LLOYDS TSB GROUP PLC
Form 20-F
June 06, 2006

As filed with the Securities and Exchange Commission on 6 June 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g)
OF THE SECURITIES EXCHANGE ACT OF 1934

OR

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended 31 December 2005

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

OR

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 001-15246

LLOYDS TSB GROUP plc

(Exact name of Registrant as Specified in Its Charter)

Scotland

(Jurisdiction of Incorporation or Organization)

25 Gresham Street
London EC2V 7HN
United Kingdom
(Address of Principal Executive Offices)

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

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

Securities registered or to be registered pursuant to Section 12(g) of the Act:
None
Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:
None

The number of outstanding shares of each of Lloyds TSB Group plc s classes of capital or common stock as of 31 December 2005 was:

Ordinary shares, nominal value 25 pence each, as of 31 December 2005...5,602,613,600

Limited voting shares, nominal value 25 pence each, as of 31 December 2005... 78,947,368

Preference shares, nominal value 25 pence each, as of 31 December 2005... 400

Preference shares, nominal value 25 cents each, as of 31 December 2005..... 0

Preference shares, nominal value 25 euro cents each, as of 31 December 2005..... 0

Preference shares, nominal value Japanese ¥25 each, as of 31 December 2005... 0

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes x No o

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Yes o No x

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x	Accelerated filer o	Non-Accelerated filer o

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

Item 17 o Item 18 x

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

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PRESENTATION OF INFORMATION

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

Lloyds TSB Group publishes its Consolidated Financial Statements expressed in British pounds (pounds sterling , sterling or £), the lawful currency of the UK. In this annual report, references to pence and p are to one-hundredth of one pound sterling; references to US dollars , US$ $ are to the lawful currency of the United States (the US); references to cent are to one-hundredth of one US dollar; references to euro or the lawful currency of the member states of the European Union that have adopted a single currency in accordance with the Treaty establishing the European Communities, as amended by the Treaty of European Union; and references to Japanese yen Japanese ¥ or ¥ are to the lawful currency of Japan. Solely for the convenience of the reader, this annual report contains translations of certain pounds sterling amounts into US dollars at specified rates. These translations should not be construed as representations by Lloyds TSB Group that the pounds sterling amounts actually represent such US dollar amounts or could be converted into US dollars at the rate indicated or any other rate. Unless otherwise stated, the translations of pounds sterling into US dollars have been made at the noon buying rate in New York City for cable transfers in pounds sterling as certified for customs purposes by the Federal Reserve Bank of New York (the Noon Buying Rate) in effect on 31 December 2005, which was $1.7188 = £1.00. The Noon Buying Rate on 31 December 2005 differs from certain of the actual rates used in the preparation of the Consolidated Financial Statements, which are expressed in pounds sterling, and therefore US dollar amounts appearing in this annual report may differ significantly from actual US dollar amounts which were translated into pounds sterling in the preparation of the Consolidated Financial Statements in accordance with International Financial Reporting Standards as adopted by the European Union.

BUSINESS OVERVIEW

Lloyds TSB Group is a leading UK-based financial services group, whose businesses provide a wide range of banking and financial services in the UK and in certain locations overseas; although, following a number of sales of overseas businesses in recent years, the Lloyds TSB Group s activities are now concentrated in the UK. At 31 December 2005 total Lloyds TSB Group assets were £309,754 million and Lloyds TSB Group had some 67,000 employees. Lloyds TSB Group plc s market capitalisation at that date was some £27,400 million. The profit on ordinary activities before tax for the 12 months to 31 December 2005 was £3,820 million and the risk asset ratios as at that date were 10.9 per cent for total capital and 7.9 per cent for tier 1 capital.

The operations of Lloyds TSB Group in the UK were conducted through over 2,100 branches of Lloyds TSB Bank, Lloyds TSB Scotland plc and Cheltenham & Gloucester plc at the end of December 2005. International business is conducted mainly in the US and continental Europe. Lloyds TSB Group s services in these countries are offered largely through branches of Lloyds TSB Bank. Lloyds TSB Group also offers offshore banking facilities in a number of countries. For additional information see Regulation .

Lloyds TSB Group s activities are organised into three segments: UK Retail Banking, Insurance and Investments and Wholesale and International Banking. Services provided by UK Retail Banking encompass the provision of banking and other financial services to personal customers, private banking and mortgages. Insurance and Investments offers life assurance, pensions and investment products, general insurance and fund management services. Wholesale and International Banking provides banking and related services for major UK and multinational companies, banks and financial institutions, and small and medium-sized UK businesses, including venture capital finance. It also provides asset finance and share registration services to personal and corporate customers, manages Lloyds TSB Group s activities in financial markets through its treasury function and provides banking and financial services overseas.

The following table shows the results of Lloyds TSB Group s UK Retail Banking, Insurance and Investments and Wholesale and International Banking segments and Central group items in each of the last two fiscal years. The impact of adopting International Financial Reporting Standards (IFRS), and in particular the increased use of fair values, has resulted in greater earnings volatility. In order to provide a more comparable representation of business performance this volatility has been separately analysed from the results of the individual business units (see Operating and financial review and prospects Results of operations for 2005 and 2004 Volatility).

	2005 **£m**	2004 £m
UK Retail Banking	**1,394**	1,639
Insurance and Investments	**725**	778
Wholesale and International Banking	**1,518**	1,272
Central group items	**(442)**	(350)
Profit before tax, excluding volatility	**3,195**	3,339
Volatility*	**625**	138
Profit before tax	**3,820**	3,477

* Volatility relates to Insurance and Investments (2005: £749 million; 2004: £138 million) and Central group items (2005: £(124) million; 2004: £nil).

Lloyds TSB Group plc was incorporated as a public limited company and registered in Scotland under the UK Companies Act 1985 on 21 October 1985 with the registered number 95000. Lloyds TSB Group plc s registered office is Henry Duncan House, 120 George Street, Edinburgh EH2 4LH, Scotland, and its principal executive offices in the UK are located at 25 Gresham Street, London, EC2V 7HN, United Kingdom, telephone number + 44 (0) 20 7626 1500.

SELECTED CONSOLIDATED FINANCIAL DATA

The financial information set out in the tables below has been derived from the annual reports and accounts of Lloyds TSB Group plc for each of the past five years adjusted for subsequent changes in accounting policy and presentation. The financial statements for the year 2001 were audited by PricewaterhouseCoopers, independent accountants; the financial statements for each of the years 2002 to 2005 have been audited by their successor firm PricewaterhouseCoopers LLP, independent accountants.

The financial statements have been prepared in accordance with IFRS which differs in certain significant respects from US Generally Accepted Accounting Principles (US GAAP). A discussion of the differences between IFRS and US GAAP and a reconciliation of certain IFRS amounts to US GAAP are included in note 56 to the financial statements.

IFRS	**2005**	2004
Income statement data for the year ended 31 December (£m)		
Net interest income	**5,671**	5,110
Other income	**17,055**	14,173
Trading surplus	**5,069**	4,364
Impairment losses on loans and advances	**(1,299)**	(866)
Profit before tax	**3,820**	3,477
Profit for the year	**2,555**	2,459
Profit for the year attributable to equity shareholders	**2,493**	2,392
Total dividend for the year[1]	**1,915**	1,914
Balance sheet data at 31 December (£m)		
Share capital	**1,420**	1,419
Shareholders equity	**10,195**	11,047
Customer accounts	**131,070**	119,811
Undated subordinated loan capital	**7,733**	5,852
Dated subordinated loan capital	**4,669**	4,400
Loans and advances to customers	**174,944**	155,318
Total assets	**309,754**	284,422
Share information		
Basic earnings per ordinary share	**44.6p**	42.8p
Diluted earnings per ordinary share	**44.2p**	42.5p
Net asset value per ordinary share	**180p**	195p
Total dividend per ordinary share[1]	**34.2p**	34.2p
Equivalent cents per share[1, 2]	**62.2c**	63.7c
Market price (year-end)	**488.5p**	473p
Number of shareholders (thousands)	**920**	953
Number of ordinary shares in issue (millions)[3]	**5,603**	5,596
Financial ratios (%)[4]		
Dividend payout ratio	**76.8**	80.0
Post-tax return on average shareholders equity	**25.6**	22.8
Post-tax return on average assets	**0.84**	0.92
Post-tax return on average risk-weighted assets	**1.81**	1.99
Average shareholders equity to average assets	**3.2**	3.9
Cost:income ratio[5]	**51.9**	54.8
Capital ratios (%)[6]		
Total capital	**10.9**	10.1
Tier 1 capital	**7.9**	8.2

1 Annual dividends comprise both interim and final dividend payments. For the purposes of the IFRS disclosures in this table, the total dividend for the year represents the interim dividend paid during the year and the final dividend which will be paid and accounted for

during the following year.

2 Translated into US dollars at the Noon Buying Rate on the date each payment was made.

3 This figure excludes the 79 million limited voting ordinary shares owned by the Lloyds TSB Foundations.

4 Averages are calculated on a monthly basis from the consolidated financial data of Lloyds TSB Group.

5 The cost:income ratio is calculated as total operating expenses as a percentage of total income (net of insurance claims).

6 In order to provide a more meaningful comparison, capital ratios are shown at 31 December 2005 and 1 January 2005, after the application of those accounting standards applied with effect from 1 January 2005.

SELECTED US GAAP FINANCIAL DATA	**2005**	2004	2003	2002	2001
Income statement data for the year ended 31 December (£m)[(1)]					
Total revenues, net of interest expense	**20,413**	16,668	14,139	10,498	9,335
Policyholder benefits and claims expense	**(7,479)**	(4,473)	(3,036)	(1,565)	(2,228)
Allowance for loan losses	**(1,613)**	(866)	(950)	(1,029)	(747)
Income before tax	**2,605**	3,214	4,220	2,378	2,221
Net income	**1,351**	1,508	3,231	1,753	1,635
Dividends	**1,914**	1,913	1,908	1,903	1,738
Balance sheet data at 31 December (£m)					
Shareholders equity	**10,981**	11,458	11,892	10,164	13,505
Deposits	**162,491**	159,546	140,451	141,777	133,419
Loans, net of provisions	**173,981**	152,428	134,043	134,202	122,485
Total assets	**305,917**	281,598	251,158	254,352	243,187
Share information (pence per ordinary share)					
Basic earnings	**24.1**	27.0	57.9	31.5	29.5
Diluted earnings	**24.0**	26.8	57.7	31.3	29.2
Net asset value	**193**	202	210	180	240
Dividends	**34.2**	34.2	34.2	34.2	31.5
Financial ratios (%)[(2)]					
Dividend payout ratio	**141.7**	126.9	59.1	108.6	106.4
Post-tax return on average shareholders equity	**12.0**	12.9	29.3	14.8	12.0
Post-tax return on average assets	**0.60**	0.65	1.29	0.73	0.72
Average shareholders equity to average assets	**3.8**	4.4	4.4	4.8	5.8

(1) For the purposes of this five year summary, income statement items in respect of discontinued operations have been aggregated with those of continuing operations.

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

EXCHANGE RATES

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

	2006 April	2006 March	2006 February	2006 January	2005 December	2005 November
US dollars per pound sterling:						
High	1.82	1.76	1.78	1.79	1.77	1.78
Low	1.74	1.73	1.73	1.74	1.72	1.71

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

	2005	2004	2003	2002	2001
US dollars per pound sterling:					
Average	1.81	1.84	1.64	1.51	1.44

On 26 May 2006, the latest practicable date, the US dollar Noon Buying Rate was $1.857 = £1.00. Lloyds TSB Group makes no representation that amounts in pounds sterling have been, could have been or could be converted into US dollars at that rate or at any of the above rates.

BUSINESS

History and development of Lloyds TSB Group

The history of Lloyds TSB Bank can be traced back to the 18th century when the banking partnership of Taylor and Lloyds was established in the UK. The late 19th and early 20th centuries were marked by many acquisitions and mergers, significantly increasing the number of banking offices in the UK. In 1988 Lloyds TSB Bank acquired a majority shareholding in Abbey Life Group Plc (renamed Lloyds Abbey Life plc (LAL)) in return for the sale to LAL of five of Lloyds TSB Bank s businesses; and in 1995 the business of Cheltenham and Gloucester Building Society was acquired.

TSB Group plc became operational in 1986 when, following UK government legislation, the operations of four Trustee Savings Banks and other related companies were transferred to TSB Group plc and its new banking subsidiaries. By 1995, the TSB Group had, either through organic growth or acquisition, developed life and general insurance operations, investment management activities, a motor vehicle hire purchase and leasing operation, and an estate agency business to supplement its retail banking activities.

In 1995, TSB Group plc merged with Lloyds TSB Bank. Under the terms of the merger, the TSB and Lloyds TSB Bank groups were combined under TSB Group plc, which was re-named Lloyds TSB Group plc. In 1999, the businesses, assets and liabilities of TSB Bank plc, the principal banking subsidiary of the TSB Group prior to the merger, and its subsidiary Hill Samuel Bank Limited were vested in Lloyds TSB Bank. In 1996, Lloyds TSB Group acquired the minority interest in LAL. In 2000, Lloyds TSB Group acquired Scottish Widows, for a total consideration of £5,947 million. In addition to being one of the leading providers of banking services in the UK, this transaction also positioned Lloyds TSB Group as one of the leading suppliers of long-term savings and protection products in the UK.

During the last three years, the Lloyds TSB Group has disposed of a number of its overseas operations, as part of the process of managing its portfolio of businesses to focus on its core markets. These disposals have resulted in a significant reduction in the size of the Lloyds TSB Group s international business. For additional information on the Lloyds TSB Group see Business Overview .

Management and resources

Lloyds TSB Group recognises that it will create value for its shareholders if it creates value for its customers. Its constant aim is to meet the rapidly changing needs and expectations of its customers. Lloyds TSB Group believes that success depends upon service, consistency and commitment and it aims, wherever possible, to maintain long-term relationships with its customers.

Lloyds TSB Group operates in a marketplace which is continually changing. No organisation can successfully manage change without the support and commitment of its staff. The pace and scope of change will not diminish as competition in the financial services market continues to increase. Lloyds TSB Group recognises that it is the staff of the organisation who have delivered, and will continue to deliver, its success. The Lloyds TSB Group invests a significant amount in training to develop the knowledge and skills of its employees, which it considers to be a key element in the achievement of its overall strategy.

Lloyds TSB Group recognises that long-term success depends on the quality of its management. It is therefore committed to developing the potential of all managers; in particular ensuring that it has the succession management capability to meet future needs for top management. Peter Ayliffe, group executive director, UK Retail Banking, left the board on 31 January 2005 and was replaced by Terri Dial, formerly group executive vice president and member of the management committee of Wells Fargo & Co, who joined the board on 1 June 2005. In the intervening period Mike Fairey acted as group executive director, UK Retail Banking in addition to his other responsibilities.

Two non-executive directors, Dr Chris Gibson-Smith and David Pritchard, left the board on 5 May 2005. Sir Julian Horn-Smith joined the board, as a non-executive director, on 1 January 2005; Jan du Plessis and Lord Leitch joined the board, also as non-executive directors, on 1 October 2005.

Sir Victor Blank, Chairman of GUS and former chairman of Trinity Mirror (until 4 May 2006) joined the board as deputy chairman on 1 March 2006. Sir Victor took over as chairman of the Lloyds TSB Group at the annual general meeting on 11 May 2006, upon the retirement of Maarten van den Bergh.

Strategy of Lloyds TSB Group

The governing objective of Lloyds TSB Group is to maximise shareholder value over time. In an environment of increasing competition and empowered customers, Lloyds TSB Group believes that this shareholder value objective can best be achieved by:

- focusing on markets where it can build and sustain competitive advantage;
- developing business strategies for those markets which are founded on being profitably different in the way it creates customer value; and
- building a high-performance organisation focused on the right goals and the best possible execution of those strategies.

Reflecting this, in 2003 the Lloyds TSB Group put in place a three-phase strategy. In phase 1, now completed, the Lloyds TSB Group focused on enhancing the quality of its earnings by exiting businesses which were not regarded as core or which added unnecessary volatility to its earnings. During this phase, the Lloyds TSB Group divested businesses in New Zealand and Latin America, markets in which it did not expect to be able to build and sustain competitive advantage. In phase 2, Lloyds TSB Group s focus is on accelerating growth by deepening its customer relationships and improving its productivity and in the process building competitive advantage through enhancing its capabilities. This has already resulted in improved earnings growth in the Lloyds TSB Group s core markets. In phase 3, the Lloyds TSB Group will look to leverage its financial strength and enhanced capabilities in new markets.

Lloyds TSB Group remains alert for opportunities to grow inorganically to complement its organic strategies and help provide new opportunities for profitable growth, both in the UK and overseas.

Markets

Lloyds TSB Group continues to focus on building competitive advantage in its core markets by seeking opportunities to consolidate its position in businesses where it is already strong, through a combination of organic growth and acquisitions, and by divesting businesses in markets where it is not a leader and cannot aspire reasonably to leadership.

Customer value

In an increasingly competitive financial services market, and with customers able to exercise choice amongst alternative providers, shareholder value creation is closely linked to customer value creation. Shareholder value can only be created by attracting and retaining customers and winning a greater share of their financial services business. Across its main businesses, Lloyds TSB Group has strong core banking franchises, but smaller market shares in associated product areas. The Lloyds TSB Group s strategy is focused on being differentiated in the creation of customer value to win a bigger share of its customers total financial services spend.

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

High performance organisation

Even the best strategies will fail to deliver shareholder value if poorly executed. Lloyds TSB Group has restructured its businesses and reinvigorated its governance and performance management processes to link plans and budgets much more closely to the highest value strategy for each business, to ensure maximum clarity and accountability for execution within all levels of its management team, and to link reward much more closely to performance.

Lloyds TSB Group measures value internally by economic profit growth, a measure of financial performance which signals unambiguously where value is being created or destroyed. It has developed a framework to be able to measure economic equity requirements across all its businesses, taking into account market, credit, insurance, business and operational risk. Economic profit is measured by applying a charge for this economic equity to post-tax earnings. Using economic profit as a key performance measure enables the Group to understand which strategies, products, channels and customer segments are destroying value and which are creating the most value and to make better strategic choices as a result.

Business and activities of Lloyds TSB Group

Lloyds TSB Group s activities are organised into three divisions: UK Retail Banking, Insurance and Investments, and Wholesale and International Banking. The main activities of Lloyds TSB Group s three divisions are described below.

UK Retail Banking

UK Retail Banking provides banking, financial services, mortgages and private banking to some 15 million personal customers through the Lloyds TSB Group s multi-channel distribution capabilities.

Branches. Lloyds TSB Group provides wide-reaching geographic branch coverage in England, Scotland and Wales, with over 2,100 branches of Lloyds TSB Bank, Lloyds TSB Scotland and Cheltenham & Gloucester as at the end of 2005.

Internet banking. Internet banking provides online banking facilities for personal customers. Some 3.7 million customers have registered to use Lloyds TSB Group s internet banking services. At the end of 2005, these customers were conducting more than 45 million transactions per month online, a 50 per cent increase on 2004.

Telephone banking. Telephone banking continues to grow and Lloyds TSB Group provides one of the largest telephone banking services in Europe. At the end of 2005, some 4.2 million customers had registered to use the services of PhoneBank and the automated voice response service, PhoneBank Express. Lloyds TSB Group s telephone banking centres handled some 69 million calls during 2005.

Cash machines. Lloyds TSB Group has one of the largest cash machine networks of any leading banking group in the UK and, at 31 December 2005, personal customers of Lloyds TSB Bank and Lloyds TSB Scotland were able to withdraw cash and check balances through some 4,200 ATMs at branches and external locations around the country. In addition, our personal customers have access to a further 54,000 cash machines via LINK in the UK and to cash machines worldwide through the VISA and MasterCard networks.

Current accounts. Lloyds TSB Bank and Lloyds TSB Scotland offer a wide range of current accounts, including interest-bearing current accounts and a range of added value accounts.

Savings accounts. Lloyds TSB Bank and Lloyds TSB Scotland offer a wide range of savings accounts and Cheltenham & Gloucester provide retail investments through their branch networks and a postal investment centre.

Personal loans. Lloyds TSB Bank and Lloyds TSB Scotland offer a range of personal loans through their branch networks and directly to the customer via the internet and telephone.

Credit cards. Lloyds TSB Group provides a range of card-based products and services, including credit and debit cards and card transaction processing services for retailers. Lloyds TSB Group is a member of both the VISA and MasterCard payment systems and has access to the American Express payment system. The Lloyds TSB Group had a 12.4 per cent share of outstanding UK credit card balances at 31 December 2005.

Mortgages. Cheltenham & Gloucester is Lloyds TSB Group s specialist residential mortgage provider, offering a range of mortgage products to personal customers through its own branches and those of Lloyds TSB Bank in England and Wales, as well as through the telephone, internet and postal service, C&G TeleDirect. Lloyds TSB Group also provides mortgages through Lloyds TSB Scotland and Scottish Widows Bank. Lloyds TSB Group is one of the largest residential mortgage lenders in the UK on the basis of outstanding balances, with mortgages outstanding at 31 December 2005 of £88,376 million, representing a market share of 9.1 per cent.

UK Wealth Management. Private Banking provides a range of tailor-made wealth management services and products to individuals from 28 offices throughout the UK. In addition to asset management, these include tax and estate planning, executor and trustee services, deposit taking, lending and insurance. Shareview Dealing provides retail stockbroking services, personal equity plan and individual savings account (ISA) products.

Insurance and Investments

Insurance and Investments offers life assurance, pensions and investment products, general insurance and fund management services.

Life assurance, pensions and investments. Scottish Widows is Lloyds TSB Group s specialist provider of life assurance, pensions and investment products, which are distributed through Lloyds TSB Bank s branch network, through independent financial advisers and directly via the telephone and the internet. The Scottish Widows brand is the main brand for new sales of Lloyds TSB Group s life, pensions, open ended investment companies and other long-term savings products.

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

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

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

General insurance. Lloyds TSB General Insurance provides general insurance through the retail branches of Lloyds TSB Bank and Cheltenham & Gloucester, and through a direct telephone operation and the internet. Lloyds TSB General Insurance is one of the leading distributors of household insurance in the UK.

Scottish Widows Investment Partnership. Scottish Widows Investment Partnership manages funds for Lloyds TSB Group s retail life, pensions and investment products. Clients also include corporate pension schemes, local authorities and other institutions in the UK and overseas.

Wholesale and International Banking

Wholesale and International Banking provides banking and related services for major UK and multinational corporates and financial institutions, and small and medium-sized UK businesses. It also provides asset finance and share registration services to personal and corporate customers, manages Lloyds TSB Group s activities in financial markets through its treasury function and provides banking and financial services overseas.

Wholesale

Corporate Markets. Combining the respective strengths of 2,700 people in Corporate Banking, Structured Finance and Financial Markets, plays an integral role in leveraging and expanding Lloyds TSB Group s customer franchise and building deep, long-lasting relationships with around 16,000 corporate customers.

Corporate Banking manages the core customer franchise, providing a relationship-based financial and advisory service to the corporate marketplace through dedicated regional teams throughout the UK and key strategic locations abroad, including New York. Customers have access to the Lloyds TSB Group s expertise and a broad range of financial solutions. The relationship managers act as a conduit to partners in Corporate Markets and other parts of the Lloyds TSB Group.

Structured Finance comprises the structured asset finance, leveraged lending and private equity and other transactional lending and structuring businesses of Corporate Markets. Structured Finance executes transactions with existing corporate customers as well as introducing new to bank relationships to the franchise.

Financial Markets provides market access to sources of liquidity, hedging tools and investment products on behalf of Lloyds TSB Group and its customers. Financial Markets also provides risk management solutions to corporate customers and structured credit and investment products to the investor community.

Registrars. Lloyds TSB Registrars, part of the Corporate Bank, operates as receiving bank and registrar to some of the UK s leading public limited companies. As market leader, it currently maintains the share registers of more than 700 clients, including around 60 per cent of the FTSE 100, managing some 22 million shareholder accounts.

Asset Finance. Lloyds TSB Group s asset finance businesses provide individuals and companies with finance through leasing, hire purchase and contract hire packages. Hire purchase, or instalment credit, is a form of consumer financing where a customer takes possession of goods on payment of an initial deposit but the legal title to the goods does not pass to the customer until the agreed number of instalments have been paid and the option to purchase has been exercised. Through its invoice discounting and factoring subsidiary, Lloyds TSB Commercial Finance, Lloyds TSB Group provides working capital finance for its customers. Specialist personal lending, store credit and the Dutton-Forshaw motor dealership group complete this group of businesses. Altogether Asset Finance has over 1.7 million individual customers and relationships with some 40,000 companies and small businesses.

Business Banking. A growing business which has relationships with some 587,000 small businesses managed by business managers based in 500 locations throughout the UK. This has been reinforced by an additional 300 business managers moving back into branches. Lloyds TSB Group has a leading share of the new business start-up market, with some 100,000 new businesses opening an account with Lloyds TSB in 2005. The main activity of The Agricultural Mortgage Corporation is to provide long-term finance to the agricultural sector.

International Banking

The Lloyds TSB Group has continued to shape its international network to support its UK operations.

Offshore banking. Lloyds TSB Group s offshore banking operations comprise offices in the UK, the Channel Islands, the Isle of Man, Hong Kong, Singapore, Malaysia and overseas representative offices in the Middle East, Africa, Asia and the Americas. The business provides a wide range of retail banking, wealth management and expatriate services to local island residents, UK expatriates, foreign nationals and to other customers requiring offshore financial services.

International private banking. Lloyds TSB Group has international private banking operations for wealthy individuals. The business is conducted through branches of Lloyds TSB Bank located in Switzerland, Luxembourg, Monaco, Gibraltar, Uruguay, Dubai and the US, supported by representative offices in Latin America.

International corporate banking. Serves the corporate and institutional market in Europe, the Middle East and Japan through offices in Belgium, the Netherlands, Spain, Dubai and Japan. Lloyds TSB Group continues to have offices in Ecuador and Uruguay which provide mainly corporate banking services. The sale of the business in Paraguay is expected to complete in 2006 after receipt of the required regulatory approval.

Material contracts

Lloyds TSB Group and its subsidiaries are party to various contracts in the ordinary course of business. In 2005, there have been no material contracts entered into outside the ordinary course of business.

Recent developments

Lloyds TSB Group issued a trading statement at its annual general meeting on 11 May 2006, which made the following comments:

In the first few months of 2006 the Group has maintained good progress in the delivery of its growth strategies. As a result, we are confident that we will deliver a satisfactory performance for the half-year.

Properties

As at 31 December 2005, Lloyds TSB Group occupied 3,370 properties in the UK. Of these, 639 were held as freeholds, 69 as long-term leaseholds and 2,662 as short-term leaseholds. The majority of these properties are retail branches, widely distributed throughout England, Scotland and Wales. Other buildings include the Lloyds TSB Group s head office in the City of London, and customer service and support properties located to suit business needs, but clustered largely in London, Birmingham, Bristol (in England), Edinburgh (in Scotland) and Cardiff and Newport (in Wales).

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

Legal actions

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

Competitive environment

Lloyds TSB Group operates in a financial services world that is experiencing consolidation at national and, to a lesser extent, international levels. The last few years have seen the beginnings of pan-European consolidation and considerable consolidation within the US.

Globalisation and developments in technology continue to expand Lloyds TSB Group s range of competitors. The rising intensity of competition is expected to put Lloyds TSB Group s margins under further pressure with many products becoming increasingly commoditised. Wholesale markets are integrating more rapidly across the European Union than their retail counterparts, leading to a deeper, more liquid, and more competitive corporate securities market, and the gradual disintermediation of traditional bank lending.

Lloyds TSB Group expects competition within the industry to continue to be based on service and relationships as well as price, particularly for core banking services. Lloyds TSB Group has significant strengths, in its portfolio of strong brands, its existing customer franchises in both retail and corporate, commercial and business banking, its multi-channel distribution capability and its knowledge and understanding of its customers.

Lloyds TSB Group s key markets are in the UK, in both the retail and corporate, commercial and business banking sectors, where the markets for basic financial and banking services are relatively mature. Retail banking markets have shown strong rates of growth in recent years, notably in consumer borrowing and mortgages, but the resultant high rates of consumer indebtedness are expected to restrain future growth. The markets for life and pensions and investment products are expected to show strong rates of growth in a number of key areas, although stock market weakness has depressed demand for some equity-based products in the recent past, and a considerable amount of uncertainty exists about the impact of regulatory change. Wholesale markets have shown strong growth recently, and cyclically low levels of bad debt. Going forward, some slowing of market growth is likely, plus a return to more normal levels of bad debt.

Lloyds TSB Group s competitors include all the major financial services and fund management companies operating in the UK. De-mutualised building societies which have become banks and life assurers which have entered the banking market have become direct competitors in the provision of banking products.

In the mortgage market, competitors include the traditional banks and building societies and new entrants to the market, with the market becoming increasingly competitive as both new entrants and incumbents endeavour to gain market share. Lloyds TSB Group s competitors in the credit card market again include both the traditional banks and new entrants, including overseas companies. In the last few years a significant share of new business has been acquired by US and new UK competitors.

In the distribution of life, pensions and investments products Lloyds TSB Group has seen increased competition from new market entrants, such as traditional retailers, primarily in specialist areas. The fragmented nature of the life, pensions and investments market in the UK has resulted in some consolidation within the sector; government regulations on product charges and competitive pressures are likely to drive further consolidation as providers seek to achieve the benefits of economies of scale. Changes to the regulation of life, pensions and investment products are expected to favour distributors, including banks, rather than product providers, although the impact of the recent government sponsored Turner Report findings is not clear.

In the general insurance sector, the market has seen significant consolidation amongst underwriters but continued fragmentation in distribution and an increasing number of new market entrants including both overseas insurers and direct operators.

In commercial and corporate markets, margins are typically finer than in retail, but probably under less overall downward pressure. Nevertheless, traditional forms of bank finance face increasing competition from market-based products as companies increasingly access those markets directly.

In addition to the challenging competitive environment, in the UK and elsewhere, there is continuing political, regulatory and competition scrutiny of banking and, in particular, retail banking.

In the UK, the Office of Fair Trading (OFT) is carrying out several inquiries:

In April 2006, the OFT launched a market study on payment protection insurance (PPI), following a super complaint submitted by the Citizens Advice Bureau in September 2005. The OFT expects to publish its report by the end of 2006.

The OFT has carried out investigations into Visa and MasterCard credit card interchange rates. In the MasterCard interchange case, the OFT decision is being appealed by MasterCard to the Competition Appeals Tribunal and the appeal is expected to be heard towards the end of 2006. The OFT s investigation in the Visa interchange case is at an earlier stage.

Following discussions with the industry, in April 2006 the OFT issued a statement on default charges in credit card contracts. In this the OFT state that it will not challenge default charges set below £12. This is lower than the current level charged by Lloyds TSB Group and most other card issuers. Lloyds TSB Group does not agree with the OFT s interpretation of the law, but has written to the OFT to confirm that it will be reducing its credit card charges to £12 from 29 June 2006.

In addition to its comments on credit cards, the OFT statement also suggested the same principles should apply to some other consumer contracts such as those for store cards, mortgages and bank accounts. So far as Lloyds TSB Group is aware these matters have not been previously discussed with the industry by the OFT. Lloyds TSB Group has informed the OFT that it strongly disagrees that these principles are applicable to current account charges.

The Competition Commission inquiry in 2002 into the supply of banking services to small and medium-sized enterprises (SMEs), resulted in a number of banks, including Lloyds TSB Group, giving certain undertakings to the OFT.The OFT announced in January 2006 that it would be reviewing these undertakings. The OFT is expected to commence that review in the second quarter of 2006 and anticipates that it will take nine months to complete. Lloyds TSB Group will cooperate fully with that review.

There is a continuing market study by the OFT into payments systems, with the OFT chairing a Payments Systems Task Force. This was established in 2004 to look at competition issues relating to payments systems over a four year period. In December 2005, the OFT welcomed proposals for reducing the clearing times for electronic banking payments. Lloyds TSB Group will continue to co-operate with the Task Force.

In addition, in June 2005, the European Union (EU) announced an inquiry into retail banking. The inquiry will cover the 25 Member states and will be executed in a phased approach. The inquiry is focusing on payment cards, retail banking (including SME banking) and business insurance in Europe generally. Lloyds TSB Group is co-operating with the inquiry and the outcome is unclear, though the European Commission has recently published a preliminary report on payment cards for consultation.

These investigations and any connected matters are likely to affect the industry and have an impact on the Lloyds TSB Group s business. Lloyds TSB Group is considering actions to mitigate any financial impact. The net effect from a product and cost/income perspective is currently under consideration, however, the Lloyds TSB Group is presently unable to quantify with any reasonable certainty the aggregate cost or income implications in relation to the above enquiries.

OPERATING AND FINANCIAL REVIEW AND PROSPECTS

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

The following discussion is based on and should be read in conjunction with the Consolidated Financial Statements and the related notes thereto included elsewhere in this annual report. For a discussion of the accounting policies used in the preparation of the Consolidated Financial Statements, see Accounting policies in note 1 to the Consolidated Financial Statements. The Consolidated Financial Statements are prepared in accordance with IFRS, which varies in certain significant respects from US GAAP. A discussion of such differences and a reconciliation of certain IFRS amounts to US GAAP is included in note 56 to the Consolidated Financial Statements. Certain information for years prior to 2004 has been prepared under UK GAAP, which is not comparable with IFRS.

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Overview and trend information

Lloyds TSB Group has operations in both the UK and overseas; however, its earnings are heavily dependent upon its domestic activities and in 2005 substantially all of Lloyds TSB Group s profit before tax was derived from its UK operations. The state of the UK economy, therefore, has significant implications for the way in which Lloyds TSB Group runs its business and its performance.

After slowing to growth of around 1.7 per cent in 2005, the UK economy is expected to recover to around 2.0 per cent to 2.5 per cent in 2006. Global economic growth is expected to remain robust and domestic consumer spending growth should gradually improve after a period of unchanged interest rates which has stabilised the UK housing market. The pace of recovery is likely to remain restrained, however, as unemployment has started to rise gradually. Increasing global economic imbalances indicate some risks around this outcome however, although continuing low inflation and the sound state of public finances in the UK suggest that the UK economy is well positioned to resist any sudden deterioration in the external environment.

Against this economic backdrop, there has been continued growth in each of Lloyds TSB Group s three divisions: UK Retail Banking, as a result of strong growth in mortgage and customer deposit balances with costs remaining tightly controlled, although impairment charges rose significantly reflecting a marketwide deterioration in retail credit quality as a result of more customers, with higher levels of indebtedness, experiencing repayment difficulties; Insurance and Investments, as a result of increased weighted sales through both the Independent Financial Adviser and bancassurance distribution channels and an increase in the life and pensions new business margin; and Wholesale and International Banking, which has seen significant progress in delivering the strategy to build an integrated wholesale bank for corporate markets, and good levels of new business growth in Business Banking and Asset Finance.

Critical accounting policies

The preparation of financial statements requires management to make estimates and assumptions that affect amounts reported therein. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be based upon amounts which differ from those estimates.

The accounting policies that are deemed critical to the Lloyds TSB Group s results and financial position, based upon materiality and significant judgements and estimates, are discussed in note 2 to the Consolidated Financial Statements.

Results of operations 2005 compared with 2004

The Lloyds TSB Group has applied IFRS as adopted by the European Union (EU) in its financial statements for the year ended 31 December 2005. IFRSs as adopted by the EU are identical in all respects to the current IFRSs as issued by the IASB, except for the EU s amendment to IAS 39. The Lloyds TSB Group has not taken advantage of the EU s amendment to IAS 39; accordingly, there would be no change to the reported income or equity if Lloyds TSB Group were to adopt fully the current IFRSs as issued by the IASB. The rules for first time adoption of IFRS require the application of certain exceptions and permit certain other transition exemptions; further information is provided on page F-8. The application of these exceptions and exemptions means that the 2004 figures disclosed are not fully comparable with those presented in respect of 2005.

The adoption of IAS 32, IAS 39 and IFRS 4 with effect from 1 January 2005 has also resulted in certain classifications being appropriate for only 2004 or 2005; in order to provide a more meaningful presentation, and to differentiate from a nil balance, shading has been used where a caption is not relevant for a particular year.

Summary

	2005 **£m**	2004 £m
Net interest income	**5,671**	5,110
Other income	**17,055**	14,173
Total income	**22,726**	19,283
Insurance claims	**(12,186)**	(9,622)
Total income, net of insurance claims	**10,540**	9,661
Operating expenses	**(5,471)**	(5,297)
Trading surplus	**5,069**	4,364
Impairment losses on loans and advances	**(1,299)**	(866)
Profit(loss) on sale and closure of businesses	**50**	(21)
Profit before tax	**3,820**	3,477
Taxation	**(1,265)**	(1,018)
Profit for the year	**2,555**	2,459
Profit attributable to minority interests	**62**	67
Profit attributable to equity shareholders	**2,493**	2,392
Profit for the year	**2,555**	2,459
Economic profit[1]	**1,616**	1,448

[1] Lloyds TSB Group defines economic profit as the earnings on the equity invested in the business less a notional charge for the cost of the equity invested in that business. See Operating and financial review and prospects Economic profit .

In 2005 the Lloyds TSB Group s profit before tax was £3,820 million, an increase of £343 million, or 10 per cent, compared to £3,477 million in 2004. Profit attributable to shareholders was £101 million, or 4 per cent, higher at £2,493 million compared to £2,392 million in 2004. Earnings per share were 44.6p compared to 42.8p in 2004, an increase of 4 per cent.

Net interest income was £561 million, or 11 per cent, higher at £5,671 million compared to £5,110 million in 2004. The international accounting standards implemented with effect from 1 January 2005 have had a marked effect on the Lloyds TSB Group s net interest income as certain amounts previously accounted for within fees receivable and administrative expenses are now included within the effective interest rate calculations. Adjusting for this effect, underlying net interest income was £403 million, or 8 per cent, higher. Average interest-earning assets increased as a result of continued strong lending growth, particularly in respect of mortgages, personal loans and credit cards as well as corporate lending and asset finance. The Lloyds TSB Group s net interest margin fell by 10 basis points to 2.62 per cent; however if the impact of the accounting standards applied with effect from 1 January 2005 and the growth in reverse repurchase agreement balances are excluded, the underlying net interest margin was 2.82 per cent in 2005, compared to 2.86 per cent in 2004; a fall of 4 basis points. This fall in the underlying margin reflected competitive pressures in both the personal and corporate lending books.

Other income, at £17,055 million, was £2,882 million, or 20 per cent, higher than £14,173 million in 2004. Fees and commissions receivable were £64 million, or 2 per cent, lower at £2,990 million; however, if the effect of the accounting standards applied with effect from 1 January 2005 are excluded, underlying fees and commissions receivable were £261 million, or 9 per cent, higher at £3,315 million compared to £3,054 million in 2004. The increase in underlying fee income reflects good growth in current account fees, mortgage and other lending fees and wealth management products. Fees and commissions payable, again excluding the impact of the accounting standards applied with effect from 1 January 2005, were £74 million higher, largely as a result of increased volumes within Scottish Widows. Net trading income was £4,262 million higher, principally within the insurance and investment businesses, and insurance premium income (excluding the impact of the accounting standards applied with effect from 1 January 2005) was £1,131 million higher. These increases reflect substantial inflows of funds from policyholders and strong investment gains over the year; this income, however, is largely for the benefit of policyholders and is matched by the commensurate increase in insurance claims.

Insurance claims, at £12,186 million, were £2,564 million, or 27 per cent, higher than £9,622 million in 2004. The impact of the accounting standards applied with effect from 1 January 2005 in respect of the insurance businesses caused a significant reduction in both the premium income and claims figures, as a large number of insurance products were reclassified as investment products. Adjusting for this effect, underlying insurance claims were £5,172 million, or 54 per cent, higher at £14,794 million compared to £9,622 million in 2004.

Operating expenses were £174 million, or 3 per cent, higher at £5,471 million compared to £5,297 million in 2004. Staff costs were £151 million, or 6 per cent, higher reflecting annual pay awards, increased bonus and incentive payments in certain areas as a result of business success and increased severance costs in relation to rationalisation programmes. Staff numbers, on a full time equivalent basis, decreased by 3,188 to 66,797 at 31 December 2005 compared to 69,985 at 31 December 2004; however, much of this fall occurred towards the end of the year and consequently there was little impact on staff costs. Premises and equipment costs were £35 million higher. Other costs were £19 million lower; an increase of £38 million in the charge in respect of provisions for customer redress, following a review of the expected cost by the Lloyds TSB Group, was more than offset by a net credit of £45 million in respect of deferred acquisition costs within the insurance businesses.

Impairment losses on loans and advances, at £1,299 million, were £433 million, or 50 per cent, higher than 2004. Excluding the impact of the accounting standards applied with effect from 1 January 2005 and a small release of £3 million from other credit risk provisions, underlying impairment losses on loans and advances were £227 million, or 26 per cent, higher at £1,093 million in 2005 compared to £866 million in 2004. The overall charge in respect of Wholesale and International Banking was little changed with the majority of the increase arising within UK Retail Banking. The underlying impairment charge in UK Retail Banking was £229 million higher as a result of volume growth in both personal loans and credit card lending, the absence of a mortgage related provision release which in 2004 totalled £39 million, and the impact of more customers with higher levels of indebtedness experiencing repayment difficulties.

A net profit of £50 million arose on the sale and closure of businesses in 2005, principally as a result of the disposal of the Goldfish credit card portfolios, compared to a loss of £21 million in 2004, which largely reflected the sale of the Lloyds TSB Group s businesses in Argentina and Colombia.

The tax charge, at £1,265 million, represented 33.1 per cent of profit before tax compared to 29.3 per cent in 2004; the increase in the effective tax rate largely reflects the IFRS requirement to include, within the tax charge, tax attributable to UK life insurance policyholder earnings and interests in Open Ended Investment Companies (OEICs).

At the end of 2005, the total capital ratio was 10.9 per cent. Risk-weighted assets increased by £13,091 million, or 10 per cent, since the beginning of 2005 to £144,921 million at the end of the year; this increase reflected new mortgage and other personal lending together with substantial growth in corporate, SME, asset finance and structured finance lending. Total assets grew by £25,332 million, or 9 per cent, to £309,754 million compared to £284,422 million at 31 December 2004. Of this growth, £9,649 million was due to the grossing-up of balances no longer eligible for set-off following the implementation of IAS 32 with effect from 1 January 2005. The remaining increase of £15,683 million was due to the lending growth and higher securities balances within the long-term insurance business.

Net interest income

	2005	2004
Net interest income £m	**5,671**	5,110
Average interest-earning assets £m	**216,153**	187,643
Average rates:		
Gross yield on interest-earning assets %	**5.82**	5.71
Interest spread %	**2.40**	2.50
Net interest margin %	**2.62**	2.72
Margin excluding average balances held under reverse repurchase agreements [4]:		
Net interest income £m	**5,671**	5,110
Average interest-earning assets £m	**201,813**	178,887
Net interest margin %	**2.81**	2.86

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

2 Interest spread is the difference between the rate of interest earned on average interest-earning assets and the rate of interest paid on average interest-bearing liabilities.

3 The net interest margin represents the interest spread together with the contribution of interest-free liabilities. It is calculated by expressing net interest income as a percentage of average interest-earning assets.

4 Comparisons of net interest income and margins are impacted by the holdings of fine margin reverse repurchase agreements. To improve comparability, figures are also shown excluding average balances held under reverse repurchase agreements (2005: £14,340 million; 2004: £8,756 million)

Net interest income increased by £561 million, or 11 per cent, to £5,671 million compared to £5,110 million in 2004. However, net interest income is impacted by the accounting standards applied with effect from 1 January 2005 and adjusting for this, net interest income was £403 million, or 8 per cent, higher at £5,513 million compared to £5,110 million in 2004.

Average interest-earning assets grew by £28,510 million, or 15 per cent, to £216,153 million in 2005 compared to £187,643 million in 2004. However, comparisons are distorted by the substantial growth, during 2004 and 2005, in assets held under reverse repurchase agreements for liquidity purposes. Excluding the balances held under reverse repurchase agreements, average interest-earning assets grew by £22,926 million, of which the grossing-up of balances subject to set-off arrangements in 2005 following the implementation of IAS 32 accounted for £6,396 million. The underlying growth in average interest-earning assets was therefore £16,530 million, or 9 per cent, adding £475 million to net interest income. Good levels of consumer lending growth increased average personal lending and credit card balances by £1,691 million and average mortgage balances by £7,808 million. Average interest-earning assets within the insurance and investment businesses, which include policyholder and long-term fund balances, increased by £1,891 million as a result of business growth and increased fund activity. Strong lending growth lead to an increase of £4,373 million in average interest-earning assets in the Business Banking and Corporate Markets franchises and average balances in Asset Finance were £484 million higher, reflecting the full year impact of lending growth over 2004.

The Lloyds TSB Group s net interest margin fell by 10 basis points to 2.62 per cent in 2005, compared to 2.72 per cent in 2004; if the average balances held under reverse repurchase agreements are excluded from both years, the margin in 2005 was 5 basis points lower at 2.81 per cent compared to 2.86 per cent in 2004. After taking into account the impact of the accounting standards applied with effect from 1 January 2005 the underlying margin fell by 4 basis points reducing net interest income by £72 million. The underlying net interest margin in UK Retail Banking was 23 basis points lower, as a result of competitive pressures and a reduced benefit from current account funding balances. Within Wholesale and International Banking the underlying net interest margin was 5 basis points higher. On this basis, margins on treasury balances improved, as a result of a change in mix; the margin in Structured Finance improved as a result of the impact of new transactions; Corporate Banking margins were lower, as a result of competitive pressures on new lending balances; and margins were also down in Business Banking.

Other income

	2005 £m	2004 £m
Fees and commissions receivable:		
UK current account fees	**593**	637
Other UK fees and commissions	**1,041**	1,087
Insurance broking	**681**	672
Card services	**545**	520
International fees and commissions	**130**	138
	2,990	3,054
Fees and commissions payable	**(842)**	(844)
Net trading income	**9,298**	5,036
Insurance premium income	**4,469**	6,070
Other operating income	**1,140**	857
Total other income	**17,055**	14,173

Other income was £2,882 million, or 20 per cent, higher at £17,055 million compared to £14,173 million in 2004.

Fees and commissions receivable were £64 million, or 2 per cent, lower at £2,990 million compared to £3,054 million in 2004. However, year-on-year comparisons are affected by the impact of IAS 39, which has been applied with effect from 1 January 2005 and has resulted in some £325 million of income previously classified within fees and commissions now being included within net interest income via the effective interest rate calculations. Adjusting for this, underlying fees and commissions receivable were £261 million, or 9 per cent, higher at £3,315 million compared to £3,054 million in 2004. Underlying UK current account fees were £117 million higher reflecting continuing growth in added value account products, the impact of pricing reviews in 2004 and 2005 and increased charges in respect of returned cheques and unauthorised borrowings. Also on this underlying basis, other UK fees and commissions were up £114 million, or 10 per cent, at £1,201 million compared to £1,087 million in 2004, reflecting increased levels of mortgage-related fees, increased wealth management fees as a result of higher sales and improved retention rates and increased levels of corporate lending and other fees. Insurance broking income was £9 million, or 1 per cent, higher at £681 million, compared to £672 million in 2004, as lower levels of loan protection income were more than offset by increased income in respect of motor insurance and retrospective commissions. Fees for card services were £25 million higher as a result of increased volumes and some tariff changes.

Fees and commissions payable were £2 million lower at £842 million compared to £844 million in 2004; however, adjusting for fees payable of £76 million included within the effective interest rate calculations in 2005, underlying fees payable were £74 million, or 9 per cent, higher at £918 million compared to £844 million in 2004. The impact of increased business and trading volumes within Scottish Widows more than offset the lower level of dealership commissions within Asset Finance as a result of reduced new business levels.

Net trading income increased by £4,262 million, or 85 per cent, to £9,298 million compared to £5,036 million in 2004. The majority of this increase is attributable to the insurance businesses and reflects significant trading gains on policyholder investments over the year, which are largely matched by an increase in claims expense.

Insurance premium income was £1,601 million, or 26 per cent, lower at £4,469 million compared to £6,070 million in 2004. However, year-on-year comparisons are affected by the impact of IFRS 4, which has caused a significant proportion of contracts to be reclassified as investment products with effect from 1 January 2005. Adjusting for this, underlying insurance premium income was £1,131 million, or 19 per cent, higher at £7,201 million in 2005. Long-term insurance income grew substantially as a result of strong sales through the bancassurance and independent financial advisor channels; however general insurance premium income was little changed as growth in creditor insurance income was largely offset by reduced levels of health insurance premiums.

Other operating income was £283 million, or 33 per cent, higher at £1,140 million compared to £857 million in 2004; excluding the impact of accounting standards applied with effect from 1 January 2005, underlying other operating income was £139 million, or 16 per cent, higher in 2005. Income from investment properties was £114 million higher, in part reflecting portfolio growth, and there were increased gains from the sale and leaseback of premises.

Operating expenses

	2005 £m	2004 £m
Administrative expenses:		
Staff:		
Salaries	**2,068**	1,970
National insurance	**154**	144
Pensions	**308**	307
Other staff costs	**325**	283
	2,855	2,704
Premises and equipment:		
Rent and rates	**305**	294
Hire of equipment	**13**	17
Repairs and maintenance	**136**	129
Other	**152**	131
	606	571
Other expenses:		
Communications and external data processing	**467**	449
Advertising and promotion	**207**	205
Professional fees	**216**	223
Provisions for customer redress	**150**	112
Other	**325**	395
	1,365	1,384
Administrative expenses	**4,826**	4,659
Depreciation	**639**	638
Impairment of goodwill	**6**	
Total operating expenses	**5,471**	5,297
Cost: income ratio (%)*	**51.9**	54.8

* Total operating expenses divided by total income, net of insurance claims

2005 compared with 2004

Operating expenses were £174 million, or 3 per cent, higher at £5,471 million compared to £5,297 million in 2004.

Staff costs were £151 million, or 6 per cent, higher at £2,855 million compared to £2,704 million in 2004. Salaries were £98 million higher at £2,068 million reflecting annual pay awards and an increase in levels of bonus and incentive payments in some parts of the Lloyds TSB Group. A reduction in overall staff numbers had little impact upon costs as this was biased towards the end of the year. National insurance costs were £10 million higher, reflecting the increase in salary costs, but pension costs were largely unchanged as a decrease in the charge in respect of defined benefit schemes was offset by an increase in cash payments to defined contribution schemes. Other staff costs were £42 million higher as decreases in agency and other costs were more than offset by an increase in severance charges, reflecting rationalisation programmes in a number of parts of the Lloyds TSB Group.

Premises and equipment costs were £35 million, or 6 per cent, higher at £606 million compared to £571 million in 2004. Rent and rates were £11 million higher as a result of general increases in property rental charges and a higher level of costs in relation to the expanding investment property portfolios within the insurance operations. A small decrease in equipment hire charges resulted from a favourable renegotiation of certain contracts, but this has been more than offset by increased repairs and maintenance expenditure, in particular in relation to ATM s and network costs. Other premises and equipment costs were £21 million higher as a result of increased energy costs and other increased costs in relation to the investment property portfolios.

Other expenses were £19 million, or 1 per cent, lower at £1,365 million compared to £1,384 million in 2004. Communications and external data processing costs were £18 million higher as a result of increased network charges. Advertising costs were little changed at £207 million and professional fees were £7 million lower, reflecting some reduction in consultancy charges. The charge of £150 million in 2005 in respect of provisions for customer redress (£38 million higher than the £112 million charge in 2004) follows a review by the Lloyds TSB Group of the estimated cost of redress payments to customers, principally relating to past sales of mortgage endowment policies through the branch network. This review took in to account the introduction of time barring and the consequent increase in claims. Other costs were £70 million lower at £325 million. Much of this decrease reflected a credit of £45 million representing the net movement in deferred acquisition costs relating to the insurance businesses, the accounting for which has changed as a result of the prospective IFRS accounting changes applied with effect from 1 January 2005. There were efficiency savings in stationery and other administrative costs and costs were also lower following the sale of certain Latin American businesses towards the end of 2004.

The depreciation charge was little changed at £639 million as a small reduction in the charge in respect of operating lease assets was offset by the effect of general portfolio growth in relation to own-use assets. There was a goodwill impairment charge in relation to an acquisition made in earlier years.

The cost:income ratio improved to 51.9 per cent in 2005 compared to 54.8 per cent in 2004.

Impairment losses on loans and advances

	2005 **£m**	2004 £m
Impairment losses on loans and advances	**1,302**	866
Other credit risk provisions	**(3)**	
Impairment losses on loans and advances and other credit risk provisions	**1,299**	866

Impairment losses on loans and advances	**2005** **£m**	2004 £m
UK Retail Banking	**1,111**	676
Insurance and Investments		(3)
Wholesale and International Banking	**191**	193
Total charge for impairment losses on loans and advances	**1,302**	866
Charge as % of average lending:	**%**	%
- Total charge	**0.76**	0.59
- Total charge, excluding impact of IAS 39	**0.66**	0.59

The impairment charge in respect of loans and advances and other credit risk provisions was £433 million, or 50%, higher at £1,299 million compared to £866 million in 2004. This represents a charge in respect of loans and advances of £1,302 million slightly offset by a release of £3 million from provisions held in respect of contingent liabilities and commitments.

The impairment charge in respect of loans and advances in 2005 was significantly affected by the adoption of the requirements of IAS 39 with effect from 1 January 2005. IAS 39 requires the impairment provision to be calculated by comparing the carrying value of the loan with the discounted value of future cashflows. As a result, in circumstances where a customer s borrowings have been rescheduled onto a concessionary rate which is below market interest rate, an impairment allowance will be required even where full recovery of the principal is anticipated; this had the effect of increasing the 2005 charge by £209 million.

Excluding this effect, underlying impairment losses on loans and advances in 2005 totalled £1,093 million, £227 million or 26 per cent higher than £866 million in 2004.

The underlying charge in UK Retail Banking rose by £229 million, or 34 per cent, to £905 million in 2005. The charges in respect of personal loans and overdrafts and credit cards increased by £112 million and £65 million respectively as a result of volume growth and some deterioration in credit quality as increasing numbers of customers are experiencing repayment difficulties. There was a charge of £13 million in respect of the mortgage portfolio, compared to a release of £39 million in 2004.

The underlying charge in Wholesale and International Banking was £188 million compared to £193 million in 2004. The underlying charge within Corporate Markets was £91 million lower as a result of lower new provisions and maintaining a good level of recoveries; this was partially offset by higher charges in Asset Finance. The charge within Business Banking, which deals with small business customers, was little changed. Within International Banking, there was a credit of £15 million in 2005 compared to a credit of £39 million in 2004; both years benefited from good recoveries in Latin America although 2004 also benefited from a release of £30 million from the Lloyds TSB Group s centrally held provision in respect of exposures in Argentina.

Overall, the Lloyds TSB Group s charge in respect of impairment losses on loans and advances expressed as a percentage of average lending increased to 0.76 per cent compared to 0.59 per cent in 2004; although excluding the impact of IAS 39 the charge represented 0.66 per cent of average lending in 2005.

Taxation

	2005	2004
	£m	£m
UK corporation tax:		
Current tax on profits for the year	**862**	759
Adjustments in respect of prior years	**(20)**	(69)
	842	690
Double taxation relief	**(138)**	(57)
	704	633
Foreign tax:		
Current tax on profits for the year	**78**	118
Adjustments in respect of prior years	**(8)**	(2)
	70	116
Current tax charge	**774**	749
Deferred tax	**491**	269
Total charge	**1,265**	1,018

The rate of tax is influenced by the geographic and business mix of profits. The effective rate of tax in 2005 was 33.1 per cent, compared to an effective rate of tax in 2004 of 29.3 per cent and the corporation tax rate in 2005 of 30 per cent. The effective tax rate is distorted by the requirement to include, within the income tax expense, policyholders tax and Open Ended Investment Company interests of £318 million (2004: £47 million); excluding these the effective tax rate in 2005 was 27.0 per cent compared to 28.3 per cent in 2004. The reduced effective tax rate in 2005 on this adjusted basis was primarily due to tax benefits arising on disposal and other gains. Lloyds TSB Group does not expect the tax rate, excluding the impact of policyholders tax and Open Ended Investment Company interests, to vary significantly from the average UK corporation tax rate.

Economic profit

In pursuit of the Group s aim to maximise shareholder value over time, management has for a number of years used a system of value based management as a framework to identify and measure value creation. Management uses economic profit, a non-GAAP measure, as a measure of performance, and believes that it provides important information for investors, because it captures both growth in investment and return; profit before tax is the comparable GAAP measure used by management. Lloyds TSB Group defines economic profit as the earnings on the equity invested in the business less a notional charge for the cost of the equity invested in that business.

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

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

The table below summarises Lloyds TSB Group s calculation of economic profit for the years indicated.

	2005	2004
	£m	£m

Average shareholders equity	**9,747**	10,493
Profit attributable to equity shareholders	**2,493**	2,392
Less: notional charge	**(877)**	(944)
Economic profit	**1,616**	1,448

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

Economic profit increased to £1,616 million in 2005 compared to £1,448 million in 2004. Profit attributable to equity shareholders increased by £101 million, or 4 per cent, to £2,493 million; the notional charge on average equity, however, was £67 million lower, as a result of a 7 per cent decrease in average equity to £9,747 million compared to £10,493 million in 2004. The decrease in average equity primarily reflects the decrease of £1,558 million arising from the implementation of IAS 32, IAS 39 and IFRS 4 with effect from 1 January 2005.

Line of business information

Summary

The impact of IFRS, and in particular the increased use of fair values, has resulted in greater earnings volatility. In order to provide a more comparable representation of business performance this volatility has been separately analysed from the results of the individual business units. The results of the businesses are set out below:

	2005 **£m**	2004 £m
UK Retail Banking	**1,394**	1,639
Insurance and Investments	**725**	778
Wholesale and International Banking	**1,518**	1,272
Central group items	**(442)**	(350)
Profit before tax, excluding volatility	**3,195**	3,339
Volatility	**625**	138
Profit before tax	**3,820**	3,477

Comparative figures for 2004 have been restated to reflect the adoption of those IFRS standards which are required to be applied retrospectively, but do not reflect the additional impacts arising from first time application of IAS 32 Financial Instruments: Disclosure and Presentation , IAS 39 Financial Instruments: Recognition and Measurement and IFRS 4 Insurance Contracts (including UK Financial Reporting Standard 27 Life Assurance), which have been implemented with effect from 1 January 2005, with the opening balance sheet at that date adjusted accordingly.

UK Retail Banking

	2005 **£m**	2004 £m
Net interest income	**3,521**	3,228
Other income	**1,605**	1,696
Total income	**5,126**	4,924
Operating expenses	**(2,697)**	(2,609)
Trading surplus	**2,429**	2,315
Impairment losses on loans and advances	**(1,111)**	(676)
Profit on sale of businesses	**76**	
Profit before tax	**1,394**	1,639
Cost:income ratio	**52.6%**	53.0%
Total assets (year-end)*	**£103,930m**	£96,472m
Total risk-weighted assets (year-end)*	**£ 60,582m**	£57,241m

* To ensure comparability, prior year asset and risk-weighted asset figures are shown as at 1 January 2005, following implementation of those international accounting standards for which restated comparatives are not required.

Profit before tax from UK Retail Banking decreased by £245 million, or 15 per cent, to £1,394 million, compared to £1,639 million in 2004. However, comparisons of performance are affected by the impact of the accounting standards implemented with effect from 1 January 2005, which has reduced the profit of UK Retail Banking in 2005 by £213 million; excluding this profit before tax was £1,607 million in 2005 which was £32 million, or 2 per cent, lower than 2004.

Net interest income was £293 million, or 9 per cent, higher at £3,521 million compared to £3,228 million; excluding the impact of IAS 39 which was implemented with effect from 1 January 2005, net interest income was £79 million, or 2 per cent, higher at £3,307 million. During 2005, good levels of growth were achieved in all key product areas. Gross new mortgage lending for the Group totalled £25,979 million; net new lending totalled £8,311 million resulting in a market share of net new lending of 9.1 per cent, and mortgage balances outstanding increased by 10 per cent to £88,376 million. Personal loan balances outstanding at the year-end were £11,023 million, an increase of 3 per cent and credit card balances totalled £7,209 million, an increase of 9 per cent, after adjusting to exclude the effect of the Goldfish disposal. Credit balances on current accounts and savings and investment accounts increased by 7 per cent. The benefit of this volume growth was, however, partly offset by reduced margins on mortgages and personal loans, as a result of competitive pressures.

Other income was £91 million, or 5 per cent, lower at £1,605 million compared to £1,696 million in 2004; however, excluding the effect of those accounting standards applied with effect from 1 January 2005 other income was £115 million, or 7 per cent, higher at £1,811 million. This increase in underlying other income reflects growth in current accounts fees, due to the continuing success of added-value accounts and the benefit of tariff reviews; increased card fee income, particularly in relation to overseas-use charges; and income from the successful new wealth management products.

Operating expenses were £88 million, or 3 per cent, higher at £2,697 million. Of this increase, £50 million is as a result of an increased charge in respect of customer redress, mainly relating to past sales of endowment products through the branch network, following a review by the Lloyds TSB Group of the expected total cost, in the light of the introduction of time-barring and a consequent increase in claims. Underlying operating expenses remain well controlled with the residual increase being largely attributable to higher levels of restructuring costs as back office operations continue to be rationalised.

Impairment losses on loans and advances, at £1,111 million, were £435 million or 64 per cent higher than 2004. The impact of the accounting standards applied with effect from 1 January 2005 accounted for £206 million of this increase; excluding this underlying impairment losses were £229 million, or 34 per cent, higher at £905 million in 2005. The charge in respect of personal loans, overdrafts and credit cards increased as a result of volume growth over recent years as well as some deterioration in credit quality as increasing numbers of customers, with higher levels of indebtedness, are experiencing repayment difficulties. Within the mortgage business there continued to be a low level of losses and as a result the impairment charge was £13 million, compared to a release of £39 million in 2004. Cheltenham & Gloucester (C&G) continued to focus on prime lending market segments during 2005. The average indexed loan-to-value ratio for C&G new mortgages and further advances written during 2005 was 64 per cent. At 31 December 2005, 95 per cent of C&G mortgage balances had an indexed loan-to-value ratio of less than 85 per cent and only 0.6 per cent of balances had an indexed loan-to-value ratio in excess of 95 per cent.

A profit of £76 million arose in 2005 on the disposal of the Goldfish credit card business.

Insurance and Investments

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

	2005 £m	2004 £m
Net interest income	**389**	283
Other income	**13,116**	10,736
Total income	**13,505**	11,019
Insurance claims	**(12,186)**	(9,622)
Total income, net of insurance claims	**1,319**	1,397
Operating expenses	**(594)**	(622)
Trading surplus	**725**	775
Impairment losses on loans and advances - credit		3
Profit before tax, excluding volatility	**725**	778
Volatility	**749**	138
Profit before tax	**1,474**	916
Analysis by area of business of profit before tax, excluding volatility		
Life, pensions and OEIC s	**500**	598
General insurance	**209**	172
Scottish Widows Investment Partnership	**16**	8
Profit before tax, excluding volatility	**725**	778

2005 compared to 2004

Profit before tax from the Lloyds TSB Group s Insurance and Investments businesses was £1,474 million which was £558 million, or 61 per cent, higher than £916 million in 2004. However, much of this increase is due to volatility arising from market movements (see Operating and financial review and prospects Line of business information Volatility) and profit before tax excluding volatility was £53 million, or 7 per cent, lower at £725 million compared to £778 million in 2004. The 2005 results were reduced by a provision of £155 million for the strengthening of mortality reserves. The impact of the new accounting standards applied with effect from 1 January 2005 has been to reduce profit before tax, excluding volatility, by £73 million; excluding this effect profit before tax was £20 million, or 3 per cent, higher at £798 million compared to £778 million in 2004.

Net interest income, excluding volatility, was £106 million, or 37 per cent, higher at £389 million compared to £283 million in 2004. This increase reflected higher average levels of cash deposit investments in long-term business and policyholder funds.

Other income, excluding volatility, was £2,380 million, or 22 per cent, higher at £13,116 million compared to £10,736 million in 2004. One of the impacts of the application of IFRS 4 with effect from 1 January 2005 has been the need to reclassify as investment contracts certain transactions that were previously treated as insurance contracts. This has resulted in a decrease in other income largely offset by a decrease in insurance claims. Adjusting for this effect, underlying other income in 2005 was £15,820 million which was £5,084 million, or 47 per cent, higher than £10,736 million in 2004. This increase in underlying other income is principally due to a £1,131 million increase in insurance premium income, reflecting improved sales and increased policyholder activity, together with a £3,728 million increase in net trading income. Net trading income represents the realised and unrealised gains on investments held in the long-term funds, together with the interest and dividend income on those investments and the significant increase in 2005 reflects improved market returns.

The increase in premium income and trading income are largely offset by a matching increase in insurance claims, reflecting the fact that the majority of the premium inflows and investment gains are for the benefit of policyholders. Insurance claims were £2,564 million, or 27 per cent, higher at £12,186 million in 2005 compared to £9,622 million in 2004. If the 1 January 2005 reclassifications to investment contracts, described above, are excluded underlying insurance claims were £5,172 million, or 54 per cent, higher at £14,794 million in 2005, compared to £9,622 million in 2004.

Operating expenses reduced by £28 million, or 5 per cent, from £622 million in 2004 to £594 million in 2005. This decrease reflects the absence of a charge in respect of customer redress (£12 million in 2004) and a net credit in respect of deferred acquisition costs of £45 million in 2005, following the adoption of IFRS 4 with effect from 1 January 2005. Adjusting for these items, underlying operating expenses were £639 million in 2005, £29 million or 5 per cent higher than £610 million in 2004. This underlying increase in operating expenses reflected increased business volumes and some targeted project expenditure.

The profits of the life, pensions and OEIC s business and the General insurance business are discussed further below.

Life, pensions and OEICs

The table below shows the level of new business premiums for the life and pensions business and OEIC sales. Management monitor these figures because they provide an indication of both the performance and the profitability of the business.

	2005 £m	2004 £m
New business and OEIC sales		
Regular premiums	**356**	343
Single premiums	**3,982**	3,141
OEIC s		
Regular premiums	**33**	33
Single premiums	**1,148**	538
Total OEIC s	**1,181**	571

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

	2005 £m	2004 £m
Weighted sales (regular + 1/10 single):		
Life and pensions	**754**	657
OEICs	**148**	86
Life, pensions and OEICs	**902**	743
Weighted sales by distribution channel:		
Bancassurance	**274**	242
Independent financial advisers	**562**	432
Direct	**66**	69
Life, pensions and OEICs	**902**	743

Overall, weighted sales in 2005 increased by 21 per cent to £902 million and as a result the Lloyds TSB Group s life, pensions and investments market share increased significantly to 6.0 per cent, compared with 5.7 per cent in 2004. New business regular premiums were £13 million, or 4 per cent, higher at £356 million compared to £343 million in 2004. Strong growth in sales of pension products, as a result of more focussed marketing, more than offset lower life protection sales, resulting from the slow down in the housing market. Single premium new business sales were £841 million, or 27 per cent, higher at £3,982 million compared to £3,141 million in 2004. Single premium life sales increased, particularly the Unit Linked Flexible Options Bond product, and single premium pension sales were higher, again as a result of the specific marketing focus.

Total OEICs sales increased significantly, by £610 million to £1,181 million in 2005 compared to £571 million in 2004. Regular premium sales were little changed with the increase being in single premium sales, primarily through bancassurance; this reflects a successful campaign in relation to the April 2005 tax year end and builds on the launch of the simplified product suite that was introduced at the end of 2004.

By distribution channel, bancassurance weighted sales were £32 million, or 13 per cent, higher at £274 million compared to £242 million in 2004; this reflected, in particular, the successful OEIC sales. Weighted sales via independent financial advisers were £130 million, or 30 per cent, higher at £562 million in 2005 compared to £432 million in 2004 supported by significant product and service enhancements; as a result the Lloyds TSB Group s market share of the IFA market improved to 6.5 per cent, compared with 5.9 per cent in 2004.

Profit before tax, excluding volatility, from life, pensions and OEICs was £98 million, or 16 per cent, lower at £500 million compared to £598 million in 2004. Profitability in 2005 benefited from the absence of a provision for customer redress but the results in 2005 were reduced by a provision of £155 million for the strengthening of mortality reserves. Adjusting for these items, profit before tax, excluding volatility, in 2005 was £655 million compared to £610 million in 2004, an increase of £45 million or 7 per cent. The strong sales lead to an increased contribution from new business, partly offset by a commensurate increase in distribution costs. Improved investment earnings resulted from higher cash balances held for the account of the shareholder. OEICs profitability has risen following improved markets and sales volumes.

General insurance

	2005	2004
	£m	£m
Net interest income	**23**	44
Other income	**543**	496
Total income	**566**	540
Insurance claims	**(197)**	(214)
Total income, net of insurance claims	**369**	326
Operating expenses	**(160)**	(154)
Profit before tax, excluding volatility	**209**	172
Volatility	**28**	8
Profit before tax	**237**	180

Profit before tax, excluding volatility, from the General insurance business was £209 million in 2005, which was £37 million, or 22 per cent, higher than £172 million in 2004. Net interest income was £21 million lower at £23 million, compared to £44 million in 2004, principally reflecting the adoption of IFRS 4 and IAS 39 from 1 January 2005.

	2005	2004
	£m	£m
Premium income from underwriting:		
Creditor	**127**	114
Home	**441**	442
Health	**16**	27
Reinsurance premiums	**(22)**	(29)
	562	554
Commissions from insurance broking:		
Creditor	**396**	442
Home	**49**	45
Health	**15**	20
Other	**221**	165
	681	672

Other income, was £47 million, or 9 per cent, higher at £543 million compared to £496 million in 2004; £18 million of this reflected the impact of the accounting standards applied with effect from 1 January 2005 giving an underlying increase of £29 million, or 6 per cent. Premium income from underwriting, net of reinsurance, was £8 million, or 1 per cent, higher at £562 million; creditor insurance income was higher as a result of the business written in conjunction with the Lloyds TSB Group s asset finance businesses but health premium income declined as a result of the transfer of part of this business to BUPA in 2004. Insurance broking commissions were £9 million, or 1 per cent, higher at £681 million compared to £672 million in 2004; creditor commissions were £46 million lower, as a result of a slowdown in unsecured lending growth during 2005. Other commissions, however, were £56 million higher due largely to higher levels of retrospective income on existing business.

Insurance claims, at £197 million, were £17 million, or 8 per cent, lower than £214 million in 2004. Creditor insurance payouts were lower due to a lower level of unemployment claims and home insurance claims were lower due to the relatively benign weather conditions. Health claims also fell, following the transfer of part of this business in 2004. The general insurance underwriting ratio improved to 34 per cent compared to 37 per cent in 2004.

Operating expenses, at £160 million, were £6 million, or 4 per cent, higher than £154 million in 2004; this increase reflects higher marketing spend together with some specific project costs.

Wholesale and International Banking

	2005 **£m**	2004 £m
Net interest income	**2,265**	2,006
Other income	**1,628**	1,558
Total income	**3,893**	3,564
Operating expenses	**(2,181)**	(2,078)
Trading surplus	**1,712**	1,486
Impairment losses on loans and advances	**(188)**	(193)
Loss on sale of businesses	**(6)**	(21)
Profit before tax	**1,518**	1,272
Cost:income ratio	**56.0%**	58.3%
Total assets (year-end) *	**£124,044m**	£123,826m
Total risk-weighted assets (year-end) *	**£ 80,154m**	£ 71,013m

* To ensure comparability, prior year asset and risk-weighted asset figures are shown as at 1 January 2005, following implementation of those international accounting standards for which restated comparatives are not required.

Profit before tax from Wholesale and International Banking in 2005 was £246 million, or 19 per cent, higher at £1,518 million compared to £1,272 million in 2004. The overall impact of the accounting standards implemented with effect from 1 January 2005 was limited and accounted for £20 million of the increase in profits.

Net interest income was £259 million, or 13 per cent, higher at £2,265 million compared to £2,006 million in 2004. Of this increase, £100 million reflects the impact of implementation of IAS 39 from 1 January 2005 which has caused certain income previously classified as fees to be included in the effective interest rate calculation. Excluding this impact, net interest income was £159 million, or 8 per cent, higher at £2,165 million compared to £2,006 million in 2004. This underlying growth in net interest income reflected good growth in average lending balances in Corporate Banking, Structured Finance, Asset Finance and Business Banking; net interest margins were higher within Financial Markets, as a result of a change in mix of balances held, and within Structured Finance, as a result of the terms of new transactions taken on, although Corporate Banking margins reduced as a result of competitive pressures.

Other income was £70 million, or 4 per cent, higher at £1,628 million compared to £1,558 million in 2004. However, excluding the impact of the accounting standards implemented with effect from 1 January 2005, other income was £152 million, or 10 per cent, higher. This growth in underlying other income reflected increases in customer volumes within Corporate Banking, Structured Finance and Business Banking which resulted in higher lending and other fees. Business Banking also benefited from tariff reviews and from a lower level of commission clawback in respect of insurance sales; Asset Finance income increased as a result of organic growth and the impact of the motor dealerships acquired by the Lloyds TSB Group s Dutton Forshaw subsidiary during 2005.

Operating expenses were £103 million, or 5 per cent, higher at £2,181 million compared to £2,078 million in 2004. This largely reflects higher staff costs in support of the substantial business growth within Wholesale and International Banking over 2005, together with the impact of the motor dealership acquisitions.

Impairment losses on loans and advances were £5 million, or 3 per cent, lower at £188 million compared to £193 million in 2004. Charges within Corporate Banking and Structured Finance reduced by £94 million as a result of lower new provisions and a good level of recoveries in 2005, in part reflecting the benign economic environment. The impairment charge within Asset Finance was £66 million higher than in 2004 as a result of the substantial lending growth in recent years, particularly in respect of personal finance. There was also a lower level of releases within the International Banking businesses, which in 2004 had benefited from a release of £30 million from the Lloyds TSB Group s centrally held provision in respect of exposures in Argentina.

Wholesale and International Banking profit in 2005 was also reduced by a charge of £6 million in respect of the sale and closure of businesses; 2004 included a loss of £21 million which principally related to the sale of the Lloyds TSB Group s businesses in Argentina and Colombia.

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Central group items

	2005 **£m**	2004 £m
Lloyds TSB Foundations	**(34)**	(31)
Funding cost of acquisitions less earnings on capital	**(380)**	(317)
Central costs and other unallocated items	**(8)**	(2)
Loss on sale and closure of businesses	**(20)**	
Profit before tax, excluding volatility	**(442)**	(350)
Volatility	**(124)**	
Profit before tax	**(566)**	(350)

2005 compared to 2004

The four independent Lloyds TSB Foundations support registered charities throughout the UK that enable people, particularly the disabled and disadvantaged, to play a fuller role in society. The Foundations receive 1 per cent of the Lloyds TSB Group s pre-tax profit after adjusting for gains and losses on the disposal of businesses and pre-tax minority interests, averaged over three years, instead of a dividend on their shareholdings. In 2005, the Lloyds TSB Group accrued £34 million for payment to registered charities. See note 42 to the financial statements.

The funding cost of acquisitions, less earnings on capital, was £63 million higher at £380 million; this increase principally reflects the reclassification, as a result of the implementation of IAS 39 with effect from 1 January 2005, of certain capital instruments from minority interests to loan capital. As a result, the funding cost is now reported within interest expense.

Volatility

	2005 **£m**	2004 £m
Banking volatility	**(124)**	
Insurance volatility	**438**	168
Policyholder interests volatility	**311**	(30)
Total volatility	**625**	138

Banking volatility

In accordance with IFRS, it is the Lloyds TSB Group s policy to recognise all derivatives at fair value. The banking businesses manage their interest rate and other market risks primarily through the use of intra-Group derivatives, with the resulting net positions managed centrally using external derivatives. IFRS does not, however, permit the intra-Group derivatives to be used in a hedge relationship for reporting purposes. Although fair value accounting can have a significant impact on reported earnings, it does not impact on the business fundamentals or cash flows of the businesses. The Group has, therefore, implemented an internal pricing structure that allows divisions to transfer to central group items the volatility associated with marking-to-market derivatives held for risk management purposes. Banking volatility is principally comprised of the difference between the result that would be recognised on an accrual accounting basis for derivatives held for risk management purposes and their mark-to-market value. The Lloyds TSB Group has set up a central hedging function to reduce the impact of this volatility by establishing, where possible, accounting hedge relationships for the external derivatives. During 2005, profit before tax included a negative banking volatility of £124 million.

Insurance volatility

Changes in market variables such as the performance of equity markets and the level of interest rates, which are beyond the control of management, can result in significant volatility in the profitability of the Lloyds TSB Group s insurance businesses. As in previous years, in order to provide a clearer representation of the underlying performance of the life and pensions and general insurance businesses, the effect of these changes is separately analysed within insurance volatility. Following the implementation of the requirements of IFRS and FRS 27, insurance volatility is principally comprised of the elements described below.

The Lloyds TSB Group s insurance businesses have substantial holdings of investments which are accounted for at fair value with changes being reflected within the income statement. The difference between the actual return on these investments attributable to shareholders and the expected return based upon economic assumptions made at the beginning of the year is included within insurance volatility. In addition, the calculation of the value of in-force business makes assumptions about future investment returns; to the extent that actual experience is different the effect is also included within insurance volatility.

The main assumptions used in the calculation of the value of in-force business were as follows:

	31 December 2005 %	31 December 2004 %
Risk-adjusted discount rate (net of tax)	**7.02**	7.40
Return on equities (gross of tax)	**6.72**	7.17
Return on fixed interest securities (gross of tax)	**4.12**	4.57
Expenses inflation	**3.79**	3.76

Changes in stock market performance also affect the realistic valuation of the guarantees and options embedded within products written in the Scottish Widows With-Profits Fund, which following the implementation of FRS 27 is now reflected on the Lloyds TSB Group s balance sheet. Fluctuations in this valuation caused by market-related movements are also included within insurance volatility. During 2005, profit before tax included positive insurance volatility of £438 million.

Policyholder interests volatility

As a result of the requirement contained in IFRS to consolidate life and pensions businesses on a line-by-line basis, the Lloyds TSB Group s income statement includes amounts attributable to policyholders which affect profit before tax; the most significant of these items is policyholder tax. Under IFRS, tax on policyholder investment returns is included in the tax charge rather than being offset against the related income, either increasing or decreasing profit before tax with a corresponding change in the tax charge. In order to provide a clearer representation of the underlying performance of the Lloyds TSB Group s life and pensions businesses the impact of these items upon pre-tax profit has been separately identified within volatility. During 2005, profit before tax included positive policyholder interests volatility of £311 million.

Future accounting developments

Future developments in relation to the Lloyds TSB Group s IFRS reporting are discussed in note 55 to the financial statements and future developments in relation to US GAAP are discussed in note 56 to the financial statements.

IFRS compared with US GAAP

Under US GAAP, Lloyds TSB Group s net income for the year ended 31 December 2005 was £1,351 million (2004: £1,508 million) compared to £2,493 million (2004: £2,392 million) under IFRS. Reconciliations between IFRS and US GAAP figures, together with detailed explanations of the accounting differences, are included in note 56 to the financial statements.

The Lloyds TSB Group s IFRS net income increased by £101 million, or 4 per cent, in 2005 compared with 2004, whereas its US GAAP net income decreased by £157 million, or 10 per cent. The US GAAP results have been adversely affected by the Lloyds TSB Group s decision not to hedge any of its financial instruments for US GAAP accounting purposes and the increased US GAAP net pension charge.

Hedge accounting. Under IFRS, changes in the fair value of derivatives that are designated as hedges are either offset against the change in fair value of the hedged asset or liability through earnings or recognised directly in equity until the hedged item is recognised in earnings, depending on the nature of the hedge. Under US GAAP, because Lloyds TSB Group has elected not to satisfy the more onerous hedging criteria of SFAS No. 133 Accounting for Derivative Instruments and for Hedging Activities in respect of derivative contracts, these instruments are treated as being held for trading purposes, with the unrealised mark-to-market gains and losses taken to income as they arise and the resulting assets or liabilities recorded on the balance sheet. As Lloyds TSB Group continues to hold a significant number of derivatives which are hedge accounted under IFRS this means that net income and shareholders equity under US GAAP are subject to greater volatility.

Pensions. IFRS requires that the pension costs in the income statement reflect the cost of accruing benefits for active employees, benefit improvements and the cost of severances borne by the schemes net of the expected return on scheme assets. The Lloyds TSB Group has elected to apply the corridor approach in respect of actuarial gains and losses and so, to the extent that the cumulative gains or losses remain within a corridor defined as the greater of 10 per cent of the scheme assets or liabilities, they are not reflected in the accounts. US GAAP prescribes a similar method but allows a certain portion of actuarial gains and losses to be deferred and allocated in equal amounts over the average remaining service lives of the current employees.

At the beginning of the year the cumulative unrecognised actuarial losses related to the Lloyds TSB Group s pension schemes exceeded the corridor limits on a US GAAP basis, but did not on an IFRS basis (as the relevant cumulative losses have only arisen since the adoption of IAS 19, Employee Benefits, on 1 January 2004) and consequently the 2005 US GAAP results include an amortisation charge which is not required under IFRS.

Other areas where differences in accounting have had a significant effect upon the Lloyds TSB Group s US GAAP results are as follows:

Insurance accounting. Under IFRS, for insurance contracts (and, in 2004, investment contracts within life assurance operations) the discounted value of the projected future cash flows attributable to the shareholder is recognised at the point of sale. IFRS therefore results in a proportion of the profit expected to accrue over the life of various products being recognised at their inception. Under US GAAP income is recognised in the income statement in the period in which it is earned and expenses in the period in which they are incurred. This results in a more even recognition of profit over the life of the related policies.

Intangible assets. Under US GAAP, the Lloyds TSB Group has recognised intangible assets reflecting the value of the customer relationships associated with acquisitions made in prior periods. These intangible assets are amortised through the income statement reducing US GAAP net income. The reconciling item still exists, despite the convergence of IFRS and US GAAP in this area, as, on transition, the Lloyds TSB Group chose not to apply IFRS to business combinations that occurred before 1 January 2004.

Average balance sheet and net interest income

The tables below have been prepared in accordance with IFRS (for 2004 and 2005) and with UK Generally Accepted Accounting Principles (for 2003) and, as a result, the information included in the tables for 2004 and 2005 is not directly comparable with that for 2003.

IFRS	**2005 Average balance £m**	**2005 Interest income £m**	**2005 Yield %**	2004 Average balance £m	2004 Interest income £m	2004 Yield %
Assets						
Treasury bills and other eligible bills:						
Domestic offices				41	2	4.88
Foreign offices				161	4	2.48
Loans and advances to banks:						
Domestic offices	**31,198**	**1,111**	**3.56**	26,731	917	3.43
Foreign offices	**2,224**	**88**	**3.96**	2,071	62	2.99
Loans and advances to customers:						
Domestic offices	**152,469**	**9,859**	**6.47**	127,646	8,221	6.44
Foreign offices	**4,948**	**236**	**4.77**	5,514	219	3.97
Available-for-sale financial assets:						
Domestic offices	**9,623**	**349**	**3.63**			
Foreign offices	**4,554**	**159**	**3.49**			
Debt securities:						
Domestic offices				9,989	300	3.00
Foreign offices				4,372	118	2.70
Lease and hire purchase receivables:						
Domestic offices	**11,137**	**787**	**7.07**	11,118	864	7.77
Foreign offices						
Total interest-earning assets of banking book	**216,153**	**12,589**	**5.82**	187,643	10,707	5.71
Total interest-earning trading securities and other financial assets at fair value through profit or loss (2004: trading assets)	**31,185**	**1,563**	**5.01**	34,037	1,536	4.51
Total interest-earning assets	**247,338**	**14,152**	**5.72**	221,680	12,243	5.52
Allowance for impairment losses on loans and advances	**(2,058)**			(1,729)		
Non-interest earning assets:						
Domestic offices	**58,916**			47,510		
Foreign offices	**919**			902		
Total average assets and interest income	**305,115**	**14,152**	**4.64**	268,363	12,243	4.56
Percentage of assets applicable to foreign activities (%)	**4.2**			4.8		

IFRS	**2005 Average interest earning assets £m**	**2005 Net interest income £m**	**2005 Net interest margin %**	2004 Average interest earning assets £m	2004 Net interest income £m	2004 Net interest margin %
Average interest-earning assets and net interest income:						

Banking business	**216,153**	**5,671**	**2.62**	187,643	5,110	2.72
Trading securities and other financial assets at fair value through profit or loss (2004: trading assets)	**31,185**	**1,114**	**3.57**	34,037	947	2.78
Net yield on interest-earning assets	**247,338**	**6,785**	**2.74**	221,680	6,057	2.73

IFRS	**2005 Average balance £m**	**2005 Interest expense £m**	**2005 Cost %**	2004 Average balance £m	2004 Interest expense £m	2004 Cost %
Liabilities and shareholders funds						
Deposits by banks:						
Domestic offices	**23,645**	**854**	**3.61**	20,199	456	2.26
Foreign offices	**4,075**	**99**	**2.43**	4,227	102	2.41
Liabilities to banks under sale and repurchase agreements:						
Domestic offices	**4,419**	**258**	**5.84**	4,200	192	4.57
&						