same instrument;
- Level 2: quoted prices in active markets for similar assets or liabilities or other valuation techniques for which all significant inputs are based on observable market data; and
- Level 3: valuation techniques for which any significant input is not based on observable market data.

42. FINANCIAL INSTRUMENTS (continued)

Determination of fair value and fair value hierarchy (continued)

	Level 1	Level 2	Level 3	Total fair value
31 December 2010	**£m**	**£m**	**£m**	**£m**
Financial assets				
Derivative financial instruments				
Interest rate caps	**–**	**0.1**	**–**	**0.1**
Interest rate floors	**–**	**1.1**	**–**	**1.1**
Interest rate swaps	**–**	**71.2**	**–**	**71.2**
Cross currency interest rate swaps	**–**	**1.0**	**–**	**1.0**
Total	**–**	**73.4**	**–**	**73.4**
Debt securities – Available-for-sale:				
Government investment securities	**1,019.4**	**–**	**–**	**1,019.4**
Analysis of transferable debt securities				
Listed	**1,165.2**	**–**	**–**	**1,165.2**
Unlisted	**–**	**679.4**	**–**	**679.4**
Total	**2,184.6**	**679.4**	**–**	**2,864.0**
Financial liabilities				
Derivative financial instruments				
Interest rate swaps	**–**	**138.3**	**–**	**138.3**
Currency swaps	**–**	**1.1**	**–**	**1.1**
Total	**–**	**139.4**	**–**	**139.4**

31 December 2009				
Financial assets				
Derivative financial instruments				
Interest rate caps	–	3.8	–	3.8
Interest rate swaps	–	24.0	–	24.0
Cross currency interest rate swaps	–	1.5	–	1.5
Total	–	29.3	–	29.3
Debt securities – Available-for-sale:				
Government investment securities	778.4	–	–	778.4
Analysis of transferable debt securities				
Listed	1,486.0	–	–	1,486.0
Unlisted	–	1,273.6	–	1,273.6
Total	2,264.4	1,273.6	–	3,538.0
Financial liabilities				
Derivative financial instruments				
Interest rate swaps	–	108.9	–	108.9
Total	–	108.9	–	108.9

42. FINANCIAL INSTRUMENTS (continued)

Financial instruments recorded at fair value
The following is a description of the determination of fair value for financial instruments which are recorded at fair value using valuation techniques. These incorporate the Society's estimate of assumptions that a market participant would make when valuing the instruments.

Derivatives
Derivative products valued using a valuation technique with observable market inputs are interest rate swaps and currency swaps. The valuation techniques applied are swap models using present value calculations. The models incorporate various assumptions including interest rate curves, foreign exchange spot and forward rates, and the credit quality of counterparties.

Financial investments – Available-for-sale
Market and counterparty prices have been used to determine the fair values of listed debt securities and permanent interest bearing shares. The fair values of all other instruments have been calculated using valuation models which use discounted cash flow analysis which incorporates observable market data including the use of prevailing interest rates and credit valuation adjustments to discount expected future cash flows.

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.

43. RELATED PARTY TRANSACTIONS

ULTIMATE CONTROLLING PARTY

The Group is controlled by Coventry Building Society registered in England and Wales, which is also considered to be the ultimate parent.

TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL

Transactions with key management personnel are on the same terms and conditions applicable to members and other employees within the Society. The directors are considered to be the only 'key management' for the purposes of the related party transactions disclosures under IAS 24.

In accordance with Section 68 of the Act, the Society maintains a register of loans falling within Section 65 made to directors and connected persons. A statement containing requisite particulars of such transactions may be inspected by members at the Society's AGM or at the Registered Office of the Society during the period 15 days prior to the AGM.

43. RELATED PARTY TRANSACTIONS (continued)

TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL (continued)

	2010	2009
Aggregate loans and deposits of directors	**£000**	£000
Loans payable by directors to the Society		
Loans outstanding at 1 January	**1,205.1**	1,040.5
Loans issued during the year (including existing loans on appointment as director)	**335.4**	234.7
Loan repayments during the year (net of interest)	**(130.7)**	(70.1)
Loans outstanding at 31 December	**1,409.8**	1,205.1
Deposits payable by the Society		
Deposits outstanding at 1 January	**2,290.2**	2,021.1
Deposits issued during the year	**1,424.1**	361.3
Deposit repayments during the year (net of interest)	**(955.4)**	(92.2)
Deposits outstanding at 31 December	**2,758.9**	2,290.2
Net interest income/(expense)		
Interest receivable	**28.7**	26.6
Interest payable	**(43.4)**	(61.2)
Total	**(14.7)**	(34.6)

TRANSACTIONS WITH GROUP COMPANIES

Transactions are entered into with related parties in the normal course of business. These include loans, deposits and the payment and recharge of administrative expenses. The volumes of related party transactions, outstanding balances at the year end, and related income and expenses for the year are as follows:

	£m	£m
Loans payable to the Society		
Loans outstanding as at 1 January	**5,313.5**	4,769.5
Acquired on transfer of engagements	**575.0**	–
Loans issued during the year	**1,315.6**	702.8
Loan repayments during the year	**–**	(158.8)
Loans outstanding as at 31 December	**7,204.1**	5,313.5
Net receivable	**231.7**	204.9
Fees and expenses paid to the Society	**1.8**	1.7

Interest on outstanding loans and deposits accrues at a transfer price rate agreed between the Society and its subsidiaries.

44. NOTES TO THE STATEMENTS OF CASH FLOWS

	Group 2010	Society 2010	Group 2009	Society 2009
	£m	£m	£m	£m
Non-cash items included in profit before tax				
Net increase in impairment provisions	11.8	8.9	19.9	14.3
Depreciation and amortisation	7.3	7.3	6.7	6.7
Interest on subordinated liabilities	3.9	3.9	4.0	4.0
Interest on subscribed capital	12.3	12.3	12.2	12.2
Increase in fair value adjustment of hedged risk	9.0	9.0	119.1	119.3
Other non-cash movements	(5.5)	(0.5)	2.1	2.1
Gain on business combinations	(43.8)	(70.7)	–	–
	(5.0)	(29.8)	164.0	158.6
Changes in operating assets				
Decrease in loans to credit institutions and other liquid assets	378.8	378.8	54.3	54.3
Increase in loans and advances to customers	(1,621.5)	(793.7)	(921.8)	(208.6)
Decrease in prepayments and accrued income	1.5	1.5	3.6	3.6
Decrease/(increase) in other assets	5.6	5.5	(1.3)	(1.3)
	(1,235.6)	(407.9)	(865.2)	(152.0)
Changes in operating liabilities				
Increase in shares	2,113.2	2,113.2	973.5	973.5
Decrease in deposits and other borrowings	(396.7)	(395.9)	(341.7)	(341.7)
(Decrease)/increase in debt securities in issue	(212.9)	(212.9)	206.5	206.5
Increase/(decrease) in accruals and deferred income	63.9	62.3	(149.7)	(149.7)
(Decrease)/increase in other liabilities	(21.8)	(20.1)	2.5	2.3
	1,545.7	1,546.6	691.1	690.9
Cash and cash equivalents				
Cash and balances with the Bank of England (note 18)	1,427.9	1,427.5	287.6	285.4
Due from other banks	109.9	109.9	40.5	40.5
	1,537.8	1,537.4	328.1	325.9

Cash and cash equivalents excludes the balance which the Society is required to maintain with the Bank of England which, at 31 December 2010, amounted to £16.3 million (2009 – £14.6 million).

45. TRANSFER OF ENGAGEMENTS

STROUD & SWINDON BUILDING SOCIETY

On 1 September 2010 the Society merged with Stroud & Swindon Building Society. The merger was approved by the members of Stroud & Swindon Building Society at a Special General Meeting and was subsequently confirmed by the FSA. The merger was accounted for using the acquisition method, following the requirements of IFRS 3 (2008 Revised) 'Business Combinations' which was endorsed by the EU in June 2009.

The Consolidated Income Statement of the Group includes merger related deal costs of £2.5 million, integration (including provisions) costs of £5.5 million and overhead costs which do not form part of the long-term ongoing business of £3.2 million. The assets and liabilities acquired and associated fair value adjustments required to conform with IFRS 3 (2008 Revised) 'Business Combinations' are set out on page 80.

NOTES TO THE ACCOUNTS
(continued)

45. TRANSFER OF ENGAGEMENTS (continued)

	Notes	Cessation accounts UK GAAP format	IFRS Re-classification (i)	Fair value adjustments	Acquisition fair values
		£m	£m	£m	£m
Assets					
Cash and balances with the Bank of England		10.8	–	–	**10.8**
Loans and advances to credit institutions		141.2	–	–	**141.2**
Debt securities	ii)	399.4	–	(0.5)	**398.9**
Other liquid assets		68.2	–	–	**68.2**
		619.6	–	(0.5)	**619.1**
Derivative financial instruments	iii)	–	2.4	3.8	**6.2**
Loans and advances to customers	iv)	1,900.7	(0.2)	(11.2)	**1,889.3**
Prepayments and accrued income	v)	14.3	(3.3)	(8.8)	**2.2**
Intangible assets	vi)	–	–	3.0	**3.0**
Property, plant and equipment	vii)	13.4	(8.8)	(2.7)	**1.9**
Investment properties	vii)	5.9	–	(0.7)	**5.2**
Current tax assets	viii)	0.6	(0.6)	–	**–**
Deferred tax assets	viii)	0.9	2.6	16.2	**19.7**
Non-current assets held for sale	vii)	–	8.8	(4.9)	**3.9**
Total assets		2,555.4	0.9	(5.8)	**2,550.5**
Liabilities					
Shares	vi) ix)	2,243.5	–	3.1	**2,246.6**
Deposits from banks		5.5	–	–	**5.5**
Other deposits		27.0	–	–	**27.0**
Amounts owed to customers		117.0	–	–	**117.0**
Derivative financial instruments	iii)	–	(0.6)	35.7	**35.1**
Other liabilities		6.4	–	–	**6.4**
Current tax liabilities		2.9	(0.4)	0.8	**3.3**
Deferred tax liabilities		–	–	0.6	**0.6**
Provisions for liabilities and charges		0.8	–	–	**0.8**
Accruals and deferred income		4.1	(1.3)	–	**2.8**
Pension benefit obligations		6.4	2.4	–	**8.8**
Subordinated liabilities		52.0	0.8	–	**52.8**
Total liabilities		2,465.6	0.9	40.2	**2,506.7**
Net identifiable assets	x)	89.8	–	(46.0)	**43.8**
Imputed consideration		–	–	–	**–**
Gain on business combination					**43.8**

We expect to receive all gross contractual amounts receivable relating to the above financial assets with the exception of the following:

	Fair value	Gross contractual amounts receivable	Cash flows not expected to be collected
	£m	£m	£m
Loans and advances to customers	1,889.3	1,905.7	29.9

The gross contractual amounts receivable represents the cessation account balance before provisions and other fair value adjustments. Cash flows not expected to be collected are the undiscounted credit losses associated with the balance.

45. TRANSFER OF ENGAGEMENTS (continued)

IFRS 3 (2008 Revised) 'Business Combinations' which was endorsed by the EU in June 2009, requires substantially all assets and liabilities to be initially recognised at fair value. Explanations of material fair value adjustments to take on balances are as follows:

i) The cessation accounts of Stroud & Swindon Building Society were prepared in accordance with UK Generally Accepted Accounting Principles (UK GAAP) and some balance sheet reclassifications have therefore been made to conform with IFRS formats. The most material of these has been to reclassify two head office buildings from 'Property, plant and equipment' to 'Non-current assets held for sale' and reclassifying the deferred tax on the 'Pension benefit obligations' to 'Deferred tax asset'.

ii) Debt securities were previously carried at amortised cost subject to impairment. These are now included at fair value using market prices or prices obtained from counterparties.

iii) Derivative financial instruments were previously carried at amortised cost and these are now included at fair value based on discounted future cash flow models, with market inputs valued consistently with the Group.

iv) Loans and advances to customers were previously carried at amortised cost subject to impairment and have been recognised at fair value at the merger date. The acquisition fair value adjustment reflects both credit and interest rate risk associated with these assets. This fair value at acquisition becomes the new amortised cost for acquired loans and receivables.

v) Stroud & Swindon Building Society incurred swap cancellation costs which were being amortised over the remaining life of the item being hedged. This treatment is not permissible under IFRS, and therefore these costs have been written off. In addition mortgage premiums which were being amortised over the average expected life of the acquired portfolio have also been written off.

vi) Identifiable intangible assets are in respect of core deposits totalling £3.0 million (recognising the benefit to the Group of the Stroud & Swindon Building Society savings book). These will be amortised over their useful lives of 16 months. The intangible assets will be subject to annual impairment review.

vii) Property and investment properties have been valued using third party valuations, and have been written down accordingly. The remaining fixed assets have been reviewed internally and written off as appropriate where there is no further use within the enlarged Society.

viii) The current and deferred tax adjustment reflects the tax consequences of the other fair value adjustments made.

ix) The fair value adjustments for shares reflect interest rate risk associated with these liabilities. Under UK GAAP these liabilities were carried at amortised cost.

x) Consideration represents the fair value of members' interests transferred. The combination of the two societies did not involve the transfer of any cash consideration. The value of the consideration has been calculated by measuring the fair value of the Stroud & Swindon Building Society business. The calculation has been made with reference to quoted financial services organisations with publicly available valuations, adjusted to take account of such items as the relative size, financial status, economic diversification and the unquoted nature of the business. This has resulted in a value of £nil attributed to the consideration.

The cessation accounts of Stroud & Swindon Building Society for the period 1 January 2010 to 31 August 2010, audited by KPMG plc, reported net interest income of £7.4 million and a post tax loss of £6.8 million. It is impractical for the Society to disclose net interest and profitability of the Group had the merger occurred at the beginning of the annual reporting year. The Society believes that estimating such a figure would include applying various significant assumptions, and may result in misleading information.

Following the merger, Stroud & Swindon Building Society ceased to exist, being subsumed by Coventry Building Society. It is impractical to separate its results post the transfer of engagements.

ANNUAL BUSINESS STATEMENT

for the year ended 31 December 2010

1. STATUTORY PERCENTAGES

	2010 %	Statutory limits %
Lending limit	**1.2**	25.0
Funding limit	**16.8**	50.0

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 the business assets not in the form of loans fully secured on residential property and is calculated as (X-Y)/X where:

X = business assets, being the total assets of the Group plus loan impairment less liquid assets, intangible assets and property, plant and equipment. The value of X used is the value at 31 December 2010.

Y = the principal value of, and interest accrued on, loans owed to the Group which are fully secured on residential property. The value of Y used is the value at 31 December 2010.

The funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals and is calculated as (X-Y)/X where:

X=shares and borrowings, being the aggregate of:

i) the principal value of, and interest accrued on, shares in the Society;

ii) the principal value of, and interest accrued on, the amounts deposited with the Society by banks, credit institutions and other customers; and

iii) the principal value of, and interest accrued on, the amounts of debt securities of the Society.

Y = the principal value of, and interest accrued on, shares in the Society held by individuals other than bare trustees (or, in Scotland, simple trustees) for bodies corporate or for persons that include bodies corporate.

2. OTHER PERCENTAGES

	2010	2009
	%	%
As a percentage of shares and borrowings:		
Gross capital	**4.32**	4.68
Free capital	**4.12**	4.51
Liquid assets	**21.4**	23.9
As a percentage of mean total assets:		
Profit for the financial year	**0.42**	0.24
Management expenses	**0.37**	0.38

The above percentages have been calculated from the Group Accounts.

'Shares and borrowings' represents the total of shares, deposits from banks, other deposits, amounts owed to other customers and debt securities in issue.

'Gross capital' represents the aggregate of reserves, subordinated liabilities and subscribed capital.

'Free capital' represents the aggregate of gross capital and collective impairment less intangible assets and property, plant and equipment.

'Liquid assets' represent the total of cash in hand and balances with the Bank of England, loans and advances to credit institutions, debt securities and other liquid assets.

'Mean total assets' represent the average of the 2010 and 2009 total assets.

'Management expenses' represent the aggregate of administrative expenses, amortisation of intangible assets and depreciation of property, plant and equipment.

ANNUAL BUSINESS STATEMENT
(continued)

3. INFORMATION RELATING TO DIRECTORS AND OTHER OFFICERS

Part 1 - Directors

Name (Date of birth)	Occupation	Other directorships	Date of appointment as a director of the Society
David A Harding, JP, BA, MPhil, FCMA (Chairman) (29.07.1947)	Company Director	Enterprise Inns plc RT Group PLC (In Members' Voluntary Liquidation) The Royal Mint The Royal Mint Limited	01.10.1996
Bridget P Blow (Deputy Chairman) (02.06.1949)	Company Director	Birmingham Hippodrome Limited Birmingham Hippodrome Theatre Trust Limited Bridget Blow Consulting Limited Harvard International plc Kensington Green (Management) Limited Trustmarque Acquisitions Limited Trustmarque Group Limited Trustmarque Intermediary Limited Trustmarque Solutions Limited	01.02.2007
Roger D Burnell, BSc, FCA (08.04.1950)	Company Director	Thomas Cook Group plc Clarence Mansions Management Company Limited	01.09.2008
Colin T Franklin, FCIB (15.06.1955)	Building Society Sales & Marketing Director	Godiva Mortgages Limited Five Valleys Property Company Limited ITL Mortgages Limited	07.07.2009
Ian S Geden, FCII (08.07.1953)	Company Director	The Police Mutual	01.09.2008
John Lowe, BA (Oxon), ACA (26.10.1972)	Building Society Finance Director	Godiva Mortgages Limited Coventry Financial Services Limited Coventry Property Services Limited Godiva Financial Services Limited Godiva Housing Developments Limited Godiva Savings Limited Godiva Securities and Investments Limited Berry Birch & Noble Management Limited (in liquidation)	14.10.2010
Ian Pickering, MA (Cantab), FCA (16.10.1955)	Company Director	Electrocab Limited Bedford Hospital NHS Trust Member of the Council of Cranfield University Member of the Auditing Practices Board of the Financial Reporting Council	01.09.2005
Fiona B Smith, LLB (03.01.1959)	Solicitor	Derwent Insurance Limited Severn Trent European Finance Limited S.a.r.l. Severn Trent European Placement SA Severn Trent Holdings NV Severn Trent Luxembourg Finance SA Severn Trent Luxembourg Holdings SA Severn Trent Luxembourg Overseas Finance SA Severn Trent Luxembourg Overseas Holdings SA	01.12.2002
Glyn Smith, MA, (Cantab), FCA (15.09.1952)	Company Director	Covent Garden Market Authority Bournemouth & Poole Teaching PCT Examiner – ICAEW ITL Mortgages Limited Stroud & Swindon Funding Company Stroud & Swindon Funding Company (No. 2) Limited	22.09.2010

3. INFORMATION RELATING TO DIRECTORS AND OTHER OFFICERS (continued)

Part 1 - Directors (continued)

Name (Date of birth)	Occupation	Other directorships	Date of appointment as a director of the Society
David Stewart, BA, ACA (18.08.1965)	Building Society Chief Executive	Godiva Mortgages Limited Coventry Financial Services Limited Coventry Property Services Limited Godiva Financial Services Limited Godiva Housing Developments Limited Godiva Savings Limited Godiva Securities and Investments Limited	11.02.2002
Philip L Vaughan, BA, FCMA (15.08.1964)	Building Society Chief Operating Officer	Corporate Transformations Limited	07.07.2009

Documents may be served on the above named directors at:
Seymours Solicitors, Queens House, Queens Road, Coventry CV1 3JN.

In 2006 the Society entered into a service contract with David Stewart, the Chief Executive. The contract expires at the age of 60, but is terminable by David Stewart on six months' notice and by the Society on one year's notice.

In 2009 the Society appointed Colin Franklin (Sales and Marketing Director) and Phil Vaughan (Chief Operating Officer) to the board. Service contracts were entered into which are terminable by the individual on six months' notice and by the Society on one year's notice.

In 2010 the Society appointed John Lowe (Finance Director) to the board. A service contract was entered into which is terminable by John Lowe on six months' notice and by the Society on one year's notice.

Part 2 – The Secretary

Name	Occupation	Directorships
Nailesh K Rambhai, MA (Oxon)	Secretary and Solicitor	Belgrade Theatre Trust (Coventry) Limited Cholmeley Court Limited

Part 3 – Senior management team

Name	Occupation
Julian M J Atkins, BSc, MBA, FCIPD, FCIB	Head of Human Resources
Rachel C Haworth, BA, MCIM	Head of Marketing & Communications
Darin J Landon	Head of Sales
Sheryl A F Lawrence, MBA, LLM, BSc, ACA	Head of Risk
Sally A Wrigglesworth, MBA, ACIB	Head of Customer Service

ANNUAL BUSINESS STATEMENT
(continued)

4. SUBSIDIARIES CARRYING ON BUSINESS

At 31 December 2010 the Society held (directly or indirectly) a 100% beneficial ownership in the following subsidiary companies, incorporated in England and Wales:

	Share capital authorised £	Share capital issued £
Godiva Mortgages Limited	1,000	20
Stroud and Swindon Funding Company	11,745,000	11,741,343
Stroud and Swindon Funding Company (No. 2) Limited	200,000,000	133,641,371
ITL Mortgages Limited	104,000,000	1,473,802
Five Valleys Property Company Limited	99,000,000	1

The Society also has an interest in Coventry Building Society Covered Bonds LLP which gives rise to risks and rewards that are in substance no different than if it was a subsidiary undertaking. Coventry Building Society Covered Bonds LLP is registered in England and Wales.

5. SUBSIDIARIES NOT CARRYING ON BUSINESS

At 31 December 2010 the Society held shares in the following directly wholly owned subsidiary companies, all of which are incorporated in England and Wales:

	Percentage owned directly by Society %	Share capital issued £
Coventry Financial Services Limited	100	20
Coventry Property Services Limited	100	20
Godiva Financial Services Limited	100	20
Godiva Housing Developments Limited	100	20
Godiva Savings Limited	100	2
Godiva Securities and Investments Limited	100	20

At the same date, the authorised share capital of Godiva Savings Limited was £1,000. The authorised share capital of each of the other subsidiary companies was £100.

6. PRINCIPAL OFFICE

Coventry Building Society is a building society, incorporated and domiciled in the United Kingdom. The address of the registered office is: Economic House, PO Box 9, High Street, Coventry CV1 5QN.

the COVENTRY
TLC not PLC

www.thecoventry.co.uk

Coventry Building Society.
Registered Office: Economic House, PO Box 9, High Street, Coventry CV1 5QN.