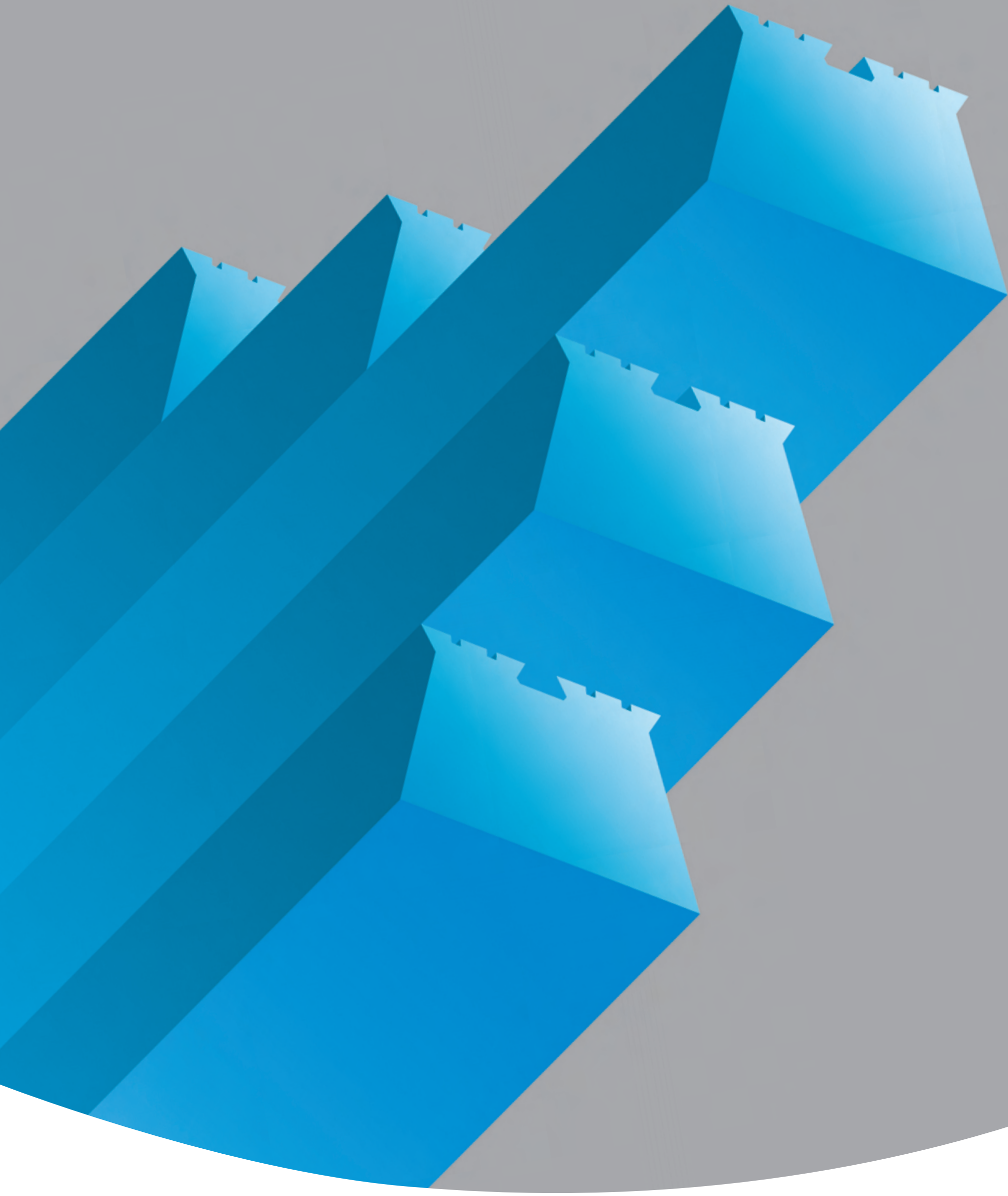
Skipton Building Society
Summary Financial Statement
2008



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SKIPTON BUILDING SOCIETY

Summary Financial Statement

This financial statement is a summary of information from the audited Annual Report & Accounts, which will be available to members and depositors free of charge on demand at every office of Skipton Building Society from 16 March 2009.

Summary Directors' Report

Introduction

The Skipton Group is pleased to report a solid financial performance in light of extremely difficult and volatile market conditions. Whilst our profits are down on the level achieved in 2007, we believe our business model, based on a traditional and prudent building society supplemented by other income generated through investment in subsidiary companies, demonstrates the long-term stability of the business. Our balance sheet remains healthy and we continue to hold strong levels of liquidity and capital.

There is no doubt we are in the midst of an uncompromising recession and the ability to forecast its severity and ending is made difficult, if not impossible, by the continuing shortage of credit in the UK markets. For this reason, our business plans for 2009 are likely to adopt a similar vein to 2008: to limit balance sheet growth, to hold above normal levels of liquidity, reduce further our reliance on wholesale funding and increase our cost control.

Skipton, in common with all building societies, has a substantial and stable retail funding base. However, unlike other building societies, we also have a Group of subsidiaries with a diversified portfolio of investments, which generate higher returns (even in this difficult economic climate).

As a result, once the banking sector and our building society peers have reported their figures, we are confident the added context will show what a solid set of results these are.

Financial highlights

- Group total assets £13.6bn (up 8.9%)
- Group mortgage assets up 1.7% (2007: up 15.9%)
- Group retail share balances £8.1bn (up 12.9%)
- Group pre-tax profit £22.5m (2007: £163.9m)
- Society management expenses ratio 47p (2007: 49p) per £100 assets
- Society interest rate margin 0.54% (2007: 0.74%)
- Group interest rate margin 0.66% (2007: 0.95%)
- Solvency ratio Basel II - 12.28% (2007: Basel I - 12.30%)

In 2008, the Society's net interest margin reduced by £12.2 million to £69.8 million. This was partly as a result of the competitive rates enjoyed by savers (as demonstrated by a growth in retail balances of 12.9%) and partly due to the high cost of securing longer-term funding and carrying above-normal levels of liquidity during the credit crunch.

In addition to providing in full against the Society's own exposure of £11.0 million to the Icelandic banking system, we have also set aside £16.3 million for our share towards the next three years' levy to be imposed by the Financial Services Compensation Scheme (FSCS) in relation to the rescue of savers in Bradford & Bingley and other banks. Group profits in 2008 are almost half what they would have been had the FSCS provision not been required. We believe it unjust that the building society sector, which has an inherently safer business model, is bearing a disproportionate cost for the troubles of some banks which had far riskier models.

Lending

2008 was a year of turmoil in the wholesale markets and, as such, our lending plans were always going to be modest – the Society's gross lending was down a third from £2.2 billion to £1.3 billion. The uncertainties of the credit crunch meant we were naturally cautious in committing funds and, where we did, they tended to be to borrowers of higher quality. By lending in this way we can avoid the stresses on funding which have been the undoing of others in the industry. Also, at this time of limited funds for borrowers, it is our members who we give priority to, recognising our existing relationship and their track record with the Society.

As the economy deteriorated, we have seen an increase in arrears. In the Society, the number of mortgages that were three months or more in arrears increased during the year from 0.20% to 0.38%. At a Group level, the figure increased from 0.41% to 1.14%, but remained well below the Council of Mortgage Lenders' industry figure of 1.89% at the year end.

Savings

During its 155 year history, the Society has always tried to balance the needs of savers with the wishes of borrowers, but never have interest rates fallen so low to make this so difficult. As a mutual, our natural inclination is to pass on in full any reduction in rates to our borrowers whilst protecting the returns for our savers. But with the Bank of England's base rate having fallen to such a low level, we are in a unique environment which challenges our best intentions. We find it perverse that UK savers, who are the bedrock for the funding of mortgages, are being penalised to help correct the fundamental imbalances in the economy. We will therefore continue to lobby central policy makers on behalf of our savers.

On the positive side, the credit crunch has done much to benefit mutuals like Skipton who are now seen as stable homes for investors' money – especially with the increased cover offered by the FSCS. This, coupled with a range of competitive products (in particular, our Branch Access Account and limited edition Fixed Rate Bonds) has meant retail balances have increased from £7,191.1 million to £8,158.2 million. In addition, Skipton's investor numbers grew from 521,000 to 565,000 during 2008 and will increase further to over 700,000 following the proposed merger with Scarborough.

Distribution

Skipton has long swum against the tide with regard to its branch network; while others closed branches, 2008 saw the Society open five new ones, plus another in early 2009, taking our total to 85. This will grow further with the branches inherited through the Scarborough merger.

The merger with Scarborough will also bring with it investors who transact by telephone. This is a channel Skipton hasn't explored before and, whilst we will initially limit this to existing products, we will evaluate its effectiveness for future expansion.

This will be balanced with the fact we have spent 2008 expanding our online offering, with new savings products added to this channel and the launch of our eMortgage service, where mortgage brokers submit applications using one of the industry's best online systems.

Wholesale funding and capital

A key reason for the healthy state of Skipton's business, in relation to many in the banking sector, is our limited reliance on the money markets, as approximately 70% of our funding comes from retail balances. However, the challenge has been in managing our non-retail funding, with an emphasis on extending the term of our loans for greater stability in our funding profile.

With regard to this, the Society has maintained its level of funding through already well diversified channels, supplemented by a covered bonds programme, established during the year, which will enable it to access further medium-term funding whilst the credit crunch continues. In addition, the Society was the first in the sector to have a call date on a tranche of its subordinated debt during the current market, and it is testament to our security and strength, the hard work of our Treasury team and our strong relationship with the investment community that we were able to renew this capital on acceptable terms in December 2008.

The Skipton Group

For a long time, the Society has extolled the benefits of having a Group of subsidiaries to complement its core business of savings and loans. During good times they provide dividends to the Society which enables us to deliver better pricing to our members. In more stressed conditions they are assets that allow us to crystallise value to protect the overall Group performance.

As a result, in 2008 the Society sold two of its subsidiaries – Direct Life & Pensions and Amber Select – generating a profit of £9.1 million. This was part of our strategy to concentrate on the Group's five key pillars: savings and lending, mortgage servicing, estate agency, financial advice and data provision. In addition, Connells disposed of its remaining holding in the property website, Rightmove, generating a profit of £22.3 million.

Overall, 2008 saw Connells' operating profits fall from £59.7 million to £10.4 million. However, when considering 2008 was the worst housing market in living memory and UK property transactions were down approximately 40% on 2007, this is in fact a very creditable performance, helped by good results in lettings, auctions, survey and valuation, and asset management of repossessed properties on behalf of lenders.

Callcredit is another Group company with a positive story to tell. Profits have grown again in 2008, and we are forecasting continued growth, not only in the supply of traditional credit checking products but also in account management, monitoring and over-indebtedness products (particularly relevant right now).

Homeloan Management (HML) is also embracing the opportunities the downturn has presented, especially by improving its range of services in the collections arena to support its portfolio of clients. This is a countercyclical business with good prospects.

New to the Group in early 2008, but not faring as well in the present climate, are two financial advisory companies – Torquil Clark, based in the Midlands, and Thomson Shepherd, based in Scotland. They were acquired as part of our strategy to strengthen our financial advice offering and longer-term, when the investment market volatility finally subsides, we are confident they will deliver a strong performance.

Another subsidiary affected by market forces is our specialist lending subsidiary, Amber Homeloans, whose borrowers were the first to feel the impact of the economic conditions. Following a review of the risks surrounding this business, Amber ceased new lending in March 2008 and is now concentrating on managing its portfolio of loans.

The future

With regard to the future, we believe a deep recession will exist throughout 2009 and well into 2010. An extremely low interest rate environment will prevail, to the benefit of borrowers, but savers will see a very noticeable difference in the lower levels of interest they receive. For those borrowers who do succumb to the economic fallout, we will endeavour to work fairly with them.

With so many uncertainties continuing in the general economy, we will not return to the levels of profit seen in 2006 and 2007 for a while, but we are confident that our prudent management of both the core business and our subsidiaries should see us deliver another solid performance.

We remain on track to complete the proposed merger with Scarborough Building Society on 30 March 2009. Our experience during the project has reconfirmed our belief that the two organisations are a close fit, in terms of commitment to mutuality, business diversification and of course geography. The reward will be a stronger mutual with the opportunity to serve a larger audience, which can only be good news for our customers and staff.

With regard to future mergers, we will consider these so long as our existing members are not compromised and there is a long-term benefit for the combined business.

Group results for the year ended 31 December	2008 £m	2007 £m
Net interest receivable	**86.0**	109.7
Other income and charges	**387.5**	468.5
Profit on disposal of associate	**22.3**	36.0
Profit on disposal of subsidiaries	**9.1**	-
Fair value losses	**(3.3)**	(3.9)
Administrative expenses	**(433.0)**	(441.0)
Impairment losses	**(46.1)**	(5.4)
Profit for the year before taxation	**22.5**	163.9
Taxation	**1.3**	(37.3)
Profit for the financial year	**23.8**	126.6
Minority interests	**(1.0)**	(1.1)
Profit for the year	**22.8**	125.5

Group financial position at 31 December	2008 £m	2007 £m
Assets		
Liquid assets	**3,178.3**	2,670.1
Mortgages	**9,488.4**	9,157.5
Other loans	**79.3**	134.4
Derivative financial instruments	**429.9**	122.3
Fixed and other assets	**471.1**	446.2
Total assets	**13,647.0**	12,530.5
Liabilities		
Shares	**8,158.2**	7,191.1
Borrowings	**4,077.8**	4,144.1
Derivative financial instruments	**280.3**	50.4
Other liabilities	**213.2**	209.7
Subordinated liabilities	**183.7**	183.7
Subscribed capital	**26.3**	26.3
Minority interests	**3.9**	3.5
Reserves	**703.6**	721.7
Total liabilities	**13,647.0**	12,530.5

Group statement of movement in reserves	2008 £m	2007 £m
Reserves at 1 January	**721.7**	600.6
Net expense for the year not recognised in the Income Statement	**(40.9)**	(4.4)
Profit for the year	**22.8**	125.5
Reserves at 31 December	**703.6**	721.7

These Accounts were approved by the Board of Directors on 24 February 2009 and were signed on its behalf by:

J B Rawlings	Chairman
D J Cutter	Chief Executive & Director
R J Twigg	Group Finance Director

Summary of key financial ratios	2008 %	2007 %
Gross capital as a percentage of shares and borrowings	**7.50**	8.25
Liquid assets as a percentage of shares and borrowings	**28.84**	23.56
Group profit after tax for the year as a percentage of mean total assets	**0.18**	1.09
Group management expenses as a percentage of mean total assets	**3.31**	3.81
Society management expenses as a percentage of mean total assets	**0.47**	0.49

Gross capital represents the general reserve, cash flow reserve and available-for-sale reserve together with minority interests, subordinated liabilities and subscribed capital, as shown in the Group Balance Sheet. The gross capital ratio measures the proportion which the Group's capital bears to the Group's liabilities to holders of shares, depositors and other providers of funds, that is, its investors.

Liquid assets represent the total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and debt securities. Liquid assets are generally readily realisable, enabling the Group to meet its general liabilities during the year.

The profit ratio measures the proportion that the Group's profit after tax for the year bears to the average of the Group's total assets during the year. Mean total assets are calculated as the average of the 2008 and 2007 total assets as shown in the Group and Society Balance Sheets. A reasonable level of profit is required each year to maintain the gross capital ratio at a suitable level to protect investors' funds.

The management expenses ratio measures the proportion that the administrative expenses bears to the average of the mean total assets during the year.

Statement of the independent auditors to the members and depositors of Skipton Building Society

Pursuant to Section 76 of the Building Societies Act 1986, we have examined the Summary Financial Statement of Skipton Building Society on pages 1 to 5.

This auditors' statement is made solely to the Society's members, as a body, and to the Society's depositors, as a body, in accordance with Section 76 of the Building Societies Act 1986. Our work has been undertaken so that we might state to the Society's members and depositors those matters we are required to state to them in such a statement and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body and the Society's depositors as a body, for our work, for this statement, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

The Directors are responsible for preparing the Summary Financial Statement, in accordance with applicable United Kingdom law. Our responsibility is to report to you our opinion on the consistency of the Summary Financial Statement with the full Annual Accounts, Annual Business Statement and Directors' Report and its conformity with the relevant requirements of Section 76 of the Building Societies Act 1986 and regulations made under it.

Basis of opinion

We conducted our work in accordance with Bulletin 1999/6 'The auditors' statement on the Summary Financial Statement' issued by the Auditing Practices Board for use in the United Kingdom. Our report on the Group's full Annual Accounts describes the basis of our audit opinion on those Annual Accounts.

Opinion

In our opinion the Summary Financial Statement is consistent with the full Annual Accounts, the Annual Business Statement and Directors' Report of Skipton Building Society for the year ended 31 December 2008 and conforms with the applicable requirements of Section 76 of the Building Societies Act 1986 and regulations made under it.

KPMG Audit Plc

Chartered Accountants

Registered Auditor

Leeds

24 February 2009

Summary Directors' Remuneration Report

The Board is committed to best practice in its remuneration policy for Directors and this report explains how the Society applies the principles in the Combined Code relating to remuneration. Additionally, a summary of this report will again be sent to all members entitled to vote at this year's Annual General Meeting, where members will have the opportunity to vote on the report.

Remuneration Committee

The Remuneration Committee, which comprises four Non-Executive Directors, is responsible for the Society's Executive remuneration policy. The Committee is also responsible for setting, reviewing and approving individual remuneration packages for Executive Directors and other senior Group Executives, and setting the Chairman's fees. The members of the Remuneration Committee are Messrs Hutton (Chairman), Rawlings, Jack and Ms Hay-Plumb. The Chief Executive may attend meetings by invitation, together with external advisers, where appropriate.

In discharging its duties, the Remuneration Committee also reviews and takes into account independently produced data and professional advice in similar financial services organisations. It also gives full consideration to the provisions set out in the Code of Best Practice of the Combined Code on Corporate Governance.

The Non-Executive Directors' Remuneration Committee, which comprises Messrs Rawlings (Chairman), Cutter and Twigg, determines the level of the other Non-Executive Directors' fees.

Directors' remuneration policy

Executive Directors' remuneration

The Board's policy is designed to ensure that Executive Directors' remuneration reflects performance and enables the Society to attract, retain and motivate a sufficient number of high calibre individuals to lead and direct the organisation and deliver continually improving business performance.

The main components of Executive Directors' remuneration are as follows:

- Basic salary – which takes into account job content and responsibilities, individual performance (assessed annually) and salary levels of similar positions in comparable organisations.
- Annual bonus – which is calculated by reference to Group and Society performance measured together with individual performance against personal objectives, both of which are linked to the achievement of the Group's strategic objectives.
- Pensions – all Executive Directors are members of the Skipton Building Society Pension & Life Assurance Scheme.
- Other benefits include provision of a car, or car allowance, and private medical insurance.
- Policy on service contracts – the Executive Directors are employed on service contracts which expire at the age of 65, with a contractual notice period of 12 months.

Non-Executive Directors' remuneration

Non-Executive Directors' fees are based on comparable data from similar financial services organisations. Non-Executive Directors do not receive bonuses, are not eligible for pension benefits and do not have service contracts.

Executive Directors' contractual terms

The Executive Directors all have notice periods of 12 months under the policy on service contracts detailed above.

Directors' remuneration

Remuneration of all the Society's Directors during the year is detailed below.

Non-Executive Directors

	2008 £000 Fees	2007 £000 Fees
Mr J B Rawlings	**70**	68
Mr A I Findlay	**50**	39
Mr P R Hales (appointed 29 May 2007)	**40**	23
Ms P M Hay-Plumb	**40**	39
Mr W J Henderson (retired 24 April 2007)	**-**	13
Mr C N Hutton	**42**	39
Mr W H Jack	**44**	46
Ms A B E Kinney	**41**	44
Mr R F Marriott (retired 27 May 2008)	**13**	39
Mr N Sherlock (retired 24 April 2007)	**-**	13
	340	363

Executive Directors 2008

	Salary £000	Bonus £000	Benefits(†) £000	Sub total £000	Increase in accrued pension £000	Total £000
Mr J G Goodfellow (note 1)	**363**	**37**	**56**	**456**	**7**	**463**
Mr D J Cutter	**246**	**26**	**41**	**313**	**7**	**320**
Mr S W Haggerty (note 2)	**210**	**-**	**34**	**244**	**12**	**256**
Mr R J Twigg	**238**	**24**	**39**	**301**	**6**	**307**
Total	**1,057**	**87**	**170**	**1,314**	**32**	**1,346**

Executive Directors 2007

	Salary £000	Bonus £000	Benefits(†) £000	Sub total £000	Increase in accrued pension £000	Total £000
Mr J G Goodfellow	325	238	54	617	25	642
Mr D J Cutter	223	115	42	380	9	389
Mr R J Twigg	220	127	40	387	10	397
Total	768	480	136	1,384	44	1,428

(†) Benefits comprise the provision of a car, or car allowance, the Society's contributions to the Skipton Building Society Pension & Life Assurance Scheme and private medical insurance contributions.

Notes

1. Mr Goodfellow retired as a Director on 31 December 2008 and will remain employed as a consultant to the Board until 31 December 2009. Under his settlement agreement, the Society will pay a total of £781,000 to Mr Goodfellow. This comprises salary and benefits of £385,000 in accordance with his service agreement and payments of £259,000 in respect of his early retirement and £137,000 in consideration of his entering into certain restrictive covenants. Additionally Mr Goodfellow will accrue pension benefits in the Skipton Building Society Pension & Life Assurance Scheme ("the Scheme") until 31 December 2009. As part of these arrangements the Society has also agreed to waive the early retirement discount factors applicable to his benefits in the Scheme with effect from 10 January 2010.

In considering these arrangements, the Committee sought advice from external advisers to reach an agreement that was both fair and reasonable to both the Society and Mr Goodfellow. The Committee believes that the amounts agreed are fair and reasonable and adhere to good practice.

2. Mr Haggerty resigned as an Executive Director on 3 December 2008. In addition to the amounts shown above, Mr Haggerty will receive a compensation payment of £242,000 in line with his contractual arrangements.

Stock code 10-8418/15/04/09/APS

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