



ARBUTHNOT BANKING GROUP (“Arbuthnot” or “the Group”)
Audited Final Results for the year to 31 December, 2009

YEAR OF PROGRESS

Growth has been achieved by all operations as Arbuthnot Banking Group continued to lend through the downturn, to increase significantly its retail banking customer base and to deliver a marked improvement in its investment banking division. Despite the weak economic environment, Arbuthnot has taken a counter-cyclical approach and invested across the Group.

Arbuthnot Banking Group PLC is the holding company for Arbuthnot Latham & Co., Limited, Secure Trust Bank PLC and Arbuthnot Securities Limited,

FINANCIAL HIGHLIGHTS

- Group pre-tax profit £5.1m (2008: loss £2.2m)
- Group earnings per share (EPS) 23.4p, increased six-fold (2008:3.5p)
- Dividend per share (DPS) up 1p to 22p (2008:21p)
- Capital, liquidity and balance sheet remain strong

OPERATIONAL HIGHLIGHTS

Private Banking - Arbuthnot Latham

- Customer balances grew £19m to £292m (2008: £273m) and loans grew 11% to £178m (2008: £159.9m) as Arbuthnot continued to lend through the credit cycle
- Loan to deposit ratio at 60%, maintaining strong liquidity
- Pre-tax profit reduced to £0.2m (2008: £2.1m) after investment in new structured products business and effect of low money market rates

Retail Banking - Secure Trust Bank

- Profit before tax up 40% to £10.2m (2008: £7.3m)
- Re-entered the consumer lending market with acquisition of two loan portfolios from Citigroup and Liverpool Victoria for £37.8m, which contributed strongly to profits
- Successful launch of Asset Finance and Prepaid Current Account
- Significant increase in customer numbers, up 66% to December 2009

Investment Banking - Arbuthnot Securities

- Story of two halves: H1 pre-tax loss of £1.3m and H2 pre-tax profit of £1.2m
- Division returning to profit on the back of improving corporate activity and market conditions
- Corporate finance income up 28% to £9.2m (2008: £7.2m)
- Secondary market business generated significant improvement with revenue growing to £7.8m (2008: £1.6m)

Commenting on the results, Henry Angest, chairman and chief executive of Arbuthnot, said: “***Arbuthnot Banking Group looks forward with confidence to 2010 and beyond, provided the economy holds up and the UK does not experience a double dip. We are in the hands of the politicians.***”

ENQUIRIES:

Arbuthnot Banking Group
Herry Angest, Chairman and Chief Executive 020 7012 2400
Andrew Salmon, Chief Operating Officer
James Cobb, Group Finance Director

Hawkpoint Partners Ltd (Nominated Advisor)
Lawrence Guthrie 020 7665 4500
Sunil Duggal

Numis Securities Ltd (Broker)
Chris Wilkinson 020 7260 1000
Mark Lander

Pelham Bell Pottinger (Financial PR)
Polly Fergusson 020 7337 1519
Zoë Pocock

The 2009 Annual Report will be posted and available on the Arbuthnot Banking Group website <http://www.arbuthnotgroup.com/Presentations.aspx> on 31 March 2010. Copies may be obtained from the Company Secretary, Arbuthnot Banking Group PLC, Arbuthnot House, 20 Ropemaker Street, London, EC2Y 9AR.

Consolidated statement of comprehensive income

	Note	Year ended 31 December	
		2009 £000	2008 £000
Interest and similar income		22,464	23,799
Interest expense and similar charges		(5,548)	(12,395)
Net interest income		16,916	11,404
Fee and commission income	6	31,816	35,241
Fee and commission expense		(795)	(961)
Net fee and commission income		31,621	34,280
Gains less losses from dealing in securities		3,763	(3,818)
Operating income		51,700	41,866
Impairment losses on loans and advances	17	(2,368)	(977)
Other income	7	2,118	-
Gain on sale of business assets	8	-	3,077
Gain on sale of subsidiary	37	-	1,528
Operating expenses	9	(46,400)	(47,644)
Profit / (loss) before income tax		5,050	(2,150)
Income tax (expense) / credit	11	(1,679)	1,152
Profit / (loss) for the year		3,371	(998)
Foreign currency translation reserve		41	(299)
Revaluation reserve			
- Revaluation of freehold premises		-	(974)
- Amount transferred to profit or loss on sale		(108)	-
Other comprehensive income for the period, net of income tax		(67)	(1,273)
Total comprehensive income for the period		3,304	(2,271)
Profit attributable to:			
Equity holders of the Company		3,507	519
Non-controlling interests		(136)	(1,517)
		3,371	(998)
Total comprehensive income attributable to:			
Equity holders of the Company		3,440	(754)
Non-controlling interests		(136)	(1,517)
		3,304	(2,271)
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in pence per share):			
- basic and fully diluted	12	23.4p	3.5p

Consolidated statement of financial position

	Note	At 31 December	
		2009 £000	2008 ⁽¹⁾ £000
ASSETS			
Cash	13	230	3,369
Derivative financial instruments	24	236	-
Loans and advances to banks	14	54,614	15,939
Loans and advances to customers	16	229,722	163,734
Trading securities - long positions	15	2,659	3,523
Debt securities held-to-maturity	18	127,597	140,639
Current tax asset		1,805	1,679
Other assets	22	18,754	15,053
Financial investments	19	5,057	3,434
Intangible assets	20	2,906	2,831
Property, plant and equipment	21	8,552	9,448
Deferred tax asset	28	383	106
Total assets		452,515	359,755
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	30	150	150
Share premium account	30	21,085	21,085
Retained earnings	31	11,684	11,257
Other reserves	31	(920)	(358)
Non-controlling interests		2,144	2,280
Total equity		34,143	34,414
LIABILITIES			
Deposits from banks	23	2,886	2,898
Trading securities - short positions	15	959	1,036
Derivative financial instruments	24	-	942
Deposits from customers	25	385,999	292,890
Current tax liability		2,208	-
Other liabilities	26	13,217	13,603
Deferred tax liabilities	28	81	-
Debt securities in issue	27	13,022	13,972
Total liabilities		418,372	325,341
Total equity and liabilities		452,515	359,755

(1) The comparatives have been reclassified to align with current year presentation (see note 39).

Chairman's statement

Arbuthnot Banking Group recorded a profit before tax of £5.1m for the year ended 31 December 2009. (2008: loss £2.2m). This result reflects a marked improvement in the performance of the Group during the second half of the year. It is an encouraging outturn, considering that the economic environment remains tough and that the results bear the cost of the investment the Group made in new business initiatives in 2009.

We continue to manage our business prudently and without any expectation of external support, and I am pleased to report that the Group is in robust financial health, with strong capital ratios, liquidity and balance sheet. This strength is, for once, reflected in the share price which has grown by 47% over the last 12 months and outperformed the FTSE Financial index by 7%.

We remain committed to a progressive dividend policy and we are proposing a 1p increase in the dividend, paying a final dividend of 11.5p per share, making it 22p for 2009 (2008: 21p).

In 2009, some of the consequences of the financial crisis have become clearer. On the positive side, it has provided us with opportunities to be corporately active. As a small banking group, it is our strategy to behave counter-cyclically and invest in people, products and businesses at the bottom of the cycle. We have taken full advantage of our opportunity by hiring high quality people, buying two books of consumer loans and investing in new business ventures. The market continues to present opportunities for us to grow our business.

On the negative side, the response to this crisis by government and regulators has produced some challenges both to us as a group and to the wider financial services industry. The bank payroll tax, for example, fell indiscriminately on the banking sector, affecting both banks which required government assistance and those, like us, which managed their businesses prudently and forewent short-term profits to ensure stability. This grossly unfair tax epitomises government's policy on the financial crisis: all banks and bankers are regarded as equally culpable, and "one-size-fits-all" where taxation and regulation are concerned.

With an impending General Election in the UK, the development of President Obama's plans for the regulation of US banks and the increased regulation for banks proposed by the European Union, this is a critical year for the UK financial services industry. The threats to the industry are very real. Damage has already been done, and if a general heavy-handed approach continues, London's place as an international financial centre will continue to be seriously damaged. I believe strongly that banking regulation should be bespoke, case specific, based on a real appreciation of the individual banking business, its risks, management culture and the corresponding capital requirements. The other threats to London are of course the punitive tax system, both personal and corporate and the ever increasing dead hand of excessive regulation, with employment laws being the most expensive.

Private Banking Division

Arbuthnot Latham recorded a profit of £0.2m (2008: profit of £2.1m). Although it is disappointing to report only a small profit in this division, it needs to be recognised that the result was heavily affected this year by two factors. In the first place, Arbuthnot Latham's results include £0.5m as part of the start-up cost associated with our new structured products business, which began hiring staff in July 2009.

The second factor affecting Arbuthnot Latham's result is the reduced return generated by surplus liquidity invested in the money market. The bank continued to operate with a loan to deposit ratio of approximately 60% as its policy is to retain strong liquidity. The rates earned on this surplus liquidity declined from an average of 5.8% in 2008 to 2.7% in 2009. Although the interest rate spread between customer loans and deposits improved in 2010, the low money market rates had a negative effect on profitability.

Despite the severity of the economic recession, the quality of Arbuthnot Latham's loan book was demonstrated by the low level of provisions made for bad debts, which were less than 1% of the book.

Retail Banking Division

Pre-tax profits for Secure Trust Bank improved significantly to £10.2m (2008: £7.3m). The Bank has taken full advantage of the opportunity created by the financial crisis to re-enter the consumer lending market. It acquired two portfolios of loans in 2009 from Liverpool Victoria and Citigroup for considerations of £16.7m and £21.1m respectively, in both cases at a discount to the gross value of the loans. These portfolios have performed in line with expectations in terms of credit quality, and have contributed strongly to profits in 2009.

The new motor finance business launched early in the year has steadily increased its business volumes, and achieved a monthly lending run-rate of £1m by the year end. This activity also made a positive profit contribution in 2009. The roll-out of the Prepaid Current Account has proceeded in line with plan and by the year end 2,740 accounts had been opened.

Secure Trust Bank has been able, without significant marketing spend, to generate customer deposits to finance lending activity. At 31 December, deposits stood at £93.4m, up 160% on the previous year end.

Investment Banking Division

Arbuthnot Securities moved strongly back into profit in the second half of the year and finished with a small full year loss of £0.1m (2008: loss of £5.2m). Corporate finance business improved markedly in the second half, with 15 transactions being completed compared with 2 in the first half. Arbuthnot Securities now has 98 clients, and remains the firm with the second largest number of nominated adviser appointments on the AIM market. Strong results were achieved by the secondary market business, improving from £1.6m in 2008 to £7.8m in 2009.

During this difficult phase of the market, Arbuthnot Securities has taken advantage of the hiring window substantially to upgrade its people. Although staff numbers have remained stable at 72, approximately one third of staff have been hired since the middle of 2008.

Board Changes and Personnel

Apart from Mr. D.M. Proctor who was appointed a director on 3 November 2009 and Mr. M.A. Bussey who resigned from the Board on 3 November, 2009, all directors served throughout the year.

These results once again reflect the continuing dedication and commitment of our employees who have done well in the current environment. On behalf of the Board I extend our thanks to all staff for their commitment and contributions made to the Group in 2009.

Dividend

The Board is proposing a final dividend of 11.5p, an increase of 1p on last year, making a total dividend for the year of 22p (2008: 21p). If approved, the dividend will be paid on 14 May 2010 to shareholders on the register as at 16 April 2010.

Outlook

Arbuthnot Banking Group looks forward with confidence to 2010 and beyond, provided the economy holds up and the UK does not experience a double dip a double dip. - We are in the hands of the politicians.

Business review

Private Banking – Arbuthnot Latham

	2009	2008
Operating income	£13.1m	£14.6m
Operating expenses	£11.6m	£13.4m
Profit before tax	£0.2m	£2.1m
Customer loans	£177.7m	£159.9m
Customer deposits	£292.0m	£272.6m
Total assets	£370.1m	£311.4m
Net interest margin	2.6%	3.3%
Loan to deposit ratio	0.61	0.59

Arbuthnot Latham seeks to provide sound wealth management solutions to its clients through financial planning and discretionary investment management, and to grow its lending book with caution.

Despite the well documented turmoil in the economy and financial services sector the Private Banking Division delivered a pleasing growth in its underlying core profitability. When the impacts of the prior year gain on the disposal of Arbuthnot Commercial Finance and the current year investment in the launch of Gilliat Financial Solutions are removed, the core business grew by £0.7m. This achievement reflects the continued fundamental strategy of maintaining a strong balance sheet and liquidity.

During 2009 deposit balances returned to growth following the small decline in 2008 caused by the financial crisis. Customer balances grew by a net £19m to £292m. This achievement reflects the bank's ability to provide a quality service to its clients.

Loans grew by £18m to £177.7m, 11% growth over 2008 (£159.9m). The bank continued to lend throughout the credit cycle, and was able to achieve slightly wider lending margins on new business. The bank also ensured that this lending was of high quality and credit losses remained at less than 1% of the asset book.

The loan to deposit ratio was maintained at a conservative level of approximately 60%. The bank continued to keep a strong liquidity ratio despite the relatively low yield on treasury assets, compared to the cost of new deposits, and believes this is the right strategy going forward. Being part of the Arbuthnot Group allows the bank to adopt an opportunistic approach and this was seen clearly in the launch during the year, of Gilliat Financial Solutions. This business packages and distributes structured products to the financial intermediary market. The investment resulted in a £0.5m cost for the bank.

After a number of years of trying to build a scalable platform with the Musical Instrument Finance business, the bank decided to exit this business line and as a result the consumer lending book was transferred within the Group to the retail banking division which is much better placed to operate this book as part of its asset finance book.

Retail Banking – Secure Trust Bank

	2009	2008
Operating income	£22.1m	£19.7m
Operating expenses	£11.8m	£14.0m
Profit before tax	£10.2m	£7.3m
Customer loans – unsecured	£51.4m	£12.8m
Customer deposits	£93.4m	£35.8m
Customer numbers ('000)	70	42
Net interest margin	15.1%	17.8%
Cost income ratio	0.45	0.63

Despite the difficult economic environment the Retail Banking Division had a good year, generating pre tax profits of £10.2m, an increase of 40% on the previous year. This is mainly the result of two loan portfolio acquisitions and the positive impact of the strategy put in place since 2007.

The lending business has grown significantly as a result of the acquisition of discounted loan portfolios which have contributed substantially to the increased profit performance. Both of these books are performing in line with expectations. Additionally, the business has found that there is a marked opportunity to cross sell to these newly acquired customers.

In addition to the purchased loan books the bank now provides point of sale vendor finance to the motor and music industries and loans to customers of affinity partners. These are provided through automated credit decision systems, which are integrated with the retailer. The combination of these different lending activities has brought in a new customer base which in turn has started to create a sustainable lending business with critical mass.

The lending book grew to £51m (after provisions) in December 2009 up from £13m the previous year. In spite of this increase the impairment charge remained in line with expectations. All lending is entirely funded through retail deposit accounts which are predominantly in the form of 60, 90 and 120 day notice accounts. The deposit balances have risen from £36m to £93m during the year.

During 2009 the bank successfully launched a new fee based current account with a Mastercard prepaid card. This provides a highly functional account with full web and telephone banking capability. The product does not provide credit to the customer. The business had 2,740 customers in December 2009 and the numbers are growing.

The core product of OneBill has become less crucial to the business. In spite of the total customer base increasing from 42,000 in January to 70,000 in December the OneBill customer numbers have continued to decline. The business strategy will be to migrate the OneBill customer base to the more functional prepaid accounts over the next couple of years.

The 2008 exit from insurance broking had a further one-off impact of £1.1m in 2009. This was achieved from a combination of deferred consideration on the Swinton deal and the release of operational provisions that were no longer required following the cessation of the business.

The intention is to continue with this combined lending and Prepaid Current Account strategy during 2010. The division will remain alert to further opportunities to acquire loan portfolios, but will focus on growing its organic loan portfolios through additional point of sale vendor finance schemes.

It will also seek to build out its distribution capabilities for its Prepaid Current Account and its newly introduced on-line account opening process will help to maintain this momentum.

Investment Banking - Arbuthnot Securities

	2009	2008
Corporate finance fees and retainers	£9.2m	£7.2m
Commission income	£4.1m	£4.7m
Gains less losses from dealing in securities	£3.7m	£(3.1)m
Operating expenses	£17.0m	£14.0m
Loss before tax	£(0.1)m	£(5.2)m
Corporate clients	93	97
Headcount	72	72

Arbuthnot Securities' performance in 2009 was a story of two halves. The first half, impacted by continuing market uncertainty and low levels of corporate activity, produced a pre-tax loss of £1.3m. The second half, benefiting both from more benign market conditions and the initiatives undertaken by management to improve the performance of the business, returned a profit of £1.2m. Overall, whilst it is clearly disappointing that the full year outcome was a small loss, the trends in the business, both in terms of financial results and operating performance, were positive and encouraging.

The number of corporate clients at the year end was 93, a slight fall attributable mainly to a number of clients de-listing. Arbuthnot Securities continues to have the second largest number of clients of any AIM nominated adviser. Notwithstanding our strong position in the AIM market, the average market capitalisation of our clients is now £147m.

Corporate Finance activity picked up strongly in the second half after a quiet start to the year. The main transaction type was secondary issues by listed companies; IPO's remained scarce in the AIM market throughout the year. In total, the company participated in the raising of £320m for clients. Corporate finance fee income totalled £9.2m (2008: £7.2m).

The secondary commissions market continues to be very competitive. Nevertheless, we have invested to upgrade both our distribution and research, as well as building our connectivity to a number of trading platforms. We have positioned our execution capability to operate at the highest possible level for the benefit of our clients.

The trading book performed very strongly, turning a loss of £3.1m in 2008 into a profit of £3.7m. This was achieved largely through tighter management control and improved trading discipline. The book remained at the low level to which it was reduced by management actions in 2008.

Financial review

Arbutnot Banking Group adopts a conservative approach to risk taking and seeks to maximise long term revenues and returns. Given its relative size, it is able to remain entrepreneurial and capable of taking advantage of market opportunities when they arise.

It provides a range of financial services to customers and clients in its three chosen niche markets of Private Banking (Arbutnot Latham), Investment Banking (Arbutnot Securities) and Retail Banking (Secure Trust Bank). The Group's revenues are derived from a combination of net interest income from its lending, deposit-taking and money market activities, fees for services provided to customers and clients, commissions earned on the sale of financial instruments and products and equity market-making profits.

Highlights

Summarised Income Statement

£'000	2009	2008
Net interest income	16,052	11,404
Net fee and commission income	31,885	34,280
Gains less losses from dealing in securities (Group and Arbutnot Securities)	3,763	(3,818)
Operating income	51,700	41,866
Other income	2,118	-
Operating expenses	(46,290)	(47,153)
FSCS levy	(110)	(491)
Gain on sale of business assets	-	3,077
Gain on sale of subsidiary	-	1,528
Impairment losses on loans and advances	(2,368)	(977)
Profit/(loss) on continuing activities before tax	5,050	(2,150)
Basic earnings per share (pence)	23.4	3.5

In the light of the deepest economic recession in living memory, the fact that the Group was able to return a healthy profit was extremely encouraging and an indication of the business's ability to act opportunistically.

The year started slowly and we were cautiously optimistic at the time of publishing our interim results. The level of profitability accelerated in the second half as the purchased loan portfolios and the strengthening of our corporate pipeline began to impact our returns positively.

The continued positive market sentiment allowed the trading book to deliver healthy gains, despite its much reduced size, reversing the losses suffered in the prior year. The net effect of this was that operating income grew to £51.7m, an increase of 23%.

During the second half of the year the Group also took the opportunity to invest in two new start up ventures, Gilliat Financial Solutions and Arbutnot Real Estate Investment Management. Despite the additional cost associated with these ventures, the operating expense line reduced by 2% as continuing cost control and the full year impact of the prior year's disposals took effect.

Impairment losses increased during the year to £2.4m which was in line with the balance sheet growth and as a percentage of assets remains consistent at 1%.

The profit before tax of the Group for the full year was £5.1m compared to a loss of £2.2m in the prior year, which represents a £7.3m improvement.

In response to the Bank Payroll Tax, the Group adopted a policy of not awarding any discretionary bonuses above £25,000. While the legislation remains in draft form, it is our expectation that our financial results will not be affected by this indiscriminate tax.

Summarised Balance Sheet

£'000	2009	2008
Assets		
Loans and advances to customers	229,722	163,734
Liquid assets	182,677	159,947
Other assets	40,116	36,074
Total assets	452,515	359,755
Liabilities		
Customer deposits	385,999	292,890
Other liabilities	32,373	32,451
Total liabilities	418,372	325,341
Equity	34,143	34,414
Total equity and liabilities	452,515	359,755

Balance Sheet Strength

The total assets of the Group increased by 26% to £452.5m (2008: £359.8m) as a result of a return to lending in the retail banking division through the purchase of two personal loan portfolios from Liverpool Victoria and Citigroup and organic growth in its asset finance portfolios launched in the year.

Following the small outflow of customer deposits in 2008, the Group is pleased to note that customer deposit balances showed strong growth of 32% to £386m (2008: £292.9m).

The Group continues with its conservative funding policy, remaining entirely funded by retail deposits and has maintained a loan to deposit ratio of 59% (2008: 56%). The surplus funding is invested in the liquid interbank certificate of deposit market with balances growing by 14% to £182.7m (2008: £159.9m).

Segmental Analysis

The segmental analysis in note 35 to the Consolidated Financial Statements to the Annual Report highlights the disclosures required under IFRS 8 'Operating Segments'. The operating segments are Private Banking (Arbuthnot Latham), International Private Banking (Arbuthnot AG), Investment Banking (Arbuthnot Securities) and Retail Banking (Secure Trust Bank). Group costs and intercompany elimination journals are shown separately to reconcile back to the Group consolidated result. The analysis presented below is prior to any consolidation adjustments to remove the impact of intergroup operating activities and is a fair reflection of the way the Directors manage the Group.

Private Banking – Arbuthnot Latham

£'000	2009	2008
Net interest income	8,880	8,225
Net fee and commission income	4,184	6,367
Operating income	13,064	14,592
Gain on sale of business assets	-	658
Gain on sale of Arbuthnot Commercial Finance Limited	-	1,528
Operating expenses	(11,598)	(13,352)
Impairment losses	(1,179)	(444)
Financial Services Compensation Scheme Levy	(81)	(450)
Restructuring costs	-	(413)
Profit before tax	206	2,119

The profit before tax fell to £0.2m (2008: £2.1m) largely due to two significant items. First, the prior year profit included a one-off gain on sale of business assets totalling £2.1m that was not repeated in 2009. Second, the bank invested £1m in the start up venture, Gilliat Financial Solutions. The Group entity contributed 50% to this investment which resulted in a net cost to the bank of £0.5m in the second half of the year.

Net fee and commission income fell by £1.3m mainly due to the disposal of Arbuthnot Commercial Finance in the prior year. It is worthwhile noting that the business had managed to improve its lending margins throughout the year, this however was offset by the decline in returns earned on its surplus liquidity in the interbank market and the increasing cost of raising deposits in the retail market.

Operating expenses continued to decline as the full year effect of the prior year business disposals and restructuring actions took effect.

Impairment losses ticked up in the year largely due to the failure of one customer in the musical instrument financing portfolio. Other than this the portfolio remains stable with losses under 1% of asset levels. The secured loan portfolio maintained an average loan to collateral value of 54%.

£'000	2009	2008
Assets		
Advances	177,745	159,908
Liquid assets	164,913	132,237
Other assets (including Group companies)	27,410	19,412
Total assets	370,068	311,557
Liabilities		
Customer deposits	292,026	272,614
Other liabilities (including Group companies)	54,997	15,447
Total liabilities	347,023	288,061
Equity	23,045	23,496
Total equity and liabilities	370,068	311,557

Total assets increased by 19% to £370.1m (2008 £311.6m) with the customer loan portfolio increasing by 11%.

The liability side of the balance sheet saw strong growth in both customer and Group deposits. Customer deposits grew by 7% to £292m (2008 £272.6m) as the business saw good inflows of new deposits.

The Private Bank remains well capitalised and funded, maintaining a total capital ratio of 11.2% and a core tier 1 ratio of 8.8% and a loan to deposit ratio of approximately 60%.

International Private Banking - Arbuthnot AG

Costs associated with establishing the Swiss Bank totalled £0.5m in the year (2008: £1.2m). The reduction is a result in a slowdown in expenditure by the Group while a partner is found to help launch the bank.

Retail Banking – Secure Trust Bank

£'000	2009	2008
Net interest income	8,587	4,214
Net fee and commission income	13,505	15,498
Operating income	22,092	19,712
Gain on sale of business assets	-	2,419
Income released relating to sale of business in prior year	1,132	
Operating expenses	(11,786)	(13,960)
Impairment losses	(1,189)	(533)
Financial Services Compensation Scheme Levy	(30)	(41)
Restructuring costs	-	(320)
Profit before tax	10,219	7,277

Profit Before tax in the business increased by 40% to £10.2m (2008: £7.3m).

The prior year results included the gain on sale of the insurance business to Swinton, which contributed £2.4m. Excluding this item the profits grew from £4.9 to £10.2m, an increase of £5.3m.

The purchase of the loan portfolios from LV and Citigroup contributed £5.5m to revenues. The profit also benefited by £1.1m as a result of the release of provisions related to the sale of the insurance business, these were offset by the investment in new business lines, the attrition in the OneBill account numbers and additional cost of surplus funding resulting from the continued conservative liquidity strategy.

£'000	2009	2008
Assets		
Advances – Personal lending & asset finance	25,960	12,551
Advances – Acquired portfolios	25,465	-
Liquid assets	16,615	24,725
Other assets (including Group companies)	46,027	14,193
Total assets	114,067	51,469
Liabilities		
Customer deposits	93,350	35,836
Other liabilities (including Group companies)	6,177	4,589
Total liabilities	99,527	40,425
Equity	14,540	11,044
	114,067	51,469

The personal lending asset balances ended the year at £51.4m (2008: £12.5m) a growth rate in excess of 300%. Excluding the purchased portfolios, the growth rate on the organic portfolios was still approximately 107%.

Customer deposit balances increased by 160% to £93.4m (2008: £35.8m).

Investment Banking - Arbuthnot Securities

£'000	2009	2008
Net interest income	(152)	(486)
Net fee and commission income	13,350	12,415
Gains less losses from dealing in securities	3,662	(3,116)
Operating income	16,860	8,813
Operating expenses	(17,007)	(14,038)
Restructuring costs	-	(691)
(Loss) / profit before tax	(147)	(5,225)

The business returned a loss before tax of (£0.1m) compared to the prior year loss of (£5.2m). The key change was the performance of the trading book which in the prior year suffered losses of £3.1m in revenues.

The fees earned from corporate finance transactions were £2m higher than in the prior year, however, 87% of the fees were earned in the second half of the year as the level of corporate activity increased during the year.

The non-controlling interest remained unchanged at 40.4% and therefore the Group's resultant share is 59.6%.

Group & Other Costs

£'000	2009	2008
Operating Income	452	(287)
Group costs		(2,921)
Group head office property costs	(973)	(989)
Subordinated loan stock interest	(618)	(964)
Total Group & other costs	(5,174)	(4,874)
Loss before tax	(4,722)	(5,161)

The Group and other costs decreased by 9% to £4.7m (2008: £5.2m) as the Group saw a positive change to the fair value of the investment securities it holds on its account, offset by the £0.5m contribution it made to the launch of Gilliat Financial Solutions.

Capital

The Group's capital management policy is focused on optimising shareholder value over the long term. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

In accordance with the EU's Capital Requirements Directive (CRD) and the required parameters set out in the FSA Handbook (BIPRU 2.2), the Individual Capital Adequacy Assessment Process (ICAAP) is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management.

The Group's regulated entities are also the principal trading subsidiaries as detailed in Note 34.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a "Pillar I plus" approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations deliver a sufficient capital sum adequately to cover management's anticipated risks. Where the Board considered that the Pillar I calculations did not reflect the risk, an additional capital add-on in Pillar II is applied.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders' funds, non-controlling interest, after deducting goodwill and other intangible assets.
- Lower Tier 2 comprises qualifying subordinated loan capital and revaluation reserves. Lower Tier 2 capital cannot exceed 50% of tier 1 capital.

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The FSA's last review of the Group's ICAAP was conducted in December 2007. The next review is scheduled to be completed in Q1 of 2010. All regulated entities have complied with all of the externally imposed capital requirements to which they are subject.

£'000	2009
Core Tier 1 capital	33,885
Tier 1 capital after deductions	30,979
Tier 2	13,280
Total capital	44,259
Core Tier 1 capital ratio (Net Core Tier 1 capital/ Basel 2 RWAs)	9.3%
Total Capital ratio (Capital/ Basel 2 RWAs)	13.3%

Risk Management

The Group regards the monitoring and controlling of risks as a fundamental part of the management process. Consequently, senior management are involved in the development of risk management policies and in monitoring their application. The Group's overall approach to managing internal control and financial reporting is described in the Corporate Governance section of the Annual Report.

The principal non-operational risks inherent in the Group's business are credit, liquidity and market risks. A detailed description of the risk management policies in these areas is set out in Note 4 to the financial statements. Credit risk is managed through the Credit Committees of Secure Trust Bank and Arbuthnot Latham & Co., Limited with significant exposures also being approved by the Group Risk Committee. Of the total gross loan book of £236.4 million at 31 December 2009, some £57.2 million represents largely unsecured loans to customers of Secure Trust Bank and £179.2 million represents the lending portfolio of Arbuthnot Latham, most of which is well secured against cash, property or other assets. A provision of £7.2 million (3% of total lending) is carried against the loan book.

Market risk arises in relation to movements in interest rates, currencies and equity markets. The Group's treasury function operates mainly to provide a service to clients and does not take significant unmatched positions in any market for its own account. Hence, the Group's exposure to adverse movements in interest rates and currencies is limited to the interest earnings on its free cash and interest rate repricing mismatches.

Through Arbuthnot Securities, the Group is also involved in market-making and underwriting UK equities. The market-making book is subject to Group-approved limits, both in aggregate and in relation to individual stocks. Outstanding positions are monitored against these limits both intraday and overnight. All significant underwriting transactions are individually approved by the Group Risk Committee.

A conservative approach is also taken to managing the liquidity profile and capital of the Group. Both of the banking subsidiaries operate with liquidity margins and capital ratios in excess of the minimum levels set by the regulators.

Dividend

The Board proposes a final dividend of 11.5 pence per share to be paid on 14 May 2010, giving a total dividend for the year of 22 pence (2008: 21 pence) per share.

Accounting Policies

This is the fourth set of group consolidated financial statements prepared in accordance with International Financial Reporting Standards (IFRS). This is the second set of accounts to include the disclosure requirements under IFRS 7 Financial Instruments.

Going Concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see note 4) and capital resources (see note 5), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are, therefore, prepared on the going concern basis.

Company statement of financial position

	Note	At 31 December	
		2009 £000	2008 ⁽¹⁾ £000
ASSETS			
Current assets			
Due from subsidiary undertakings		15,448	14,610
Financial investments	19	465	364
Other debtors		1,703	2,087
Non-current assets			
Shares in subsidiary undertakings	35	28,624	28,524
Property, plant and equipment	21	78	74
Due from subsidiary undertakings		7,750	6,350
Total assets		54,068	52,009
EQUITY AND LIABILITIES			
Equity			
Share capital	30	150	150
Share premium account	30	21,085	21,085
Other reserves	31	(920)	(425)
Retained earnings	31	1,862	3,927
Total equity		22,177	24,737
LIABILITIES			
Current liabilities			
Deposits from banks		2,618	2,609
Due to subsidiary undertakings		15,621	9,860
Accruals		630	831
Non-current liabilities			
Debt securities in issue	27	13,022	13,972
Total liabilities		31,891	27,272
Total equity and liabilities		54,068	52,009

⁽¹⁾ A credit balance of £7,196k previously included under due from subsidiary undertakings have been reclassified to due to subsidiary undertakings.

The Company has elected to take the exemption under section 408 of the Companies Act 2006 to not present the Parent Company profit and loss account. The profit for the Parent Company for the year is presented in the Statement of changes in equity.

Consolidated statement of changes in equity

	Attributable to equity holders of the Company								
	Share capital	Share premium account	Foreign currency translation reserve	Revaluation reserve	Capital redemption reserve	Treasury shares	Retained earnings	Non-controlling interests	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2009	150	21,085	(299)	366	20	(445)	11,257	2,280	34,414
Total comprehensive income for the period									
Profit / (loss) for 2009	-	-	-	-	-	-	3,507	(136)	3,371
Other comprehensive income, net of income tax									
Foreign currency translation reserve	-	-	41	-	-	-	-	-	41
Revaluation reserve									
- Amount transferred to profit or loss on sale	-	-	-	(108)	-	-	-	-	(108)
Total other comprehensive income, net of income tax	-	-	41	(108)	-	-	-	-	(67)
Total comprehensive income for the period	-	-	41	(108)	-	-	3,507	(136)	3,304
Transactions with owners, recorded directly in equity									
Contributions by and distributions to owners									
Purchase of own shares	-	-	-	-	-	(495)	-	-	(495)
Final dividend relating to 2008	-	-	-	-	-	-	(1,541)	-	(1,541)
Interim dividend relating to 2009	-	-	-	-	-	-	(1,539)	-	(1,539)
Total contributions by and distributions to owners	-	-	-	-	-	(495)	(3,080)	-	(3,575)
Balance at 31 December 2009	150	21,085	(258)	258	20	(940)	11,684	2,144	34,143

Consolidated statement of changes in equity (continued)

	Attributable to equity holders of the Company								
	Share capital	Share premium account	Foreign currency translation reserve	Revaluation reserve	Capital redemption reserve	Treasury shares	Retained earnings	Non-controlling interests	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2008	150	21,085	-	1,382	20	-	15,419	4,430	42,486
Total comprehensive income for the period									
Profit / (loss) for 2008	-	-	-	-	-	-	519	(1,517)	(998)
Other comprehensive income, net of income tax									
Foreign currency translation reserve	-	-	(299)	-	-	-	-	-	(299)
Revaluation reserve									
- Revaluation of freehold premises	-	-	-	(974)	-	-	-	-	(974)
- Amount transferred to profit or loss on sale	-	-	-	(42)	-	-	42	-	-
Total other comprehensive income, net of income tax	-	-	(299)	(1,016)	-	-	42	-	(1,273)
Total comprehensive income for the period	-	-	(299)	(1,016)	-	-	561	(1,517)	(2,271)
Transactions with owners, recorded directly in equity									
Contributions by and distributions to owners									
Sale of Arbutnot Commercial Finance Limited	-	-	-	-	-	-	-	(26)	(26)
Purchase of own shares	-	-	-	-	-	(445)	-	-	(445)
Final dividend relating to 2007	-	-	-	-	-	-	(3,361)	(607)	(3,968)
New share capital subscribed	-	213	-	-	-	-	-	-	213
Transfer to retained earnings in lieu of cash dividends	-	(213)	-	-	-	-	213	-	-
Interim dividend relating to 2008	-	-	-	-	-	-	(1,575)	-	(1,575)
Total contributions by and distributions to owners	-	-	-	-	-	(445)	(4,723)	(633)	(5,801)
Balance at 31 December 2008	150	21,085	(299)	366	20	(445)	11,257	2,280	34,414

Company statement of changes in equity

Attributable to equity holders of the Company

	Share capital £000	Share premium account £000	Capital redemption reserve £000	Treasury shares £000	Retained earnings £000	Total £000
Balance at 1 January 2008	150	21,085	20	-	5,000	26,255
Total comprehensive income for 2008, net of income tax	-	-	-	-	3,650	3,650
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Purchase of own shares	-	-	-	(445)	-	(445)
Final dividend relating to 2007	-	-	-	-	(3,361)	(3,361)
New share capital subscribed	-	213	-	-	-	213
Transfer to retained earnings in lieu of cash dividends	-	(213)	-	-	213	-
Interim dividend relating to 2008	-	-	-	-	(1,575)	(1,575)
Total contributions by and distributions to owners	-	-	-	(445)	(4,723)	(5,168)
Balance at 1 January 2009	150	21,085	20	(445)	3,927	24,737
Total comprehensive income for 2009, net of income tax	-	-	-	-	1,015	1,015
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Purchase of own shares	-	-	-	(495)	-	(495)
Final dividend relating to 2008	-	-	-	-	(1,541)	(1,541)
Interim dividend relating to 2009	-	-	-	-	(1,539)	(1,539)
Total contributions by and distributions to owners	-	-	-	(495)	(3,080)	(3,575)
Balance at 31 December 2009	150	21,085	20	(940)	1,862	22,177

Consolidated statement of cash flows

	Note	Year ended 31 December	
		2009 £000	2008 ⁽¹⁾ £000
Cash flows from operating activities			
Interest and similar income received		21,600	23,663
Interest and similar charges paid		(5,548)	(12,185)
Fees and commissions received		31,885	34,280
Net trading and other income		5,881	(3,818)
Recoveries on loans previously written off		202	213
Cash payments to employees and suppliers		(46,183)	(45,636)
Taxation received		207	1,280
Cash flows from operating profits / (losses) before changes in operating assets and liabilities		8,044	(2,203)
Changes in operating assets and liabilities:			
- net decrease in trading securities		787	15,478
- net increase in derivative financial instruments		(1,178)	-
- net (increase) / decrease in loans and advances to customers		(68,369)	6,442
- net (increase) / decrease in other assets		(3,701)	20,661
- net decrease in deposits from other banks		(12)	(9,828)
- net increase / (decrease) in amounts due to customers		93,109	(8,030)
- net decrease in other liabilities		(386)	(27,746)
Net cash inflow / (outflow) from operating activities		28,294	(5,226)
Cash flows from investing activities			
Disposal of financial investments		(1,623)	2,767
Purchase of computer software	20	(426)	(255)
Purchase of property, plant and equipment	21	(543)	(1,318)
Proceeds from disposal of businesses		-	3,565
Disposal of subsidiaries, net of cash and cash equivalents disposed	37	-	2,996
Proceeds from sale of property, plant and equipment		367	659
Purchases of debt securities		(248,688)	(277,343)
Proceeds from sale of debt securities		253,730	251,305
Net cash from investing activities		2,817	(17,624)
Cash flows from financing activities			
Purchase of treasury shares		(495)	(445)
Dividends paid		(3,080)	(5,330)
Net cash used in financing activities		(3,575)	(5,775)
Net increase / (decrease) in cash and cash equivalents		27,536	(28,625)
Cash and cash equivalents at 1 January		27,308	55,933
Cash and cash equivalents at 31 December	33	54,844	27,308

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

Company statement of cash flows

		Year ended 31 December	
		2009	2008
	Note	£000	£000
Cash flows from operating activities			
Dividends received from subsidiaries		4,126	5,627
Interest and similar income received		359	912
Interest and similar charges paid		(747)	(1,461)
Net trading and other income		741	(702)
Cash payments to employees and suppliers		(5,549)	(1,332)
Taxation received		1,121	1,632
Cash flows from operating profits before changes in operating assets and liabilities		51	4,676
Changes in operating assets and liabilities:			
- net decrease / (increase) in group company balances		4,923	(6,793)
- net decrease in other assets		384	58
- net increase in other liabilities		(201)	(378)
Net cash inflow / (outflow) from operating activities		5,157	(2,437)
Cash flows from investing activities			
Loans to subsidiary companies		(1,400)	2,000
Increase investment in subsidiary		(100)	-
Disposal of subsidiaries, net of cash and cash equivalents disposed		-	2,842
(Acquisition) / Disposal of financial investments		(101)	1,409
Disposal of property, plant and equipment		17	25
Purchase of property, plant and equipment	21	(7)	(3)
Net cash from investing activities		(1,591)	6,273
Cash flows from financing activities			
Purchase of treasury shares		(495)	(445)
Increase in borrowings		-	-
Dividends paid		(3,080)	(4,724)
Net cash used in financing activities		(3,575)	(5,169)
Net decrease in cash and cash equivalents		(9)	(1,333)
Cash and cash equivalents at 1 January		(2,609)	(1,276)
Cash and cash equivalents at 31 December	33	(2,618)	(2,609)

Principal accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

1.1. Reporting entity

Arbuthnot Banking Group PLC is a company domiciled in United Kingdom. The registered address of the Arbuthnot Banking Group PLC is One Arleston Way, Solihull B90 4LH. The consolidated financial statements of the Arbuthnot Banking Group PLC as at and for the year ended 31 December 2009 comprise the Arbuthnot Banking Group PLC and its subsidiaries (together referred to as the "Group" and individually as "subsidiaries"). The Company is primarily involved in banking and financial services.

1.2. Basis of presentation

The Group's consolidated financial statements and the Company's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs as adopted and endorsed by the EU), IFRIC Interpretations and the Companies Act 2006 applicable to companies reporting under IFRS. They have been prepared under the historical cost convention, as modified by the revaluation of land and buildings, available-for-sale financial assets, and financial assets and financial liabilities at fair value through profit or loss.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 2.

The Group's business activities and financial position, the factors likely to affect its future development and performance, and its objectives and policies in managing the financial risks to which it is exposed and its capital are discussed in the Financial Review. The Directors have assessed, in the light of current and anticipated economic conditions, the Group's ability to continue as a going concern. The Directors confirm they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future. For this reason, they continue to adopt the 'going concern' basis for preparing accounts.

1.2.a) Standards, interpretations and amendments effective in 2009 - relevant to the Group

- IAS 1 (Revised), 'Presentation of financial statements'. Revises the overall requirements for the presentation of financial statements, guidance for their structure and minimum content requirements. The revised standard requires the presentation of all non-owner changes in equity within a statement of comprehensive income.
- IFRS 2 (Amendment), 'Share-based payment'. The amendment restricts the definition of vesting conditions to include only service conditions and performance conditions and deals with the accounting consequences of a failure to meet a condition other than a vesting condition including how to deal with cancellations by the counterparty and circumstances where neither the entity nor the counterparty is in a position to choose whether or not to meet a vesting condition.
- IAS 32 (Amendment), 'Financial instruments: Presentation', and IAS 1 (Amendment), 'Presentation of financial statements' – 'Puttable financial instruments and obligations arising on liquidation'. The amended standards require entities to classify puttable financial instruments and instruments, or components of instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation as equity, provided the financial instruments have particular features and meet specific conditions.
- IFRS 7 (Amendment), 'Financial instruments: Disclosure'. The amendment requires enhanced disclosures about fair value measurements and liquidity risk in respect of financial instruments. The main change relates to fair value measurements which should now be disclosed in a 3 level hierarchy that reflects the significance of the inputs. Specific disclosures are required for Level 3 (significant unobservable inputs), movements between level 1 and 2, and around changes in valuation techniques between different periods.
- IFRS 8, 'Operating segments'. IFRS 8 replaces IAS 14 Segment Reporting and requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes.
- Improvements to IFRSs. Sets out minor amendments to IFRS standards as part of annual improvements process.

1.2.b) Standards, interpretations and amendments to existing standards that are not yet effective and have not been early adopted by the Group

The following standards, interpretations and amendments to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 January 2010 or later periods, but the Group has not early adopted them:

- IFRS 3 (Revised), 'Business combinations' (effective from 1 July 2009). The revised standard continues to apply the acquisition method to business combinations, however, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the income statement. There is a choice on an acquisition-by-acquisition basis to measure the non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. All acquisition-related costs should be expensed.
- IAS 27 (Revised), 'Consolidated and separate financial statements' (effective from 1 July 2009). The revised standard requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control. Any remaining interest in an investee is re-measured to fair value in determining the gain or loss recognised in profit or loss where control over the investee is lost.
- IAS 24 (Revised), 'Related party disclosures' (effective from 1 January 2011). The revised standard includes an exemption from the disclosure requirements for related party transactions between "state-controlled" entities and includes a revised definition for related parties. The revised standard will not have a material impact on the Group's financial accounts.*
- IFRS 9, 'Financial instruments' (effective from 1 January 2013). This standard deals with the classification and measurement of financial assets and will replace IAS 39. The requirements of this standard represent a significant change from the existing requirements in IAS 39. The standard contains two primary measurement categories for financial assets: amortised cost and fair value. The standard eliminates the existing IAS 39 categories of 'held to maturity', 'available for sale' and 'loans and receivables'. The potential effect of this standard is currently being evaluated but it is expected to have a pervasive impact on the Group's financial statements, due to the nature of the Group's operations.*

* - The revised IAS 24 and IFRS 9 have not yet been endorsed by the EU.

Principal accounting policies

1.3. Consolidation

(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's shares of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Special purpose entities

Special purpose entities (SPEs) are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets, or the execution of a specific borrowing or lending transaction. SPEs are consolidated when the substance of the relationship between the Group and the entity and the evaluation of the Group's exposure to the risks and rewards of the SPE indicates control. The following circumstances may indicate control by the Group and would therefore require consolidation of the SPE:

- in substance, the activities of the SPE are being conducted on behalf of the entity according to its specific business needs so that the entity obtains benefits from the SPE's operation;
- in substance, the entity has the decision-making powers to obtain the majority of the benefits of the activities of the SPE or, by setting up an 'autopilot' mechanism, the entity has delegated these decision-making powers;
- in substance, the entity has rights to obtain the majority of the benefits of the SPE and therefore may be exposed to risks incident to the activities of the SPE; or
- in substance, the entity retains the majority of the residual or ownership risks related to the SPE or its assets in order to obtain benefits from its activities.

The assessment of whether the Group has control over an SPE is carried out at inception and the initial assessment is only reconsidered at a later date if there were any changes to the structure or terms of the SPE, or there were additional transactions between the Group and the SPE.

(c) Transactions and non-controlling interests

The Group applies a policy of treating transactions with non-controlling interests as transactions with parties external to the Group. Disposals to non-controlling interests results in gains and losses for the Group that are recorded in the income statement. Purchases from non-controlling interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

1.4. Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Group Board. The Group Board, which is responsible for allocating resources and assessing performance of the operating segments, has been identified as the chief operating decision maker. All transactions between segments are conducted on an arm's length basis. Income and expenses directly associated with each segment are included in determining segment performance. There are four main operating segments:

- Retail Banking
- International Private Banking
- UK Private Banking
- Investment Banking

1.5. Foreign currency translation

(a) Functional and presentational currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in pounds sterling, which is the Company's functional and the Group's presentational currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

(c) Group companies

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentational currency are translated into the presentation currency as follows:

- assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and
- all resulting exchange differences are recognised as a separate component of equity.

Principal accounting policies

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is partially disposed of or sold, exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

1.6. Interest income and expense

Interest income and expense are recognised in the statement of comprehensive income for all instruments measured at amortised cost using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group takes into account all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

1.7. Fee and commission income

Fees and commissions which are not considered integral to the effective interest rate are generally recognised on an accrual basis when the service has been provided. Loan commitment fees are deferred and recognised as an adjustment to the effective interest rate on the loan. Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party — such as the issue or the acquisition of shares or other securities or the purchase or sale of businesses — are recognised on completion of the underlying transaction. Asset and other management, advisory and service fees are recognised based on the applicable service contracts, usually on a time apportioned basis. The same principle is applied for financial planning and insurance services that are continuously provided over an extended period of time.

1.8. Gains less losses arising from dealing in securities

This includes the net gains arising from both buying and selling securities and from positions held in securities, including related interest income and dividends, recognised on trade-date - the date on which the Group commits to purchase or sell the asset.

1.9. Financial assets and financial liabilities

The Group classifies its financial assets and financial liabilities in the following categories: financial assets and financial liabilities at fair value through profit or loss; loans and receivables; held-to-maturity investments; available-for-sale financial assets and other financial liabilities. Management determines the classification of its investments at initial recognition. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(a) *Financial assets and financial liabilities at fair value through profit or loss*

This category comprises financial assets and financial liabilities held for trading and listed securities. All listed securities are held for trading. Financial assets and liabilities at fair value through profit or loss are initially recognised on trade-date — the date on which the Group becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities at fair value through profit or loss are subsequently carried at fair value.

(b) *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. Loans are recognised when cash is advanced to the borrowers. Loans and receivables are carried at amortised cost using the effective interest method.

(c) *Held-to-maturity*

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. Held-to-maturity investments are carried at amortised cost using the effective interest method.

(d) *Available-for-sale*

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. Included in available-for-sale are equity investments in special purpose vehicles set up to acquire and enhance the value of commercial properties and equity investments in unquoted vehicles. These investments are of a medium term nature. There is no open market for these assets and there are no available-for-sale debt securities. Unquoted equity securities whose fair value cannot reliably be measured are carried at cost. All other available-for-sale investments are carried at fair value. Fair value changes on the equity securities are recognised in other comprehensive income (fair value reserve) until the investment is sold or impaired. Once sold or impaired the cumulative gains or losses previously recognised in other comprehensive income is reclassified to profit or loss.

(e) *Other financial liabilities*

Other financial liabilities are non-derivative financial liabilities with fixed or determinable payments. Other financial liabilities are recognised when cash is received from the depositors. Other financial liabilities are carried at amortised cost using the effective interest method.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the statement of financial position. In transactions in which the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset. There has not been any instances where assets have only been partially derecognised.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

Principal accounting policies

Amortised cost measurement

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, minus principal payments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date. The fair value of assets and liabilities traded in active markets are based on current bid and offer prices respectively. If the market is not active the Group establishes a fair value by using appropriate valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis.

1.10. Derivative financial instruments

All derivatives are recognised at their fair value. Fair values are obtained from quoted market prices in active markets, including recent arm's length transactions. Derivatives are shown in the statement of financial position as assets when their fair value is positive and as liabilities when their fair value is negative. Changes in the fair value of derivatives are recognised immediately in the statement of comprehensive income.

1.11. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

1.12. Impairment of financial assets

(a) Assets carried at amortised cost

On an ongoing basis the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include, but are not limited to, the following:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Initiation of bankruptcy proceedings;
- Deterioration in the value of collateral;
- Deterioration of the borrower's competitive position;

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the income statement.

(b) Assets classified as available for sale

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

(c) Renegotiated loans

Loans that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans.

1.13. Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in 'intangible assets'. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

The Group reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place and carry goodwill at cost less accumulated impairment losses. Assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or "CGU"). For impairment testing purposes goodwill cannot be allocated to a CGU that is greater than a reported operating segment. CGUs to which goodwill has been allocated are aggregated so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination.

Principal accounting policies

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. Management considers the value in use for the core Arbuthnot Latham CGU (currently the only CGU with goodwill attached to it) to be the discounted cash flows over 5 years with a terminal value (2008: 5 years with a terminal value). The 5 year plan with a terminal value is considered to be appropriate as the goodwill relates to an ongoing well established business and not underlying assets with finite lives. A growth rate of 7% (2008: 7%) was used for income and 4% (2008: 4%) for expenditure from 2010 to 2012 (these rates were the best estimate of future forecasted performance), while a 4% (2008: 4%) percent growth rate for income and expenditure (a more conservative approach was taken for latter years as these were not budgeted for in detail as per the three year plan approved by the Board of Directors) was used for cash flows after the approved three year plan. Cash flows were discounted at a pre-tax rate of 12% (2008: 12%) to their net present value. The discount rate of 12% is considered to be appropriate after evaluating current market assessments of the time value of money and the risks specific to the assets or CGUs.

Impairment losses are recognised in profit and loss if the carrying amounts exceed the recoverable amounts.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives (three to five years).

Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred.

1.14. Property, plant and equipment

Land and buildings comprise mainly branches and offices and are stated at the latest valuation with subsequent additions at cost less depreciation. Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, applying the following annual rates, which are subject to regular review:

Freehold buildings	2%
Office equipment	5% to 15%
Computer equipment	20% to 33%
Motor vehicles	25%

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement. Depreciation on revalued freehold buildings is calculated using the straight-line method over the remaining useful life.

1.15. Leases

(a) As a lessor

Assets leased to customers under agreements which transfer substantially all the risks and rewards of ownership, with or without ultimate legal title, are classified as finance leases. When assets are held subject to finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

Assets leased to customers under agreements which do not transfer substantially all the risks and rewards of ownership are classified as operating leases. When assets are held subject to operating leases, the underlying assets are held at cost less accumulated depreciation. The assets are depreciated down to their estimated residual values on a straight line basis over the lease term. Lease rental income is recognised on a straight line basis over the lease term.

(b) As a lessee

Rentals made under operating leases are recognised in the income statement on a straight line basis over the term of the lease.

1.16. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises cash on hand and demand deposits, and cash equivalents comprise highly liquid investments that are convertible into cash with an insignificant risk of changes in value with a maturity of three months or less at the date of acquisition, including certain loans and advances to banks and building societies and short-term highly liquid debt securities.

1.17. Employee benefits

(a) Post-retirement obligations

The Group contributes to a defined contribution scheme and to individual defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees.

The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

There are no post-retirement benefits other than pensions.

(b) Share-based compensation

The Group operates a number of equity-settled, share-based compensation plans. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. At each balance sheet date, the entity revises its estimates of the number of options that are expected to vest. It recognises the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity.

The proceeds received net of any directly attributable transaction costs are credited to share capital (nominal value) and share premium when the options are exercised.

Principal accounting policies

The grant by the Company of options over its equity instruments to the employees of subsidiary undertakings in the Group is treated as a capital contribution. The fair value of employee services received, measured by reference to the grant date fair value, is recognised over the investing period as an increase to investment in subsidiary undertakings, with a corresponding credit to equity.

1.18. Taxation

Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise. Income tax recoverable on tax allowable losses is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits.

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax is not accounted for if it arises from the initial recognition of goodwill, the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the statement of financial position date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

1.19. Issued debt and equity securities

Issued financial instruments or their components are classified as liabilities where the contractual arrangement results in the Group having a present obligation to either deliver cash or another financial asset to the holder, to exchange financial instruments on terms that are potentially unfavourable. Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Company. The components of issued financial instruments that contain both liability and equity elements are accounted for separately with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component.

Financial liabilities, other than trading liabilities and financial liabilities designated at fair value, are carried at amortised cost using the effective interest method as set out in policy 1.5. Equity instruments, including share capital, are initially recognised at net proceeds, after deducting transaction costs and any related income tax. Dividend and other payments to equity holders are deducted from equity, net of any related tax.

Notes to the consolidated financial statements

1.20. Share capital

(a) Share issue costs

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

(b) Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are approved.

(b) Share buybacks

Where any group company purchases the company's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the company's equity holders until the shares are cancelled or reissued.

1.21. Fiduciary activities

The Group commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

2. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

2.1. Estimation uncertainty

Credit losses

The Group reviews its loan portfolios and held-to-maturity investments to assess impairment at least on a half-yearly basis. The basis for evaluating impairment losses is described in accounting policy 1.11. Where financial assets are individually evaluated for impairment, management uses their best estimates in calculating the net present value of future cash flows. Management has to make judgements on the financial position of the counterparty and the net realisable value of collateral, in determining the expected future cash flows.

In determining whether an impairment loss should be recorded in the income statement, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans or held-to-maturity investments with similar credit characteristics, before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Goodwill impairment

The accounting policy for goodwill is described in note 1.12 (a). The Company reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. Significant management judgements are made in estimations, to evaluate whether an impairment of goodwill is necessary. Impairment testing is done at CGU level and the following two items, with judgements surrounding them, have a significant impact on the estimations used in determining the necessity of an impairment charge:

- Future cash flows - Cash flow forecasts reflect managements view of future business forecasts at the time of the assessment. A detailed three year budget is done every year and management also uses judgement in applying a growth rate. The accuracy of future cash flows is subject to a high degree of uncertainty in volatile market conditions. During such conditions, management would do impairment testing more frequently than annually to ensure that the assumptions applied are still valid in the current market conditions.
- Discount rate - Management also apply judgement in determining the discount rate used to discount future expected cash flows. The discount rate is derived from the cost of capital for each CGU.

At the time of the impairment testing, if the future expected cash flows decline and/or the cost of capital has increased, then the recoverable amount will reduce.

2.2. Judgements

Impairment of equity securities

A significant or prolonged decline in the fair value of an equity security is objective evidence of impairment. The Group regards a decline of more than 20 percent in fair value as "significant" and a decline in the quoted market price that persists for nine months or longer as "prolonged".

Valuation of financial instruments

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices. If the market is not active the Group establishes a fair value by using appropriate valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis. The objective of valuation techniques is to determine the fair value of the financial instrument at the reporting date as the price that would have been agreed between active market participants in an arm's length transaction.

The Group measures fair value using the following fair value hierarchy that reflects the significance of the inputs used in making measurements:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Notes to the consolidated financial statements

The tables below analyses financial instruments measured at fair value by the level in the fair value hierarchy into which the measurement is categorised:

At 31 December 2009	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Trading securities - long positions	2,633	26	-	2,659
Derivative financial instruments	-	236	-	236
	2,633	262	-	2,895
Trading securities - short positions	959	-	-	959
	959	-	-	959

At 31 December 2008	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Trading securities - long positions	3,093	158	272	3,523
	3,093	158	272	3,523
Trading securities - short positions	1,036	-	-	1,036
Derivative financial instruments	-	942	-	942
	1,036	942	-	1,978

The following table reconciles the movement in level 3 financial instruments during the year:

Movement in level 3	2009 £000	2008 £000
At 1 January	272	272
Losses recognised in the profit and loss	(272)	-
At 31 December	-	272

There were no significant transfers between level 1 and level 2 during the year.

Notes to the consolidated financial statements

3. Maturity analysis of assets and liabilities

The table below shows the maturity analysis of assets and liabilities as at 31 December 2009:

At 31 December 2009	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash	230	-	230
Derivative financial instruments	236	-	236
Loans and advances to banks	54,614	-	54,614
Loans and advances to customers	203,751	25,971	229,722
Trading securities - long positions	2,659	-	2,659
Debt securities held-to-maturity	119,559	8,038	127,597
Current tax asset	1,805	-	1,805
Other assets	16,674	2,080	18,754
Financial investments	1,533	3,524	5,057
Intangible assets	-	2,906	2,906
Property, plant and equipment	-	8,552	8,552
Deferred tax asset	-	383	383
Total assets	401,061	51,454	452,515
LIABILITIES			
Deposits from banks	2,886	-	2,886
Trading securities - short positions	959	-	959
Deposits from customers	384,583	1,416	385,999
Current tax liability	2,208	-	2,208
Other liabilities	13,214	3	13,217
Debt securities in issue	-	13,022	13,022
Deferred tax liabilities	81	-	81
Total liabilities	403,931	14,441	418,372

The table below shows the maturity analysis of assets and liabilities as at 31 December 2008:

At 31 December 2008	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash	3,369	-	3,369
Loans and advances to banks	15,939	-	15,939
Loans and advances to customers	141,547	22,187	163,734
Trading securities - long positions	3,523	-	3,523
Debt securities held-to-maturity	140,639	-	140,639
Current tax asset	1,679	-	1,679
Other assets	14,348	705	15,053
Financial investments	-	3,434	3,434
Intangible assets	-	2,831	2,831
Property, plant and equipment	-	9,448	9,448
Deferred tax asset	-	106	106
Total assets	321,044	38,711	359,755
LIABILITIES			
Deposits from banks	2,898	-	2,898
Trading securities - short positions	1,036	-	1,036
Derivative financial instruments	942	-	942
Deposits from customers	292,054	836	292,890
Other liabilities	9,771	3,832	13,603
Debt securities in issue	-	13,972	13,972
Total liabilities	306,701	18,640	325,341

The comparatives have been reclassified to align with current year presentation (see note 39).

Notes to the consolidated financial statements

4. Financial risk management

Strategy

By their nature, the Group's activities are principally related to the use of financial instruments. The Directors and senior management of the Group have formally adopted a group Risk and Controls Policy which sets out the Board's attitude to risk and internal controls. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board, in addition to which key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

The principal non-operational risks inherent in the Group's business are credit, market and liquidity risks.

a.) Credit risk

The Company and Group take on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment provisions are provided for losses that have been incurred at the balance sheet date. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration in the Company and Group's portfolio, could result in losses that are different from those provided for at the balance sheet date. Credit risk is managed through the Credit Committees of the banking subsidiaries, with significant exposures also being approved by the Group Risk Committee.

The Company and Group structure the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower or groups of borrowers. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. The limits are approved periodically by the Board of Directors and actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of collateral for fund advances, which is common practice. The principal collateral types for loans and advances include, but are not limited to:

- Charges over residential and commercial properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities;
- Personal guarantees; and
- Charges over other chattels

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In order to minimise any potential credit loss the Group will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances. Repossessed collateral, not readily convertible into cash, is made available for sale in an orderly fashion, with the proceeds used to reduce or repay the outstanding indebtedness. Where excess funds are available after the debt has been repaid, they are available either for other secured lenders with lower priority or are returned to the customer.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

Notes to the consolidated financial statements

The Group's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

	2009 £000	2008 ⁽¹⁾ £000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Cash	230	3,369
Derivative financial instruments	236	-
Loans and advances to banks	54,614	15,939
Loans and advances to customers - Arbuthnot Latham	177,744	151,183
Loan and advances to customers - Secure Trust Bank	51,425	12,551
Trading securities - long positions	2,659	3,523
Debt securities held-to-maturity	127,597	140,639
Financial investments	5,057	3,434
Other assets	15,657	8,762
Credit risk exposures relating to off-balance sheet assets are as follows:		
Guarantees	1,135	816
Loan commitments and other credit related liabilities	14,163	15,596
At 31 December	450,517	355,812

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

The Company's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

	2009 £000	2008 £000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Due from subsidiary undertakings	23,198	20,960
Financial investments	465	364
Other debtors	1,703	2,087
Credit risk exposures relating to off-balance sheet assets are as follows:		
Guarantees	2,500	2,500
At 31 December	27,866	25,911

The above table represents the maximum credit risk exposure (net of impairment) to the Group and Company at 31 December 2009 and 2008 without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures are based on the net carrying amounts as reported in the balance sheet.

Concentration risk

The Group is well diversified in the UK, being exposed to retail banking, private banking and investment banking. Management assesses the potential concentration risk from a number of areas including:

- geographical concentration
- product concentration; and
- high value residential properties

Due to the well diversified nature of the Group and the significant collateral held against the loan book, the Directors do not consider there to be a potential material exposure arising from concentration risk.

4.b.) Operational risk

The Group's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness and to avoid control procedures that restrict initiatives and creativity. Operational risk arises from all of the Group's operations.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the senior management within each subsidiary.

Compliance with Group standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of the Internal Audit reviews are discussed with the company's senior management, with summaries submitted to the Arbuthnot Banking Group Audit Committee

4.c.) Market risk

Price risk

The Company and Group is exposed to equity securities price risk because of investments held by the Group and classified on the consolidated balance sheet either as available-for-sale or at fair value through the income statement. The Group is not exposed to commodity price risk. To manage its price risk arising from investments in equity securities, the Group diversifies its portfolio. Diversification of the portfolio is done in accordance with the limits set by the Group.

Based upon the trading book exposure given in note 15 and the financial investment exposure (in note 19), a stress test scenario of a 10% (2008: 10%) decline in market prices, with all other things being equal, would result in a £250,000 (2008: £158,000) decrease in the Group's income and equity.

Notes to the consolidated financial statements

Based upon the financial investment exposure given in note 19, a stress test scenario of a 10% (2008: 10%) decline in market prices, with all other things being equal, would result in a £46,500 (2008: £42,100) decrease in the Company's income and equity.

Currency risk

The Company and Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure for both overnight and intra-day positions, which are monitored daily. The table below summarises the Group's exposure to foreign currency exchange rate risk at 31 December 2009. Included in the table below are the Group's assets and liabilities at carrying amounts, categorised by currency.

At 31 December 2009	GBP (£) £000	USD (\$) £000	Euro (€) £000	Other £000	Total £000
ASSETS					
Cash	230	-	-	-	230
Derivative financial instruments	236	-	-	-	236
Loans and advances to banks	48,002	4,587	816	1,209	54,614
Loans and advances to customers	192,681	3,579	31,430	2,032	229,722
Trading securities - long positions	2,199	460	-	-	2,659
Debt securities held-to-maturity	127,597	-	-	-	127,597
Current tax asset	1,805	-	-	-	1,805
Financial investments	18,577	41	136	-	18,754
Other assets	8,552	-	-	-	8,552
Total assets	399,879	8,667	32,382	3,241	444,169
LIABILITIES					
Deposits from banks	1,241	7	21	1,617	2,886
Trading securities - short positions	959	-	-	-	959
Deposits from customers	370,600	8,720	5,475	1,204	385,999
Current tax liability	2,208	-	-	-	2,208
Other liabilities	13,215	1	1	-	13,217
Debt securities in issue	-	-	13,022	-	13,022
Total liabilities	388,223	8,728	18,519	2,821	418,291
Net on-balance sheet position	11,656	(61)	13,863	420	25,878
Credit commitments	13,865	3	295	-	14,163

The table below summarises the Group's exposure to foreign currency exchange risk at 31 December 2008:

At 31 December 2008	GBP (£) £000	USD (\$) £000	Euro (€) £000	Other £000	Total £000
ASSETS					
Cash	3,369	-	-	-	3,369
Loans and advances to banks	10,381	4,410	1,092	56	15,939
Loans and advances to customers	136,940	3,159	23,635	-	163,734
Trading securities - long positions	3,067	456	-	-	3,523
Debt securities held-to-maturity	140,639	-	-	-	140,639
Current tax asset	1,679	-	-	-	1,679
Financial investments	364	57	3,013	-	3,434
Other assets	13,575	370	1,108	-	15,053
Total assets	310,014	8,452	28,848	56	347,370
LIABILITIES					
Deposits from banks	2,823	11	64	-	2,898
Trading securities - short positions	1,036	-	-	-	1,036
Deposits from customers	279,652	7,905	5,292	41	292,890
Derivative financial instruments	942	-	-	-	942
Other liabilities	13,389	33	181	-	13,603
Debt securities in issue	-	-	13,972	-	13,972
Total liabilities	297,842	7,949	19,509	41	325,341
Net on-balance sheet position	12,172	503	9,339	15	22,029
Credit commitments	15,231	1	364	-	15,596

* The 2008 Group comparative schedule has been expanded to include all the categories as per the statement of financial position, previously Cash, Trading securities - long positions, Current tax asset, Intangible assets, Property, plant and equipment and Deferred tax asset were shown as part of Other assets and Trading securities - short positions and Derivative financial instruments were shown as part of Other liabilities. The 2008 comparatives have also been reclassified to align with the current year presentation (see note 39) and there was also a reclassification of £14,598,000 from GBP to Euro under Loans and advances to customers.

Notes to the consolidated financial statements

A 10% strengthening of the pound against the US dollar would lead to negligible (2008: £50,000) decrease in Group profits and equity, while a 10% weakening of the pound against the US dollar would lead to the same increase in Group profits and equity. Similarly a 10% strengthening of the pound against the Euro would lead to £42,000 (2008: £52,000) decrease in Group profits and equity, while a 10% weakening of the pound against the Euro would lead to the same increase in Group profits and equity. The above results are after taking into account the effect of derivative financial instruments (see note 23), which covers most of the net exposure in each currency.

The table below summarises the Company's exposure to foreign currency exchange rate risk at 31 December 2009:

At 31 December 2009	GBP (£)	USD (\$)	Euro (€)	Other	Total
	£000	£000	£000	£000	£000
ASSETS					
Due from subsidiary undertakings	7,814	-	13,352	2,032	23,198
Financial investments	465	-	-	-	465
Other debtors	1,703	-	-	-	1,703
Shares in subsidiary undertakings	28,624	-	-	-	28,624
Total assets	38,606	-	13,352	2,032	53,990
LIABILITIES					
Deposits from banks	1,001	-	-	1,617	2,618
Due to subsidiary undertakings	15,621	-	-	-	15,621
Debt securities in issue	(297)	-	13,319	-	13,319
Total liabilities	16,325	-	13,319	1,617	31,261
Net on-balance sheet position	22,281	-	33	415	22,729

The table below summarises the Company's exposure to foreign currency exchange risk at 31 December 2008:

At 31 December 2008	GBP (£)	USD (\$)	Euro (€)	Other	Total
	£000	£000	£000	£000	£000
ASSETS					
Due from subsidiary undertakings	4,727	-	14,598	1,635	20,960
Financial investments	364	-	-	-	364
Other debtors	2,087	-	-	-	2,087
Shares in subsidiary undertakings	28,524	-	-	-	28,524
Total assets	35,702	-	14,598	1,635	51,935
LIABILITIES					
Deposits from banks	1,004	-	-	1,605	2,609
Due to subsidiary undertakings	9,860	-	-	-	9,860
Debt securities in issue	(310)	-	14,282	-	14,282
Total liabilities	10,554	-	14,282	1,605	26,441
Net on-balance sheet position	25,148	-	316	30	25,494

A 10% strengthening of the pound against the Euro would lead to £3,000 (2008: £32,000) decrease in the Company profits and equity, conversely a 10% weakening of the pound against the Euro would lead to the same increase in the Company profits and equity. A 10% strengthening of the pound against the Swiss Franc would lead to £43,000 (2008: £3,000) decrease in the Company profits and equity, conversely a 10% weakening of the pound against the Swiss Franc would lead to the same increase in the Company profits and equity.

Interest rate risk

Interest rate risk is the potential adverse impact on the Company and Group's future cash flows from changes in interest rates; and arises from the differing interest rate risk characteristics of the Company and Group's assets and liabilities. In particular, fixed rate savings and borrowing products expose the Group to the risk that a change in interest rates could cause either a reduction in interest income or an increase in interest expense relative to variable rate interest flows. The Group seeks to "match" interest rate risk on either side of the balance sheet. However, this is not a perfect match and interest rate risk is present on: Money market deposits of a fixed rate nature, Fixed rate loans and Fixed rate savings accounts. The principal interest rate mismatch is in Arbutnot Latham and this is monitored on a daily basis in conjunction with liquidity and capital. The interest rate mismatch is daily monitored, throughout the maturity bandings of the book on a parallel scenario for both 50 and 100 basis points movement. This typically results in a pre-tax mismatch of £0.1m (2008: £0.1m to £0.2m) for the Group, with the same impact to equity pre-tax. The Company has no fixed rate exposures, but a change of 50 basis points on variable rates would impact pre-tax profits and equity by £7,000 (2008: £7,000).

4.d.) Liquidity risk

The Company and Group is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs and guarantees, and from margin and other calls on cash-settled trading securities. The Group does not maintain cash resources to meet all of these needs, as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Group's liquidity is therefore managed on a mismatch basis, the mismatch being the difference between the levels of assets and liabilities in the same maturity bands. The Group's aim is to maintain a prudent liquidity margin when compared with the mismatch criteria set by the regulators. The Company and Group maintains long-term committed bank facilities and use is made of certificates of deposit (debt securities) in the management of liquidity. The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Group. It is normal practice for banks to operate liquidity on a mismatch basis.

Notes to the consolidated financial statements

The table below analyses the contractual undiscounted cash flows for the Group into relevant maturity groupings at 31 December 2009:

At 31 December 2009	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Non-derivative liabilities						
Deposits from banks	2,886	(2,886)	(2,886)	-	-	-
Trading securities - short positions	959	(959)	(959)	-	-	-
Deposits from customers	385,999	(386,177)	(317,736)	(66,931)	(1,510)	-
Other liabilities	13,217	(13,367)	(4,564)	(8,303)	(500)	-
Debt securities in issue	13,022	(13,022)	-	-	-	(13,022)
Issued guarantee contracts		(1,135)	(1,135)	-	-	-
Unrecognised loan commitments		(14,163)	(14,163)	-	-	-
	416,083	(431,709)	(341,443)	(75,234)	(2,010)	(13,022)
Derivative liabilities						
Risk management:	-	-	-	-	-	-
- Inflows		-	-	-	-	-
- Outflows		-	-	-	-	-
	-	-	-	-	-	-

The table below analyses the contractual undiscounted cash flows for the Group into relevant maturity groupings at 31 December 2008:

At 31 December 2008	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Non-derivative liabilities						
Deposits from banks	2,898	(6,023)	(2,956)	(3,067)	-	-
Trading securities - short positions	1,036	(1,036)	(1,036)	-	-	-
Deposits from customers	292,890	(293,097)	(219,266)	(72,881)	(950)	-
Other liabilities	13,603	(14,592)	(12,771)	(1,435)	(386)	-
Debt securities in issue	13,972	(13,972)	-	-	-	(13,972)
Issued guarantee contracts		(816)	(816)	-	-	-
Unrecognised loan commitments		(15,596)	(15,596)	-	-	-
	324,399	(345,132)	(252,441)	(77,383)	(1,336)	(13,972)
Derivative liabilities						
Risk management:	942	-	-	-	-	-
- Inflows		9,188	8,980	208	-	-
- Outflows		(10,130)	(9,927)	(203)	-	-
	942	(942)	(947)	5	-	-

The comparatives have been reclassified to align with current year presentation (see note 39).

Notes to the consolidated financial statements

The table below analyses the contractual undiscounted cash flows for the Company into relevant maturity groupings at 31 December 2009:

At 31 December 2009	Carrying amount	Gross nominal inflow/ (outflow)	Not more than 3 months	More than 3 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years
	£000	£000	£000	£000	£000	£000
Non-derivative liabilities						
Deposits from banks	2,618	(2,618)	(2,618)	-	-	-
Due to subsidiary undertakings	15,621	(15,621)	(15,621)	-	-	-
Accruals	630	(630)	-	(630)	-	-
Debt securities in issue	13,022	(13,022)	-	-	-	(13,022)
Issued financial guarantee contracts	-	(2,500)	(2,500)	-	-	-
	31,891	(34,391)	(20,739)	(630)	-	(13,022)

The table below analyses the contractual undiscounted cash flows for the Company into relevant maturity groupings at 31 December 2008:

At 31 December 2008	Carrying amount	Gross nominal inflow/ (outflow)	Not more than 3 months	More than 3 months but less than 1 year	More than 1 year but less than 5 years	More than 5 years
	£000	£000	£000	£000	£000	£000
Non-derivative liabilities						
Deposits from banks	2,609	(2,609)	(2,609)	-	-	-
Due to subsidiary undertakings	9,860	(9,860)	(9,860)	-	-	-
Accruals	831	(831)	-	(831)	-	-
Debt securities in issue	13,972	(13,972)	-	-	-	(13,972)
Issued financial guarantee contracts	-	(2,500)	(2,500)	-	-	-
	27,272	(29,772)	(14,969)	(831)	-	(13,972)

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates and exchange rates.

Fiduciary activities

The Group provides trustee, investment management and advisory services to third parties, which involve the Group making allocation and purchase and sale decisions in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these financial statements. These services give rise to the risk that the Group may be accused of maladministration or underperformance. At the balance sheet date, the Group had investment management accounts amounting to approximately £179 million (2008: £156 million). Additionally the Group provides investment advisory services.

Notes to the consolidated financial statements

4.e.) Financial assets and liabilities

The tables below sets out the Group's financial assets and financial liabilities into the respective classifications:

At 31 December 2009	Note	Trading £000	Designated at fair value £000	Held-to- maturity £000	Loans and receivables £000	Available- for-sale £000	Other amortised cost £000	Total carrying amount £000	Fair value £000
Cash	13	-	-	-	230	-	-	230	230
Derivative financial instruments	24	236	-	-	-	-	-	236	236
Loans and advances to banks	14	-	-	-	54,614	-	-	54,614	54,614
Loans and advances to customers	16	-	-	-	229,722	-	-	229,722	229,722
Trading securities - long positions	15	2,659	-	-	-	-	-	2,659	2,659
Debt securities held-to-maturity	18	-	-	127,597	-	-	-	127,597	127,597
Financial investments	19	465	-	-	-	4,592	-	5,057	5,057
		3,360	-	127,597	284,566	4,592	-	420,115	420,115
Deposits from banks	23	-	-	-	-	-	2,886	2,886	2,886
Trading securities - short positions	15	959	-	-	-	-	-	959	959
Derivative financial instruments	24	-	-	-	-	-	-	-	-
Deposits from customers	25	-	-	-	-	-	385,999	385,999	385,999
Debt securities in issue	27	-	-	-	-	-	13,022	13,022	13,022
		959	-	-	-	-	401,907	402,866	402,866

At 31 December 2008	Note	Trading £000	Designated at fair value £000	Held-to- maturity £000	Loans and receivables £000	Available- for-sale £000	Other amortised cost £000	Total carrying amount £000	Fair value £000
Cash	13	-	-	-	3,369	-	-	3,369	3,369
Loans and advances to banks	14	-	-	-	15,939	-	-	15,939	15,939
Loans and advances to customers	16	-	-	-	163,734	-	-	163,734	163,734
Trading securities - long positions	15	3,523	-	-	-	-	-	3,523	3,523
Debt securities held-to-maturity	18	-	-	140,639	-	-	-	140,639	140,639
Financial investments	19	421	-	-	-	3,013	-	3,434	3,434
		3,944	-	140,639	183,042	3,013	-	330,638	330,638
Deposits from banks	23	-	-	-	-	-	2,898	2,898	2,898
Trading securities - short positions	15	1,036	-	-	-	-	-	1,036	1,036
Derivative financial instruments	24	942	-	-	-	-	-	942	942
Deposits from customers	25	-	-	-	-	-	292,890	292,890	292,890
Debt securities in issue	27	-	-	-	-	-	13,972	13,972	13,972
		1,978	-	-	-	-	309,760	311,738	311,738

Notes to the consolidated financial statements

5. Capital management

The Group's capital management policy is focused on optimising shareholder value. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

In accordance with the EU's Capital Requirements Directive (CRD) and the required parameters set out in the FSA Handbook (BIPRU 2.2), the Individual Capital Assessment Process (ICAAP) is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management. The Group's regulated entities are also the principal trading subsidiaries as detailed in Note 35.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a "Pillar I plus" approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequately to cover managements' anticipated risks. Where the Board considered that the Pillar I calculations did not reflect the risk, an additional capital add-on in Pillar II is applied, as per the Individual Capital Guidance (ICG) issued by the FSA.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders' funds, non-controlling interests, after deducting goodwill and other intangible assets.
- Lower Tier 2 comprises qualifying subordinated loan capital and revaluation reserves. Lower Tier 2 capital cannot exceed 50% of tier 1 capital.

The following table shows the regulatory capital resources as managed by the Group:

	2009	2008
	£000	£000
Tier 1		
Share capital	150	150
Share premium account	21,085	21,085
Retained earnings	11,684	11,257
Other reserves	(1,178)	(724)
Non-controlling	2,144	2,280
Goodwill	(1,991)	(1,991)
Other deductions	(915)	(840)
Total tier 1 capital	30,979	31,217
Tier 2		
Revaluation reserve	258	366
Debt securities in issue	13,022	13,972
Total tier 2 capital	13,280	14,338
Total tier 1 & tier 2 capital	44,259	45,555

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The FSA's last review of the Group's ICAAP was last conducted in December 2007 and the regulatory capital requirements for all entities have subsequently been agreed, as part of the ICG issued by the FSA. The FSA sets ICG for each UK bank calibrated by references to its Capital Resources Requirement, broadly equivalent to 8 percent of risk weighted assets and thus representing the capital required under Pillar 1 of the Basel II framework. The ICAAP is a key input into the FSA's ICG setting process, which addresses the requirements of Pillar 2 of the Basel II framework. The FSA's approach is to monitor the available capital resources in relation to the ICG requirement. Each entity maintains an extra internal buffer and capital ratios are reviewed on a monthly basis to ensure that external requirements are adhered to. All regulated entities have complied with all of the externally imposed capital requirements to which they are subject.

6. Fee and commission income

	2009	2008
	£000	£000
Fee and commission income		
Trust and other fiduciary fee income	1,922	1,997
Stockbroking fee and commission income	13,580	12,818
Other fee income	16,314	20,426
	31,816	35,241

7. Other income

Other income mainly consist of a contribution of £0.5m towards the cost of the Swiss entity received from a possible investor, and income released relating to business assets sold in the prior year of £1.1m (see note 8).

Notes to the consolidated financial statements

8. Gain on sale of business assets

In June 2008, the Group announced that its subsidiary, Secure Trust Bank PLC, as part of its restructuring process, sold its insurance branch network to the UK's leading high street insurance retailer, Swinton. At a Group level, this generated a gain on disposal of business assets of £2,419,100.

Also in June 2008, the Group announced that its subsidiary, Arbutnot Latham & Co., Ltd, sold its pension administration business to Premier Pension Services. At a Group level, this generated a gain on disposal of business assets of £658,300.

As part of the sale of business assets during 2008, accruals and deferred income included a provision in respect of various warranties included in the respective Sale and Purchase Agreements, refer to Note 26 for further details. During 2009 these warranties (£482,000) were written back to the profit and loss account as they expired and £688,000 of trade payables were written off.

9. Operating profit on ordinary activities before tax

Operating expenses comprise:	2009	2008
	£000	£000
Staff costs, including Directors:		
Wages and salaries	23,255	21,761
Social security costs	2,458	2,556
Pension costs	1,448	1,640
Amortisation of computer software (Note 20)	351	366
Depreciation (Note 21)	1,171	1,215
Profit on disposals of property, plant and equipment	(99)	(168)
Financial Services Compensation Scheme Levy	258	491
Charitable donations	27	20
Operating lease rentals	2,249	2,312
Restructuring costs	127	1,458
Other administrative expenses	15,155	15,993
Total operating expenses	46,400	47,644

The auditors' remuneration for the audit of the Company's accounts was £70,000 (2008: £41,000) and fees payable for the audit of the accounts of subsidiaries of the Company was £205,000 (2008: £316,000). Remuneration of the auditors for non-audit services was: services related to taxation £15,000 (2008: £24,000) and all other services £25,000 (2008: £46,000).

Notes to the consolidated financial statements

10. Average number of employees

	2009	2008
Retail banking	208	257
Private banking	121	126
Investment banking	72	72
Group	14	14
	415	469

11. Income tax (credit) / expense

	2009	2008
	£000	£000
United Kingdom corporation tax at 28% (2008: 28.5%)		
Current taxation		
Corporation tax charge - current year	1,691	(916)
Corporation tax charge - adjustments in respect of prior years	95	(288)
	1,786	(1,204)
Deferred taxation		
Origination and reversal of temporary differences	(212)	52
Adjustments in respect of prior years	105	-
	(107)	52
Income tax expense / (credit)	1,679	(1,152)
Tax reconciliation		
Profit / (loss) before tax	5,050	(2,150)
Tax at 28% (2008: 28.5%)	1,414	(613)
Permanent differences	65	(251)
Tax rate change	-	-
Prior period adjustments	200	(288)
Corporation tax (credit) / charge for the year	1,679	(1,152)

During 2008, as a result of the change in UK Corporation Tax rates which was effective from 1 April 2008, deferred tax balances were remeasured. Deferred tax relating to temporary differences which were expected to reverse prior to 1 April 2008 were measured at 30% and deferred tax relating to temporary differences expected to reverse after 1 April 2008 are measured at the tax rate of 28% as these are the tax rates that apply on reversal.

12. Earnings per ordinary share

Basic and fully diluted

Earnings per ordinary share are calculated on the net basis by dividing the profit attributable to equity holders of the Company of £3,507,000 (2008: £519,000) by the weighted average number of ordinary shares 14,999,619 (2008: 14,999,619) in issue during the year. There is no difference between basic and fully diluted earnings per ordinary share.

Notes to the consolidated financial statements

13. Cash

	2009	2008
	£000	£000
Cash in hand included in cash and cash equivalents (Note 33)	230	3,369

14. Loans and advances to banks

	2009	2008 ⁽¹⁾
	£000	£000
Placements with banks included in cash and cash equivalents (Note 33)	54,614	15,939

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

The table below presents an analysis of loans and advances to banks by rating agency designation as at 31 December, based on Moody's long term ratings:

	2009	2008 ⁽¹⁾
	£000	£000
Aaa	-	5,973
Aa1	-	4,517
Aa2	31	5,381
Aa3	54,583	68
A1	-	-
A2	-	-
	54,614	15,939

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

None of the loans and advances to banks is either past due or impaired.

15. Trading securities, all held at fair value through profit or loss

	2009	2008
	£000	£000
<i>Unlisted equity securities:</i>		
Long positions	80	430
<i>Listed equity securities:</i>		
Long positions	2,579	3,093
Short positions	(959)	(1,036)

The following table shows the Group's trading book exposure to market price risk for the year ended 31 December 2009:

	Highest exposure £000	Lowest exposure £000	Average exposure £000	Exposure as at 31 December £000
Equities:				
Long	4,298	1,575	2,824	2,659
Short	(1,976)	(516)	(1,131)	(959)

The following table shows the Group's trading book exposure to market price risk for the year ended 31 December 2008:

	Highest exposure £000	Lowest exposure £000	Average exposure £000	Exposure as at 31 December £000
Equities:				
Long	23,070	2,921	11,767	3,523
Short	(7,505)	(669)	(4,628)	(1,036)

The average exposure has been calculated on a daily basis. The highest and lowest exposures occurred on different dates and therefore a net position of these exposures does not reflect a spread of the trading book. The basis on which the trading book is valued each day is given in the accounting policies in note 1.9.

Notes to the consolidated financial statements

16. Loans and advances to customers

	2009	2008 ⁽¹⁾
	£000	£000
Gross loans and advances	237,023	168,856
Less: allowances for impairment on loans and advances (Note 17)	(7,301)	(5,122)
	229,722	163,734

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

For a maturity profile of loans and advances to customers, refer to Note 4.

Loans and advances to customers include finance lease receivables as follows:	2009	2008
	£000	£000
Gross investment in finance lease receivables:		
- No later than 1 year	158	1,485
- Later than 1 year and no later than 5 years	111	108
- Later than 5 years	2	-
	271	1,593
Unearned future finance income on finance leases	(14)	(96)
Net investment in finance leases	257	1,497
The net investment in finance leases may be analysed as follows:		
- No later than 1 year	150	1,396
- Later than 1 year and no later than 5 years	105	101
- Later than 5 years	2	-
	257	1,497

Loans and advances to customers can be further summarised as follows:

	2009	2008 ⁽¹⁾
	£000	£000
Neither past due nor impaired	212,455	147,876
Past due but not impaired	15,748	12,044
Impaired	8,820	8,936
Gross	237,023	168,856
Less: allowance for impairment	(7,301)	(5,122)
Net	229,722	163,734

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

a.) Loans and advances past due but not impaired

Gross amounts of loans and advances to customers that were past due but not impaired were as follows:

	2009	2008
	£000	£000
Past due up to 30 days	3,460	1,907
Past due 30 - 60 days	1,587	559
Past due 60 - 90 days	2,295	3,336
Over 90 days	8,406	6,242
Total	15,748	12,044

Loans and advances normally fall into this category when there is a delay in either the sale of the underlying collateral or the completion of formalities to extend the credit facilities for a further period. Management have no material concerns regarding the quality of the collateral that secures the lending.

b.) Loans and advances renegotiated

Restructuring activities include external payment arrangements, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Renegotiated loans that would otherwise be past due or impaired totalled £NIL (2008: £NIL).

Notes to the consolidated financial statements

c.) Collateral held

An analysis of loans and advances to customers past due or impaired by reference to the fair value of the underlying collateral is as follows:

	2009	2008
	£000	£000
Past due but not impaired	20,215	31,657
Impaired	1,275	3,420
Fair value of collateral held	21,490	35,077

The fair value of the collateral held is £21,490,000 against £13,312,000 secured loans, giving an average loan-to-value of 62% (2008: 41%).

The gross amount of individually impaired loans and advances to customers before taking into account the cash flows from collateral held is £8,820,000 (2008: £8,936,000).

Interest income on loans classified as impaired totalled £644,000 (2008: £338,000).

17. Allowances for impairment of loans and advances

A reconciliation of the allowance account for losses on loans and advances by class is as follows:

	2009	2008
	£000	£000
At 1 January	5,122	5,381
Adjustments for disposals	-	(1,264)
Impairment losses	2,368	977
Loans written off during the year as uncollectible	(391)	(185)
Amounts recovered during the year	202	213
At 31 December	7,301	5,122

A further analysis of allowances for impairment of loans and advances is as follows:

	2009	2008
	£000	£000
Loans and advances to customers - Arbutnot Latham	1,472	684
Loan and advances to customers - unsecured - Secure Trust Bank	5,829	4,438
At 31 December	7,301	5,122

18. Debt securities held-to-maturity

Debt securities represent certificates of deposit. The Group's intention is to hold them to maturity and, therefore, they are stated in the balance sheet at amortised cost. Amounts include nil (2008: £8,000,000) with a maturity, when placed, of 3 months or less included in cash and cash equivalents (Note 33).

The movement in debt securities held to maturity may be summarised as follows:

	2009	2008 ⁽¹⁾
	£000	£000
At 1 January	140,639	122,306
Exchange difference on monetary assets	-	61
Additions	248,688	277,343
Redemptions	(261,730)	(259,071)
At 31 December	127,597	140,639

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

Notes to the consolidated financial statements

The table below presents and analysis of debt securities by rating agency designation at 31 December, based on Moody's long term ratings:

	2009	2008 ⁽¹⁾
	£000	£000
Aaa	-	-
Aa1	-	44,868
Aa2	20,132	82,849
Aa3	107,465	12,922
A1	-	-
	127,597	140,639

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

None of the debt securities held-to-maturity are either past due or impaired.

19. Financial investments

	2009	2008
	£000	£000
Group:		
Financial investments comprise:		
- Listed securities (at fair value through profit and loss)	465	421
- Unlisted securities (available-for-sale)	4,592	3,013
Total financial investments	5,057	3,434

a.) Unlisted securities

The Group has made equity investments in unlisted special purpose vehicles set up to acquire and enhance the value of commercial properties. These investments are of a medium term nature. There is no open market for these investments therefore the Group has valued them using appropriate valuation methodologies.

The Directors intend to dispose of these assets when a suitable buyer has been identified and when the Directors believe that the underlying assets have reached their maximum value.

	2009	2008
	£000	£000
Company:		
Financial investments comprise:		
- Listed securities (at fair value through profit and loss)	465	364

Notes to the consolidated financial statements

20. Intangible assets

Goodwill	2009	2008
Group:	£000	£000
Opening net book amount	1,991	2,042
On acquisition	-	-
On disposal (Note 37)	-	(51)
Closing net book amount	1,991	1,991

Computer software

Group:	£000
Cost	
At 1 January 2008	3,187
Additions	255
Disposals	(143)
At 31 December 2008	3,299
Additions	426
Disposals	-
At 31 December 2009	3,725

Accumulated amortisation

At 1 January 2008	(2,091)
Amortisation charge	(366)
Disposals	(2)
At 31 December 2008	(2,459)
Amortisation charge	(351)
Disposals	-
At 31 December 2009	(2,810)

Net book amount

At 31 December 2008	840
At 31 December 2009	915

Total intangible assets:	2009	2008
	£000	£000
Goodwill	1,991	1,991
Computer software	915	840
Net book amount at 31 December	2,906	2,831

Notes to the consolidated financial statements

21. Property, plant and equipment

Group:	Freehold land and buildings £000	Computer and other equipment £000	Operating leases £000	Motor vehicles £000	Total £000
Cost or valuation					
At 1 January 2008	6,581	12,008	1,934	928	21,451
Additions	-	875	157	286	1,318
Revaluation	(1,380)	-	-	-	(1,380)
Disposals	(101)	(702)	-	(660)	(1,463)
At 31 December 2008	5,100	12,181	2,091	554	19,926
Additions	-	500	4	39	543
Revaluation	-	-	-	-	-
Disposals	(250)	(1,187)	-	(265)	(1,702)
At 31 December 2009	4,850	11,494	2,095	328	18,767
Accumulated depreciation					
At 1 January 2008	(365)	(8,762)	(161)	(712)	(10,000)
Depreciation charge	(118)	(874)	(151)	(72)	(1,215)
Disposals	-	330	-	407	737
At 31 December 2008	(483)	(9,306)	(312)	(377)	(10,478)
Depreciation charge	(80)	(879)	(156)	(56)	(1,171)
Disposals	34	1,188	-	212	1,434
At 31 December 2009	(529)	(8,997)	(468)	(221)	(10,215)
Net book amount					
At 31 December 2008	4,617	2,875	1,779	177	9,448
At 31 December 2009	4,321	2,497	1,627	107	8,552

The Group's freehold property at 1 Arlestone Way, Solihull, 890 4LH, was valued on 17 December 2008 by an External Valuer, Graham Piercy, FRICS, of DWD2 Limited, Property Consultants. The Valuation was in accordance with the requirements of the RICS Valuation Standards 6th Edition and the International Valuation Standards. The Valuation of the property was on the basis and assumption it is an Owner/occupied property, valued to Market Value assuming that the property will be sold as part of the continuing business. The Valuer's opinion of Market Value was primarily derived using comparable recent market transactions on arms-length terms. As a Regulated Purpose Valuation, the Valuer, Graham Piercy FRICS, confirms this was the first occasion on which he had provided a Valuation of the Property. DWD2 Limited had had no previous relationship with the Company and accordingly received no fees in DWD2 Limited's preceding financial year. The Directors do not believe that the fair value of freehold property is materially different from the carrying value. All freehold land and buildings are occupied and used by Group companies. The carrying value of freehold land not depreciated is £0.5 million (2008: £0.5 million).

The historical cost of freehold property included at valuation is as follows:

	2009 £000	2008 £000
Cost	3,778	3,980
Accumulated depreciation	(753)	(731)
Net book amount	3,025	3,249

Motor vehicles include the following amounts where the group is a lessee under a finance lease:

	2009 £000	2008 £000
Cost - capitalised finance leases	160	206
Accumulated depreciation	(53)	(29)
Net book amount	107	177

The Group leases various vehicles under non-cancellable finance lease agreements with original lease terms of three years.

Notes to the consolidated financial statements

21. Property, plant and equipment continued

Company:	Computer and other equipment £000	Motor vehicles £000	Total £000
Cost or valuation			
At 1 January 2008	116	164	280
Additions	3	-	3
Disposals	-	(164)	(164)
At 31 December 2008	119	-	119
Additions	7	-	7
Disposals	-	-	-
At 31 December 2009	126	-	126
Accumulated depreciation			
At 1 January 2008	(41)	(137)	(178)
Depreciation charge	(4)	(10)	(14)
Disposals	-	147	147
At 31 December 2008	(45)	-	(45)
Depreciation charge	(3)	-	(3)
Disposals	-	-	-
At 31 December 2009	(48)	-	(48)
Net book amount			
At 31 December 2008	74	-	74
At 31 December 2009	78	-	78

22. Other assets

	2009 £000	2008 ⁽¹⁾ £000
Trade receivables	15,090	9,965
Reposessed collateral - Held-for-sale	1,950	1,913
Prepayments and accrued income	1,714	3,175
	18,754	15,053

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

23. Deposits from banks

	2009 £000	2008 £000
Deposits from other banks	2,886	2,898

For a maturity profile of deposits from banks, refer to Note 4.

24. Derivative financial instruments

	2009			2008		
	Contract/ notional amount	Fair value assets	Fair value liabilities	Contract/ notional amount	Fair value assets	Fair value liabilities
	£000	£000	£000	£000	£000	£000
Currency swaps	16,516	236	-	8,817	-	942
	16,516	236	-	8,817	-	942

The principal derivatives used by the Group are exchange rate contracts. Exchange rate related contracts include forward foreign exchange contracts and currency swaps. A forward foreign exchange contract is an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate. Currency swaps generally involve the exchange of interest payment obligations denominated in different currencies; exchange of principal can be notional or actual.

Notes to the consolidated financial statements

The table below presents and analysis of derivative financial instruments contract/notional amounts by rating agency designation at 31 December, based on Moody's long term ratings:

	2009 £000	2008 £000
Aaa	-	-
Aa1	-	8,817
Aa2	-	-
Aa3	16,516	-
A1	-	-
	16,516	8,817

25. Deposits from customers

	2009 £000	2008 ⁽¹⁾ £000
Retail customers:		
- current/demand accounts	131,649	105,662
- term deposits	254,350	187,228
	385,999	292,890

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

Included in customer accounts are deposits of £10,035,000 (2008: £11,185,000) held as collateral for loans and advances. The fair value of these deposits approximates the carrying value.

For a maturity profile of deposits from customers, refer to Note 4.

26. Other liabilities

	2009 £000	2008 ⁽¹⁾ £000
Trade payables	4,449	3,002
Finance lease liabilities	112	181
Accruals and deferred income	8,656	10,420
	13,217	13,603

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

As part of the sale of business assets during the year, accruals and deferred income include a provision of nil (2008: £482,000) in respect of various warranties included in the respective Sale and Purchase Agreements, as of the year end no claims have been made against this provision.

The Financial Services Compensation Scheme provides compensation to customers of financial institutions in the event that an institution is unable, or is likely to be unable, to pay claims against it. During 2008, a number of institutions failed. In order to meet its obligations to the depositors of these institutions, the FSCS has borrowed £19.7 billion from HM Treasury, which is on an interest only basis until September 2011. These borrowings are anticipated to be repaid wholly or substantially from the realisation of the assets of the above named institutions. The FSCS raises annual levies from the banking industry to meet its management expenses and compensation costs. Individual institutions make payments based on their level of market participation (in the case of deposits, the proportion that their protected deposits represent of total market protected deposits) at 31st December each year. If an institution is a market participant on this date it is obligated to pay a levy. Banking subsidiaries of Arbutnot Banking Group PLC were market participants at 31st December 2008 and 2009. The Group has accrued £443,000 for its share of levies that will be raised by the FSCS including the interest on the loan from HM Treasury in respect of the levy years to 31st March 2011. The accrual includes the Director's estimates for the interest FSCS will pay on the loan and estimates of the Group's market participation in the relevant periods. Interest will continue to accrue on the HM Treasury loan to the FSCS until September 2011 and will form part of future FSCS management expenses levies. If the assets of the failed institutions are insufficient to repay the HM Treasury loan in 2011, the FSCS will agree a schedule of repayments with HM Treasury, which will be recouped from the industry in the form of additional levies. At the date of these financial statements, it is not possible to estimate the quantum and timing of additional levies on the industry, the level of Group's market participation or other factors that may affect the amounts or timing of amounts that may ultimately become payable, nor the effect that such levies may have upon operating results in any particular financial period.

Notes to the consolidated financial statements

a.) Finance lease liabilities

Lease liabilities are effectively secured as the rights to the leased asset revert to the lessor in the event of default.

	2009 £000	2008 £000
Gross finance lease liabilities - minimum lease payments		
Within 1 year	61	95
Later than 1 year and no later than 5 years	58	95
Later than 5 years	-	-
	119	190
Future finance charges on finance leases	(7)	(9)
Present value of finance lease liabilities	112	181

The present value of finance lease liabilities is as follows:

Within 1 year	58	90
Later than 1 year and no later than 5 years	54	91
Later than 5 years	-	-
	112	181

27. Debt securities in issue

	2009 £000	2008 £000
Subordinated loan notes 2035	13,022	13,972

The subordinated loan notes 2035 were issued on 7 November 2005 and are denominated in Euros. The principal amount outstanding at 31 December 2009 was €15,000,000 (2008: €15,000,000). The notes carry interest at 3% over the interbank rate for three month deposits in euros and are repayable at par in August 2035 unless redeemed or repurchased earlier by the Company.

The contractual undiscounted amount that will be required to be paid at maturity of the above debt securities is €15,000,000.

Given the fact that the Group has never been subject to a published credit rating by any of the relevant agencies and the notes in issue are not quoted, it is not considered possible to approximate a fair value for these notes. The Directors do not believe the users of the accounts would be able to draw any meaningful conclusions from the information if it were practical to derive it.

28. Deferred taxation

	2009 £000	2008 £000
The deferred tax asset comprises:		
Unrealised surplus on revaluation of freehold property	(56)	(90)
Accelerated capital allowances and other short-term timing differences	259	196
Tax losses	99	-
Deferred tax asset / (liability)	302	106
At 1 January	106	(247)
Revaluation reserve	(20)	430
Profit and loss account - accelerated capital allowances and other short-term timing differences	117	(50)
Profit and loss account - tax losses	99	-
Deferred tax asset / (liability) at 31 December	302	106

The above balance is made up as follows:

	2009 £000	2008 £000
Deferred tax assets within the Group	383	106
Deferred tax liabilities within the Group	(81)	-
Deferred tax asset / (liability) at 31 December	302	106

Deferred tax assets are recognised for tax losses to the extent that the realisation of the related tax benefit through future taxable profits is probable.

Notes to the consolidated financial statements

29. Contingent liabilities and commitments

Capital commitments

At 31 December 2009, the Group had capital commitments of £NIL (2008: £NIL) in respect of equipment purchases.

Credit commitments

The contractual amounts of the Group's off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

	2009	2008
	£000	£000
Guarantees and other contingent liabilities	1,135	816
Commitments to extend credit:		
- Original term to maturity of one year or less	14,163	15,596
	15,298	16,412

Operating lease commitments

Where a group company is the lessee, the future aggregate lease payments under non-cancellable operating leases are as follows:

	2009	2008
	£000	£000
Expiring:		
Within 1 year	1,862	2,040
Later than 1 year and no later than 5 years	2,168	4,016
Later than 5 years	89	120
	4,119	6,176

Other commitments

At 31 December 2009 a commitment exists to make further payments with regard to the Financial Compensation Scheme Levy for 2011 and thereafter. Due to uncertainties regarding the calculation of the levy and the Group's share thereof, the Directors consider this cost to be unquantifiable.

30. Share capital

	Number of shares	Ordinary shares	Share premium
		£000	£000
At 1 January 2008	14,943,944	150	21,085
New share capital subscribed	55,675	-	213
Transfer to retained earnings in lieu of cash dividends	-	-	(213)
At 31 December 2008 and 31 December 2009	14,999,619	150	21,085

The total authorised number of ordinary shares at 31 December 2009 and 31 December 2008 was 418,439,000 with a par value of 1 pence per share (2008: 1 pence per share). All issued shares are fully paid.

At 31 December 2009 the Company held 340,274 shares (2008: 141,699) in treasury.

Notes to the consolidated financial statements

31. Reserves and retained earnings

	2009	2008
Group	£000	£000
Revaluation reserve	258	366
Foreign exchange translation reserve	(258)	(299)
Capital redemption reserve	20	20
Treasury shares	(940)	(445)
Retained earnings	11,684	11,257
Total reserves as 31 December	10,764	10,899

The revaluation reserve represents the unrealised change in the fair value of properties.

The foreign exchange translation reserve represents the cumulative gains and losses on the retranslation of the Group's and the Company's net investment in foreign operations, net of the effects of economic hedging.

The capital redemption reserve represents a reserve created after the company purchased its own shares which resulted in a reduction of share capital.

There is currently no available-for-sale reserve as the recognition criteria as set out in note 2.2 has not been met.

	2009	2008
Company	£000	£000
Capital redemption reserve	20	20
Treasury shares	(940)	(445)
Retained earnings	1,862	3,927
Total reserves as 31 December	942	3,502

32. Dividends per share

Final dividends are not accounted for until they have been approved at the Annual General Meeting. At the meeting on 12 May 2010, a dividend in respect of 2009 of 11.5 pence per share (2008: actual dividend 10.5 pence per share) amounting to a total of £1,685,825 (2008: actual £1,560,082) is to be proposed. The financial statements for the year ended 31 December 2009 do not reflect the final dividend which will be accounted for in shareholders' equity as an appropriation of retained profits in the year ending 31 December 2010.

33. Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises the following balances with less than three months maturity from the date of acquisition.

	2009	2008 ⁽¹⁾
Group	£000	£000
Cash (Note 13)	230	3,369
Loans and advances to banks (Note 14)	54,614	15,939
Debt securities held to maturity (Note 18)	-	8,000
	54,844	27,308

⁽¹⁾ The comparatives have been reclassified to align with current year presentation (see note 39).

	2009	2008
Company	£000	£000
Deposits from banks	(2,618)	(2,609)
	(2,618)	(2,609)

Notes to the consolidated financial statements

34. Related-party transactions

Related parties of the Company and Group include subsidiaries, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

Other than the Directors' remuneration, payment of dividends and transactions with subsidiaries, there were no related party transactions within the parent Company. A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits. Except for the directors' disclosures, there were no other Key Management Personnel disclosures; therefore the tables below relate to directors.

Directors:	2009	2008
	£000	£000
Loans		
Loans outstanding at 1 January	1,459	1,438
Loans advanced during the year	1,754	1,067
Loan repayments during the year	(277)	(1,046)
Loans outstanding at 31 December	2,936	1,459
Interest income earned	117	69

The loans to directors are secured on property or shares and bear interest at rates linked to base rate. No provisions have been recognised in respect of loans given to related parties (2008: £NIL). Details of Directors' remuneration are given in the Remuneration Report. The Directors not believe that any other key management disclosures are required.

Directors:	2009	2008
	£000	£000
Deposits		
Deposits at 1 January	864	1,569
Deposits placed during the year	4,790	1,307
Deposits repaid during the year	(3,774)	(2,012)
Deposits at 31 December	1,880	864
Interest expense on deposits	40	81

Details of principal subsidiaries are given in note 34. Transactions and balances with subsidiaries are shown below:

	Subsidiaries			
	2009		2008	
	Highest balance during the year £000	Balance at 31 December £000	Highest balance during the year £000	Balance at 31 December £000
ASSETS				
Due from subsidiary undertakings	23,645	23,198	22,605	20,960
Shares in subsidiary undertakings	28,624	28,624	28,524	28,524
Total assets	52,269	51,822	51,129	49,484
LIABILITIES				
Due to subsidiary undertakings	15,621	15,621	15,302	9,860
Total liabilities	15,621	15,621	15,302	9,860
Issued guarantee contracts	2,500	2,500	2,500	2,500

The disclosure of the year-end balance and the highest balance during the year is considered the most meaningful information to represent the transactions during the year. The above transactions arose during the normal course of business and are on substantially the same terms as for comparable transactions with third-parties. Arbutnot Securities Limited received a fee of £15,000 in 2008 in its capacity as stockbroker for the Group, it ceased to be stockbroker to the Group on 10th December 2008.

Notes to the consolidated financial statements

Share-based payment options

At 31 December 2009, the Company had the following equity settled share-based payment awards outstanding:

On 21 May 2008 Mr. Salmon was granted an option to subscribe between May 2011 and May 2015 for 100,000 ordinary 1p shares in the Company at 337.5p. The fair value of the option at grant date was nil.

On 5 November 2008 Mr. Cobb was granted an option to subscribe between November 2011 and November 2015 for 50,000 ordinary 1p shares in the Company at 320p. The fair value of the option at grant date was nil.

On 22 December 2009 Dr. Turrell was granted an option to subscribe between December 2012 and December 2016 for 50,000 ordinary 1p shares in the Company at 380p. The fair value of the option at grant date was nil.

35. Shares in subsidiary undertakings

	Shares at cost	Impairment provisions	Net
	£000	£000	£000
Arbuthnot Banking Group PLC:			
At 1 January 2009	31,503	(2,979)	28,524
Allotment of shares in Arbuthnot Unit Trust Management Limited	100	-	100
At 31 December 2009	31,603	(2,979)	28,624

	2009	2008
	£000	£000
Subsidiary undertakings:		
Banks	24,486	24,486
Other	4,138	4,038
Total unlisted	28,624	28,524

On 31 July 2008, the Group sold 100% of its investment in Arbuthnot Commercial Finance Limited for a total consideration of £2,996,314. These shares represent 98% of the issued ordinary share capital of Arbuthnot Commercial Finance Limited, refer to Note 37 for further details.

The principal subsidiary undertakings of Arbuthnot Banking Group PLC at 31 December 2009 were:

	Country of incorporation	Interest %	Principal activity
Secure Trust Bank PLC	UK	100	Retail banking
Arbuthnot Latham & Co., Limited	UK	100	Private banking
Arbuthnot AG	Switzerland	100	Private banking
Arbuthnot Securities Limited	UK	59.6	Investment banking

(i) All the above subsidiary undertakings are included in the consolidated financial statements and have an accounting reference date of 31 December.

(ii) All the above interests relate wholly to ordinary shares.

Notes to the consolidated financial statements

36. Operating segments

The Group is organised into four main operating segments, arranged over four separate companies with each having its own specialised banking service, as disclosed below:

- 1) Retail banking — incorporating household cash management, personal lending and banking and insurance services.
- 2) International Private banking — incorporating private banking and wealth management outside the UK.
- 3) UK Private banking — incorporating private banking and wealth management.
- 4) Investment banking — incorporating institutional stockbroking, equity trading and corporate finance advice.

Transactions between the operating segments are on normal commercial terms. Centrally incurred expenses are charged to operating segments on an appropriate pro-rata basis. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balance sheet.

Year ended 31 December 2009	Retail banking £000	International Private banking £000	UK Private banking £000	Investment banking £000	Group (reconciling items) £000	Group Total £000
Interest revenue	9,932	-	13,061	82	359	23,434
Inter-segment revenue	-	-	(661)	-	(359)	(970)
Interest revenue from external customers	9,932	-	12,450	82	-	22,464
Fee and commission income	13,505	-	4,731	13,580	-	31,816
Revenue from external customers	23,437	-	17,181	13,662	-	54,280
Interest expense	(1,345)	-	(4,163)	(234)	812	(4,930)
Subordinated loan note interest	-	-	-	-	(618)	(618)
Segment operating income	22,092	-	13,064	16,860	(316)	51,700
Impairment losses	(1,189)	-	(1,179)	-	-	(2,368)
Segment profit / (loss) before exceptional items	10,219	(506)	206	(147)	(4,722)	5,050
Exceptional items	-	-	-	-	-	-
Segment profit / (loss) before tax	10,219	(506)	206	(147)	(4,722)	5,050
Income tax (expense) / income	(2,903)	-	(33)	132	1,125	(1,679)
Segment profit / (loss) after tax	7,316	(506)	173	(15)	(3,597)	3,371
Segment total assets	114,067	162	370,068	17,710	(49,492)	452,515
Segment total liabilities	99,527	2,081	347,023	11,258	(41,517)	418,372
Other segment items:						
Capital expenditure	(485)	-	(357)	(119)	(8)	(969)
Depreciation and amortisation	(727)	(71)	(662)	(59)	(3)	(1,522)

The "Group" segment above includes the parent entity and all intercompany eliminations and fulfils the requirement of IFRS8.28.

Notes to the consolidated financial statements

Year ended 31 December 2008	Retail banking	International private banking	UK Private banking	Investment banking	Group (reconciling items)	Group Total
	£000	£000	£000	£000	£000	£000
Interest revenue	4,981	-	19,204	190	912	25,287
Inter-segment revenue	-	-	(576)	-	(912)	(1,488)
Interest revenue from external customers	4,981	-	18,628	190	-	23,779
Fee and commission income	15,498	-	6,925	12,818	-	35,241
Revenue from external customers	20,479	-	25,553	13,008	-	59,237
Interest expense	(767)	-	(10,455)	(676)	467	(11,431)
Subordinated loan note interest	-	-	-	-	(964)	(964)
Segment operating income	19,712	-	14,592	8,813	(287)	42,830
Impairment losses	(533)	-	(444)	-	-	(977)
Segment profit / (loss) before exceptional items	4,858	(1,160)	1,461	(5,225)	(6,689)	(6,755)
Exceptional items	2,419	-	658	-	1,528	4,605
Segment profit / (loss) before tax	7,277	(1,160)	2,119	(5,225)	(5,161)	(2,150)
Income tax (expense) / income	(1,898)	-	(11)	1,465	1,596	1,152
Segment profit / (loss) after tax	5,379	(1,160)	2,108	(3,760)	(3,565)	(998)
Segment total assets	46,209	-	311,363	16,391	(14,208)	359,755
Segment total liabilities	35,165	1,453	287,967	9,602	(8,846)	325,341
Other segment items:						
Capital expenditure	(665)	(199)	(652)	(54)	(3)	(1,573)
Depreciation and amortisation	(699)	(49)	(724)	(94)	(14)	(1,580)

Segment profit is shown prior to any intra-group eliminations.

Other than the International private banking operations which are in Switzerland, all the Group's other operations are conducted wholly within the United Kingdom and geographical information is therefore not presented.

37. Disposals

On 31 July 2008, the Group disposed of 100% of the share capital of its subsidiary, Arbuthnot Commercial Finance Limited.

The net asset position of Arbuthnot Commercial Finance Limited at 31 July 2008, together with the resulting profit on disposal of shares and related net cash inflow, is shown below:

	£000
Loans and advances to customers	26,277
Property, plant and equipment	106
Other assets	63
Deposits from banks	(10,466)
Other liabilities	(14,695)
Net assets	1,285
Add: Goodwill	51
Less: Non-controlling interests	(26)
Net assets disposed	1,310
Net gain on disposal	1,528
Costs accrued	158
Net cash inflow on sale	2,996

38. Ultimate controlling party

The Company regards Henry Angest, the Group Chairman and Chief Executive Officer, who has a beneficial interest in 52.8% of the issued share capital of the Company, as the ultimate controlling party. Details of his remuneration are given in the Remuneration Report and Note 34 of the consolidated financial statements includes related party transactions with Mr Angest.

Notes to the consolidated financial statements

39. Reclassification of 2008 numbers

The following reclassifications took place on the consolidated statement of financial position for 2008:

	Balance as per 2008 financial statements £000	Interest reclassification £000	Comparative balance 2009 financial statements £000
ASSETS			
Loans and advances to banks	15,930	9	15,939
Loans and advances to customers	163,350	384	163,734
Debt securities held-to-maturity	137,916	2,723	140,639
Other assets	18,169	(3,116)	15,053
	335,365	-	335,365
LIABILITIES			
Deposits from customers	291,742	1,148	292,890
Other liabilities	15,693	(1,148)	14,545
	307,435	-	307,435

A complete third balance sheet was not included above, as the reclassifications are not considered significantly material.

The following reclassifications took place on the consolidated statement of cash flows for 2008:

	Balance as per 2008 financial statements £000	Interest reclassification £000	Comparative balance 2009 financial statements £000
Changes in operating assets and liabilities:			
- net decrease / (increase) in loans and advances to customers	6,826	(384)	6,442
- net decrease / (increase) in other assets	17,545	3,116	20,661
- net (decrease) / increase in amounts due to customers	(9,178)	1,148	(8,030)
- net (decrease) / increase in other liabilities	(26,598)	(1,148)	(27,746)
Net cash (outflow) / inflow from operating activities	(7,958)	2,732	(5,226)
Cash flows from investing activities			
Purchase of debt securities	(274,620)	(2,723)	(277,343)
Net cash from investing activities	(14,901)	(2,723)	(17,624)
Net decrease in cash and cash equivalents	(28,634)	9	(28,625)
Cash and cash equivalents at end of year	27,299	9	27,308

The above reclassifications took place to align with the current year presentation. Interest receivable was reclassified from other assets to loans and advances to banks, loans and advances to customers and debt securities held-to-maturity. Interest payable was reclassified from other liabilities to deposits from customers. Interest receivable and payable is now reflected with the principal amount outstanding.

40. Events after the balance sheet date

There were no material post balance sheet events.

Notes to the consolidated financial statements

Five year summary

In the table below, all the figures are presented in accordance with IFRS.

	2005	2006	2007	2008	2009
	(i)				
	£000	£000	£000	£000	£000
Profit / (Loss) before tax and exceptional items*	7,367	7,551	8,579	(2,150)	5,050
Profit / (Loss) before tax	7,676	14,062	8,579	(2,150)	5,050
Earnings per share					
Basic (p)	45.8	63.0	23.8	3.5	23.4
Adjusted* (p)	32.6	32.0	23.8	3.5	23.4
Dividends per share (p)	32.0	32.5	33.0	21.0	22.0

* In 2005 exceptional items included reorganisation and redundancy costs of £486,000, the costs of moving to AIM of £55,000 and a profit on the sale to non-controlling interests of £850,000 and in 2006 exceptional items include the profit on disposal of Arbuthnot House of £12,623,000, long term bonuses of £1,900,000, restructuring costs of £1,312,000 and affinity bad debt of £2,900,000.

(i) The prior year adjustments, referred to in Note 9 of the 2007 Annual Report, of £1,028,000 relating to years earlier than 2006 have not been included in the pre 2006 figures disclosed in the table above.