

LEEDS BUILDING SOCIETY
BASEL II PILLAR 3 DISCLOSURES
AT 31ST DECEMBER 2009



Leeds
Building Society

CONTENTS

SECTION 1 - OVERVIEW	3
BACKGROUND.....	3
BASIS AND FREQUENCY OF DISCLOSURES	3
SCOPE.....	4
LOCATION & VERIFICATION.....	4
SECTION 2 - RISK MANAGEMENT OBJECTIVES AND POLICIES.....	5
RISK CONTROL STRUCTURE.....	5
BOARD SUB-COMMITTEES	6
SECTION 3 - CAPITAL RESOURCES.....	7
TOTAL AVAILABLE CAPITAL.....	7
TIER 1	7
TIER 2.....	7
SECTION 4 – CAPITAL ADEQUACY	8
CAPITAL MANAGEMENT	8
INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS.....	8
MINIMUM CAPITAL REQUIREMENT:.....	8
SECTION 5 - RISK MEASUREMENT AND REPORTING.....	10
CREDIT RISK OVERVIEW	10
EXPOSURES TO REAL ESTATE PROPERTY.....	10
EXPOSURES TO INSTITUTIONS.....	11
IMPAIRMENT OF LOANS AND ADVANCES TO CUSTOMERS	13
CREDIT RISK CONCENTRATIONS.....	16
CREDIT RISK MITIGATION.....	16
RESIDENTIAL MORTGAGES	17
COMMERCIAL.....	17
TREASURY	17
CREDIT RATING DOWNGRADES.....	19
SECTION 6 - MARKET RISK.....	20
MARKET RISK OVERVIEW.....	20
INTEREST RATE RISK.....	20
FOREIGN CURRENCY RISK.....	21
OTHER PRICE RISK.....	21
SECTION 7 – OPERATIONAL RISK.....	22
OPERATIONAL RISK OVERVIEW.....	22
SECTION 8 - CONTACTS	23

Section 1 - Overview

Background

Leeds Building Society is the sixth largest building society in the UK with 68 branches throughout the UK and offices in Gibraltar and Dublin, assets of £9.5bn and a membership of 681,000 members.

The Society's mission statement is: "To be a successful independent Building Society, providing excellent value through quality customer services, efficiency and competitive products."

Basel II was implemented in the European Union via the Capital Requirement Directives (CRD) and came into effect on the 1 January 2007. The Basel framework is made up of three 'pillars':

- Pillar 1 – Sets out the minimum capital requirements for credit, market and operational risk;
- Pillar 2 – The Internal Assessment and Supervisory Review and Evaluation Process (SREP), assesses whether additional capital should be held against risks not covered or fully covered in Pillar 1; and
- Pillar 3 – A firm is required to disclose key pieces of information on its capital, risk exposures and its risk management. Disclosures are designed to promote market discipline and complement Pillar 1 and Pillar 2.

Leeds Building Society ("Leeds") adopted the Pillar 1 Standardised Approach to Credit Risk and the Basic Indicator Approach to Operational Risk from 1 January 2008; it also became subject to Pillars 2 and 3 from that date. The disclosures in this document are on the standardised basis.

The Pillar 3 disclosures within this document cover credit risks (section 5), market risks (section 6) and operational risks (section 7).

Basis and Frequency of Disclosures

Leeds has prepared this document in accordance with the requirements of Pillar 3. Unless otherwise stated, all figures are at 31st December 2009, Leeds' financial year-end. Future disclosures will be issued on an annual basis and published within four months of the publication of the Annual Report and Accounts.

The Society will produce interim disclosures should there be any significant changes to its risk profile.

Scope

Leeds Building Society is regulated by the FSA (Financial Services Authority). The Basel II Framework therefore applies to Leeds and its subsidiary undertakings (together “the Group”).

There is a requirement to calculate and maintain regulatory capital ratios, on both a Group basis and on a “solo consolidation” basis. However, there are no differences between the basis of consolidation of the Group for accounting and prudential purposes. The principal subsidiaries included under solo consolidation are:

- Leeds Financial Services Ltd
- Leeds Financial Services (Overseas) Ltd
- Leeds Mortgage Funding Ltd
- Leeds Overseas (Isle of Man) Ltd
- Countrywide Rentals 1 Ltd
- Countrywide Rentals 2 Ltd
- Countrywide Rentals 3 Ltd
- Countrywide Rentals 4 Ltd
- Countrywide Rentals 5 Ltd
- Mercantile Asset Management Ltd
- Headrow Commercial Property Services Ltd
- Leeds Building Society Covered Bonds LLP

All of the Group’s subsidiaries are included in the Pillar 3 disclosures. The Group does not foresee any practical or legal impediments to the transfer of capital resources or the repayment of liabilities within the Group. Full details of the principal subsidiary undertakings are included in Note 17 to the Annual Report and Accounts.

Location & Verification

These disclosures have been reviewed by the Group’s Audit Committee and are published on the Leeds website (www.leedsbuildingsociety.co.uk). The disclosures are not subject to external audit, except where they are equivalent to those prepared under accounting requirements for inclusion in the Group’s Annual Report and Accounts.

Section 2 - Risk Management Objectives and Policies

The Society has developed a Risk Management Framework that is designed to identify, assess, mitigate and manage risks that may impair the delivery of its strategic and business objectives.

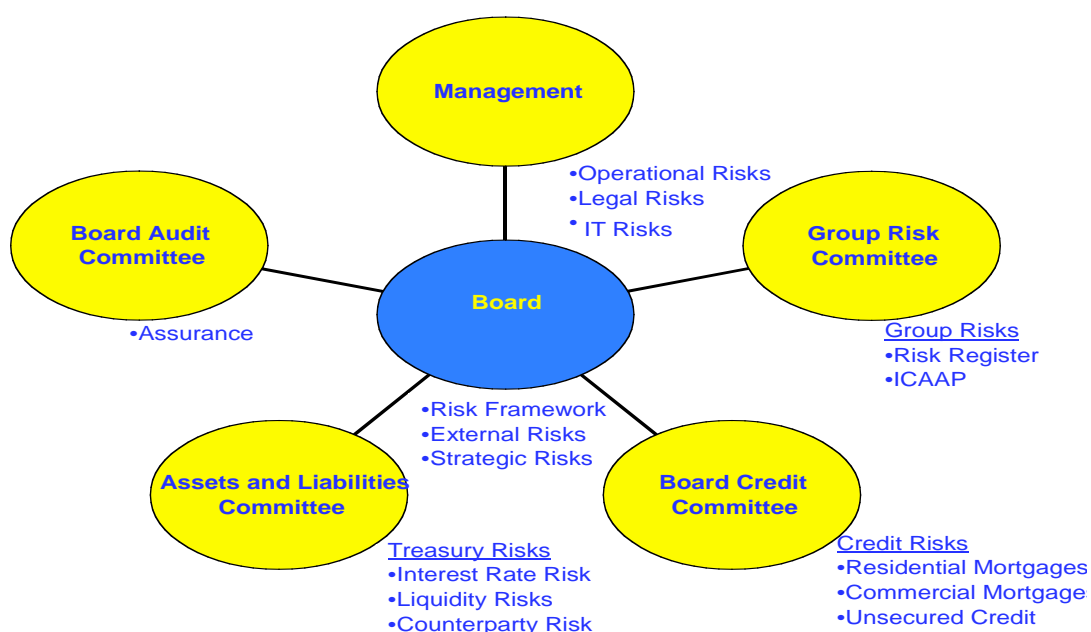
The oversight and direction of the Board is central to the Risk Management Framework and it ensures, through a series of Board sub-committees and Management fora, that appropriate policies, procedures and processes are implemented across the business to control and monitor Society risk exposure.

The Framework identifies the operational roles and responsibilities, both individual and collective, in the risk management process to ensure exposed risks are aligned to the Risk Appetite of the Board and that any unacceptable risk exposures are mitigated.

In addition to the ongoing assessment of known risk exposures, Management monitors external and emerging risks within its rolling ICAAP refresh process. Management has fostered an open communication culture that promotes the immediate escalation of actual or emerging risks.

The Board is ultimately responsible for the governance of risk and defines, through its Risk Appetite, the acceptable levels and types of risk exposure that it considers likely to arise in the delivery of its strategic objectives. As noted above, the Board's risk governance is supported through a series of sub-committees, or by Management, operating under delegated mandates.

Risk Control Structure



Board Sub-Committees

In principle, each of the Board Sub-Committees fulfil a similar role, in that operating under a Board delegated mandate, they provide a forum for the direction and challenge of Management whilst monitoring business performance and risk exposures.

Each of the Board Sub-Committees includes at least two Non Executive Directors with other Committee members being drawn from the Executive and appropriate members of Senior Management.

The **Group Risk Committee** (GRC) is mandated to monitor and review the consolidated risk picture across the Society. It is responsible for the ongoing development, and maintenance of the ICAAP, and its annual submission to the Board. The GRC receives, on a quarterly basis, standing reports on the Corporate Risk Register, external risk indicators and emerging risks.

The **Assets and Liabilities Committee** (ALCO) is responsible for ensuring that the Society's Treasury Risk exposures, (interest rate, liquidity, Counterparty and currency), are managed and mitigated in line with the Board approved Financial Risk Management Policy.

The **Board Credit Committee** (BCC) is responsible for ensuring that the Society's Credit Risk exposures, (Residential, Commercial, Lifetime and Unsecured), are managed and mitigated in line with the Board's Risk Appetite.

The **Board Audit Committee** (BAC) has overarching responsibility for the Society's systems of control. It receives and considers reports from business areas, including Internal Audit, IT security, Financial Crime, Legal & Compliance and Operational Risk. It also validates the financial reporting of the Society.

Operationally, the Board Sub-Committees above are supported by Management in the form of a Management Assets and Liabilities Committee, Business Continuity Group, Information Security Forum, Integrated Assurance Group and a Pricing Committee, amongst others.

More general oversight and direction is delivered through weekly **Operational Review Meetings** (ORM) and monthly **Strategic Review Meetings** (SRM), that enable Senior Management to manage the day-to-day risks within the business.

Section 3 - Capital Resources

Total Available Capital

The table below illustrates the Group's regulatory capital position as at 31st December 2009. The Group has complied with the capital requirements set out by the Financial Services Authority.

Capital Resources	As at 31/12/2009 £m	As at 31/12/2008 £m
Tier 1		
<i>Core Tier 1 Reserves</i>	469.8	448.1
<i>PIBS</i>	25.0	25.0
Total Tier 1 Capital	494.8	473.1
Tier 2		
Subordinated debt	40.0	40.0
Revaluation reserve	16.9	16.9
Collective provisions	15.5	18.6
Total Tier 2 Capital	72.4	75.5
Total Capital Resources	567.2	548.6

Tier 1

Tier 1 capital comprises the general reserve and Permanent Interest Bearing Shares (PIBS)¹. The general reserve represents the Group's accumulated accounting profits as well as adjustments for pension obligations and property disposals. It excludes available for sale and cashflow reserves.

PIBS are unsecured deferred shares and rank behind the claims of all subordinated noteholders, depositors, creditors and investing members of Leeds. Leeds currently has no innovative Tier 1 instruments.

Tier 2

Tier 2 capital comprises the Group's property revaluation reserve, qualifying subordinated debt and collective impairment provisions.

Under FSA rules, qualifying subordinated notes cannot exceed 50% of the total of Tier 1 capital, and Tier 2 capital cannot exceed Tier 1 capital.

Subordinated notes² are unsecured and rank behind the claims of all depositors, creditors and investing members, other than holders of PIBS, of the Society.

In accordance with FSA guidance, in the last five years to maturity, the subordinated debt will be amortised on a straight-line basis.

¹ Details about PIBS are provided in note 29 to the 2009 Annual Report and Accounts

² Details of the subordinated notes are included in note 28 to the 2009 Annual Report and Accounts

Section 4 – Capital Adequacy

Capital Management

Leeds has adopted the Standardised Approach to Credit Risk and the Basic Indicator Approach to Operational Risk since 1 January 2008, in order to calculate the Basel II Pillar 1 minimum capital requirement.

The Group manages its capital supply and demand by balancing capital efficiency and prudence. The Board believes that this approach fits in with the Group's approach towards capital adequacy, preserves the Group's competitive position in relation to capital requirements, and maintains and enhances the Group's reputation in the financial services industry.

Capital is measured on a regulatory basis. Regulatory capital covers all Pillar 1 risks (i.e. credit risk and operational risk) for all significant portfolios. Leeds determines its Pillar 1 Capital Resource Requirement (CRR) using a regulatory capital calculator that is compliant with BIPRU (The FSA's Prudential sourcebook for Banks, Building Societies and Investment Firms). Regulatory capital is reported in the monthly Management Pack to the Board.

Internal Capital Adequacy Assessment Process

The ICAAP is an articulation of the Society's approach to risk, its identification, quantification and management. The ICAAP is a dynamic document to reflect the changing nature of the risks facing the Society. The ICAAP will, at least annually, be fully updated to reflect the business strategy as part of the corporate planning process. In the intervening period, on a quarterly basis, or as often as necessary, the Board sub-committees will monitor the risks, using the Risk Register, and the applicable stress testing, and their results, to confirm their continued relevance.

The ICAAP is produced by the Risk department, reviewed by Internal Audit, and presented to the Group Risk Committee for recommendation to the Board, for approval. The final ICAAP will be submitted to the FSA and reviewed as part of their Supervisory Review and Evaluation Process (SREP).

Minimum Capital Requirement:

The table overleaf shows Leeds overall minimum capital requirement for credit risk under the standardised approach (expressed as 8% of the risk weighted exposure amounts for each of the applicable standardised credit risk exposure classes) at 31st December 2009:

Capital Requirement	As at 31/12/2009 £m	As at 31/12/2008 £m
Financial Institutions (<i>inc. Liquidity Collateral Deposits</i>)	28.1	47.4
Unsecured lending	0.6	0.9
Secured on real estate property (<i>inc. Lifetime Mortgages</i>)	232.3	240.9
Past due items	24.5	11.7
Other items	8.8	11.1
Sub Total	294.3	312.0
Operational Risk (<i>Basic indicator Approach</i>)	17.8	16.8
Pillar 1 Total	312.1	328.8

Section 5 - Risk Measurement and Reporting

Credit Risk Overview

Credit risk is the risk of financial loss where borrowers or counterparties are not able to meet their obligations as they fall due. The Group is firmly committed to the management of this risk in both its retail and commercial lending activities and its investment of liquid assets.

The Group employs appropriate underwriting and fraud detection techniques to support sound decision making to minimise losses in its lending activities. In addition, a proactive approach to the control of bad and doubtful debtors is maintained within the collections area.

Experienced risk functions operate within the Group, and are driven both by the recognised need to manage the potential and actual risks, but also by the need to continually develop new processes to ensure sound decisions are made in the future. In this way, any variations in risk from market, economic or competitive changes are identified and the appropriate controls developed and put in place.

Comprehensive management information on movement and performance within the various personal and wholesale portfolios ensure that credit risk is effectively controlled, and any adverse trends are identified before they impact on performance. Group performance is also measured against the industry, where appropriate, to ensure debt default levels do not deviate from that of the industry average. This management information is distributed widely across the Group and monitored within tight boundaries at Board and Sub Board committees. The Board Credit Committee is responsible for the formulation of policy pertaining to asset quality and credit risk for approval by the Board.

Policy statements covering, amongst other things, criteria to be used in considering limits on counterparties and countries are reviewed at least annually by the ALCO and the Board. Authorised limits on a counterparty are determined following rigorous analysis giving due consideration to both internal and external credit ratings.

Exposures to Real Estate Property

Leeds calculates credit risk for exposures secured by mortgages on residential real estate and commercial real estate using the Standardised Approach.

The table overleaf shows the Group's exposure to real estate property as at the 31st December 2009.

Category	Risk Weight 2009	Exposure £m 2009	Risk Weight 2008	Exposure £m 2008
Secured on residential real estate	39%	6,519.2	38%	6,542.3
Other Loans	100%	579.5	100%	625.8

The exposure value and average risk weight figures above include past due items.

The following table shows the residual maturity of the Group's exposure to real estate property as at 31st December 2009.

	Up to 12 Months	1 – 5 years	More than 5 years	Total
Residential Mortgages	156.6	739.4	5,623.2	6,519.2
Other Loans	53.2	262.8	263.5	579.5

The following table shows the residual maturity of the Group's exposure to real estate property as at 31st December 2008.

	Up to 12 Months	1 – 5 years	More than 5 years	Total
Residential Mortgages	162.3	709.8	5,670.2	6,542.3
Other Loans	44.6	240.8	340.4	625.8

Exposures to Institutions

The Group uses external credit assessments provided by Moody's, Fitch and Standard & Poors. All three rating agencies are recognised by the FSA as eligible external credit assessment institutions (ECAI) under the Capital Requirements Regulations 2006 (SI 2006/3221) for the purposes of the Standardised Approach.

The table overleaf shows the Group's exposure to each of the credit quality steps for long and short-term investments to institutions at 31 December 2009.

Short-term Investments (Maturity 3 months or less)

Credit Quality Step	Risk Weight 2009	Exposure £m 2009	Risk Weight 2008	Exposure £m 2008
1	20%	976.4	20%	945.4
2	20%	-	20%	-
3	20%	-	20%	-
4	50%	-	50%	-
5	50%	-	50%	-
6	150%	-	150%	-
Unrated	20%	69.2	20%	86.8
Total		1,045.6		1,032.2

Long-term Investments (Maturity greater than 3 months)

Credit Quality Step	Risk Weight 2009	Exposure £m 2009	Risk Weight 2008	Exposure £m 2008
1	20%	841.4	20%	1,008.4
2	50%	173.3	50%	275.3
3	50%	26.4	50%	50.7
4	100%	-	100%	-
5	100%	-	100%	-
6	150%	-	150%	-
Unrated	50%	22.7	50%	42.7
Total		1,063.8		1,377.1

The following table shows the Group's regulatory credit risk exposure to Treasury counterparties by sector at 31st December 2009:

Concentration by sector	£m 2009	£m 2008
Financial Institutions	1,769.4	2,037.8
Local Authorities	-	-
Asset backed securities	340.0	371.5
Total	2,109.4	2,409.3

The following table shows the residual maturity of the Group's treasury exposures as at 31st December 2009.

	Up to 12 Months	1 – 5 years	More than 5 years	Total
Financial Institutions	1,296.4	469.7	3.3	1,769.4
Asset backed securities	-	-	340.0	340.0

The maturity of exposures is shown on a contractual basis. In addition, it does not take into account any instalments receivable over the life of the exposure.

The following table shows the residual maturity of the Group's treasury exposures as at 31st December 2008.

	Up to 12 Months	1 – 5 years	More than 5 years	Total
Financial Institutions	1,531.0	465.4	41.4	2,037.8
Asset backed securities	-	-	371.5	371.5

Impairment of Loans and Advances to Customers

Individual assessments are made of all mortgage loans in possession, and, based upon these assessments, an individual impairment reduction of these assets is made.

In addition, an impairment reduction is made against those loans and advances to customers where objective evidence indicates that it is likely that losses may ultimately be realised. The impairment value is calculated by applying various factors to each loan. These factors take into account the Group's experience of default and delinquency rate, loss emergence periods, regional property price movements and adjustments to allow for forced sale values. Impairment provisions are made to reduce the value of other impaired loans and advances to the amount that is considered to be ultimately received based upon objective evidence.

2009 Impairment losses on loans and advances to customer³

Group	Loans fully secured on residential property	Loans fully secured on land	Other loan	Total
	£m	£m	£m	£m
Collective impairment	9.0	7.0	2.6	18.6
Individual impairment	8.2	14.0	3.5	25.7
At 1 January 2009	17.2	21.0	6.1	44.3
Income and expenditure account				
Charge for the year				
Collective impairment	-	(2.0)	(1.2)	(3.2)
Individual impairment	12.5	42.3	1.2	56.0
Adjustments to impairment losses for bad and doubtful debts resulting from recoveries during the year.	(0.3)	-	-	(0.3)
	12.2	40.3	-	52.5
Amount written off during the year				
Individual impairment	9.1	26.7	1.9	37.7
Collective impairment	9.0	5.0	1.4	15.4
Individual impairment	11.3	29.6	2.8	43.7
At 31 December 2009	20.3	34.6	4.2	59.1

³ Note 11 to the 2009 Annual Report and Accounts

2008 Impairment losses on loans and advances to customer⁴

Group	Loans fully secured on residential property	Loans fully secured on land	Other loan	Total
	£m	£m	£m	£m
Collective impairment	6.3	5.1	2.3	13.7
Individual impairment	1.4	-	2.4	3.8
At 1 January 2008	7.7	5.1	4.7	17.5
Income and expenditure account				
Charge for the year				
Collective impairment	2.7	1.9	0.3	4.9
Individual impairment	8.7	17.2	1.7	27.6
Adjustments to impairment losses for bad and doubtful debts resulting from recoveries during the year.	(0.4)	-	-	(0.4)
	11.0	19.1	2.0	32.1
Amount written off during the year				
Individual impairment	1.5	3.2	0.6	5.3
Collective impairment	9.0	7.0	2.6	18.6
Individual impairment	8.2	14.0	3.5	25.7
At 31 December 2008	17.2	21.0	6.1	44.3

⁴ Note 11 to the 2008 Annual Report and Accounts

The table below provides further information on loans and advances by payment due status as at 31 December 2009⁵.

	Value of Loan Asset 2009		Value of Loan Asset 2008	
	£m	%	£m	%
Not impaired:				
- neither past due nor impaired	6,689.4	91.8	6,837.8	92.7
- past due up to 3 months but not impaired	285.4	3.9	348.4	4.7
Impaired:				
- Past due 3 to 6 months	138.2	1.9	107.1	1.4
- Past due 6 to 12 months	104.1	1.4	50.0	0.7
- Past due over 12 months	41.3	0.6	5.2	0.1
- Possessions	32.7	0.4	26.5	0.4
Total Exposures	7,291.1		7,375.0	

Notes:

Definition of past due – Exposures which have not been repaid 90 days after the due payment date.

Credit Risk Concentrations

For residential lending, loan to value and geographic concentration, limits are set within the Lending Policy. The Society is geographically well diversified with no region accounting for more than 15% of total balances. By their nature, our residential mortgages comprise of intrinsically highly diversified small loans and have a low volatility of credit risk outcomes.

The Society's commercial loan portfolio represents less than 10% of total loan advances. Exposures to commercial lending are managed through limits, which restrict the exposure to a single counterparty and the monitoring of industry sector and geographical concentrations.

Policy limits have also been set to enable the management of treasury credit risk concentrations. These limits are actively monitored and relate to aggregate counterparty and asset class exposures.

Credit Risk Mitigation

The Group uses a wide range of techniques to reduce the credit risk of its lending. The most basic of these is performing an assessment of the ability of a borrower to service the proposed level of borrowing without distress. The Group obtains the following further security to further mitigate the risk for the funds advanced.

⁵ Note 35 to the 2009 Annual Report and Accounts

Residential Mortgages

Residential property is the Group's main source of collateral and means of mitigating credit risk inherent in its residential mortgage portfolios. All mortgage lending activities are supported by an appropriate form of valuation using an independent firm of valuers, indexed valuation (further advances) or Automated Valuation Model subject to business rules and confidence levels.

Commercial

Collateral for commercial loans comprises a first legal charge over freehold or long leasehold property and additional security as appropriate, which might include: -

- Guarantees;
- Debentures; and
- Charged cash deposits.

In certain limited circumstances the Society's first charge is subject to other priority arrangements. The Society ensures that security is insured for full replacement cost and its interest is noted on the relevant policy.

Treasury

Derivatives are contracts or arrangements whose value is derived from one or more underlying price, rate or index inherent in the contract or arrangement, such as interest rates, exchange rates or stock indices. Derivatives are only used by the Group in accordance with Section 9A of the Building Societies Act 1986, to reduce the risk of loss arising from changes in interest rates or other factors of a prescribed description which affect the business. Accordingly, such instruments are not used in trading activity or for speculative purposes. Counterparty Credit Risk in relation to derivatives is the risk that a swap could default. The risk is mitigated by offsetting the amounts due to the same counterparties ('Netting benefits') and by cash deposited by certain of the counterparties ('Collateral held'), under a Credit Support Annex.

Credit Support Annexes (CSA) exist for collateralising derivative transactions with counterparties to which the Group has derivative exposures in order to mitigate the risk of loss on default. The Credit Support Annexes allow margin calls to be made on the net mark to market value of derivative exposures with a particular counterparty. Although these CSAs are taken into consideration when setting the internal credit risk limits for derivative counterparties, the Group does not currently recognise the risk mitigating effect of these CSAs in its Pillar 1 capital calculations.

The Society manages its Treasury Credit Risk in conformance with geographic, sector and counterparty limits, determined by the methodology outlined within approved policy, which has been ratified by its Assets and Liabilities Committee ("ALCO").

Limits are based on a methodology using the rating structures of Moody's, Standard and Poor's and Fitch, combined with qualitative and quantitative analysis. All limits are formally reviewed by ALCO on a quarterly basis.

An ongoing assessment of investment quality is undertaken by the credit risk function that resides within Treasury. ALCO receives a suite of monthly reports detailing any changes in perceived credit quality. If necessary, exception reporting also takes place following a breach of predefined triggers or changes in the external environment.

For derivative exposures, the Society uses risk mitigation techniques such as Credit Support Annexes and netting to reduce Credit Risk emanating from its swap portfolio.

The table below describes the significant activities undertaken by the Group, the related risks associated with such activities and the types of derivatives which are typically used in managing such risks. These risks may alternatively be managed using on balance sheet instruments or natural hedges that exist in the Group's balance sheet.

Activity	Risk	Type of Derivative
Fixed rate savings products	Sensitivity to falls in interest rates	Received fixed interest rate swaps
Fixed rate mortgage lending	Sensitivity to increases in interest rates	Pay fixed interest rate swaps
Fixed rate funding	Sensitivity to falls in interest rates	Receive fixed interest rate swaps
Fixed rate asset investments	Sensitivity to increases in interest rates	Pay fixed interest rate swaps

The table below shows the derivative instruments used by the Group for hedging purposes at 31st December 2009⁶.

Derivatives held for hedging	2009 £m	2008 £m
Derivatives designated as fair value hedges	3,988.2	5,033.1
Derivatives designated as cashflow hedges	310.0	450.0
Other derivatives held for hedging	1,508.7	1,586.4
Total derivative asset / liabilities held for hedging	5,806.9	7,069.5

The following table shows the current derivatives contracts as at 31st December 2009 using the Mark to Market Method:

	Replacement Cost £m	Credit Exposure £m	Total Exposure £m
Book	142.1	50.6	192.7

⁶ Note 14 to the 2009 Annual Report and Accounts

The following table shows the current derivatives contracts as at 31st December 2008 using the Mark to Market Method:

	Replacement Cost £m	Credit Exposure £m	Total Exposure £m
Book	197.1	60.2	257.3

Credit Rating Downgrades

A one notch short term rating downgrade would require the Group to consider arranging an alternate swap counterparty to take responsibility for the swaps that the Society provides to its covered bond subsidiary.

Section 6 - Market Risk

Market Risk Overview

Market risk is the potential adverse change in Group income or the value of Group net worth arising from movements in interest rates, exchange rates or other market prices. Market risk exists to some extent in all the Group's businesses. The Group recognises that the effective management of market risk is essential to the maintenance of stable earnings and the preservation of member value.

The Group's exposure to market risk is governed by a policy approved by the ALCO. This policy sets out the nature of risk which may be taken and aggregate risk limits. Based on these aggregate limits, the ALCO assigns risk limits to all Group businesses and monitors compliance with these limits. At each meeting the ALCO reviews reports showing the Group's exposure to market and liquidity risks.

The Group's exposure to market risk is managed by Group Treasury. Group Treasury manages market risk by using appropriate hedging instruments, or by taking advantage of natural hedges within the Group's businesses. Market risk is managed within a clearly defined framework of policy limits.

Market risk is measured and reported using a variety of techniques, according to the appropriateness of the technique to the exposure concerned. The techniques used include interest rate gap analysis, duration analysis, basis point value analysis, scenario analysis, and earnings at risk.

There has been no change in the year to the Group's exposure to market risks or the manner in which it manages and measures the risk.

Interest rate risk

The primary market risk faced by the Group is interest rate risk. The net interest income and market value of the Group is exposed to movements in interest rates. This exposure is managed through the use of appropriate hedging instruments, or by taking advantage of natural hedges within the Society's balance sheet.

The Group does not run a trading book and therefore does not have the type of higher risk exposure run by many banking institutions. Given our policy of hedging fixed rate assets and liabilities back to floating rate, outright interest rate risk arises mainly from the Board's decision to invest the Group's reserves according to a specified fixed rate maturity profile.

The level of risk can deviate from this, subject to limits, in particular as a result of decisions made by the Group's Treasury department to temporarily deviate from the benchmark profile in the light of market conditions. The Group uses interest rate stress testing and gap analysis to manage its interest rate position.

The following table details the Group's sensitivity to a 200 basis point change in interest rates at the year-end, with all other variables held constant. A positive number indicates an increase in profit or loss and other equity.

	Group 2009 £m	Group 2008 £m
200 basis point increase		
Profit or loss	5.8	(11.0)
Other equity	18.0	25.4
200 basis point decrease		
Profit or loss	(10.2)	10.2
Other equity	(32.4)	(49.2)

Foreign currency risk

The Group's policy is not to run material, speculative foreign exchange positions.

The Group issues Euro mortgages as well as receiving funding via its commercial paper program in foreign currencies; hence exposures to exchange rate fluctuations arise. Cross-currency interest rate swaps are utilised to reduce both the interest rate and exchange rate risk exposures that come from funding in foreign currency.

Other price risk

The Group's policy is to have no material exposure to equity markets. Any exposures arising from the Group's products are eliminated, as far as it is practicable, by appropriate hedging contracts

Section 7 – Operational Risk

Operational Risk Overview

Leeds has adopted the Basic Indicator Approach to Operational Risk. This approach links the capital charge for operational risk to a single risk indicator (gross income) for the whole of the Society, including its subsidiaries.

Operational risk is defined by the Society as ‘the potential risk of financial loss or impairment to reputation resulting from inadequate or failed internal processes and systems, from the actions of people or external events’. Within the Group, operational risk is sub-categorised by type such as regulatory, theft or fraud, systems failure and people risk.

An independent risk function has the overall responsibility for establishing the framework within which operational risk is managed and for its consistent application across the Group. The framework is based on industry best practice and anticipated regulatory requirements. Day to day management of operational risk rests with line managers. It is managed through a combination of internal controls, processes and procedures and various risk mitigation techniques, including insurance and business continuity planning.

The Group monitors its operational risk through a variety of techniques. These include the Group Risk Committee being presented with an assessment of the extent of each of the Group’s key operational risks documents in its Corporate Risk Register.

In particular the Group manages its regulatory risk through a compliance function that proactively identifies and deals with emerging and current regulatory risks.

Section 8 - Contacts

Should you have any queries regarding this document, please contact: -

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